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BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of	Docket No. 890148-EI
Petition of the Florida Industrial Power Users Group to Discontinue Florida Power and Light Company's Oil Backout Cost Recovery Factor.	HEARING SECOND DAY - MORNING SESSION VOLUME - III Pages 328 through 494

FPSC Hearing Room 106
Fletcher Building
101 East Gaines Street
Tallahassee, Florida 32399-0871

Wednesday, August 23, 1989

Met pursuant to notice at 9:30 a.m.

BEFORE: COMMISSIONER MICHAEL McK. WILSON, Chairman
COMMISSIONER GERALD L. GUNTER
COMMISSIONER JOHN T. HERNDON
COMMISSIONER THOMAS M. BEARD
COMMISSIONER BETTY EASLEY

APPEARANCES:

(As heretofore noted.)

REPORTED BY: CAROL C. CAUSSEAUX, CSR, RPR
and
JOY KELLY, CSR, RPR

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P R O C E E D I N G S

(Hearing reconvened at 9:30 a.m.)

CHAIRMAN WILSON: We will call the hearing to order.

MR. GUYTON: We call Mr. Waters to the stand.

CHAIRMAN WILSON: Mr. Waters has been previously sworn?

MR. GUYTON: I believe he has. Mr. Chairman, before we started Mr. Waters, yesterday I handed out FIPUG's responses to FPL"s First Request for Admission and FPL's Second Request for Admission. I don't believe we marked that and perhaps it would be appropriate to do so.

CHAIRMAN WILSON: Let me find it first. (Pause) All right. What would be the number?

MR. PRUITT: The first one would be 211 and the second one would be 212.

CHAIRMAN WILSON: All right. 211 and 212. No. 211 is FPL's First Request for Admissions and 212 is the Second Request for Admissions.

(Exhibit Nos. 211 and 212 marked for identification.)

CHAIRMAN WILSON: And I commend the Company for using the Request for Admissions. I have been urging the use of that technique for a number of years to cut down on the amount of interrogatories and other data that very often is entered into the record in Commission proceedings. This seems to me like a much more economic method for getting information into the record.

SAMUEL S. WATERS

appeared as a witness on behalf of Florida Power and Light Company and, having been first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. GUYTON:

Q Would you state your name?

A My name is Samuel S. Waters.

Q By whom are you emploveed and in what capacity?

A I am employed by Florida Power and Light Company as the Manager of Power Supply Planning.

Q Mr. Waters, have you filed prefiled direct testimony in this proceeding consisting of some 29 typewritten pages dated July 13th, 1989?

A Yes, sir, I have.

Q Mr. Waters, have you had cause to pass out this morning an errata sheet to that direct testimony?

A Yes, I have.

Q Mr. Waters, do you have any corrections to make to the errata sheet?

A Yes, I have errata to the errata sheet. The last line of the errata sheet that says "Document 4, Line P," should say, "Document 4, Page 1 of 2, Line P."

COMMISSIONER HERNDON: I'm still looking for where I am supposed to change the P to a 3.

MR. GUYTON: Commissioner, that's the last line of the first page of the errata.

COMMISSIONER HERNDON: I know, I've got that, but I am looking for the actual --

MR. GUYTON: On the left hand margin where it says "Document 4, Line P."

CHAIRMAN WILSON: Document 4, Page 1 of 2 or Page 2 of 2?

WITNESS WATERS: Page 1 of 2.

MR. GUYTON: Right, Page 1 of 2.

WITNESS WATERS: After the equation, B-C+D.

COMMISSIONER HERNDON: Over on the errata sheet, can you explain to me what changing parentheses to brackets means?

MR. GUYTON: Yes, sir. In the quotation where that appears on Page 11, Line 19?

COMMISSIONER HERNDON: Right. Oh, that's a quote, there is no quotation marks around mine so I didn't realize it was a quote.

MR. GUYTON: Right. That is a quotation and we want to clearly indicate that that is an editorial insertion.

COMMISSIONER HERNDON: Okay. Now I understand what you are doing.

Q (By Mr. Guyton) Mr. Waters, with those corrections, as are reflected on your errata sheet and your testimony this morning, if you were asked the same questions that appear in your direct testimony would your answers be the same?

A Yes, they would.

COMMISSIONER EASLEY: Hold it just a moment. On the errata on rebuttal -- have you done both of them?

MR. GUYTON: No, ma'am, I have not done rebuttal yet.

COMMISSIONER EASLEY: Excuse me. Never mind.

Q (By Mr. Guyton) With those corrections, do you adopt your prefiled testimony?

A Yes, I do.

MR. GUYTON: Mr. Chairman, we would ask that Mr. Waters' prefiled direct testimony be inserted into the record as though read.

CHAIRMAN WILSON: Without objection, his prefiled direct testimony will be inserted into the record, and I would ask you to provide corrected pages for the court reporter with those -- well, the corrected pages to the testimony.

MR. GUYTON: We will do so, Mr. Chairman.

Q (By Mr. Guyton) As part of your direct testimony, and attached thereto, did you file an exhibit in this proceeding?

A Yes, I did.

Q And has that been identified in the Prehearing Order as Exhibit No. 208?

A Yes, sir.

Q Your errata sheet also indicates any corrections that are necessary to that exhibit?

A Yes. The last change on the errata sheet is a change to the exhibit.

Q With those corrections, do you believe that the information contained in your exhibit is true and correct to the best of your knowledge and belief?

A Yes, I do.

(Exhibit No. 208 marked for identification.)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

TESTIMONY OF SAMUEL S. WATERS

DOCKET NO. 890148-EI

JULY 13, 1989

Q. Please state your name and business address.

A. My name is Samuel S. Waters and my business address is 9250 West Flagler Street, Miami, Florida 33174.

Q. By whom are you employed and what position do you hold?

A. I am employed by Florida Power & Light Company ("FPL") as the Manager of Power Supply Planning.

Q. Please describe your education and professional experience.

A. I graduated from Duke University with a Bachelor of Science Degree in Electrical Engineering in 1974. From 1974 until 1985, I was employed by the Advanced Systems Technology Division of Westinghouse Electric Corporation as a consultant in the areas of Transmission Planning and Power System Software. While employed at Westinghouse, I earned a Masters Degree in Electrical Engineering from Carnegie-Mellon University.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address several issues in the Florida Industrial Power Users Group's (FIPUG) Petition to Discontinue FPL's Oil Backout Cost Recovery Factor. The Petition erroneously contends that FPL's 500 KV Transmission Project ("Project") has not achieved its purpose, and that the claimed capacity deferral benefits of the Project are illusory because they are based on fictional units. My testimony discusses these issues as they relate to the Project and the associated capacity purchases, or Unit Power Sales ("UPS"), from the Southern Companies and their consideration in the Oil Backout Cost Recovery Factor.

First, I will describe the Project and the associated purchases. I explain how the Project revenue requirements, the capacity charges paid to the Southern Companies and more recently, net savings, have been recovered through the Oil Backout Cost Recovery Factor. I also present a brief historical overview of the Project, including a discussion of original qualification and subsequent regular review by the Commission.

Second, my testimony reestablishes the fact that the Project and the associated power purchases from Southern Company meet the primary purpose of economically displacing oil-fired generation. This was demonstrated to the Commission using the Primary Purpose Test in the original qualification proceedings. The Project continues to meet the Primary Purpose Test, even when viewed in light of significantly lower oil prices than originally projected. In reviewing this test, I discuss why inclusion of the UPS capacity payments in the performance of the test is incorrect.

Third, I also discuss, in general terms, how the planning process identifies the need for capacity and the timing of decisions required to meet future needs. I discuss how capacity deferral benefits have been used by FPL to calculate and recover savings accruing from the Project and UPS purchases through the Oil Backout Cost Recovery Factor since 1987. In this discussion, I show how these savings are associated with the deferral of Martin Coal Unit Nos. 3 and 4, and that these units were, in fact, deferred by the Project.

Finally, I will present my conclusions regarding the impact of the Project and the propriety of its cost recovery through the Oil Backout Cost Recovery Factor.

Q. Do you have any documents attached to your testimony?

A. Yes. Attached to my testimony are Document Nos. 1 through 4.

Project Overview

Q. Please describe FPL's 500 KV Transmission Project, which is being recovered through the Oil Backout Cost Recovery Factor.

A. The Project is comprised of two 500 KV transmission lines and associated substation facilities. The Project runs along the Florida east coast from the Georgia-Florida state line to the Martin and Midway substations in Martin and St. Lucie Counties, respectively. There, the lines tie into other portions of FPL's 500 KV network, which extends to Dade County and the west coast of Florida. The substation facilities in the Project integrate the Project with FPL's other 500 KV lines and FPL's 230 KV transmission system. My Document No. 1 contains a graphic showing FPL's 500 KV Transmission Project.

Q. Please explain how the Project was built.

A. The Project was built in three phases, with varying completion dates for specific Project elements. The construction phasing allowed earlier and fuller utilization of the UPS purchases. The Project phases were consistently completed at or ahead of schedule, thereby reducing Project revenue requirements. My Document No. 2, which relies in part on Mr. Scalf's Project Description in the original certification proceeding, shows the phasing of the Project, the scheduled completion dates and the actual completion dates.

Q. You state that the Project was constructed ahead of schedule; how do the Project's actual construction costs compare to those projected by FPL in the certification proceeding?

A. Quite favorably. FPL originally projected that the investment in the Project, when fully completed, would be $484,109,000. FPL's actual construction cost and investment in the Project was $326,020,276 when the last segment was brought on-line in June, 1985.

Q. Please describe the UPS power purchases associated with the Project.

A. In the Project's qualification proceeding, FPL explained that the development of the 500 KV Transmission Project was related to UPS purchases from the Southern system. Southern had offered for sale, from the early 1980's through the mid-1990's, power generated at coal-fired power plants in their system. With FPL's major load centers in South Florida, to take advantage of this coal-fired power, FPL and Southern would have to transmit the power from the Southern Companies' power plants to FPL load centers through high voltage transmission lines.

As Mr. Scalf explained in the qualification proceeding, the UPS agreement with the Southern Companies provided for increased purchases from relatively small amounts in mid-1982 to significant levels in 1985 through 1992. Then, as the Southern Companies' load increased in the 1990's, needing the UPS capacity for their own use, the purchases decreased between 1993 and 1995, with the UPS purchases ending in May, 1995.

