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November 13, 2015

VIA: ELECTRONIC FILING

Ms. Carlotta S. Stauffer
Commission Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850


Re: Fuel and Purchased Power Cost Recovery Clause with Generating
Performance Incentive Factor; FPSC Docket No. 150001-EI

Dear Ms. Stauffer:

Attached for filing in the above docket is Tampa Electric Company's Brief and Post-Hearing Statement of Issues and Positions.

Thank you for your assistance in connection with this matter.

Sincerely,


James D. Beasley

JDB/pp
Attachment

cc: All Parties of Record (w/attachment)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Fuel and Purchased)
Power Cost Recovery Clause)
And Generating Performance)
Incentive Factor.)
_____)

DOCKET NO. 150001-EI

FILED: November 13, 2015

**TAMPA ELECTRIC COMPANY'S BRIEF
AND POST-HEARING STATEMENT OF ISSUES AND POSITIONS**

Tampa Electric Company ("Tampa Electric" or "the company"), pursuant to the Prehearing Order¹ issued in this proceeding on October 29, 2015, submits this its Brief and Post-Hearing Statement of Issues and Positions in the above matter.

BRIEF

Background

In light of the Commission's Staff's diligent efforts and the cooperation among the parties to this proceeding, the bulk of the issues typically addressed in the November fuel adjustment hearing each year in this docket have been resolved by way of stipulation this year. Following the hearing conducted on November 2 and 3, 2015 only three issues relating to Tampa Electric remain to be decided. Those issues are as follows:

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

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

ISSUE 6B: Should the Commission approve Tampa Electric's 2016 Risk Management Plan?

¹ Order No. PSC-15-0512-PHO-EI

For purposes of this Brief and Post-Hearing Statement Tampa Electric will occasionally refer to natural gas financial hedging simply as "natural gas hedging" or "hedging", not to be confused with physical hedging of natural gas or other fossil fuels.

Recent History of Natural Gas Hedging in Florida

Observations made by the Commission in its orders addressing financial hedging and hedging audits by the Commission's Staff suggest that utilities hedge using systematic and prudent methods, consumers benefit from the utilities' financial hedging activities, and that no changes need to be made to the manner in which electric utilities conduct their financial hedging activities.

In 2002 the Commission issued an order² ("the Hedging Order") approving a proposed resolution of issues relating to financial hedging, between and among Florida Power & Light ("FPL"), Duke Energy Florida's ("DEF") predecessor, Gulf Power Company ("Gulf"), Tampa Electric, Office of Public Counsel ("OPC") and the Florida Industrial Power Users Group ("FIPUG"). The Hedging Order established a framework and direction for the Commission and the parties to follow with respect to risk management for fuel procurement. That framework, with some later modifications, constitutes the risk management policy and procedures the Commission follows today.

In the Hedging Order, the Commission noted that the resolution it approved appeared to remove disincentives that may have existed for IOUs to engage in financial hedging transactions that may create customer benefits by providing a cost recovery mechanism for prudently incurred financial hedging transaction costs, gains and losses, and incremental operating and maintenance expenses associated with new and expanded hedging programs.

² Order No. PSC-02-1484-FOF-EI, issued October 30, 2002 in Docket No. 011605-EI

Order No. PSC-08-0316-PAA-EI³ was the first of two clarification orders in 2008 to the Hedging Order. This Order established a requirement that each IOU file a current-year, financial hedging review (Hedging Information Report) that provides actual hedging information for the period August 1 through July 31 of each year. The reporting requirement was established to enhance the Commission's tools for reviewing the prudence of the utilities' most recent financial hedging activities.

The Commission then entered Order No. PSC-08-0667-PAA-EI⁴, affirming its long-term support for financial hedging. In reviewing FPL's guidelines for financial hedging, the Commission noted that hedging can reduce the volatility of fuel adjustment charges paid by customers and that a well-managed financial hedging program does not involve speculation. The Commission further noted that in the 2008 mid-course corrections for DEF, FPL and Gulf, hedging gains significantly reduced the projected under-recoveries. The Commission said that it had previously found that customers benefit from stable rates that allow the customers to budget for electric bills and hedging has contributed to the stability of fuel factors.

