BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for rate increase by Florida Power & Light Company	Docket No. 160021-EI
In re: Petition for approval of 2016-2018 storm hardening plan, by Florida Power & Light Company	Docket No. 160061-EI
In re: 2016 depreciation and dismantlement study by Florida Power & Light Company	Docket No. 160062-EI
In re: Petition for limited proceeding to modify and continue incentive mechanism by Florida Power & Light Company	Docket No. 160088-EI
	Filed: September 19, 2016

CITIZENS' POST-HEARING BRIEF

Pursuant to Order No. PSC-16-0341-PHO-EI, issued August 19, 2016, the Citizens of the State of Florida by and through the Office of Public Counsel ("Citizens" or "OPC"), hereby submit this Post-Hearing Brief.

STATEMENT OF BASIC POSITION

FPL's request for a base rate increase is excessive for 2017, without even considering the additional requests for the subsequent time periods. FPL has amended its request to seek an approximately $826 million base rate increase in 2017. In addition, FPL is asking for another $270 million increase in 2018, plus a third increase of $209 million in mid-2019 for the Okeechobee Clean Energy Center ("Okeechobee"). (TR 147) FPL claims its petition covers a four-year period and that it will not seek another increase if it receives its entire request; however, there is no prohibition for the Company filing for an increase should it earn below its authorized return. In fact, Mr. Silagy conceded that "anything less, we'll [FPL] have to look and see what the opportunity to stay out or not." (TR 148) FPL is also are asking for a 100 basis points (or 1% point increase over its currently authorized return on equity ("ROE") midpoint of 10.5% to 11.5%, including a 50 basis point "adder." (Petition at pp. 1-2). This level of ROE is unwarranted, and would be disproportionate to current market conditions as well as other ROE's that have recently been awarded by other state utility commissions.

OPC's multiple expert witnesses conducted an extensive and thorough review of FPL's petition, Minimum Filing Requirements ("MFRs"), discovery responses, and testimonies filed in this base rate proceeding (Docket No. 160021-EI), as well as the same documentation for Dockets Nos. 160061-EI, Storm Hardening Plan, 160088-EI, Incentive Mechanism, and 160062-EI, Depreciation and Dismantlement, which have been consolidated with the base rate case. The following experts testified at hearing on behalf of OPC: Dr. David Dismukes, Incentive Mechanism and Forecasting; Helmuth Schultz, C.P.A, Accounting Adjustments; Ralph Smith, C.P.A., Accounting Adjustments and Revenue Requirement; Dr. Randy Woolridge, Return on Equity; Kevin O'Donnell, C.F.A., Capital Structure; and Dan Lawton, Financial Integrity and Surplus ROE Inflator. OPC's experts testified regarding three principal areas for adjustment: Revenues; Capital Structure; and Return on Equity.

Revenue Increase

Dr. Dismukes reviewed FPL's forecasts for 2017 and 2018. After comparing the 2015 Net Energy For Load ("NEL") forecast FPL used for its Ten Year Site Plan ("TYSP") and its Okeechobee need determination case with the forecast used to prepare this rate case, Dr. Dismukes testified that FPL's rate case forecast significantly understates revenues in the test year. He recommends the Commission reject FPL's proposed rate case forecast and employ the 2015 NEL forecast previously submitted by FPL and used by the Commission to approve the Okeechobee need determination. Adopting the 2015 NEL forecast decreases the Company's revenue requirement request by $206.5 million in 2017 and $259.5 million in 2018. (TR 3368-3369, 3386-3389)

Capital Structure

Mr. O'Donnell testified regarding FPL's excessive equity ratio request of 59.6% equity. As Mr. O'Donnell testified, FPL's request puts an unnecessary costly burden on FPL's ratepayers - an extra $40.97 per year to typical residential customers - and should not be allowed. (TR 3539-3540) Mr. O'Donnell's examination of capital structures demonstrates that FPL's proxy group average equity ratio is 49.3% and the national average for allowed equity ratios is 49%. (TR 3553,

3557) Rather than utilizing FPL's proposed unreasonable, hypothetical capital structure of 59.6% equity, Mr. O'Donnell recommends using a more rational hypothetical capital structure of 50% equity. Applying a 50% equity ratio, which is in line with industry averages (and still more than the equity ratios of both NextEra's consolidated group and the FPL proxy group average), results in an approximately $337 million reduction to FPL's 2017 request. (TR 3558-3559)

Return on Equity ("ROE")

Dr. Woolridge testified regarding his evaluation of FPL's requested ROE in light of current market conditions and the changes since FPL's last rate case. (TR 3194-3195) FPL's requested 11% ROE, especially with its requested 59.6% equity ratio, is clearly excessive under current market conditions. Dr. Woolridge testified that both interest rates and awarded ROEs have decreased since 2012. (TR 3185-3189) Dr. Woolridge, applying the Discounted Cash Flow ("DCF") method checked by the Capital Asset Pricing Model ("CAPM") method with a proposed capital structure of 50% and utilizing a comparable electric proxy group, determined the appropriate ROE for FPL is 8.75%. (TR 3184) Utilizing an 8.75% ROE would result in an approximately $540 million reduction from FPL's 2017 request. (TR 207, 208)

Additional Issues

OPC experts recommend additional adjustments based on their thorough examination of FPL's requests. Mr. Schulz recommend reductions to FPL's requested increases related to unneeded new employee positions, incentive compensation, storm hardening related expenses, and Director and Officers Liability Insurance. (TR 3463, 3469, 3488, 3493) Mr. Smith recommends reductions for Plant Held for Future Use ("PHFFU"), rate case expenses, generation overhaul expenses, and tax-related costs. (TR 3725, 3734, 3736) Mr. Lawton discussed FPL's ability to maintain its financial integrity with the implementation of OPC's recommendations. Mr. Lawton further testified that no ROE inflator should be allowed. He noted performance bonuses are incentives that regulatory authorities already appropriately use for management and employees, and questioned why shareholders should receive an ROE inflator when they have done nothing to justify it. (TR 3657-3658, 3666)

Burden of Proof

Pursuant to Section 366.06, Florida Statutes ("F.S."), a public utility shall not, directly or indirectly, charge or receive any rate that has not been approved by the Commission. When a utility wants to change any rate, an application for change in rates shall be made to the Commission which has the authority to determine and fix fair, just, and reasonable rates for that utility. In accordance with Section 366.07, F.S., if after a public hearing, the Commission finds the rates unjust, unreasonable, insufficient, excessive, or unjustly discriminatory or preferential or in anywise in violation of law, the Commission shall determine and fix fair and reasonable rates. These public hearings are governed by Section 120.57, F.S., which sets forth the procedures for the Commission's proceedings. Under Section 120.57, the findings of fact shall be based upon a preponderance of evidence and shall be based exclusively on the evidence of record and on matters officially recognized. See, Section 120.57(j), F.S. The Commission observed in a water case that:

> we are charged with the statutory responsibility of setting rates which are fair and reasonable. It is neither our nor our staff's responsibility to make the utility's case. The burden of proof is upon the utility to show that its present rates are unreasonable, fail to compensate the utility for its prudently incurred expenses, and fail to produce a reasonable return on its investment.

Order No. PSC-07-0129-SC-WS, issued February 14, 2007, in Docket No. 060262-WS. The Florida Supreme Court stated in Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (1982) that the "burden of proof in a commission proceeding is always on a utility seeking a rate change, and upon other parties seeking to change established rates." Thus, it is FPL's burden of proof to demonstrate by a preponderance of evidence in the record in this proceeding that current rates are unjust, unreasonable or insufficient and that the changes FPL has requested are necessary and will result in rates that are fair, just and reasonable.

Conclusion

An extensive review of the record in this proceeding will demonstrate that a rate **decrease** of $327.5 million is appropriate for 2017, and that no rate increases are needed for 2018 or for the Okeechobee limited scope adjustment in 2019. (TR 3706)

POSITIONS AND ARGUMENT ON DISPUTED ISSUES

ISSUE 1: Does the Commission possess the authority to grant FPL's proposal to continue utilizing the storm cost recovery mechanism that was part of the settlement agreements approved in Order Nos. PSC-11-0089-S-EI and PSC-13-0023-S-EI?

POSITION: *The Commission may have the authority to implement the mechanism under certain conditions. *

ARGUMENT:

Florida law provides guarantees of due process to parties who can show their substantial interests will be affected by agency action, and who raise disputed issues of material fact. Sections 120.569 and 120.57(1), Florida Statutes, require an agency that is subject to the Florida Administrative Procedure Act (such as the Commission) to afford an opportunity for parties to respond, to present evidence and argument, and to conduct cross-examination before it enters findings of fact and conclusions of law.

In addition, before the Commission sets rates, it must comply with the provisions of Chapter 366, Florida Statutes. Chapter 366 provides, among other things, that actions pursuant to the file-and-suspend ratemaking provisions must provide for a public hearing (Sections 366.06(2) and 366.07, Florida Statutes). Failure to comply with these statutory provisions would subject the Commission's order to remand on appeal. Sections 120.68(7)(a) and 120.68(7)(b), Florida Statutes.

The Citizens contend that stipulation is the appropriate way for a party to negotiate away the rights that these statutory provisions create and protect. In the negotiated settlement agreement that the Commission approved in Order No. PSC-10-0153-FOF-EI, OPC and other parties agreed to a storm cost recovery mechanism (SCRM) provision establishing certain procedural and substantive storm cost-related terms, to be effective for a finite period of time. (The terms to which they agreed enabled FPL, among other things, to begin collecting storm-related costs within 60 days of filing a petition, and to do so without reference to its ability to absorb costs within its earnings, regardless of the magnitude of its earnings levels.) OPC agreed to these terms in the context of a give-and-take global compromise, in which each party agreed to accept individual provisions, which it would otherwise contest, because each party believed the value it received through its participation in the entire stipulation more than offset the concessions it made in individual terms. This SCRM provision was renewed in the three-party settlement embodied in Order No. PSC-13-0023-S-EI.

The current settlement agreement, including the SCRM provision, will expire at the end of 2016. At that point, OPC and other parties who will be affected by Commission action in the areas that have been the subject of the settlement agreement will again have full rights of due process provided by law to dispute any aspect of FPL's request, unfettered by the obligations of expired contractual terms.

Inherent to a utility's request to recover costs of repairing storm damage are potential issues of material fact. Prior to the Commission's decision regarding the approval of a future storm cost recovery factor for FPL, OPC or other parties may wish to contest the utility's calculation of costs to be recovered, or contest the period of time over which the utility should collect costs, or dispute the magnitude of the storm reserve that FPL proposes, or contest the size of the cost recovery factor that FPL proposes to apply to customers' bills, or present evidence and argument supporting its view that the utility's earnings are such that it should absorb a portion of the storm costs in earnings before requiring customers to pay all of its storm-related costs. The particular circumstances of such future petitions by FPL may give rise to issues that cannot be anticipated in advance.

Each such issue will be a function of the specific factual circumstances attending each future storm event that leads FPL to petition for the recovery of storm-related costs. With the termination of the existing agreement, OPC (like other affected parties) will be able to avail itself of the rights guaranteed by Chapters 120 and 366, Florida Statutes.

However, the SCRM may be appropriate if any petition that is filed according to its provisions is appropriate under the limited proceeding statute (Section 366.076, Fla. Stat.) and the Commission provides certain protections to the parties. The SCRM was first established by stipulation in a 2010 settlement between Progress Energy Florida (now Duke Energy Florida) and the OPC and other intervenors. Order No. PSC-10-0398-S-EI, issued June 18, 2010 in Docket Nos. 900079-EI, 090144-EI, 090145-EI, and 100136- EI. The mechanism was adopted seven months later by FPL in its settlement with the same Duke intervenor parties plus the SFHHA. Order No. PSC-11-0089-S-EI in Docket Nos. 08677-EI and 090130-EI. The SCRM was adopted in virtually identical verbiage in the 2012 agreement adopted by the Commission in Order No. PSC-13-0023-S-EI on January 14, 2013 in Docket No. 120015-EI.

To the OPC's knowledge, there are no orders of the Commission reflecting that the SCRM has ever been invoked by FPL (or any other Company) filing a petition and tariff for recovery of storm-related costs. The OPC would not dispute that the Commission may possess the authority to independently establish the SCRM if it is strictly treated as an interim cost recovery mechanism pursuant to a file-and-suspend tariff, with full evidentiary and hearing rights pursuant to Section 120.57, Fla. Stat. and other applicable provisions of Chapter 120, and is treated as a petition for a limited proceeding. Sections 366.06(3); 366.076, Fla. Stat. See also Citizens v. Wilson, 567 So.2d 889, 891. Of course, consistent with these principles of law, any allowance of recovery on an expedited, interim basis utilizing the SCRM does not create a presumption of correctness for the costs that FPL might claim under the mechanism. That determination would come in the final hearing that the Commission is obligated to hold. Wilson at 892. Furthermore, as FPL's own highly touted regulatory expert, Terry Deason testified, the company has the burden of proof to prove the reasonableness and prudence of the costs for which it seeks recovery. (TR 5823). If found to be within its authority to do so and is thus allowed, the Commission should insure that access to the interim mechanism is expressly conditioned on at least three fundamental requirements:

a. That the storms that trigger the mechanism are named tropical storms by the National Hurricane Center or its successor.
b. That any party with standing shall be entitled to fully participate in the final determination of the reasonableness and prudence of the storm restoration costs as to amount and basis for incurrence in accordance with Rule 25-6.0143, F.A.C., and Commission precedent where the utility has the burden to prove all elements of recovery. (TR 5823; 2528-2529).
c. That it is clear that any surcharge must be based on exhaustion of any existing reserve balance.

ISSUE 2: Does the Commission have the authority to approve FPL's requested limited scope adjustment for the new Okeechobee Energy Center in June of 2019?

POSITION: *OPC has not contested the authority of the Commission to approve a limited scope adjustment in this proceeding. However, OPC does not believe that a limited scope adjustment is reasonable or necessary based on OPC's recommended revenue requirements for 2017 and 2018 for the reasons set forth in Issues 124 through 133.*

ARGUMENT:

OPC has not contested the authority of the Commission to approve a limited scope adjustment in this proceeding. However, OPC does not believe that a limited scope adjustment is reasonable or necessary based on OPC's recommended revenue requirements for 2017 and 2018 for the reasons set forth in Issues 124 through 133.

ISSUE 3: Does the Commission possess the authority to adjust FPL's authorized return on equity based on FPL's performance?

POSITION: *** The Commission has the authority to adjust a utility's authorized rate of return upwards or downwards on the basis of management efficiency; however, the case law says nothing about "FPL's performance." See Gulf Power Co. v. Cresse, 410 So. 2d 492 (Fla. 1982); Gulf Power Co. v. Wilson, 597 So. 2d 270, 273 (Fla. 1992). If "FPL's performance" equates to "management efficiency", the answer is yes; otherwise, no. ***

ARGUMENT:

The Commission has the authority to adjust a utility's authorized return on equity upward or downward on the basis of *management efficiency*. See Gulf Power Co. v. Cresse, 410 So. 2d 492 (Fla. 1982) (finding the Commission did not abuse its discretion to add ten basis points to Gulf Power's ROE in recognition of its energy conservation efforts); Gulf Power Co. v. Wilson, 597 So. 2d 270, 273 (Fla. 1992) (finding the Commission has "the discretion to reward, within the reasonable rate of return range, for management efficiency" as well as "the authority to reduce the rate of return for mismanagement, as long as the resulting rate of return falls within the reasonable range set by the Commission."

As the issue is framed, FPL is seeking a reward or adder for utility performance, not necessarily management efficiency. If utility performance is equivalent to management efficiency, then yes, a reward or penalty can be authorized. However, as a matter of sound regulatory policy, the utility should not be granted a reward or penalty for utility performance when many factors outside of utility management's control contribute to the utility's good or bad performance. In FPL's case, historically low natural gas prices have contributed greatly to lower overall rates (TR 3610) when compared with neighboring utilities who are not as heavily dependent on natural gas for generation. If fortunes change, and natural gas prices soar, could FPL be penalized for its management's decisions to increasingly rely upon natural gas?

Whatever ROE reward or penalty is approved for any utility, it still must comport with the *Hope* and *Bluefield*[1] standards. In *Hope*, the U.S. Supreme Court found that:

> the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital.

320 U.S. at 603. The Commission has the authority to establish a return on equity commensurate with the *Hope* and *Bluefield* standard. And Florida case law is clear that the reward or penalty must fall within the reasonable range of rate of return established by the Commission for that utility based on that standard. Gulf Power Co. v. Wilson, 597 So. 2d at 273. In the Gulf Power case, the Commission approved an upward adjustment of 25 basis points to Gulf Power Company's equity return for performance related to conservation measures. *See* Order No. PSC-02-0787-FOF-EI, issued June 10, 2002, in Docket No. 010949-EI at pp. 35-36. The Commission set rates using the midpoint and 25 basis point adjustment yet it maintained the 100 basis point range based on the cost-based mid-point approved by the Commission in that case.

Therefore, if the Commission does approve a surplus ROE inflator adder to FPL's authorized ROE based on performance, the inflator adder (1) should not exceed the range of the rate of return determined to be reasonable; and (2) should not shift or expand the range, because the reward or penalty must fall within the range. Gulf Power Co. v. Wilson, 597 So. 2d at 273.

[1] *Federal Power Commission v. Hope Natural Gas Co*., 320 U.S. 591 (1944) ("*Hope*") and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923) ("*Bluefield*").

While the legal basis for allowing a reward or penalty for *management efficiency* is settled, the question remains: can utility performance form the basis for the awarding of a reward or penalty, when many factors outside management's control contribute to utility performance: That legal distinction is something this Commission must resolve.

ISSUE 4: Does the Commission have the authority to include non-electric transactions in an incentive mechanism?

POSITION: *No. In Citizens v. Graham, 191 So. 3d 897 (Fla 2016), the Florida Supreme Court stated that under the plain meaning of Section 366.01 and Section 366.02, Florida Statutes, cost recovery is permissible only for costs arising from the "generation, transmission, or distribution" of electricity. Id. at 7. It would exceed the Commission's authority to grant cost recovery to the extent FPL proposes to earn a return for non-electric transactions in an incentive mechanism.*

ARGUMENT:

FPL Witness Forrest testified that FPL is seeking approval of the Incentive Mechanism (IM) which was approved as a four-year pilot program as part of the 2012 Settlement. (TR 2053, Order No. PSC-13-0023-S-EI, issued January 14, 2013, in Docket No. 120015-EI). The 2012 IM allows the sharing of gains resulting from electric wholesale purchases and sales, and asset optimization. The asset optimization included gas storage utilization, city-gate gas sales using existing transport, production area gas sales, capacity release of gas transport and electric transmission, and outsourcing of the optimization function. See Order No. PSC-13-0023-S-EI at p. 6. The threshold for customers receiving 100 percent of the gain is set at $46 million, $36 million (Customer Saving Threshold) and an additional $10 million (Additional Customer Savings). Thereafter, the customers and FPL would share the gains as follows: 1) between $46 million and $100 million, customers receive 40 percent of the incremental gains; and 2) over $100 million, customers receive 50 percent of the incremental gains. Order No. PSC-13-0023-S-EI at pp. 6 and 7. The 2012 IM also allowed FPL to recover its reasonable and prudent incremental O&M costs for the program through the Fuel Clause. Id. at p. 7. In addition, the variable power plant O&M costs incurred to generate additional output in order to make wholesale sales would be included if the level of sales exceeds 514,000 MWh. Id.

FPL Witness Forrest acknowledged that the 2012 IM would automatically terminate at the end of 2016 unless authorized to continue as part of this base rate request. (TR 2053) FPL proposed to continue the 2012 IM with two modifications. First, FPL proposes to lower the total customer sharing threshold from $46 million to $36 million due to the ending of a Unit Power Sales contract with Southern Company at the end of 2015. (TR 2054) Second, FPL proposes to eliminate the 514,000 MWh threshold before sharing of variable power plant O&M for Fuel Clause inclusion because FPL choose not to include any wholesale O&M in the base rate case filing. (TR 2054) The policy reasons why not to approve this requested IM as modified are addressed in Issue 134.

Since the last base rate case, in which the Commission approved the 2012 IM, the Florida Supreme Court in Citizens v. Graham, 191 So. 3d 897 (Fla 2016) ruled on the Commission's approval of the Woodford project. The Woodford project was FPL's joint venture with PetroQuest, a publically traded independent oil and natural gas company. Pursuant to the agreement, FPL would invest in PetroQuest's shale gas reserves and in return receive the rights to share in the physical gas produced. Citizens v. Graham at p. 3.

In Citizens v. Graham, the Court stated that under the plain meaning of Sections 366.01 and Section 366.02, F.S., cost recovery is permissible only for costs arising from the "generation, transmission, or distribution" of electricity. Id. at p. 7. Further, the Court also noted that utilities through the fuel clause do not earn a return on money spent to purchase fuel or earn a return on the cost of hedging positions purchased. Id. at pp. 8-9. Thus, it would exceed the Commission's authority to grant cost recovery to the extent FPL proposes to earn a return on non-electric transactions in an incentive mechanism.

Specifically, under Citizens v. Graham, it is highly unlikely that the Commission has the authority to approve some if not all of the activities in the asset optimization portion of the IM. As stated above, the asset optimization activities includes **gas storage utilization**, **city-gate gas sales using existing transport**, **production area gas sales**, capacity release of gas transport and electric transmission, and outsourcing of the optimization function. See Order No. PSC-13-0023-S-EI at p. 6. In Citizens v. Graham, the Court plainly stated that, "under the plain meaning of these two statutes [sections 366.06(1) and 366.02(2)], cost recovery is permissible only for costs arising from 'generation, transmission, or distribution' of electricity." Id. at p. 7. The Court also noted that utilities through the fuel clause do not earn a return on money spent to purchase fuel or earn a return on the cost of hedging positions purchased. Id. at pp. 8-9. Clearly, under Citizens v. Graham, it is beyond the Commission's authority to approve recovery relating to sales of production gas since the Commission has no authority to authorize or allow recovery of natural gas production. Id. at 10. Moreover, including in an IM any activities whereby FPL can earn a profit on fuel (i.e. the natural gas in storage or city-gas natural gas sales) is contrary to the plain language of Citizens v. Graham. Id. at p. 10. Capacity is also recovered through the fuel clauses. (TR 3425) Thus, under the rationale of Citizens v. Graham where the Court noted utilities do not earn a return on "fuel" and also that capacity is part of the fuel clause, it is highly arguable whether FPL has the statutory authority to earn a profit on these types of fuel clause activities. Id. at p. 10. Thus, OPC submits it would exceed the Commission's authority to approve activities for which FPL proposes to earn a return for non-electric transactions in an incentive mechanism.

ISSUE 5: Does the Commission have the authority to approve proposed depreciation rates to be effective January 1, 2017, based upon a depreciation study that uses year-end 2017 plant balances?

POSITION: *Under the facts and circumstances of this case, the study may well meet the requirements of the Commission's depreciation rule.*

ARGUMENT:

On April 28, 2016 Rule 25-6.0436(4)(d) was amended to provide that:

> The plant balances may include estimates. Submitted data including plant and reserve balances or company planning involving estimates shall be brought to the effective date of the proposed rates.

This subsection was part of an amendment to the rule that was proposed on March 1, 2016, two weeks before the study was filed, and which became final after the filing of the study. FPL was undoubtedly on notice at the time of filing on March 15, 2016 that the Commission intended that future depreciation studies would align the expenses would be calculated based on plant balances aligned with the effective date of rate changes where the study was filed in conjunction with the date of rates becoming effective. The record indicates that the study was delivered to FPL on March 5, 2016 but was substantially completed in 2015 (TR 1884; HE 133, p. 2).

Even if the study was lawfully filed under the rule, by projecting the rates to the end of the rate year, FPL has effectively overstated expenses. This is troubling and the OPC shares the concern voiced by SFHHA Witness Kollen. (TR. 4053-4058). The Commission should not give any weight to the fact that FPL has stated expense in this manner in considering whether to allow a 2018 step increase. Furthermore, if FPL's filed study is accepted, it should be modified to deny the overly aggressive recovery of combined cycle production plant lives and for the aggressive proposed interim retirements and capital spare parts, concepts addressed in Issues 42 and 44.

STORM HARDENING ISSUES

APPROVAL OF STORM HARDENING PLAN

ISSUE 21: Should the Company's Storm Hardening Plan for the period 2016 through 2018 be approved?

POSITION: *To the extent the plan is based on excessive and unnecessary levels of expenditures, it should not be approved.*

ARGUMENT:

To the extent the plan is based on excessive and unnecessary levels of expenditures, it should not be approved.

TEST PERIOD AND FORECASTING

ISSUE 24: Is FPL's projected test period of the 12 months ending December 31, 2017, appropriate?

POSITION: *Yes, with appropriate adjustments.*

ISSUE 25: Do the facts of this case support the use of a subsequent test year ending December 31, 2018 to adjust base rates?

POSITION: * A subsequent test year is not necessary or good policy. The appropriate test year should be representative of rates on a going-forward basis and negate any need for a subsequent rate adjustment absent any extraordinary circumstances, which FPL has not shown. OPC's recommendation is for a reduction of approximately $327 million based on the 2017 test year ($329 million with growth in 2018) and an overall revenue reduction of approximately $147 million for 2018. *

ARGUMENT:

OPC Witness Smith testified that using a subsequent test year is not necessary or good policy. (TR 3743) The test year should be representative of rates on a going-forward basis. (TR 3743)

As the Commission stated in Order No PSC-10-0153-FOF-EI, at page 9, "we have used the test year concept for setting rates. Under this concept, the test year is deemed to be representative of the future, and used to set rates that will allow the utility the opportunity to earn a rate of return within an allowed range." The Commission further stated that "[i]f the test year is truly representative of the future, then the utility should earn a return within the allowed range for at least the first 12 months of new rates." The Commission further noted that these types of back-to-back rate cases deprive the Commission and ratepayers of twelve months of actual economic data and operating history of the Company. Id. In addition, the Commission stated that "[w]e believe that back to back rate increases should be allowed only in extraordinary circumstances." Id. (TR 3743) In Order No. 10-0153-FOF-EI, the Commission noted that because of the unpredictability of the economy, it was possible that FPL's perceived need for a subsequent base rate increase could be offset by changes in sales growth, billing determinates, the Stimulus Bill, and other cost-decreasing measures. Id. at 10. Given the economic downturn and its negative impact on ratepayers, the Commission decided to wait and see if a subsequent rate case was justified. Id. The Commission found that FPL's request for a subsequent rate increase was simply too speculative and was rejected. Id. The Commission should follow that same logic in this case.

Witness Barrett agreed that the test year is supposed to be representative of rates on a going-forward basis. (TR 4577) However, he criticized Witness Smith's contention that there is no need for a 2018 rate increase. Witness Barrett argued that Witness Smith's calculation would show an incremental revenue deficiency irrespective of the outcome for 2017. (TR 4578) However, earlier in his testimony, Witness Barrett admitted that Witness Smith's calculation of a 2018 deficiency only results if OPC's original revenue reduction of $807 million is was approved by the Commission. (TR 4577) Based upon OPC revising its revenue decrease to $327.469 million for 2017 (HE 190), the Commission would need to approve a revenue decrease by $147.282 million or more for 2017 to create revenue deficiency for 2018. (HE 191) Therefore, only in the event the Commission approves a revenue decrease for 2017 greater than $147.282 million would there be any justification for a rate increase in 2018. Moreover and more importantly, on a stand-alone basis, there has been no showing that a subsequent 2018 test year is necessary or appropriate. (HE 191)

The Company has not shown any extraordinary need for a subsequent test year. (TR 3743) Furthermore, OPC's recommendation is to reduce current rates by approximately $327.469 million based on the 2017 test year ($329.339 million with growth in 2018), which would result in an overall revenue reduction of approximately $147.282 million for 2018.

ISSUE 26: Has FPL proven any financial need for rate relief in any period subsequent to the projected test period ending December 31, 2017?

POSITION: *No. Based on the 2017 test year, revenues should be reduced by approximately $327 million. Thus, no subsequent year adjustment is necessary. Based on the 2018 test year, if no rate change occurred in 2017, an overall revenue reduction of approximately $147 million is appropriate. (Smith)*

ARGUMENT:

For the reasons articulated in Issue 25, FPL has not met its burden to prove any financial need for rate relief for any period subsequent to the 2017 projected test year. Based on the 2017 test year, revenues should be reduced by approximately $327 million in 2017. Thus, no subsequent year adjustment is necessary. Based on the 2018 test year, if no rate change occurs in 2017, an overall revenue reduction of approximately $147 million is appropriate for 2018. (HE 191)

<u>ISSUE 27</u>: Is FPL's projected subsequent test period of the 12 months ending December 31, 2018, appropriate?

