BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition on behalf of Citizens of the State of Florida to require Progress Energy Florida, Inc. to refund customers $143 million.	DOCKET NO. 060658-EI ORDER NO. PSC-07-0816-FOF-EI ISSUED: October 10, 2007

The following Commissioners participated in the disposition of this matter:

LISA POLAK EDGAR, Chairman
MATTHEW M. CARTER II
KATRINA J. McMURRIAN
NANCY ARGENZIANO
NATHAN A. SKOP

APPEARANCES:

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On behalf of the Citizens of the State of Florida (OPC).

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On behalf of AARP (AARP).

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On behalf of the Office of the Attorney General, State of Florida (AG).

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On behalf of White Springs Agricultural Chemicals, Inc., d/b/a PCS Phosphate White Springs (White Springs).

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On behalf of the Florida Public Service Commission (Staff).

ORDER REQUIRING PROGRESS ENERGY FLORIDA TO REFUND CUSTOMERS $12,425,492, PLUS INTEREST AND REQUIRING THE FILING OF SUPPLEMENTAL TESTIMONY IN DOCKET NO. 070001-EI

BY THE COMMISSION:

I. Background

By motion filed September 30, 2005, in Docket No. 050001-EI, In re: fuel and purchased power cost recovery clause with generating incentive performance, the Office of Public Counsel (OPC) petitioned the Commission to establish a "separate 'spin-off' docket to evaluate the prudence and reasonableness of certain coal purchases made by Progress Energy Florida, Inc. (PEF) from its affiliate Progress Fuels Corporation." Id. The prehearing officer denied OPC's motion, and the issue was included in the November 2005 fuel proceeding.[1] On November 4, 2005, OPC filed a motion to defer the issue of the prudence of PEF's coal procurement until the next fuel proceeding. At the conclusion of the fuel clause hearing, we granted the motion to defer the issue.[2]

On August 10, 2006, OPC filed a petition to require PEF to refund customers $143 million. This docket was opened to address the petition. OPC alleged that PEF, instead of burning the design basis blend of coal for Crystal River Units 4 and 5 (CR4 and CR5), favored affiliates and bought only bituminous coal and synfuel for the units for the period 1996-2005. OPC further alleged PEF's actions were imprudent because PEF did not give timely consideration to a coal blend of 50 percent Powder River Basin (PRB) coal and 50 percent bituminous coal – the design blend. PRB coal is sub-bituminous coal mined in Wyoming and Montana, and has a lower heat content than bituminous coal. Nationwide the use of PRB coal for generating electricity grew during the 1980s and 1990s. OPC calculated the excess cost to be $134.5 million over the period 1996 through 2005 and recommended that we require PEF to refund the excess cost, with interest, to customers. PEF defended, arguing that it was prudent in its procurement decisions. Moreover, PEF asserted that customers received a benefit from PEF's use of bituminous coals. Finally, AARP asked that we also consider penalizing PEF, if we determined that PEF willfully violated a rule, statue or order administered by us.

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[1]Order No. PSC-05-1106-PHO-EI, issued November 3, 2005, in Docket No. 050001-EI, In re: fuel and purchased power cost recovery clause with generating incentive performance, p.52. The issue was included as Issue 13L: Were the prices that PEF paid to Progress Energy Fuels Corporation for coal reasonable in amount? If not, what adjustment should be made?
[2]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 incentive performance, pp. 27-28.

On August 30, 2006, PEF moved to dismiss OPC's petition, arguing that we lacked authority to review PEF's coal expenditures from 1996 to 2005. PEF's arguments were based on the doctrines of administrative finality, retroactive ratemaking, improper hindsight review, and due process violations. We denied the motion to dismiss.[3]

The Attorney General, AARP, Florida Industrial Power Users Group (FIPUG), OPC, PCS Phosphate/White Springs, and PEF were parties to the proceeding. On April 2-5, 2007, we conducted a full evidentiary hearing in this matter.

A. Prudence Review

At issue in this matter is whether PEF acted prudently in its coal procurement practices from 1996 to 2005. Prudence has been defined as "what a reasonable utility manager would have done in light of conditions and circumstances which were known or reasonably should have been known at the time the decision was made."[4] In Order No. 13452, issued June 22, 1984, in Docket No. 820001-EU-A, In re: Investigation of Fuel Cost Recovery Clauses of Electric Utilities (Gulf Power Company – Maxine Mine)(Maxine Mine Order), we described in detail the type of review we would perform in reviewing prudence:

> Significant controversy has arisen over the manner in which we should review Gulfs actions to determine whether its decisions regarding Maxine Mine Coal purchases were prudent. Theories have ranged from a prohibition against looking at the prudence of entering into a contract at any time except immediately after it is entered into, to a proposal to view the prudence of a contract from a purely retrospective basis. We believe that it is important to strike proper balance, and we believe that we have done so.
>
> The fact that it is a utility's actions rather than our own that we are reviewing dictates that utility contract problems will not come to our attention immediately. Many problems in procurement have a gradual aspect which can be perceived by the persons directly involved but not by third parties. Any approach to reviewing the prudence of contract decisions must recognize the propriety of looking at past actions, otherwise the natural lag in our ability to detect procurement problems will preclude us from acting on them. An approach that limits the review of prudence to contemporaneous events fails to recognize the duty of this Commission to protect the ratepayers' interest and the fact that utilities are not entitled to recover expenses imprudently incurred. On the other hand, the use of pure hindsight in assessing the prudence of past action is patently unfair. A utility should not be charged with knowledge of facts which cannot be foreseen or be expected to comply with future regulatory policies. Expectations are not always borne out. The prudence of decision making should be viewed from the perspective of the decision maker at the time of the decision.

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[3]Order No. PSC-07-0059-PCO-EI, issued January 22, 2007, in Docket No. 060658, In re: Petition on behalf of Citizens of the State of Florida to require Progress Energy Florida, Inc. to refund customers $143 million.
[4] City of Cincinnati v. Public Utilities Commission, 620 N.E. 2d 826 (Ohio 1993).

> Contract administration must be viewed at a point in time which takes into consideration the facts which were known or which should have been known at the time the contract is entered into or amended. If during the period of contract administration there is a period of mismanagement, whether short or long, any additional costs incurred as a result of that mismanagement should be disallowed even though the average price over the life of the contract is close to average market price.
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> In this case, we have looked at the prudence of Gulf's actions in terms of the facts that were known or that should have been known at the time of the decision. In so doing, we believe that we have properly protected Gulf's ratepayers' interests while recognizing Gulf's need to engage in independent decision making. We do not intend to become involved in the actual management of a utility. However, we expect a utility's management to act prudently. We have not sought to retroactively apply new policies to Gulf's prior actions and we have recognized that a utility cannot foresee the future. In this case we have determined that Gulf acted imprudently, that Gulf's imprudence resulted in excessive costs, and that the excessive costs should be disallowed and refunded to Gulf's ratepayers.

We must avoid impermissibly applying hindsight review, which is the application of facts that are known today to decisions made in the past (i.e., Monday morning quarterbacking). As we consider whether PEF acted prudently, we must ask ourselves, did PEF know or should PEF have known about a particular set of circumstances, when it made the coal procurement decisions OPC has challenged.

B. <u>Historical Background of the Fuel Cost Recovery Clause</u>

The fuel cost recovery clause (fuel clause) is a regulatory tool designed to pass through to utility customers the costs associated with fuel purchases. The purpose is to prevent regulatory lag. Regulatory lag occurs when a utility incurs expenses but is not allowed to collect offsetting revenues until the regulatory body approves cost recovery. Regulatory lag has historically been a problem because of the volatility of fuel costs. Regulatory lag is not of as much concern when expenses, such as capital improvements, and operations and management costs, can be planned for and included in base rate calculations. Different states have addressed volatile fuel costs in differing ways. Several jurisdictions, like Florida, have allowed recovery of fuel costs in a fuel adjustment clause. The operation of the fuel adjustment clause varies from state to state. Our practice of allowing cost recovery through the fuel adjustment clause has developed over the years.

Currently, the fuel clause hearing is held in November of each year.[5] It is typically scheduled as a several day proceeding during which we consider all of the cost recovery clauses.[6]

[5] <u>See,e.g.</u>, Order No. PSC-07-0221-PCO-EI, issued March 12, 2007, in Docket No. 070001-EI, <u>In re: Fuel and purchased power cost recovery clause with generating performance incentive factor</u>.

During the proceeding, testimony and exhibits are admitted for each of the five dockets. At the conclusion of the fuel clause proceeding, we set a factor for the fuel cost recovery clause based on three years of data. The utilities present testimony showing the actual costs expended for the prior year, the actual and projected costs for the current year, and the projected costs for the following year for both fuel and purchased power costs. In addition, the utilities submit testimony as to whether they achieved their performance goals for the prior year and also set goals for the following year. There is a standard list of issues which we consider every year. In addition, parties and our staff may propose additional issues for our consideration. Those issues may be adjudicated at the fuel proceeding, spun out into a separate docket (as this was), or otherwise addressed by the prehearing officer.[7]

From 1925 to 1951, prior to our obtaining jurisdiction over investor-owned electric utilities, Florida's electric utilities benefited from a monthly fuel adjustment clause. Starting in 1951, when the legislature granted us jurisdiction over investor-owned electric utilities, the utilities applied a Commission-approved formula and placed the resulting charge on customers' bills. While some auditing functions were performed by our staff, no formal public hearing was held. In 1973-1974, a foreign oil embargo substantially increased the cost of oil, leading to increased consumer concern over fuel adjustment charges. On October 7, 1974, we opened a docket to fully review the clause process.[8] Two days later, on October 9, 1974, the Attorney General issued an advisory opinion which stated that the practice of allowing changes in the fuel adjustment charges without a public hearing was illegal under Florida law. 74 Op. Att'y. Gen. Fla. 309 (1974). On October 11, 1974, the first fuel adjustment clause hearing was held, which led to the approval of a stipulation that provided for a monthly hearing format on all fuel adjustment clauses.[9] During the 1974 proceeding, we also considered recommendations on the modification of the clause. Having considered input from interested parties, we implemented a two-month lag between utilities filing for fuel clause recovery and our decision on those cost recoveries. At the time, the two month lag was intended as an incentive to the utilities to optimize fuel costs.

In 1980, we modified the clause again.[10] By Order 9273, utilities were able to collect fuel and fuel related expenses on a current basis. We subsequently modified the recovery clauses to allow recovery on the projections of future fuel and fuel related expenditures subject to a true-up hearing. A true-up hearing is a hearing in which the utilities' projected fuel expenditures are

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[6] Docket No. 060001-EI, In re: fuel and purchased power capacity cost recovery clause with generating incentive performance. Docket No. 060002-EG, In re: conservation cost recovery clause. Docket No. 060003-GU, In re: purchased gas adjustment true-up. Docket No. 060004-GU, In re: natural gas conservation recovery clause. Docket No. 060007-EI, In re: Environmental Cost Recovery Clause.

[7] See,e.g., 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, which is the final order approving fuel cost recovery factors to be applied in 2006.

[8] Order No. 6357, issued November 26, 1974, in Docket No. 74680, In re: General Investigation of Fuel Adjustment Clauses of Electric Companies.

[9] Id.

[10] Order No. 9273, issued March 7, 1980, in Docket No. 74680, In re: General Investigation of Fuel Cost Recovery Clause. Consideration of Staff's Proposed Projected Fuel and Purchased Power Cost Recovery Clause with an Incentive Factor.

adjusted to recover only actual expenditures. Also, during the time from 1980 to 1998, we modified our fuel adjustment hearings, scheduling them from once a month to every six months to its current schedule, which is once a year.[11] We were aware that the process associated with such an approach, which involved the use of projections, would not necessarily permit us to scrutinize the claimed costs with care prior to the initial approval of the collections. Thus, after implementing the 1980 clause modification, we considered the issue of our jurisdiction to adjust the dollar amounts that flowed through the clause if subsequent, more detailed evidence disclosed that the dollar amounts were imprudent or unreasonable.

In 1983, we conducted a hearing on the issue of whether we had jurisdiction to adjust past dollar amounts that flowed through the clause. At the hearing, our staff and OPC proposed that we adopt a mechanism to specifically identify any prudence issues within three years of the date collection is approved.[12] The seminal order, Order No. 12645, issued November 3, 1983, in Docket No. 830001-EU, In re: Investigation of Fuel Adjustment Clauses of Electric Utilities (Order No. 12645), changed the way the fuel clause proceedings were conducted. We rejected any attempts to limit our ability to identify issues linked to past collected amounts to a specific time frame. We also rejected our staff's proposal to limit prudence jurisdiction to three years, stating:

> We see no justification in limiting our ability to scrutinize past transactions. We fully intend to review a utility's procurement decisions solely in light of the facts known or knowable at the time a decision was made. The appropriate limitation of our jurisdiction is based on whatever statute of limitations or other jurisdictional limitations applies to our actions as a matter of law.

Order 12645 at 8-9. As of today, there is no statute of limitation or jurisdictional limitation placed on our ability to review past expenditures. In Order 12645, we stated that:

> [a]t the true-up hearing that follows a six month period a utility will still be free to present whatever evidence of prudence it chooses to provide. We note that certain utilities have periodically presented broad statements as to the prudence of their fuel procurement activities. Such presentations are not inappropriate, but they hardly elucidate the subject matter. Fuel procurement is an exceedingly complex

[11] Order No. PSC-98-0691-FOF-PU, issued May 19, 1998, in Docket No. 980269-PU, In re: Consideration of change in frequency and timing of hearings for fuel and purchased power cost recovery clause, capacity cost recovery clause, generating performance incentive factor, energy conservation cost recovery clause, purchased gas (PGA) true-up, and environmental cost recovery clause.

[12] "The staff proposed that we change the clause so that, instead of requiring proof of prudence at the true-up immediately following a six month period, we simply limit our jurisdiction over all transactions passed through the fuel clause for a period of three years from the date we approve the amount at the true-up hearing. Under the staff proposal, if before the end of the three year period the Commission indicates a need for further review for any specific transaction, the Commission would explicitly retain jurisdiction over amounts passed through the fuel clause relating to that transaction. The Commission may then continue jurisdiction over those amounts until a final order is issued. Once a specific transaction which has been explicitly set aside for review has been ruled upon by the Commission, the Commission would lose jurisdiction over that transaction for the period reviewed by the Commission." Order No. 12645, issued November 3, 1983, in Docket No. 830001-EU, In re: Investigation of Fuel Adjustment Clauses of Electric Utilities.

> matter and a determination of the prudence of procurement decisions requires a complex analysis. While a utility may feel satisfied that it has properly met its burden by such a presentation, we expect the quality and quantity of evidence to be presented in support of the prudence of fuel procurement decisions to match the complexity of the subject matter. We will therefore accept any relevant proof a utility chooses to present at true-up, but we will not adjudicate the question of prudence, nor consider ourselves bound to do so until all relevant facts are analyzed and placed before us. We will be free to revisit any transaction until we explicitly determine the matter to be fully and finally adjudicated.

Id. at 9. We further stated that:

> [t]he question of whether we may review the prudence of expenditures made during prior true-up periods is governed by whether the prudence of expenditures has been adjudicated. The issuance of a true-up order does not adjudicate the question of prudence per se. As pointed out by staff, the true-up hearings have never been relied upon by the Commission or any other party as the point at which prudence is actually reviewed. With rare exception, prudence has not been alleged, proven nor ruled upon during those proceedings. An actual adjudication of prudence depends on whether an allegation of prudence was made, evidence was presented thereon and a ruling made. Where an expenditure has been disputed and its prudence examined on the record, a ruling in favor of prudence should be inferred even if none is explicitly made. This approach to jurisdiction over prior true-up periods naturally involves a review of the record of prior proceedings. Since several hearings are held each year, this process is necessarily complex. We will defer such a review until such time as we must face the question for a particular utility.

Id. at 10.

In the Maxine Mine Order,[13] we faced the question of prudence for Gulf Power Company. This case involved a review of certain costs associated with Gulf Power's 1974 contract extension to purchase coal from the Maxine coal mine in Alabama. We considered whether to adjust the expenses that had flowed through the fuel clause from the 1974 contract extension to 1983. We found that because of the rising cost of coal in the market, the rate payers were not harmed until 1980. We opined that Gulf Power should have negotiated and administered the extension of its contract differently. Gulf Power argued that we could not reach back to a period prior to a 1981 true-up order. Citing to Order No. 12645, we reiterated our holding that the issuance of a true-up order does not adjudicate the issue of prudence of past expenditures.[14] We explained the rationale behind our decision as follows:

[13] Order No. 13452.
[14] Maxine Mine Order at pp. 18-19.

> The approach announced in Order No. 12645 is fair to all involved. In normal ratemaking a utility is not entitled to receive a rate increase until after it has demonstrated that it is not earning a fair rate of return on its investment in property used and useful in the public service. The utility must demonstrate that its investment was prudent, its capital costs are reasonable, and that its expenses were prudently incurred. The delay in receiving rate relief under normal ratemaking is referred to as regulatory lag. Regulatory lag arises because it is the utility and not the Commission that possesses the information needed to decide the issues. The time needed by the Commission to collect and analyze relevant information causes regulatory lag . . . . A utility may now recover its entire fuel cost concurrent with the expense . . . . Although the effect of regulatory lag on a utility's rates is now eliminated, regulatory lag still exists. It still takes time for the Commission to collect and analyze information relevant to the accuracy and prudence of fuel expenditures. Under the new clause recovery is immediate. There is a trade-off under the new clause, however, as a utility remains uncertain as to whether the Commission will ultimately determine its expenditures to be prudent.

Id. at 18.