Q. Are the costs of the UPS purchases recovered through FPL's Oil Backout Cost Recovery Factor?

A. Yes, in part. In the original proceeding authorizing FPL to recover costs through its Oil Backout Cost Recovery Factor, the Commission authorized the recovery of the capacity and wheeling charges associated with FPL's UPS purchases. In Order No. 11210, the Commission stated:

> The primary purpose of the 500 KV transmission project, as determined in the qualification hearings, is economic oil backout. Savings associated with the importation of coal by wire over the 500 KV transmission project could not be obtained without paying capacity and wheeling charges to Southern Company. Hence, capacity and wheeling charges should be collected through either the Fuel Adjustment Factor or the Oil Backout Cost Recovery Factor. . . . We find that the capacity and wheeling charges should be collected through the Oil Backout Cost Recovery Factor to reduce confusion and to facilitate the review of costs being recovered by the Company.

Consistent with this decision in September, 1982, in each subsequent recovery proceeding FPL has sought and the Commission has approved recovery of the UPS capacity and wheeling charges through the Oil Backout Cost Recovery Factor. Energy costs associated with the UPS purchases are recovered through FPL's Fuel and Purchased Power Cost Recovery Factor ("Fuel Clause").

Q. Please summarize the 500 KV Transmission Project Oil Backout Qualification Proceeding.

A. FPL initiated that proceeding on March 30, 1982 by filing with the Commission a petition seeking authority to recover the cost of the proposed Project through an Oil Backout Cost Recovery Factor. Both FIPUG and the Office of Public Counsel ("Public Counsel") intervened and actively opposed FPL's petition. After hearings in June, July and August, 1982, the Commission issued on October 1, 1982 a detailed order, Order No. 11217, finding that FPL's 500 KV Transmission Project qualified for recovery under an Oil Backout Cost Recovery Factor.

Both Public Counsel and FIPUG sought reconsideration of Order No. 11217. The Commission denied reconsideration in Order No. 11537 issued on January 24, 1983.

In the meantime, the Commission had issued Order No. 11210 authorizing FPL to begin recovery of the Project and the associated UPS capacity and wheeling charges through an approved Oil Backout Cost Recovery Factor. FIPUG and Public Counsel participated actively in that proceeding as well, opposing recovery of the Project through an Oil Backout Cost Recovery Factor.

Public Counsel appealed both Order No. 11210, the order approving recovery and Order No. 11217, the order finding the project qualified, to the Florida Supreme Court. On April 12, 1984, the Supreme Court issued its decision in Citizens v. Public Service Commission, 448 S.2d 1024, affirming both orders of the Commission.

Q. **What costs does FPL recover through its Oil Backout Cost Recovery Factor?**

A. In addition to the UPS capacity and wheeling costs previously discussed, FPL recovers revenue requirements on its Project. FPL has also been recovering and taking as accelerated depreciation on the Project, two-thirds of the actual net savings experienced as a result of the Project. As I discuss later in my testimony, these actual net savings reflect, among other things, capacity deferral benefits associated with Martin Unit Nos. 3 and 4, two coal units deferred by the Project, and the related UPS purchases from the Southern Companies.

Q. How often does the Commission consider FPL's recovery of costs through the Oil Backout Cost Recovery Factor?

A. The Commission has reviewed the computation and approved a factor every six months since the original decision in September, 1982 allowing FPL to begin recovery through the factor. This is done as part of the Commission's ongoing Fuel Clause hearings. FPL has always supported the computation of its factor with prefiled testimony. As in the case of the Fuel Clause Proceeding, the Oil Backout Cost Recovery Factor is subject to true-up calculations to assure an accurate recovery of costs from ratepayers. In addition, in FPL's last rate case, FPL requested that the Commission remove the recovery of some Project revenue requirements from the factor and place them in base rates. The Commission specifically declined to do this. There has been regular, formal Commission scrutiny of FPL's recovery of costs through the Oil Backout Cost Recovery Factor.

Primary Purpose - Economic Oil Displacement

Q. What is the primary purpose of the Project?

A. The primary purpose of the Project is economic displacement of oil-fired generation. Proof of this purpose was required by the Commission to qualify the project for cost recovery under the Oil Backout Cost Recovery Factor rule.

In its adoption of the Oil Backout Cost Recovery Factor rule, the Commission stated in Order No. 10554 that: "Rule 25-17.16 is intended to be used by investor owned electric utilities for the recovery of costs of implementing specified supply side conservation measures which will economically displace oil generated electricity." Similar language regarding the necessary primary purpose of an Oil Backout Project is found in the Rule itself. Section (2)(a) of the Rule states:

> (a) The Oil Backout Cost Recovery Factor is to be utilized for the recovery of costs of implementing any of the following supply side, oil conservation measures the primary purpose of which is the economic displacement of oil generated electricity in Florida . . . .

Among the supply side, oil conservation measures specifically listed is "Transmission Line Construction Cost . . . . when the primary purpose the construction of the lines is to increase the importation or transfer of non-oil derived electrical energy on either a firm or non-firm basis." Consistent with these statements that the primary purpose of a project must be economic oil displacement, Section (3)(a)1. provides that for a project to qualify for recovery through the Oil Backout Cost Recovery Factor, the Commission must have made a finding that: "The primary purpose of the proposed project is the economic displacement of oil fired generation in the State of Florida."

Q. How was the determination made that the primary purpose of FPL's Project was the economic displacement of oil-fired generation?

A. The Commission has established a means of testing that issue. In the final order in the Project's qualification proceeding, Order No. 11217, the Commission devoted an entire section to the discussion of "The Primary Purpose Test." FPL proposed, and the Commission Staff supported, a Primary Purpose Test which was met if gross fuel savings expected from the Project outweighed all other gross savings on a net present value basis. Neither FIPUG nor Public Counsel proposed a test, but Public Counsel, based on an examination of system expansion plans and projected oil usage, argued that FPL's Project and the related unit power purchases were primarily intended to meet load growth rather than displace oil. The Commission rejected these alternatives and stated:

> In our mind, the issue [determination of primary purpose] is best resolved by allocating the fuel costs of the project against the fuel savings and the capacity costs of the project against the capacity savings. We think it proper to allocate costs and benefits in this case because the Company could have purchased the coal by wire power on a non-firm basis, thereby avoiding the

> capacity costs due Southern but also foregoing the deferred capacity benefits.

Having stated that UPS capacity costs should not be allocated against fuel savings in determining the Project's primary purpose, the Commission specifically embraced a methodology for determining whether the Primary Purpose Test was satisfied:

> If the net fuel savings exceed the cost of the Project, the Company has met its burden of proof on this issue and demonstrated that the primary purpose of the Project is oil displacement. The Company has done this in Exhibit 15(j).

Q. **Have you examined Exhibit 15(j) from the Qualification Proceeding?**

A. Yes. I have attached a copy of the original Exhibit 15(j) and a supporting schedule in Docket No. 820155-EU as my Document No. 3. As stated in Commission Order No. 11217, this exhibit reflects the methodology used by the Commission in determining whether or not a project meets the Primary Purpose Test. That is, for the first ten years of the Project, net fuel savings are compared to Project revenue requirements.

Q. Given this specific statement and application of the Primary Purpose Test, has the FIPUG petition properly determined whether or not the project has achieved its primary purpose?

A. No, it has not. In contending that the Project has not met its purpose, FIPUG has attached a schedule to its Petition, Schedule 2 which improperly includes the capacity charges associated with the UPS agreement with Southern Company. This severely distorts the original Commission test. FIPUG erroneously compares net fuel savings to project revenue requirements **plus UPS costs**. By misstating the test and erroneously including UPS capacity costs, FIPUG makes it appear that the project results in a loss. In fact, the Project has produced net fuel savings as well as actual total savings. If the Primary Purpose Test had been performed in FIPUG's manner in the original qualification proceedings, the Project would not have passed.

Q. If UPS capacity costs were not considered in the Commission's Primary Purpose Test, how were they considered in the qualification proceeding?

A. UPS capacity costs were considered in a separate test, the Cumulative Present Value Test. In that test, the Commission recognized not only the UPS capacity costs, but also the capacity deferral benefits associated with the Project and the importation of coal by wire. It is quite clear from the application of the tests in the qualification order that the Commission intentionally segregated energy costs and savings from capacity costs and savings in applying the Primary Purpose Test and recognized both capacity costs and savings in the Cumulative Present Value Test.

Q. **What about FIPUG's contention in its Petition that the Project has failed to meet its principal purpose due to lower than projected oil prices and that the Commission relied on FPL's forecast to qualify the Project?**

A. Neither is true. Because of the recognized uncertainty in projecting oil prices, three oil price forecasts were presented in the original qualification proceeding; a high band forecast, prepared by the Department of Energy, a mid band forecast, prepared by the Florida Power Electric Coordinating Group, Inc. (FCG) and a low band forecast, prepared by FPL and characterized as "conservative." The relevant coal price forecast was provided by the Southern Companies. In Order No. 11217, the Commission stated:

> Based on the evidence before us, we find that the fuel price forecasts are reasonable and are of sufficient reliability to warrant their use as the starting point for our determination that the project qualifies under the rule.

FPL was straightforward in acknowledging the difficulty in accurately projecting oil prices. It is clear from a review of the transcript that the Commission was fully apprised of the probability that actual experience would deviate from the projections and that the deviation might be substantial.

Oil prices have, in fact, been lower than any of the forecasts used in the original qualification. However, the original intent of presenting a banded forecast was to present a range of possible outcomes, and it was FPL that produced the low band forecast. More importantly, even with actual oil prices lower than those originally projected, the Project has economically displaced oil fired generation.

Q. Does the Project still pass the Primary Purpose Test, using actual data and current forecasts?

A. Yes, however, I would like to add that I do not think it is proper to "requalify" a project. Decisions on whether to qualify a project for Oil Backout Cost Recovery should be made based on the best available information at the time qualification is sought. That is the time when project decisions must be made, information justifying the project is readily available and the Commission is fully apprised of current circumstances affecting a project. Requalification or reevaluation of qualification through hindsight, as FIPUG appears to want to do, is difficult and unfair.

However, putting aside whether it is fair to reconsider Project qualification, it is important in light of FIPUG's allegations for the Commission to know that the Project still passes the Primary Purpose Test. **Despite significantly lower oil prices than originally projected, the Project has produced and is still producing net fuel savings which exceed the revenue requirements of the Project.**

I have repeated the original Primary Purpose Test updating with actual data through May, 1989 and using current FPL projections of fuel prices. As with the original Exhibit 15(j), this analysis is performed over the initial ten years of the Project. The results are attached as Document No. 4. Referring to the document, the test adds direct fuel savings of $1,840,852,000 and fuel related savings of ($393,121,000), then subtracts the foregone benefit of lower system fuel costs if the Martin units had been built as originally planned, $796,424,000, to yield a total fuel savings of $651,307,000. This is well above the total ten year Project revenue requirements of $295,754,000.

The contention by FIPUG that the project has not achieved its purpose is untrue. It is the misapplication of the Primary Purpose Test by FIPUG, not lower oil prices, which results in their contention that the project does not meet its purpose.