POSITION: * No, the subsequent test year adjustment is not necessary or good policy. FPL has not shown an extraordinary circumstance or need that warrants a 2018 test year. Based on the 2017 test year, revenues should be reduced by approximately $327 million. Thus, no subsequent year adjustment is necessary. Based on the 2018 test year, if no rate change occurred in 2017, an overall revenue reduction of approximately $147 million is appropriate. (Smith)*

ARGUMENT:

For the reasons articulated in Issue 25, FPL has not met its burden to prove that its use of a 2018 subsequent test year is appropriate. Based on the 2017 test year, revenues should be reduced by approximately $327 million in 2017. Thus, no subsequent year adjustment is necessary. Based on the 2018 test year, if no rate change occurs in 2017, an overall revenue reduction of approximately $147 million is appropriate for 2018. (HE 191)

<u>ISSUE 28</u>: Are FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the 2017 projected test year appropriate?

POSITION: * FPL's forecast of KWH by Rate Schedule and Revenue Class are based upon a faulty NEL energy sales forecast that the Commission should reject as unacceptable for ratemaking purposes. Instead the Commission should adopt the 2015 TYSP NEL forecast which will increase test year weather-normalized retail delivered energy by 3,896 gigawatt-hours or 3.5 percent. The adjustment will decrease the Company's needed revenue requirement increase by $206.5 million in 2017. *

ARGUMENT:

OPC Witness Dr. Dismukes reviewed FPL's load forecast and test year billing determinants included in the rate case filing. (TR 3368) FPL Witness Dr. Morley stated that the 2012 settlement in the last rate case implemented a change in rates based on the test year billing determinants derived from FPL's load forecast. (TR 1175) Therefore, it is important to examine the appropriateness of the forecasts FPL is proposing to develop its billing determinates.

FPL used multiple econometric models for customer growth, future electric load requirements, and winter/summer peak load requirements. (TR 3370) Witness Dismukes stated

FPL's load forecasting models can be grouped into three categories. The first group is the customer and sales models, 13 in total, which estimate the individual monthly customer and energy sales by major customer class (e.g. residential, small commercial, large commercial, small industrial, and large industrial). The second group is the two peak demand models to estimate summer and winter peaks. (TR 3371) The summer peak demand forecast is estimated on a per-customer basis using an economic process based on historical information and seven independent variables. (TR 3372) Finally, there is the Net Energy for Load ("NEL") model that estimates aggregate monthly energy requirements. The NEL model is estimated on a per-customer basis using an econometric process with 23 separate independent variables. Witness Dismukes testified the NEL model is estimated separately from the Company's monthly customer class sales models (which estimate energy on a per-class, as opposed to aggregated, basis). He further explained that any discrepancy between the two models (i.e. the sum of the individual customer class models versus the results from the aggregate energy sales, or NEL model) is allocated on an equal percentage basis between the Company's residential and commercial classes. (TR 3371)

In his testimony, Witness Dismukes identified problems in the Company's NEL forecast used for the rate case as compared to a 2015 NEL forecast that FPL previously prepared and relied upon. (TR 3368-3369) In 2015, FPL had 1.4 percent growth in customers and forecasted customer growth at a compound rate of 1.5 percent per year during the 2015-2020 period. (TR 3373) Weather-normalized retail-delivered sales grew at 0.8 percent compound rate between 2011 and 2015. Based upon this information, Witness Dismukes projects a weather-normalized retailed delivered sales growth rate of 0.7 percent on a compounded basis between 2015 and 2020. (TR 3373) In addition, Witness Dismukes testified that the Company's apparent comparison to historical trends is flawed because it mismatched time periods and did not compare years individually. (TR 3373)

Witness Dismukes prepared comparisons between the historic and expected trends in FPL's retail delivered sales for the years 2011-2020. (TR 3374) His comparison highlighted that FPL is erroneously anticipating a contraction (decrease) of overall sales relative to reported 2015 numbers, and that its overall sales numbers will not recover until 2019. (TR 3374) Witness Dismukes' comparison between the Company's NEL forecasts and peak load forecasts also demonstrated that customer and peak demand forecasts are moving in one direction (upwards), while its energy sales forecasts are estimated to move in an entirely opposite direction (downwards). (TR 3375)

Witness Dismukes concludes that there is a serious disconnect between FPL's peak demand, customer and sales forecasts. He opines that FPL anticipates relatively strong and consistent customer and peak demand growth while at the same time anticipating flat sales growth (excluding wholesale sales) relative to 2015 levels. Witness Dismukes testified that, if FPL's rate case forecasts are accurate, then it would imply that FPL's system average load factor, a degree of aggregate demand efficiency, is falling, not increasing. (TR 3375-3376)

Witness Dismukes also compared the historic load factor trend with the load forecast for the rate case. FPL's annual system load factor has remained stable with no clear upward or downward trend over the 2008 to 2015 timeframe (2009 low of 56.81%, 2008 high of 60.22%, with average of 58.77%). (TR 3376-3377) However, Witness Dismukes' examination of FPL's load factor shows that the Company projects its annual load factor to decline on a going-forward basis, dropping each and every year for the foreseeable future. By 2025, FPL forecasts its load factor to reach a level of 53.3% (5.3% lower than the eight-year average, or 3.3% below the lowest value during the eight year historical period). (TR 3377) Witness Dismukes noted that FPL is the only IOU projecting a consistently decreasing load factor over the 2016 to 2025 timeframe. (TR 3377-3378) Such a forecast implies that either (a) the Company is about to witness a significant and consistent reduction in end-use efficiency that will have considerable cost and generation resource planning implications or (b) the Company's projections, particularly its load projections arising from its NEL model, are significantly understated. (TR 3377) The NEL forecasts need to be 5.6% and 6.1% higher over the two rate years in order to bring the Company's estimated load factor in line with historical averages which would increase 2017 electricity sales by 6,677 gigawatt-hours and 2018 electricity sale by 7,340 gigawatt-hours. (TR 3379)

As a result of his analysis, Witness Dismukes determined the rate case NEL that FPL is proposing is unacceptable for ratemaking purposes. (TR 3368) He concluded that the 2015 TYSP energy forecast, which was virtually the same as the one filed later in FPL's 2015 Okeechobee need determination, should be used by the Commission for this rate case. (TR 3368) The Commission approved the Okeechobee need determination based upon the fact that the energy and peak demand forecasts submitted in that proceeding were consistent with the 2015 TYSP forecasts. (TR 3369) Witness Dismukes noted the 2015 TYSP and Okeechobee forecast are comparable.

However, the 2015 TYSP and Okeechobee forecast are not consistent with the energy sales forecast proposed by FPL to be used in this rate case because the differences are quite considerable, go far beyond updating the forecast models with more contemporaneous data, and have not explained or justified by the Company. (TR 3369)

Witness Dismukes made comparisons of the summer peak demand and NEL forecasts between the 2015 TYSP and rate case proceedings. He found that while there are some differences between the two peak demand forecasts, those differences were relatively small. However, he did find a large difference between the two NEL forecasts. Witness Dismukes determined that FPL's current rate case NEL forecasts for 2017 and 2018 are understated by more than four percent relative to the NEL forecast FPL provided in its 2015 TYSP. (TR 3384)

Witness Dismukes determined the 2015 TYSP load factor (NEL load divided by peak) is comparable to the 2011-2015 historic average load factor of 58.77%. The 2015 TYSP load factor projections were consistently between 56.8% and 58.3% for the 2016-2024 timeframe which is consistent with historical averages and trends over the past decade; however, the rate case forecast was not consistent with these historical averages and trends. (TR 3385) Witness Dismukes noted the Company's annual average load factor is calculated as the quotient of its annual load and its peak demand (times the number of hours in the year). The implied load forecast estimated from the Company's load forecast and peak demand forecasts reveals trends that are dramatically at odds with historic trends. (TR 3385)

Based on his analysis, Witness Dismukes concluded that in this proceeding either (1) FPL's proposed NEL forecast is in error, or (2) FPL's peak demand forecast is in error. However, the weight of the evidence suggests that it is FPL's NEL forecast that is in error since (1) the peak demand forecast included in this proceeding is relatively consistent with peak demand forecasts in the Okeechobee need determination and the 2015 TYSP, and (2) the Commission explicitly found that the peak demand forecasts in the 2015 TYSP and Okeechobee need determination were appropriate. Witness Dismukes concluded that FPL's NEL forecast needs to be adjusted for ratemaking purposes in this proceeding. (TR 3385)

Witness Dismukes also analyzed the difference between FPL's NEL forecast to the sum of the individual revenue models. The results of these various models should be close to one another if they are intended to be accurate, unbiased estimates for future load, regardless of whether that load is estimated in the aggregate (NEL forecast) or on a per revenue class basis. (TR 3386)

Witness Dismukes found that the NEL model significantly underestimates total retail sales by as much as two percent in 2016, three percent in 2017 and more than four percent in 2018. (TR 3386) The revenue class models, collectively, estimate retail sales that start around 115 million MWhs in 2015 and increase to 119 million MWhs in 2018. However, the NEL model shows estimates retail sales at approximately 114 million MWhs for the entire period 2015 to 2018. (TR 3386-3387)

Witness Morley argues that Witness Dismukes' criticism of the rate case forecast are meritless. Her first argument is that the declining sales forecast is not wrong. (TR 4957) She pointed to a question that had an error which was subsequently corrected in errata to delete the words "weather-normalized". (HE 713) Witness Morley also criticized the use of unadjusted, non-weather normalized sales as a yardstick for future sales (TR 4961); however, Witness Dismukes only used historic sales to identify a problem as it relates to historic trends. (TR 3374) He noted historic sales demonstrated that FPL was anticipating a contraction (decrease) of overall sales relative to its reported 2015 numbers, and that its overall sales numbers will not recover until 2019. (TR 3374) As discussed earlier, Witness Dismukes' analysis of the sales forecast revealed a problem with the rate case forecast, which created the need for additional investigation.

Witness Morley's second criticism of Witness Dismukes relates to his load forecast analysis. She attempted to confuse the point of his analysis. Witness Dismukes' analysis did not claim that the load factor remained constant, but rather that the load factor should remain consistent with historic trends. (TR 3385, 4963) In fact, Witness Dismukes in DED-5 examined FPL's historic averages and projections on a weather-normalized basis and it showed a declining load factor. (TR 3378) Witness Morley does not dispute that the load factor is declining (TR 4966), rather, she argued that the summer peak and NEL have not consistently moved in unison. (TR 4965) However, she conceded that in the short-term, the forecast growth in summer peak demands is expected to surpass that of NEL before they converge to a similar growth in 2020. (TR 4966) Although she attempted to explain the variation between summer peak and NEL as a result of conservation measures, she did not explain why that is expected to end in 2020. (TR 4966) Moreover, Witness Dismukes noted that on a weather-normalized basis, FPL's projections implied that its load factors, for each of the next three years (2016, 2017, and 2018) will be lower than any other reported since 2009 (over the past six years). Witness Morley also attempted to dismiss the fact that the no other Florida IOUs showed declining load factors in the near future, by claiming each IOU has unique circumstances. (TR 4967-4968) However, it is telling FPL is the only Florida IOU to show declining load factors and that those declining load factors simply happen to coincide during the projected test years in this rate case.

Finally, Witness Morley suggested that the discrepancy between FPL's sales models and its NEL model in this case should be ignored because the NEL model is superior. (TR 4970) However, this criticism does not explain why the sales models are in line with the 2015 TYSP NEL forecast, the Okeechobee NEL forecasts and historical trends. (TR 3375-3376) It is interesting to note that Witness Morley is forced into a position of implying that FPL's most recently approved NEL forecasts used in the 2015 TYSP and Okeechobee need determination are "clearly inferior alternative[s]." (TR 4971) Either that or she is deliberately attempting to confuse the Commission by suggesting that Witness Dismukes used the 2015 TYSP NEL forecast with the 2016 sales models forecasts with no reconciliation to the NEL in his recommendation – which is <u>not</u> his recommendation – to prove FPL's proposed rate case NEL is more accurate. (TR 4971) Witness Morley's criticism of Witness Dismukes' analysis failed to address the fundamental underlying problem which is FPL's proposed rate case NEL is significantly under forecasting sales for the test years and will only "recover" after the test years.

Due to this apparent manipulation of rate case NEL forecast, Witness Dismukes recommended using the 2015 TYSP NEL forecast which the Commission has already approved and relied upon. FPL's proposed rate case forecast significantly understates sales as compared to its previously used 2015 NEL forecast. The differences between FPL's proposed rate case forecast and the 2015 forecast go far beyond updating the forecasting model data, and have not been explained or justified. (TR 3388-3389)

Thus, FPL's proposed forecast of KWH by Rate Schedule and Revenue Class are based upon a faulty NEL energy sales forecast that the Commission should reject as unacceptable for ratemaking purposes. Instead, the Commission should adopt new forecasts of KWH by Rate Schedule and Revenue Class based upon the 2015 TYSP NEL forecast already approved by the Commission, which will increase test year weather-normalized retail delivered energy by 3,896 gigawatt-hours or 3.5 percent for 2017. This adjustment will decrease the Company's requested revenue requirement by $206.5 million in 2017. (TR 3369)

<u>ISSUE 29</u>: Are FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the 2018 projected test year appropriate, if applicable?

POSITION: *No. The Commission should reject FPL's NEL energy sales forecast as unacceptable for ratemaking purposes and instead should adopt the 2015 TYSP NEL forecast. The proposed adjustment will increase subsequent year weather-normalized retail delivered energy by 4,882 gigawatt-hours, or 4.3 percent. The adjustment will decrease the Company's revenue requirement by $259.5 million in 2018. (Dismukes)*

ARGUMENT:

For the reasons set forth in Issue 28, FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the 2018 projected test year are not appropriate. The Commission should reject FPL's NEL energy sales forecast as unacceptable for ratemaking purposes and instead adopt the 2015 TYSP NEL forecast which the Commission has already approved. The proposed adjustment will increase subsequent year weather-normalized retail delivered energy by 4,882 gigawatt-hours, or 4.3 percent for 2018. This adjustment will decrease the Company's requested revenue requirement by $259.5 million in 2018. (TR 3369)

<u>ISSUE 30</u>: Are FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the period June 2019 to May 2020, appropriate, if applicable?

POSITION: *No. FPL has not provided a separate forecast for the June 2019 to May 2020 period. However, for the reasons set forth in Issue 28 and 29, FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the 2017 and 2018 projected test years are not appropriate. The Commission should reject FPL's NEL energy sales forecasts as unacceptable for ratemaking purposes and instead should adopt the 2015 TYSP NEL forecast. (Dismukes)*

ARGUMENT:

FPL did not provide a separate forecast for the June 2019 to May 2020 period. However, for the reasons set forth in Issues 28 and 29, FPL's forecasts of Customers, KWH, and KW by Rate Schedule and Revenue Class, for the 2017 and 2018 projected test years are not appropriate. The Commission should reject FPL's NEL energy sales forecasts as unacceptable for ratemaking purposes and instead adopt the 2015 TYSP NEL forecast already approved by the Commission, which will increase test year weather-normalized retail delivered energy by 3,896 gigawatt-hours or 3.5 percent in 2017. Likewise, the proposed adjustment will increase subsequent year weather-normalized retail delivered energy by 4,882 gigawatt-hours, or 4.3 percent in 2018. This adjustment will decrease the Company's requested needed revenue requirement increase by $206.5 million in 2017 and $259.5 million in 2018. (TR 3369)

ISSUE 31: Are FPL's projected revenues from sales of electricity by rate class at present rates for the 2016 prior year and projected 2017 test year appropriate?

POSITION: *No. For the reasons set forth in Issue 28, FPL's projected revenues from sales of electricity by rate class at present rates for the 2016 prior year and projected 2017 test year ae not appropriate. Instead the Commission should adopt the 2015 TYSP NEL forecast, which will increase test year weather-normalized retail delivered energy by 3,896 gigawatt-hours or 3.5 percent for 2017. The adjustment will decrease the Company's revenue requirement by $206.5 million in 2017. (Dismukes)*

ARGUMENT:

For the reasons set forth in Issues 28, FPL's projected revenues from sales of electricity by rate class at present rates for the 2016 prior year and projected 2017 test year are not appropriate. Instead, the Commission should adopt the 2015 TYSP NEL forecast which it already approved, and which will increase test year weather-normalized retail delivered energy by 3,896 gigawatt-hours or 3.5 percent for 2017. This adjustment will decrease the Company's requested revenue requirement by $206.5 million in 2017. (TR 3369)

ISSUE 32: Are FPL's projected revenues from sales of electricity by rate class at present rates for the projected 2018 test year appropriate, if applicable?

POSITION: *No. For the reasons set forth in Issues 28 and 29, FPL's projected revenues from sales of electricity by rate class at present rates for the projected 2018 test year are not appropriate. The Commission should adopt the 2015 TYSP NEL forecast. The proposed adjustment will increase subsequent year weather-normalized retail delivered energy by 4,882 gigawatt-hours, or 4.3 percent for 2018. The adjustment will decrease the Company's revenue requirement by $259.5 million in 2018. (Dismukes)*

ARGUMENT:

For the reasons set forth in Issues 28 and 29, FPL's projected revenues from sales of electricity by rate class at present rates for the projected 2018 test year are not appropriate. The Commission should reject FPL's NEL energy sales forecasts as unacceptable for ratemaking purposes and instead should adopt the 2015 TYSP NEL forecast. The proposed adjustment will increase subsequent year weather-normalized retail delivered energy by 4,882 gigawatt-hours, or 4.3 percent for 2018. The adjustment will decrease the Company's revenue requirement by $259.5 million in 2018. (TR 3369)

<u>ISSUE 33</u>: What are the appropriate inflation, customer growth, and other trend factors for use in forecasting the 2017 test year budget?

POSITION: *For the reasons set forth in Issues 28, FPL's proposed rate case forecast significantly understates sales as compared to the previously used 2015 NEL forecast. The Commission should adopt the energy sales forecast included in FPL's 2015 TYSP. Further, FPL proposes to use an overstated inflation factor of 2.5% based on a single source. A more appropriate 2.06% inflation should be used which is based on weighting multiple sources for 2017. *

ARGUMENT:

For the reasons set forth in Issues 28, FPL's proposed rate case forecast significantly understates sales as compared to the previously used 2015 NEL forecast. The difference between FPL's proposed rate case forecast and the 2015 forecast go far beyond updating the forecasting model data, and have not been explained or justified. The Commission should adopt the energy sales forecast included in FPL's 2015 TYSP, which the Commission previously approved and relied upon. (TR 3369)

FPL also proposes to use an overstated inflation factor of 2.5% based on a single source. (TR 3396) Witness Dismukes testified that use of a sole source without any input from other economic forecasters who routinely assess and forecast inflationary pressures within the economy is less accurate. This is considered a very limited approach in developing an inflation factor forecast, as academic research has consistently shown that a survey of economic forecasts is more accurate than relying too heavily on a single forecast which may have intrinsic biases from the forecaster. (TR 3396)

Witness Dismukes further testified that, other than using Global Insight information, FPL did not use any additional research in developing its proposed inflation factor for this rate case. (TR 3397) The Company's claimed that its forecast of overall Consumer Price Index ("CPI") is consistent with inflation projections developed by other experts, including the Philadelphia Federal Reserve Banks Survey of Professional Forecasters and the National Association for Business Economics ("NABE"). (TR 3391, 3397) However, Witness Dismukes correctly pointed out the Philadelphia survey found an average estimate for Consumer Price Index for all urban consumers ("CPI-U") Inflation of 1.5% for 2016, and 2.1% for 2017 and the NABE found the median annual forecast of CPI-U was estimated to be 1.6% for 2016, and 2.3% for 2017. (TR 3391, 3398)

Witness Dismukes noted that FPL's analysis showed its proposed test year inflation measure of 2.5% differs from recent trends with no explanation for the rationale of those differences. The Company acknowledged that between 2010 and 2014, overall CPI increased at a compound annual rate of 2.1% a year. FPL also acknowledged that the overall CPI during this time was fairly steady, fluctuating between 3.1% and 1.5% a year through the 2010-2014 timeframe and was virtually flat in 2015 (increasing only 0.1% from 2014 price levels). (TR 3398-3399) FPL claimed that its inflation forecast is consistent with the consensus view that a moderately positive rate of inflation can be expected for the next few years. (TR 3399) However, Witness Dismukes testified that there are conceptual proposed rates of inflation over the next two years. (TR 3399) First, he noted that the Federal Open Market Committee ("FOMC") has targeted an annual inflation rate of 2.0% and will implement monetary policy to help maintain an inflation rate of 2.0% over the medium term. (TR 3399-3401) While Witness Dismukes acknowledged that it is not impossible for inflation to increase to a rate of 2.5%, he believed that it was unlikely that the FOMC would not engage in aggressive monetary policy to maintain the 2.0% inflation level. (TR 3401)

The average expectations of the Wall Street Journal survey of economists as of June 15, 2016, is that the CPI levels will reach 1.8% by the end of 2016 and then level off at 2.3% by the end of 2017. (TR 3403) And Witness Morley acknowledged the Wall Street Journal survey June 2016 average CPI forecast was 2.2% for 2017. At its March 16, 2016 meeting, the FOMC expected inflation to only reach 1.2% by the end of the year, increase to 1.9% by the end of 2017, and reach 2.0% in early 2018. (TR 3403)

Witness Dismukes recommended that the Commission adopt an inflation rate equal to a weighted average of the median result of the Wall Street Journal's June survey and the FOMC's official median projection for use in computing expected near-term inflation. He specifically recommended a weighted average that places a 60% weighting on the forecasts of the FOMC and a 40% weighting on the forecasts of other industry professionals. This results in a 2016 general price inflation of 1.44%, and a subsequent 2017 general price inflation of 2.06%.

Witness Morley attempted to justify FPL's use of an overstated inflation rate of 2.5%, based on a year-old June 2015 Wall Street Journal Survey which projected a 2.3% increase in the CPI-U by the end of 2016 and a 2.4% increase by the end of 2017. (TR 4979) She claimed that it was the most recent survey available at the time FPL's inflation factor was developed. (TR 4979) However, even the June 2015 Wall Street Journal survey demonstrated that a 2.5% CPI is overstated. Witness Morley also claimed that the core CPI (which excludes the volatile energy and food sectors) is increasing at an annual rate of 2.2%, up from an increase of 1.8% during 2015. (TR 4980) Yet, the 2.2% is another indication that FPL's 2.5% CPI-U is overstated, since historically the input cost inflation of electric utilities has been significantly lower than that seen in the economy as a whole. (TR 3404)

Based on the above, the Commission should use a weighted average that places a 60% weighting on the forecasts of the FOMC and a 40% weighting on the forecasts of other industry professionals, which results in a 2016 general price inflation of 1.44%, and a subsequent 2017 general price inflation of 2.06%. A more appropriate 2.06% inflation rate should be used which is based on weighting multiple sources for 2017. (TR 3403-3404)

<u>ISSUE 34</u>: What are the appropriate inflation, customer growth, and other trend factors for use in forecasting the 2018 test year budget, if applicable?

POSITION: *FPL's proposed rate case forecast significantly understates sales as compared to the previously used 2015 NEL forecast which go far beyond updating the forecasting model data and have not been explained or justified. The Commission should adopt the energy sales forecast included in FPL's 2015 TYSP. Further, FPL proposes to use an overstated inflation factor of 2.5% based on a single source. A more appropriate 2.06% inflation should be used which is based on weighting multiple sources. (Dismukes)*

ARGUMENT:

For the reasons set forth in Issues 28 and 29, FPL's proposed rate case forecast significantly understates sales as compared to the previously used 2015 NEL forecast. The difference between FPL's proposed rate case forecast and the 2015 forecast go far beyond updating the forecasting model data, and have not been explained or justified. The Commission should adopt the energy sales forecast included in FPL's 2015 TYSP, which was previously approved and relied upon by the Commission. (TR 3369) 0Further, for the reasons discussed in Issue 33, the Commission should use a weighted average that places a 60% weighting on the forecasts of the FOMC and a 40% weighting on the forecasts of other industry professionals, which this results in a 2016 general price inflation of 1.44%, and a subsequent 2017 general price inflation of 2.06%. A more appropriate 2.06% inflation should be used which is based on weighting multiple sources for 2017. (TR 3403-3404)

ISSUE 35: Are FPL's estimated operating and tax expenses, for the projected 2017 test year, sufficiently accurate for purposes of establishing rates?

POSITION: *No. See OPC's positions on Issues 89-120.*

ISSUE 36: Are FPL's estimated operating and tax expenses, for the projected 2018 subsequent year, sufficiently accurate for purposes of establishing rates, if applicable?

POSITION: *No. See OPC's positions on Issues 89-120.*

ISSUE 37: Are FPL's estimated Net Plant in Service and other rate base elements, for the projected 2017 test year, sufficiently accurate for purposes of establishing rates?

POSITION: *No. See OPC's positions on Issues 53-77.*

<u>ISSUE 38</u>: Are FPL's estimated Net Plant in Service and other rate base elements, for the projected 2018 subsequent year, sufficiently accurate for purpose of establishing rates, if applicable?

POSITION: *No. See OPC's positions on Issues 53-77.*

<u>QUALITY OF SERVICE</u>

<u>ISSUE 39</u>: Is the quality of the electric service provided by FPL adequate taking into consideration: a) the efficiency, sufficiency and adequacy of FPL's facilities provided and the services rendered; b) the cost of providing such services; c) the value of such service to the public; d) the ability of the utility to improve such service and facilities; e) energy conservation and the efficient use of alternative energy resources; and f) any other factors the Commission deems relevant.

POSITION: *FPL's quality of service is adequate for general ratemaking purposes. FPL's so-claimed "superior performance" results from investments already in base rates and its duty under the regulatory compact to provide excellent electric service. When considering the quality of electric service, this Commission should also take into consideration the fact that hypersaline water from FPL's Turkey Point Nuclear Units cooling canal system is infiltrating into the Biscayne Aquifer drinking water supply, and the potential liabilities may result. *

ARGUMENT:

FPL's quality of electric service is adequate for general ratemaking purposes; however, it is not superior. According to OPC witness Lawton, "FPL's management performance, like any other regulated utility, is always expected to be prudent in (1) seeking the lowest reasonable costs to consumers, while maintaining the highest reasonable level of reliability; (2) maintaining the lowest reasonable level of emissions from power plants; (3) maintaining the highest reasonable level of consumer service; (4) maintaining the highest level of efficiency and reliability in generating plants; and (5) seeking the lowest reasonable non-fuel O&M costs for consumers. If FPL's management has adequately satisfied those performance expectations on an historical basis, that was presumed because such prudent management behavior was certainly an expectation of the regulatory bargain. However, prudent management and historical success in keeping costs down, improving generation efficiency, and electric reliability are reasonable consumer expectations and do not form the basis for additional future profits." (TR 3608-09) Not only is this expectation true for past performance, but it is also true for future performance.

Satisfactory quality of electric service is required by the regulatory compact between the monopoly and its captive customer. (TR 3616); *see also* Section 366.03, Florida Statutes. When granted a monopoly franchise by the state, monopolies have a duty to provide superior performance in exchange for cost recovery plus an opportunity to earn a fair and reasonable return or profit commensurate with profits earned from similar risk ventures. Enhanced customer value includes providing service at the lowest rates consistent with good service. FPL has the duty and obligation to provide electric service at the lowest rates with good service. (TR 3616) In other words, efforts to keep rates as low as reasonably possible are part and parcel FPL's obligation to serve. (TR 3609)

There is no dispute that FPL management does a good job in terms of service quality and reliability. However, what FPL characterizes as superior customer value is the result of investments and expenditures paid for by customers, and which are already being returned to FPL's shareholders through existing rates. (TR 3611) OPC witness Lawton addresses and refutes FPL's "superior" performance claims as it related to low bills, high reliability, low emissions, high customer satisfaction, high fossil fleet reliability, low heat rates, and low non-fuel O&M. (TR 3611-16)

As it relates to the cost of providing electric service and the value of such service to the public (subpart (b) and (c) of the issue), while FPL may currently have the lowest overall bill in Florida, FPL's base rates for a 1,000 kWh bill have increased 44% since 2006. (TR 3612) Moreover, enjoying the lowest rates in the state is also a function of the type and vintage of FPL's generating equipment, customer mix, density of development, historically low natural gas prices, and other factors, such as economies of scale, that are not measurements of superior management performance. Reliability is improving; however, customers have been and will continue to pay for the costs of these improvements. (TR 3612-13) The bottom line is that customers have received what they paid for – a modernized, storm hardened, and reliable transmission and distribution grid. (TR 3613) Witness Lawton noted that, while overall bills may be lower today relative to 2006, that is in large measure because the market cost of natural gas has declined dramatically from earlier periods. (TR 3612) FPL does not have any control or influence over the market cost of gas, thus, lower rates resulting from lower natural gas prices should not be factored into the quality of service analysis. (TR 3612) As to claimed customer benefits related to low emissions, high fossil fuel fleet reliability, low heat rates, and low non-fuel O&M, these are the direct result of FPL's transformation and modernization of its generating fleet to more efficient gas units and continued on-going capital expenditures; and such improvements or benefits are expected from prudent decisions. (TR 3614)

As to energy conservation and the efficient use of alternative energy resources (subpart (e) of the issues), FPL's demand-side management energy efficiency goals were significantly reduced during the last goal setting proceeding, and customer solar rebates were canceled.[2]

When considering whether FPL's quality of the electric service provided is adequate, the Commission should also consider other relevant factors (subpart (f) of the issue), such as the environmental impacts from FPL's operations. Currently, FPL is subject to a Florida Department of Environmental Protection *Consent Order* for a discharge permit violation related to hypersaline water emanating from its Turkey Point Nuclear Units cooling canal system. (TR 3617-18) FPL will spend tens of millions of dollars, perhaps hundreds of millions, attempting to resolve the permit violation and prevent hypersaline water from infiltrating further into the Biscayne Aquifer drinking water supply. It is unknown whether FPL's plan will even work. FPL expects to spend approximately $50 million in the first year alone attempting to resolve this permit violation. (TR 3618). FPL expects its customers to be responsible for these costs. These are serious environmental issues with no easy solutions. In addition to the question of who pays to prevent the hypersaline water from infiltrating further into the Biscayne Aquifer (FPL or its customers), there may be years of protracted litigation in state and federal courts, as well as cost recovery proceedings before the Commission, before hypersaline water issue can be resolved.