Gulf Power appealed Order No. 13452. Gulf Power Company v. Florida Public Service Commission, 487 So. 2d 1036 (Fla. 1986). On appeal, Gulf Power raised several issues including whether the refund order constituted retroactive ratemaking. Id. The Florida Supreme Court affirmed our decision, holding that the order did not constitute retroactive ratemaking. Id. at 1037. The Court stated:

> [f]uel adjustment charges are authorized to compensate for utilities' fluctuating fuel expenses. The fuel adjustment proceeding is a continuous proceeding and operates to a utility's benefit by eliminating regulatory lag. This authorization to collect fuel costs close to the time they are incurred should not be used to divest the commission of the jurisdiction and power to review the prudence of these costs. The order was predicated on adjustments for 1980, 1981, and 1982. We find them to be permissible.

Id. Thus, our ability to review past expenditures by utilities is essentially a quid pro quo that was established in return for the benefit utilities receive.

Since the Maxine Mine Order, we have continuously held that we have jurisdiction to review past fuel expenditures of utilities to determine if they were prudently incurred. In final orders entered after a fuel proceeding, we have stated that "the estimated true-up amounts contained in the fuel cost recovery factors approved herein are hereby authorized subject to final true-up, and further subject to proof of the reasonableness and prudence of the expenditures upon which the amounts are based."[15]

In Order No 15486, issued December 23, 1985, in Docket No. 840001-EI-A, In re: Investigation into Extended Outage of Florida Power and Light Company's St. Lucie Unit No. 1, we reviewed a past expenditure that was sixteen years old. In that case, FPL sought to recover through the fuel clause expenses it incurred because a 822 megawatt nuclear generating unit was inoperative for fifteen months. FPL alleged that damages that occurred to the unit's reactor required extensive repairs to the reactor core support barrel and the reactor thermal shield. When analyzing FPL's expenses to supplant the unit's generation, we reviewed the prudence of FPL's decision to design a unit that included a thermal shield sixteen years earlier and stated:

> Examining the facts surrounding a decision made 16 years ago is difficult at best . . . . Notwithstanding the difficulty involved, our responsibility is to investigate and then determine the reasonableness and prudence of given expenditures by attempting to analyze the actions of the decision-makers in light of the circumstances then known to them or that they should have reasonably been aware of if they were proceeding in a reasonable, prudent and efficient manner. For the reasons that follow, we find that FPL's decision to include a thermal shield in the design of SL1 was prudent when we consider the information known to the decision-makers at the time of the relevant decisions.

Id. at 8. Ultimately, we decided that FPL's actions were prudent.

Upon consideration of the record in this matter, we find that we have the legal authority to review PEF's coal procurement decisions for the years 1996 to 2005. We find that we have previously established the policy of reviewing and requiring refunds of expenditures through the fuel clause when facts are presented to us showing a utility was imprudent in its fuel procurement decisions. Upon review of the record, we find that PEF was prudent in its coal procurement decisions for CR4 and CR5 for the years 1996 to 2001. In 2001 and 2002, PEF's management failed to seek revisions to its environmental permit, to conduct PRB coal test burns, to modify its plant to burn PRB coal on a long-term basis, and to purchase PRB coal. Record evidence shows that PEF recognized in May 2001 that PRB was very competitive, on an evaluated basis, with the types of coal that it had historically purchased. We find that PEF management's lack of action, despite its knowledge that PRB coal was a cost effective alternative, was imprudent. We find that because of PEF's imprudent conduct, PEF paid excessive fuel costs from 2003 through 2005. While PEF was not prudent in its management decisions in 2001 and 2002, it would have taken a number of months for PEF to prepare CR4 and CR5 to burn PRB. Accordingly, PEF's actions did not cause customers to incur excess coal costs until 2003. We find that PEF did not pay excessive fuel costs for the years 1996 through

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[15] See, e.g., Order No. PSC-97-1045-FOF-EI, in Docket 970001-EI, issued on September 5, 1997, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor; Order No. PSC-98-1223-FOF-EI, issued on September 17, 1998, in Docket No. 980001-EI, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor; and Order No. PSC-02-1761-FOF-EI, issued on December 13, 2002, in Docket No. 020001-EI, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor.

2002. The following is our findings of fact and conclusions of law on the issues raised at the April 2 – 5, 2007 hearing. We have jurisdiction over this matter pursuant to Sections 366.01, 366.04, 366.041, 366.05, 366.06 and 366.07, Florida Statutes.

II. PSC Legal Authority to Conduct Prudence Reviews

PEF challenged our legal authority to conduct prudence reviews for costs approved in prior fuel proceedings, asserting the position that, the final true-up of costs to projections amounts to our prudence review and, therefore, administrative finality attaches to the issue of prudence of those costs approved in prior fuel proceedings. PEF asserted that in the course of the prior fuel proceedings, we have received or had available to us all the information we needed to have determined the prudence of PEF's coal procurement decisions for 1996 through 2005. PEF also reasserted the issues it raised in its prior motions seeking to dismiss the case or exclude evidence. In fact, the majority of its post-hearing brief focuses on the argument of administrative finality.[16] PEF alleged that the doctrine of administrative finality applies to the final orders for each fuel proceeding.

A. Administrative Finality

PEF argued that the issue of the prudence of PEF's coal procurement costs was decided at prior fuel clause proceedings, and that the doctrine of administrative finality precludes further review. We acknowledge that the doctrine of administrative finality applies to our final orders, and parties are entitled to the certainty that finality provides. See Austin Tupler Trucking, Inc. v. Hawkins, 377 So. 2d 679 (Fla. 1979) (finding that the Commission could not reopen dormant trucking certificate case after time for reconsideration had passed). See also, Florida Power Corporation v. Garcia, 780 So. 2d 34, 44 (Fla. 2001) (citing with approval Austin Tupler). We disagree that there has been a final Commission decision on the prudence of PEF's coal costs.

Even when finality has attached to an order, there is a significant exception to the application of the doctrine, and finality will not apply where it is shown that some mistake, misrepresentation, or fraud, or a matter of great public interest compels our review. See Peoples Gas v. Mason, 187 So. 2d 335, 339 (Fla. 1966), wherein the Court prohibited review of the Commission's approval of a territorial agreement, but elucidated the exception described above. The Court cautioned against a too doctrinaire approach to the application of administrative finality, stating:

> We understand well the differences between the functions and orders of courts and those of administrative agencies, particularly those regulatory agencies which exercise a continuing supervisory jurisdiction over the persons and activities regulated. For one thing, although courts seldom, if ever, initiate proceedings on

[16] In addition to arguing that we are precluded from reaching a decision regarding PEF's prudence by the doctrine of administrative finality, PEF also reasserts that the doctrines of retroactive ratemaking, due process, and impermissible hindsight review preclude review of PEF's expenditures approved in prior fuel clause proceedings. Those arguments were raised by PEF and addressed by us earlier in this proceeding. See Order No. PSC-070059-PCO-EI, issued January 22, 2007, and Order No. PSC-07-0270-PCO-EI, issued March 30, 2007 in the instant docket.

> their own motion, regulatory agencies such as the commission often do so. Further, whereas courts usually decide cases on relatively fixed principles of law for the principal purpose of settling the rights of the parties litigant, the actions of administrative agencies are usually concerned with deciding issues according to a public interest that often changes with shifting circumstances and passage of time. Such considerations should warn us against a too doctrinaire analogy between courts and administrative agencies and also against inadvertently precluding agency-initiated action concerning the subject matter dealt with in an earlier order.

In ratemaking proceedings, where we establish fair, just, and reasonable utility rates, the courts have been more inclined to apply exceptions to the doctrine. See, e.g., Sunshine Utilities v. Florida Public Service Commission, 577 So. 2d 663, 666 (Fla. 1st DCA 1991), wherein the Court affirmed our decision to review a five-year-old rate order to correct going forward an "incorrect assumption." See also, Reedy Creek Utilities v. Florida Public Service Commission, 418 So. 2d 249 (Fla. 1982) (affirming our decision to revisit rate order), and Richter v. Florida Power Corporation, 366 So. 2d 798 (Fla. 2d DCA 1979) (arising out of the Daisy Chain fuel procurement scandal where the Court upheld our authority to review prior rate decisions).

In our fuel clause proceedings, our need to retain the ability to review the prudence of fuel costs precludes application of the doctrine of administrative finality until we specifically address the prudence of particular costs. In Order No. 12645, we said:

> We will therefore accept any relevant proof a utility chooses to present at true-up, but we will not adjudicate the question of prudence, nor consider ourselves bound to do so until all relevant facts are analyzed and placed before us. *We will be free to revisit any transaction until we explicitly determine the matter to be fully and finally adjudicated. . . .* An actual adjudication of prudence depends on whether an allegation of prudence was made, evidence was presented thereon and a ruling made. Where an expenditure has been disputed and its prudence examined on the record, a ruling in favor of prudence should be inferred even if none is explicitly made.

Id at 9 (emphasis added). Since 1983, final orders resulting from our annual fuel proceeding have included language "that the estimated true-up amounts contained in the fuel cost recovery factors approved herein are hereby authorized subject to final true-up, and further subject to proof of the reasonableness and prudence of the expenditures upon which the amounts are based."[17]

PEF argues that by submitting records and discovery to our staff during the course of the annual fuel proceedings, PEF has placed sufficient evidence before us to establish the prudence of its fuel costs. In fact, PEF urges us to assume the burden of finding imprudence rather than requiring the utilities to prove prudence. In its brief, PEF states: "[t]here is, therefore, a three-

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[17] Order No. PSC-02-1761-FOF-EI, issued December 13, 2002, in Docket No. 020001-EI, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor.

year period in which OPC, staff or any other party can raise an issue as to the prudence of any fuel cost." In other words, PEF would place the burden of questioning prudence on other parties, rather than, as Order 12645 requires, placing the burden of proving prudence on PEF.

To agree with PEF is to depart from the previous 24 years of precedent based upon Order 12645, where we said: "[t]he issuance of a true-up order does not adjudicate the question of prudence per se. As pointed out by staff, the true-up hearings have never been relied upon by the Commission or any other party as the point at which prudence is actually reviewed." We further explained: "[u]nder the new structure, rather than explicitly considering prudence at the end of each six month period, we will consider only the question of comparing projected to actual results. Questions of prudence require careful and often prolonged study."

PEF argues that we have already determined the prudence of PEF's fuel costs at each final true-up hearing from 1996-2005. However, PEF failed to introduce any prior Commission order that found PEF prudent in its coal procurement. Instead, PEF reasons that in fuel proceedings, our staff had the information before it, our staff engaged in discovery, our staff was assigned the function of evaluating a utility's activities for prudence, and, therefore, we must have adjudicated the issue of PEF's prudence in coal procurement practices. PEF referred to testimony from current staff and former staff witnesses in this proceeding to characterize the type of review our staff performs annually in the fuel clause proceeding, as a prudence review.

We cannot delegate our ratemaking authority to administrative staff. See Order No. 6986, issued October 30, 1975, in Docket No. 74807-EU, In re: Petition of Florida Power Corporation for authority to increase its rates and charges, in which we stated:

> In essence, Movant has predicated its request on the premise that the staff operates as the alter ego of the Commission or that the Commission delegates de facto authority to its staff to act in its stead. Such an assertion is patently incorrect for it overlooks the fact that staff members are not public officers of the State, elected or appointed. They exercise no sovereign powers of the State. They have no decisional powers, either by Statute or Rule, and no decisional powers have been delegated to them by the Commissioners. For that matter, we are unaware of any lawful basis by which such authority could be delegated.

See also, Citizens v. Wilson, 567 So. 2d 889, 892 (Fla. 1990) (explaining that, only by specific direction, could Commission staff perform the "ministerial task of seeing whether these [revised supplemental service rider] conditions were met"). Only the Commission may make a finding of prudence. Proof of our finding of prudence would be explicitly set forth in prior fuel orders, or implicitly set forth in transcripts of prior fuel proceedings. PEF has provided no proof that the Commission has made any findings of prudence for the events and time period at issue here.

While our staff's actions do not rise to the level of an adjudication of prudence by the Commission, our staff does conduct a preliminary review of the appropriateness of the recovery of costs. Staff's preliminary review may lend credibility to PEF's argument that PEF was indeed prudent in its procurement decisions over the past decade. But as diligent as our staff might have been in attempting to uncover imprudent utility decisions, it is a difficult task, made more difficult by the fact that the utility is the one who holds all of the information. It is the responsibility of the utility to identify and specifically seek our approval of its decisions. As illustrated here and in the Maxine Mine Order, the level of investigation needed to examine prudence can be significant and it can take several years before a question of prudence becomes apparent.

In the Maxine Mine Order, we recognized that often an imprudent decision will not "come to our attention immediately. Many problems in procurement have a gradual aspect which can be perceived by the persons directly involved but not by third parties." Maxine Mine Order at 7. For instance, in the Maxine Mine Order, the imprudence of Gulf's decision to enter into a long-term contract for coal procurement without demanding an early termination clause did not become evident for several years, because the prices Gulf paid for Maxine Mine coal were not out of line with other coal purchased. Gulf's imprudence became obvious only when the Maxine Mine coal prices became excessive in comparison to other coal prices and Gulf could not terminate its contract. Like this case, the coal procured by Gulf from Maxine Mine went through the fuel clause and our staff did not observe the imprudence of Gulf's coal procurement until 1981 when "the full attention of staff was focused on Maxine Mine." Maxine Mine Order at 13.

PEF also argued that there is nothing more that we can or should do beyond what we currently do in the fuel cost recovery clause proceedings to determine prudence. PEF contends that there is no further Commission process after the true-up proceeding to later determine prudence. However, this proceeding before us, as well as various other prudence reviews previously conducted, contradicts PEF's argument. See Order No. 18690, issued January 13, 1988, in Docket No. 860001-EI-B, In re: Investigation of Florida Power Corporation's Crystal River Unit No. 3's outages since December 1, 1982 (finding FPC prudent after reviewing all unplanned outages at Crystal River 3 for the period 1982 to date, spanning 5 years, at the request of OPC), and Order No. 15486, issued December 23, 1985, in Docket No. 840001-EI-A, In re: Investigation into extended outage of Florida Power and Light Company's St. Lucie Unit No. 1 (finding FPL prudent after reviewing a management decision made 16 years prior to our review). Our practice is to conduct prudence reviews where they are warranted.

B. Hindsight Review

Throughout its brief, PEF also argued that certain evidence required us to indulge in impermissible hindsight review. As we noted in our prior order denying PEF's motion to dismiss, the doctrine of hindsight review does not preclude us from considering the previous actions of a utility, as long as we apply the appropriate standard in reviewing those actions. That standard is whether the utility acted prudently and reasonably in light of the facts that it knew or should have known at the time it made its decision. Gulf, 487 So. 2d at 1037. In Gulf, the Court reviewed our decision on Gulf's prior management decisions concerning the Maxine Mine. In affirming our finding of managerial imprudence, the Court stated, "[c]ontrary to Gulf's contentions, the commission sought to evaluate Gulf's managerial decisions *under the conditions and times they were made.*" Id. at 1037 (emphasis added). Similarly here, we may review the actions of PEF to determine if its management's decisions regarding fuel procurement were prudent under the conditions and time they were made. Improper hindsight review involves applying facts as we know them today to evaluate decisions made in the past, thereby making a different course of action look preferable. In a proper prudence review, we consider the prudence of decisions made in the past by applying facts that were available to the company at the time of its management decision.

C. Retroactive Ratemaking

In its brief, PEF argued that requiring a refund of the previously approved fuel costs constituted retroactive ratemaking. In Gulf, the Supreme Court also addressed the issue of whether review of prior decisions constitutes prohibited retroactive ratemaking. The Court opined:

> Nor do we find that the order constitutes prohibited retroactive ratemaking fuel adjustment. Fuel adjustment charges are authorized to compensate for utilities' fluctuating fuel expenses. The fuel adjustment proceeding is a continuous proceeding and operates to a utility's benefit by eliminating regulatory lag. This authorization to collect fuel costs close to the time they are incurred should not be used to divest the commission of the jurisdiction and power to review the prudence of these costs. The order was predicated on adjustments for 1980, 1981 and 1982. We find them to be permissible.

Id. at 1037.

The facts in Gulf are very similar to the facts here. In Gulf, the Supreme Court had before it an order of the Commission requiring Gulf to refund its customers for several years of costs that had previously been allowed through the fuel clause. The only distinction between Gulf and this proceeding is that in this case we are being asked to review the utility's actions over the prior ten years rather than four years. We have, however, been asked to review the prudence of utility decisions as far back as sixteen years. In Order No. 15486, we reviewed Florida Power and Light Company's management decisions to include thermal shields in the design of St. Lucie Unit No. 1. In Order No. 18690, we reviewed the prudence of purchased power costs for PEF from 1982-1987 because of extended and repeated outages at the nuclear power plant at Crystal River 3.

D. Due Process

Finally, PEF has asserted that reviewing past utility decision-making violates due process and is fundamentally unfair to the utility. A close review of Order 12645 and its application over the years belies PEF's argument. We established the current fuel clause proceedings to eliminate the regulatory lag inherent in base rate proceedings for recovery of volatile fuel costs. We allowed the utilities to present their costs for recovery without proving prudence. PEF was on notice of this procedure from 1983 forward. PEF has often participated in our proceedings regarding the prudence of its prior conduct, with full knowledge that a refund could be ordered. According to Order 12645, a utility may present proof of prudence and, if the facts are before us, we may take the steps necessary to determine the prudence of fuel costs passed through the clause.

As OPC explained, the fuel clause benefits utilities. Requiring the utilities to bear the burden of proving prudence protects customers and is needed to assure fair, just and reasonable rates. Our ability to review and disallow expenses in the future protects the ratepayers. To maintain a balance between utility and ratepayer interests in fuel proceedings, we must retain jurisdiction over fuel costs after final true-up.

E. Findings and Conclusion

In fuel cost recovery proceedings we have specifically reserved for future decisions issues of prudence regarding the costs that were trued-up in the fuel clause hearings. As stated in Order 12645, the fuel clause is a comparison of a utility's projected fuel costs to the costs actually expended. It is not a prudence review. We will consider prudence of fuel expenditures when the issue is brought to us by the parties, but the issue of prudence of particular fuel costs will only be final when we have specifically addressed the issue.