Actual Net Savings - Deferral Of Martin Unit Nos. 3 And 4

Q. Has FPL collected any revenues for the project which have resulted from actual net savings?

A. Yes. As authorized by the Rule, and as determined appropriate by the Commission in Order Nos. 18136, 19042, 20133 and 20966, FPL has and is collecting revenues above Project revenue requirements because the project has produced net savings.

Section (4)(a) of the Rule authorizes collection of revenues equal to:

- Straight line depreciation, plus
- Project cost of capital, plus
- Actual tax expense, plus
- Oil/non-oil O&M differential, plus
- Two-thirds of the actual net savings (if positive)

The amount identified as two-thirds of the actual net savings is recovered through the Oil Backout Cost Recovery Factor and applied as additional depreciation. This recovery is to continue until the Project investment is fully recovered.

Q. How were actual net savings derived in each of the instances?

A. The specific methodology for determining the actual net savings for inclusion in FPL's Oil Backout Cost Recovery Factor was presented in D. L. Babka's testimony in Docket Nos. 870001-EI and 880001-EI. The methodology was the same in all cases and part of the calculation included deferred capacity benefits associated with the Martin coal units. The Martin coal units were deferred as a result of the Project and the related UPS agreement with the Southern Companies.

Q. When did capacity deferral benefits first appear in FPL's calculation of net savings in an FPL Oil Backout filing?

A. The first time capacity deferral benefits were projected in an FPL Oil Backout filing was in FPL's January, 1987 testimony for the April, 1987 - September, 1987 recovery period in Docket No. 870001-EI. The capacity deferral benefits were the result of the deferral of Martin Coal Unit No. 3, which would have been placed in service in June 1987, without the purchases from the Southern Companies. Although the recognition of capacity deferral benefits did not produce net savings in the projection of the April, 1987 - September, 1987 period, neither FIPUG nor Public Counsel, who were parties to the Docket, objected to FPL's recognition of capacity deferral benefits in its calculation of net savings.

Q. Has FPL claimed any additional capacity deferral benefits since that time?

A. Yes. The benefits of deferral of Martin Coal Unit No. 3 have continued to appear in all subsequent FPL Oil Backout Cost Recovery Factor filings. Without construction of the Project and the UPS Agreement, Martin Coal Unit No. 4 would have come into service in December of 1988. Consequently, FPL began to accrue capacity deferral benefits for Martin Unit No. 4 in its October, 1988 through March, 1989 filing in Docket No. 880001-EI. This was also supported in FPL's prefiled testimony. The resultant Levelized Oil Backout Cost Recovery Factor of 0.886 cents/KWH for the period October, 1988 - March, 1989 was approved without objection by FIPUG or Public Counsel.

Q. Is FIPUG questioning in this proceeding issues previously raised by FPL and decided by the Commission?

A. Yes. During 1987 and 1988, FPL presented the methodology and underlying assumptions for its calculation of capacity deferral benefits used in qualifying actual net benefits to be recovered through the Oil Backout Cost Recovery Factor. This was consistent with the Commission's directive in the original certification proceeding that the proper measure of savings to be recovered was to be determined "at such time as the deferred units would have come on-line, absent the Oil Backout Project, i.e., 1987." Even though FIPUG had notice as far back as 1982 and even though FIPUC has been an active party in the Oil Backout proceedings throughout 1987 and 1988, FIPUG waited until significant dollars of actual net savings had been recovered before raising a challenge in January, 1989.

Q. Was it appropriate for FPL and the Commission to include the deferral of Martin Coal Unit Nos. 3 and 4 in the calculation of net savings in these previous proceedings?

A. Yes. The Martin Coal Units were identified in the qualification proceeding as the capacity additions which would have been required if the Project had not been constructed and the power purchases from the Southern Companies had not been made. The construction of the Project and the purchases from Southern Companies allowed the units to be deferred to the 1990's. This deferral was recognized by the Commission in qualifying the Project by including the units' capacity deferral benefit in the Cumulative Present Value Test. In addition, the deferral of Martin Coal Unit Nos. 3 and 4 was the basis for FIPUG's and Public Counsel's argument in the certification proceeding that the primary purpose of the Project was to meet future load growth. Thus, it appears that at least in 1982, all the parties agreed that the Martin Coal Units would be deferred by the Project and the UPS purchases.

Q. In its Petition, FIPUG contends that the capacity deferral benefits used to calculate actual net savings are illusory, because the Martin Units are not now part of FPL's expansion plan and have not been since 1983. Please address this contention.

A. FIPUG's claim is based on faulty logic and erroneous impressions. FIPUG maintains that because FPL has identified in its recent generation expansion plans units other than the Martin Coal Units as its next capacity additions, the Martin Units are "fictional". The conclusion does not flow from the premise. This allegation also shows a misunderstanding of the generation planning process and how decisions to bring new capacity on line are made.

The ability to change the capacity type is an additional benefit arising only because the Project and the UPS purchases deferred the Martin Units. This is a distinct benefit over and above the benefit associated with the deferral of the Martin Units. In Mr. Scalf's testimony during the original qualification hearing, he testified under cross examination: "It would be our hope that in that time frame we might see some change in the commercial availability of alternatives that may produce cheaper types of construction." And he further stated:

> I think there is significant progress being made in research today in some of the coal conversion technologies. To mention only one as looking promising

would be coal conversion and gasification which would then be used in a combined cycle type plant, which should have a much lower capital cost than the conventional units that we see today.

It appears to me that Mr. Scalf recognized that the decision to pursue the Project and the UPS purchases would result in the deferral of the Martin Coal Units from 1987 and 1988 until 1992 and 1993. It also appears that Mr. Scalf recognized that another potential benefit of deferring construction of the Martin Coal Units out of the 1987-1988 time frame might be providing time for technological advancements. Because of lower projected fuel prices, FPL and its customers may able to enjoy the fruits of such advances by using less costly combined cycle technology in FPL's next generating unit addition. However, the current prospect that FPL will build a generating unit other than the Martin Coal Units when it eventually undertakes capacity additions does not change the fact that absent the Project and the UPS purchases, the Martin Coal Units would have been built. Consequently, the Martin Coal Units were the units deferred by the Project, and taking advantage of this additional benefit of intervening technological advances does not make the original units "mythical" or make the capacity deferral benefits "illusory."

Q. Please clarify your assertion that FIPUC's allegations show a misunderstanding of the generation planning process?

A. FIPUG has confused what FPL intends to do in the 1990's with what FPL would have done to meet capacity needs in 1987, absent the Oil Backout Project. The two cannot be compared.

In developing generation expansion plans, the need for new capacity must be identified far enough in advance so that all required activities, e.g., siting, licensing, design, engineering and construction, can be performed to meet the required in-service date. The amount of time required to perform these activities establishes the lead time required between a decision to install a new unit and its completion. For Martin Unit No. 3, the required lead time was approximately eight years. This means that to meet the in-service date of June, 1987, FPL would have had to begin expenditures on the unit in 1980. Similarly, for Martin Unit No. 4, the required lead time was seven years. To meet a Martin Unit No. 4 in-service date of December, 1988, expenditures by FPL would have had to begin in 1982. If FPL had not committed to the Project and the UPS purchases from Southern Companies, FPL would have had to construct Martin Unit Nos. 3 and 4 and these units would now be completed and in operation.

Q. Why do you believe these units would now be in operation, absent the Project and UPS purchases from Southern?

A. FPL evaluates a number of generating unit alternatives when considering capacity additions. In doing so, we look at total expected life cycle costs on a present value basis. When Martin Unit Nos. 3 and 4 were identified as the next unit additions in FPL's generation expansion plans, these coal-fired units had been evaluated against other options on a life cycle basis and found to be less costly. The decision to construct the Project and enter the UPS Agreement was made in 1981, thereby effectively deferring the Martin Units at that point in time. The total life cycle cost relationship between coal-fired units and other alternatives did not change until 1985 planning studies were performed. These studies were then focusing on capacity needs in the mid-1990's. It was not until 1985 when FPL first reflected in its generation expansion plan a combined cycle unit as the next planned generating addition.

I have no reason to believe anything but that the Martin Coal Units would have or could have been built to meet FPL capacity needs in 1987 and 1988. It was not up until 1985, when fuel forecasts for oil and gas showed a significant decline, that combined cycle technology became attractive. Prior to this time, it would have been more economical for FPL to have built its coal-fired units than it would have been to switch to combined cycle technology. Other factors demonstrate this to be the case. Several coal units were certified by the Commission and/or constructed during the period of 1980-1985. Moreover, as late as May, 1984, the Commission determined that a coal-fired generating unit would be more economical than a combined cycle unit and should be used as the avoided unit for cogeneration pricing. Putting aside Fuel Use Act uncertainty over the use of oil and gas as a primary fuel as well as more limited natural gas supplies during this time period, simple economics suggest that absent the UPS purchases, coal-fired generation was the preferred generating alternative until, at least, late 1985.

One other consideration must be mentioned. The project lead time for a combined cycle unit during the 1980-1985 period was five to seven years. Thus, to meet the 1987 and 1988 capacity needs which would have existed without the UPS purchases, FPL would have to have begun construction on a combined cycle unit (and cancelled construction of the Martin Coal Units) in 1981 and 1982. Of course, the Commission had already approved a 1982 generation expansion plan in qualifying the Project in 1982. Even if combined cycle technology had been more cost effective after 1982, project lead time alone would have dictated the completion of the Martin Coal Units to meet capacity needs in 1987 and 1988.

Q. FPL did in fact, change the type of unit it plans to build, as FIPUG points out. Does this suggest that a different type of unit would have replaced Martin 3 and 4?

A. No. In late 1985, FPL moved from a pulverized coal unit to a combined cycle unit as its next capacity option to be added in the mid-1990's. If we evaluate this decision and its impact on Martin Unit Nos. 3 and 4, we need to examine the scenario with no power purchases from Southern and then ask whether the Martin Units would be replaced by combined cycle units. By the end of 1985, Martin Unit No. 3 would have been approximately 78% complete and Martin Unit No. 4 would have been approximately 47% complete. In my opinion, the least cost capacity alternative at that point would certainly have been completion of the units. Life cycle costs of coal and combined cycle units to be placed in service in the mid-1990's were virtually identical in 1985, and if the significant costs of cancelling the Martin Units were recognized, as they should be, in the cost of a combined cycle unit, the economic advantage of completing the Martin Units is significant. In addition, new combined cycle units begun in late 1985 would not have been available to meet the Martin Unit No. 3 in-service date, since less than a two year lead time would exist at that point. As previously noted, five to seven years would normally be required. This also means it is unlikely that Martin Unit No. 4 could have been replaced by combined cycle units.