In its ruling in Order No. PSC-08-0667-PAA-EI, the Commission stated that by approving FPL's proposed guidelines, "we demonstrate our support for hedging." The Commission further stated:

We find that utility hedging programs provide benefits to customers. By approving these guidelines we provide regulatory support and guidance regarding hedging programs.

The benefits of hedging were highlighted in a management audit conducted by the Commission's Staff in 2008. Upon completion of the Staff's audits of the IOU's hedging activities, the management audit concluded:

³ Order No. PSC-08-0316-PAA-EI, issued May 14, 2008 in Docket No. 080001-EI

⁴ Order No. PSC-08-0667-PAA-EI, issued October 8, 2008 in Docket No. 080001-EI

Overall, audit staff believes that the use of financial hedges for fuel purchases provides a benefit to utility customers. Each program is appropriately controlled, efficiently organized, and operates under a non-speculative format. There are areas of improvement, which are outlined later in each company's chapter. Generally, each company has successfully mitigated the price volatility for its customers. There have been years in which each company's hedging program provided a gain on its fuel cost, and years in which each program has incurred losses. This is to be expected. Hedging commodities involves the risk of higher prices at the expense of attempting to reduce price volatility. For each company, there is an acceptable level or risk tolerance between the two. Each utility must continue to gauge its customers' tolerance of the cost associated with hedging versus the benefits of reduced fuel cost volatility and any resulting rate increase.

Through its initial approval of the proposed resolutions in 2002 and later, through subsequent orders clarifying the Commission's view on hedging, the Commission and its Staff have recognized the benefits of financial hedging and its impact on the utilities' customers. Additionally, the Commission has carefully monitored and evaluated the conduct of each IOU's financial hedging activities with no suggestion of imprudence.

In 2011, the Commission reviewed the current natural gas financial hedging program in a workshop in which all affected persons were afforded an opportunity to provide input. After considering all of the input in that workshop the Commission saw fit to allow the hedging programs to continue.

As reflected above, natural gas hedging has been the subject of considerable study and discussion before the Commission, and the consistent conclusion has been that hedging benefits investor-owned electric utility customers in Florida through the mitigation of natural gas price volatility and the resulting volatility of fuel and purchased power cost recovery factors.

The November 2015 Fuel Hearing

In the recently completed cost recovery hearing, OPC, FIPUG, the Florida Retail Federation ("FRF") and White Springs Agricultural Chemicals, Inc., d/b/a PCS Phosphate-White Springs ("PSC Phosphate") (collectively, "Intervenors") uniformly took the position that, given cumulative opportunity costs (losses) incurred by the Florida IOUs through operation of their Commission approved natural gas hedging programs, the Commission should curtail those hedging programs. FPL, DEF, Gulf and Tampa Electric asserted that their currently approved hedging programs have enabled their respective customers to avoid the effects of natural gas price volatility and the resulting impacts on the amounts they are required to pay through the fuel and purchased power cost recovery charges.

The current financial hedging programs of FPL, DEF, Gulf and Tampa Electric have been carefully developed, reassessed and reaffirmed over the past 13 years as being in the consumers' best interests. The issues to be resolved are whether those programs should be retained, terminated or modified, and whether Tampa Electric's proposed Risk Management Plan for 2016 should be approved.

SUMMARY OF TAMPA ELECTRIC'S ARGUMENT

Tampa Electric believes it is appropriate for the Commission to approve the continuation of the company's financial hedging program for natural gas purchases, without modification, and urges the Commission to approve the company's proposed 2016 Risk Management Plan. The same risks associated with natural gas price volatility that formed the basis for the Commission's Hedging Order in 2002 remain present today. OPC's witness Lawton failed to establish a compelling basis for abandoning the current hedging model and readily conceded that he cannot predict the future.