In denying PEF's Motion to Dismiss, we previously determined that our hearing of OPC's petition would not constitute retroactive ratemaking and that hearing OPC's petition would not require us to improperly apply hindsight review. We may make our decision regarding the conduct of the utility by reviewing the utility's actions in the light of what the utility knew or should have known at the time the utility made its decisions. In Gulf, the Florida Supreme Court recognized that the fuel proceedings do not prohibit us from later reviewing the prudence of prior expenditures and ordering a refund when the expenditures that were collected prove to be unjust and unreasonable. That refund does not, in the circumstance of the fuel clause proceedings, constitute retroactive ratemaking.

Finally, having taken advantage of the expedited cost recovery proceedings offered to it through the fuel clause, PEF cannot now be heard to complain that the proceedings are unfair and lacking in due process. PEF has knowledge of the existence of Order 12645 and the substantive and procedural requirements therein. It has previously participated in prudence reviews which are separate from the fuel hearings. The fact that PEF may now be responsible for the refund of monies it allegedly improperly collected does not suddenly make the process unfair. Therefore, we find that we have the authority to grant the relief requested by OPC.

III. Commission Policy Regarding Refund of Imprudent Expenditures

PEF also argued that as a matter of policy we have not reached back, nor should we reach back to prior years and require fuel clause approved refunds. PEF argued that it is not acceptable to reconsider cost recovery amounts for the years 1996 through 2003. It contends the investment community would react negatively if we were to find in OPC's favor in this proceeding. Witnesses Fetter, Lawton, and Bohrmann addressed this subject at the hearing.

PEF witness Fetter testified that if we were to reconsider fuel costs that have previously been approved for cost recovery going back ten years, it would create a regulatory environment within which no issue is ever finally resolved. He stated that the three major rating agencies would be "stunned" if we were to validate OPC's theory of the case. He also testified that he expects investors would react to such a development by requiring higher returns on equity and debt, not only for PEF but potentially for all of Florida's investor-owned utilities. Witness Fetter concluded that such a process would be unfair to both investors and ratepayers and, thus, would represent bad regulatory policy.

OPC witness Lawton testified that OPC's prudence challenge regarding past PEF coal procurement is in line with our previous rulings on fuel cost reviews and is supported by the Gulf decision. He also states that no utility, investor, or the investment community at large reasonably expects a regulatory commission to permit imprudent expenditures to be recovered from ratepayers. Finally, witness Lawton concluded that credit market problems, if any, arising from a disallowance would be the result of management conduct and it would be our responsibility to shield ratepayers from any such higher capital costs in the same manner it would prevent any other unreasonable costs from being borne by ratepayers.

Witness Bohrmann, also testified on behalf of OPC, and referred to numerous Commission Orders to support OPC's contention that we retain jurisdiction to consider and review the prudence of costs recovered through the fuel adjustment clause beyond the fuel adjustment proceedings. Witness Bohrmann also testified that PEF witness Fetter "either misunderstands or ignores the structure and the purpose of the fuel cost recovery mechanism as it has been consistently applied in Florida since the early 1980's." Witness Bohrmann concluded that, if we find that PEF was imprudent in its fuel procurement for CR4 and CR5, we have the jurisdiction and supporting precedent to order a refund as proposed by OPC.

PEF acknowledges to investors in its Form 10–K filed with the Securities and Exchange Commission (SEC) that while state commissions allow fuel costs to be recovered through recovery clauses, there is a potential that a portion of these costs could be deemed imprudent by the respective commissions. Based on the explicit language from numerous Commission Orders and the company's own statements in filings made with the SEC, all parties were on appropriate notice that past fuel costs were subject to prudence review in the event evidence came to light that identified imprudently incurred costs.

The role of regulatory commissions in general, and the function of performing prudence reviews in particular, are generally recognized and understood by the investment community. Witness Fetter acknowledged that we have long been regarded by the investment community as being a regulatory body that fosters and maintains a fair and constructive regulatory climate. He also acknowledged that, based on his experience as a Public Service Commissioner in Michigan and his testimony as a consultant before the Arkansas Public Service Commission, it is appropriate for regulatory commissions to disallow recovery of imprudently incurred costs.

Given our knowledge of the role of the investment community and recognizing that the fuel costs in question represent less than 1.6 percent of PEF's total fuel costs over the period under review, we believe PEF has overstated the reaction the investment community will have to carrying out our generally accepted statutory responsibility. For the reasons discussed above, we are not dissuaded from making the appropriate adjustment based on PEF's argument that the investment community would react unfavorably.

We are of the opinion that Order No. 12645 and subsequent decisions support our review of prior conduct, including conduct from 10 years past. PEF argues that the Commission's policy has been to consider the final true-up as the prudence review. The question of the timing of prudence reviews is an issue that affects all parties in the fuel docket. Since not all parties to the fuel docket participated in this docket, we encourage the parties to Docket No. 070001-EI to address, in their projection testimony to be filed in September 2007, the issue of whether and how we should conduct prudence reviews for fuel and purchased power costs approved for cost recovery in the fuel docket.

IV. Prudence of PEF's Actions in Purchasing Coal

Having concluded that as a matter of law and of policy, we should consider the matter of PEF's coal procurement decisions, we turn to whether PEF was indeed imprudent in its coal purchases for CR4 and CR5 for the years 1996 to 2005. We have analyzed the record and the parties' briefs in this case. We conclude that for the period from 1996 to 2001, PEF did act prudently in procuring coal for CR4 and CR5. We find that in 2001 and 2002 PEF acted imprudently by failing to put itself in the position to use coal that was known to be less expensive. Because of PEF's imprudent decisions in 2001 and 2002, PEF was not prudent in purchasing coal for CR4 and CR5 during the period 2003 through 2005. As a result, customers should be refunded the amount of $12,425,492 in excess coal and SO2 emissions costs for the years 2003 through 2005. PEF did not incur excess coal or SO2 emissions costs for the years 1996 through 2002.

Evidence, testimony and briefs for this hearing were organized by the prehearing officer into eight categories. Those categories were for organizational purposes. (1) The Environmental Permitting topic concerned whether PEF maintained the appropriate permitting for using the most economical coal. The (2) Coal Procurement Practices and (3) Coal Cost and Availability topics addressed PEF's coal procurement for the period including the RFP process, the appropriate transportation costs, and the use of South American coal. Safety, blending, handling, and storage issues related to PRB coal were covered by the (4) CR3 and (5) CR4 and CR5 Operational Matters topics. Whether burning PRB coal could cause a loss of MW output at CR4 and CR5 was addressed in the (6) Megawatt Capacity topic. PEF used an affiliated company, Progress Fuels Corporation (PFC), for coal supply during the period. The (7) Affiliates topic covers whether PEF, in purchasing coal, had inappropriate dealings with affiliated companies. The final topic, (8) Other Factors, did not include any evidence not addressed in the other 7 topics and so is not addressed in this order. Our findings and conclusions regarding the topics are set forth below.

A. Environmental Permitting

The parties debated the prudence of several key environmental permitting decisions at CR4 and CR5. We believe these decisions were critical to the utility's ability to burn PRB coal at CR4 and CR5.

In 1978, the company's initial site certification process allowed for the use of a 50/50 fuel blend of bituminous and sub-bituminous coals. We agree with PEF that no explicit governmental authority to burn sub-bituminous coal was granted through the site certification process. However, based on the initial certification, we agree with OPC that the company did have implicit authority to burn sub-bituminous coal during the early years of CR4 and CR5 operation. However, the record reflects that PRB coal was not an economical option for PEF during the 1980s.

In 1996, Title V of the 1990 amendments to the Clean Air Act imposed new requirements upon utilities. PEF was required to indicate the specific fuel it intended to burn at its plants, including CR4 and CR5. PEF specified that it would continue to rely on 100 percent bituminous coal that had powered CR4 and CR5 since their initial commercial operation. In 1996, PEF considered the economic viability of sub-bituminous coal to still be in doubt. The company asserted that this application required it to specify the fuels with which it could meet the applicable emission standards. Since only the performance of bituminous coal was known, PEF specified that fuel on the application. We agree that the company could not have listed sub-bituminous coal on the application without conducting a test burn, and that absent a cost analysis showing sub-bituminous coal to be the economic choice, a 1996 test burn would have been premature. Accordingly, we find that PEF's approach to its Title V application in 1996 was not unreasonable.

In 1999, another decision point was brought about by PEF's decision to purchase and burn synfuel at CR4 and CR5. This change required the company to revise its still-pending Title V application. No test burn was required since synfuel was expected to have similar burn characteristics as its main ingredient, central Appalachian bituminous coal. PEF again opted not to add sub-bituminous coal to its application. The record supports PFC's claim that sub-bituminous coal was still not economical for PEF in 1999. Furthermore, as of that point in time, the company had received no PRB coal bids. We find that this step-wise approach to amending the Title V permit was reasonable.

PFC became seriously interested in PRB coal in 1998. Its interest was evidenced early by a 1998 internal memorandum written by PFC's Vice President for Coal Procurement, Dennis Edwards. After discussing barge versus rail transport plans, he stated, "I believe we should recognize that we will, in all likelihood, be using PRB coals at [CR] 4 & 5 by about 2000 (my guess)." Also, in 1999, PFC's internal analysis showed PRB would potentially be the most economical by 2003.

In 2001, PFC received through an RFP solicitation its first economically competitive offer for sub-bituminous coal. PFC management was faced with the decision of whether to actively pursue the Title V permit modification necessary to utilize this fuel option. The company did not seek the modification to its permit, although the fuel had become a cost effective alternative based on its own analysis.

In 2003, PFC and PEF decided that sub-bituminous coal was becoming a viable option, and therefore attempted a test burn at Crystal River in spring 2004. However, a planning and communication failure by PEF management brought a halt to the test burn. Significantly, PEF's permitting personnel had to inform both PEF plant operations and PFC personnel that the company did not have the proper permits that would allow the burning of PRB coal on site. We believe this omission significantly delayed the completion of a full test burn until 2006. The company states it "continued evaluating PRB coal blends in 2005, after the 2004 hurricane season, which disrupted the evaluation of other coals." Based on a combination of internal and external evaluation results conducted in 2005, the company chose to conduct another test burn in April 2006. PEF recognized that by the time the 2006 test burn was conducted, the economic benefits of PRB coal had diminished.

Witness Kennedy testified that the Title V permit "imposes much more detailed requirements than the previous state air permits and Conditions of Certification," including "detailed fuel specification and data demonstrating assurance of compliance with all regulatory and permit condition limitations and requirements." Witness Kennedy stated that prior to the Title V permitting process, CR4 and CR5:

> . . . never burned anything except bituminous coal. Because burning sub-bituminous coal increases particulate matter and opacity levels, and PEF had to adhere to opacity and mass emission rate limits, PEF could not have burned sub-bituminous coal at CR4 and CR5 without at least notifying the DEP and EPA and probably doing a test burn of sub-bituminous coal. PEF did not do such a test burn, thus it did not have the unconditional authority to burn sub-bituminous coal at CR4 and CR5.

If test burns were required, the process would have taken approximately 14 months. The record reflects that as a result of its 1999 Title V application amendment to add synfuel (approved in 2000), and its 2006 Title V request for inclusion of sub-bituminous coal, that a modification to the Title V permit was obtainable within a reasonable period of time.

Therefore, we believe PEF's approach of including only known fuels in its Title V permit was reasonable. Operating under this approach, however, required PEF and its management to remain knowledgeable and attuned to the permitting process. Though PEF correctly modified its Title V permit in 1999 to include synfuel, it failed to proactively obtain the proper permitting requirements in 2004 for conducting a sub-bituminous coal test burn. This failure by PEF and PFC to remain aware of the Title V constraints caused the interruption of the 2004 test burn, thereby delaying possible future use of sub-bituminous coal at CR4 and CR5. PEF's failure to obtain proper permitting for the 2004 test burn caused PEF to lose flexibility in its ability to evaluate various types of coal. Looking at facts known to management at that time and under the circumstances we find this was an avoidable management error that could have been prevented were there better communications and control by PEF's management.

B. <u>Coal Procurement Practices</u>

OPC challenged PEF's coal procurement practices during the time frame in question. PEF testified that in obtaining coal for CR4 and CR5, PFC contracted directly with coal vendors, transportation providers, and transloading facilities. According to testimony, PFC established written coal procurement policies and procedures in 1987 to comply with the PSC guidelines and good business practices. Witness Davis testified that PFC's coal procurement efforts were overseen by the Vice President for Coal Procurement. Under his direction, coal prices were monitored on a continuing basis.

The record testimony reflects that when coal purchases were needed to supply PEF's plants, a competitive solicitation process was employed. RFPs were provided to all coal suppliers on the bidder list maintained by PFC. This list was comprised of over 100 suppliers, including PRB suppliers. In addition, PFC published notices of RFPs in coal industry publications to insure that anyone not on the bidders list had an opportunity to request to be on the list and to receive a copy of the RFP prior to the deadline. Coal procurement RFPs always included specifications for both bituminous and sub-bituminous coals, and solicited suppliers and brokers for domestic and foreign coals. PEF stated that it treated PRB suppliers the same as it did bituminous suppliers responding to the RFP. Any coal supplier would be added to the PFC bidders list upon request.

Once bids were received, they were evaluated and ranked based on evaluated cost or busbar cost using the Coal Quality Impact Model (CQIM). According to PEF, the model is a recognized industry standard and provides a "paper test burn" of the coal in a specific unit's boiler.

After the CQIM analysis identified the leading bids, in most instances, negotiations were then conducted with several bidders offering the lowest evaluated cost coals to obtain further price reductions. PEF used the same process for all of the RFPs issued over the period of 1996 through 2006.

Noting that witness Sansom testified that PEF could have encouraged PRB bids by sending letters directly to the coal producers, PEF contended it "sent seven such 'letters,' i.e. 'RFPs' to PRB coal producers" during 1996-2006 and received bids in response to four. OPC witness Sansom agreed that the PRB suppliers on PFC's bidders list comprised 70 to 80 percent of the PRB coal market production.

The record reflects that PFC examined the use of PRB coal regularly, including comparison of its fuel costs to those of Tampa Electric Company, which burned similar coal at its Gannon plant. Ongoing PFC comparisons showed that Tampa Electric Company was paying more for sub-bituminous coal than for bituminous coal. Sub-bituminous was not the lowest cost coal offered on an evaluated cost basis. In fact, it was generally not even competitive with other coal options.

PFC's interest in PRB coal was evidenced early by a 1998 internal memorandum written by PFC's Vice President for Coal Procurement, Dennis Edwards. After discussing barge versus rail transport plans, he stated, "I believe we should recognize that we will, in all likelihood, be using PRB coals at [CR] 4 & 5 by about 2000 (my guess)." Also, in 1999, PFC's internal analysis showed PRB would potentially be the most economical by 2003.

PEF made a procurement and operational decision to burn bituminous synfuel products in its CR4 and CR5 units beginning in 1999.[18] By 2001 and 2003, when spot purchasing peaked, the majority of these spot purchases were for synfuel. In 2001, 66 percent of PEF's coal was purchased on the spot market, followed by 60 percent in 2002, and 55 percent in 2003.

During the period of 1996-2002, PEF issued three coal bid solicitations, in 1996, 1998, and 2001. No PRB coal suppliers responded to the 1996 and 1998 bid solicitations. However, competitive PRB bids were submitted in response to the 2001 solicitation. PEF's evaluation of these bids identified PRB coal as the lowest evaluated cost alternative for a five-year contract. In fact, the most competitive bid received in response to the May 2001 RFP in terms of evaluated price was the PRB coal bid at two years offered by Arch Coal.[19] PEF ultimately negotiated a one-year contract for imported bituminous coal after negotiating with bidders who had submitted three-year contract offers. Regardless of the fact that PRB was not selected in the 2001 bid evaluations, we find that because these PRB bids were competitive in 2001, this knowledge should have triggered actions by PEF to put itself in a position to buy sub-bituminous coal if it should prevail in the very next coal solicitation. As noted above, PEF did not do so.

Furthermore, Witness Davis testified that in 2002, two large long-term contracts for bituminous coal expired. These were high-volume contracts. One of those expiring contracts, the Massey contract, constituted a purchase of over one million waterborne tons per year. Accordingly, PEF would have been in the position to augment its supply of coal for CR4 and CR5 with either a long-term PRB coal contract to replace expiring contracts, or spot purchases in those instances when PRB coal was the most cost-effective alternative.

We note that the relative mix of spot versus contract purchases made by PFC on behalf of PEF may have played a role in the emphasis, or lack thereof, given to PRB coal. During the period 1996-2005, PEF's mix of spot versus contract coal purchases varied widely. Witness Davis testified that PFC considered it prudent to have a "mixture of coal supply contracts by having an appropriate balance of long term, medium term, and 'spot' supply contracts." She also stated that the company would evaluate and forecast, using various industry services, "how much of our coal supply we wanted to be on medium-term contracts (such as 18 months to three years) and how much we wanted to purchase on a spot basis during a year."

The record reflects that while busbar analyses were conducted to evaluate bids, PEF did not always find it necessary to conduct an evaluated or busbar cost if PFC and PEF were familiar

[18] Synfuel is coal that has been chemically altered by the addition of reagents, such as Bunker C oil, i.e., heavy fuel oil. Coal and coal fines are the feedstock for synfuel and can be combined with fuel oil under heat and pressure to produce coal briquettes. OPC has argued that PEF bought synfuel from its affiliates. PEF responded that synfuel was purchased from affiliates and non affiliates, alike, at a discount to bituminous coal.

[19] As set forth in Exhibit 41, the May 2001 RFP required a minimum of 425,000 tons annually. The Arch Coal PRB bid for the 2 year contract was for 2.4 million tons, or 1.2 million tons per year, at an evaluated price of \$241.59/MMBtu. The next lowest evaluated bid price was \$243.61/MMBtu, a foreign coal bid by Carbones Del Quasare, S.A., a three year contract offered at 1.6 million tons, or 530,000 tons per year. The lowest evaluated bid price for CAPP coal was \$251.46/MMBtu, a three year contract offered at 1.425 million tons, or 480,000 tons per year. Three other PRB bids were received at evaluated prices lower than the lowest CAPP coal evaluated price, but all at significantly more tonnage than the minimum requirement.

with the pool of suppliers, and "with whose coal [PFC] had substantial experience, or on which [PFC] had previously done a busbar analysis." In contrast, witness Davis testified that sub-bituminous coal was a "type of coal in which an evaluated cost or busbar cost analysis could provide important information." Witness Davis also testified that "it was not practical to subject short term spot purchases to such modeling."