For all the reasons discussed herein, FPL's quality of service should be deemed adequate for general ratemaking purposes.

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[2] Order No. PSC-14-0696-FOF-EU, issued December 16, 2014, in Docket No. 130199-EI.

DEPRECIATION STUDY

ISSUE 41: What is the appropriate depreciation study date?

POSITION: *FPL has the burden to show that the date for its depreciation study is reasonable and appropriate.*

ARGUMENT:

See discussion on Issue 5.

ISSUE 42: If the appropriate depreciation study date is not December 31, 2017, what action should the Commission take?

POSITION: *FPL has the burden to show that the date for its depreciation study is reasonable and appropriate. OPC agrees with SFHHA.*

ISSUE 43: Should accounts 343 and 364 be separated into subaccounts and different depreciation rates be set for the subaccounts using separate parameters? If so, how should the accumulated depreciation reserves be allocated and what parameters should be applied to each subaccount?

POSITION: *No. The Commission should retain the existing interim retirement ratios established by the Commission in the prior case, with one exception. That one exception reinstates a single interim retirement rate for Account 343 – Prime Movers

For Account 364, FPL's first time proposal to separate poles between wood and concrete into two subaccounts should also be denied. The Company's proposal of using a 40R2 life-curve results in an artificially short ASL for wood poles. *

ARGUMENT:

The Commission should retain the existing interim retirement ratios established by the Commission in the prior case, with one exception. That one exception reinstates a single interim retirement rate for Account 343 – Prime Movers. By retaining the interim retirement ratio approach and again denying the use of truncated interim retirement Iowa survivor curves, the Commission eliminates one of FPL's more unreasonable aggressive depreciation tools from consideration. Retention of the existing interim retirement ratios, after reversing the separation of Account 343, on a standalone basis would result in a $165.6 million reduction to depreciation expense. Citizens agree with Witness Kollen (TR 4059-4063) on this issue.

For Account 364, FPL's first time proposal to separate poles between wood and concrete into two subaccounts should also be denied. The Company's proposal of using a 40R2 life-curve results in an artificially short ASL for wood poles

<u>ISSUE 44</u>: What are the appropriate depreciation parameters (e.g., service lives, remaining lives, net salvage percentages, and reserve percentages) and resulting depreciation rates for the accounts and subaccounts related to each production unit?

POSITION: *FPL's 40-year life span is part of an aggressive and continued effort to understate the realistic life spans for its combined cycle generating facilities based on the current understanding and expectations of their life characteristics. The Commission should challenge the judgment and conclusions of FPL's witness Allis and the lives he recommends, and instead consider longer lives of up to 45 years*

ARGUMENT:

The Commission should be concerned that FPL is understating the realistic life spans of its combined cycle (CC) plants at a time when it is on a massive conversion of its fossil fleet to natural gas-fired combined cycle generation. FPL's gross investment in CC plant in service in the test year is $10.8 billion. (HE 113, p. 7). This is a very significant portion of the overall depreciable plant amounting to $46.0 billion. (TR 1863). Utilities have the burden of proof to demonstrate the reasonableness and prudence of all costs they seek to recover. <u>Florida Power Corp v. Cresse,</u> 43 So.2d 1187, 1191 (Fla. 1982) (Finding that the burden of proof in a Commission proceeding is always on a utility seeking a rate change). The witness FPL offers as its regulatory expert with 35 years' experience emphatically agreed that he strongly believes the utility shoulders the burden of proof to justify the costs they seek to recover from customers. (TR 5822-5823).

In the face of a rate increase request cumulatively totaling $4.4 billion over the next four years, the Commission must hold FPL to that burden. Merely asking for cost recovery does not meet that burden. Neither does the absence of Intervenor testimony grease the skids for FPL's request. The depreciation area is no exception to this concept of burden of proof, especially given the level of subjectivity inherent in the determination of depreciation parameters. In the face of this single $47 million increase in depreciation expense, FPL fails to provide any empirical evidence rebutting the assertion that 45 years was a reasonable and appropriate life span for FPL's combined cycle units. Rather, FPL merely offers vague generalizations. In response to OPC discovery that asked:

> Depreciation Other Production Life. Please state whether a 5-year increase in life span for combined cycle generation is a reasonable and appropriate life span as compared to the proposed life spans. To the extent the response is other than fully affirmative, provide all support and justification for a contrary position. The response should identify and justify the criteria relied upon for the position taken, and to the extent judgment is relied upon for the response include the specific input values or information that formed and supports the results of the claimed judgment process.

(HE 472, Resp. to OPC Int. No. 333) In its response, FPL included the following general and conclusory statements:

1. "First, a 45 year life would be long when compared to life span estimates of other utilities."
2. "FPL's operating environment is still subject to corrosion at a higher level than in drier climates with less salt in the air."
3. "FPL's load profile also results in more cycling of the units, which increases the wear and tear on components (and can impact the operating costs of the plants as they plants [sic])."
4. "Finally, as combined cycle plants age, the costs to maintain and continue to operate the facilities increase."

On the surface, these statements may be directionally, though minimally, supportive of FPL's position. However, when one asks "compared to what and where," it is clear that there is nothing but bare rhetoric here and the support reveals itself as vague and disconnected – and unhelpful. No facts; no details; no locations, no plant comparisons – just words with no quantification. Especially when it is considered in the context of the question asked on a $47 million issue, the superficiality of the support is startling. No input values or comparative information is provided in support of the judgment that was behind the suggested 40-year life span. This is not what is meant by meeting a burden of proof. FPL acknowledged that the 30-year life span it convinced the Commission to adopt in the 2009 study is now known to be wrong.

(TR 1840; HE 113, pp. 666-678). Even the experience with the old Putnam combined cycle units that were retired after 36 and 37 years exceeded the aggressively short 30-year estimate FPL convinced the Commission to accept in 2009. (HE 472, Resp. to OPC Int. No. 333).

Selection of a 40-year point on the continuum is no less arbitrary, especially when the vagueness of the support and lack of experience in FPL's depreciation witness is thrown into the mix. Witness Allis may possess a mathematical education background, analytical skill and an aptitude for software development, but these admirable qualities and his adroitness on the stand do not substitute for cumulative experience in the field that adequately supports the judgment needed to estimate life spans of combined cycle plants. When boiled to its essence, Mr. Allis' experience consists of a handful of cases with only a half dozen or so full opportunities to present testimony to a regulatory commission on a regulated electric utilities' depreciation studies. In only three of these cases did he testify by himself and not as a member of a panel in full support of a depreciation study he performed. (TR 1901-1907). His ability to personally observe and compare and contrast combined cycle plants from across the United States and Canada was limited to a concentration of repeat assignments for utilities located in California, Pennsylvania and Missouri by a non-engineer. (TR 1902-1907; HE 114). He only began testifying in support of Comprehensive Depreciation Studies in 2013. (TR 1905; HE 114). Notably, FPL did not put a company engineer on as a witness to provide empirical details to support life span estimates for such a critical component of their production fleet. For a single issue that means a $47 million annual revenue requirement to FPL's customers, the Commission should give little – if any – deferential weight to FPL and Gannet-Fleming's offer of its judgment and experience in support of a 40-year versus a 45-year life span for combined cycle generating units. The OPC asks the Commission to consider a life span beyond the Company's proposed 40-year parameter, given all of the facts and circumstances of this issue.

<u>ISSUE 45</u>: What are the appropriate depreciation parameters (e.g., service lives, remaining lives, and net salvage percentages) and resulting depreciation rates for each transmission, distribution, and general plant account, and subaccounts, if any?

POSITION: * The record in this proceeding does not support significant modification to the expenses and parameters and resulting theoretical reserve imbalance submitted by FPL based on its study and expert testimony, except possibly for the adjustments proposed by SFHHA witness Kollen and FEA Witness Andrews.[3]* (TR4059-4066; 3953-3970)

ARGUMENT:

The record in this proceeding does not support significant modification to the expenses and parameters and resulting theoretical reserve imbalance submitted by FPL based on its study and expert testimony, except possibly for the adjustments proposed by SFHHA's witness Kollen and FEA's witness Andrews.

<u>ISSUE 46</u>: Based on the application of the depreciation parameters and resulting depreciation rates that the Commission deems appropriate, and a comparison of the theoretical reserves to the book reserves, what are the resulting imbalances?

POSITION: *The record in this proceeding does not support significant modification to the expenses and parameters and resulting theoretical reserve imbalance submitted by FPL based on its study and expert testimony, except possibly for the adjustments proposed by SFHHA's witness Kollen and FEA's witness Andrews[4].* (TR4059-4066; 3953-3970)

ARGUMENT:

The record in this proceeding does not support significant modification to the expenses and parameters and resulting theoretical reserve imbalance submitted by FPL based on its study and expert testimony, except possibly for the adjustments proposed by SFHHA's witness Kollen and FEA's witness Andrews.

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[3] FEA Witness Andrews, in response to a question from FPL's attorney stated that application of his proposed lives to the three accounts to which he testified, would increase the TRI imbalance by $140 million. TR 3980. However, he did not specifically state whether his calculation was based on year-end 2016 or 2017 plant balances. He did not provide calculations or workpapers to support his statement.

[4] See footnote 3.

<u>ISSUE 47</u>: If the Commission accepts FPL's depreciation study for purposes of establishing its proposed depreciation rates and related expense, what adjustments, if any, are necessary?

POSITION: * Adjustments to accumulated depreciation are addressed in Issues 58 and 60, and depreciation expense in Issue 114.*

<u>ISSUE 48</u>: What, if any, corrective reserve measures should be taken with respect to the imbalances identified in Issue 46?

POSITION: * None are warranted based on the study that FPL filed and did not change in its direct case[5].*

ARGUMENT:

If the Commission makes adjustments to depreciation parameters and resulting expense levels based on competent substantial evidence, then the resulting impact on any theoretical reserve imbalance should be addressed consistent with Commission precedent and policy. The creation of a reserve imbalance is not an end unto itself, but is rather a fallout of sound and principled depreciation policy that is based on facts demonstrated on the record in accord with the appropriate burden of proof. In this case, the only evidence FPL put on in its direct case was that, depending upon whether the plant balance is year-end 2016 or 2017, a theoretical reserve balance ranges from a negative ($99 million) to a positive $80 million. (TR 1791-1792, HE 113, 331). FPL witnesses Allis and Ferguson characterized this amount as a "minor difference," "relatively small" and "quite small." (TR 1787-1788, 1863-1864; HE 427) (FPL resp. to Staff Int. 382). There is no competent substantial evidence in the record of this case that supports the existence of a material theoretical reserve imbalance ("TRI") or, to the extent one were to exist, that supports the appropriate disposition of a positive TRI.

In FPL's 2009 rate case, the Commission determined that a positive TRI of 15 times (1,208/80 = 15.2) the size of the one that exists in this case needed to be corrected. In that case,

[5] The Citizens incorporate by reference the argument advanced in its Motion to Dismiss FPL's Amended Request for Creation of a Reserve Amount Amortization Mechanism or Alternatively, Motion for Directed Final Decision That FPL Has Failed to Produce Any Evidence in Support of its Request, filed on August 29th.

the Commission engaged in an extensive analysis of the possible customer benefitting dispositions and the financial impact of what was an agreed surplus. In this case, based on the depreciation study that the company filed, there is effectively no TRI and, as such, no corrective measures need to be taken. Further, there is no evidence that would support any finding in support of any disposition other than remaining life or a mechanism that is developed in the next depreciation study. There is no record basis to consider disposition her of excesses, if any, amortization from the 2009 and 2012 cases. See position and argument on Issue114.

<u>ISSUE 49</u>: What should be the implementation date for revised depreciation rates, capital recovery schedules, and amortization schedules?

POSITION: *The new depreciation rates should be implemented in January 2017.*

<u>ISSUE 50</u>: Should FPL's currently approved annual dismantlement accrual be revised?

POSITION: *FPL has the burden to show that its annual dismantlement accrual is reasonable and appropriate. The OPC agrees with SFHHA.*

<u>ISSUE 51</u>: What, if any, corrective dismantlement reserve measures should be approved?

POSITION: *FPL has the burden to show that its annual dismantlement accrual corrective dismantlement reserve measures are reasonable and appropriate. The OPC agrees with SFHHA *

<u>ISSUE 52</u>: What is the appropriate annual accrual and reserve for dismantlement

A. For the 2017 projected test year?

POSITION: *FPL has the burden to show that its annual dismantlement accrual and reserve for dismantlement are reasonable and appropriate for the 2017 test year. The OPC agrees with SFHHA *

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden to show that its annual dismantlement accrual and reserve for dismantlement are reasonable and appropriate for the 2018 test year. The OPC agrees with SFHHA*

RATE BASE

ISSUE 53: Should the revenue requirement associated with West County Energy Center Unit 3 currently collected through the Capacity Cost Recovery Clause be included in base rates?

POSITION: *As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.*

ISSUE 55: Has FPL made the appropriate adjustments to remove all non-utility activities from Plant in Service, Accumulated Depreciation and Working Capital

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that only utility-related costs are properly recorded on its books and records and reflected in the 2017 MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

OPC: *FPL has the burden of demonstrating that only utility-related costs are properly recorded on its books and records and reflected in the 2018 MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 56: What is the appropriate amount of Plant in Service for FPL's Large Scale Solar Projects?

POSITION: *FPL has the burden of demonstrating that its Large Scale Solar Projects costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 57: Is FPL's replacement of its peaking units reasonable and prudent?

POSITION: *FPL has the burden of demonstrating that its replacement of its peaking units are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 58: If adjustments are made to FPL's proposed depreciation and dismantling expenses, what is the impact on rate base

A. For the 2017 projected test year?

POSITION: *An adjustment to increase rate base should be made to reflect OPC witness Schultz' adjustment of $.475 million (total and jurisdictional) for the 2017 storm hardening plant.*

ARGUMENT:

An adjustment to increase rate base should be made to reflect OPC's witness Schultz' adjustment of $.475 million (total and jurisdictional) for the 2017 storm hardening plant. (HE 715)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *An adjustment to increase rate base should be made to reflect OPC's witness Schultz' adjustment of $.683 million (total and jurisdictional) for the 2018 storm hardening plant in Issue 59.*

ARGUMENT:

An adjustment to increase rate base should be made to reflect OPC's witness Schultz' adjustment of $.683 million (total and jurisdictional) for the 2018 storm hardening plant in Issue 59. (HE 715)

<u>ISSUE 59</u>: What is the appropriate level of Plant in Service (Fallout Issue)

A. For the 2017 projected test year?

POSITION: *To reflect the reduction to plant recommended by OPC witness Schultz for storm hardening, 2017 plant should be reduced by $31.546 million on a total and jurisdictional basis.*

ARGUMENT:

In accordance with one of the overriding themes of this case, FPL has over projected its rate base as it applies to capital to be deployed to harden its network. As acknowledged by its regulatory expert and former Commission chairman and consumer advocate, Terry Deason, FPL has the burden to demonstrate that its costs are reasonable and prudent before customers should be required to pay for them. (TR 5823). OPC's witness Schultz testified that FPL's projected two-year capital spending plan for hardening approximates the four-year spend that the company actually incurred in 2012 – 2015. (TR 3496) He recommends a more achievable and reasonable level that involves a reduction of $31.546 million to the projected test year 2017 and $45.335 million to the subsequent projected test year 2018. (TR 3497; HE 188).

Mr. Schultz acknowledges that FPL has made significant strides in hardening the system and has expended more than planned during the years 2012 through 2015; however, he testified that the projected increase in spending for 2016 through 2018 is overly optimistic. The cumulative capital spending in this area for the four years 2012 through 2015 that coincided with FPL's Stipulation and base rate freeze totaled $1.001 billion. At the same time, the proposed spending for just the two years 2016 and 2017 is projected to be $1.075 billion. That is $74 million more spending in half the time. The projected total storm hardening capital spending for the three year period of 2016 through 2018 of $1.943 billion is almost double the spending for the previous four years. At the time Witness Schultz filed his testimony, the year-to-date (May 2016) amount totaled

$186 million, which when annualized, totals $446 million. That $446 million is $25 million less than the 2016 forecasted capital spending of $471 million. Witness Schulz also observed with the storm season approaching that completing any makeup of the underspent amount in the second half of the year would be difficult. (TR 3497). Mr. Schultz, who has testified in over 600 cases (TR 3449), noted that acceleration in spending is significant and that he did not share the Company's optimism for its capital storm spending levels. Based on the ratio of actual under-spending through May 2016 versus the budget, Witness Shultz based his adjustment on application of a factor of 5.21% to the FPL's 2017 and 2018 forecasted storm hardening capital. (TR 3497).

FPL's witness Miranda acknowledged that 2016 capital spending is behind budget. (TR 2678) His only direct response was one of relative hyperbole that he is "extremely confident that FPL can continue to execute" the capital expenditure plan for this area. (TR 2678) Witness Miranda, who testified out of order in rebuttal before Mr. Schultz in order to attend to the advent of FPL's potential first hurricane (TR 2664), further acknowledged that the ability to catch up in the second half of 2016 could be impacted by hurricane season. Nevertheless, without further explication, he asserts that that should not be a basis for disallowance. (TR 2679) This unsupported claim and his "extreme confidence" do not – even when taken together – come close to meeting FPL's burden to demonstrate that its own projected future spending levels will be accurate. This is especially the case in light of the admitted budget post-test year forecasting misses (TR 1470-1474; 4625-4638; 2720; 2734, 1954-1956; HE 673, 736) and its forecasting gaps elsewhere.

Perhaps most importantly, FPL has demonstrated in this case that spending after the conclusion of a rate case, including capital spending, has led to under runs in the CWIP area. (TR 1637-1645; HE 556). Far from meeting its burden to show that it should recover from customers these excessive estimated costs, FPL should only be allowed to recover the reasonable levels of storm hardening capital expenditures. Notably, Witness Miranda does not represent to the Commission that any reduction in the estimated plant expenditures in the amounts Mr. Shultz recommends in such a critical area as storm hardening would impact FPL's ability to harden its system. His silence is another indicator that Mr. Schultz has identified an unnecessary level of spending. Mr. Schultz presents a reasonable estimation of the adjustment of $31.546 million for 2017 as explained in his testimony and exhibit. (TR 3496-3498, 3510; HE 188).

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *To reflect the reduction to plant recommended by OPC witness Schultz for storm hardening, 2018 plant should be reduced by $45.335 million on a total and jurisdictional basis.*

ARGUMENT:

See argument for year 2017. Projected plant for the subsequent projected test year 2018 should be reduced by $45.335 million, reflecting the projected 5.21% lower 2018 capital expenditure for storm hardening based on the likely 2016 under-spend trend. (TR 3497; HE 188)

<u>ISSUE 60</u>: What is the appropriate level of Accumulated Depreciation (Fallout Issue)

A. For the 2017 projected test year?

POSITION: * An adjustment to increase rate base should be made to reflect OPC witness Schultz' adjustment of $.475 million ($.475 million jurisdictional) for the 2017 storm hardening plant.*

ARGUMENT:

This is essentially a fallout issue. The OPC supports the recognition of a lower 2017 accumulated depreciation balance, based on the adjustment to reduce over-projected capital expenditures in 2016 and 2017. For 2017, accumulated depreciation should be $.475 million. (Total and jurisdictional). (TR 3497-3498, 3528; HE715)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: * An additional adjustment to increase rate base should be made to reflect OPC witness Schultz' adjustment of $.683 million ($.683 million jurisdictional) for the 2018 storm hardening plant*

ARGUMENT:

This is essentially a fallout issue. The OPC supports the recognition of a lower 2018 accumulated depreciation balance, based on the adjustment to reduce over-projected capital expenditures in 2016 and 2017. For 2018, accumulated depreciation should be $.683 million. (Total and jurisdictional). (TR 3497-3498, 3528; HE 715)

<u>ISSUE 61</u>: Are FPL's proposed adjustments to move certain CWIP projects from base rates to the Environmental Cost Recovery Clause appropriate?

POSITION: *No. FPL's proposed adjustments to move certain CWIP projects from base rates to the ECRC should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.*

ARGUMENT:

FPL's proposed adjustments to move certain CWIP projects from base rates to the ECRC should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.

<u>ISSUE 62</u>: Are FPL's proposed adjustments to move certain CWIP projects from base rates to the Energy Conservation Cost Recovery Clause appropriate?

POSITION: *No. FPL's proposed adjustments to move certain CWIP projects from base rates to the ECCR should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.*

ARGUMENT:

FPL's proposed adjustments to move certain CWIP projects from base rates to the ECCR should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.

<u>ISSUE 63</u>: Is the company's proposed adjustment to remove Fukushima-related costs from the rate base and recover all Fukushima-related capital costs in the Capacity Cost Recovery Clause appropriate?

POSITION: *No. FPL's proposed adjustments to move certain CWIP projects from base rates to the CCRC should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.*

ARGUMENT:

FPL's proposed adjustments to move certain CWIP projects from base rates to the CCRC should be denied. As a general matter, and absent any countervailing consideration that would be to the detriment of customers, OPC favors placing capital items in rate base rather than in cost recovery clauses.

ISSUE 64: What is the appropriate level of Construction Work in Progress to be included in rate base

A. For the 2017 projected test year?

POSITION: *CWIP should not be afforded rate base treatment. CWIP, by its very nature, is plant that is not completed and is not providing service to customers. More specifically, and in reference to this proceeding, CWIP is not used or useful in delivering electricity to FPL's customers. Rate base recovery of CWIP should be limited to extraordinary circumstances and removal of CWIP from FPL's rate base will not materially impact FPL's earnings or financial indicators.*

ARGUMENT:

OPC's witness Smith testified that as a general regulatory principle, CWIP should be excluded from rate base and from costs being charged to customers until such time as it is providing service to those customers. CWIP, by its very nature, is plant that is not completed and is not providing service to customers, nor is it used or useful in delivering electricity to FPL's customers. Some jurisdictions exclude CWIP from rate base, requiring that assets be classified as used and useful in serving customers prior to earning a return on those assets being recovered from ratepayers. (TR 3724). While Mr. Smith stated that the FPSC has allowed the inclusion of non-interest-bearing CWIP projects for electric utilities in rate base, he did not made a reduction to CWIP in rate base. The fact that the removal has not been reflected in OPC's revenue requirement calculations in this case should not be interpreted to mean that OPC's position on this issue has changed, or that OPC will not pursue this important policy issue in this rate case or future proceedings. (TR 3724-3725). However, OPC notes that the Utility has a history of overstating the CWIP in rate case filings from the amounts actually incurred after the conclusion of each of the last several rate cases. (HE 407, Bates 1230-1236). According to FPL's witness Barrett, the Utility over projected CWIP in its prior rate cases. In 2009, the variance was 14.73% (TR1641), in 2010 it was 46.36% (TR1642), in 2011 it was 53.52% (TR 1644) and in 2012, the variance was 26.47% (TR 1645). The OPC supports the Commission adjusting FPL's gross balance of projected test year CWIP based on the consistent post-rate case under runs versus the budget used for rate-setting. (TR 2582-2591; 3464-3465; 3492; 3499; HE 556). At a minimum, the Commission should make a corresponding reduction to the projected amounts of CWIP based on the ratio of projected to actual.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *CWIP should not be afforded rate base treatment. CWIP, by its very nature, is plant that is not completed and is not providing service to customers. More specifically, and in reference to this proceeding, CWIP is not used or useful in delivering electricity to FPL's customers. Rate base recovery of CWIP should be limited to extraordinary circumstances and removal of CWIP from FPL's rate base will not materially impact FPL's earnings or financial indicators.*

ARGUMENT: See OPC's argument in Issue 64-A above.

<u>ISSUE 65</u>: Are FPL's proposed reserves for Nuclear End of Life Material and Supplies and Last Core Nuclear Fuel appropriate

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed reserves for Nuclear End of Life Material and Supplies and Last Core Nuclear Fuel are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed reserves for Nuclear End of Life Material and Supplies and Last Core Nuclear Fuel are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs*.

<u>ISSUE 66</u>: What is the appropriate level of Nuclear Fuel (NFIP, Nuclear Fuel Assemblies in Reactor, Spent Nuclear Fuel less Accumulated Provision for Amortization of Nuclear Fuel Assemblies, End of Life Materials and Supplies, Nuclear Fuel Last Core)

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level of Nuclear Fuel (NFIP, Nuclear Fuel Assemblies in Reactor, Spent Nuclear Fuel less Accumulated Provision for Amortization of Nuclear Fuel Assemblies, End of Life Materials and Supplies, Nuclear Fuel Last Core) are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level of Nuclear Fuel (NFIP, Nuclear Fuel Assemblies in Reactor, Spent Nuclear Fuel less Accumulated Provision for Amortization of Nuclear Fuel Assemblies, End of Life Materials and Supplies, Nuclear Fuel Last Core) are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs.*

<u>ISSUE 67</u>: What is the appropriate level of Property Held for Future Use

A. For the 2017 projected test year?

POSITION: * FPL has made no showing why the PHFFU projects that have been in rate base for more than 10 years, and some more than 40 years, and are not expected to provide service more than 10 years after the test year, are reasonably needed to provide reliable service to existing and future customers. Customers should not be required to continue to provide FPL with a rate base return, including shareholder profits, on these projects when FPL has failed to show why these properties are

> needed or why a 40- to 50-year planning horizon is reasonable for identifying assets to be included in rate base. Sites with a projected in-service date of 2026 or later (more than ten years beyond the test year), in the PHFFU, should be removed from rate base. As such, PHFFU for the 2017 test year should be reduced by $14.681 million total ($14.228 million jurisdictional).*

ARGUMENT:

OPC Witness Smith reviewed the details associated with the Company's requested level of Plant Held for Future Use ("PHFFU"). Witness Smith contends that several items should be removed and not included in rate base at this time. (TR 3720) Ratepayers should not be required to pay a return to FPL's shareholders for the costs of sites that have an expected in-service date that is beyond the 10-year planning horizon because it is not used and useful to current customers and will not be used within a reasonable timeframe in the future. (TR 3721) Witness Smith noted that Section 366.06, F.S., provides:

> [t]he commission shall investigate and determine the actual legitimate costs of the property of each utility, <u>actually used and useful in the public service</u>, and shall keep a current record of the net investment of each public utility company in such property which value, as determined by the commission, shall be used for ratemaking purposes and shall be the money honestly and prudently invested by the public utility company in such property <u>used and useful in serving the public</u>, . . . (Emphasis added)

FPL Witness Deason alleged that an electric plant is held to a higher standard for inclusion in PHFFU because of the USOA's requirement that there be a definite plant for the land's future use. (TR 5770) Yet, he then testified that the USOA recognizes that land and land rights may need to be acquired for possible future use. Thus, he concludes the USOA does not prescribe that the land and land rights have a definite future use in order to be treated as PHFFU. (TR 5770) He cited Order No. 5278, issued November 30, 1971, in Docket No. 70532-EU, for the Commission's policy change for inclusion of PHFFU in rate base. Witness Deason testified the original policy was that –there had to be a definite plan for the use of the land acquired, and that the use of the land must be imminent. Witness Deason then argues that this policy changed to: as long as the land acquisition is considered a responsible and prudent investment and it appears that it will be used for utility purposes in the reasonably near future in light of prevailing conditions, the land can be included in PHFFU in rate base. (TR 5771) Witness Deason further claims that the 10 year horizon is arbitrary and contrary to Commission policy and good regulatory policy. (TR 5772) He arbitrarily changes the standard to suggest you consider what amount of PHFFU is reasonably needed to cost-effectively provide reliable service to existing and future customers (TR 5773), but then wants the Commission to ignore the requirement that the property must be used for utility purposes in the reasonably near future, in light of prevailing conditions.