If, notwithstanding the foregoing points, the Commission decides to curtail financial hedging of natural gas prices by the IOUs, any such curtailment should be done prospectively and should not impact any hedges made prior to the effective date of any such curtailment. Any such curtailment should remain in place until such time as the Commission orders approval of new risk management plans after taking into consideration input from all affected persons.

POINT I

THE COMMISSION SUPERVISED NATURAL GAS HEDGING PROGRAMS HAVE ACCOMPLISHED THEIR INTENDED GOAL OF MITIGATING NATURAL GAS PRICE VOLATILITY AND FUEL ADJUSTMENT FACTOR VOLATILITY.

The Commission has recognized on many occasions that customers of the IOUs have benefitted from the utilities' hedging programs through the reduction of natural gas price volatility and the corresponding reduction in fuel cost recovery factor volatility. For example, in its order⁵ clarifying the Hedging Order, the Commission observed:

We note that in the recent 2008 mid-course corrections for PEF, FPL and Gulf, hedging gains significantly reduced the projected under-recoveries. In these particular cases, hedging significantly reduced the amount of mid-course factor increases.

In that Order the Commission further stated:

We have previously found that customers benefit from receiving accurate price signals through cost base rates, and that customers benefit from stable rates that allow the customer to budget for electric bills. Hedging has contributed to the stability of fuel factors.

In the recently concluded hearing, Tampa Electric's witness Brent Caldwell testified that, measured over the history of Tampa Electric's hedging program, the standard deviation of monthly market prices of natural gas has been 43 percent, whereas the standard deviation of

⁵ Order No. PSC-08-0667-PAA-EI, issued October 8, 2008 in Docket No. 080001-EI

monthly hedged prices has been 30 percent. This reflects a significant "smoothing" of the price of natural gas used for the projection and true-up of the fuel cost recovery factor. (Tr. 1058)

Mr. Caldwell further testified that a non-speculative risk management program diminishes the likelihood of mid-course corrections and significant over-recoveries and under-recoveries, thereby reducing annual fuel cost recovery factor volatility. (Tr. 1058-1059)

FPL's witness Yupp testified that his company's hedging program has been successful in reducing the volatility of fuel costs paid by customers. He stated that over the 13-year period, 2002 through 2014, FPL was outside of the plus or minus 10 percent mid-course correction threshold band just once with hedges included, but would have been outside that band nine times with the impact of hedges removed, clearly demonstrating the effectiveness of hedging as a means of reducing the volatility of fuel costs. (Tr. 939-940)

Even OPC's witness Lawton agreed that the Florida companies' hedging programs accomplish the goal of limiting natural gas price volatility, stating that it is an "automatic" result. He observed that just as daily price changes, by definition, create the certainty of daily price volatility, locking in and fixing future prices, rather than relying on day-to-day market prices, automatically reduces volatility. (Tr. 839). Mr. Lawton only questioned the need for the Florida IOUs to continue hedging, although he readily conceded that he could not predict the future. (Tr. 896)

It is clear from the record that the hedging programs of the Florida utilities have achieved their goal of mitigating the volatility of natural gas prices and fuel adjustment charges, devoid of any effort on the part of the utilities to speculate or attempt to profit on natural gas price swings.

POINT II

WHILE INTERVENORS HAVE EXPRESSED A CONCERN OVER HEDGING OPPORTUNITY COSTS (LOSSES) IN A DOWN MARKET FOR NATURAL GAS, THOSE CONCERNS WOULD NOT BE PRESENT IF THE PRICE OF NATURAL GAS WERE RISING AND CUSTOMERS WERE RECEIVING GAINS THROUGH HEDGING.