Q. What do you conclude about FIPUG's allegations concerning deferral of the Martin Units?

A. FIPUG has attempted to infer from recent FPL generation expansion plans that Martin Unit Nos. 3 and 4 were not deferred by the Project. This is a fallacious argument which obscures the main issue, which is what would FPL have done absent the power purchases from Southern. The only way to address this issue is to look at the facts as they existed when the original decisions on the project were made. The deferral of Martin Unit Nos. 3 and 4 occurred when FPL decided to cease spending on the units. While it is true that FPL's generating expansion plans have changed since 1982 and now show combined cycle units as the next planned generating additions, this is a benefit directly attributable to the deferral of the Martin Units, not a reason to assume that they were never part of FPL's plans. The advanced technology combined cycle and coal-gasification combined cycle units which are now part of the FPL Generation Expansion Plans were not available as alternatives to the Martin units. To suggest that the Martin Units are fictional or that the Martin Units were not deferred because of what FPL currently plans to do would be a gross misapplication of fact.

Conclusions

Q. Would you please summarize your conclusions concerning FIPUG's petition?

A. I believe the FIPUG petition and supporting schedules are seriously flawed for several reasons:

- FIPUG erroneously asserts that FPL's 500 KV project has resulted in significant losses, when, in fact, it has provided significant fuel savings as well as total Project actual net savings.

- FIPUG has misinterpreted and misapplied the Primary Purpose Test, which was clearly defined by the Commission in its calculation of project savings.

- FIPUG has engaged in an "apples and oranges" argument about capacity deferral by comparing what FPL currently plans to do with what would have been done in 1982 absent UPS purchases from Southern.

- FIPUG has suggested that the original Project qualification was based on FPL's fuel price projections alone. This was not the case.

- FIPUG ignores the fact that since qualification of the FPL Project, all cost recovery, including the net savings resulting from the Project, has been subject to regular Commission review. Application of the benefits of capacity deferral has been accepted by the Commission, without objection, for nearly two years.

For these reasons, I believe that the Commission should deny the FIPUG Petition and continue to apply FPL's Oil Backout Cost Recovery Factor, subject to regular review.

Q. Does this conclude your testimony?
A. Yes it does.

Q (By Mr. Guyton) Mr. Waters, have you also had occasion to prefile rebuttal testimony in this case dated July 27th, 1989, consisting of some 48 typewritten pages?

A Yes, I have.

Q Do you have any corrections to make to that?

A Yes. I have also submitted an errata sheet for the rebuttal testimony and, as with the direct testimony, I have the errata to the errata sheet. The second line of the errata sheet says "Page 9, Lines 24 to 25," the correction should be to remove "by a preponderance of the evidence," with preponderance of the evidence in quotes. That's the only change I have to the errata sheet.

COMMISSIONER EASLEY: There's another one. Would you look at the one showing Page 10, Lines 1 through 2, and tell me how "positive cumulative present value of expected net savings" changes to "positive cumulative present value of expected net savings"?

COMMISSIONER HERNDON: One is in quotes.

COMMISSIONER EASLEY: One is in quotes?

MR. GUYTON: Commissioner, we are simply adding quotes.

COMMISSIONER EASLEY: Oh, I'm sorry, I missed that.

(Laughter)

CHAIRMAN WILSON: The case will probably rise and fall on the existence of those quotations.

COMMISSIONER HERNDON: No, it will rise and fall on the change of parentheses to brackets.

COMMISSIONER BEARD: That certainly eliminates all the questions I have on rebuttal. (Laughter)

Q (By Mr. Guyton) Mr. Waters, with those essential corrections to your rebuttal testimony, do you adopt it as your testimony in this proceeding?

A Yes, I do now.

MR. GUYTON: Mr. Chairman, we would ask that Mr. Waters' rebuttal testimony be inserted into the record as though read.

CHAIRMAN WILSON: Without objection, the rebuttal testimony will be inserted into the record as though read; likewise, I would ask you to provide corrected pages to the court reporter.

MR. GUYTON: We will do so, Mr. Chairman.

Q (By Mr. Guyton) Mr. Waters, did you also have occasion to file with your rebuttal testimony an exhibit, which is identified as Exhibit 209?

A Yes, I did.

Q And is the information in it true and correct to the best of your knowledge and belief?

A We have a revised Document 3 to submit that updates the numbers on that document.

COMMISSIONER EASLEY: While you are doing that, Mr. Chairman, on the direct testimony I am missing Pages 11, 13, 14, Q (By Mr. Guyton) Mr. Waters, have you also had occasion to prefile rebuttal testimony in this case dated July 27th, 1989, consisting of some 48 typewritten pages?

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COMMISSIONER HERNDON: That may be an advantage.

COMMISSIONER EASLEY: Yes, it would make for shorter reading. (Supplied)

Q (By Mr. Guyton) Mr. Waters, should this revised Document No. 3 be substituted for the original Document No. 3?

A Yes, it should.

Q With that substitution, is the information in your exhibit in your rebuttal testimony, Exhibit 209, true and correct to the best of your knowledge and belief?

A Yes, it is.

(Exhibit No. 209 marked for identification.)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

REBUTTAL TESTIMONY OF S.S. WATERS

DOCKET NO. 890148-EI

JULY 27, 1989

Q. Please state your name and business address.

A. My name is Samuel S. Waters, and my business address is 9250 West Flagler Street, Miami, Florida 33174.

Q. Have you previously filed direct testimony in this docket?

A. Yes, I have.

Q. What is the purpose of your rebuttal testimony?

A. I address several points raised in Mr. Jeffry M. Pollock's direct testimony. First, I address Mr. Pollock's contention that FPL's 500 kV Project ("Project") has not resulted in the economic displacement of oil fired generation. Mr. Pollock has made this assertion based on a test of his own design which is entirely inconsistent with the Primary Purpose Test that the Commission has developed and applied. In discussing this misapplication of the Primary Purpose Test by Mr. Pollock, I show that the Commission has previously rejected a test similar to Mr. Pollock's. I also show that the Primary Purpose Test is still the appropriate test to determine whether the Project economically displaces oil. I have applied this test in my direct testimony and demonstrated that the Project economically displaces oil fired generation. Even Mr. Pollock, in his direct testimony, admits that the Project passes the Primary Purpose Test.

Second, I address Mr. Pollock's misleading statements regarding the alleged recovery of capacity costs associated with the Martin coal units and the alleged double recovery of capacity costs through the Oil Backout Cost Recovery Factor. I explain that FPL recovers through additional depreciation only its investment in the 500 kV Project. No costs of the deferred units are recovered through the Oil Backout Cost Recovery Factor. Consequently, there is no double recovery of capacity costs. In addition to addressing Mr. Pollock's misstatements, I demonstrate that for the 1987-1989 time period, the Martin Unit Nos. 3 and 4 are the only units which can reasonably be used as the basis for calculating capacity deferral benefits used in determining actual net savings, two thirds of which are recovered and applied as additional depreciation of the 500 kV Project. I also establish that the cost estimates for the Martin coal units are reasonable.

Third, I explain that there are no significantly changed circumstances that warrant reconsideration of whether the Project should continue to receive cost recovery through the Oil Backout Cost Recovery Factor. In so doing, I demonstrate that the Commission was fully aware of the possibility of actual circumstances varying from forecast, and that this possibility was fully considered at the time the Project was qualified.

Finally, I draw some basic conclusions regarding the allegations and requests made by FIPUG and Mr. Pollock in this proceeding. I believe that Mr. Pollock's conclusions regarding the Project are totally in error, and that his requests for a refund of collected revenues and discontinuation of recovery are unfair and unjustified. I question the fairness of these requests in light of Mr. Pollock's acknowledgement of the many benefits of the Project. I also note that few, if any, issues which have not already been decided by the Commission have been presented in this proceeding.

Q. Do you have an exhibit attached to your rebuttal testimony?

A. Yes. Attached to my rebuttal testimony is Exhibit No. 209, comprised of Document Nos. 1, 2 and 3. It is identified as Exhibit SSW-2.

Primary Purpose - Economic Displacement Of Oil

Q. Have Mr. Pollock's direct testimony and exhibits established that the Project has failed to economically displace oil fired generation?

A. No.

Q. Please explain.

A. Although Mr. Pollock asserts that the Project has not economically displaced oil fired generation, his direct testimony refutes his assertion. For example, in his attempt to dramatize the difference between the original projections and actual results adjusted for more current projections, Mr. Pollock points out on page 10 of his direct testimony that the "net fuel savings," while substantially below the original projection, are still a positive $1.3 billion on a nominal dollar basis. This calculation is also shown on Mr. Pollock's chart appearing on page 11 of his direct testimony.

Q. Would you agree that the reduction in net fuel savings from that originally forecasted has been substantial?

A. Yes. But, even if these savings were relevant to deciding whether oil backout cost recovery should continue, they still remain positive, and the $1.3 billion Mr. Pollock calculates still represents substantial savings.

Q. Mr. Pollock asserts (page 10) that the original projections showed $3.5 billion in "net fuel savings." Is that number correct?

A. No. Mr. Pollock, perhaps in an attempt to be consistent with his other assertion that there are no capacity deferral savings, has failed to reflect the foregone fuel savings that would have occurred had the deferred coal units, in fact, been built.

Q. What is the impact on the "net fuel savings" calculation had it been performed correctly by Mr. Pollock?

A. As shown on Exhibit 15(j), the exhibit relied upon by the Commission in Docket No. 820155-EU to determine whether the primary purpose of the Project was the economic displacement of oil, the projected fuel savings were $1.4 billion, not the $3.5 billion Mr. Pollock has constructed for this proceeding. In overstating net fuel savings, Mr. Pollock has also overstated the difference between forecasted net fuel savings and actual net savings by almost three times. He then uses this overstatement to support his argument about "changed circumstances."

Q. Is the methodology which Mr. Pollock has used to support his argument that the Project has not achieved the economic displacement of oil fired generation correct?

A. No. It is in conflict with the Oil Backout Rule, in conflict with the Commission's order qualifying the Project and internally inconsistent.

Q. Please explain how it is internally inconsistent.

A. As I pointed out earlier, on pages 10 and 11 of his direct testimony, Mr. Pollock shows that the "actual/current forecast" of "net fuel savings" for the Project is $1.3 billion. Mr. Pollock, however, then subtracts additional non-fuel costs from his "net fuel savings" and concludes that "actual net savings" are negative. In essence, Mr. Pollock has mixed the terms "net fuel savings" with "net savings" to support a faulty conclusion.

Q. With what section of the Oil Backout Rule is Mr. Pollock's methodology in conflict?

A. Rule 25-17.016 refers to the "economic displacement of oil fired generation" in subsections (2)(c) and (3)(a). Subsection (3)(a) requires a finding that the primary purpose of a project is the economic displacement of oil fired generation as one of three findings the Commission must make in order for a project to qualify as an oil backout project under the Rule. It is the alleged failure of the Project to economically displace oil that FIPUG and Mr. Pollock rely upon for the relief requested in this proceeding.