Witness Deason's assertion that Witness Smith is employing a rigid 10-year criteria ignores the fact that an examination of the individual properties in question reveals these properties have been in rate base for many years prior to the test year and will not be used for utility purposes for an additional ten years beyond this rate case. (HE 190) The properties identified by Witness Smith in Hearing Exhibit 190 have been on the books for at least 5 years and will not be placed into utility service for at least 10 more years. Although FPL Witness Miranda offered congestion and future needs as justification for keeping these properties in PHFFU (TR 2769-2770), this is an issue of fairness to ratepayers and who should pay to hold on to property for decades. Witness Smith testified FPL has made no showing why the projects that have been in rate base for more than 10, and some more than 40 years, and which are not expected to provide service for at least another 10 years after this rate case is concluded, are reasonably needed to provide reliable service to existing and future customers. (TR 3722) As Witness Smith testified, customers should not be required to continue to provide FPL with a rate base return, including shareholder profits, on these properties when FPL has failed to meet it burden to show why these properties were needed. Moreover, FPL has failed to explain why a 40 to 50-year planning horizon is reasonable for identifying assets to be included in rate base as used and useful plant. (TR 3722)

B. If applicable, for the 2018 subsequent projected test year?

POSITION *FPL has made no showing why the PHFFU projects that have been in rate base for more than 10 years, and some for more than 40 years, which are not expected to provide service for more than 10 years after the test year, are reasonably needed to provide reliable service to existing and future customers. Customers should not be required to continue to provide FPL with a rate base return, including shareholder profits, on these projects when FPL has failed to show why these properties were needed or why a 40 to 50-year planning horizon is reasonable for identifying assets to be included in rate base as used and useful plant. For the 2018 future test year, the jurisdictional adjustment decreases average 2018 jurisdictional rate base by $14.235 million.*

ARGUMENT:

See argument to Issue 67A.

<u>ISSUE 68</u>: What is the appropriate level of fossil fuel inventories

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level of fossil fuel inventories are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level of fossil fuel inventories are reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 69</u>: Should the unamortized balance of Rate Case Expense be included in Working Capital and, if so, what is the appropriate amount to include

A. For the 2017 projected test year?

POSITION: *The Commission should follow its long-standing policy in electric cases of not allowing inclusion of the unamortized rate case expense in rate base. The Commission found it would be unfair for customers to pay a return on the costs incurred by the Company in this case when these are being used to increase customer rates. Working capital should be reduced by the full amount of the unamortized balance of rate case expense of $4.309 million.*

ARGUMENT:

The Commission should adhere to its long-standing policy in electric rate cases of not allowing the inclusion of unamortized rate case expense in rate base. (TR 3730-3732) In Order No. PSC-10-0131-FOF-EI, issued March 5, 2010, in Dockets Nos. 090079-EI, 090144-EI, and 090145-EI, in the Progress Energy Florida, Inc. (Progress) base rate case, this Commission reaffirmed its policy of disallowing the unamortized rate case expense in rate base. The Commission stated:

> We have a long-standing policy in electric and gas rate cases of excluding unamortized rate case expense from working capital, as demonstrated in a number of prior cases. The rationale for this position was that ratepayers and shareholders should share the cost of a rate case; i.e., the cost of the rate case would be included in the O&M expenses, but the unamortized portion would be removed from working capital. It espouses the belief that customers should not be required to pay a return on funds expended to increase their rates.
>
> While this is the approach that has been used in electric and gas cases, water and wastewater cases have included unamortized rate case expense in working capital. The difference stems from a statutory requirement that water and wastewater rates be reduced at the end of the amortization period (Section 367.0816, F.S.). While unamortized rate case expense is not allowed to earn a return in working capital for electric and gas companies, it is offset by the fact that rates are not reduced after the amortization period ends.
>
> We agree with the long-standing policy that the cost of the rate case should be shared, and therefore find that the unamortized rate case expense amount of $2,787,000 shall be removed from working capital. (Order No. PSC-10-0131-FOF-EI at p. 71-72, TR 3730, footnote omitted)

Witness Smith listed numerous additional Commission Orders which support this policy for electric and gas cases: Order 23573, issued October 3, 1990, in Docket No. 891345-E1, In re: Application of Gulf Power Company for a rate increase; Order No. PSC-09-0283-FOF-RI, issued April 30, 2009, in Docket No. 080317 -EI, In re: Petition for rate increase by Tampa Electric Company; Order No. PSC-09-0375-PAA-GU, issued May 27, 2009, in Docket No. PSC-09-0375·PAA-GU, In re: Petition for rate increase by Florida Public Utilities Company. (Order No. PSC-10-0131-FOF-EI at p. 71, TR 3731) Furthermore, the Commission reaffirmed its long-standing policy of not allowing unamortized rate case expense in rate base in the last litigated FPL rate case in Docket No. 080677-EI and the Gulf Power base rate case in Docket No. 110138-EI. (TR 3731-3732)

FPL witness Ousdahl acknowledged the Commission's long-standing policy to disallow unamortized rate case expense in rate base. (TR 4842) She did not address the fundamental rationale for this policy, but argued this policy imposes an unwarranted penalty and implicitly disallows prudently incurred rate case expense. (TR 4842) Contrary to Witness Ousdahl's assertion that unamortized rate case expense is essentially being disallowed if it is not approved in working capital, the Commission previously addressed this issue and stated that "[w]hile unamortized rate case expense is not allowed to earn a return in working capital for electric and gas companies, it is offset by the fact that rates are not reduced after the amortization period ends." Order No. 09-0375-PAA-GU, at p. 21. In other words, unlike water and wastewater cases where rates are reduced at the end of the amortization period, prudently incurred rate case expense in electric rate cases remains as an O&M expense in an electric utility base rates beyond any amortization period. (TR 3730)

In discovery responses, FPL cited to its settlement order in the 2012 rate case and Florida Public Utilities Company ("FPUC") base rate case to support its position that unamortized rate case expense should be allowed in rate base. (TR 3732) However, both of these cases are distinguishable from a fully litigated electric base rate case. In the FPUC rate case, the Commission stated "[t]he inclusion of amortized rate case expense in working capital in FPUC's case is an exception to our long-standing policy." Order No. 09-0375-PAA-GU, at pp. 21-22. Witness Smith noted that FPUC has had this exception since 1993, (Id. at p. 22) and that the 2012 settlement specifically states that "[n]o party will assert in any proceeding before the Commission that this Agreement or any of the terms in the Agreement shall have any precedential value." Order No. PSC-13-0023-S-EI, issued January 14, 2013, in Docket No. 120015-EI, at p. 26. Neither the FPUC order nor the order approving the 2012 settlement supports a change in the Commission's long-standing policy of disallowing rate case expense in rate base. (TR 3732-3733)

Consistent with the Commission's findings in the most recent Progress Energy Florida base rate cases, the Gulf Power Company base rate case cited above, and FPL's 2010 rate case, it would be unfair for customers to pay a return on the costs incurred by the Company in this case when these costs are being used to increase customer rates. Working capital should be reduced by the full amount of the unamortized balance of rate case expense of $4.309 million. (TR 3729)

B. If applicable, for the 2018 subsequent projected test year

POSITION: *No. The Commission should follow its long-standing policy in electric cases of not allowing inclusion of the unamortized rate case expense in rate base. Consistent with the Commission's findings in the most recent Progress Energy Florida base rate cases, the Gulf Power Company base rate case, and FPL's 2010 rate case, it would be unfair for customers to pay a return on the costs incurred by the Company in this case when these are being used to increase customer rates. Working capital should be reduced by the full amount of the unamortized balance of rate case expense of $3.078 million. (Smith)*

ARGUMENT:

For the reason articulated in Issue 69A, the Commission should follow its long-standing policy in electric cases of not allowing the inclusion of the unamortized rate case expense in rate base. Consistent with the Commission's findings in the most recent Progress Energy Florida base rate cases, the Gulf Power Company base rate case, and FPL's 2010 rate case, it would be unfair for customers to pay a return on the costs incurred by the Company in this case when these are being used to increase customer rates. Working capital should be reduced by the full amount of the unamortized balance of rate case expense of $3.078 million.*

ISSUE 70: What is the appropriate amount of injuries and damages (I&D) reserve to include in rate base?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level of injuries and damages ("I&D") reserve is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year

POSITION: *FPL has the burden of demonstrating that its proposed level of injuries and damages ("I&D") reserve is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 71: What is the appropriate amount of deferred pension debit in working capital for FPL to include in rate base?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level deferred pension debit in working capital is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level deferred pension debit in working capital is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 72</u>: Should the unbilled revenues be included in working capital

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level unbilled revenues in working capital is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its proposed level unbilled revenues in working capital is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 73</u>: What is the appropriate methodology for calculating FPL's Working Capital

A. For the 2017 projected test year?

POSITION: *The appropriate method of calculating working capital is the balance sheet method. (STIPULATED)*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate method of calculating working capital is the balance sheet method.*

<u>ISSUE 74</u>: If FPL's balance sheet approach methodology for calculating its Working Capital is adopted, what adjustments, if any, should be made to FPL's proposed Working Capital

A. For the 2017 projected test year?

POSITION: *Based on OPC witness Smith's testimony, 2017 working capital should be reduced by the full amount of the unamortized balance of rate case expense of $4.309 million. Other adjustments to working capital may also be appropriate, based on the evidence adduced at hearing.*

ARGUMENT:

Based on OPC witness Smith's testimony, 2017 working capital should be reduced by the full amount of the unamortized balance of rate case expense of $4.309 million.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Based on OPC witness Smith's testimony, 2018 working capital should be reduced by the full amount of the unamortized balance of rate case expense of $3.078 million. Other adjustments to working capital may also be appropriate, based on the evidence adduced at hearing.*

ARGUMENT:

Based on OPC witness Smith's testimony, 2018 working capital should be reduced by the full amount of the unamortized balance of rate case expense of $3.078 million.

<u>ISSUE 75</u>: Should FPL's requested change in methodology for recovering nuclear maintenance outage costs from accrue-in-advance to defer-and-amortize be approved? If so, are any adjustments necessary?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its requested change in methodology for recovering nuclear maintenance outage costs from accrue-in-advance to defer-and-amortize is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its requested change in methodology for recovering nuclear maintenance outage costs from accrue-in-advance to defer-and-amortize is reasonable and prudent and that the costs are properly recorded on its books and records and reflected in the MFRs. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 76</u>: What is the appropriate level of Working Capital (Fallout Issue)

A. For the 2017 projected test year?

POSITION: *Based on OPC witness Smith's testimony, 2017 working capital should be $867.037 million. Other adjustments to working capital may also be appropriate, based on the evidence adduced at hearing.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Based on OPC witness Smith's testimony, 2018 working capital should be $912.686 million. Other adjustments to working capital may also be appropriate, based on the evidence adduced at hearing.*

<u>ISSUE 77</u>: What is the appropriate level of rate base?

A. For the 2017 projected test year?

POSITION: *Based on the testimony of OPC witnesses, 2017 rate base should be $32,492.235 million. Other adjustments to rate base may also be appropriate, based on the evidence adduced at hearing.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Based on the testimony of OPC witnesses, 2018 rate base should be $33,830.719million. Other adjustments to rate base may also be appropriate, based on the evidence adduced at hearing.*

COST OF CAPITAL

<u>ISSUE 78</u>: What is the appropriate amount of accumulated deferred taxes to include in the capital structure and should a proration adjustment to deferred taxes be included in capital structure

A. For the 2017 projected test year?

POSITION: *ADITs for 2017 should be decreased by $1.9 million to reflect the impact of removing deferred rate case expense from working capital. The appropriate amount of ADIT included in the capital structure should be $7,368.582 million. After a reconciliation adjustment to increase ADIT by $9.938 million based on OPC's increase to rate base, results in a total ADIT balance of $7,358.644 million.* (TR 3733-3734)

ARGUMENT:

OPC witness Smith testified that ADITs for 2017 should be decreased by $1.9 million to reflect the impact of removing deferred rate case expense from working capital. The appropriate amount of ADIT included in the capital structure should be $7,368.582 million. After a reconciliation adjustment to increase ADIT by $9.938 million based on OPC's increase to rate base, results in a total ADIT balance of $7,358.644 million.* (TR 3733-3734)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *ADITs for 2018 should be decreased to reflect the impact of removing deferred rate case expense from working capital of deferred rate case expense from working capital. The appropriate amount of ADIT included in the capital structure should be $7,753.738 million. After a reconciliation adjustment to increase ADIT by $9.197 million, results in a total ADIT balance of $7,744.541 million.*

ARGUMENT:

OPC witness Smith testified that ADITs for 2018 should be decreased to reflect the impact of removing deferred rate case expense from working capital. The appropriate amount of ADIT included in the capital structure should be $7,753.738 million. After a reconciliation adjustment to increase ADIT by $9.197 million, results in a total ADIT balance of $7,744.541 million. (TR 3734)

<u>ISSUE 79</u>: What is the appropriate amount and cost rate of the unamortized investment tax credits to include in the capital structure

A. For the 2017 projected test year?

POSITION: *Unamortized ITCs for 2017 in the capital structure are $106.275 million with a reconciliation adjustment to increase ITCs by $.143 million, for a total ITC balance of $106.132 million.*

ARGUMENT:

Unamortized ITCs for 2017 in the capital structure are $106.275 million with a reconciliation adjustment to increase ITCs by $.143 million, for a total ITC balance of $106.132 million.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Unamortized ITCs for 2018 in the capital structure are $100.559 million with a reconciliation adjustment to increase ITCs by $0.119 million, for a total ITC balance of $100.440 million.*

ARGUMENT:

Unamortized ITCs for 2018 in the capital structure are $100.559 million with a reconciliation adjustment to increase ITCs by $0.119 million, for a total ITC balance of $100.440 million.

<u>ISSUE 80</u>: What is the appropriate amount and cost rate for short-term debt to include in the capital structure

A. For the 2017 projected test year?

POSITION: *Short term debt should be increased by $144.799 million to correct the test year equity ratio for a total adjusted test year amount of $757.738 million. After reconciliation to rate base, the appropriate short term amount for the 2017 projected test year is $756.716 million. The appropriate cost rate for short-term debt is 1.85%.*

ARGUMENT:

FPL's requested short-term debt ratio for All Capital Sources is 1.88% and 2.49% for Investor-Only Sources. (TR 3551) Witness O'Donnell has recommended a 50% equity ratio for common equity with an 8.75% return on equity based on Dr. Woolridge's testimony. (TR 3558) Witness O'Donnell further recommends a short-term debt ratio of 3.07% with a cost rate of 1.85% for Investor-Only Sources. (TR 3558)

Based on Witness O'Donnell's testimony, short term debt should be increased by $144.799 million to correct the test year equity ratio for a total adjusted test year amount of $757.738 million. After reconciliation to rate base, the appropriate short term amount for the 2017 projected test year is $756.716 million. The appropriate cost rate for short-term debt is 1.85%. (HE 190)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Short term debt should be increased by $76.765 million to correct the test year equity ratio for a total adjusted test year amount of $398.376 million. After reconciliation to rate base, the appropriate short term debt for the 2018 projected test year is $397.903 million. The appropriate cost rate for short-term debt is 2.68%.*

ARGUMENT:

FPL's requested short-term debt ratio for All Capital Sources is 1.88% and 2.49% for Investor-Only Sources. (TR 3551) Witness O'Donnell has recommended a 50% equity ratio for common equity with an 8.75% return on equity based on Dr. Woolridge's testimony. (TR 3558)

Based on Witness O'Donnell's testimony, short term debt should be increased by $76.765 million to correct the test year equity ratio for a total adjusted test year amount of $398.376 million. After reconciliation to rate base, the appropriate short term debt for the 2018 projected test year is $397.903 million. The appropriate cost rate for short-term debt is 2.68%. (HE 191)

<u>ISSUE 81</u>: What is the appropriate amount and cost rate for long-term debt to include in the capital structure?

A. For the 2017 projected test year?

POSITION: *Long term debt should be increased by $2,210.810 million to correct the test year equity ratio for a total adjusted test year amount of $ 11,569.227 million. After reconciliation to rate base, the appropriate long term amount for the 2017 projected test year is $11,553.623 million. The appropriate cost rate for long term debt is 4.62%. (Smith, O'Donnell)*

ARGUMENT:

FPL's requested long-term debt ratio for All Capital Sources is 28.76% and 37.96% for Investor-Only Sources. (TR 3551) Witness O'Donnell has recommended a 50% equity ratio for common equity with an 8.75% return on equity based on Dr. Woolridge's testimony. (TR 3558) Witness O'Donnell further recommends a long-term debt ratio of 46.93% with a cost rate of 4.62% for Investor-Only Sources. (TR 3558)

Based on Witness O'Donnell's testimony, long term debt should be increased by $2,210.810 million to correct the test year equity ratio for a total adjusted test year amount of $11,569.227 million. After reconciliation to rate base, the appropriate long term amount for the 2017 projected test year is $11,553.623 million. The appropriate cost rate for long term debt is 4.62%. (HE 190)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Long term debt should be increased by $2,392.637 million to correct the test year equity ratio for a total adjusted test year amount of $12,416.744 million. After reconciliation to rate base, the appropriate long term amount for the 2018 projected test year is $12,402.015 million. The appropriate cost rate for long term debt is 4.87%.*

ARGUMENT:

FPL's requested long-term debt ratio for All Capital Sources is 28.76% and 37.96% for Investor-Only Sources. (TR 3551) Witness O'Donnell has recommended a 50% equity ratio for common equity with an 8.75% return on equity based on Dr. Woolridge's testimony. (TR 3558)

Based on Witness O'Donnell testimony, long term debt should be increased by $2,392.637 million to correct the test year equity ratio for a total adjusted test year amount of $12,416.744 million. After reconciliation to rate base, the appropriate long term amount for the 2018 projected test year is $12,402.015 million. The appropriate cost rate for long term debt is 4.87%. (HE 191)

<u>ISSUE 82</u>: What is the appropriate amount and cost rate for customer deposits to include in the capital structure

A. For the 2017 projected test year?

POSITION: *Per OPC adjustments, the appropriate amount of 2017 customer deposits is $406.779 million, after adjustments to reconcile the capital structure to rate base. The appropriate cost rate for customer deposit is 2.05%.*

ARGUMENT:

Per OPC adjustments, the appropriate amount of 2017 customer deposits is $406.779 million, after adjustments to reconcile the capital structure to rate base. The appropriate cost rate for customer deposit is 2.05%. (HE 190)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Per OPC adjustments, the appropriate amount of 2018 customer deposits is $385.902 million, after adjustments to reconcile the capital structure to rate base. The appropriate cost rate for customer deposit is 2.04%. (Smith)*

ARGUMENT:

Per OPC adjustments, the appropriate amount of 2018 customer deposits is $385.902 million, after adjustments to reconcile the capital structure to rate base. The appropriate cost rate for customer deposit is 2.04%. (HE 191)

<u>ISSUE 83</u>: What is the appropriate equity ratio to use in the capital structure for ratemaking purposes?

A. For the 2017 projected test year?

POSITION: *The appropriate equity ratio is 50% for the 2017 projected test year. The equity component of jurisdictional capital structure should be reduced by $2,355.609 million with corresponding increases to the long and short term debt components. The amount of common equity is $12,310.339 million for the 2017 projected test year after the reconciliation to rate base. The FPL proxy group average equity ratio is 49.3% and the national average for allowed equity ratios is 49%. Rather than utilizing FPL's proposed hypothetical capital structure of 59.6% equity, OPC recommends using a more rationale, hypothetical capital structure of 50% equity. FPL's bloated 59.6% equity ratio request in this case puts an unnecessary cost burden on FPL's ratepayer - an extra $40.97 per year to typical residential customers - and should be rejected. Applying a 50% equity ratio results in an approximately $337 million reduction to FPL's 2017 request.*

ARGUMENT:

FPL is requesting a capital structure with an excessive equity ratio of 59.60%. (TR 3539) Witness O'Donnell testified that FPL's requested equity ratio places an unnecessary costly burden on the FPL ratepayers and should not be allowed. (TR 3539) Witness O'Donnell recommended a more appropriate 50.0% equity ratio. (TR 3540)

Witness Dewhurst claimed FPL has deliberately chosen to maintain a stronger-than-average financial position because of their "unique" risk profile. (TR 5912) Witness Dewhurst testified that FPL's nuclear and natural gas exposure are part of that risk profile. (TR 2491-2492) Yet, there was no analysis or other evidence presented by FPL demonstrating that its risk profile is any higher or worse than other electric utilities around the nation. Moreover, in looking at FPL Witness Hevert's proxy electric group, it includes South Carolina Electric and Gas ("SCANA") which is building a nuclear power plant and has a 53% equity ratio. (TR 5694-5695)

Witness Dewhurst also testified that the Commission in Order No. 850246-EI stated the capital structure used for ratemaking purposes should bear an appropriate relationship to the utility's actual sources of capital. (TR 2468) However, Witness O'Donnell correctly pointed out that, if the actual capital structure was being used that is based on the marketplace, NextEra's unregulated subsidiaries would have equity ratios higher than 27% and FPL would have an equity ratio lower than the 59.6% requested in this case. (TR 3553-3557) He further noted that any capital structure in a regulated parent/subsidiary structure is hypothetical because NextEra has pre-determined the capital structure ratios. (TR 3555) NextEra's equity ratio as determined by the market is 43.8%. Witness Hevert's comparable electric utility group has an average equity ratio of 49.3% and the national average of allowed equity ratios for regulated utilities is 49.0%. (TR 3556-3557) Witness Hevert testified that his mean average of his proxy group of operating companies was 52.17%. (TR 5699) He also testified FPL's equity ratio was within the range of his proxy group of operating companies. (TR 5699) When asked about his testimony in other jurisdictions, he relied on both the range of equity ratios as well as the median common equity ratio of your proxy companies (TR 5700), which is different from the way he supported the 59.6% equity ratio in this case.

Witness O'Donnell testified that the 59.6% equity ratio FPL is requesting is not an actual capital structure, but a hypothetical capital structure. (TR 3558) Since neither FPL nor Witness O'Donnell's recommended capital structures are market driven, it is appropriate to consider the other factors identified by Witness O'Donnell that were used to develop his 50% equity ratio. (TR 3558) When the factors of NextEra's actual equity ratio, the electric proxy group equity ratio, and the average equity ratios approved by regulators are considered, they strongly favor Witness O'Donnell recommended 50% equity ratio. (TR 3556-3557)

However, Witness Dewhurst speculated that OPC's recommended 50% equity ratio would negatively affect FPL's credit metrics. (TR 5614) This naked speculation by Witness Dewhurst is rebutted by OPC Witness Lawton's analysis of the impact of OPC's recommended adjustments on FPL's financial integrity and financial metrics. (TR 3620-3626) Witness Lawton opined that FPL's financial integrity will remain strong and viable under OPC's recommendations based on an evaluation of the pertinent quantitative financial metrics. (TR 3626) FPL Witness Dewhurst also claimed that FPL should be allowed to maintain its high equity ratio because it is the under-pinning of FPL's overall financial strength which has served the customers well and added customer "value". (TR 2462, 5912) Nevertheless, Witness O'Donnell correctly noted that, even if a speculative rating downgrade occurred relative to FPL's request for an excessively high equity ratio, the speculative increase in costs of debt would be dwarfed by the increase to customers for the higher equity costs to FPL. (TR 3563) FPL's excessive equity ratio will result in an additional $337 million annually for FPL shareholders as compared to a reasonable 50% equity ratio. (TR 3559) Witness O'Donnell appropriately explained that FPL's requested 59.60% equity ratio results in an additional cost to a typical residential customer of FPL at an extra $40.97 per year over his more normal equity ratio of 50% common equity and 50% debt. (TR 3539-3540) He also testified that by using a 50% equity ratio would result in savings of $38,665 to $51,872 for an industrial customer using a 2,000 kW load. (TR 3561-3562) During cross-examination, Witness Dewhurst attempted to justify the additional costs to customers for the higher equity rate by citing to FPL's lower bills, (TR 5915) thus, making a nonsensical argument that since ratepayers pay less in bills they should expect and be happy to pay more for equity.

Thus, the appropriate equity ratio for FPL is 50% for the 2017 projected test year. The equity component of jurisdictional capital structure should be reduced by $2,355.609 million with corresponding increases to the long and short term debt components. (HE 190) The amount of common equity is $12,310.339 million for the 2017 projected test year after the reconciliation to rate base. (HE 190) FPL's bloated 59.6% equity ratio request in this case puts an unnecessary cost burden on FPL's ratepayer and should be rejected. (TR 3539-3540) As explained above, FPL's proxy group average equity ratio is 49.3% and the national average for allowed equity ratios is 49%. (TR 3556-3557) Rather than utilizing FPL's proposed hypothetical capital structure of 59.6% equity, OPC recommends using a more rationale, hypothetical capital structure of 50% equity. (TR 3540, 3558-3559, 3564, 3569) Applying a 50% equity ratio, which is in-line with industry averages (and still more than the equity ratios of both NextEra's consolidated group and the FPL proxy group average), results in an approximately $360 million reduction to FPL's 2017 request. (HE 190)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate equity ratio is 50% for the 2018 subsequent projected test year. Equity should be reduced by $2,469.402 million with corresponding increases to long and short term debt. The amount of common equity is $12,799.919 million for the 2018 subsequent projected test year, after the reconciliation to rate base. FPL's bloated 59.6% equity ratio request in this case puts an unnecessary costly burden on FPL's ratepayer and should not be allowed. The FPL proxy group average equity ratio is 49.3% and the national average for allowed equity ratios is 49%. Rather than utilizing FPL's proposed bloated capital structure of 59.6% equity, OPC recommends using a more rationale, hypothetical capital structure of 50% equity. (O'Donnell)*

ARGUMENT:

For the same reasons discussed above, the appropriate equity ratio for FPL is 50% for the 2018 subsequent projected test year. Equity should be reduced by $2,469.402 million with corresponding increases to long and short term debt. The amount of common equity is $12,799.919 million for the 2018 subsequent projected test year, after the reconciliation to rate base. (HE 191) FPL's bloated 59.6% equity ratio request in this case puts an unnecessary costly burden on FPL's ratepayer and should not be allowed. The FPL proxy group average equity ratio is 49.3% and the national average for allowed equity ratios is 49%. Rather than utilizing FPL's proposed bloated capital structure of 59.6% equity, OPC recommends using a more rationale, hypothetical capital structure of 50% equity. (TR 3540, 3558-3559, 3564, 3569)

<u>ISSUE 84</u>: Should FPL's request for a 50 basis point performance adder to the authorized return on equity be approved?

POSITION: * No. FPL's request should be denied. The requested surplus ROE inflator adder would cost customers approximately $120 million per year, providing nothing in return. FPL does not need a gratuitous financial inducement to continue delivering what it deems "superior customer value." Regulated utilities are required to provide customers the best service possible at the lowest price. FPL has invested billions in new technologies, and those investments – in base rates – have worked. Having the lowest rates in the state is a function of the type and vintage of FPL's generating equipment, customer mix, density of development, historically low natural gas prices, and other factors that are not simply measurements of superior management performance. Shareholders should not reap a bonus or reward simply because FPL management decisions have worked. Moreover, FPL conveniently ignores the potential impacts from violating its Turkey Point Nuclear Units cooling canal system discharge permits, and creating a hypersaline water infiltration issue in the Biscayne Aquifer drinking water supply, costing at least $50 million in the first year and potentially more from protracted litigation and unknown environmental costs. *

ARGUMENT:

The Commission should deny FPL's request for an adder (TR 2472) or surplus equity return inflator to be added to an already inflated 11.0% requested ROE. (TR 3598) FPL's request, if approved, for a 50 basis point ROE inflator would cost customers over $120 million per year, or a total of almost $500 million over a four year period. (TR 3602)

FPL does not need a surplus ROE inflator in order to maintain its financial integrity or to continue providing safe, adequate, and reliable service to its customers. As long as an ROE is set in accordance with the *Hope* and *Bluefield* standard, no additional return is necessary for FPL. Moreover, FPL's own expert, Witness Deason, stated that FPL could continue providing the same electric service to its customers without any surplus adder. (TR 5862)

According to OPC witness Lawton, FPL claims that its efforts in historical or past performance led to the delivery of superior value to customers and that it should be rewarded with a surplus ROE adder. (TR 3607) With respect to the past, FPL has recovered all of its O&M expenses and a fair return on its investments. Customers who received electric service paid the historical Commission authorized tariff rates to FPL for that service. In addition, the Company was authorized to, and did, earn a return on the investments it made through those rates from those same customers. (TR 3607) Commission approved tariffs contain no bonus or incentive provision. Contrary to the regulatory compact, FPL is requesting a retroactive review of its past performance in order to justify higher shareholder profits in the future. (TR 3607) Such retroactive ratemaking is simply not appropriate.)TR 3607); *See e.g.,* Miami v. Fla. Pub. Serv. Com., 208 So. 2d 249, 259-60 (Fla. 1968) (explaining why retroactive ratemaking is not permitted). Customers cannot seek a return of past, excess profits; therefore, FPL should not be allowed to receive additional profits from past decisions. (TR 3608)

In addition, Witness Lawton opined that "FPL's management performance, like any other regulated utility, is always expected to be prudent in (1) seeking the lowest reasonable costs to consumers, while maintaining the highest reasonable level of reliability; (2) maintaining the lowest reasonable level of emissions from power plants; (3) maintaining the highest reasonable level of consumer service; (4) maintaining the highest level of efficiency and reliability in generating plants; and (5) seeking the lowest reasonable non-fuel O&M costs for consumers. If FPL's management has adequately satisfied those performance expectations on an historical basis, that was presumed because such prudent management behavior was certainly an expectation of the regulatory bargain. However, prudent management and historical success in keeping costs down, improving generation efficiency, and electric reliability are reasonable consumer expectations and do not form the basis for additional future profits." (TR 3608-09) Not only is this expectation true for past performance, it is also true for future performance.