As Tampa Electric witness Caldwell testified, it is very doubtful we would be seeing criticisms of financial hedging of natural gas prices if those prices were rising. It is only because prices have declined more than the prices built into the utilities' hedging programs that we see opposition to the current hedging model. It is important to put the issue in context. All customers have benefitted from the decline of natural gas prices. The issue raised by intervenor witnesses is that customers haven't also received the difference between the hedged prices and the lower market prices. That is a natural consequence of a financial hedging program. Had prices been rising over time, the utilities' hedging programs would have protected customers from having to pay the amount by which higher market prices exceeded the hedged prices. (Tr. 1054)

FPL's witness Yupp surmised that had FPL's hedging activities resulted in significant gains over the last 13 years, we likely would not be debating the propriety of hedging, although in reality FPL's customers would have paid significantly more in fuel costs. (Tr. 952)

OPC's witness Lawton focuses on lost opportunity costs and suggests that hedging should be terminated, given the low level of natural gas prices at the current time. He further suggests that the Commission could revisit hedging as circumstances change in the future. This is nothing more than a chasing-the-market approach that could constitute exactly the sort of speculation the Commission directed utilities to avoid when it first announced hedging guidelines in 2002. (Id.)

POINT III

OPC'S WITNESS LAWTON OVERLOOKS OR DISMISSES FACTORS WARRANTING THE CONTINUATION OF THE UTILITIES' HEDGING PROGRAMS.

OPC's witness Lawton concluded that the abundance of shale gas has changed natural gas market dynamics to the extent that financial hedging of natural gas purchases will no longer be needed. As witness Caldwell explained, this totally discounts the history of natural gas pricing. There have been similar periods of natural gas production growth and surplus such as the deep water Gulf of Mexico development in the late 1990's and the promise of an international bounty of liquefied natural gas ("LNG") in the early to mid-2000's. In both cases natural gas prices decreased at first but, ultimately, demand recovered and exceeded supply to the point that natural gas prices spiked until new supply could restore balance. (Tr. 1056)

Witness Caldwell could not say whether history will repeat itself with non-conventional shale gas production. However, he could not be as certain as witness Lawton that the surplus provided by shale gas is here for the foreseeable future. (Id.)

Witness Lawton also failed to give full consideration to the changing electric generation mix in Florida and nationally. As witness Caldwell explained, this changing generation increases the demand for natural gas, as coal-fired and dual fuel natural gas units with oil backup are replaced with gas only generation, and the U. S. nuclear fleet ages toward retirement. As witness Caldwell testified, this increasing reliance on natural gas for electric generation not only puts upward pressure on prices due to demand growth, but it also increases the total cost impact and volatility of prices. Natural gas is a larger percentage of the electric generation cost, and there is little to no diversity of fuel alternatives during periods of high demand or supply constraint. (Tr. 1057)

Witness Lawton's testimony fails to acknowledge or summarily dismisses significant factors that may impact the future volatility of natural gas prices and the resulting cost of electricity to Florida consumers.

POINT IV

NO CHANGES SHOULD BE MADE TO THE MANNER IN WHICH ELECTRIC UTILITIES CONDUCT THEIR NATURAL GAS FINANCIAL HEDGING ACTIVITIES.

None of the Intervenors has suggested any modification to the manner in which electric utilities conduct their natural gas financial hedging activities. They simply have urged the Commission to curtail those activities.

The only time this issue was raised during the hearing was through cross-examination of the utilities' witnesses. When asked whether it would be appropriate to have a sharing of the gains and losses from financial hedging as between utility customers and the utilities, no utility witness responded that such a sharing would be appropriate. In fact, witness Caldwell for Tampa Electric observed that if a utility were afforded an opportunity to profit from hedging, but the real objective is to obtain stable prices for customers, there would be a potential for a conflict. (Tr. 1067)

The current natural gas financial hedging model was developed and approved only after careful consideration and deliberation by the Commission and all affected persons. There is no record basis for modifying the current model. The essential choice before the Commission is whether to continue the current model or curtail its use.