We find that since PFC did not conduct this type of analysis on spot market purchases, sub-bituminous coal may have suffered from being an unknown quantity during periods when the company emphasized spot market purchases. As witness Davis recognized, "Progress Fuel Corporation was a substantial purchaser in the spot market." We find this procurement focus created limitations that affected PEF's evaluation of PRB coals. This focus did not stem from a bias against PRB coals, but from the overall spot/contract mix and factors such as fuel price trend expectations.

We conclude that the overall purchasing methods and approach employed by PEF and PFC were generally reasonable. As required by Order No. 12645, PFC's coal procurement practices involved a competitive solicitation process. PEF provided substantial evidence of PFC's formal procedures regarding fuel procurement, including the application of such a competitive solicitation process. However, despite having an overall adequate process, we find that the company should have taken timely action to put PEF in a position to use PRB coal at an earlier point in time. Though the first-ever PRB coal bids were extremely competitive in 2001, PEF failed to take the actions that should reasonably have followed this development. PEF should have realized that PRB bids may prevail in its next RFP, and that taking actions such as preparing environmental permitting and acquiring a test-burn quantity of PRB coal should have begun immediately.

C. Coal Availability and Costs

1. Cost and Availability

We also analyzed whether PRB was available to CR4 and CR5 at a lower cost than that purchased by PEF for the years 1996 to 2005. OPC's witness Sansom presented the numbers of tons of PRB coal produced by year from 1992 to 2005 in Exhibit 7. Over the 1992 to 2005 period, production increased steadily from 200,000,000 to over 425,000,000 tons. During the 1996 to 2005 period, PRB coal producers were in an over capacity situation.

The situation was reflected in PRB coal prices in the 1990's, when Southern Company found it economical to convert ten of its coal units to PRB coal units. Witness Putnam testified that during his employment with Southern Company in the 1990's, he worked on converting several coal burning units in Alabama, Georgia, and Mississippi to PRB coal burning units, that some of the most competitive bidding competitions he experienced at Southern Company involved PRB opportunities, and that Southern Company and its utilities were "covered up with coal people . . . begging us to come visit the PRB region and to their mines so we would consider their coals."

PEF's witness Heller also presented spot prices in dollars per ton for 8,800 Btu/Lb PRB coal for 1994 to 2006 and annual spot prices for 8,800 Btu/Lb PRB Coal for 1996 to 2005, as set forth below:

Annual Spot Prices of PRB Coal	
Year	$/Ton
1996	5.00
1997	4.36
1998	4.01
1999	4.63
2000	4.54
2001	4.66
2002	11.30
2003	7.08
2004	6.09
2005	6.57

PEF evaluated its potential coal purchases on a delivered price (including transportation costs) basis, and a busbar ("evaluated") basis, accounting for coal quality characteristics on unit performance, and considered other factors such as transportation and supply reliability. This "busbar" evaluation is necessary to determine how the coal would perform when burned at CR4 and CR5. PEF used a standard industry model for evaluating coal. PEF notes that CR4 and CR5 are base load units and that the coal supply and consistent energy production are essential. PEF included PRB coal suppliers in all RFPs and was aware of possible supply disruptions and cost impacts from burning a 50/50 blend of PRB/CAPP coal, including a potential megawatt derating. PEF first received offers from PRB suppliers in 2001, and began making PRB coal evaluations. Starting in 2001, PEF began receiving PRB bids. PEF argued that based on evaluations of those 2001 RFP responses, PRB coal was not competitive. PEF made similar evaluations following its 2003 RFP, with different conclusions, and made test burns of 18 to 22 percent blends in April 2004. PEF made further test burns in 2006 and concluded that, by then, PRB coal was again more expensive to burn than its present supply.

PEF pointed out that witness Sansom's delivered price analysis is flawed because: 1) the prices are not from the same period, 2) TECO's transportation costs do not include Gulf terminaling, and transloading, and 3) TECO's transportation costs do not include PEF's waterborne proxy. PEF pointed out that witness Sansom's analysis also excluded considerations for capital and O&M costs that would have been necessary had PEF changed its coal supply to a 50/50 blend. PEF defended its assertion that additional blending costs for PRB coal would have been incurred by using a 50/50 blend.

PEF pointed out that, although witness Sansom based his overcharge calculation on using the supply route through New Orleans, he claimed that using the route through Mobile, Alabama, would have been more economical, but that none of the OPC witnesses offered defensible evidence to support that claim. PEF relied on witness Heller's interpretation of witness

Sansom's analysis. Witness Heller concluded that had PEF burned a 50/50 blend of PRB/CAPP coal from 1996 to 2005, recovered transportation costs using the waterborne proxy, and included blending charges and capital and O&M costs, it would have in fact paid $51 million more in coal costs.

Based on the information presented by witness Sansom regarding PRB coal production and the testimony of witness Putman regarding the efforts of PRB coal producers to make coal available to customers, we believe ample supplies of PRB coal were available for purchase during the period 1996 through 2005. We find that the annual spot prices in dollars per ton and cents per MMBtu, the prices in Column (1) of witness Heller's Exhibit 84, to be credible. These prices, which did not include transportation costs, were uncontested in the hearing. Transportation costs must be added to the mine price to accurately reflect the delivered cost of coal to CR4 and CR5.

2. Transportation Strategies

PEF argued that the Commission-approved waterborne proxy, when added to the cost of PRB, made PRB more costly than what PEF actually burned. OPC stated that the argument offered by PEF for not burning PRB coal involved using the "waterborne proxy" to calculate PRB coal delivered prices. Witness Sansom testified that PRB coal could have been moved via three possible options: an all-rail route from the Powder River Basin to Crystal River, an all-barge river/Gulf route, or a mixed route of rail to Mobile and Gulf barge to Crystal River. Witness Sansom stated, however, that such shipments of PRB coal would have reduced the affiliates' barge and dock revenues. Sansom stated that the most economical route would be via McDuffie terminal in Mobile and that this fact was confirmed by the bids for all rail coal transported to McDuffie received in PEF's August 2002 and May 2003 RFPs. Witness Sansom reasoned that PRB coal would have been less expensive than bituminous coal barged to IMT in New Orleans and transloaded to barge for delivery to Crystal River. He stated that the least expensive route to move PRB coal to Crystal River would be by rail to the Alabama state docks at McDuffie. Witness Sansom stated that the McDuffie terminal had capacity, could blend coal if necessary, and would have been a less expensive barge haul than from the IMT in New Orleans. Therefore, in his opinion, it was the most efficient route for PRB coal to CR4 and CR5.

Witness Sansom testified that our orders do not apply to transportation rates for PRB coal, and that we never accepted witnesses Davis's and Heller's mileage prorate method of estimating barge rates. Witness Sansom testified further that the waterborne proxy applies only to moves from upriver docks via river barges and imported coal. Witness Sansom notes, however, that had PEF actually made purchases of PRB coal, the rail-to-St. Louis route would not have been economical compared to the mine-to-Mobile, Alabama, rail route. Regarding the application of the waterborne proxy to PRB coal purchases in their bid analyses, witness Sansom testified that "they assumed in their bid analysis, that is the proxy, rather than relying on the market and, therefore, denied the ratepayers the benefit of market forces through the application of a methodology."

PEF witness Davis described PEF's coal transportation options to CR4 and CR5 as CSX rail and water barge, pointing out that the waterborne option provides an alternative in the event of a rail strike and other disruptions. The existence of two alternatives provided leverage in negotiating rates for both forms of transportation. Witness Davis stated that transportation was a significant portion of the delivered price of all coal purchases, and in the case of sub-bituminous coal, transportation costs surpass the commodity cost of the coal itself.

Witness Davis stated that PFC's approach to coal transportation for CR4 and CR5 was to maximize the use of rail transport, as directed by us. Of the two long-term contracts that ended in 2002, one called for rail delivery and one for barge delivery. She claimed that this complied with our directive to maximize rail deliveries. Witness Davis said that because CR4 and CR5 burned compliance coal, PFC found it harder to obtain rail transport for compliance coal, so waterborne transport was emphasized for CR4 and CR5. Witness Davis said that it would be neither possible nor desirable to receive all coal shipments at CR4 and CR5 by rail.

Witness Davis pointed out that CSX railroad is the only railroad serving Florida and maintains a one-way only rail line between Dunnellon and Crystal River. This makes it impossible to run more than one train at a time to the Crystal River complex, which is served by a rail loop going to the plant and back out to the main line. Due to operational limitations of its facilities, it would not be possible for all of its coal to be received via rail, thus ruling out one option for PRB delivery suggested by OPC witness Sansom.

The waterborne proxy is a number of dollars per ton used by PEF to recover water transportation costs since 1992. PEF evaluated any potential PRB coal purchases using estimated rail rates to St. Louis and a fraction (995/1564, based on mileages) of the Ceredo Dock to New Orleans proxy. The proxy charges appear by year in witness Heller's Exhibit 84, along with additional charges for rail-to-barge transloading (St. Louis) and blending (New Orleans).

For the waterborne transport of domestic coal, witness Davis said that until 2004 PEF used a waterborne proxy rate established by us to compute transportation costs for coal delivered by water to CR4 and CR5. The waterborne proxy rate included truck transfer from the mine to the river dock, transloading to the river barges, transport costs down river on the Ohio and Mississippi rivers, transfer to coal storage or to transload from a river barge to an ocean barge at IMT in New Orleans, and cross Gulf barge rates for delivery to CR4 and CR5. The waterborne proxy established in 1993 was based on 1992 actual costs and was thereafter annually escalated upward or downward as waterborne transport rates changed. The proxy was replaced in 2004 by a stipulated charge, to which OPC agreed, and again in 2005 to market-based rates, to the extent they existed. Witness Davis noted that in 2004, we approved a waterborne proxy for imported coal, FOB the barge, for transport activities associated with barging imported coal to Crystal River during 2001-2003, less the transloading component incurred by the imported coal supplier.

Witness Davis testified that proxy transportation rates were established by us to replace cost-plus pricing, which had led to lingering suspicions that it resulted in higher costs due to affiliate transactions, and that PEF could have lost money under the proxy arrangement. Witness Davis further testified that when PEF purchased foreign coal at IMT, in the second year of proxy cost recovery, we agreed to allow PEF to apply 50.2 percent of the "full proxy" to those tons, to recover transloading and cross-Gulf transportation costs.

Witness Davis states that in evaluating the delivered cost of coal to CR4 and CR5, PFC employed the applicable waterborne proxy rates established by us in 1993 to each transport stage as necessary. Though OPC disagrees, PEF contends that this proxy is applicable to any domestic coal, and, therefore, that its use in evaluating the delivered cost of PRB coal is appropriate.

We find that central to the topic of transportation strategy is the question of whether, in its evaluation of PRB coal costs, PEF should have used the waterborne market proxy coal transportation rates established for PEF.

Order No. PSC-93-1331-FOF-EI[20] describes the components that are included in the transportation market price proxy:

> The market price for EFC's water-borne deliveries would cover the transportation components to the Crystal River plant site. This would include short-haul rail/truck transportation to the up-river dock, up-river barge transloading, river barge transportation, Gulf barge transloading (IMT), Gulf barge transportation (Dixie Fuels), as well as port fees and assist tug. The market price would also cover, i.e., replace, the return on EFC's equity investment in IMT and Dixie Fuels currently provided under cost-plus pricing for water transportation.

Id. at 5. By Order No. PSC-94-0390-FOF-EI,[21] the market price proxy for PEF was clarified:

> The parties agreed that the existing market pricing mechanism for the transportation of domestic coal should be modified to exclude cost components (e.g., river barging costs) not involved in the transportation of foreign coal.

Id. at 4.

We believe that PEF's use of the waterborne market proxy rates for evaluating PRB coal was appropriate. Order No. PSC-93-1331-FOF-EI did not limit its application and, in fact, the clarifying order explained that the pricing mechanism is for transportation of domestic coal. PEF testified that it followed our orders in calculating transportation costs. Inclusion of the proxy in the purchase price affected PEF's evaluated price for burning PRB coal. We also believe that the busbar analysis was appropriate and did not penalize PRB coal. Therefore, we find that PEF's evaluations of potential PRB purchases were the proper prices for PRB coal-purchase evaluations. However, even applying the waterborne market proxy coal transportation rates, we find that the costs of PRB were lower than the coal actually procured by PEF for the years 2003, 2004, 2005. We discuss these costs more specifically below.

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[20] Order No. PSC-93-1331-FOF-EI, issued September 13, 1993, in Docket No. 930001, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor.

[21] Order No. PSC-94-0390-FOF-EI, issued April 4, 1994, in Docket No. 940001-EI, In re: Fuel and Purchased Power Cost Recovery Clause and Generating Performance Incentive Factor.

D. Megawatt Capacity

PEF argued that its customers received a benefit by the use of higher btu bituminous coal at CR4 and CR5. PEF testified that it was able to generate 750 and 770 MW gross from the plant rather than the 665 MW gross the plant was designed for. OPC disagreed and testified that the plant was designed to generate the 750 and 770 MW using the design blend of 50/50 PRB and bituminous coals.

As stated, the CR4 and CR5 units are baseload, must-run units providing low cost power on a first-call basis, and any action that causes a reduction to the generation output of CR4 and CR5 would necessarily be replaced by generation that is more costly. We believe the continuing reliable operation of CR4 and CR5 is of paramount importance. Witness Toms testified that the basic issue in the operation of these units is reliable generation:

> [T]he biggest concern for me in terms of operation of Crystal River 4 and 5 is a potential derate. The company's energy control center expects me to run these units to get 732 and 735 net megawatt output.

Witness Toms explained that the units have historically operated at overpressure to produce 750 and 770 MW gross when called upon, providing about 732 to 735 MW to meet consumer demands. He attributed this high output to the larger boilers in these units, allowing for more coal to be burned. He testified that PEF's customers have gotten the benefit of increased output from the units. Witness Toms testified that he cannot achieve an output of 750 megawatts with only five pulverizers operating. He explained that changing particle size to increase feeder speed tends to slag the boiler. He later stated that, as to particle size, "smaller is better."

PEF witness Davis testified that PEF was aware of PRB coal in the period 1996-2002, and examined it regularly. She stated that, if PRB coals were to be used, PEF saw potential for derating and additional costs because of the difference between that fuel and the bituminous coal. Witness Davis testified that she worked closely with Mr. Dennis G. Edwards, who was VP of Coal Procurement and that he looked at PRB many times. Witness Davis described certain discussions she had with Mr. Roy Potter, who was manager of technical services and performed the quality analysis of coals to be used at Crystal River. According to witness Davis, Roy Potter was very highly regarded for his coal analysis, and that he responded to her inquiries with an explanation that burning the lower quality PRB coal would derate the boilers. Witness Davis provided documents that demonstrate that PEF continued to monitor PRB coal for potential future use in the period of 1996 through 2002.

In support of its position that there would be no derate with the design blend, OPC offered testimony of the design engineers, testimony regarding the operation of similar units, and exhibits consisting of portions of the original contract documents. We find that the testimony and exhibits are not conclusive evidence that CR4 and CR5 would continue to operate at 750 to 770 MW capacity if a 50/50 blend of coal were used.

The similar units that were discussed by OPC witnesses Sansom and Putman, along with the descriptive information provided by the witnesses, do not provide a sufficient basis to assume that they are identical to CR4 and CR5 with regard to design or performance. While the units may be the same or similar vintage, the record is limited as to evidence of capacity rating, efficiency, and performance of those units. Similar design of units is just one of a multitude of factors that might contribute to similar or dissimilar performance of those units at the present time. The record does not address how the units compare to each other in categories such as rank within the dispatch of their native generation fleet – except for the information that Plant Daniel was not called on as much as other plants. It would be a matter of speculation to draw an inference about how experience at any particular plant might be similar to, or dissimilar from, the expectations for PRB coal use at Crystal River.

The testimony provided by OPC witness Barsin was very detailed in regard to the efforts made within the original design to provide a sufficiency of fuel, as well as accommodations for slagging and fouling factors associated with PRB coal. However, there is not sufficient evidence of a "guarantee" of gross generation in a range of 750 MW to 770 MW, without regard to the fuel that might be involved. Notwithstanding the extensive effort described by witness Barsin to design a unit that would run well using the PRB blend, the record documents show the term "guarantee" only on the projected performance associated with steam flow of 4,737,900 lb/hr at 2500 psig and 1005 degrees Fahrenheit. The same documents confirm that the steam is to be supplied to a turbine rated at 665 MW. The contract documents included with the "Projected Performance" information make no mention of output beyond 700 MW. We find that the guarantee of 665 MW gross generating capacity burning the 50 percent PRB fuel blend is evident in the record. In addition, the record reflects that the steam equipment, as installed, is designed to operate without any time limit at pressures 5 percent greater than that required for the 665 MW nameplate capacity. While we believe that burning a 50 percent blend of PRB and bituminous coals would cause operational difficulties, we find that burning a lower percentage blend appears to be a viable option.

A test burn of lower percentage PRB was conducted by PEF at the Crystal River site in 2004. The blending was done off-site. The 2004 test burn was not completely successful. The PEF Strategic Engineering Group investigated the possibility of using PRB as fuel for CR4 and CR5 and issued a report which indicated that using PRB blended off-site at less than 30 percent and delivered by barge would offer substantial savings and fuel flexibility. The report concluded that a blend with bituminous coal and less than 30 percent PRB coal would act like bituminous coal. The report predicted savings for the years 2007-2010 from a 20 percent PRB blend, based on a high level of costs. Some expensive items, such as water cannons and soot blowers, would be necessary capital additions. Witness Hatt also indicated that PRB coal at blends under 25 percent could likely be used.