Furthermore, FPL does not need a financial inducement to continue delivering what it deems as superior customer value. (TR 3609) When granted a monopoly franchise by the state, monopolies have a duty to seek to provide superior performance in exchange for cost recovery plus an opportunity to earn a fair and reasonable return or profit commensurate with profits earned from similar risk ventures. Enhanced customer value includes providing service at the lowest rates consistent with good service. In other words, efforts to keep rates as low as reasonably possible are part and parcel FPL's obligation to serve. (TR 3609)

As a rate regulated monopoly, FPL enjoys advantages that competitive, unregulated enterprises must envy. A few advantages include: the absence of competition for market share; a suite of cost recovery mechanisms that greatly reduce the risks that costs will not be recovered; and the ability to seek changes in prices when necessary to have an opportunity to earn a fair return. (TR 3609). Because FPL enjoys such a privileged position compared to other Florida industries, no additional surplus equity inflator is necessary for FPL to continue providing safe, adequate, and reliable service. Further, any surplus equity return inflator simply redistributes customer wealth to shareholders, thus removing potentially millions of dollars each year from customers that could be spent on other commodities in Florida.

There is no dispute that FPL management does a good job in terms of service quality and reliability. However, what FPL characterizes as superior customer value is the result of investments and expenditures paid for by customers, and which are already being returned to FPL's shareholders through existing rates. (TR 3611) OPC witness Lawton addresses and refutes FPL's performance claims as it related to low bills, high reliability, low emissions, high customer satisfaction, high fossil fleet reliability, low heat rates, and low non-fuel O&M. (TR 3611-16) While FPL may currently have the lowest overall bill in Florida, FPL's base rates for a 1,000 kWh bill have increased 44% since 2006. (TR 3612). Witness Lawton noted that, while overall bills may be lower today relative to 2006, that is in large measure because the market cost of natural gas has declined dramatically from earlier periods. (TR 3612) FPL does not have any control or influence over the market cost of gas and certainly FPL should not receive hundreds of millions of dollars in equity return bonuses because the market price of natural gas has declined. Likewise, one would not look to penalize FPL if the price of natural gas increases in the future. (TR 3612)

Moreover, enjoying the lowest rates in the state is also a function of the type and vintage of FPL's generating equipment, customer mix, density of development, historically low natural gas prices, and other factors, such as economies of scale, that are not measurements of superior management performance. While reliability may have improved, this simply means customers have received what they paid for – a modernized, storm hardened, and reliable transmission and distribution grid. (TR 3613)

FPL witness Reed testified that all of FPL's investments have led to improved operational metrics, improved heat rates, improved availability factors, increased reliability, decreased duration of outages (in the aggregate), and decreased fuel costs. (TR 454-57) He agreed that customers and FPL have benefited from historically low natural gas prices. (TR 456) He further agreed that, because FPL made these investments, the customers will repay FPL for those investments, plus a return on and of those investments. (TR 457-58). Also, as a result of these investments, a prudent investor or manager should reasonably expect to see improvements in FPL's metrics, as well as more efficiencies, not less. (TR 458). Therefore, FPL's management and the customers are getting what they paid for, and the shareholders have received a fair return on these investments. However, the shareholders should not receive an additional surplus ROE bonus inflator simply for the fact that FPL's investments have panned out.

Under the regulatory compact between the monopoly and its captive customer, FPL has the duty to provide superior performance in exchange for cost recovery plus an opportunity to earn a fair return or profit commensurate with profits earned from similar risk ventures. 'Superior performance' includes providing service at the lowest rates consistent with good service. In other words, efforts to keep rates as low as possible are part and parcel FPL's obligation to serve. It is basic that an *obligation* does not require an incentive or a bonus to fulfill. (TR 3616; *see also* Section 366.03, Florida Statutes)

With respect to bonuses and rewards for management, if management made the investment and operational decisions that resulted in improvements, then management should get the bonus or reward; however, this does not apply to shareholders who have done nothing to earn that incentive. (TR 3655) The Commission allows incentive compensation for management and employees in rates, usually split 50:50 between shareholders and customers. (TR 3660) If management is appropriately recognized for doing a good job, they should be the ones considered to receive bonuses and financial incentives. (TR 3658) Shareholders on the other hand have done nothing to earn a bonus, and the Commission should not create a mechanism to reward shareholders who have truly done nothing to earn it. (TR 3658)

Witness Lawton agreed that incentives play a role in effective and efficient regulation, and incentives are used in the competitive markets. (TR 3667) Shareholders use incentives in competitive, non-regulated industries to incent excellent work from employees and management, and not themselves. Thus, shareholders do not need an incentive or reward from a regulatory commission simply because the management of the utility does a good job for the captive customers.

With regard to whether FPL's requested surplus ROE inflator is cost-based, FPL's own experts disagree. Witness Dewhurst testified the surplus ROE inflator was "absolutely" not cost based, and that it would simply be added to FPL's requested 11.0% ROE. (TR 2518/lines 10-18) Witness Dewhurst is a former employee of FPL and former Chief Financial Officer of NextEra, who has intimate knowledge of the preparation of FPL's current rate case. (TR 2448, 2450; 2517-18) Witness Deason, a former Commissioner testifying in support of FPL's gratuitous request, stated the surplus adder was cost based (TR 5861), basing his opinion on the testimony of Dewhurst and others. (TR 5861) Nevertheless, Witness Deason agreed that FPL did not need the surplus ROE adder to provide safe, adequate, and reliable service to its customers. (TR 5862) OPC asserts that the surplus ROE inflator is not cost based, but an arbitrary and unjustified request for what amounts to additional monies for FPL's shareholders.

When considering whether FPL should receive a surplus ROE inflator for superior performance to electric customers, the Commission should also consider whether environmental impacts from FPL's operations have also been superior. Currently, FPL is subject to a Florida Department of Environmental Protection *Consent Order* for a discharge permit violation related to hypersaline water emanating from its Turkey Point Nuclear Units cooling canal system. (TR 3617-18) FPL will need to spend tens of millions of dollars, perhaps hundreds of millions, attempting to resolve the permit violation and prevent hypersaline water from infiltrating further into the Biscayne Aquifer drinking water supply. And it is unknown whether FPL's plan will even work. FPL expects to spend approximately $50 million in the first year alone attempting to resolve this permit violation, which it intends to attempt to recover from its ratepayers. (TR 3618). These are serious environmental issues with no easy solutions. In addition to the question of who pays to prevent the hypersaline water from infiltrating further into the Biscayne Aquifer (FPL or its customers), there may be years of protracted litigation in state and federal courts, as well as cost recovery proceedings before the Commission, before the hypersaline water issues can be resolved.

For all the reasons discussed above, FPL's requested ROE inflator should be denied. Shareholders do not need additional incentives to invest in low risk, rate-regulated monopoly utilities. OPC submits that a regulated utility's customers are entitled to the utility's best efforts to deliver high quality service at the lowest reasonable prices possible. Therefore, FPL's gratuitous request should be completely rejected.

<u>ISSUE 85:</u> What is the appropriate authorized return on equity (ROE) to use in establishing FPL's revenue requirement?

A. For the 2017 projected test year?

POSITION: *The appropriate ROE is 8.75%. FPL's requested 11% ROE with a .5% surplus ROE inflator and a 59.6% equity ratio is extravagant and excessive under current market conditions. Both interest rates and awarded ROEs have decreased since 2012. Applying the Discount Cash Flow ("DCF") method checked by the Capital Asset Pricing Model ("CAPM") method with a proposed capital structure of 50% and also applying the electric proxy groups, demonstrates the appropriate ROE for FPL is 8.75%. Utilizing an 8.75% ROE would result in an approximately $540 million reduction from FPL's 2017 request.*

ARGUMENT:

There are three reasons why ROE, capital structure, and the 50 basis point adder matter.

The three largest issues in this case are: (1) FPL's authorized return on equity (11.0% vs 8.75%), (2) the appropriate percentage of equity in the capital structure for ratemaking purposes (59.6% vs 50.0%), and (3) the 50 basis point ROE adder/surplus inflator requested by FPL. According to FPL, each 1.0% (or 100 basis points) added to FPL's ROE represents approximately $240 million more annually that ratepayers will have to pay.

The difference between FPL's and OPC's recommended ROEs represents $540 million (2.25% x $240m); the difference between FPL's and OPC's recommended capital structure for ratemaking purposes represents $360 million; and the inclusion of a 50 basis point adder/surplus ROE inflator represents $120 million (0.50% x $240m). The total difference between FPL's and OPC's recommendations on these three issues totals approximately $1.02 billion more that ratepayers will have to pay annually unless the Commission rejects FPL's recommendations on these issues.

Introduction. FPL's requested return on equity is clearly inflated in light of current market conditions. Each intervenor witness recommended an ROE which was lower than FPL witness Hevert's ROE. Witness Hevert's recommended 11.0% ROE is an outlier among all the recommended ROEs in this case, including those in constructive jurisdictions. (TR 5662-5665; HE 383 (Recently Authorized ROEs)) He admitted it has been nearly five years since a regulatory commission approved an ROE at or above 11.0%. (TR 5684-5687; HE 353 (Bond Yield Risk Premium)) Dr. Woolridge performed a robust and thorough ROE analysis along with a clinical dissection of witness Hevert's flawed ROE analysis, methodologies, and inflated ROE recommendation. Based upon the facts in evidence, this Commission should give greater weight to Dr. Woolridge's ROE analysis and recommendation than to witness Hevert's upwardly biased, tailored-to-fit-FPL's-desired ROE and range.

Dr. Woolridge's testimony is essentially a textbook on understanding rates of return required by utilities in current capital market conditions. (TR-3188-3280) His analysis is spot on and should be more strongly considered than the other ROE witnesses. His critique of witness Hevert is thorough and exhaustive.

Dr. Woolridge's recommended ROE. Dr. Woolridge recommends an 8.75% ROE based on a 50% common equity ratio supported by OPC witness O'Donnell; however, if the Commission adopts FPL's requested 59.60% common equity ratio for ratemaking purposes, Dr. Woolridge asserts that a lower ROE is appropriate (TR 3191) because an inflated equity ratio makes FPL a less risky investment than other companies. (TR 3197) His ROE recommendation is derived from the proper use of the discounted cash flow ("DCF") model as well as the capital asset pricing model ("CAPM"); plus he utilizes two proxy groups – both his and witness Hevert's – in his DCF and CAPM analyses. (TR 3191)

Market Conditions Since 2012. Dr. Woolridge presents a detailed summary analysis of what has changed in the capital markets since FPL's last rate case. (TR 3192-3196) Namely, authorized ROEs for U.S. electric utilities, according to the Regulatory Research Associates April 2016 publication, have steadily declined since 2012 – from 10.01% in 2012, to 9.80% in 2013, to 9.76% in 2014, to 9.58% in 2015, and to 9.68% in the first quarter of 2016. (TR 3193-94, Figure 2; See also witness Hevert's HE 383, Recently Authorized ROEs) Further, Hearing Exhibit 353, attached to witness Hevert's rebuttal testimony, shows that the last time any regulatory commission in the U.S. approved an ROE at or above 11.0% was on September 2, 2011, for an

Alaskan utility. Prior to that, it was December 29, 2010. (TR 5684-5687; HE 353) Witness Hevert admitted that it had been approximately 5 years since any electric company received such a high ROE. (TR 5685-5687) Therefore, witness Hevert's recommended ROE flies in the face of what other regulatory commissions have and are currently approving for electric companies. (HE 353, HE 383) And, since FPL's last rate case, FPL has been one of the top performing electric utilities in the U.S. with its authorized ROE of 10.5% and an earned ROE of approximately 11.5%. Moreover, FPL has enjoyed an excellent credit rating compared to other electric companies. (TR 31943195) Therefore, FPL has not been hampered by its currently authorized 10.5% ROE.

When estimating FPL's required ROE, one must take into account FPL is less risky when compared to other electric companies, especially if you apply FPL's requested capital structure for ratemaking purposes. (TR 3196-3197) Witness Hevert's flawed assessment of capital market conditions relies upon economists' interest rate forecasts, as well as assumptions of higher interest rates and capital costs. (TR 3197-3198) In addition, Witness Hevert has testified several times in the past that interest rates will increase; yet, long-term interest rates and capital costs are still at historically low levels, and long-term capital costs are likely to remain low. (TR 3197; HEs 659-661, 664-667, 669-674 (containing witness Hevert's testimonies from 2008 to March 2016, from various jurisdictions)). In fact, long-term interest rates are lower today (2.3%) than they were during the 2013 Tampa Electric Rate Case (5.1%), when he first presented testimony to this Commission. (HE 661; TR 2313-2315)[6]

All the business risk factors relied upon by witness Hevert to inflate his recommended ROE and earnings range – from capital expenditure program, geography, and nuclear risk – have already been considered by the rating agencies S&P and Moody's which have still rated FPL at A- and A1, respectively. (TR 3197) Furthermore, witness Hevert admitted that a utility would be less risky in a jurisdiction that allowed for fuel cost recovery, environmental cost recovery, energy efficiency recovery, nuclear cost recovery, and storm cost recovery, as compared to a jurisdiction that did not. (TR 2288)

<u>Reasons why the Commission should give no weight to witness Hevert's ROE recommendation.</u> In a systematic and stepwise manner, Dr. Woolridge analyzes and identifies the critical flaws in Witness Hevert's ROE recommendation and analysis. (TR 3256-3278). Witness

[6] In 2013, Hevert agreed that people were projecting interest rates would increase and he used interest rates as high as 5.15%. (TR 2315-16)

Hevert's assessment of capital market conditions is flawed because "He has relied on upwardly biased economists' interest rate forecasts in assessing capital costs and in estimating FPL's ROE." (TR 3256) A less risky electric utility like FPL requires a lower ROE from investors to attract capital. (TR 3257) Witness Hevert has changed his equity cost rate approach and testimony in this proceeding by erroneously giving primary weight to his CAPM and RP approach (with their inflated results), and virtually no weight to his DCF approach. (TR 3257; HE 661) In addition, witness Hevert's DCF approach include errors, such as relying upon overly optimistic and upwardly biased earnings per share ("EPS") growth forecasts. (TR 3198-3199)

According to Dr. Woolridge, there are numerous errors in witness Hevert's DCF, CAPM, and RP approaches, which he illustrates in great detail. (TR 3257-3278) These errors have resulted in witness Hevert's upwardly biased ROE and range of ROE. He erroneously includes various business risk factors in this ROE analysis, even though the credit rating agencies take these risks into consideration when determining FPL's credit rating. (TR 3258-3259) And witness Hevert also erroneously includes a 0.12% flotation costs in his ROE analysis in order to recommend his inflated 11.0% ROE; however, flotation costs should not be included because NextEra issues equity, not FPL. (TR 3259, 3278-3280)

Depending on the jurisdiction, witness Hevert relies upon either the DCF model, the CAPM model, or all the models for his recommended ROEs. Thus, he is not consistent. In his 2010 South Carolina testimony (HE 660, p. 31), witness Hevert relied upon the DCF model, and used the CAPM model and risk premium models for assessing his DCF results. (TR 2305, 2307) In his 2013 TECO testimony (HE 661, p. 19), witness Hevert also relied upon the constant growth DCF model, and used CAPM and risk premium as corroborating methodologies to arrive at his recommended ROE. (TR 3197-3202; 3209-3210.) He agreed in this case he changed his methodology for recommending ROEs, emphasizing CAPM over DCF, and claiming the market has changed. (TR 2310) Witness Hevert has virtually abandoned his constant-growth and multi-stage DCF results in favor of his flawed CAPM approach. (TR 3198-3200) His CAPM analysis is flawed because it uses projected, long-term Treasury yields which were more than 200 basis points higher than current long-term Treasury rates. (TR 3199) His market risk premiums are projected (10.68% and 9.87%), based on earnings per share ("EPS") projections which include unrealistic assumptions regarding future economic and earnings growth and stock returns. (TR 3199-3200) Moreover, his risk premiums have steadily increased from 7.10% in 2008 to 10.82%

in 2015. (HE 670) His risk premium is nearly double that of Dr. Woolridge's 5.5% market risk premium. (TR 3200) When one uses inflated data inputs in the CAPM model, one receives inflated results.

Moreover, witness Hevert's risk premium ("RP") equity cost estimates are too high because they range from 10.04% to 10.53%; however, as shown on his own exhibit, HE 353, authorized ROEs for electric companies are declining and are now below 10% in 2016. (TR 3201-3202, 3251-3252) The mean ROE for the 71 vertically integrated electric utilities was 9.88% and the median was 9.83%, more than 100 basis points lower than witness Hevert's 11.0% recommended ROE. (HE 383) Even with authorized ROEs trending lower (TR 3201-3202, 3251-3252; HE 383), earned ROEs for electric utilities have been in the 9.0% to 9.5% range for the first half of 2016 according to the AUS Utilities Report. (TR 3254)

Furthermore, witness Hevert's methodologies appear to change in order to suit the jurisdiction he is providing testimony in. Hearing Exhibit 673 contains testimony by witness Hevert filed in Missouri, District of Columbia, North Carolina, and Florida, all filed in February and March 2016. His recommended ROEs for the District of Columbia and each state other than Florida are all below that of his recommended ROE in this case. (HE 673) Only in Florida does witness Hevert primarily rely upon the CAPM methodology for his recommended ROE (HE 673) He admitted that he tailors his ROE recommendation to suit the needs of each jurisdiction. When cross examined about his Exhibit 42, Recently Authorized ROEs (HE 383), he was asked about the meaning of "above average," "average," and "below average" designation. (TR 5660-63) He testified those were designations made by Regulatory Research Associates ("RRA"), and he agreed that "above average" related to the ROEs authorized by regulatory jurisdictions which RRA considered "more constructive" and that the "below average" designation related to jurisdictions which RRA considered to be "less constructive." (TR 5661-5663) He further agreed the data in his exhibit showed that higher ROEs were awarded in more constructive jurisdictions. (TR 5664) By implication, lower ROEs were authorized in less constructive jurisdictions.

When asked whether his ROE recommendation would be higher in a more constructive environment, witness Hevert initially waffled in his response, then admitted that "Investor expectations are based, in large measure, on the constructiveness of the jurisdiction." (TR 5664-5665) And that "this relationship [between recommended ROE and constructiveness of the jurisdiction] makes sense from that perspective." (TR 5664, 5665/lines 3-5, 10-11) When pressed again, he agreed that "knowing the jurisdiction in which you are seeking to invest or in which, in your case, you're analyzing is important to assessing what an appropriate ROE should be." (TR 5665/lines 12-15) Later, he admitted that he considered the regulatory environment as an analyst when making his recommendation. (TR 5668/lines 15-16) Thus, the reliability of his ROE recommendations is called into question because Mr. Hevert admits he takes into account whether the jurisdiction is considered constructive or not when recommending an ROE for approval in that jurisdiction.

When cross examined concerning his CAPM analysis, witness Hevert admitted that "CAPM Application and Theory per New Regulatory Finance" by Roger A. Morin, PhD. (HE 689) was a practitioner's text that is widely referenced. (TR 2008-2009) According to Dr. Morin, "For reasons of consistency, the market index employed should be the same as the market index used in deriving estimates of beta." (TR 2409) Witness Hevert was questioned whether he "mixed-and-matched" two different values for beta and two different risk-premium estimates he obtained from Bloomberg and Value Line to arrive at a range of CAPM results for his CAPM analysis in HE 125 (RBH-2). (TR 2412) Even though his methodology runs contrary to the excerpt from Dr. Morin's authoritative practitioners' text for calculating CAPM results, he would not admit that he "mixed-and-matched" beta and risk-premium values to obtain his CAPM results. (TR 2412-2413) This further illustrates how witness Hevert creates a CAPM analysis that he feels represents the view of investors (TR 2413), and then presents that view to regulatory commissions.

A review of witness Hevert's prior testimonies in this and other jurisdictions demonstrates how he has changed and adjusted his emphasis on the DCF, CAPM, and RP approaches as well as his data inputs. *See e.g.,* Hearing Exhibits 659-661, 664-667, 669-674 (containing his testimonies before numerous regulatory jurisdictions from 2008 through March 2016). In fact, the last time he testified for a Florida utility, he primarily relied upon the constant growth DCF model (HE 661, page 19), yet, three years later, now relies on CAPM instead and expresses "concerns" with the constant growth DCF model. (TR 5557) Such jurisdictional flexibility is simply not credible.

<u>Capital costs in today's markets.</u> Changes in the capital market since 2012 clearly support a lower cost of capital. Dr. Woolridge's detailed explanation of capital costs in today's markets explains the impact of Federal Reserve policy on near-term and long-term interest rates and the BREXIT vote, as well as how the impact of the slowdown in global economic growth, slack in the economy, declining energy and commodity prices, and the slow pace of inflation have all impacted

the capital markets required return on equity. (TR 3202-3214) It is axiomatic that, since the regulated electric industry is less risky than other industries, the required return on equity is lower for the electric industry. Likewise, if a particular electric company is less risky than another, its required ROE should be lower as well.

Dr. Woolridge's Recommended ROE. Dr. Woolridge prepared a DCF analysis and a CAPM analysis for both his proxy group and witness Hevert's proxy group, and testified that the constant growth DCF model is the most appropriate for public utilities. (TR 3229-3250) His DCF results were 8.45% for his proxy group and 8.85% for Hevert's proxy group, and his CAPM with proper data inputs were 7.90% and 8.10% respectively. (TR 3250) Dr. Woolridge's properly calculated CAPM results are lower than witness Hevert's flawed, upwardly biased CAPM results; thus, showing the importance of utilizing the proper date inputs in preparing a ROE analyses. As a result, Dr. Woolridge's appropriate equity cost rate or ROE for FPL is 8.75% with a range of 7.90% to 8.85%.

Appropriateness of 8.75% for FPL. Dr. Woolridge describes four reasons why 8.75% is appropriate, reasonable, and fair for FPL: (1) low capital costs for utilities; (2) low risk as measured by Beta; (3) high credit rating for FPL; and (4) declining nationwide ROEs for electric companies, with the average now below 10.0%. (TR 3251-3252) Further, in 2015, Moody's acknowledged that regulated utilities' "…credit profiles . . . will remain intact. . . regulators will continue to trim . . . profitability by lowering its authorized returns on equity (ROE). . . . [Moody's] view cash flow measures as more important rating driver than authorized ROEs. . . .' " (TR 3252) Thus, Moody's is more concerned about cash flow than authorized ROE. (TR 3252) Moreover, utilities in Florida benefit from a number of pass-through clauses that help facilitate and maintain utilities' cash flow.

Hope and Bluefield standards. The constitutional standard to apply in approving a return on equity for regulated utilities was established by the U.S. Supreme Court in the *Hope* and *Bluefield* cases. As long as returns on capital are "(1) comparable to returns investors expect to earn on investments with similar risk; (2) sufficient to assure confidence in the company's financial integrity; and (3) adequate to maintain the company's credit and to ·attract capital," the constitutional standard will be satisfied. (TR 3253-3254) Dr. Woolridge provides direct market-based evidence that his 8.75% ROE recommendation meets the *Hope* and *Bluefield* standards. (TR 3254)

The current earned ROE's for electric utilities have been in the 9.0% to 9.5% range in the first half of 2016, according to the *AUS Utilities Report*. (TR 3254) Figure 10 in Dr. Woolridge's testimony provides the year-to-date stock performance of the Dow Jones Utilities Index ("DJU") and the S&P 500 ("GSPC"). (TR 3255) While the S&P 500 is up 1.22%, the DJU is up 17.71%. (TR 3254) This current market-based data provides direct evidence that an ROE of 9.0% to 9.5% is clearly more than enough to meet investor return requirements. Therefore, Dr. Woolridge's 8.75% recommendation satisfies the *Hope* and *Bluefield* standards of providing a comparable return to investors that is sufficient to assure the company's financial integrity is adequate to maintain credit quality and attract capital.

<u>Findings and conclusions of law by the Missouri Public Service Commission.</u> The weight to be given to witness Hevert's recommended ROE can be summed up in the findings and conclusions of law contained in the September 2, 2015, Report and Order of the Missouri Public Service Commission. See HE 675, containing excerpt from that final order.

In paragraph 30, on pages 18-19, the Missouri commission stated: "State public utility commissions in the country are reducing authorized returns on equity to follow the significant decline in capital market costs. A comparison of industry authorized returns on equity indicates that they have been steadily declining over the last several years." (HE 675; TR 2338)

Regarding the credibility of witness Hevert's testimony in that case, on pages 19-20, paragraph 33, the Missouri Commission made the following comments: his 10.3% ROE would be excessive and his ROE "estimate is high because (1) his constant growth DCF results are based on excessive and unsustainable long-term growth rates, (2) his multi-stage DCF is based on a flawed accelerated dividend cash flow timing and an inflated gross domestic product growth estimate as a proxy for long-term sustainable growth, (3) his CAPM is based on inflated market risk premiums, and (4) his bond yield plus risk premium is based on inflated utility equity risk premiums." (HE 675; TR 2339) In its conclusions of law on page 22, the Missouri Commission found the ROE recommendations of three other witness to be "reasonable and an accurate estimate of the current market cost of capital" for the utility. However, witness Hevert was not among the witnesses whose recommendation were considered reasonable and accurate. (HE 675)

<u>Conclusion.</u> For the reasons stated above, the Commission should give little weight to witness Hevert's recommendations and consider more strongly the recommendations of Dr. Woolridge. The ROE issue has the greatest impact in this case. The delta between OPC and FPL

is 225 basis points, or approximately $540 million dollars per year. The Commission should reject FPL's inflated ROE, and select an ROE that is more reasonable, as exemplified by Dr. Woolridge's recommendation.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: * See position on ISSUE 85(a) above.*

ARGUMENT:

See argument on ISSUE 85(a) above.

ISSUE 86: What is the appropriate weighted average cost of capital to use in establishing FPL's revenue requirement?

A. For the 2017 projected test year?

POSITION: *The weighted cost rates for the 2017 project test year are as follows: Long-term debt – 1.64%; Short-term debt – 0.04%; Common Equity – 3.32%; Customer deposits – 0.03%; Deferred taxes – 0.00%; and Investment tax credits – 0.02%. Pursuant to the standards set forth in *Hope* and *Bluefield*, FPL will maintain its financial integrity under OPC's recommended capital structure of 8.75% equity return with a 50% debt/50% equity capital structure with a 5.05% overall rate of return.*

ARGUMENT:

Three reasons why ROE, capital structure, and the surplus ROE inflator adder matter

The three largest issues in this case are: (1) FPL's authorized return on equity (11.0% vs 8.75%), (2) appropriate percentage of equity in the capital structure for ratemaking purposes (59.6% vs 50.0%), and (3) the ROE adder/surplus inflator requested by FPL. According to FPL's assertion, each 1.0% (or 100 basis points) added to FPL's ROE represents approximately $240 million more annually that ratepayers will have to pay.

The difference between FPL's and OPC's recommended ROEs represents $540 million (2.25% x $240m); the difference between FPL's and OPC's recommended capital structure for ratemaking purposes represents $337 million; and the inclusion of a 50 basis point adder/surplus ROE inflator represents $120 million (0.50% x $240m). The total difference between FPL's and OPC's recommendations on these three issues totals approximately $997 million more that ratepayers will have to pay annually unless the Commission rejects FPL's recommendations on these issues.

FPL's financial integrity

OPC Witnesses Dr. Woolridge and Lawton both address the financial integrity of FPL in light of OPC's recommended adjustments and the constitutional standard set forth in *Hope* and *Bluefield.*[7] Dr. Woolridge testifies that an 8.75% ROE is consistent with current market evidence and expectations, and will allow FPL sufficient financial integrity to attract capital. (TR 3253-54)

OPC Witness Lawton analyzed the impact of all of OPC's recommended adjustments on FPL's financial integrity and financial metrics, including ROE, capital structure, and other recommended adjustments. (TR 3619-26) He testified that Dr. Woolridge's recommended 8.75% ROE as well as Witness O'Donnell's recommended 50% equity ratio in the capital structure satisfy the constitutional standard set forth in *Hope* and *Bluefield* while maintaining FPL's financial integrity and ability to attract capital. (TR 3619-26) To arrive at this conclusion, Witness Lawton evaluated FPL's March 31, 2016, Moody's credit report and the impact of OPC's recommendations on its financial metrics.