Q. But, doesn't Mr. Pollock's methodology simply assume that if all costs associated with the Project, including the cost of capacity, are subtracted from total fuel savings, and if the capacity deferral benefits are excluded, then the Project has negative net savings?

A. That is what his methodology does. I cannot fault the mathematics: the failure to reflect approximately $2.7 billion of net deferral savings and the inclusion of approximately $2.6 billion of non-fuel capacity costs will produce a loss. If one were to include net capacity deferral savings in Mr. Pollock's methodology, it might provide information about total savings but not fuel savings. In fact, this is what the "Cumulative Present Value" test of subsection (3)(b) of the rule addresses.

Q. Please explain the test described by subsection (3)(b) of the Rule.

A. The term "Cumulative Present Value of Expected Net Savings" is defined by subsection (1)(c) of the Rule. This definition reads in part:

> (c) "Cumulative Present Value of Expected Net Savings" **means cumulative present value of total net savings** associated with the proposed oil backout project, ... (Emphasis added).

All Mr. Pollock has done is to attempt to quantify "total net savings." From this attempt he concludes, incorrectly, that the Project does not economically displace oil. In quantifying "total net savings," Mr. Pollock excluded capacity deferral benefits because he "believes" these have been "improperly collected." Mr. Pollock's methodology, despite what he believes, is thus in conflict with the Rule - it does not calculate fuel savings or determine whether oil fired generation has been economically displaced, and it does not correctly calculate total net savings.

Q. Do you agree with Mr. Pollock's assertion that the Project has failed to economically displace oil?

A. No, absolutely not. Consistent with the Oil Backout Rule, the Commission approved the Project for cost recovery because its primary purpose was to economically displace oil fired generation. The Project has achieved this purpose. The method of establishing this primary purpose was clearly defined by the Commission in the Primary Purpose Test. Not only was this Primary Purpose Test established in Commission Order

No. 11217, but also the exhibit reflecting the test, Late Filed Exhibit 15(j) in Docket No. 820155-EU, was prepared by FPL at the request of the Commission. Mr. Pollock, in pages 15 through 18 in his direct testimony, acknowledges that the Project originally passed the test and continues to pass the test. In light of his own testimony, which demonstrates that the Project continues to economically displace oil, I fail to see the reasoning behind Mr. Pollock's assertion to the contrary.

Q. Mr. Pollock asserts (page 12) that the Commission approved the Project for cost recovery even though FPL was projecting to accumulate substantial net losses. Please comment.

A. This is a total misrepresentation of fact. The Commission did not, as Mr. Pollock alleges, base its Project qualification decision on the possibility of additional fuel savings provided by Alternate and Supplementary energy purchases from the Southern Companies, offsetting "forecasted" losses. None of the economic tests applied by the Commission, either during the qualification proceeding or since, has shown the accumulation of substantial net losses.

It is almost absurd for Mr. Pollock to assert that FPL projected substantial net losses for the Project, when the Commission actually found that FPL had proven that the Project would economically displace oil fired generation and that FPL had proven by a "preponderance of the evidence" that the Project would produce a "positive cumulative present value of expected net savings" within the first ten years of operation.

Q. Is Mr. Pollock's testimony consistent with the FIPUC Petition in this docket?

A. No. FIPUC's Petition asks that the Commission: "determine that FPL's Transmission Project has failed to achieve the 'primary purpose' which led the Commission to qualify it under Rule 25-17.016, F.A.C." (FIPUC Petition, page 14). By Mr. Pollock's own admission, on pages 17 and 18 of his direct testimony, the Project passes the Primary Purpose Test, even when actual data is used. I can only surmise from this contradiction that in preparing the Petition, either FIPUC and Mr. Pollock failed to inform themselves as to how the "primary purpose" of the Project was determined by the Commission, or they were aware of how the Commission originally determined the primary purpose of the Project and intentionally chose to ignore or misstate it. Given that Mr. Pollock now concedes that the Project passes the Primary Purpose Test, the Commission should find that the Project has achieved its primary purpose of economic displacement of oil fired generation.

Q. What then, is the basis for Mr. Pollock's current conclusions that the Project does not economically displace oil?

A. Mr. Pollock has applied a test of his own creation, clearly with the knowledge that the Primary Purpose Test does not support his position. His test is an improper means of determining whether the Project economically displaces oil for several reasons:

- A virtually identical test was presented by Public Counsel's witness, Mr. Dittmer, in the Project qualification proceeding, and the Commission chose instead to adopt the analysis in Exhibit 15(j). Simply stated, in determining whether the primary purpose of the Project was economic oil displacement, the Commission declined to use a test that included coal by wire capacity costs.

- By including the capacity charges associated with the purchases from the Southern Companies without recognizing corresponding capacity deferral benefits, Mr. Pollock has grossly misrepresented and understated the Project savings. I will further address the issue of capacity deferral later in my testimony.

- The test applied by Mr. Pollock is totally inconsistent with the prescribed test the Commission has found to be

appropriate, the Primary Purpose Test. By including capacity costs in his test, Mr. Pollock has created a test that is seriously flawed and meaningless. In the original qualification proceeding, the Commission recognized that capacity benefits and fuel displacement benefits should be separated.

- **The Commission has a means of considering both fuel and capacity costs and benefits in a qualification proceeding, the Cumulative Present Value Test. When this test is properly applied, the Project continues to produce net savings within ten years of qualification. I have demonstrated this in Document No. 4, page 2 of 2, attached to my direct testimony.**

Q. Mr. Pollock asserts that the Primary Purpose Test is no longer meaningful. Do you agree?

A. No. This is nothing more than an attempt to retry the position of FIPUG in the original qualification proceeding that the primary purpose of the Project was to defer capacity. The tests for qualification do not compare fuel displacement benefits to capacity deferral benefits as Mr. Pollock proposes.

Q. Please address the specific reasons Mr. Pollock gives for his argument that the Primary Purpose Test is no longer meaningful.

A. The reasons Mr. Pollock gives to support his statement are not new, and they have been rejected by this Commission before. First, he argues that the "ability to purchase firm coal by wire capacity and all the many reliability benefits associated with the Project more than outweigh any prospective oil displacement benefits" (page 19). The Commission specifically rejected this type of comparison of gross savings in the original qualification proceeding. Order No. 11217 notes that both Staff and FPL argued that the primary purpose of a project was economic oil displacement if fuel displacement benefits exceeded capacity deferral benefits. The Commission responded:

> We reject the Staff's position of simply comparing gross savings as wholly determinative. Whether the primary purpose of the project is oil displacement requires a keener analysis.

That is the appropriate response to FIPUG's "outweighing" argument, as well.

Second, Mr. Pollock argues (page 19) that the emphasis of the Project has changed from oil displacement in 1982 to meeting customer demands today. There has been no change in emphasis. FPL has always acknowledged that in the ten year period of analysis prescribed by the Oil Backout Rule, the Project provides a number of benefits in addition to the economic displacement of oil. In the original economic analysis in the qualification proceeding, capacity deferral benefits were projected to start five to six years into the first ten years of the Project. The fact that those projections have proven correct does not mean the emphasis of the Project has changed. It is unreasonable to look at a few years in isolation out of the ten year analysis horizon. The Project still economically displaces oil, and as the Commission noted in Order No. 11537 denying FIPUG's motion to reconsider qualification of the Project, economic displacement and meeting load growth are not unrelated:

> Displacing oil and providing capacity to meet load growth are not mutually exclusive purposes. The oil backout rule merely requires a determination that the <u>primary</u> purpose of a project is oil displacement to qualify a project under it; the rule does <u>not</u> require a determination that a project will not also

provide capacity to meet load growth.
(Emphasis in original).

Q. Is the Primary Purpose Test flawed?

A. No. Mr. Pollock's observations to that effect are either irrelevant or unsupported. As Mr. Pollock points out, the Primary Purpose Test is not designed to test reliability benefits, and it should not be. Increased reliability is no more mutually exclusive from oil displacement than meeting load growth. The question is whether oil displacement is the Project's primary purpose; it is not whether oil displacement is the exclusive purpose. Mr. Pollock's second observation, that the Primary Purpose Test assumes that coal by wire purchases displace oil fired generation, is a reasonable assumption on FPL's system. Finally, Mr. Pollock's self-serving "question" regarding FPL's statement of total Project cost is totally unsupported. As I note later in my testimony, Mr. Pollock has done nothing to show that FPL's calculation of Project revenue requirements is inaccurate. It is true the Project has required less investment than originally projected; surely Mr. Pollock does not mean to suggest FPL should have spent more money on the Project simply because that is what FPL originally projected.

Q. Is the Primary Purpose Test invalidated simply because oil prices have differed from projections since qualification?

A. No. The primary purpose of the Project was, and continues to be, the economic displacement of oil, which it has done. The fact that fuel savings have been less than projected cannot change the purpose of the Project. In recognition of the fact that there were multiple benefits of the Project, the Commission created the Primary Purpose Test. The Primary Purpose Test was developed to determine if the Project economically displaced oil; it was never intended to measure the benefits of capacity deferral or enhanced system reliability. The Commission articulated its intent to allocate fuel costs against fuel savings and capacity costs against capacity savings. The Project, as I have stated before, still passes the Primary Purpose Test, a point with which Mr. Pollock agrees, but tries to ignore.

I equate Mr. Pollock's reasoning to suggesting that if, after planting a fruit tree, it provides more shade than fruit, then the primary purpose of the tree must have been shade from the beginning. He would also probably argue that we demand a refund from the seller since he sold us a shade tree.

Mr. Pollock continually confuses what we might do today with what we did in 1982. His time travel approach to analysis

clouds the fundamental issue of whether the Project economically displaces oil.

Q. Mr. Pollock has also questioned FPL's handling of minimum-energy scheduling obligations in its Oil Backout filings. Please comment.

A. Mr. Pollock has stated (page 20) that FPL has "totally ignored" the minimum-energy scheduling obligations associated with the 1982 Unit Power Sales ("UPS") Agreement with the Southern Companies in the calculation of energy savings. He is, at best, misinformed. He presents a schedule (Schedule 5) that purports to prove that oil generation has been less expensive than coal by wire during certain periods in the past. Based on his fuel price comparison, he would eliminate $400 million from the net fuel savings (page 21). His approach reflects a basic misunderstanding of how net fuel savings are computed. Also, he has committed significant errors in both the fuel price comparison and his adjustment of net fuel savings.

Q. How are minimum-energy scheduling requirements treated in developing net fuel savings?

A. The calculation of net fuel savings begins with a determination of the total amount of additional fuel costs that would have been incurred by FPL if none of the coal by wire had been purchased. From this total of avoided or foregone fuel costs is subtracted total coal by wire energy costs, including minimum-energy scheduling requirements. The remainder is the net fuel savings of the coal by wire purchases. For every reporting period, net fuel savings have always been positive.