In 2005, PEF hired Sargent & Lundy to assess the use of PRB coal at CR4 and CR5. That study indicated that a blend under 30 percent was likely to prove cost effective. Blending off-site was recommended in that report as well. In 2006, PEF successfully completed a short-term test burn of a lower blend of PRB (20 percent) and bituminous coal.

We agree with PEF that the performance of CR4 and CR5 must not be compromised. To date, the evidence provided by PEF shows that CR4 and CR5 will be able to maintain availability and capacity while using a low percentage of PRB coal. The studies have all assumed that blending will be done off-site. We concur.

E. CR4 and CR5 Operational Matters

In addition to the potential for derate, the parties debated on the record whether the use of a blend of PRB coal would have created operational difficulties at CR4 and CR5. OPC argued that a change from the bituminous coal that has been burned at CR4 and CR5 to the "design blend" would involve minimal risks to the operation of CR4 and CR5. On the other hand, PEF argued that after CR4 and CR5 came on line, and before 1996, extensive trade knowledge developed regarding several operational issues associated with the use of coal from the Powder River Basin.

Witness Sansom testified that the boilers at CR4 and CR5 were sister units to the Belle River unit near Detroit and the Miller Plant in Alabama. He stated that all these boilers were designed together. He recounted some details regarding the way the boilers were designed to accommodate burning PRB. PEF witness Hatt, however, argued that OPC's witness Sansom "provides an ultra-simplistic explanation of the differences" associated with handling and using PRB coal, from an operational and safety perspective. PEF witness Hatt provided an assessment of the "sister units" concept used by the OPC witnesses. He explained that the similarities in design may be limited to specific sections of the equipment, such as the boiler. Witness Hatt stated that the coal-yard situations of the "sister units" are completely different from the Crystal River coal yard. Further, as to the matter of "similar design," witness Hatt used the illustration of two cars of the same make, model, motor, and drive train that could have significant performance and maintenance differences, as when one car is a "lemon." He testified that similar differences can exist between "sister units."

Moreover, the information provided by OPC's witnesses do not provide sufficient actual data for comparison with any operation other than Crystal River. Witness Putman's testimony regarding Plant Daniel reverting to high Btu fuel in order to return to full load generation implied that the Plant Daniel units have not operated at a high capacity factor when fueled with PRB coal. However, CR4 and CR5 are routinely high in the dispatch order and generate at a high capacity factor. We find that the issues of pulverizer capacity, burn rate, and capacity factors for those sister units are not sufficiently addressed in the record. These factors are critical factors by which to compare generating units. For example, we believe it would have been important to know how components of those comparable units work together in such functions as fuel storage, feeding and processing, or whether the fuel is drier or the particles are larger at the boiler entry point. The information provided indicates that some units do manage PRB successfully, according to their needs and requirements, but it is not possible to make a direct comparison between the alleged comparable units and CR4 and CR5 and how they would incorporate PRB coal in a cost effective manner.

OPC's argument on the operational affects of burning a PRB blend at CR4 and CR5 was also based on design documents that included PRB coal as a possible fuel, along with Illinois coal or high Btu bituminous coal. The facilities for CR4 and CR5 at Crystal River were designed and installed prior to 1985. OPC alleged that the capability of CR4 and CR5 to use a 50 percent blend of PRB was guaranteed in the design documents. According to OPC witness Barsin, in his experience the entire projected performance document was treated as a guarantee. He testified that the attorney for his company told him it was a guarantee. OPC argued that because the guarantee is part of the document, PEF should be able to operate CR4 and CR5 at overpressure and produce the same MW output as PEF produces with the bituminous coal now being burned. As addressed above, we are not persuaded by OPC's guarantee documents.

In contrast, PEF offered testimony of the actual experience at Crystal River. PEF witness Toms testified as to the day-to-day operations at CR4 and CR5, and the factors that are crucial to the units operating with the performance reliability that they have shown. For example, witness Toms testified that if the fuel rating falls lower than the range of 11,000 to 11,300 Btu/pound, CR4 and CR5 are not able to operate at overpressure. He explained that particle size of the fuel entering the boiler is crucial -- the smaller the better. He stated that in his experience five pulverizers are not sufficient to maintain the units at full capacity. Alternatively, the fuel grind might be set for a larger particle size in order to increase the flow through the pulverizer, but the pulverizers must grind to a size that does not slag the boiler.

We find the testimony of witness Toms to be persuasive. In comparing the experience recounted by witness Toms to the assertions made by witnesses Sansom and Barsin, there are different views as to the performance to be expected from CR4 and CR5. Although witness Barsin's explanation of his design, along with the calculations provided, might lead to a presumption that five pulverizers are adequate to supply either of the CR4 or CR5 units, the experience of witness Toms contradicts that presumption. Based on actual operating experience, witness Toms testified that with only five pulverizers available, the units cannot produce the expected 750 or 775 MW. The record indicates that particle size and silo capacity (or through-put) limit the production of the utility. Witness Barsin's testimony addressed design calculations. It does not sufficiently address particle size, or show why limits on silo capacity would not curtail the steam production.

OPC witnesses asserted that the installed equipment has been suitable for storing and blending PRB coal as fuel for generating electricity from the in-service date through 2006. We do not believe that the record supports the position that blending the "design basis coal" on-site at Crystal River. Issues of safety and cost are relevant to PEF's analysis. Current industry standards, as indicated in testimony and exhibits of PEF witness Hatt, are designed to manage the explosive characteristics associated with PRB coal. We believe that PEF would need to bring the Crystal River site up to current operating standards for handling PRB coal if that material were to be blended on site.

While we found that on-site blending and the burning of a 50 percent blend of PRB and bituminous coals would cause operational difficulties, we find that burning a lower percentage blend appears to be a viable option. A test burn of lower percentage PRB was conducted by PEF at the Crystal River site in 2004. The blending was done off-site. The PEF Strategic Engineering Group investigated the possibility of using PRB as fuel for CR4 and CR5 and issued a report which indicated that using PRB blended off-site at less than 30 percent and delivered by barge would offer substantial savings and fuel flexibility. The report concluded that a blend with bituminous coal and less than 30 percent PRB coal would act like bituminous coal. The report predicted savings for the years 2007-2010 from a 20 percent PRB blend, based on a high level of costs. Some expensive items, such as water cannons and soot blowers, would be necessary capital additions. Witness Hatt also indicated that PRB coal at blends under 25 percent could likely be used. Dust control would be necessary with the lower percentage blend, but capital investments are much lower when blending is offsite. In 2005, PEF hired Sargent & Lundy to assess the use of PRB coal at CR4 and CR5. That study indicated that a blend under 30 percent was likely to prove cost effective. Blending off-site was recommended in that report as well. The report recommends some equipment additions and modifications to go forward, and included a confidential assessment of cost for material and installation.

F. CR3

PEF argued that PRB coal carries significant risks of fires and explosions. PEF witnesses Franke and Miller testified that there are safety and regulatory concerns about burning PRB coal in units sited with a nuclear plant. The Crystal River site has a nuclear unit – CR3 – and four coal units – CR1, CR2, CR4, and CR5. CR3 has a capacity of approximately 838 MW and came online in early 1977. The nuclear unit is subject to regulation by the Nuclear Regulatory Commission (NRC). Both witnesses Franke and Miller testified that there are no nuclear units collocated with coal plants that burn PRB.

CR1 and CR2 were the first units built at the Crystal River site. CR3 followed and began operation in 1977. CR4 and CR5 were built after CR3. PEF updated its Final Safety Analysis Report (FSAR), an important NRC licensing document, when CR4 and CR5 were built. According to witness Franke, PEF did not tell the NRC that the units were designed to burn a 50/50 blend of bituminous and sub-bituminous coal. The FSAR reflected PEF's expectation to use bituminous coal at CR4 and CR5. The updated FSAR reflected the site's layout, including coal piles, handling equipment and conveyors and the proximity of these features to the reactor building. We note that both the industry's understanding of the risks posed by PRB coals and nuclear safety standards have changed since CR4 and CR5 became operational.

As stated, in 2004, a test burn for a blend of PRB coal was conducted. CR3 staff were contacted when the 2004 test burn was planned. The CR3 staff expressed concern and required that the blend with PRB coal be blended off-site. The blend burned during the 2004 test burn had 15 percent to 22 percent PRB coal.

In its brief, White Springs stated the following:

> In sum, at most Mr. Franke and Mr. Miller's testimonies do little more than describe the NRC rule on risk assessment and possible license amendments. Since none of the assessments Mr. Franke claims must be performed have even been started, there is only conjecture regarding what action (e.g., filing a report, mentioning PRB coal use in the next update to the FSAR, request for a license amendment, etc.) might be required by the NRC.

Witness Franke testified, however, that he does not want PRB coal at the Crystal River site given its potential problems.

PEF witness Miller and Franke testified that, if PRB coal is to be burned at the Crystal River site, then a risk evaluation would be required by 10 C.F.R. 50.59. Neither witness Miller nor witness Franke can say whether this evaluation would lead to the requirement of a license amendment application with the NRC. Though PEF has planned and carried out test burns of PRB coal, the CR3 staff had not begun a 10 C.F.R. 50.59 analysis.

In its brief, White Springs stated that CR3 staff was aware that PRB coal was at the Crystal River site in 2004 and 2006. White Springs argued that, if PRB coal would trigger an incremental risk evaluation pursuant to NRC regulations, then PEF already should have performed the evaluation. According to White Springs, delays in performing the evaluation may be a separate instance of imprudence.

The record shows that PRB coal has unique issues regarding dust and combustibility. We agree that this would have triggered an NRC risk evaluation had PEF committed to long-term use of PRB coal at Crystal River. While this evaluation may not lead to a license amendment application with the NRC, it might lead to capital expenditures for dust control and fire protection equipment. The record does not quantify any costs. We find, however, that the NRC safety regulations governing CR3 would not preclude PRB coal from being blended off-site and burned at the Crystal River site.

G. Affiliates

OPC alleged that PEF ignored PRB to favor its affiliates. The evidence shows that PEI owns 100 percent of PEF (formerly Florida Power Corporation), PFC, Black Hawk Synfuel, KRT Holdings and Kanawha River Terminals. PEI also owns 10 percent of New River Synfuel. Black Hawk supplies coal to New River as a feedstock for synfuel. New River sells the synfuel to utilities and industrial customers, including PEF. Witnesses Davis, Pitcher, and Weintraub have worked for Black Hawk Synfuel. Affiliate relationships definitely existed for PEF coal procurement during 1996 through 2005.

New River pays Black Hawk fees for marketing synfuel, acquiring feedstock, and operating and maintaining the synfuel plant. Also, at times, PFC, on behalf of PEF, and Black Hawk are competing in the same coal markets. New River, which apparently is 90 percent owned by GE Capital, owns the plant and land but Black Hawk manages the business.

PEF witnesses Davis and Pitcher testified that PEF's affiliate relationships have been disclosed to us and have been the subject of a number of Commission proceedings. Witness Pitcher testified there was no favoritism toward PEF affiliates. He stated that when he was on the sales side of PFC, he was treated like any other bidder. When he was on the procurement side, he treated affiliates like any other bidder. A firewall prevented bidders, PEF affiliates or otherwise, from gaining an unfair advantage in the RFP process.

PEF witnesses Davis, Pitcher, and Weintraub all testified that they bought coal for PEF on the basis of lowest delivered cost consistent with coal quality specifications. Coal bids were evaluated for cost and performance with a CQIM model, which is a "paper test burn." Synfuel and coal were evaluated in the same manner. PFC on behalf of PEF also looked at coal quality and the reliability of the supplier. PFC sold coal to PEF at cost.

According to witnesses Davis, Pitcher, and Weintraub, synfuel was sold at a discount to bituminous compliance coal. The discount was about one to two dollars per ton with similar heat content. The coal feedstock for synfuel was priced higher than synfuel, with the spread being about four dollars per ton. This business model worked because the synfuel could generate tax credits. On this point, PEF witness Heller stated "the discount for synfuels reflects a sharing of the producers' tax savings with the customer as an inducement to the customer to purchase synfuels rather than coal."

We note that the approximately four dollar per ton spread between the price of coal feedstock for synfuel going into the plant and the price of synfuel coming out of the plant could have provided suppliers incentive to sell coal to synfuel producers rather than utilities. However, PEF testified that it evaluated and bought coal and synfuel on the lowest delivered cost basis consistent with coal specifications. Also, as noted, synfuel sold at a discount to coal. We believe that such a possible incentive is not tantamount to PEF being biased in its procurement practices.

If a company had a majority equity interest in a synfuel producer, sales from that producer to affiliates would not create tax credits. The parent company of PEF did receive tax credits for affiliate sales of synfuel to CR4 and CR5 based primarily on its 10 percent equity interest in New River. However, the tax credits generated by affiliate synfuel sales to CR4 and CR5 were a very small percentage of the overall synfuel-related tax credits that PEI claimed for the period 2000 through 2005. From 2003 to 2005, synfuel sales to CR4 and CR5 decreased significantly because import coals became less expensive.[22] PFC affiliated synfuel production remained relatively constant.[23] Given PEF's change to import coal from synfuel four years before the expiration of the synfuel tax credit, we believe OPC's argument that affiliated transactions influenced PEF's coal procurement decisions fails.

As stated, Black Hawk Synfuel LLC is wholly-owned by PFC and ultimately by PEI. Black Hawk operated the New River synfuel plant and handled New River's purchasing and marketing. This arrangement could provide PEF with some incentive to favor New River synfuel. However, PFC purchased coal and synfuel for PEF on the basis of lowest delivered

[22]In this regard, witness Weintraub testified, "In other words, it was cheaper to bring import coals in from foreign sources across the Gulf than transport coals across the country. When PFC and PEF were displacing synfuels with these cheaper import compliance coals it obviously was not with an affiliated producer."

[23]Witness Weintraub testified, "After 2002, the synfuel tons sold to PEF for CR4 and CR5 has dropped off dramatically from prior synfuel sales for CR4 and CR5, falling about two-thirds in 2003, to a little over 100,000 tons in 2004, and only 12,481 tons in 2005 (as a carryover from the prior year). During the same period, however, affiliated synfuel producers were producing 12.4 million tons of synfuel in 2003, 8.3 million tons of synfuel in 2004, and 10.1 million tons in 2005, and selling this synfuel in those years to other utilities and industrial customers."

costs consistent with coal quality specifications. We believe that PEF's coal procurement practices, as carried out by PFC, would have eliminated this possible incentive.

Elaborating on the charge of favoritism, witness Sansom recounts a July 2003 bid analysis in which a non-affiliate offer, initially determined to be the low bidder, was later turned down after PFC negotiated with its affiliate, Black Hawk Fuels. Witness Sansom points out that Black Hawk had no firm supply of coal to back its offer, though a supply was located during the negotiations. Ultimately no purchase was made by PFC from either supplier but witness Sansom states that ratepayers were harmed since the coal needed was obtained in 2004 at higher prices. We disagree with the favoritism charge and note that Black Hawk was a broker and, as such, would not own or control coal that it bids. PEF bought coal on the basis of lowest delivered and evaluated cost. Moreover, we believe these kinds of transactions are common when dealing with coal brokers. Generally a coal broker who does not own or control coal can respond to an RFP without having a firm supply.

The record does not support the argument that PFC purchases from affiliates resulted from preferential treatment of affiliate companies. Though PFC bought a large amount of synfuel from affiliates in the early part of this decade, we believe this is reasonable because these affiliates were among the nation's largest producers of synfuel. The record reflected that PFC purchased synfuel from non-affiliates, as well.

Other utilities purchased the majority of the synfuel sold by PEI affiliates during these years, with the PEF purchases representing a miniscule percentage of both total sales. The unusual opportunity for utilities to take advantage of the tax credits while simultaneously paying a lower price for synfuel products than for bituminous coal created an industry phenomenon for a period of time. Finally, the relatively small percentage of PEI's total synfuel credits represented by PEF's synfuel purchases argues against OPC's contention that the synfuel use was an effort to pad the profitability of its parent company. Although PEF bought and transported coal using affiliate companies during the period, the record does not reflect that PEF inappropriately dealt with its affiliates for purposes of procuring coal during 1996 to 2005. We find PEF's activities with affiliates met our guidelines.

H. Conclusion on Prudence of PEF Coal Procurement Activity

We find that PEF acted prudently in purchasing coal for CR4 and CR5 from 1996 to 2001. We find, however, that beginning in 2001, PEF did not act prudently in placing itself in a position to purchase PRB coal for CR4 and CR5. During 2001 and 2002 PEF did not seek revisions to its environmental permit, it did not conduct PRB coal test burns, it did not modify its plant to burn PRB coal on a long-term basis, nor did it purchase PRB coal.[24] Despite the fact that PFC recognized in May 2001 that PRB coal was very competitive, on an evaluated basis, with the types of coal it had historically purchased (CAPP coal and foreign coal) on behalf of

[24] While PFC purchases coal on behalf of PEF, PEF management are fully responsible for the purchase decisions of PFC management. Page 4 of Order No. 21847, issued September 7, 1989, states that we will review and subject the activities of EFC (Electric Fuels Corporation, the predecessor to PFC) to the same scrutiny and standards that we would apply to FPC (Florida Power Corporation, the predecessor of PEF) if they had procured their own fuel.

PEF, prudent steps were not taken. We find that PEF management's failures to act despite its affiliate managements' knowledge that PRB coal was a cost-effective alternative was imprudent. We find that while PEF did not pay excessive fuel costs for the years 1996 through 2002 it did pay excessive fuel costs from 2003 through 2005.