According to Moody's, "FPL is one of the strongest regulated electric utilities in the U.S. The political and regulatory environment for Florida utilities is stable. . . ." (TR 3621) "Its large, mainly residential service territory is growing, and the economic recovery will result in organic growth in sales and a need for new infrastructure." (TR 3621) FPL has strong credit metrics and financials according to rating agencies like Moody's. (TR 3621) In addition, Witness Lawton analyzed the financial metrics – cash flow coverage of interest, cash flow as a percentage of debt, and debt leverage ratio – that bond rating agencies consider in evaluating credit risk to a company. (TR 3621-3626) Under OPC's recommended 8.75% ROE, 50% equity capital structure, and 5.05% overall rate of return (as shown on revised DJL-5 of his testimony (HE 197), FPL's financials fall within the benchmarks except for 50% debt ratio. (TR 3626) Therefore, in Witness Lawton's opinion, FPL's financial integrity will remain strong and viable under OPC's recommendations based on an evaluation of the pertinent quantitative financial metrics. (TR 3626)

[7] *Federal Power Commission v. Hope Natural Gas Co*., 320 U.S. 591 (1944) ("*Hope*") and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923) ("*Bluefield*").

Thus, FPL will maintain its financial integrity under OPC's recommended capital structure of 8.75% equity return with a 50% debt/50% equity capital structure with a 5.05% overall rate of return.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The weighted cost rates for the 2017 project test year are as follows: Long-term debt – 1.79%; Short-term debt – 0.03%; Common Equity – 3.31%; Customer deposits – 0.02%; Deferred taxes – 0.00%; and Investment tax credits – 0.02%. Pursuant to the standards set forth in *Hope* and *Bluefield*, FPL will maintain its financial integrity under OPC's recommended capital structure of 8.75% equity return with a 50% debt/50% equity capital structure with a 5.17% overall rate of return. (O'Donnell, Woolridge, Lawton, Smith)*

ARGUMENT:

See Argument for Issue 86 A.

NET OPERATING INCOME

ISSUE 87: What are the appropriate projected amounts of other operating revenues

A. For the 2017 projected test year?

POSITION: *The appropriate projected amounts of other operating revenues per OPC adjustments for the 2017 projected test year is $192.897 million.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate projected amounts of other operating revenues per OPC adjustments for the 2018 projected test year is $194.137 million.*

ISSUE 88: What is the appropriate level of Total Operating Revenues

A. For the 2017 projected test year?

POSITION: *Test year revenues should be increased by $201.596 million to reflect OPC witness Dismukes' adjustment to correct the sales forecast, for a total of $6,128.441 million for 2017.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Test year revenues should be increased by $254.008 million to reflect OPC witness Dismukes' adjustment to correct the sales forecast, for a total of $6,221.118 million for 2018. *

<u>ISSUE 89</u>: Has FPL made the appropriate test year adjustments to remove fuel revenues and fuel expenses recoverable through the Fuel Adjustment Clause

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove fuel revenues and fuel expenses recoverable through the Fuel Adjustment Clause for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove fuel revenues and fuel expenses recoverable through the Fuel Adjustment Clause for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 90</u>: Has FPL made the appropriate test year adjustments to remove capacity revenues and capacity expenses recoverable through the Capacity Cost Recovery Clause

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove capacity revenues and capacity expenses recoverable through the Capacity Cost Recovery Clause for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove capacity revenues and capacity expenses recoverable through the Capacity Cost Recovery Clause for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 91</u>: Has FPL made the appropriate test year adjustments to remove environmental revenues and environmental expenses recoverable through the Environmental Cost Recovery Clause

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove environmental revenues and environmental expenses recoverable through the Environmental Cost Recovery Clause for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove environmental revenues and environmental expenses recoverable through the Environmental Cost Recovery Clause for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 92</u>: Has FPL made the appropriate test year adjustments to remove conservation revenues and conservation expenses recoverable through the Energy Conservation Cost Recovery Clause

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove conservation revenues and conservation expenses recoverable through the Energy Conservation Cost Recovery Clause for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove conservation revenues and conservation expenses recoverable through the Energy Conservation Cost Recovery Clause for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 93: Has FPL made the appropriate adjustments to remove all non-utility activities from operating revenues and operating expenses

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove all non-utility activities from operating revenues and operating expenses for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to remove all non-utility activities from operating revenues and operating expenses for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 94: What is the appropriate percentage value (or other assignment value or methodology basis) to allocate FPL shared corporate services costs and/or expenses to its affiliates

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to reflect the appropriate percentage value (or other assignment value or methodology basis) to allocate FPL shared corporate services costs and/or expenses to its affiliates for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to reflect the appropriate percentage value (or other assignment value or methodology basis) to allocate FPL shared corporate services costs and/or expenses to its affiliates for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 95</u>: What is the appropriate amount of FPL shared corporate services costs and/or expenses (including executive compensation and benefits) to be allocated to affiliates

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to reflect the appropriate amount of FPL shared corporate services costs and/or expenses (including executive compensation and benefits) to be allocated to affiliates for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to reflect the appropriate amount of FPL shared corporate services costs and/or expenses (including executive compensation and benefits) to be allocated to affiliates for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 96</u>: Should any adjustments be made to FPL's operating revenues or operating expenses for the effects of transactions with affiliated companies

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to FPL's operating revenues or operating expenses for the effects of transactions with affiliated companies for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that it has made the appropriate test year adjustments to FPL's operating revenues or operating expenses for the effects of transactions with affiliated companies for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 97</u>: What is the appropriate amount of FPL's vegetation management expense?

A. For the 2017 projected test year?

POSITION: *Vegetation management expenses should be reduced by $4.647 million (total and jurisdictional) for a total of $60.953 million, a reduction to the Company's projected 2017 spending. This adjustment was determined by multiplying FPL's 2015 budgeted spending of $63.100 million by the budget-to-actual variance of 96.6% for the years 2013 through 2015. *

ARGUMENT:

OPC witness Schultz demonstrated that FPL's actual vegetation management spending for 2013-2015 was less than the amount budgeted for those years, while in each of the years the actual miles cut exceeded the miles projected to be cut. (TR 3490; HE 185).

Ultimately, FPL's estimates for vegetation management in 2017 and 2018 are just that: estimates. Based on the recent historical trend reviewed by OPC witness Schultz, FPL has been consistently high with its estimates for the three years beginning with the last rate case test year (2013), immediately after rates had just been set and when a comparison to actual is made. The difference between OPC witness Schultz' recommendation and FPL's request is that Mr. Schultz applied a known and measurable factor to the estimate. The known and measurable factor is that FPL spent 3.4% less (or historical variance rate) on vegetation management and hardening than it originally estimated from 2013-2015. For these reasons, Mr. Schultz calculated a reduction to vegetation management/hardening expense of $4.647 million ($4.647 million jurisdictional) in 2017 by applying the historical variance rate to FPL's estimate. (TR 3490)

Specifically, this adjustment was determined by calculating a reasonable test year vegetation management spend of $60,953,000 based on the historical budget-to-actual variance calculated by multiplying the three-year average (2013 through 2015) budget-to-actual variance of 96.6% by the 2015 budgeted vegetation management amount of $63,100,000. (HE 185). This process resulted in a $4,647,000 difference from FPL's test year proposal of $65,600,000, which is the OPC's 2017 vegetation management O&M adjustment. (TR 3490; HE 185) Mr. Schultz appropriately applied the variance factor to the 2015 budgeted amount – which was greater than the actual 2015 spend – because the company budgeted the same number of miles to trim in 2017 and 2018 as it did for 2015. Assumedly, the 2016 budgeted miles were at the same level; however, the company chose to provide only the year-to-date ("YTD") budgeted miles instead of both full year 2016 budgeted miles and YTD actual. (HE 704) FPL witness Miranda criticized Mr. Schultz for not applying the historical adjustment to his purely estimated 2017 year, (TR 2673) while acknowledging that the 2016 YTD actuals are under-running the budget by 32%! (TR 2734). Given the mileage equivalence and the 2016 over-projection, the modest adjustment to the 2017 budget appears to be conservative. Mr. Shultz correctly applied the adjustment to the 2015 budgeted expenses to yield the 2017 adjustment given the downward trend in expenses and historical budget under runs.

Given FPL's track record for overstating vegetation management costs and other O&M expenses (TR 3464-3465; 3490; 3492; 2582-2591), this adjustment is reasonable and is a moderate adjustment that does not impair needed hardening efforts. Mr. Schultz demonstrated that FPL has achieved efficiency gains in the form of a declining average cost per mile of trimming and that, even with the under-spending and increased miles trimmed, they are ahead of the three year trim cycle by about a factor of 20% (2.4 years versus 3.0 years). (TR 3491-3492). His adjustment further insures that FPL does not use this area of the budget to achieve unauthorized shareholder gains at its customers' expense.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Vegetation management expenses should be reduced by $7.428 million (total and jurisdictional) for a total of $62.172 million, a reduction to the Company's projected 2018 spending. This adjustment was determined by escalating witness Schultz' 2017 vegetation management expense by witness Dismukes' recommended inflation factor of 2%. Over the past three years, the Company spent less that its budget for tree trimming, despite exceeding the miles actually trimmed over its budgeted miles. Thus, it is appropriate to make an adjustment to reflect the expected and normal level of vegetation management hardening expense.*

ARGUMENT:

For 2018, the OPC adjustment was determined using the same process as was developed and applied to 2017 vegetation management expenses, modified to provide an increase in allowable expenses by giving recognition to a 2% inflation factor. (TR 3491; HE 185). This results in a reduction to 2018 vegetation management O&M expense of $7.428 million (total and jurisdictional).

<u>ISSUE 98</u>: What is the appropriate level of generation overhaul expense

A. For the 2017 projected test year?

POSITION: *FPL's projected 2017 generation overhaul expenses are significantly higher than a normalized cost level. Since generation overhaul types and work vary annually, any base rate effect should be normalized. Normalizing generational overhaul expense results in a reduction of $3.803 million ($3.603 million jurisdictional) to the 2017 projected test year.*

ARGUMENT: FPL projected generation overhaul expense in 2017 test year has increased significantly over prior years. FPL Witness Kennedy claims the non-construction CAPEX expenditure for 2017 is $649 million higher than the 2014-2018 average level of approximately $480 million because of numerous major overhauls scheduled in 2017. She further noted that there are more major overhauls in 2017 than any other year during the 2014-2018 timeframe. (TR 816)

Witness Smith testified that for ratemaking purposes, the cost of generation overhaul should be normalized. (TR 3734) He noted generation facilities are not overhauled on an annual basis, and that the amount of overhaul expense incurred varies depending on the type of overhaul and the type of work needed during the overhaul. (TR 3734) Witness Kennedy admitted, the 2017 test year has higher costs because there are more major overhauls than during an average year. (TR 815-816) However, Witness Smith correctly pointed out that, since these costs will impact base rates and will be in effect for more than one year, these costs should be based on a normalized cost level. (TR 3734) Therefore, he recommended using a four-year average cost level from 2014 through 2017. (TR 3734-3735)

Witness Kennedy contended that the generation overhaul costs should not be normalized (TR 4914-4916) yet, she acknowledged that the maintenance for these types of units is cyclical, and not annual. (TR 4915) Thus, the cyclical nature of the overhaul expense versus the impact of setting rates based on a single year supports normalizing these costs. Witness Kennedy also argued that FPL's fleet has increased in the last twenty years, so maintenance costs have increased and historical maintenance cycles do not relate to future cycles. (TR 4914) However, as Witness Smith testified, he has addressed this issue and recommended using a blending of the most recent historical periods (2014 and 2015) and projected periods (2016 and 2017). (TR 3734-3735) This use of recent maintenance period data incorporates the higher projected maintenance costs of the 2017 test year tempered by the more recent maintenance cost periods.

FPL's projected 2017 projected generation overhaul expenses are significantly higher than a normalized cost level. Since generation overhaul types and work vary annually, any base rate effect should be normalized. Witness Smith utilized a 4-year average based on the actual 2014 and 2015 and projected 2016 and 2017 generation overhaul expenses. The 2017 levels were escalated using the 2.06% inflation rate recommended by OPC witness Dismukes. Normalizing generational overhaul expense results in a reduction of $3.803 million ($3.603 million jurisdictional) to the 2017 projected test year. (TR 3735, HE 191)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL's projected 2018 projected generation overhaul expenses are significantly higher than a normalized cost level. Since generation overhaul types and work vary annually, any base rate effect should be normalized. Witness Smith took a 5-year average based on the actual 2014 and 2015 and the projected 2016, 2017 and 2018 generation overhaul expenses. The 2017 and 2018 levels were escalated using the 2.06% inflation rate recommended by OPC witness Dismukes. Normalizing generational overhaul expense results in a reduction of $9.037 million ($8.562 million jurisdictional) to the 2018 projected test year.*

ARGUMENT:

For the reasons set forth in Issue 98A, generation overhaul expense should be reduced. FPL's projected 2018 projected generation overhaul expenses are significantly higher than a normalized cost level. Since generation overhaul types and work vary annually, any base rate effect should be normalized. Witness Smith utilized a 5-year average based on the actual 2014 and 2015 and the projected 2016, 2017 and 2018 generation overhaul expenses. The 2017 and 2018 levels were escalated using the 2.06% inflation rate recommended by OPC witness

Dismukes. Normalizing generational overhaul expense results in a reduction of $9.037 million ($8.562 million jurisdictional) to the 2018 projected test year. (TR 3735, HE 191)

<u>ISSUE 99</u>: What is the appropriate amount of FPL's production plant O&M expense?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its production plant O&M expenses are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its production plant O&M expenses are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 100</u>: What is the appropriate amount of FPL's transmission O&M expense

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its transmission O&M expenses are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its transmission O&M expenses are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 101</u>: What is the appropriate amount of FPL's distribution O&M expense

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its distribution O&M expenses are reasonable for the 2017 test year. FPL has overstated the pole inspection component of its distribution O&M for 2017. A reduction of $1,664,000 ($1,663,000 jurisdictional) is required. In addition, refer to OPC Basic Position under Burden of Proof.*

ARGUMENT:

OPC witness Schultz testified that actual pole inspection expenses were below budget during the period 2012 through 2015, even though the actual number of inspections exceeded the planned number of inspections. (TR 3492-3493). As shown on HE 186, he determined an adjustment to FPL's estimate of pole inspection expense by multiplying the Company's request of $5.800 million by the budget-to-actual variance factor of 71.3% for the years 2013 through 2015 and subtracting the result from the amount requested by the Company. (TR 3482)

FPL witness Miranda complains that Mr. Schultz's adjustments are based on a three- year, instead of a five-year, variance determination and that he has not considered the capital portion. As to the base period, the Commission can make its own determination about the reasons why 2011 and 2012 were higher than the subsequent years; however, it is probable that those were the historical periods upon which the last rate case test year was, in part, based and that test year showed a under run in the budget as opposed to the years 2011 and 2012 which not unsurprisingly had over runs in the budget. The trend thereafter has been to under run the budget – especially in 2014, which saw more poles inspected than 2013 but at one-quarter the cost. (HE 185). With respect to the complaint that Mr. Schultz only looked at the O&M portion of the pole inspection program, the issue before the Commission is only the O&M portion and it is clear that FPL has under run the budget in the expense portion in the past three years – after the conclusion of the 2012 rate case. Mr. Schultz's adjustments are reasonable under the facts of the recent history.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its distribution O&M expenses are reasonable for the 2018 test year. . FPL has overstated the pole inspection component of its distribution O&M for 2018. A reduction of $1.693 million ($1.692 million jurisdictional) is required In addition, refer to OPC Basic Position under Burden of Proof.*

ARGUMENT:

See argument for 2017. The 2018 adjustment is a reduction of $1.693 million ($1.692 million jurisdictional). (HE 185).

<u>ISSUE 102</u>: Should the Commission approve FPL's proposal to continue the interim storm cost recovery mechanism that was part of the settlement agreements approved in Order Nos. PSC-11-0089-S-EI and PSC-13-0023-S-EI?

POSITION: *See OPC's position on Issue 1*

ARGUMENT:

See OPC's argument on Issue 1

<u>ISSUE 103</u>: What is the appropriate annual storm damage accrual and storm damage reserve?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its storm damage reserve is reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its storm damage reserve is reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 104</u>: What is the appropriate amount of Other Post Employment Benefits expense

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its Other Post Employment Benefits expenses are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its Other Post Employment Benefits expenses are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 105: What is the appropriate amount of FPL's requested level of Salaries and Employee Benefits

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its salaries and employee benefits expenses are reasonable for the 2017 test year. The Commission should specifically adjust salaries and employee benefits in the following areas:

1. For excessive projected employee complement, jurisdictional O&M should be reduced by $15.899 million ($15.381 million jurisdictional);
2. Consistent with prior Commission decisions, employee incentive compensation should be reduced in the amount of $35.616 million ($34.458 million jurisdictional); and
3. Corresponding adjustments should be made to reduce employee benefits by $2.395 million ($2.319 million jurisdictional). Payroll taxes should be reduced by $1.032 million ($1.018 million jurisdictional) for the excessive projected employee complement, and by $2.240 million ($2.210 million jurisdictional) for the incentive compensation adjustments recommended by OPC witness Schultz.*

ARGUMENT:

Over-projected headcount adjustment

OPC's adjustment in this area is simple and straightforward. FPL has a track record of asking for more employees than needed. And even when the Commission gives them less than they ask for, they still do not fill the authorized level of positions. Consistent with other areas of FPL's post-rate case O&M levels trending below test year forecasts, OPC witness Schultz identified a continuation of the trend where the Company has projected its payroll based on an increased number of employees. Mr. Schultz also noted that the Company's justification for over-stuffing the employee complement is similar in this case to that which proved to be unsupported by the after-case facts on the ground. (TR 3463). Based on the company's track record, Mr. Schultz testified that the Company's support for the amount of payroll included in O&M expense is insufficient. Part of his basis for this is that FPL's subject matter witness Slattery used similar justification for increased headcount to that used in the last case even though staffing levels declined overall and positions went unfilled or were eliminated despite the cries of "wolf!" from FPL. (TR 3463).

The undisputed facts are that the average number of employees for the historic years 2015 and 2014 was 8,836 and 8,847, respectively. The 2014 average of 8,847 was a decline from the average employee complement for 2013 of 9,506. (TR 3463-3464; HE 28, MFR Schedule C-35). A similar phenomenon was observed in the 2012 case. (TR 3464). In the Company's 2016 request, payroll is based on a projected average of 9,087 employees in 2016, a projected average of 9,091 employees in 2017 and a projected average of 9,067 employees in 2018. Against this backdrop, FPL seeks an increase from 2015 to 2017 – this time of 255 employees. (HE 28, MFR Schedule C-35). Despite the seeming modesty, any increase cannot be justified in this case, given FPL's track record.

Witness Schultz pointed out that there was parallel in the 2012 case where FPL claimed that there would be an employee complement of 10,311 employees in 2012 and 10,147 employees in 2013. We now know that the actual average employee complement in 2013 as shown on Exhibit No. HWS-2, Page 2, for 2013 was 9,506. That is a difference of 641 from test year forecasted employees or a reduction of 6.32%. Given this information, Witness Schulz dug back further in time. He observed that Order PSC-10-0153-FOF-EI (page 143) revealed the same pattern of conduct in the 2009 case. FPL asked for 11,111 employees for the 2010 projected test year. The fact is that the average actual employee complement for 2010 was 10,195 – a difference of 916 employees! (TR 3464-3465)

Clearly, FPL has established a pattern of conduct where they ask for far more employees than they really need and then either cut staff or do not fill positions once the rate case order is final. This history imposes a high hurdle for the Company to climb over in meeting its burden of proof. FPL's 2017 employee positions were based on actual year-to-date 2015 figures adjusted for forecasted positions. (TR 3465). Witness Schultz cautioned that, because the trend of variance between authorized and filled positions has noticeably widened over time, if not addressed it will in turn again result in an excessive revenue requirement if the Commission accepts it. (TR 3465).

Mr. Schultz further noted that the reasons advanced by witness Slattery in this case were virtually identical to those offered in the 2012 case. These are the same claims that Witness Slattery provided in Docket No. 120015-EI, on the eve of FPL cutting its workforce by 6.42%. (TR 3465-3466; 1927-1928) Similar arguments were made in the 2009 rate case. (TR 3466). However, the facts speak for themselves.

The Citizens urge the Commission to consider the Company's history of making requests for an increased number of employees while in actuality the number of FPL employees has decreased every year since 2008 and they do not hire at or near the level the Commission has authorized and upon which customer rates are established. 2009 is a good illustration of this scenario. There, FPL was implicitly authorized 10,880 positions for 2010 when the Commission made a 2.08% reduction to projected headcount, yet the actual 2010 average achieved was only 10,195. FPL effectively collected from ratepayers $45.6 million for 685 non-existent employees. (TR 3467).

To remedy this overreach, Witness Schultz testified that the number of estimated positions in the projected test year of 2017 should be reduced from 9,091 to 8,835, which is the 2015 average. This is a conservative recommendation since the year-end actual headcount was only 8,801. (TR 3468). Witness Schulz' adjustment reduces 2017 total payroll by $26.766 million, but does not include incentive compensation, as it is the subject of a separate adjustment. (TR 3469-3470). Based on FPL's correct O&M allocation factor (TR 5195), this equates to a reduction in payroll expense of $15.899 million ($15.382 million jurisdictional). (HE 181; 715).

FPL attempted to counter this adjustment by arguing that total payroll was at or above the projected payroll in 2011-2015. (TR 5271; HE 351). The Company, nevertheless, admits that payroll is driven by headcount. (TR 5270-5271). This fundamental fact cannot be ignored; nor can the long term trend of asking for a larger complement than is actually employed. The evidence indicates that the historical averages in head count are driven by temporary labor in either June or (mostly) July. (TR 5276-5277; HE 777). In 2012, 2013, and 2015, the highest level of temporary headcount was in the month of July and for 2014 June was the highest by 5 over July. After July, the August temporary headcount dropped significantly in each of the four years, perhaps coinciding with the end of summer vacation for the permanent employees. (HE 777).

In 2016, the same trend continues with temporary workers numbering between 15 and 84 in the first 5 months and spiking at 183 and 187 in June and July, respectively. Obviously, the temporary headcount has a distinct July peak and is relatively low for the balance of the other months. These facts do not suggest that the company is filling turnover with temporary headcount as suggested. Notably, the actual-to-budget under run continues in 2016. Year-to-date in July, the forecasted average total headcount included in the filing was 9,185 or (9,164 + 21) (TR 5275; HE 776) while the actual headcount for July is 9,092, including 187 temporary workers. (HE 778)

More troubling is that witness Slattery did not deny that some of the "gap" in the actual to budget headcount driven cost was being filled with incentive compensation. She said it was not a driver but was very careful not to deny that it was a component of the gap, as she also suggested that it fluctuated. (TR 5272-5273).

As stated earlier, FPL has a track record of asking this Commission to authorize a ghost complement of employees for which the customers pay the full freight. Then at its discretion, the Company always maintains a complement at a significantly lower level than the Commission authorized, while efficiencies in the business are driving the total average annual headcount to lower levels. The Commission should insist on integrity in the forecasting process and adherence to the principal that witness Deason so adamantly advocated – that the utility has the burden to demonstrate that the costs it seeks customers to pay for are reasonable and prudent. FPL's forecasted headcount does not meet this test.

Incentive Compensation Adjustment

There are two principal issues that the OPC has with the incentive compensation portion of FPL's 2017 and 2018 O&M. One is an outgrowth of what appeared to be a miscommunication and/or oversight in the 2009 rate case that affects $47.478 million of non-executive cash-based incentive compensation. More precisely the issue is whether the Company followed Order No. PSC-10-0153-FOF-EI in Docket No. 080677-EI as it was written or as the adjustment to incentive compensation was calculated and intended to be implemented. Mr. Schultz demonstrates convincingly why FPL has misconstrued and misapplied the intent of that order. The other issue is whether the incentive compensation attributable to customers properly incorporates the stated goals into the incentive compensation process. Witness Schulz also presented strong evidence that FPL failed to properly align the purported goals that were incorporated into the incentive compensation process that customers should be expected to pay. Accordingly, he recommends that the Company's 2017 O&M expense be reduced by $35.616 million ($34.458 million jurisdictional).

OPC's witness Schultz testified that in the last fully litigated rate case in 2009, the Commission decided that 100% of executive incentive compensation should be excluded from rates and "that 50 percent of the non-executive incentive compensation" shall be excluded from O&M expense borne by ratepayers. In this case, FPL Witness Slattery stated on page 12 of her direct testimony that "FPL has excluded from its expense request the portions of executive and non-executive incentive compensation that were excluded by the 2010 Rate Order, Order No. PSC-

10-0153-FOF." She explained that, even though FPL believes the expense is reasonable and properly recoverable in rates, this adjustment was made in an effort to narrow the items at issue in this rate case. This aspect of her testimony is essentially identical to the testimony provided in Docket No. 120015-EI.

Mr. Schultz noted however that the justification in 2009 for disallowing 50% (instead of the 100% disallowed for executives) was that the Commission was "hesitant to conclude that one hundred percent of the non-executive incentive compensation benefited only shareholders." Mr. Schultz also testified that in the Commission's Order in Docket Nos. 090079-EI, 090144-EI and 090l45-EI (Progress Energy Florida's rate case – now Duke – and decided only 12 days before the FPL case) stated that 100% of all the incentive compensation (both executive and non-executive) should be disallowed. (TR 3477).

FPL, as part of what it presents as its compliance adjustment, reduced O&M expense $679,000 ($657,000 jurisdictional) in 2017 and $679,000 ($657,000 jurisdictional) in 2018 for the equity portion of non-executive incentive compensation, and represents that this is consistent with the Commission adjustment in Order No. PSC-10-0153-FOF. Mr. Schultz pointed out that this insignificant adjustment may have omitted some small amount of executive incentive compensation; however, it really served to highlight that that the real oversight was that the O&M portion – $50.853 million – of the overall non-executive incentive cash compensation totaling $79.130 million remained in the case for customers to pay. (TR. 5253; HE 715; 773; 805).

Mr. Schultz initially relied on an FPL response to Staff Interrogatory 21 (HE 772) to use $60.807 million as his starting point to calculate the proper adjustment. It turned out that this was an incomplete response based on a narrow interpretation that FPL gave to the Staff's question. (TR. 5239-5240) On the stand, witness Slattery identified total expensed and capitalized employee incentives to be $79.130 million instead of the $60.807 million. (TR5253; HE 773) In the revised exhibit (HE 715), witness Schultz corrected his adjustment to use the $79.130 total amount that contained the $50.853 million O&M component, yielding the adjustment of $35.616 before the retail jurisdictional allocator is applied. (See discussion at the end of this section and calculation of adjustment based on these numbers below.)

This adjustment recommended by OPC is appropriate because it fulfills the true intent of the Commission's 2009 decision and it properly allocates the incentive compensation based on the goals that could reasonably be deemed in the customers' interest as opposed to the shareholders.

Mr. Schultz acknowledges that the adjustment made in the 2010 rate order from the 2008 rate case, Order No. PSC-10-0153-FOF, and the adjustment made by the Company in the current filing, except for the non-removal of the cash portion of the non-executive incentive compensation, appear generally to be consistent with the mechanics of the Commission's determination, with the noted exception to the level of dollars involved. (TR 3475).

As was also pointed out in Docket No. 120015-EI, before certain parties to the case settled it without an adjudication of the issue, a problem persisted then with the treatment of non-executive compensation. Mr. Schultz testified that the problem is that there was an inadvertent oversight reflected in the Commission's 2010 order regarding what should have been included as part of the adjustment in that proceeding. The OPC witness' testimony on that issue in 2009 was entitled "Non-Executive Incentive Compensation" and the questions discussed issues related to "Non-Executive Incentive Compensation"; however, the testimony dealt only with the non-executive long term incentive compensation. This was a different plan than the more costly, general, non-executive type compensation plan.

The Commission's order also refers repeatedly to non-executive incentive compensation, which suggests the Commission was also under the impression that the OPC witness' recommended adjustment was similar to the executive incentive compensation cost adjustment recommendation that consisted of both cash-based incentives as well as stock-based incentives. Therefore, the non-executive compensation adjustment in Docket No. 080677-EI appears to have inadvertently omitted the cash-based portion of the non-executive incentive compensation when the decision was made with respect to what should have been adjusted. There was no explanation or rationale contained in the order as to why one component would be excluded from rates while the other would be included. That is why a significant difference exists in this filing when compared to the mechanics of the overall executive incentive compensation adjustment.

The difference on a total Company basis in Docket No. 080677-EI amounted to approximately $52.966 million. Thus, the amount of non-executive incentive compensation at issue in this docket based on the intended adjustment in the 2010 order for 2017 is $79.130 million ($50.853 million of which is FPL regulated O&M) identified in Witness Slattery's late filed deposition exhibit No. 2, provided to the parties on August 12th and contained in HE 773. (TR 3475-3476).

Mr. Schultz's adjustment here is further consistent with the Commission's Order in Docket No. 080677-EI as it applies to customer-related goals. In this case, Mr. Schulz identified the portion of non-executive incentive compensation that was addressed and disallowed at the 50% level, but which was not explicitly identified in Docket No. 080677-EI. FPL failed to identify and remove this amount in the filing. (TR 3477). The Commission should correct this error for the Company.