Q. What would be the effect on net fuel savings of removing minimum-energy scheduling requirements if coal by wire energy were more expensive than FPL's cost to generate the same energy?

A. If, as Mr. Pollock speculates, the cost of the scheduled minimum energy exceeded the cost at which FPL could have generated that energy with oil, then that result would already be reflected in FPL's calculation of net fuel savings. It would lower the overall savings for the period. Consequently, the removal of scheduled minimum energy from the calculation of net fuel savings under such circumstances would increase, rather than decrease, the positive net fuel savings reported by FPL. In other words, if FPL has ever paid more for coal by wire minimum energy requirements than it would have cost FPL to generate the same energy, that fuel penalty would already be reflected in the net fuel savings reported. Mr. Pollock's attempt to remove $400 million of actual, positive net fuel savings is conceptually wrong. If there had been any minimum-energy scheduling fuel penalties, they would already be reflected in the $651 million of Project net fuel savings, shown on Document No. 4 in my direct testimony.

Q. In addition to this conceptual flaw in Mr. Pollock's minimum-energy scheduling argument, are there other flaws in Mr. Pollock's attack on minimum-energy scheduling?

A. Yes, there is one additional flaw. His comparison of actual oil generation costs and coal by wire energy charges is improper and not meaningful.

Q. Please explain why Mr. Pollock's comparison of actual fuel cost associated with oil generation and the coal by wire energy charges shown on Mr. Pollock's Exhibit JP-1, Schedule 5, is improper and not meaningful.

A. The fuel cost associated with oil generation shown on Schedule 5 is the actual fuel cost incurred by FPL with coal by wire purchases. It reflects the lowest costs of oil fired generation available on FPL's economically dispatched system. Without coal by wire purchases, the energy necessary to replace the coal by wire purchases would have to be generated on FPL's economically dispatched system using less efficient, higher fuel cost units. Consequently, the use of actual oil generation costs during a period when coal by wire purchases were made tells nothing about what oil generation would have cost without the coal by wire purchases.

To determine whether oil fired generation on FPL's system would have been more costly than coal by wire energy costs, the proper analysis is to compare coal by wire energy costs with avoided oil generation costs, the costs which would have been incurred without the coal by wire purchases. That comparison is shown in Exhibit 209 (my Exhibit SSW-2, Document No. 1). The avoided energy oil generation costs shown were derived by dividing, for each recovery period, avoided fuel savings reported in FPL's true-up filings by coal by wire energy purchases reported. This comparison is the proper comparison. It also shows that the premise underlying Mr. Pollock's entire minimum-energy scheduling argument is unfounded. Coal by wire energy was less expensive than avoided oil generation in all recovery periods.

Q. Mr. Pollock also "questions" the Transmission Project revenue requirements used in the Primary Purpose Test (pages 19-20). Please comment.

A. Mr. Pollock has done nothing more than attempt to cast doubt on the Project costs. He has not shown that FPL's reported costs are inaccurate. The cost of the Project and the associated revenue requirements have been presented to the Commission several times in the Oil Backout proceedings. They have also been audited by the Commission's Staff since April 1985. The

Commission has accepted the calculations, and Mr. Pollock has provided no factual basis on which to question them.

Q. What do you conclude about Mr. Pollock's claims that the Project has not economically displaced oil?

A. His conclusions are based on the results of an improper economic test which does not conform to any of the criteria used by the Commission in qualifying the Project. In addition to creating a test designed to show substantial losses, Mr. Pollock has raised a number of peripheral and sometimes irrelevant issues to support his allegations. Despite his arguments, he has presented no evidence which is contradictory to the fact that the project economically displaces oil, which is its primary purpose.

Cost Recovery Of The Project

Q. Mr. Pollock, on pages 8 and 37 of his direct testimony, suggests FPL is recovering capacity twice in its Oil Backout Cost Recovery Factor, once for UPS capacity purchases and again for the deferred capacity carrying costs for Martin Unit Nos. 3 and 4 and Unsited Unit No. 1. Are the deferred capacity carrying costs for the Martin coal units being recovered through the Factor?

A. No. FPL does not now collect, nor has it ever collected, any of the revenue requirements associated with the deferred coal units. Mr. Pollock's statements are extremely misleading. There are two major flaws in his characterization. First, the units which were deferred do not represent a cost at all, but a benefit or reduction in cost to the ratepayers. Second, Section 4(a) of the Oil Backout Rule allows collection of revenues equal to two-thirds of the actual net savings of the Project, to be applied as **"additional depreciation of the Project"**. (Emphasis added). Thus, FPL is recovering the costs of the Transmission Project in the form of additional depreciation, not any revenue requirements of the deferred units. Mr. Pollock's allegation that FPL is recovering the costs of facilities which are not used and useful is totally wrong. Only the costs of the 500 kV facilities, which Mr. Pollock acknowledges provide many benefits, are being recovered through FPL's Oil Backout Cost Recovery Factor as additional depreciation.

Q. Does FPL recover the costs of the UPS capacity charges through the Oil Backout Cost Recovery Factor?

A. Yes. Recovery of these costs was specifically authorized in Order No. 11210 and it has been authorized by the Commission since then in the regularly held Oil Backout proceedings. FPL has not, as I previously stated, recovered the costs of Martin Unit Nos. 3 and 4 through the Oil Backout Cost Recovery Factor. So, there is no double recovery of capacity costs as suggested by Mr. Pollock on pages 8 and 37 of his direct testimony.

Q. What other costs are recovered through the Oil Backout Cost Recovery Factor?

A. The Rule explicitly defines what costs may be recovered:

- Straight line depreciation of the Project
- Cost of capital of the Project
- Actual tax expense
- Oil/non-oil O&M expense differential
- Two-thirds of the actual net savings of the project, to be applied as additional depreciation

The "project," in this case, refers to the FPL 500 kV lines and associated facilities. FPL cannot and does not recover the costs of deferred capacity through the Oil Backout Cost Recovery Factor.

Q. How, then, do the deferred coal units enter into the formulation of cost recovery for the Project?

A. As prescribed by the Rule, the deferred units are considered in the determination of actual net savings of the Project. The revenue requirements that would have been incurred had the units been built are included as a benefit to the customer in the calculation of actual net savings, since these revenue requirements will not be incurred due to the power purchases from the Southern Companies. This benefit is added to other benefits, then total benefits are compared to total costs to determine actual net savings.

Q. Please identify the elements of benefits and costs that are used to determine actual net savings.

A. In each recovery period, actual net savings for the Project have been calculated. The elements of benefits and costs which are recognized in the computation of actual net savings are shown below.

Benefits	Costs
Avoided Energy Fuel Savings	Coal by Wire Energy Charges
Spinning Reserve Fuel Savings	Foregone Martin Fuel Savings
Deferred Martin Unit Carrying Charges	Coal by Wire Capacity Charges
Deferred Martin Unit Fuel Charges	500 kV Project Revenue Requirements

Q. How long does this recovery of additional depreciation continue?

A. Provided that net savings remain positive, under the Rule FPL can continue to recover two-thirds of the actual net savings until the investment in the Transmission Project is fully depreciated. After the Project is fully depreciated, 100% of actual net savings will flow to FPL customers. Of course, FPL customers will also benefit from a lower Oil Backout Cost Recovery Factor.

Q. Has FPL been recovering additional depreciation through the realization of actual net savings?

A. Yes. Except for a brief period in 1982, the Project did not show actual net benefits until 1987, when Martin Unit No. 3 would have been placed in service. In every recovery period since that time, there have been actual net savings. FPL has recovered two-thirds of these savings and applied them as additional depreciation on the 500 kV Project. By the end of August, 1989, the Project is expected to be fully depreciated.

Q. What conclusions can be drawn concerning Mr. Pollock's allegations of double recovery of capacity costs (pages 8 and 37)?

A. His arguments are incorrect and very misleading. FPL recovers UPS capacity charges and the revenue requirements associated with the 500 kV Project through the Factor. Additional cost recovery represents only FPL's two-thirds share of actual net savings provided by the Project, which is applied as additional depreciation on the 500 kV Project. The avoided revenue requirements of the deferred coal units are only one of several elements in the calculation of how much actual net savings will be included as additional depreciation of the Project. It is incorrect and extremely misleading to characterize this additional depreciation of the Project as recovery of deferred capacity costs.

Calculation Of Capacity Deferral Benefits

Q. Do you agree with Mr. Pollock's argument (pages 34-42) that the Martin coal units should not be used to calculate actual net savings when determining the Oil Backout Cost Recovery Factor?

A. No. Mr. Pollock has once again introduced irrelevant comparisons in an attempt to prove the Project has not produced savings. While I have addressed this issue in my direct testimony, I feel it must be readdressed due to Mr. Pollock's persistence in presenting misleading and irrelevant information.

The fundamental issue to be considered here is what FPL would have done had it not committed to the Project and firm power purchases from the Southern Companies. What FPL plans to do to meet load requirements in the mid-1990's is entirely irrelevant to this issue. On one point Mr. Pollock and I agree, that the Martin coal units have not been, and may never be, built. This admission in Mr. Pollock's testimony (page 36) is the premise upon which capacity deferral benefits are based; **the Martin coal units were not built due to the commitment to purchase power from the Southern Companies and FPL's ability to move that power over the Project.** The argument that the Martin coal units will not be "used and useful" is a very shallow attempt to obscure the fact that the costs which FPL is recovering through additional depreciation are only those associated with 500 kV Transmission Project, which is used and useful by Mr. Pollock's own admission. Once again, Mr. Pollock is implying that FPL is recovering capacity costs associated with the deferred units, which is not the case, as I have previously discussed.

Q. Mr. Pollock states that Martin Unit Nos. 3 and 4 are no longer consistent with least cost planning. Do you agree?

A. No, not when the analysis is performed, as it should be, from the perspective of making a decision in 1982. I agree that FPL currently does not see large pulverized coal units as the most economic choice for service in the mid-1990's, but that is irrelevant to this issue, and as I stated in my direct testimony, this change in preferred technologies for the 1990's is actually an additional benefit attributable to the deferral of the Martin units.

Q. Please explain why you believe Martin Units 3 and 4 would have been placed in service in 1987 and 1988?

A. Mr. Pollock has stated in his testimony (page 23) that FPL's projected reserve margins would be inadequate in the absence of coal by wire purchases. His Exhibit JP-1, Schedule 7 demonstrates that from 1989 through 1992, FPL would have inadequate reserve margins without these purchases. Beyond 1992, he has mistakenly subtracted the capacity associated with

FPL's 1988 Agreement with the Southern Companies, but I do not believe this materially affects the issue of whether Martin Unit Nos. 3 and 4 would have been placed in service in earlier years.