PFC's evaluation of the market response to the May 2001 RFP proved that PEF could no longer afford to be unprepared to purchase PRB coal on either a spot or contract basis. With the May 2001 bid responses, PEF's management had received incontrovertible evidence, even assuming PEF waterborne proxy transportation rates, that PRB represented a very competitive coal purchase option for PEF's CR4 and CR5 generating units for both current and future coal purchases. To prepare for such purchases, PEF should have immediately sought a permit revision and conducted test-burns of PRB coal at CR4 and CR5. According to PEF's witness Kennedy it would have taken PEF approximately 14 months to amend its Title V permit. If PEF management had pursued PRB coal aggressively beginning in May 2001, PEF would have positioned itself to be permitted and ready to burn PRB coal by no later than January 2003. However, as PEF's testimony reveals, PEF did not know that it was not allowed to burn PRB coal per its Title V permit at the time of its April 2004 test burn. The period of May 2001 through April 2004 represents a three-year period during which PEF's lack of awareness of the permit status of its own power plants cannot be viewed as simple managerial oversight.

Order No. 12645 includes a recovery criterion that all expenses associated with fuel procurement be reasonably competitive in cost or value relative to what other buyers are paying under similar terms and conditions. CR4 and CR5 were designed to burn PRB coal, PRB coal was evaluated by PEF as a competitive alternative in May 2001, coal transport options were available to PEF for PRB coal deliveries, and many other Southeastern utilities were purchasing PRB coal for their power plants. Given these circumstances, we find that PEF was imprudent to not immediately seek permit modification to allow PRB to be burned at CR4 and CR5 after its May 2001 bid evaluation.

On the matter of coal procurement practices, we find that if PEF had taken the prudent step of obtaining a revision to its Title V permit in mid-2001, it would have been in the position to seize upon market opportunities for PRB coal by January 2003. Two high-volume long-term coal contracts for CR4 and CR5 expired in 2002, and one of those expiring contracts was the Massey contract, constituting a purchase of over one million waterborne tons per year. PEF would have been in the position to augment its supply of coal for CR4 and CR5 with either a long-term PRB coal contract to replace expiring contracts, or spot purchases in those instances when PRB coal was the most cost-effective alternative. We find that it was imprudent for PEF to not purchase PRB coal when it was cost-effective to do so in 2003-2005.

Regarding CR4 and CR5 operational matters related to burning PRB coal, the capital and operational cost impacts of burning PRB coal at these units would be quite limited if the quantities were restricted to blends less than 30 percent PRB coal blended off-site. Thus, we find that the evidence in the record indicates that PRB coal blends less than 30 percent for CR4 and CR5 could have been purchased for the January 2003 through December 2005 period without incurring large incremental capital or operating costs. We find that PEF was imprudent to not incur the minimal operational and capital costs to be able to safely burn a 20 percent blend of PRB coal beginning in 2003.

We agree that the 50/50 blend could cause a derate of the MW capacity at CR4 and CR5. However, we find the evidence in the record supports a long-term 80/20 blend of bituminous coal to PRB coal with no derate at CR4 and CR5.

PEF's imprudence in failing to seek modification of its Title V permit and to conduct test burns of PRB was not without consequence. PEF incurred excess costs by failing to purchase PRB in 2003, 2004, and 2005. The calculation of excess costs is considered below. PEF witness Heller concludes his direct testimony with the following statement: "In 2004-2005, it appears that the evaluated price of PRB to Crystal River would have been less than the delivered price of CAPP and imported coals." We concur with witness Heller's assessment, but find that the evaluated price of PRB coal for CR4 and CR5 in 2003 is less than CAPP and imported coals when PRB coal accounts for 25 percent or less of the blend, as discussed below. Thus, we find that PEF's imprudence has been verified by the market evaluation for all three of the years in question.

In 2003-2005, PEF paid excessive fuel costs due to its failure to earnestly pursue the ability to burn PRB coal at CR4 and CR5 beginning in May 2001. These excessive fuel costs were passed on to PEF's ratepayers via PEF's fuel cost recovery factors. Because PEF paid excessive fuel costs from 2003 through 2005, customers shall be refunded for that period of time. The prudence of PEF's coal purchases of 2006 and 2007 was not considered in this proceeding. Accordingly, we direct PEF to supplement its 2006 Final True-Up Testimony in Docket No. 070001-EI to address whether the Company was prudent in its 2006 and 2007 coal purchases for CR4 and CR5.

V. Amount and Timing of Refunds

The parties also debated the amount, if any, of refund, as well as the timing of any refund. In his direct testimony, OPC witness Sansom identified PEF's excessive coal and SO2 allowance costs from 1996 through 2005. OPC's refund amount was based on an analysis of the differential between CAPP and PRB coal costs, where CAPP coal costs were identified as costs actually incurred per FERC Form 423 data and PRB coal costs were OPC's assessed costs of PRB coal if the utility had purchased market-based pricing for PRB and utilized specific modes and sources of coal transportation which OPC believes were available to PEF during the time period. The refund amount by OPC is further based upon a two-year increase in PRB coal volumes starting in 1996 (75/25 CAPP/PRB blend in 1996, 50/50 CAPP/PRB blend in 1997). Witness Sansom allowed a 7.5 percent reduction in PRB volumes in 2005 to recognize rail transportation disruptions which occurred during that year. SO2 Allowance Costs were developed based on: (1) the differential in SO2 emissions between bituminous coal and PRB coal; (2) the heat content of PRB coal (8,800 btu/lb); (3) the volume of PRB coal (in MMBtu) replacing CAPP/foreign coal; and (4) the market price of SO2 allowances each year in 2003-2005. Witness Sansom provided an analysis of SO2 costs for all relevant years.

PEF witness Heller testified that rather than incurring excessive costs for coal procurement, the company achieved a total value of $733,323,926 in savings from 1996 to 2005 by using exclusively bituminous coals at CR4 and CR5 rather than a 50/50 blend of CAPP coal and PRB coal. According to PEF, this total savings amount was a combination of three separate calculations: (1) witness Heller's estimate of fuel savings ($51,376,000) assuming all fuel and operational costs but excluding replacement power costs which would have resulted from derates due to using a 50/50 blend of CAPP and PRB coals at CR4 and CR5 during the 1996 to 2005 period, (2) witness Crisp's estimate of the derate costs ($696,963,130) due to using a 50/50 blend, and (3) witness Dean's offsetting SO2 allowance costs (-$15,015,204).

Witness Heller analyzed the potential for savings based on a comparison of his evaluated price of PRB coal to the actual delivered price of CAPP coal for all years. For annual PRB delivered coal prices, witness Heller utilized market information to obtain an FOB mine price for PRB coal, the cost of specific rail movements to docks on the Mississippi River, PEF-specific barge transfer costs, and the Commission-approved waterborne coal transportation proxies for the remainder of the transport costs (river, terminaling, and cross-Gulf transportation). Witness Heller adjusted PRB delivered prices to derive evaluated prices in order to account for additional operation and maintenance costs due to the impact of variations in the quality of the coal on boiler operations. Finally, witness Heller included the mid-point of the capital and operating costs identified by witness Hatt associated with the capital and operating costs associated with converting CR4 and CR5 to burn a 50/50 blend of CAPP/foreign coal and PRB coal.

According to PEF witnesses, the excessive SO2 allowance costs for 2003 through 2005 amount to $2,779,308. These costs were calculated based on the same procedure used by witness Sansom except PEF's calculation includes no ash adjustment but does include an adjustment to OPC's MMBtu data. Witness Dean provided an analysis of SO2 costs for all relevant years.

We found, as set forth above, that PEF was prudent in its coal purchases from 1996 through 2001. Thus, consistent with our analysis above, we find the appropriate refund amount for those years is zero.

Although we find PEF's coal purchases to be prudent from 1996 to 2001, beginning in 2001, PEF made imprudent management decisions. As more specifically discussed above, had PEF followed a prudent course of conduct in 2001 and 2002, ratepayers would have benefited from lower coal and emissions costs from 2003 to 2005. We find that PEF would have needed time to prepare itself to burn PRB. The record reflects that it would have taken 14 months to obtain a Title V permit amendment. Had PEF taken the appropriate actions in 2001, it would have been ready to burn PRB by 2003. We find that PEF's excessive coal costs in 2003 through 2005, inclusive of SO2 emissions costs, as shown on Attachment A, amounted to $12,425,492. These costs were calculated based on:

- Waterborne delivery of 2.4 million tons of coal per year from IMT to Crystal River, based on an 80/20 blend of CAPP/foreign coal to PRB coal for CR4 and CR5, including 480,000 PRB coal tons per year for 2003 and 2004, and 444,000

PRB coal tons in 2005 (thereby taking into account waterborne coal delivery constraints at Crystal River and rail transportation constraints in 2005);

- Assurance that the 480,000 tons per year of PRB coal in 2003 and 2004 does not exceed the waterborne coal supply requirements not yet contracted prior to 2003;

- A cost-effectiveness test of PRB coal for 2003, 2004, and 2005 for PEF, wherein the delivered price of CAPP/Foreign coal cost was shown to be higher than the evaluated price of PRB coal on a $/MMBtu basis;

- The PRB coal evaluated price was inclusive of those specific plant and operational incremental costs necessary for expected use of an 80/20 blend of CAPP/Foreign to PRB Coals at CR4 and CR5;

- The blending costs associated with PRB coals in Davant was included in the delivered PRB coal costs and was consistent with the PRB blending costs recognized by both OPC and PEF; and

- SO2 emissions costs based on the PRB tonnages cited above (480,000 tons per year for 2003-2004 and 444,000 tons in 2005) and PEF Witness Dean's estimates of PRB's SO2 content, heat rate, and SO2 emission allowances prices.

We accepted the testimony of witness Heller that Crystal River transportation constraints would have limited the waterborne delivery of coal to CR4 and CR5 to 2.4 million tons per year. Witness Heller said that PEF has attempted to exceed this amount but incurred operational problems when it did. No intervenor challenged this delivery constraint. An 80/20 blend of CAPP/foreign to PRB coal with the constraint of 2.4 million tons per year, blended off-site, is consistent with our analysis above, and yields a maximum tonnage of PRB of 480,000 tons (20 percent times 2.4 million tons per year).

We examined whether PEF could reasonably have contracted for 480,000 tons of waterborne coal during 2003 through 2005 without exceeding their supply requirements not already contracted. We note that PEF engaged in spot purchases of waterborne bituminous coal during 2003 through 2005 in amounts in excess of the PRB coal volumes necessary to achieve an 80/20 blend of CAPP/foreign coal to PRB coal. PEF also engaged in new long-term contracts for waterborne bituminous coal purchases during the 2003 through 2005 period. We find that PEF could reasonably have purchased 480,000 tons of coal each year without exceeding CR4 and CR5 waterborne coal supply requirements for those years not already contracted.

The record indicated that the capital and ongoing O&M costs for a 20 percent PRB coal blend at CR4 and CR5 would have been minimal compared to the costs required for a 50 percent PRB blend at CR4 and CR5. Our cost-effectiveness test for the 20 percent PRB coal blend, blended off-site, recognizes ten percent of the total capital costs requirements for 50/50 blend, blended on-site, per witness Heller. The Sargent and Lundy report gave a range of costs that would be incurred if PEF blended less than 30 percent PRB coal. We selected ten percent as a reasonable midpoint of the range of costs given the "coal blends less than 30 percent PRB" cost estimate put forth by the Sargent and Lundy Coal Conversion Cost Report and PEF's estimate of PRB potential at PRB coal blends less than 30 percent at CR4 and CR5. Our adjustment to the evaluated price of PRB coal (in $/MMBtu) to account for the capital recovery requirement is the difference in the PRB evaluated price (Attachment A, Table A, Column h) and the PRB Adjusted Evaluated Price (Attachment A, Table A, Column c).

The evidence reflected a problem in 2005 with rail deliveries of PRB coal. Accordingly, similar to the adjustment made by witness Heller and witness Sansom, we included in our cost-effectiveness analysis the assumption that 7.5 percent of planned PRB coal deliveries would fail to be delivered in 2005 due to rail congestion issues. Thus, instead of 480,000 tons of PRB coal delivered in 2005 to CR4 and CR5, it is assumed that only 444,000 tons of PRB coal would have been delivered.

Witness Heller presented, as part of his testimony, a cost effectiveness analysis which demonstrated whether savings would have been realized using PRB. Witness Heller concluded there would have been savings in 2001, 2004, and 2005 if one were to assume a 50/50 blend with no derate and a 30-year recovery life for "incremental" capital requirements. In reaching our decision that PRB would have been cost effective, we used the cost effectiveness analysis of witness Heller. Based on record evidence, we lowered the amount of PRB coal needed because we find that the record reflects that CR4 and CR5 could burn a 20 percent blend of PRB coal without a derate; we reduced the volume of PRB coal in 2005 by 7.5 percent of the shipping volume to account for rail transportation disruptions which occurred that year; and we lowered the amount of capital improvements needed to recognize a 20 percent blend of PRB coal to be used at CR4 and CR5. We then performed the mathematical computations established by witness Heller's analysis and determined that the use of PRB coal would have been cost effective for PEF for the years 2003, 2004, and 2005. Taking all such adjustments into account, we performed the cost-effectiveness test using witness Heller's analysis. The cost effectiveness test indicated that PRB savings were available to PEF in 2003, 2004, and 2005, totaling $9,056,256, exclusive of SO2 cost savings. (Attachment A, Table A, Column g)

We compared our analysis of the cost effectiveness to the evidence presented by OPC. Our analysis of the evaluated price difference between PRB coal and CAPP coal in 2003 was lower than OPC's estimate ($0.43/MMBtu versus our $0.13/MMBtu). But OPC's estimate of the difference for 2004 and 2005 is only slightly lower than ours ($.46/MMBtu and $.68/MMBtu versus $0.35MMBtu and $0.64MMBtu, respectively for 2004 and 2005). We believe the large gap in the price differential in 2003 between OPC and our finding is tied to OPC's assumption that the waterborne coal transportation market price proxy would not apply in that year. We previously found that the waterborne market proxy rates for evaluating PRB coal is appropriate for all years up to and including 2003.

The refund amount is restricted to the types of costs which normally flow through the fuel clause. The capital and operating costs associated with converting the power plant to burn PRB coal is not the type of costs normally recovered via the fuel clause. Thus, the excess coal cost as calculated above ($9,056,256), while useful for purposes of a cost-effectiveness test, is not the correct refund amount. Instead, the correct amount for purposes of cost recovery, hence refund, is the differential in the delivered costs of CAPP/foreign coal and the evaluated costs of

PRB coal for 2003 through 2005, as shown in Attachment A. For purposes of cost recovery, we removed the operational and capital costs required to upgrade CR4 and CR5 to burn PRB, because these types of costs are normally recovered via base rates. Using witness Heller's analysis, we were also able to perform the mathematical computations to determine the amount that PEF overpaid for coal. Using the analysis, the excessive coal cost refund amount for 2003-2005, exclusive of excess costs related to SO2 emissions, is $9,797,568.

Our calculation of SO2 emissions costs is based on witness Dean's estimate of SO2 per MMBtu. We estimated the tons of PRB coal, and using witness Dean's PRB coal heat rate of 8,800 btu/lb, as well as Witness Dean's allowance price per ton, we arrived at the excess SO2 emissions costs of $2,627,924. The total excess coal and SO2 emissions costs for 2003-2005 are $12,425,492. (Attachment A, Table B, Column i, and Attachment A, Table C, Column i)

The parties previously stipulated to the computation of interest. Accordingly, interest for the refund shall be calculated as set forth in Stipulation 1 of the prehearing order, Order No. PSC-07-0266-PHO-EI. Interest shall continue to accrue until the refund has been completed.

In the November 2006 fuel hearing, we approved $2,095,303,822 as the projected net fuel and purchased power cost recovery amount to be included in the 2007 fuel factors, resulting in a levelized fuel factor of 5.132 cents per KWH.[25] The refund amount represents 0.66 percent of the total amount approved for PEF to recover in its 2007 fuel factors. Reducing the Commission-approved 2007 levelized fuel factor of 5.132 c/KWH by 0.66 percent would result in a levelized fuel factor of 5.098 c/KWH, or a 0.034 c/KWH reduction. We find that the magnitude of the impact on the 2008 fuel factor will be similar, and, therefore, find it is reasonable to require PEF to refund the $12,425,492, plus interest, over a 12-month period through the 2008 fuel factors.

VI. Penalty

AARP conceded that its case for a penalty is dependent upon the Commission accepting OPC's case that PRB coal should have been purchased and that PEF knowingly chose not to. AARP argues that PEF favored its affiliated companies at the expense of ratepayers. AARP acknowledged that only if we determine that PEF knew that a lower priced fuel was available to it, but intentionally continued to purchase higher priced coal and synfuel, then a penalty would be warranted to deter future conduct of this type by PEF or any other utility. According to AARP, to find that a penalty is appropriate in this case, we must determine that PEF set out to cheat its customers by charging them higher fuel costs than were otherwise reasonably obtainable and that it did so for the benefit of its affiliates.

AARP asserted that the statutory basis for the Commission to impose a penalty under the facts of this case was found in Sections 366.095, 366.03, and 366.07, Florida Statutes. Section 366.095 Florida Statutes, allows the Commission to impose penalties if a utility is found to have refused to comply with, or willfully violated any rule, or order of the Commission, or of any

[25] See Order No. PSC-06-1057-FOF-EI, issued on December 22, 2006, Docket No. 060001-EI, In Re: Fuel and Purchased Power Cost Recovery Clause with Generating Performance Incentive Factor, at p 11.

provision of chapter 366. According to AARP, PEF had a statutory duty to not intentionally overcharge its customers. The specific statutory duty is set forth in section 366.03 and 366.07 where the legislature stated that rates shall be fair and reasonable. When it knowingly charged its customers higher than reasonable fuel charges in order to benefit its corporate affiliates, PEF intentionally and willfully failed to comply with chapter 366.

AARP's witness Stewart testified at hearing that the Commission has previously imposed an equity penalty in a rate case with Gulf Power Company. The penalty in that case, according to AARP, was for mismanagement in connection with "corrupt practices that took place at Gulf Power Company from the early 1980s through 1988…." According to AARP, the Florida Supreme Court upheld the penalty imposed on Gulf Power Company as long as the penalty did not "impose a penalty that would deny Gulf Power a reasonable rate of return." Gulf Power Company v. Wilson, 597 So. 2d 270, 273 (Fla. 1992).