In its determination of shareholder allocation of the non-executive cash incentive compensation on this issue, the OPC asks the Commission to distinguish between goals that require improvement and goals that simply allow incentive payments for performing at a level that is expected in day-to-day performance and/or a level that has previously been achieved. The Commission should not include in customer rates expenses that are oriented towards enhancing shareholder value at the expense of customers. Witness Schultz acknowledges that a properly designed employee incentive compensation plan will provide enhanced performance that benefits shareholders and ratepayers equally, and that ratepayers should share equally in the costs of such a plan with shareholders. (TR 3477-3478).

In order to determine if the goals related to incentive compensation are realistic and would stimulate improved performance, Mr. Schultz reviewed both the goals and achievements over the past five years. He testified that the information supplied on the goals and achievements in response to Staff Interrogatory No. 20 (HE 490) are in some cases generic, vague, very limited or otherwise inadequate. (TR 3479). Certainly, FPL's explanations are inconsistent with the burden of proof that the Commission should expect of a utility seeking to recover nearly $80 million in incentive compensation from its customers. Mr. Schultz noted, for example, that the customer satisfaction goal, for residential and business components alike, for each of the five plan years was listed as "aggressive goal." However, that description is not very informative and does not provide any way to measure performance.

With the exception of the 2015 residential component, the achievement result identified was "beat goal," which provides no measurement value. The exception result for the 2015 residential satisfaction simply stated "[s]lightly missed goal." Witness Schultz pointed out that the measurement of satisfaction is generally based on surveys and should require that, as a level of satisfaction is achieved, the applicable goal is increased the following year to a higher level. He did not see any evidence that FPL's incentive compensation mechanism had a practice of "moving the goal posts" each year to incent additional improvement for the benefit of customers. (TR 3479).

Mr. Schultz also notes an indication that the Company is willing to relax the requirements – even in the service reliability components – in order to allow a better opportunity for achieving an incentive payout. (TR 3480). He also noted a particularly egregious example of a recent past instance where the goal for an incentive indicator labeled "[c]ompletion of base rate proceeding" was "fair outcome for customers and shareholders" and the Company indicated that the goal was achieved. He further testified that a compensation plan element that determines the payment of extra compensation to employees (a cost the Company is seeking from ratepayers) based on how the Company perceives the outcome of a base rate filing – in part for its shareholders – is not only insulting to ratepayers but also disingenuously subjective. TR 3480). While such a goal is not readily apparent in the current case, the mere fact that it has recently been a part of the goal-setting and incentive payment process calls into question the Company's assertions that the goals are designed for customer value.

Of perhaps most significant concern to Citizens are subtle inclusion of shareholder-benefit oriented Company's goals which include financial metrics that if achieved are designed primarily to benefit shareholders. For example, Mr. Schultz notes that reducing O&M means more income for shareholders and that capital spending provides investors with more of a basis on which to earn a return. By way of example, he noted that the real-life example of FPL budgeting $62.2 million for vegetation maintenance (in a test year) and only spending $58.5 million (see HE 185) allows the Company to earn more. FPL witnesses Slattery and Deason could not refute that, despite rhetoric that FPL's goals were designed to benefit customers as purportedly demonstrated by the list of "true financial measures" (TR 5196) that are excluded from the FPL plan, that the actual goals are really financial goals in disguise. (TR 3480-3481; 5254-5257; 5826-6828).

Both FPL witnesses acknowledged that reductions in O&M, increases in capital expenditures (and rate base) and increases in ROE inure to the benefit of shareholders. Id. Even so, FPL wants its customers to pick up the tab for incenting employees to achieve these shareholder-enriching results. This is improper and unreasonable for ratepayers to pay.

Witness Schultz further testified that the goals, as depicted in the Company response to HE 490 (FPL Resp. to Staff Int. 20), are limited at best and they suggest that the FPL decision makers will do what is necessary to provide some assurance that the so-called at-risk pay is not really at risk. To remedy this abuse, based on the 2015 weighting of goals, Witness Schulz recommended assignment of the 40% financial metric to shareholders and the remaining 60% performance and so called customer goals should be split at best 50/50 between shareholders and ratepayers. (TR 3480-3481). Through such an adjustment, the Commission can and should incent the Company through ratemaking disallowances to design and enforce goals that are real goals that create an incentive to improve performance for the benefit of customers, and if not then the cost of the incentive plan(s) will be borne by shareholders. (TR 3481).

Contrary to the weak delineation that FPL seeks to make between customer goals and "true" financial goals, Mr. Schultz testifies that the evidence must establish the goals used to determine whether payment will be made must be set at a level that creates a true incentive to perform for the benefit of customers at a higher level than previously achieved. FPL's consistent failure to set true incentive goals could even serve as a basis for recommending a total disallowance. (TR 3482).

Moreover, the Commission should decline to give any weight to claims that the Company might discontinue incentive compensation if shareholders bear more of the costs that benefit them. Witness Slattery admitted that, despite past disallowances, the Company still has maintained the plans. (TR 5262). She offered no evidence that any utility had ever discontinued incentive compensation when an allocation to shareholders had occurred. Mr. Schultz, a veteran of over 600 cases, also testified that he had never observed any utility eliminate its incentive compensation plan despite having some or all of it disallowed for ratemaking purposes. Furthermore, compensation studies used by companies to justify the employee compensation are focused on total compensation and should not be given much credence unless they also indicate what portion of total compensation is allocated to shareholders in the ratemaking process. (TR 3482-3484)

To properly allocate the benefits of incentive compensation received by shareholders as shown on (HE 715 and 806), Witness Schultz began with the $79.130 million identified by the Company (HE 773) as employee incentive compensation. He excluded $31.652 million or 40% of the incentive compensation that is projected to be paid out based on achievement of the financial-related goals. That resulted in $47.478 million in incentive compensation that is projected to be paid out and it is associated with what the Company claims are customer goals. That $47.478 million was allocated 50/50 for an equal sharing of the cost of achieving these goals. The $55.391 million ($31.652 million associated with financial goals plus $23.739 million representing the shareholders' half of the customer-related goal component) is the total assigned to shareholders. This adjustment was determined by applying the corrected O&M allocation of 64.30% (50,853/79,130 = .64265 or 64.3%) that was based on the late-filed deposition exhibit of witness Slattery. (HE 773). The result is an adjustment of $35.616 million ($34.458 million jurisdictional) to the O&M non-executive incentive compensation expense included in the filing for 2017. (TR 3484-3485; HE 715, 773, 806).

Benefits and Payroll

OPC's recommended adjustment to payroll and benefits are shown on Exhibits 183 and 184. These are essentially fallout adjustments based on the formula presented. Adjustments should be made to reduce employee benefits by $2.395 million ($2.319 million jurisdictional) for the excessive projected employee complement adjustment requested by FPL and identified by OPC Witness Schultz. Payroll taxes should be reduced by $1.032 million ($1.018 million jurisdictional) for the excessive projected employee complement, and by $2.240 million ($2.210 million jurisdictional) for the incentive compensation adjustments recommended by OPC's witness Schultz.

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its salaries and employee benefits expenses are reasonable for the 2018 test year. The Commission should specifically adjust salaries and employee benefits in the following areas:

1. For excessive projected employee complement, jurisdictional O&M should be reduced by $14.887 million ($14.354 million jurisdictional);
2. Consistent with prior Commission decisions, employee incentive compensation should be reduced in the amount of $37.189 million ($35.979 million jurisdictional); and
3. Corresponding adjustments should be made to reduce employee benefits by $2.246 million ($2.177 million jurisdictional). Payroll taxes should be reduced by $.966 million ($.953 million jurisdictional) for the excessive projected employee complement, and by $2.339 million ($2.307 million jurisdictional) for the incentive compensation adjustments recommended by OPC witness Schultz.*

ARGUMENT:

Over-projected headcount adjustment

See argument for 2017. For 2018, Mr. Schultz reduces 2018 total payroll by $24.937 million, but does not include incentive compensation, as it is the subject of a separate adjustment. (TR 3469-34-70) Based on FPL's correct O&M allocation factor (TR 5195), this equates to a reduction in payroll expense of $14.887 million ($14.354 million jurisdictional). (HE 181; 715)

Incentive Compensation Adjustment

See argument for 2018. The result is an adjustment of $37.189 million ($35.979 million jurisdictional) to the O&M non-executive incentive compensation expense included in the filing for 2018. (TR 3484-3485; HE 715; 806)

Benefits and Payroll

OPC's recommended adjustment to payroll and benefits are shown on Exhibits 183 and 184. These are essentially fallout adjustments based on the formula presented. Adjustments should be made to reduce employee benefits by $2.246 million ($2.177 million jurisdictional) for the excessive projected employee complement adjustment requested by FPL and identified by OPC witness Schultz. Payroll taxes should be reduced by $.966 million ($.953 million jurisdictional) for the excessive projected employee complement, and by $2.339 million ($2.307 million jurisdictional) for the incentive compensation adjustments recommended by OPC's witness Schultz.

ISSUE 106: What is the appropriate amount of Pension Expense

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its pension expenses are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its pension expenses are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

<u>ISSUE 106A:</u> Should an adjustment be made to the amount of the Directors and Officers Liability Insurance expense that FPL included in the 2013 projected test year?

POSITION: *Yes. The Commission should reduce Directors and Officers Liability Insurance expense by $1,391,000 ($1,369,000 system) consistent with Commission precedent that allocates the cost evenly between shareholders and ratepayers.*

ARGUMENT:

OPC is proposing the same adjustment amount in this case as was proposed in the 2012 case. In its response to OPC Interrogatory No. 60 in the 2012 case, FPL has included $2,781,173 of expense in Account 925 for Directors and Officers Liability ("DOL") insurance. (HE 187) As OPC witness Schultz testified, the Company did not itemize the DOL insurance costs separately in response to Staff's discovery in this case so he used the same amount from that 2012 case for the 2017 adjustment. (TR 3494) FPL did not take issue with this amount in rebuttal. He testified in support of the OPC position that ratepayers and shareholders should share DOL insurance premium costs equally ($1.391 million system and $1.369 million jurisdictional each) for the several reasons.

Primarily, the cost associated with acquiring DOL insurance is a necessary business expense designed to protect shareholders from the decisions they made when they selected the Company's Board of Directors and when the Board of Directors hired the officers of the Company. The questions in this case are whether this cost (which FPL elected to incur) is for the benefit of shareholders and/or ratepayers, and if it benefits both, who should be responsible for the costs associated with acquiring this coverage. Even though shareholders are the primary beneficiaries, OPC witness Schultz recommends that this business expense be shared equally between shareholders and ratepayers. FPL witness Deason did not dispute that shareholders receive benefits from the insurance and the cost that provides it. (TR 5835-5838).

As noted by Mr. Schultz, in the recent Gulf Power Company rate case (Docket No. 110138-EI), the Commission determined that the cost of DOL insurance should be shared equally between shareholders and ratepayers. In addition, in the 2009 Progress Energy Florida rate case (Docket No. 090079-EI), the Commission observed that other jurisdictions make an adjustment for DOL insurance and that it has disallowed DOL insurance in wastewater cases. In the Progress Energy case, the Commission allowed the utility to place one-half the cost of DOL insurance in test year expenses. Therefore, as a result of its decisions in the Gulf and Progress Energy cases the Commission has recognized that, while DOL insurance is a legitimate business expense, this expense is unique in that it is designed primarily to protect shareholders from their past decisions. (TR 3495).

Further, even if DOL insurance costs had not been ordered shared in the Gulf and Progress Energy cases, OPC witness Schultz would still recommend an equal sharing approach for two reasons. First, the cost associated with DOL insurance benefits shareholders and they also are the ones who receive the insurance proceeds in any judgment or settlement. Witness Deason agreed with this. (TR5837-5838). Second, utilities like FPL are regulated entities subject to certain criteria for cost recovery, such as prudence and customer benefit. In ratemaking, a prudent cost should follow the benefit. Mr. Schultz further points out that, the reason for incurring that prudent cost is often to protect shareholders from imprudent decision-making by directors and officers. The benefit of this insurance clearly inures primarily to shareholders; some of whom generally are the parties initiating any suit against the directors and officers. (TR3495-3496).

The Commission's decisions on this issue in the Gulf and Progress Energy rate case dockets were fair, and should be followed in this Docket. (TR 3496). Because of these reasons, OPC witness Schultz recommends a 50% reduction to Account 925 of $1.391 million ($1.369 million jurisdictional). (TR 3493-3494; EXH 187)

ISSUE 107: What is the appropriate amount and amortization period for Rate Case Expense

A. For the 2017 projected test year?

POSITION: *FPL's projected rate case expense appears significantly overstated and should be reduced. The requested costs for employee travel (especially with respect to the number of FPL employees attending the Customer Hearings) and professional services are excessive. Inclusion of FPL overtime labor cost is inappropriate. The complexity of the rate case with two forecasted test years and an additional 2019 step increase has also increased rate case expense, and is unreasonable to be borne by ratepayers. Rate case expense should be limited to 2008 rate case levels escalated to 2017 levels which results in overall rate case expense of $3.620 million, or $1.305 million less than FPL's MFR requested amount of $4.925 million. A 4-year amortization period results in $905,000 in annual rate case expense, which is a reduction of $326,000 to FPL's requested expense. *

ARGUMENT:

FPL's requested rate case expense appears to be significantly overstated and should be reduced. (TR 3726) Witness Ousdahl testified that FPL originally requested $4.925 million in rate case expense which was subsequently reduced by the Company to $4.242 million. (TR 1678, 4855) This is a reduction of approximately $700,000.

Witness Smith testified that additional adjustments to rate case should be made. First, he stated that FPL labor cost should be removed. FPL has included $82,100 for "Labor Non-Exempt OT" and $19,982 in "FPL Labor-Related Overhead" in its request. (TR 3726) These categories include current fiscal year costs such as overtime. Although these costs are being incurred in 2016 and are already covered in base rates, FPL is proposing to add these 2016 labor costs to rate case expense to be amortized in 2017. (TR 3726) This fails to take into consideration whether FPL's earnings for 2016 were adequate to allow it to earn within its authorized range. In addition, witness Smith testified that the Commission has previously determined it is inappropriate for FPL to include additional pay or labor costs as part of the rate case expense to be recovered from ratepayers in future periods. (TR 3726) These costs including any overtime are included in the current 2016 fiscal year and, so long as FPL is earning within its authorized rates, these costs are already being recovered. (TR 3726) As of December 2015, FPL was earning at the top of its authorized range of 11.5%. (HE 573)

Second, Witness Smith addressed reducing the $505,800 in employee related travel and the amount for temporary labor and professional. (TR 3727) Looking just at the September lodging expense of $215,000 divided by 12 days for the 10-day hearing, this equates to almost $18,000 per day, which is clearly excessive. At a room rate of $150 per night, this would allow for approximately 120 employees to stay per night. (TR 3727) Witness Smith did a similar estimate for meals for a 12-day period, which equated to $11,000 per day or almost $100 per day for 110 employees. (TR 3727) Based on Witness Smith's estimates discussed above, the lodging and meal estimates are excessive. (TR 3727) Witness Ousdahl attempted to rebut Witness Smith by stating he used an overly simplistic analysis and failed to account for the cost of necessary common space. She also argued that FPL was housing more than FPL employees. (TR 4858) In discovery, FPL identified that 78 FPL employees (which in and of itself is excessive) plus 6 outside witnesses and 2 outside attorneys would be attending the hearing at a room rate of $130 to $151 per room. (HE 756) Updating Witness Smith's analysis shows that the $18,000 original per day lodging estimate minus $ 12,986 updated per day lodging costs (total 86 identified attendees times $151 room rate) would allow for $5,014 per day for common room rental and $127 per day for meals ($11,000 divided by 86), which are excessive. (TR 4858; HE 756) In addition, given that the hearing ended a full day and half early, this further illustrates that the lodging and meal estimates are overstated.

Witness Smith also suggested reducing rate case expense based on temporary and professional expenses. As an example, he noted that $400,000 was included for Concentric Energy for Reed, but only $58,190 was paid as of March 2016. (TR 3728) Hearing Exhibit 759 showed that as of July 31, 2016, the actual amount for Witness Reed was $156, 537. The estimated amount for Witness Reed's remaining rate case expense is $170,000 ($50,000 – July, $70,000 –August, $40,000 –September, and $10,000 – October). (HE 758) Therefore, the estimate/actual amount for Witness Reed is approximately $326,537 which is $73,463 less than the estimated $400,000 amount. (HE 758)

Witness Smith also pointed out that the Company included $40,000 for William Feaster, which was revised its $48,000 when asked to update rate case expense with July 31, 2016, Mr. Feaster's actual through July 31, 2016 was $24,000, although he did not file any testimony. (TR 3728; HE 755, 759) The only example of rate case related activities that Witness Ousdahl could identify for Mr. Feaster was regulatory consulting and he helped her prepare for cross-examination, yet Mr. Feaster is not listed as an attorney. (TR 4865-4866; HE 755) Witness Smith also noted that Mr. Hevert's total rate case expense of $250,000 is excessive. (TR 3728) Mr. Hevert's actual expense as of July 31, 2016 was $113,178, with $105,000 remaining. Thus, his expense is overstated by $31,822. (HE 755, 758) As Witness Smith noted the $250,000 appears excessive for an ROE witness, especially when one compares it to all three of OPC's cost of capital witness are less than $100,000 collectively. (TR 3728)

Witness Smith recommended that rate case expense be limited to the prior 2008 rate case authorized amount of $3,207,000 escalated for inflation. (TR 3729) Witness Ousdahl argued that using the 2009 rate case expense as a proxy is not supported. (TR 4841) She claims that the actual rate case expense for 2009 was $4.7 million, not the $3.2 million that Witness Smith used. (TR 4841) However, Witness Smith is clearly using the rate case expense that was approved by the Commission (TR 3729), as it would be inappropriate to include any costs that the Commission disallowed.

In Hearing Exhibit 754, FPL reduced its hotel and lodging expense forecast by $10,000. In the same exhibit, FPL reduced its forecast of expert witness expense by $771,400. (HE 754) Further, the rate case expense for Squire, Sanders & Dempsey of $270,000 should be excluded since it is for a "possible appeal." (TR 4869) Moreover, the rate case expense of $60,000 for a settlement witness should be excluded, since there is no settlement. (HE 755)

Thus, FPL's projected rate case expense is significantly overstated and should be reduced. The requested costs for employee travel (especially with respect to the number of FPL employees attending the Customer Hearings) and professional services are excessive. Inclusion of FPL's overtime labor cost is also inappropriate. The complexity of the rate case with two forecasted test years and an additional 2019 step increase has also increased rate case expense, and is unreasonable to be borne by ratepayers. Rate case expense should be limited to the 2008 rate case levels escalated to 2017 levels which results in overall rate case expense of $3.620 million, or $1.305 million less than FPL's requested amount of $4.925 million. A 4-year amortization period results in $905,000 in annual rate case expense, which is a reduction of $326,000 to FPL's requested expense. (TR 3729)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *See OPC's response to Issue 107A. *

ARGUMENT:

Please see OPC's response to Issue 107A.

<u>ISSUE 108</u>: What is the appropriate amount of uncollectible expense and bad debt rate

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its uncollectible expense and bad debt rate are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its uncollectible expense and bad debt rate are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 109: Has FPL included the appropriate amount of costs and savings associated with the AMI smart meters

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its costs and savings associated with the AMI smart meters are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its costs and savings associated with the AMI smart meters are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 110: If the proposed change in accounting to defer and amortize the nuclear maintenance reserve is approved, is the company's proposed adjustment to nuclear maintenance expense appropriate?

POSITION: *FPL has the burden of demonstrating that its proposed adjustment to nuclear maintenance expense is appropriate for the 2017 test year, if the proposed change in accounting to defer and amortize the nuclear maintenance reserve is approved. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 111: What are the appropriate expense accruals for: (1) end of life materials and supplies and 2) last core nuclear fuel?

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its expense accruals for: (1) end of life materials and supplies and (2) last core nuclear fuel are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its expense accruals for: (1) end of life materials and supplies and (2) last core nuclear fuel are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 112: What are the appropriate projected amounts of injuries and damages (I&D) expense accruals

A. For the 2017 projected test year?

POSITION: *FPL has the burden of demonstrating that its accruals for injuries and damages (I&D) expense are reasonable for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden of demonstrating that its accruals for injuries and damages (I&D) expense are reasonable for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 113: What is the appropriate level of O&M Expense (Fallout Issue)

A. For the 2017 projected test year?

POSITION: *Based on the testimony of OPC witnesses, the appropriate level of O&M expenses is $1,262.855 million for the 2017 test year.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Based on the testimony of OPC witnesses, the appropriate level of O&M expenses is $1,303.602 million for the 2018 test year.*

ISSUE 114: What is the appropriate amount of depreciation, amortization, and fossil dismantlement expense (Fallout Issue)

A. For the 2017 projected test year?

POSITION: * Any surplus reserve amortization balance from the 2012 Settlement Agreement remaining on December 31, 2016, should be credited to customers evenly in 2017 and 2018.

ARGUMENT:

As noted by witness Schultz, the initial order establishing the $894.6 million reserve required a four-year amortization period for the surplus. Order No. PSC-10-0153-FOF-EI, issued March 17, 2010. It is important to note that this amount was not in dispute as it was the remainder (after reserve transfers of $314.2 million) of what all parties agreed was at least a $1.208 billion reserve imbalance. Id. at 81, 87. Shortly thereafter, Order No. PSC-11-0089-S-EI issued February 1, 2011, modified the straight-line amortization to allow some variance up to a maximum, subject to certain earnings conditions. Id. at 20-21. This provision was further modified by the Stipulation and Order No. PSC-13-0023-S EI, issued January 14, 2013, which stated that the remaining amount of depreciation reserve surplus (coupled with a complementary amount of dismantlement reserve surplus) in the aggregate amount of $400 million was to be amortized by the end of 2016 unless earnings exceeded 11.50%. Id. at 20-21.

Mr. Schultz estimated that, with a $263 million reserve amortization balance at the beginning of 2016 and based on the historical trend he observed, there could be over $150 million of unused surplus reserve at the end of 2016. (TR 3501). The Commission also heard evidence that could have a bearing on that estimate. (HE 636) Given the fact that ratepayers have waited beyond the initial time frame (2010 – 2013) set for the return of funds which they advanced to the Company, ratepayers should be entitled to some accounting to their benefit for how the portion remaining of the $263 million was used (or remains unused and subject to refund).

In the original 2010 order, the Commission addressed factors, including intergenerational inequity, in directing that the agreed surplus be applied for the benefit of customers in accord with the matching principle. Order No. PSC-10-0153-FOF-EI, at 81-87. Some six years later, the customers are still waiting for complete recognition of the benefit of these funds. The OPC contends that they should receive the benefit in a tangible way in the form of a direct refund. FPL witness Barrett agreed that the Commission had the authority to refund any remaining surplus or to use is to offset revenue requirements for the benefit of customers. (TR 1482). Therefore, OPC urges the Commission to return to customers – in the form of a two year refund[8] -- the benefit of the customer-provided funds which have been identified, segregated and set aside for their benefit in the past three rate orders. These funds, to the extent they exist or will exist at the end of 2016, have not been taken into consideration in the establishment of the depreciation rates or expenses as they were deemed to have been entirely exhausted in the depreciation study filed by FPL. (TR 1477-1478)

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Any surplus reserve amortization balance from the 2012 Settlement Agreement remaining on December 31, 2016, should be credited to customers evenly in 2017 and 2018

ARGUMENT: See argument for 2017.

<u>ISSUE 115</u>: What is the appropriate level of Taxes Other Than Income (Fallout Issue)

A. For the 2017 projected test year?

POSITION: * Payroll taxes should be reduced by $1.032 million ($1.018 million jurisdictional) for the excessive projected employee complement, and by $2.240 million ($2.210 million jurisdictional) for the incentive compensation adjustments recommended by OPC witness Schultz in Issue 105. The appropriate level of taxes other than income is $574.963 million for the 2017 test year.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: * Payroll taxes should be reduced by $.966 million ($.953 million jurisdictional) for the excessive projected employee complement, and by $2.339 million ($2.307 million jurisdictional) for the incentive compensation adjustments recommended by OPC witness Schultz in Issue 105. The appropriate level of taxes other than income is $612.213 million for the 2018 test year.*

[8] Mr. Schultz did not recommend that any remaining portion of the surplus be used to offset 2017 revenue requirements (TR 3501). Nevertheless, the OPC does not object to a direct reduction of revenue requirements so long as the customers receive a direct benefit and the funds are not turned over to the discretion of the management to use the funds to peg earnings at the top of the authorized range solely for the benefit of shareholders.

ISSUE 116: What is the appropriate level of Income Taxes?

A. For the 2017 projected test year?

POSITION: *Based on the testimony of OPC witnesses, the appropriate level of income taxes is $788.841 million for the 2017 test year. *

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *Based on the testimony of OPC witnesses, the appropriate level of income taxes is $740.067 million for the 2018 test year. *

ISSUE 117: What is the appropriate level of (Gain)/Loss on Disposal of utility property

A. For the 2017 projected test year?

POSITION: *The appropriate level of gain on disposal of utility property is $5.759 million for the 2017 test year. *

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate level of gain on disposal of utility property is $10.759 million for the 2018 test year. *

ISSUE 118: What is the appropriate level of Total Operating Expenses? (Fallout Issue)

A. For the 2017 projected test year?

POSITION: *The appropriate level of total operating expenses is $4,287.136 million for the 2017 test year.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate level of total operating expenses is $4,381.397 million for the 2018 test year. (Smith)*

<u>ISSUE 119</u>: Is the company's proposed net operating income adjustment to remove Fukushima-related O&M expenses from base rates and recover all Fukushima-related expenses in the capacity cost recovery clause appropriate?

POSITION: *FPL has the burden of demonstrating that its proposed net operating income adjustment to remove Fukushima-related O&M expenses from base rates and recover all Fukushima-related expenses in the capacity cost recovery clause is reasonable.*

<u>ISSUE 120</u>: What is the appropriate level of Net Operating Income (Fallout Issue)

A. For the 2017 projected test year?

POSITION: *The appropriate level of net operating income is $1,841.305 million for the 2017 test year. (Smith)*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate level of net operating income is $1,839.721 million for the 2018 test year.*

<u>REVENUE REQUIREMENTS</u>

<u>ISSUE 121</u>: Is the Section 199 Manufacturer's deduction properly reflected in the revenue expansion factor?

A. For the 2017 projected test year?

POSITION: *FPL has the burden to show that the Section 199 Manufacturer's deduction is properly reflected in the revenue expansion factor for the 2017 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *FPL has the burden to show that the Section 199 Manufacturer's deduction is properly reflected in the revenue expansion factor for the 2018 test year. In addition, refer to OPC Basic Position under Burden of Proof.*

ISSUE 122: What are the appropriate revenue expansion factor and the appropriate net operating income multiplier, including the appropriate elements and rates for FPL?

A. For the 2017 projected test year?

POSITION: *The appropriate revenue expansion factor is 1.63025 for the 2017 test year. *

B. If applicable, for the 2018 subsequent projected test year?

POSITION: The appropriate revenue expansion factor is 1.63025 for the 2018 test year.

ISSUE 123: What is the appropriate annual operating revenue increase or decrease (Fallout Issue)?

A. For the 2017 projected test year?

POSITION: *The appropriate annual revenue decrease is $327.469 million for the 2017 test year.*

B. If applicable, for the 2018 subsequent projected test year?

POSITION: *The appropriate annual revenue decrease should be $147.282 million for the 2018 test year, on a stand-alone 2018 test year basis.*

OKEECHOBEE LIMITED SCOPE ADJUSTMENT

ISSUE 124: Should the Commission approve or deny a limited scope adjustment for the new Okeechobee Energy Center? And if approved, what conditions/adjustments, if any should be included?