Had Mr. Pollock included the years 1987 and 1988 in his Schedule 7, he would have noted that FPL reserve margins would also have been inadequate. To demonstrate this, I have corrected Mr. Pollock's Schedule 7 with the years 1987 and 1988 added and attached the results as Exhibit SSW-2, Document No. 2. As shown, FPL reserve margins would have been inadequate throughout the years 1987 through 1992 without the coal by wire purchases. New capacity would be required to meet the deficiency in 1987.

To meet these requirements without power purchases from the Southern Companies, FPL would have had to begin the siting, licensing, design, engineering and construction of Martin Unit No. 3 no later than 1980. However, I will begin my analysis in 1982 since that is when the Project was qualified for cost recovery and when the Commission last had occasion to rely upon a generation expansion plan showing the Martin Coal Units with completion dates of 1987 and 1988. My analysis consists of comparing the thirty year capital revenue requirements of Martin Unit No. 3 with the thirty year capital revenue requirements for combined cycle units, which Mr. Pollock apparently believes is the proper basis for comparison for each of the years 1982 through 1985. To that difference, I add the thirty year fuel revenue requirement advantage of the Martin coal units. My analysis assumes that for each year from 1982 through 1985, FPL "changed its mind" on the type of capacity it would build. The relevant fuel and load forecast assumptions for each of the years were used. Sunk costs of Martin Unit No. 3 are charged to the in-service cost of the combined cycle units in each year.

The results of the analyses are summarized in Document No. 3 of my Exhibit SSW-2, Exhibit No. 209. The results show that Martin Unit No. 3 would be the clear economic choice in 1982, and the decision to proceed with Martin Unit No. 3 construction would not have been altered despite changes in fuel price forecasts. By 1985, when FPL changed the type of capacity it planned to build for the 1990's to combined cycle units, sufficient sunk costs would have been incurred in Martin Unit No. 3 that it would have been far more economical to complete the unit for service in 1987 than to build a new combined cycle unit for service in 1987. My Document No. 3 shows that a net present value savings of over $500 million would have resulted from completion of Martin Unit No. 3. In addition to the economic advantages of Martin Unit No. 3 over combined cycle units, it would have been impossible to bring the new combined cycle units in service in 1987, assuming the commencement of the siting, licensing, design and construction activities in 1985.

Q. What do you conclude from your analysis?

A. Based on this analysis, it is my judgment that Martin Unit No. 3 would have been the most economic choice to meet a required in-service date of 1987. I believe a similar analysis performed on Martin Unit No. 4 would yield similar results. This study suggests that Martin Unit Nos. 3 and 4 are consistent with what Mr. Pollock has referred to as a least cost plan, when viewed from 1982 to meet 1987, rather than mid-1990's, need.

Q. Does this mean that the revenua requirements of the deferred units are appropriately considered in determining actual net savings?

A. Yes. Given that the units would have been constructed in the absence of firm power purchases from the Southern Companies, the revenue requirements associated with the units represent the costs FPL customers would be paying without the purchases. Thus, these forgone revenue requirements are actually a savings attributable to the Project and the associated power purchases, which should be used in the calculation of actual net savings. When savings from capacity deferral and fuel displacement are offset by the costs of UPS capacity and energy charges, foregone fuel benefits, etc., the Project produces actual net savings, of which, consistent with the Rule, FPL recovers a portion and applies as additional depreciation to the Project.

Q. Doesn't the fact that the Martin coal units are not in-service or under construction actually suppo t the premise that the Project has deferred capacity?

A. Yes, absolutely. In the original qualifica..o.. proceeding, FPL projected that the Martin units would be needed in 1987/88 without the Project and associated coal by wire purchases. Actual savings have resulted from the decision to pursue the Project rather than construct the units. Mr. Pollock has not disputed the need for capacity in the years 1987 and 1988. In fact, he has argued that since capacity is needed in those years, the primary purpose of the transmission lines is to enable FPL to meet demand (page 24 of Mr. Pollock's testimony). If capacity would be needed in the absence of the Project, a point on which Mr. Pollock and I agree, then the fact that the units were not built can only support the position that they represent an "avoided cost" attributable to the Project.

Mr. Pollock cites no authority for his contention that the Martin units must eventually be constructed for actual net savings to occur. In fact, his argument is totally illogical. I would emphasize again that the only relevant way to determine capacity deferral benefits is to identify what would have been done to meet capacity needs in 1987/88. What will or will not be built in the 1990's has nothing to do with the basic calculation of actual net savings.

Q. **Mr. Pollock states (page 21) that "For the primary purpose of the Project to be oil backout, the purchases must provide capacity in excess of FP&L's reserve requirements." Do you agree?**

A. No. Mr. Pollock has once again attempted to introduce a new concept of "primary purpose." I do not find any basis for his contention. If this statement were true, a Project could not have any capacity deferral benefits and still qualify under the Rule. Such a result is inconsistent with Section (4)(c) of the Rule which recognizes "other benefits" in calculating net savings. It is also inconsistent with the Commission's calculation of expected benefits in the qualification proceedings. As I have discussed previously, the Commission clearly recognized that economic displacement of oil and capacity deferral are not mutually exclusive.

The Commission has established a basis for determining that economic oil displacement is the Project's primary purpose. It is based on economic oil displacement rather than capacity displacement criteria, as it should be. The fact that the Project in the later years of the original ten year analysis horizon is being used to meet load in addition to economically displacing oil does not mean the primary purpose of the Project has changed. This additional Project use and benefit was anticipated when the Project was determined to have the primary purpose of economically displacing oil.

Q. Mr. Pollock's testimony suggests that the costs of the Martin units were inflated to increase capacity deferral benefits (page 39). Is this accurate?

A. No. Mr. Pollock has taken unit costs out of context, put them in a table without adjusting for the different in-service dates, and claimed they demonstrate that the Martin costs are too high. He has also failed to point out that FPL's estimated direct costs for the Martin coal units presented on page 40 of his testimony include escalation, while the costs for the other estimates in his Schedule 12 are "overnight construction costs" that do not include escalation. This omission alone accounts for the majority of the difference. In fact, FPL's estimated Martin unit costs are representative of what the actual costs would have been to construct the units.

Q. **How were capital costs for the Martin units determined?**

A. The capital costs of the Martin units were based on the original Bechtel unit package, and they reflect the original economic, market and design conditions which existed at that time. FPL has adjusted the original in-service cost estimates of the units to reflect actual inflation and cost of capital. This significantly lowered the cost estimates. I believe that this approach is entirely reasonable.

As I previously noted, FPL's Martin unit costs reflect escalation, while the costs used by Mr. Pollock do not. The Florida Electric Power Coordinating Group, Inc. ("FCG") filing for the 1989 Annual Planning hearing showed that escalation would add approximately 25% to the overnight construction costs of a pulverized coal unit (FCG Form 1.5, page 3 of 3). That being the case, I do not believe that FPL's estimated costs of the Martin coal units are out of line with the estimates presented in Mr. Pollock's Schedule 12.

Q. **What do you conclude about Mr. Pollock's attempts to show that the capacity deferral benefits of the Martin coal units are improperly included in the calculation of the Oil Backout Cost Recovery Filing (pages 34-42)?**

A. I believe it is clear that Mr. Pollock, understanding the weakness of his position, has attempted to attack the capacity deferral issue from several angles. He has claimed the units were not deferred because FPL has never built them. If we do not accept this position, then he would have us believe that a different type of capacity, i.e., combined cycle units, has been deferred. If we do not accept this position, then he would like us to believe that the capacity costs of the Martin coal units have been inflated. If we accept none of his arguments that capacity was not deferred or his argument that deferred capacity costs are incorrectly calculated, then he would like to suggest that since capacity really was deferred, this capacity deferral was really the primary purpose of the Project after all, rather than economic oil displacement. He has certainly tried to cover all the bases.

The facts are that the Martin coal units are properly used in the calculation of actual net savings. The estimate of Martin coal unit costs is reasonable. FPL is not recovering any costs of the deferred units. The only costs FPL has recovered through additional depreciation are costs of the 500 kV Project, and even that recovery will soon end when the Project investment is fully depreciated.

All of these issues have been addressed in previous FPL Oil Backout filings, and FIPUG raised no objection. There is no basis for its objection now. My overall conclusion is that the

accelerated cost recovery of the Project costs resulting from actual net savings, which are premised in part on Martin unit deferral, is appropriate and should be allowed to continue.

Changed Circumstances

Q. Mr. Pollock asserts that changed circumstances warrant a reexamination of the Project by the Commission. Do you agree?

A. No. I have been informed by Counsel that "changed circumstances" cannot warrant the discontinuance of Project cost recovery as a matter of law, but from my perspective, there are no meaningful or significant changed circumstances that should affect cost recovery, even if it could be discontinued. Mr. Pollock has suggested that circumstances have changed such that (1) economic oil displacement (oil backout) is no longer the primary purpose of the Project and coal by wire purchases (page 21) and (2) deferred capacity savings no longer should be included in the calculation of actual net savings (page 38). I do not believe that there are any significant changed circumstances that justify reassessing whether the Project and associated purchased power costs should be recovered through the Oil Backout Cost Recovery Factor.

I believe that the changed circumstances alleged by Mr. Pollock are either irrelevant or do not significantly affect the conclusions reached by the Commission in the original qualification proceeding.

Q. Please address Mr. Pollock's first assertion, that the primary purpose of the Project and coal by wire purchases is no longer oil backout, due to changed circumstances.

A. While actual oil prices have been lower than originally projected, this does not change the fact that the Project and the associated coal by wire purchases still pass the Primary Purpose Test established by the Commission. The Primary Purpose of the Project is still the economic displacement of oil.

More importantly, the Commission has previously recognized this possibility of lower oil prices, and the intent was not to allow lower oil prices to be an excuse for reconsidering Project recovery through the Factor. The Rule does not provide for "unqualifying" a project should actual conditions not turn out as projected.

In the June 22, 1982 Agenda Conference for Docket No. 820257-EU, amending Rule 25-17.16, F.A.C., Commissioner Cresse stated:

It seems to me that the primary purpose, as I recall when I suggested that we adopt this rule, was to provide an incentive to the electric power companies that we regulate to provide more economic electricity to their ratepayers than would business as usual provide their ratepayers.

And one outstanding way in which that can be done in the state of Florida is to provide mechanisms where within a reasonable projection of cost differential between oil and coal that we have a mechanism whereby we could replace some of our present oil-fired electricity with coal fired electricity.

Now, that was the broad objective that I think everybody was talking about, at least I was talking about when I proposed the rule.