AARP asserted that although the Wilson case came from a base rate proceeding before the Commission, there is nothing to preclude the Commission from penalizing a utility outside of base rate proceedings. Such a limitation, argued AARP, would severely limit the Commission since most of the rates charged by electric utilities are now recovered through fuel and other adjustment charges. If the Commission is prevented from punishing a utility for mismanagement, a "safe harbor" is provided to utilities.

PEF stated that AARP witness Stewart applied the wrong standard when he stated that if the Commission finds that PEF acted intentionally against its ratepayers and that it is necessary to discourage the utility from future misconduct, the Commission may impose a penalty. All parties agree that we can impose a penalty only upon a finding that a willful violation of any lawful Commission order, Commission rule or statute has occurred. According to PEF, we have no other legal basis to impose a penalty against PEF.

We conclude that the imposition of fines and comparable penalties pursuant to Chapter 350, or Section 366.095, Florida Statutes, is limited to instances where a utility refuses to comply with or willfully violates any Commission rule, order, or statute administered by us. Neither OPC nor AARP presented evidence to support that PEF willingly or knowingly charged its customers unfair or unreasonable rates. Neither OPC nor any other party has successfully demonstrated that PEF's actions were part of an overall scheme designed to cheat its customers while benefiting its parent company and affiliates.

The Wilson case cited by AARP in support of its position, is distinguishable from the case at hand. That case involved a base rate proceeding. In a base rate proceeding, we are charged with evaluating management efficiency. In Wilson, we found that the management of Gulf was particularly inefficient and downgraded the rate of return, deducting 50 points. The Supreme Court of Florida, in confirming our action, specifically found that deducting points for management inefficiency is not a penalty. Id. Our decision was therefore permissible.

Upon consideration, we find that no party identified a Commission rule, order or statute that PEF failed to implement or comply with for the period 1996 through 2005. Thus, we find that the record does not support the imposition of a fine or penalty in this case.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the findings and the stipulation set forth in the body of this Order are hereby approved. It is further

ORDERED that Progress Energy Florida, Inc. shall refund to its customers the amount of $12,425,492, plus interest. It is further

ORDERED that the refund shall take place through the 2007 fuel clause proceedings and shall be deducted from Progress Energy Florida's 2008 fuel factor. It is further

ORDERED that Progress Energy Florida shall supplement its 2006 Final True-Up Testimony in Docket No. 070001-EI to address whether Progress Energy Florida was prudent in its 2006 and 2007 coal purchases for CR4 and CR5. It is further

ORDERED that upon expiration of the time for appeal, this docket shall be closed.

By ORDER of the Florida Public Service Commission this 10th day of October, 2007.

Ann Cole

ANN COLE
Commission Clerk

(S E A L)

LCB

CONCURRENCE BY: COMMISSIONERS ARGENZIANO AND SKOP
DISSENT BY: COMMISSIONER MCMURRIAN

COMMISSIONER ARGENZIANO, concurring with opinion as follows:

I fully concur in the decision that PEF's coal procurement actions were imprudent, and that $12.45 Million, plus interest, should be refunded to PEF's customers. While I am comfortable that my decision is fully supported by this record, I also wish to make my position clear. My dissatisfaction with the vote is strictly limited to the issue of reopening the record, as proposed by Commissioners McMurrian and Skop. I am of the opinion that, when available, one should seek to have every bit of information available in one's possession.

My review of thousands of pages of hearing transcripts and exhibits in the record left me with many questions. Not having had the opportunity to participate in the hearing, I was unable to answer these questions. None of these questions lead me to believe PEF's actions were not imprudent and that a refund was not required; had I the opportunity to ask additional questions, however, I may have come to the conclusion that additional refunds were warranted or even required.

COMMISSIONER SKOP, concurring specially with a separate opinion:

I concur with the majority view only to the extent that I agree that Progress Energy Florida (PEF) customers were entitled to a refund in this case. Writing separately, I firmly believe that the refund amount of $12,425,492 (plus interest) ordered by the commission was patently insufficient based upon the substantial record evidence supporting a larger refund due to PEF customers.

Based upon the record evidence before the commission, I would hold that the appropriate remedy should consist of the following:

Fuel Clause Adjustment

In the instant case, the record clearly reflects that the uprate benefit associated with the CR4 and CR5 units could be maintained through burning a bituminous/sub-bituminous fuel blend comprised of up to 30% Powder River Basin (PRB) sub-bituminous coal. Substituting the 70/30 fuel blend reflected in the record testimony for the 80/20 fuel blend assumption recommended by staff and subsequently adopted by this commission would have effectively doubled the refund amount due to PEF customers.

Rate Base Adjustment

The record conclusively establishes the fact that the CR4 and CR5 units were designed and built to burn a 50/50 design fuel blend comprised of 50% Central Appalachian (CAPP) bituminous coal and 50% PRB sub-bituminous coal. The record evidence further establishes the fact that PEF failed to conduct contractual acceptance testing of the CR4 and CR5 units with the design fuel blend, the fact that PEF subsequently surrendered the ability to burn PRB coal through omissions in the initial filing and renewal of its Title V operating permit, and the fact that PEF's parent holding company set up various subsidiaries which were later utilized to procure, mine, and deliver CAPP bituminous coal for the CR4 and CR5 units. Therefore, in a manner analogous to the legal concept of waste, PEF failed to preserve the inherent design capability to burn a bituminous/sub-bituminous fuel blend for the CR4 and CR5 units, thereby effectively denying its customers of the very capability that they had been paying for since the CR4 and CR5 units became part of the PEF rate base in the mid 1980's.

Accordingly, having denied its customers the benefit of the bargain of capturing the potential fuel savings associated with the capability of burning a bituminous/sub-bituminous fuel blend for the CR4 and CR5 units, it seems only equitable that PEF be disgorged of the amount that it was unjustly enriched by its actions; namely the forfeiture of the Return on Equity (ROE) earned upon the incremental capital investment that was spent to make the CR4 and CR5 units capable of burning the design fuel blend. The amount by which PEF was unjustly enriched (plus appropriate interest) could be readily calculated utilizing the record testimony and historical ROE values from prior orders which could have been judicially noticed. Furthermore, a proposed remedy of this nature is certainly not without precedent. In Order No. 15486[26] this commission, in the context of a fuel clause proceeding directly analogous to the instant case, revisited the rate base to review historical management decisions related to the initial design and subsequent operation of the Florida Power and Light (FPL) Saint Lucie No. 1 (SL1) nuclear generating unit. Specifically, the commission held that FPL's actions associated with the decision to include a thermal shield in the initial design of the SL1 nuclear generating unit, the operation of the unit prior to the extended outage, the subsequent repair of the unit, and return of the unit to service were all prudent. Therefore, the subject order clearly provides commission precedent for reviewing historical management decisions associated with the rate base in the instant case.

Having established commission precedent for reviewing issues associated with the rate base in the procedural posture of a fuel clause proceeding, the issues of administrative finality, hindsight review, and retroactive ratemaking must also be evaluated under controlling case law. In this regard, the same legal arguments that staff advanced in its recommendation to rebut PEF's position regarding these issues in the fuel clause proceeding seem equally applicable to rebutting similar arguments for reviewing issues associated with the rate base.[27]

With respect to the doctrine of administrative finality, even when finality has attached to an order, there is a significant exception to the application of the doctrine, and finality may not apply where it is shown that some mistake, misrepresentation, fraud, or a matter of great public interest compels review.[28] Accordingly, Florida case law recognizes that an administrative agency may alter a final decision under extraordinary circumstances.[29] In the instant case, the record clearly reflects extraordinary circumstances warranting an exception to the administrative finality rule. Admittedly, had PEF demonstrated that it had no underlying duty to preserve the capability of burning the bituminous/sub-bituminous fuel blend in CR4 and CR5 units then this entire case should have been dismissed on the merits without any refund. The record clearly reflects, however, that the ability to burn a bituminous/sub-bituminous fuel blend was inherent in the design of the CR4 and CR5 units. To conclude otherwise would mean that this commission impliedly waived this capability and determined that the PEF practice of burning 100% CAPP coal was prudent within one or more subsequent rate cases. PEF never advanced this argument.

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[26] Order No. 15486, issued December 23, 1985, Docket No. 840001-EI-A, In re: Investigation into extended outage of Florida Power and Light Company's St. Lucie No. 1.
[27] Staff Recommendation in Docket No. 060658-EI at 81-86.
[28] Richter v. Florida Power Corp., 366 So. 2d 798, 800 (Fla. 2d DCA 1979) (referencing 73 A.L.R. 2d 939, 951-52 (1960) dealing with the power of administrative agencies to alter final orders).
[29] Id. (citing Davis v. Combination Awning & Shutter Co., 62 So. 2d 742, 745 (Fla. 1953)).

From a policy perspective, however, a plurality within the majority heavily criticized and rejected this aspect of the proposed remedy on the basis that it would cause regulatory uncertainty within the capital markets. Without question, the views of my colleagues are well taken as any decision regarding a rate base adjustment is not one to be taken lightly. I would respectfully suggest, however, that the capital markets are sophisticated enough to recognize the need for accountability when warranted by a particular set of circumstances, that the capital markets do not expect regulators to acquiesce to imprudently incurred costs, and that upholding the public interest often times requires making unpopular decisions guided by past commission precedent and controlling case law.

Therefore, although such a remedy could have been adopted by this commission *sui sponte* based upon the record evidence, procedural safeguards would have more cautiously warranted reopening the record for the limited purpose of taking additional testimony with respect to the rate base (i.e., the incremental capital investment that was spent to make the CR4 and CR5 units capable of burning the design fuel blend) in order to adequately protect PEF's due process interests prior to rendering a decision on the merits regarding the appropriate refund amount. Under either approach, however, such a remedy would have substantially increased the refund amount due to PEF customers.

Denial of Restoration Costs

I would also hold that PEF has an underlying obligation to restore the capability of burning a bituminous/sub-bituminous fuel blend in the CR4 and CR5 units, and that any such costs associated with this effort (e.g., fuel burn testing, permitting revision, etc.) should not be eligible for recovery from PEF customers.

In summary, I firmly believe that the refund amount ordered by the commission was patently insufficient and that the three prong remedy outlined above would provide the appropriate measures necessary to ensure a fair and equitable result in view of the record evidence.

COMMISSIONER MCMURRIAN, dissenting with opinion as follows:

Background

On August 10, 2006, the Office of Public Counsel (OPC) filed a petition against Progress Energy Florida (PEF) alleging that PEF mismanaged their coal procurement at Crystal River Units 4 and 5 (CR4 and CR5) between 1996 and 2005. In particular, OPC alleged that *PEF should have been burning a 50/50 blend* of bituminous and sub-bituminous Powder River Basin (PRB) coal (50/50 blend) at CR4 and CR5.

OPC's position was fully vetted before the Commission. Indeed, we conducted a four-day hearing in April 2007, in which the bulk of the evidence addressed *whether PEF should have been burning a 50/50 blend* at CR4 and CR5.

After the taking of all testimony and evidence, after a four-day hearing, and after the record was closed, Commission staff concluded, in their recommendation, that PEF ***did not act imprudently in not burning a 50/50 blend***. The Commission agreed.

The majority erred, however, in holding that PEF had acted imprudently in not burning an 80 percent bituminous and 20 percent sub-bituminous PRB coal blend (80/20 blend) from 2003 to 2005. The notion only came before the Commission by virtue of our staff's *sua sponte* and "after-the-fact" introduction of the claim in its June 27, 2007, primary recommendation.[30] Neither the petitioner nor any other party alleged that PEF's not burning an 80/20 blend was imprudent, and no party ever sought to amend its pleadings, its testimony, or the prehearing order to make this claim. As such, the majority's decision does not comport with fundamental requirements of due process, namely that a party be on notice of the specific claims made against it and have a full opportunity to defend against those claims.

For the reasons set forth herein, I must respectfully dissent from the majority's decisions on Issue 1 (prudence of coal purchases for CR4 and CR5 from 1996-2005), Issue 2 (whether to order refund if imprudence found in Issue 1), and Issue 4 (amount of refund).

The Majority's Decision Does Not Comport with Due Process

As noted, the gravamen of OPC's petition was the allegation that PEF should have been burning a 50/50 blend of bituminous and sub-bituminous PRB coal at CR4 and CR5. After the case presented was fully vetted by the parties, Commission staff concluded in their primary recommendation to the Commission that PEF had not acted imprudently in not burning a 50/50 blend. Notwithstanding their recommendation on the claim before the Commission, Commission staff *sua sponte* put forth a new claim in their recommendation – the claim that PEF should have been burning a different coal blend – specifically, an 80/20 blend – between 2003 and 2005.

By adopting the staff's primary recommendation that PEF had acted imprudently in not burning an 80/20 coal blend without affording a reasonable opportunity for parties to rebut such a claim, the majority ran afoul of due process rights guaranteed to every party. Neither PEF, nor OPC, nor the Commissioners who presided over the hearing were on notice that the Commission would be adjudicating a claim that PEF's not using an 80/20 blend was imprudent. As no such claim had been made, PEF had no opportunity to defend against it. Likewise, OPC and the other parties had no opportunity to rebut any perceived inadequacy of a 20 percent PRB blend.

The Commission's process affords staff and each party the opportunity to avoid such due process concerns. Like the parties to the case, staff had the opportunity to sponsor expert testimony for consideration on the issue of whether not burning an 80/20 blend was imprudent. Staff did not avail themselves of that opportunity. However, staff did sponsor testimony containing information about foreign coal during the 1996-2005 time period. The existence of that pre-filed staff testimony provided notice to all parties of an avenue that might have been

[30] Commission staff's June 27, 2007, recommendation in this matter also contained an alternative recommendation, which stated that PEF acted prudently in purchasing coal for CR4 and CR5 during the period 1996 through 2005.

pursued by the staff. Had staff filed testimony on an 80/20 blend, parties would have been similarly put on notice. As the prehearing officer in this case, I would have allowed staff the opportunity to present testimony on an 80/20 blend, just as I allowed staff the opportunity to present testimony on foreign coal over PEF's objections. I had no concerns that staff's testimony violated any party's due process rights, as there remained a future opportunity for parties to rebut any aspect of, and to conduct discovery on, that testimony.

With respect to the 80/20 blend proposal introduced in staff's primary recommendation, the parties were afforded **no such opportunity**, as staff recommendations are filed **after a hearing has been concluded and the record has been closed.** The Commission's process does not allow the parties to argue, rebut, or provide feedback of any kind relating to the recommendation. As in any trial, once the case is closed, the judging authority must sift through the record and come to a decision based only on those materials. However, in their recommendation, staff for the first time claimed that PEF should be found to have acted imprudently for not having burned an 80/20 blend in the past. Because this claim was made after the parties presented their cases and after the closing of the record, there was no procedurally proper opportunity for parties to go on record with respect to the 80/20 blend proposal. This violates the parties' right to due process, which affords each party the right to know the issues before them and allow them ample opportunity to provide arguments for or against. The complexity of this case, which tasked the Commission with piecing together events as far back as 1996, renders due process all the more critical.

Staff's assertion that PEF offered the lesser PRB percentages into evidence and put the parties on notice is misguided. PEF indeed submitted the 2005 Sargent & Lundy study that suggested a blend under 30 percent, with offsite blending and certain equipment additions and modifications, could prove viable. PEF also submitted testimony that PRB blends under 25 percent could likely have been used. An important distinction, however, is that none of the evidence presented included a proposal by PEF or any other party or the staff that an 80/20 blend (or any other of a range of PRB blends with the exception of a 50/50 blend) should have been burned at CR4 and CR5 between 1996 and 2005. PEF appears to have submitted the evidence regarding lower PRB blends for the purpose of rebutting the 50/50 blend proposal and to show that they were, in fact, prudent for not burning a 50/50 blend. The preponderance of the evidence presented, including the evidence submitted by PEF with respect to lesser PRB percentages, showed that use of a 50/50 blend might result in a detrimental impact on the megawatt output of CR4 and CR5 and a loss of the savings associated with the uprate achieved over this period.

Due process affords a party the right to know of the specific claims against them and to defend against those charges. In this case, OPC filed a petition that alleged PEF was being imprudent for not burning a 50/50 blend during the period of 1996 to 2005. PEF was on notice to this issue, prepared accordingly, and ultimately prevailed on that claim.

The issue of whether PEF should have burned another type of blend – be it a 60/40, 65/35, 90/10 – is inapposite because such was not brought by OPC and was not made by OPC or any other party prior to or during the hearing on this matter. The notion of an 80/20 blend was not introduced until after closure of the hearing. The parties as well as the Commission did not have the opportunity to fully scrutinize this 80/20 blend proposal during the hearing process. Finding PEF imprudent for not burning an 80/20 blend under such circumstances does not comport with due process. In short, PEF was not, and could not have been, on notice of that claim.

Applying the Standard of Review to the Record Dictates No Finding of Imprudence

The Record

In the case before the Commission, the record does not support a finding of imprudence. The claim fully vetted before the Commission was that PEF acted imprudently in not burning a 50/50 coal blend beginning back in 1996. Evidence clearly indicated that a 50/50 blend would not have been a prudent choice for CR4 and CR5 given the likelihood of a derate. Commission staff recommended that PEF not be found to have acted imprudently for not burning a 50/50 blend, and the Commission agreed. Based on the case before the Commission and the record developed to support and to rebut that case, the only conclusion that can properly be reached is that PEF did not act imprudently.

Standard of Review

The Commission was tasked with determining whether PEF acted prudently and reasonably in light of the facts that it knew or should have reasonably known at the time it made its decision.[31] What is "reasonable" varies from case to case and is necessarily a subjective matter. Such flexibility provides businesses with the freedom to make independent decisions based on the unique circumstances of their company at a given point in time rather than burdening them with rigid bright-line rules that might discourage innovation and the benefits to consumers that may well result.