POSITION: *The Okeechobee June 2019 limited scope adjustment (LSA) should not be approved. FPL has revenue excesses for both 2017 and 2018 and the reasonableness and accuracy of FPL's 2019-2020 projections are highly suspect. If considered, then OPC'S 2018 ROR should be used; operating costs associated with the project should be updated based on a more recent forecast; and start-up costs included in FPL's projects should be removed to normalize costs and exclude one-time, non-recurring costs.*

ARGUMENT:

FPL projects that the Okeechobee Clean Energy Center will be completed and placed into service mid-2019. (TR 3744) FPL is requesting a step-increase that would go into effect on June 1, 2019, when the project is projected to be placed into service and begins serving customers. (TR 1665-1666, 3744) FPL is requesting the costs of the Okeechobee Project to be treated as a base rate step increase after project completion base on an annualized cost level. The requested first-year annualized revenue requirement (2019) for the Okeechobee Project is $209,024,000. (TR 3744-3745)

Witness Smith recommended FPL's proposed Okeechobee June 1, 2019 limited scope adjustment ("LSA") increase request not be approved at this time. (TR 3745) This is based upon his recommended revenue reductions for 2017 and 2018. (TR 3745) In Hearing Exhibit 190, Witness Smith calculated the impact of all the recommendations for OPC's witnesses for the test year 2017, which calculation showed a total revenue reduction of $327.469 million is appropriate. In Hearing Exhibit 191, Witness Smith calculated the impact of the same OPC recommendations for 2018 (HE 190), and this calculation showed a $147.282 revenue requirement increase for 2018 is appropriate (assuming the $327.469 million reduction is approved for 2017). (HE 191)

Witness Barrett argued the Okeechobee LSA calculation is designed to earn at the "mid-point of the Commission allowed range and as such is earning neutral." (TR 4580) However, even if the Okeechobee LSA is calculated to be mid-point seeking, this does not address the fundamental issue of whether all of this revenue requirement related to the Okeechobee project would be absorbed through existing rates as evidenced by FPL continuing to earn within its authorized earnings range. Witness Smith testified that, prior to the approval of any Okeechobee LSA, updated estimates should be provided by FPL. This would allow the Commission to determine whether any increase for the LSA is warranted when it goes into service. Moreover, the Commission should reject the Okeechobee LSA because OPC Witnesses have shown significant revenue excesses for 2017 and 2018, and FPL has not demonstrated that a mid-2019 increase would be necessary to keep FPL from falling below its authorized ROE range. Thus, Witness Smith testified that approval of a projected mid-2019 step increase at this time would be premature. (TR 3750)

Witness Barrett, however, claimed that the assumption and process used in developing these plan/forecasts are robust and reasonable, and the plans/forecasts can be relied upon for rate setting. (TR 1415) Nevertheless, Witness Smith testified that he was skeptical of the accuracy and reasonableness of FPL's 2019-2020 projections, given that they are three years into the future. (TR 3745) Moreover, Witness Barrett admitted that he was not aware of any utility asking for a rate increase three years out. (TR 1466) He also conceded that FPL did not file MFRs or a forecast for 2019. (TR 1467) Furthermore, Witness Dismukes has testified that the rate case forecast proposed by FPL in this proceeding should not be used for ratemaking purposes due to an understated revenue forecast. (TR 3388-3389) The difference between the energy sales forecasts filed in this case (which should not be used for ratemaking) and the energy sales forecasts used for the 2015 TYSP and to approve the Okeechobee need determination are quite considerable, and have not been explained by the Company. (TR 3388-3389)

Witness Barrett did testify that the cost assumptions used in developing the base revenue requirements for the 2019 Okeechobee LSA are based on the Commission's Need Determination Order No. PSC-16-0032-FOF-EI. The base revenue requirements reflect the first-year return on and of the capital investment in the Okeechobee Unit, along with all non-fuel operating costs and taxes. (TR 1403) While Witness Smith recommended the Okeechobee Project LSA not be approved, he stated that if the Commission considers the LSA, the following contingent adjustments to FPL's request should be made. (TR 3745) First, the appropriate rate of return to apply to the projected rate base should be based on OPC's overall recommended 2018 rate of return. The projected amount of rate base and operating costs associated with the project should also be updated based on more recent forecasts, which should be provided by FPL in 2019 prior to the approval of the project. Additionally, the start-up costs included in FPL's projections should be removed so that base rates established at the time of the proposed step increase are based on normalized costs and exclude one-time non-recurring charges. (TR 3745) The start-up costs FPL projects to expense in the twelve-month period ending May 31, 2020, are one-time, non-recurring expenses that should not be incorporated into the Okeechobee LSA. (TR 3750)

The proposed Okeechobee June 1, 2019 LSA increase requested by FPL should not be approved at this time due to FPL's revenue excesses for both 2017 and 2018. Further, the reasonableness and accuracy of FPL's 2019-2020 projections is highly suspect and should not be used. However, if the Commission considers the Okeechobee LSA, then (1) OPC'S 2018 ROR should be used; (2) operating costs associated with the project should be updated by FPL based on a more recent forecast; and (3) start-up costs included in FPL's projects should be removed to normalize costs and exclude one-time, non-recurring costs. (TR 3745)

<u>ISSUE 125</u>: Has FPL proven any financial need for single-issue rate relief in 2019, based upon only the additional costs associated with the Okeechobee generating unit, and with no offset for anticipated load and revenue growth forecasted to occur in 2019?

POSITION: *No, due to FPL's revenue excesses for both 2017 and 2018, the reasonableness and accuracy of FPL's 2019-2020 projections is highly suspect.*

ARGUMENT:

For the reasons set forth in Issue 124, FPL has not proven any financial need for single-issue rate relief in 2019, based upon only the additional costs associated with the Okeechobee generating unit, and with no offset for anticipated load and revenue growth forecasted to occur in 2019. Due to FPL's revenue excesses for both 2017 and 2018, the reasonableness and accuracy of FPL's 2019-2020 projections is highly suspect.

<u>ISSUE 126</u>: What are the appropriate depreciation rates for the Okeechobee Energy Center?

POSITION: *FPL has the burden to show that the appropriate depreciation rates for the Okeechobee Energy Center are reasonable and appropriate. OPC agrees with SHHA *

<u>ISSUE 127</u>: What is the appropriate treatment for deferred income taxes associated with the Okeechobee Energy Center?

POSITION: *Total company accumulated deferred income taxes, as well as all other sources of capital included in the 2018 OPC recommended overall rate of return should be used to establish rates whether in a full test year or limited scope adjustment. This is consistent with prior Commission practice regarding step increases.*

ARGUMENT:

OPC Witness Smith stated on cross-examination by Staff that the IRS guidance is still relevant regarding deferred income taxes in the capital structure; however, he withdrew his assertion that FPL's incremental cost of capital would violate the IRS normalization requirements. He reiterated that OPC's position remains that the 2018 overall cost of capital should be used instead of an incremental cost of capital without deferred income taxes. (TR 3756)

<u>ISSUE 128</u>: Is FPL's requested rate base of $1,063,315,000 for the new Okeechobee Energy Center appropriate?

POSITION: *No mid-2019 step increase is warranted nor should it be granted. If the Commission does consider any LSA, OPC recommends that the projected amount of rate base and operating costs associated with the project be updated based on more recent forecasts, which should be presented by FPL in 2019 prior to approval of the project.*

ARGUMENT:

For the reasons set forth in Issue 124, no mid-2019 step increase for the Okeechobee Energy Center is warranted nor should it be granted. If the Commission does consider any LSA, OPC recommends the projected amount of rate base and operating costs associated with the project be updated based on more recent forecasts, which should be provided by FPL in 2019 prior to approval of the project. (TR 3744-3745) Further, the rate base revenue requirement should be adjusted as set forth in Issues 124, 129, and 131.

<u>ISSUE 129</u>: What is the appropriate weighted average cost of capital, including the proper components, amounts and cost rates associated with the capital structure, to calculate the limited scope adjustment for the new Okeechobee Energy Center?

POSITION: *No mid-2019 step increase is warranted nor should it be granted. However, if one is considered, it is appropriate to use the OPC's adjusted 2018 cost of capital as a proxy rate of return. The resultant overall cost of capital is 5.17%.*

ARGUMENT:

For the reasons set forth in Issue 124, no mid-2019 step increase is warranted nor should it be granted. If the Okeechobee LSA is considered, then the projected rate base should be based on OPC's overall recommended 2018 rate of return. (TR 3745)

In calculating the contingent revenue requirement for the June 1, 2019 LSA, FPL based its calculation of the increase on an overall rate of return of 8.87%. (TR 3744, 3746) Witness Smith testified that he reproduced how FPL developed its proposed overall rate of return based on the following hypothetical capital ratio: 39.61% for long-term debt, 60.39% for equity, 4.87% for long-term debt, and an 11.50% rate of return on equity. (TR 3746) FPL did not include any deferred income taxes, customer deposits, or investment tax credits in its cost of capital for the LSA. (TR 3746) Witness Smith testified that it is not appropriate to use a different capital structure and overall rate of return to calculate the revenue requirement associated with the Okeechobee LSA. (TR 3746) Since FPL did not provide the projected amounts for the total cost of capital as of June 2019 in its MFRs for the Okeechobee LSA, he did not have a reasonable basis to determine or project the amounts necessary to calculate the overall cost of capital uses. (TR 3746) Therefore, Witness Smith used as an appropriate proxy the OPC adjusted 2018 cost of capital for a rate of return. (TR 3746-3747) Based on this 2018 cost of capital, Witness Smith calculated an overall cost of capital of 5.17%. (TR 3746-3747; HE 191, HE 192)

Witness Barrett testified that the cost assumptions used in developing the base revenue requirements for the 2019 Okeechobee LSA are based on the Commission Need Determination Order No. PSC-16-0032-FOF-EI. He stated that the base revenue requirements reflect the first-year return on and of the capital investment in the Okeechobee Unit along with all non-fuel operating costs and taxes. (TR 1403) Witness Smith noted MFR Schedule D-1a-June 2019 Step Increase shows that the capital structure reflects the incremental sources of capital consistent with the analysis submitted in connection with FPL's need determination proceedings. (TR 3747) However, FPL's explanation for the use of a different capital structure for 2018 was not supported by their explanation. (TR 3747-3748)

Witness Smith stated it was his understanding that for this type of step increase, the Commission in the past has relied on authorized overall rate of return approved in the base rate case. (TR 3747) He noted in Order No. PSC-12-0179-FOF-EI, issued April 3, 2012, in the Gulf Power rate case, the Commission applied the authorized overall rate of return from the base rate case for the January 2013 step increase for Crist Units 6 & 7 turbine upgrades projects. (TR 3747) Witness Smith further noted that in Order No. PSC-09-0283-FOF-EI, issued April 30,2009, in the TECO rate case, the Commission also applied the authorized overall rate of return from the base rate case for the January 2010 step increase for the five combustion turbines units. (TR 3747-3748)

Therefore, based on Witness Smith's recommended adjustments, in the event the Commission considers the step increase, the appropriate amount for the June 2019 LSA is $145 million, which is $64 million less than the $209 million requested by FPL in its original filing. (TR 3751) Witness Smith's calculation is based on OPC's adjusted overall cost of capital of 5.17%. (TR 3751)

<u>ISSUE 130</u>: Is FPL's requested net operating loss of $33.868 million for the new Okeechobee Energy Center appropriate?

POSITION: * A mid-2019 Okeechobee LSA is not warranted nor should it be granted. If considered, then OPC's 2018 ROR should be used; the operating costs associated with the project should be updated based on more recent forecasts; and start-up costs included in FPL's projects should be removed to normalize costs and exclude one-time, non-recurring costs. Applying OPC's recommended adjustments results in a LSA of $145 million, $64 million less than the $209 million LSA FPL requested. *

ARGUMENT:

For the reasons set forth in Issues 124 and 129, no mid-2019 step increase is warranted nor should it be granted. If the Okeechobee LSA is considered by the Commission, then the projected rate base should be based on OPC's overall recommended 2018 rate of return. (TR 3745) Therefore, based on Witness Smith's recommended adjustments, in the event the Commission considers the step increase, the appropriate amount for the June 2019 LSA is $145 million, which is $64 million less than the $209 million requested by FPL in its original filing. (TR 3751) Witness Smith's calculation is based on OPC's adjusted overall cost of capital of 5.17%. (TR 3751)

ISSUE 131: What is the appropriate Net Operating Income Multiplier for the new Okeechobee Energy Center? (Fallout)

POSITION: *A mid-2019 step increase is not warranted nor should it be granted. However, if the Okeechobee LSA is considered, then the appropriate Net Operating Income Multiplier should be 1.63024. (Smith)*

ARGUMENT:

For the reasons set forth in Issues 124 and 129, no mid-2019 step increase is warranted nor should it be granted. If the Okeechobee LSA is considered, then the projected rate base should be based on OPC's overall recommended 2018 rate of return. (TR 3745) However, if the Okeechobee LSA is considered, then the appropriate Net Operating Income Multiplier should be 1.63024. (HE 192)

ISSUE 132: Is FPL's requested limited scope adjustment of $209 million for the new Okeechobee Energy Center appropriate?

POSITION: *A mid-2019 Okeechobee LSA is not warranted nor should it be granted. If considered, then OPC's 2018 ROR should be used; the operating costs associated with the project should be updated based on more recent forecasts; and start-up costs included in FPL's projects should be removed to normalize costs and exclude one-time, non-recurring costs. Applying OPC's recommended adjustments results in a LSA of $145 million, $64 million less than the $209 million LSA FPL requested. *

ARGUMENT:

For the reasons set forth in Issues 124 and 129, no mid-2019 step increase is warranted nor should it be granted. If the Commission should consider the Okeechobee project, then the projected rate base should be based on OPC's overall recommended 2018 rate of return. In addition, the operating costs associated with the project should be updated and based on more recent forecasts, start-up costs included in FPL's projects should be removed to normalize costs and one-time, non-recurring costs should be excluded. (TR 3745) Therefore, based on Witness Smith's recommended adjustments, in the event the Commission considers the step increase, the appropriate amount for the June 2019 LSA is $145 million, which is $64 million less than the $209 million requested by FPL in its original filing. (TR 3751) His calculation is based on OPC's adjusted overall cost of capital of 5.17%. (TR 3751)

ISSUE 133: What is the appropriate effective date for implementing FPL's limited scope adjustment for the new Okeechobee Energy Center?

POSITION: *No 2019 Okeechobee LSA should be implemented. However, if the Okeechobee LSA is considered, then the effective date should be no sooner than the in-service date, and subject to verification by the Commission as to the reasonableness of the costs and projections used. (Smith)*

ARGUMENT:

For the reasons set forth in Issues 124 and 129, no mid-2019 step increase is warranted nor should it be granted. If the Commission considers the Okeechobee project, then the projected rate base should be based on OPC's overall recommended 2018 rate of return. In addition, the operating costs associated with the project should be updated and based on more recent forecasts, and start-up costs included in FPL's projects should be removed to normalize costs and one-time, non-recurring costs should be excluded. (TR 3745) Therefore, based on Witness Smith's recommended adjustments, in the event the Commission considers the step increase, the appropriate amount for the June 2019 LSA is $145 million, which is $64 million less than the $209 million requested by FPL in its original filing. (TR 3751) Witness Smith's calculation is based on OPC's adjusted overall cost of capital of 5.17%. (TR 3751) Further, the effective date should be no sooner than the in-service date of the project, and subject to verification by the Commission as to the reasonableness of the costs and projections used.

ASSET OPTIMIZATION INCENTIVE MECHANISM

ISSUE 134: Should the asset optimization incentive mechanism as proposed by FPL be approved?

POSITION: *No. The Commission should reject FPL's request to extend and recalibrate its modified incentive mechanism ("IM") program. Aside from any potential legal prohibitions, FPL has not demonstrated the proposed IM is in the public interest or has led to verifiable and positive changes in the Company's actions or how, if at all, those changes result in net public interest benefits above and beyond the Commission's long-standing off-system sales incentive policies. Further, due to the policy implications well beyond simple ratemaking, changes to the Commission's off-system sales incentive policy should be considered in a separate proceeding. (Dismukes)*

ARGUMENT:

FPL is seeking approval of the Incentive Mechanism ("IM") which was approved as a four-year pilot program in the 2012 Settlement. (TR 2053, Order No. PSC-13-0023-S-EI, issued January 14, 2013, in Docket No. 120015-EI). The 2012 IM allows the sharing of gains resulting from electric wholesale purchases and sales, and asset optimization. The asset optimization includes gas storage utilization, city-gate gas sales using existing transport, production area gas sales, capacity release of gas transport and electric transmission, and outsourcing of the optimization function. See Order No. PSC-13-0023-S-EI at p. 6. The threshold for customers receiving 100 percent of the gain was set at $46 million, $36 million (Customer Saving Threshold) and $10 million (Additional Customer Savings). Thereafter, the customers and FPL would share the gains as follows: 1) between $46 million and $100 million, customers receive 40 percent of the incremental gains; and 2) over $100 million, customers receive 50 percent of the incremental gains. Order No. PSC-13-0023-S-EI at pp. 6 and 7. The 2012 IM also allowed FPL to collect the reasonable and prudent incremental O&M costs for the program in the Fuel Clause. Id. at p. 7. In addition, the variable power plant O&M costs incurred to generate additional output in order to make wholesale sales would be included if the level of sales exceeds 514,000 MWh. Id.

FPL Witness Forrest acknowledged that the 2012 IM will automatically terminate at the end of 2016 unless authorized to continue as part of this base rate request. (TR 2053) FPL proposed to continue the 2012 IM with two modifications. First, FPL wants to lower the total customer sharing threshold from $46 million to $36 million due to the ending of a Unit Power Sales contract with Southern Company at the end of 2015. (TR 2054) Second, FPL proposes to eliminate the 514,000 MWh threshold before sharing of variable power plant O&M for Fuel Clause inclusion because FPL choose not to include any wholesale O&M in the base rate case filing. (TR 2054)

Issue 4 addresses the legal rationale for denying the extension of the request IM. In summary, under the rationale of Citizens v. Graham where the Florida Supreme Court noted that utilities do not earn a return on "fuel" and that capacity has been treated as part of the fuel clauses, it is highly arguable whether FPL has the statutory authority to earn a profit on these types of fuel clause activities. Id. at p. 10. Thus, OPC submits it would exceed the Commission's authority to approve activities for which FPL proposes to earn a return for non-electric transactions in an incentive mechanism.

Assuming arguendo that the Commission has the authority to approve an IM as requested by FPL, there are several policy reasons to deny FPL's request. First, OPC witness Dismukes testified that in his opinion the Company has failed to meet its burden of proof to demonstrate that the extension and proposed recalibration of its modified IM is in the public interest. (TR 3318) Witness Dismukes recommends that FPL should revert to the Commission's long-standing off-system sales incentive policies and allow the 2012 IM to lapse.

Based on his review of the information provided by FPL, Witness Dismukes found several areas where there was a dearth of information. Witness Dismukes identified the areas where the Company provided no substantive evidence to support continuing the IM: (1) the extent to which FPL's physical assets have been meaningfully and significantly optimized as a result of the modified IM; (2) the extent to which ratepayers will benefit form a continuation and recalibration of FPL's modified IM; and (3) the extent to which the modified IM represents a considerable improvement over the Commission's long-standing off-system sales mechanism. (TR 3319-3320) Witness Forrest argues that customers received $21.7 million of additional benefits under the 2012 IM as compared to what customers would have benefited under the Commission's long-standing incentive sales incentive policy. (TR 2059) However, he acknowledged that $33 million of the "additional" benefits over the three-year period were due to "optimization activities" under the 2012 IM, which should be disallowed pursuant to Citizens v. Graham. There is no evidence regarding the amount of "additional" benefits without the optimization activities. (TR 2059)

Furthermore, Witness Forrest did not identify or compare the economic purchase activities that are part of the "additional" benefits versus the Commission's long-standing off-system gain on sales mechanism. (TR 2056-2057) Although economic purchase activities were included as part of the 2012 IM, it is not appropriate to include economic purchase activities in any future IM. Economic purchases arise when a utility can purchase lower-cost electricity on the market rather than utilizing electricity generated from its own power plants. (TR 3356) As Witness Dismukes affirmed, a utility has an obligation to provide least-cost service. Public utilities have the statutory obligation to provide reasonably sufficient, adequate, and efficient service. See, Section 366.03, F.S. Witness Dismukes' interpretation of "efficient" from an economist's prospective means minimizing inputs for a given level of outputs, and minimizing inputs are minimizing costs. (TR 3437) Thus, a prudent utility would be expected to purchase electricity on the open market when it can do so at a lower cost than it would cost the utility to generate that same electricity.

Witness Dismukes further testified that allowing financial incentives from off-system purchases represents a radical departure from current Commission policy. He explained that allowing off-system purchases runs counter to the *quid pro quo* policy of reduced risk through the fuel clauses balanced with the expectation that a utility will secure the optimum least-cost, reliable resources on behalf of their ratepayers, regardless of whether those resources are self-generated, or come from the market. (TR 3360-3362) Further, several Commission rules explicitly identify as a requirement "least cost" such as in the Request for Proposal, Rule 25-22.082(4), F.A.C., and "equal or less than market" as in the affiliate rule, Rule 25-6.1351, F.A.C. FPL's off-systems purchase incentive runs contrary to the underlying policies in Florida Statutes and Commission Rules.

Witness Dismukes also testified regarding his concerns that the modified IM can lead to inappropriate incentives for over-development of capacity resources and, as a result, over-capitalization or inefficient capacity-related expenses. Witness Forrest implied that, since FPL did not renew its Unit Power Sales ("UPS") contract, this somehow demonstrates that Witness Dismukes' concerns relating to the over-development of capacity is unfounded. (TR 4693) However, Witness Dismukes testified that his concerns regarding an over-capacity incentive went beyond longer-term purchase power agreements ("PPA") and actually looked more on the physical development side (i.e., building generation). (TR 3431)

In addition, Witness Dismukes discussed that the modified IM has anti-competitive market implications including the potential to: (1) use of regulated assets and vertical market power to create an unfair competitive advantage in competitive wholesale energy market transactions; (2) the creation of an unequal playing field between FPL and the state's other IOUs; and (3) the creation of an unequal playing field between FPL and other competitive energy marketers. (TR 3320) He also stated there were potentially other anti-competitive issues could arise.

Second, Witness Dismukes identified concerns with affording the parties enough time to review the broad policy implications of an IM, particularly as it relates to the other Florida electric utilities, in lieu of approving the modified IM in this current proceeding. (TR 3319) Dr. Dismukes noted that in the past, the Commission has recognized the larger policy implication ramifications of such incentive mechanisms, including the impacts on existing and emerging markets and resource efficiency. (TR 3319, 3324-3325) If the Commission were inclined to explore the proposed IM, rather than allowing it to terminate, then a separate proceeding with the other state electric utilities and stakeholders should be held. (TR 3319) Witness Forrest argued that the amount of discovery undertaken and ability to conduct audits negates the need for a separate proceeding. (TR 4687-4689) However, Witness Dismukes testified that the audits would not change his opinion of the modified IM. (TR 3436) Further, Witness Forrest did not address the broader ramification of continuing the modified IM with regard to the other Florida IOUs. As Witness Dismukes correctly points out, the 2012 IM was part of a larger settlement and from a policy perspective there is nothing in the original settlement suggesting that the modified IM, on its own, is in the public interest. (TR 3365-3366) As such, the modified IM should be denied and FPL should be allowed to revert to the Commission's long-standing gain on off-system sales mechanism. Prior to the Commission considering approval on any of the additional IM activities, a separate proceeding with all the Florida electric utilities and stakeholders should be held.

COST OF SERVICE AND RATE DESIGN ISSUES

ISSUE 139: Is FPL's proposal to recover a portion of fixed distribution costs through the customer charge instead of energy charge appropriate for residential and general service non-demand rate classes?

POSITION: *No, FPL's proposal to shift $2.00 from energy charge to fixed distribution costs is not appropriate and should not be approved.*

ARGUMENT:

FPL witness Tiffany Cohen testified that FPL is proposing to increase by $2.00 the customer charge for residential (RS-1) and non-demand General Service rate class (GS(T)). (TR 2815) Witness Cohen states that over 80 percent of FPL's costs recovered through base rates are fixed costs but only 26 percent of these fixed costs are recovered through a fixed charge (i.e. the customer charge). (TR 2815) Witness Cohen argues that under traditional ratemaking principles, costs that do not vary with the amount of electricity used (fixed costs) are recovered through fixed charges and costs that vary with the amount of electricity used (variable costs) are generally recovered through variable demand and energy charges. (TR 2815) However, this is not how FPL's rates are currently designed.

As Witness Cohen admits, 80 percent of what she terms as fixed costs are currently being adequately recovered through the energy and demand charges. FPL has not met its burden to demonstrate that there is a need to change the established rate structure. In fact, under its current rate design, FPL has been earning at or near the top of its range for the last four years. (HE 573) The only proof Witness Cohen offers is a recitation of her understanding of "traditional ratemaking principles." However, the current rate design approved by the Commission in FPL's last rate case rebuts her supposition that fixed costs are only appropriately recovered through fixed charges. See Order PSC-13-0023-S-EI, issued January 14, 2013, in Docket No. 120015-EI. As Witness Cohen conceded, if the Commission were not to approve shifting $2.00 from the energy charge (variable rate) to the customer charge (fix rate), FPL would still collect the necessary revenues through the energy charge. (TR 2831)

<u>ISSUE 140</u>: How should the change in revenue requirement be allocated to the customer classes?

POSITION: *The revenue requirement approved by the Commission should be applied in accordance with the Commission's long-standing practice in designing new rates. See, Order No. PSC-09-0283-FO-EI at pp. 86-87.*

ARGUMENT:

The revenue requirement approved by the Commission should be applied in accordance with the Commission's long-standing practice in designing new rates. As noted by the Commission in the TECO rate case, in designing new rates: (1) to the extent possible, consistent with other parameters, the revenue increase should be allocated so as to bring all rate classes as close to parity as practicable; (2) no class should receive an increase greater than 1.5 times the system average increase in total; and (3) no class should receive a decrease. See, Order No. PSC-09-0283-FO-EI at pp. 86-87.

<u>ISSUE 146</u>: What are the appropriate customer charges?

A. Effective January 1, 2017?

POSITION: *The appropriate customer charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.*

ARGUMENT:

The appropriate customer charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.

B. Effective January 1, 2018?

POSITION: *No change is appropriate for 2018.*

ARGUMENT: No change is appropriate for 2018.

<u>ISSUE 147</u>: What are the appropriate demand charges?

A. Effective January 1, 2017?

POSITION: *The appropriate demand charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.*

ARGUMENT:

The appropriate demand charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.

B. Effective January 1, 2018?

POSITION: *No change is appropriate for 2018.

ARGUMENT:

No change is appropriate for 2018.

<u>ISSUE 148</u>: What are the appropriate energy charges?

A. Effective January 1, 2017?

POSITION: *The appropriate energy charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.*

ARGUMENT:

The appropriate energy charge should be based on OPC's recommend revenue requirement and rates that implement the Commission's long-standing practice for establishing new rates as stated in Issue 140.

B. Effective January 1, 2018?

POSITION: *No change is appropriate for 2018.*

ARGUMENT: No change is appropriate for 2018.

<u>ISSUE 156</u>: Is FPL's proposed allocation and rate design for the new Okeechobee Energy Center limited scope adjustment, currently scheduled for June 1, 2019, reasonable?

POSITION: *No, for the reasons stated in Issues 124-133.*

ISSUE 157: Should FPL's proposal to file updated base rates in the 2018 Capacity Clause proceeding to recover the Okeechobee Energy Center limited scope adjustment be approved?

POSITION: *No, for the reasons stated in Issues 124-133.*

ISSUE 160: Should the Commission give staff administrative authority to approve tariffs reflecting Commission approved rates and charges effective January 1, 2017, January 1, 2018, and tariffs reflecting the commercial operation of the new Okeechobee Energy Center (June 1, 2019)?

POSITION: *Yes for 2017. No, for 2018 (See Issue 27) and no for the Okeechobee Energy Center for the reasons stated in Issues 124-133.*

ISSUE 161: What are the effective dates of FPL's proposed rates and charges?

POSITION: *The effective date for the 2017 rate change should be January 2, 2017.*

OTHER ISSUES

ISSUE 162: Should the Commission approve FPL's proposal to transfer the Martin-Riviera pipeline lateral to Florida Southeast Connection (FSC)?

POSITION: *If the Commission approves the proposed transfer of the Martin-Riviera pipeline lateral to Florida Southeast Connection, the impact to FPL ratepayers should be revenue neutral.*

ARGUMENT:

If the Commission approves the proposed transfer of the Martin-Riviera pipeline lateral to Florida Southeast Connection, the impact to FPL ratepayers should be revenue neutral.

<u>ISSUE 163</u>: What requirements, if any, should the Commission impose on FPL if it approves FPL's proposed transfer of the Martin-Riviera pipeline lateral to Florida Southeast Connection?

POSITION: *If the Commission approves the proposed transfer of the Martin-Riviera pipeline lateral to Florida Southeast Connection, the Commission should impose requirements that make the impact to FPL ratepayers revenue neutral.*

ARGUMENT:

If the Commission approves the proposed transfer of the Martin-Riviera pipeline lateral to Florida Southeast Connection, the Commission should impose requirements that make the impact to FPL ratepayers revenue neutral.

<u>ISSUE 164</u>: Did FPL's Third Notice of Identified Adjustments remove the appropriate amount associated with the Woodford project and other gas reserve costs?

POSITION: *FPL has the burden to show that it made the adjustments to remove the appropriate amounts associated with the Woodford project and other gas reserve costs.*

<u>ISSUE 166</u>: Should a mechanism be established to capture for the benefit of ratepayers savings, if any, that result from any mergers, acquisitions or reorganizations by NextEra Energy?

POSITION: *Yes, a mechanism should be established, if it does not already exist, to allocate benefits of any mergers, acquisitions or reorganization by NextEra Energy.*

ARGUMENT:

Yes, a mechanism should be established, if it does not already exist, to allocate benefits of any mergers, acquisitions or reorganization by NextEra Energy.

ISSUE 167: Should this docket be closed?

POSITION: *No position.*

Dated this 19th day of September, 2016

Respectfully submitted,

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CERTIFICATE OF SERVICE
Docket No. 160021-EI

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by electronic mail on this 19th day of September, 2016, to the following:

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