POINT V

IF, NOTWITHSTANDING THE FOREGOING POINTS, THE COMMISSION DECIDES TO CURTAIL FINANCIAL HEDGING OF NATURAL GAS BY THE IOUs, IT SHOULD BE DONE PROSPECTIVELY AND NOT IMPACT ANY HEDGES MADE PRIOR TO THE EFFECTIVE DATE OF ANY SUCH CURTAILMENT.

Tampa Electric believes that foregoing points place natural gas hedging in the proper perspective and provide the Commission an ample basis for denying the Intervenors' request that hedging be curtailed based on speculation about future natural gas prices and price volatility. However, in the event the Commission elects to curtail natural gas hedging, it should be done prospectively and not impact hedges entered into prior to the effective date of any such curtailment.

Even OPC's witness Lawton recommended that financial hedging of natural gas should be discontinued on a going-forward basis. Mr. Lawton stated:

. . . [I]f they stopped hedging now, I would expect that all hedges that are in place be left in place until they expire in the future when the hedge contract requires. (Tr. 871-872)

Witness Ball, testifying for Gulf, was asked about the appropriate treatment of already existing hedges in the event the Commission ordered the utilities to cease hedging. He recommended against going mark-to-market and immediately unwinding previously executed hedges and, instead, recommended letting them expire under their own terms. His first reason was that under an immediate unwinding, all of the IOUs in the state of Florida would be unwinding all of their hedges at the same time which would be a significant market event. He explained:

...and believe me, the financial counterparties would take advantage of that and they would extract as much financial gain as they possibly could because of that event. (Tr. 705)

Mr. Ball's second reason for not unwinding ahead of hedge maturities is that existing hedges are in place to mitigate price risk out into the future. As Mr. Ball explained:

So if you settle those hedges today, essentially what you do is you incur all the costs associated with the hedges, but you get none of the benefits in the future from potential future price volatility. There is really no reason to settle these hedges or unwind these hedges on January 1st of 2016.

Mr. Ball concluded that the reasonable thing to do, in his opinion, is just to allow the hedges to naturally expire and naturally settle as they were originally intended. (Id.)

Tampa Electric's witness Caldwell concurred and stated that he would not want to unwind everything at one time. According to Mr. Caldwell, that much selling into the market could certainly deflate the price. He further stated his belief that allowing the hedges to expire naturally would be the best way to protect customers from price spikes while allowing the existing hedging policies run their course. (Tr. 771)

Assuming, but not conceding, that the financial hedging of natural gas prices should be curtailed, any attempt to immediately unwind existing hedges is clearly inappropriate, not in the best interests of consumers in Florida and could accelerate projected losses into the current year as realized losses, when they otherwise could be deferred into future years and possibly turn into gains, depending upon the natural gas market.

On this point Tampa Electric submits that if the Commission determines the financial hedging of natural gas prices should be curtailed, such curtailment should remain in effect until such time as any new hedging program may be established by final order of the Commission, after a proceeding affording the opportunity for input from all affected persons. Such was the process followed by the Commission in 2002, as modified in 2008.

POST-HEARING STATEMENT OF ISSUES AND POSITIONS

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

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

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

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

ISSUE 6B: Should the Commission approve Tampa Electric's 2016 Risk Management Plan?

TECO: *Yes. Tampa Electric's 2016 Risk Management Plan provides prudent non-speculative guidelines for mitigating price volatility while ensuring supply reliability. This Plan like the ones that preceded it, has been prepared in

accordance with the Commission's Hedging Order and subsequent orders refining hedging guidelines.* (Caldwell)

SUMMARY

Based on the foregoing, Tampa Electric urges the Commission to approve the continuation of Tampa Electric's natural gas financial hedging activities and to approve the company's proposed 2016 Risk Management Plan.

DATED this 13th day of November 2015.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Brief and Post-Hearing Statement of Issues and Positions, filed on behalf of Tampa Electric Company, has been furnished by electronic mail on this 13th day of November 2015, to the following:

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