Witness Fetter, a former Michigan Public Service Commissioner, made the following important point about the range of reasonableness:

> Management decisions in complex areas are rarely 'black and white.' Rather, there's a range of decision-making that prudent, equally-informed managements could make. Absent a management decision clearly falling outside this range, there is no basis upon which the regulator should substitute its judgment for that of the utility's management.

It is entirely possible that PEF's actions were prudent and that staff's 80/20 blend proposal, had it been the course of action followed, might also have been prudent. A 75/25 coal blend might have been reasonable; so might have been a 90/10 blend. In fact, there are several

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[31] For example, in determining whether PEF was imprudent not to have begun a permit amendment application and test burns for PRB coal in 2001, one should not rely on the 2005 Sargent & Lundy study results that suggested that amounts of PRB coal equal to 30 percent and under might be viable without a detrimental impact on megawatt output. There can be no dispute that information from a 2005 study was not available to PEF in 2001, the year primary staff proposes PEF should have taken action to be ready to burn a 20 percent PRB blend by 2003.

courses of action that might have been deemed prudent. *A finding that burning an 80/20 blend might have been a prudent decision does not independently render a different course of action by utility management imprudent.* Business decisions are rarely "black and white."

Had a claim been made against PEF that it had acted imprudently in not burning an 80/20 blend, and had the parties had an opportunity to fully vet this claim before the Commission, the Commission would have a basis for concluding whether PEF's chosen coal blend was clearly outside the range of reasonableness.

Conclusion – No Imprudence

Based on the parties' evidence regarding the propriety (or lack thereof) of burning a 50/50 blend at CR4 and CR5, as well as the propriety (or lack thereof) of burning foreign coal at CR4 and CR5, and applying the appropriate standard of review, there is no competent, substantial evidence of imprudence. It appears that the majority is in agreement on that limited point.

For the reasons set forth above, I cannot join my colleagues in finding that PEF acted imprudently in not adopting an 80/20 coal blend. This was not the subject of the petition brought by OPC. This was not the case PEF or any other party had the opportunity to defend or rebut.

Even if one overlooked the violations of due process, given the evidence in the record about what PEF knew at the time and PEF's ultimate decisions about fuel procurement over the 1996-2005 timeframe, there is no competent basis upon which to conclude that PEF's not using the 80/20 blend between 2003 and 2005 was imprudent. Nor can I say more generally that PEF's coal purchases between 1996 and 2005 were imprudent based on an 80/20 blend, a 70/30 blend, or any other blend ratio, as such claims were not litigated before the Commission.

The case as presented was based on the argument that PEF should have been burning a 50/50 blend. The fact that the decision was based on a different blend proposal, one for which parties were not put on notice nor given the opportunity to rebut, sets an unfavorable precedent. In the process of revisiting decade-old business decisions, we have found imprudence based on a proposal in which the decisionmakers did not have an opportunity to be fully heard.

Therefore, I must dissent from the majority's decision of imprudence and the corresponding refunds. Specifically, I dissent with respect to the decisions on Issues 1, 2, and 4.

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Office of Commission Clerk, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water and/or wastewater utility by filing a notice of appeal with the Office of Commission Clerk, and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

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Excess 2003-2005 Coal and SO2 Costs at CR4 and CR5 and Recommended Fuel Refund)

A. Excess 2003-2005 Coal Costs at CR4 and CR5 and Fuel Refund (exclusive of SO2 credit adjustment and interest adjustment)

a	b	c	d	e	f	g	h	i
Year	CAPP/Foreign Delivered Price ($/MMBtu)	PRB Adjusted Evaluated Price ($/MMBtu)	Price Difference ($/MMBtu)	Maximum PRB Tons	MMBtu	Excess Coal Costs (adjusted)	PRB Coal Eval. Price ($/MMBtu)	Coal Costs Refund (via Fuel Clause)
2003	2.73	2.60	0.13	480,000	8,448,000	$1,098,240	2.57	$1,351,680
2004	2.63	2.28	0.35	480,000	8,448,000	$2,956,800	2.25	$3,210,240
2005	3.07	2.43	0.64	444,000	7,814,400	$5,001,216	2.40	$5,235,648
TOTAL EXCESS COAL COSTS, 2003-2005						$9,056,256		$9,797,568

b : EXH 85, Column 4 , or Witness Heller's delivered price of CAPP/Import Coal to CR4 and CR5
c : EXH 84, Column 10 + 0.1(Column 11), or Witness Heller's evaluated PRB coal price plus adjustment to recognize estimated capital recovery requirement.
d : b - c
e : 20% of 2.4 Mmtpy, or the barge limit of PRB tons for CR4 and CR5 per Witness Heller, with 7.5% reduction for 2005 (TR 926)
f : Column E tons x 2,000 lb/ton x .0088 MMBbtu/lb, equal to the MMBtus derived from PRB coal at 20% blend
g : d x f (establishes that PRB was cost-effective to buy)
h : EXH 84, Column 10, or Witness Heller's evaluated PRB coal price
i: (b - h) x f, Commission calculated excess costs incurred via the Fuel Clause and ECRC

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B. Excess 2003-2005 Costs Related to SO2 Allowances at CR4 and CR5 and Fuel Refund

a	b	c	d	E	f	g	h	i
Year	Increased SO2 (lbs per MMBtu)	MMBtu	Excess SO2 tons	SO2 Price ($/ton)		Excess SO2 Cost		SO2 Allowance Refund (via ECRC)
2003	0.43	8,448,000	1,774	176		$319,672		$319,672
2004	0.44	8,448,000	1,859	442		$821,484		$821,484
2005	0.44	7,814,400	1,680	906		$1,486,768		$1,486,768
TOTAL EXCESS SO2 COSTS, 2003-2005						$2,627,924		$2,627,924

b : EXH 97, Column 3, or Witness Dean's calculated difference in SO2 lbs/MMBtu between bituminous and PRB Coals
c: MMBtu obtained by 480,000 tons of PRB with heat rate of 8,800 btu/lb (see table at top of page)
d : (b x c)/2,000 lbs.
e : EXH 97, Column 6, or Witness Dean's SO2 allowance price per ton
g and i : d x e (Given "Excess Coal Costs" as shown above, this further establishes PRB was cost effective to buy)

C. Excess 2003-2005 Coal and SO2 Costs and Fuel Refund

a	b	c	d	e	f	g	h	i
Year						Excess Coal / SO2 Costs (adjusted)		Coal / SO2 Cost Refund Total
2003						$1,417,912		$1,671,352
2004						$3,778,284		$4,031,724
2005						$6,487,984		$6,722,416
TOTAL EXCESS COAL AND SO2 COSTS (ADJUSTED) AND FUEL REFUND (exclusive of interest adjustment)						$11,684,180		$12,425,492

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Progress Energy Florida, Inc.
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Interest Calculation

Month	Beginning Balance	Monthly Excess Fuel Charge	Average Monthly Balance	Annual Interest Rate	Monthly Interest	Ending Balance
Jan-96	$0	$0	$0	5.605 %	$0	$0
Feb-96	0	0	0	5.365 %	0	0
Mar-96	0	0	0	5.415 %	0	0
Apr-96	0	0	0	5.450 %	0	0
May-96	0	0	0	5.400 %	0	0
Jun-96	0	0	0	5.460 %	0	0
Jul-96	0	0	0	5.485 %	0	0
Aug-96	0	0	0	5.425 %	0	0
Sep-96	0	0	0	5.420 %	0	0
Oct-96	0	0	0	5.410 %	0	0
Nov-96	0	0	0	5.415 %	0	0
Dec-96	0	0	0	5.700 %	0	0
Jan-97	0	0	0	5.700 %	0	0
Feb-97	0	0	0	5.440 %	0	0
Mar-97	0	0	0	5.585 %	0	0
Apr-97	0	0	0	5.680 %	0	0
May-97	0	0	0	5.610 %	0	0
Jun-97	0	0	0	5.610 %	0	0
Jul-97	0	0	0	5.600 %	0	0
Aug-97	0	0	0	5.570 %	0	0
Sep-97	0	0	0	5.545 %	0	0
Oct-97	0	0	0	5.530 %	0	0
Nov-97	0	0	0	5.565 %	0	0
Dec-97	0	0	0	5.675 %	0	0
Jan-98	0	0	0	5.625 %	0	0
Feb-98	0	0	0	5.515 %	0	0
Mar-98	0	0	0	5.540 %	0	0
Apr-98	0	0	0	5.540 %	0	0
May-98	0	0	0	5.515 %	0	0
Jun-98	0	0	0	5.550 %	0	0
Jul-98	0	0	0	5.580 %	0	0
Aug-98	0	0	0	5.540 %	0	0
Sep-98	0	0	0	5.370 %	0	0
Oct-98	0	0	0	5.160 %	0	0
Nov-98	0	0	0	5.300 %	0	0
Dec-98	0	0	0	5.200 %	0	0
Jan-99	0	0	0	4.855 %	0	0
Feb-99	0	0	0	4.830 %	0	0
Mar-99	0	0	0	4.865 %	0	0
Apr-99	0	0	0	4.840 %	0	0
May-99	0	0	0	4.825 %	0	0
Jun-99	0	0	0	4.950 %	0	0

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Month	Beginning Balance	Monthly Excess Fuel Charge	Average Monthly Balance	Annual Interest Rate	Monthly Interest	Ending Balance
Jul-99	0	0	0	5.075 %	0	0
Aug-99	0	0	0	5.210 %	0	0
Sep-99	0	0	0	5.310 %	0	0
Oct-99	0	0	0	5.300 %	0	0
Nov-99	0	0	0	5.425 %	0	0
Dec-99	0	0	0	5.575 %	0	0
Jan-00	0	0	0	5.700 %	0	0
Feb-00	0	0	0	5.800 %	0	0
Mar-00	0	0	0	5.935 %	0	0
Apr-00	0	0	0	6.125 %	0	0
May-00	0	0	0	6.375 %	0	0
Jun-00	0	0	0	6.575 %	0	0
Jul-00	0	0	0	6.540 %	0	0
Aug-00	0	0	0	6.490 %	0	0
Sep-00	0	0	0	6.490 %	0	0
Oct-00	0	0	0	6.495 %	0	0
Nov-00	0	0	0	6.570 %	0	0
Dec-00	0	0	0	6.575 %	0	0
Jan-01	0	0	0	6.025 %	0	0
Feb-01	0	0	0	5.350 %	0	0
Mar-01	0	0	0	5.075 %	0	0
Apr-01	0	0	0	4.685 %	0	0
May-01	0	0	0	4.155 %	0	0
Jun-01	0	0	0	3.870 %	0	0
Jul-01	0	0	0	3.775 %	0	0
Aug-01	0	0	0	3.610 %	0	0
Sep-01	0	0	0	3.070 %	0	0
Oct-01	0	0	0	2.445 %	0	0
Nov-01	0	0	0	2.130 %	0	0
Dec-01	0	0	0	1.910 %	0	0
Jan-02	0	0	0	1.775 %	0	0
Feb-02	0	0	0	1.760 %	0	0
Mar-02	0	0	0	1.775 %	0	0
Apr-02	0	0	0	1.775 %	0	0
May-02	0	0	0	1.760 %	0	0
Jun-02	0	0	0	1.760 %	0	0
Jul-02	0	0	0	1.740 %	0	0
Aug-02	0	0	0	1.720 %	0	0
Sep-02	0	0	0	1.735 %	0	0
Oct-02	0	0	0	1.705 %	0	0
Nov-02	0	0	0	1.475 %	0	0
Dec-02	0	0	0	1.295 %	0	0

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Month	Beginning Balance	Monthly Excess Fuel Charge	Average Monthly Balance	Annual Interest Rate	Monthly Interest	Ending Balance
Jan-03	0	139,279	69,640	1.280 %	74	139,354
Feb-03	139,354	139,279	208,993	1.260 %	219	278,852
Mar-03	278,852	139,279	348,492	1.215 %	353	418,485
Apr-03	418,485	139,279	488,124	1.185 %	482	558,246
May-03	558,246	139,279	627,886	1.200 %	628	698,153
Jun-03	698,153	139,279	767,793	1.105 %	707	838,139
Jul-03	838,139	139,279	907,779	1.025 %	775	978,194
Aug-03	978,194	139,279	1,047,834	1.055 %	921	1,118,395
Sep-03	1,118,395	139,279	1,188,034	1.060 %	1,049	1,258,724
Oct-03	1,258,724	139,279	1,328,363	1.055 %	1,168	1,399,171
Nov-03	1,399,171	139,279	1,468,810	1.025 %	1,255	1,539,705
Dec-03	1,539,705	139,279	1,609,344	1.030 %	1,381	1,680,365
Jan-04	1,680,365	335,977	1,848,354	1.045 %	1,610	2,017,952
Feb-04	2,017,952	335,977	2,185,940	1.005 %	1,831	2,355,760
Mar-04	2,355,760	335,977	2,523,748	0.980 %	2,061	2,693,798
Apr-04	2,693,798	335,977	2,861,786	1.005 %	2,397	3,032,171
May-04	3,032,171	335,977	3,200,160	1.035 %	2,760	3,370,909
Jun-04	3,370,909	335,977	3,538,897	1.185 %	3,495	3,710,380
Jul-04	3,710,380	335,977	3,878,369	1.400 %	4,525	4,050,882
Aug-04	4,050,882	335,977	4,218,871	1.535 %	5,397	4,392,256
Sep-04	4,392,256	335,977	4,560,244	1.685 %	6,403	4,734,636
Oct-04	4,734,636	335,977	4,902,625	1.855 %	7,579	5,078,192
Nov-04	5,078,192	335,977	5,246,180	2.080 %	9,093	5,423,262
Dec-04	5,423,262	335,977	5,591,251	2.280 %	10,623	5,769,862
Jan-05	5,769,862	560,201	6,049,963	2.420 %	12,201	6,342,265
Feb-05	6,342,265	560,201	6,622,365	2.575 %	14,210	6,916,676
Mar-05	6,916,676	560,201	7,196,777	2.715 %	16,283	7,493,160
Apr-05	7,493,160	560,201	7,773,261	2.880 %	18,656	8,072,018
May-05	8,072,018	560,201	8,352,118	3.020 %	21,019	8,653,238
Jun-05	8,653,238	560,201	8,933,339	3.165 %	23,562	9,237,001
Jul-05	9,237,001	560,201	9,517,102	3.350 %	26,569	9,823,771
Aug-05	9,823,771	560,201	10,103,872	3.535 %	29,764	10,413,737
Sep-05	10,413,737	560,201	10,693,838	3.715 %	33,106	11,007,045
Oct-05	11,007,045	560,201	11,287,145	3.910 %	36,777	11,604,023
Nov-05	11,604,023	560,201	11,884,124	4.120 %	40,802	12,205,027
Dec-05	12,205,027	560,201	12,485,127	4.255 %	44,270	12,809,498
Jan-06	12,809,498	0	12,809,498	4.405 %	47,022	12,856,520
Feb-06	12,856,520	0	12,856,520	4.520 %	48,426	12,904,946
Mar-06	12,904,946	0	12,904,946	4.655 %	50,060	12,955,006
Apr-06	12,955,006	0	12,955,006	4.870 %	52,576	13,007,582
May-06	13,007,582	0	13,007,582	4.985 %	54,036	13,061,618
Jun-06	13,061,618	0	13,061,618	5.150 %	56,056	13,117,674
Jul-06	13,117,674	0	13,117,674	5.325 %	58,210	13,175,884

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Month	Beginning Balance	Monthly Excess Fuel Charge	Average Monthly Balance	Annual Interest Rate	Monthly Interest	Ending Balance
Aug-06	13,175,884	0	13,175,884	5.315 %	58,358	13,234,242
Sep-06	13,234,242	0	13,234,242	5.265 %	58,065	13,292,307
Oct-06	13,292,307	0	13,292,307	5.265 %	58,320	13,350,627
Nov-06	13,350,627	0	13,350,627	5.260 %	58,520	13,409,147
Dec-06	13,409,147	0	13,409,147	5.260 %	58,777	13,467,924
Jan-07	13,467,924	0	13,467,924	5.265 %	59,091	13,527,015
Feb-07	13,527,015	0	13,527,015	5.260 %	59,293	13,586,308
Mar-07	13,586,308	0	13,586,308	5.260 %	59,553	13,645,861
Apr-07	13,645,861	0	13,645,861	5.260 %	59,814	13,705,676
May-07	13,705,676	0	13,705,676	5.260 %	60,077	13,765,752
Jun-07	13,765,752	0	13,765,752	5.270 %	60,455	13,826,207
TOTAL		$12,425,492			$1,400,715	**$13,826,207**

Acronyms and Abbreviations

AARP – AARP
AGO - Attorney General's Office
Btu - British thermal unit
CAPP - Central Appalachian
CFR - Code of Federal Regulations
Commission - Florida Public Service Commission
CQIM - Coal Quality Impact Model, currently updated it is the VISTA model
CR1 and CR2 - Crystal River Units 1 and 2
CR3 - the Crystal River Unit 3 nuclear unit
CR4 and CR5 – Crystal River Unit 4 and Crystal River Unit 5
CSX - the CSX railroad
DEP – Department of Environmental Protection
EFC – Electric Fuel Corporation, the predecessor to PFC
FIPUG – Florida Industrial Power Users Group
FPC- Florida Power Corporation, the predecessor to PEF
IMT - International Marine Terminal
KWH - kilowatt hour
MMBtu - million British thermal units
MW - megawatt
MWH - megawatt hour
NRC - Nuclear Regulatory Commission
OPC – Office of Public Counsel
PEI - Progress Energy, Inc., the parent company of PEF and PFC
PEF - Progress Energy Florida; formerly Florida Power Corporation
PFC - Progress Fuels Corporation fka Electric Fuels Corporation or EFC, the PEI subsidiary that bought fuel for PEF
PRB - Powder River Basin
RFP - Request for Proposals
Title V - Title V of the 1990 Amendments to the Clean Air Act
Siting Board – Florida Electrical Power Plant Siting Board
Synfuel - synthetic fuel