We said, I think, first, that we want to provide that incentive for the utilities to get involved in it with today's type of financial difficulties and problems. And second, since

> we're not very good at projecting what the prices are of these differentials - because, you know, less than fifteen years ago if you had projected what would be the cheapest today, everybody would have come down on the side of oil.
>
> We want a reasonable time frame whenever these projects will pay out, very simple pay out. And in the event we are wrong, we won't be placing the burden on the ratepayers in the future. And we chose ten years. Why ten? Ten is better than 12? We have a ten-year forecast. Twelve might not be a bad idea; eight might not be a bad idea; but we chose ten, and that was somewhat arbitrarily chosen to show that the project would be cost beneficial to the ratepayers over a ten-year period. . . .

And he further states:

> . . . what we do is split the savings, pay for the project, use the decelerated (sic) depreciation, get it off the books. Then if

your forecast is wrong on prices, and ten years from now it turns out to be a bad deal, we will at least in the next four or five years have recovered some of the costs of that investment, and not be burdened on future ratepayers.

Later at the same Agenda Conference, Commissioners Leisner and Cresse had the following discussion regarding continued recovery if anticipated fuel savings did not materialize:

Commissioner Leisner: No. What we are saying is you could always recover you [sic] costs. And **then the idea of this rule was you recover your costs always**, then if there is a fuel differential that benefits the ratepayers, benefits everybody, you split the savings.

Commissioner Cresse: I understand that. Commissioners, I think there -- don't have any misunderstanding. If we approve one of these projects, the utility will recover the costs anyway, prudently incurred. (Emphasis added).

Again, in the project qualification proceeding, Commissioner Cresse restated his understanding. In response to a suggestion by Staff Counsel that a change in the coal-oil price differential would not be grounds for redetermining the prudence of a project, Commissioner Cresse observed:

> Don't misunderstand me. I **think that once we have said that this would be incorporated into the oil backout clause that's that decision**, just like whenever we say you ought to build a plant . . . . (**Emphasis added**).

Q. Mr. Pollock argues (page 22) that since purchases do not provide capacity in excess of reserve requirements, the Project's primary purpose is to meet load growth. Do you agree?

A. No. Mr. Pollock is playing both sides of this issue, claiming capacity benefits or alternatively no capacity benefits, as required to make his case. It is important to remember that the Commission established a ten year period for examination of project economics, not an isolated year. The Commission understood from the beginning that the Project provided reliability benefits and in the later years of the ten year analysis period, capacity deferral benefits. This was permissible under the Rule provided the economic displacement of oil remained the primary purpose.

In addition, Mr. Pollock has acknowledged that FPL load growth has been essentially as projected in 1982. Power purchases have also been as projected in 1982. These facts lead to the inescapable conclusion that the capacity deferral benefits provided by the Project remain essentially unchanged. This certainly does not suggest that there are any changed circumstances since 1982 which have altered the primary purpose of the Project.

Q. Have any of the important factors changed regarding economic oil displacement as the primary purpose of the Project?

A. No. The Project still passes the Primary Purpose Test. Capacity needs are essentially as FPL projected. I see no reason to take FPL to task because load growth, capacity deferral and power purchases have materialized as forecast.

Q. What about Mr. Pollock's second issue, that changed circumstances warrant revisiting the use of capacity deferral benefits of the Martin units in the calculation of actual net savings?

A. I have already demonstrated that the Martin Coal Units were deferred by the Project and are therefore the appropriate basis for the calculation of net savings. The fact that these units have not appeared in FPL's ten year generation expansion plans since 1986 is irrelevant. The only relevant question is what would FPL have built had it not completed the Project and committed to the associated power purchases from the Southern Companies. The answer is undeniably the Martin Coal Units. Current FPL plans to construct other types of units in the 1990's do not have any effect on this conclusion.

Q. Mr. Pollock also contends (page 25) that the new UPS Agreement between FPL and Southern Companies represents a changed circumstance warranting the revisiting of the capacity deferral issue. Please address this contention.

A. I believe the introduction of the new UPS agreement is totally irrelevant to the issues in this proceeding for several reasons. First, the time period for examination of the Project, as defined in the Rule, is ten years, which limits the focus to the 1982-1992 period. The new UPS Agreement does not begin until 1993, which is outside of this horizon.

Second, the availability of purchased power beyond 1992 does not alter the fact that the Martin units were deferred by the original Agreement. It does not change the fact that actual net savings have occurred since 1987. It is fortunate that the additional power from the Southern Companies became available, but this does not in any way change the purpose of the Project.

Q. Would you please summarize your conclusions about Mr. Pollock's "changed circumstances" arguments?

A. Mr. Pollock's arguments do not substantiate his claims that circumstances have changed significantly enough to require a requalification proceeding by the Commission. He has merely clouded the straightforward issues around which this proceeding revolves: Is the primary purpose of the Project the economic displacement of oil and has the Project deferred Martin Unit Nos. 3 and 4? The answer to both questions is undeniably yes. As a result, FPL should be allowed to continue to recover Project and coal by wire costs through the Oil Backout Cost Recovery Factor. The Martin coal units' capacity deferral benefits have properly been used in the calculation of actual net savings. FPL's recovery of revenues equal to two thirds of actual net savings is consistent with the Rule. In addition, FPL's application of those revenues as additional depreciation on the 500 kV Project is consistent with the Oil Backout Rule and will lower future oil backout recovery since the Project will be fully depreciated in August, 1989. There are no significant changed circumstances. The Oil Backout Rule has worked as envisioned, and both FPL and its customers, including FIPUG's members, have benefited.

__Conclusions__

Q. Do you believe that the relief requested by FIPUG and Mr. Pollock is fair to FPL?

A. No, I do not. The Project has produced substantial benefits to FPL's customers, which Mr. Pollock acknowledges, yet Mr. Pollock and FIPUG are suggesting that FPL be denied the ability to recover the costs associated with the Project. Mr. Pollock has testified that the Project passes the Primary Purpose Test. He has acknowledged that the Project provides capacity deferral benefits, and he has acknowledged that the Project provides reliability benefits. Despite these admissions, FIPUG and Mr. Pollock believe that cost recovery under the Oil Backout Cost Recovery Factor should be discontinued, and they raise questions as to whether any adjustment to FPL's base rates should be made to assure cost recovery if the Factor is discontinued. This is particularly unfair since FPL has previously requested and has been denied base rate recovery of the costs associated with the Project in Order No. 13537 in Docket No. 830465-EI.

Q. Has Mr. Pollock raised any new issues in his testimony?

A. Very few, if any, of Mr. Pollock's arguments are new. Most have been presented to, and rejected by, the Commission. The Commission has established a Primary Purpose Test, rejecting tests similar to the one presented by Mr. Pollock. The Commission has heard the arguments about energy based oil backout charges, i.e., cents/kWh, and rejected them in numerous prior proceedings. Capacity deferral benefits were recognized in the original FPL qualification proceeding and have been approved by the Commission on three prior occasions without objection by FIPUG, yet FIPUG is now belatedly seeking a refund. FPL is being called upon to defend settled issues. This represents a tremendous cost to the Company.

Q. What do you conclude about the merits of Mr. Pollock's requests?

A. Mr. Pollock has not presented any substantive basis for reconsidering the way the Oil Backout Cost Recovery Factor is calculated or applied. He has not provided any factual basis for requesting a refund of collected revenues; therefore, no refund is warranted.

Cost recovery of the Project is essentially complete. Continued recovery of the remaining Project costs and the UPS capacity charges through the Factor is consistent with prior Commission decisions, and it protects the customer and the Company alike by providing for regular review and true-up of such costs.

In summary, Mr. Pollock has failed to make a case for reconsideration of cost recovery of the Project. FIPUG's petition should be denied.

Q. Does this conclude your testimony?

A. Yes, it does.

Q (By Mr. Guyton) Mr. Waters, would please summarize your direct testimony?

A Yes, sir. Commissioners, my direct testimony addresses several issues raised in the Florida Industrial Power Users Group petition to discontinue Florida Power and Light Company's oil backout cost recovery factor. Specifically, my testimony discusses a key assertion made by FIPUG that the capacity deferral benefits used in the calculation of actual net savings are based on fictional generating units. In addressing this point I have presented an historical overview of the FPL 500 kV project, and the associated power purchases from the Southern Companies, including a review of the original qualification proceeding.

I have also discussed the savings produced by the project; re-established that the primary purpose test is still passed, although I understand that this is no longer an issue in this proceeding; and I have reviewed the planning process as it relates to the capacity deferral benefits associated with Martin Coal Units 3 and 4.

I conclude from my review of the facts that there is no basis for FIPUG's contention that there are no capacity deferral benefits associated with the project. The Martin Coal Units were, in fact, deferred. I believe that no other conclusion is possible, and for this reason conclude that FIPUG's claims that capacity deferral benefits are illusory(?) and based on fictional units are totally without merit. This concludes my summary.

Q Mr. Waters, would you please summarize your rebuttal testimony?

A Yes, sir. My rebuttal testimony addresses several points raised in the direct testimony of Mr. Jeffry Pollock in support of the Florida Industrial Power Users Group petition to discontinue FPL's oil backout cost recovery factor. Specifically, I have refuted two areas in Mr. Pollock's testimony: One, his misleading suggestions to the effect that FPL is recovering capacity costs associated with the deferred Martin Coal units, and, two, his contention that oil backout revenues have been improperly collected due to the inclusion of capacity deferral benefits associated with Martin Units 3 and 4 in the calculation of actual net savings.

I state in my testimony that FPL does not collect any costs associated with the deferred generating units. I also state that the costs of the units used in the calculation of net savings were properly derived from the original Bechtel package and adjusted for actual inflation and cost of capital.

Finally, my testimony questions the fairness of the contentions made by FIPUG. Mr. Pollock acknowledges that the project has produced $1.3 billion of, in his words, net fuel savings. He acknowledges that the project still passes the Commission's primary purpose test, even in light of lower oil prices. He contends that the reliability benefits of the project far outweigh the oil displacement benefits. He further acknowledges that the project has enabled FPL to defer the construction of Martin Units 3 and 4.

In light of Mr. Pollock's own description of the many benefits provided to FPL customers by the project, FIPUG's request for a refund of accelerated recovery of the project is unfair. This concludes my summary.

MR. GUYTON: We tender Mr. Waters for cross examination.

MR. HOWE: We have no questions.

CHAIRMAN WILSON: Mr. McGlothlin?

MR. McGLOTHLIN: Yes, sir.

CROSS EXAMINATION

BY MR. McGLOTHLIN:

Q Mr. Waters, on the subject of accelerated depreciation and the relationship between the deferred capacity and the amount of accelerated depreciation taken, as I understand it, the relationship is this: The higher the value assigned to the cost of constructing the deferred unit, the greater the impact on net savings, and, to the extent that net savings are calculated, the greater the rate of accelerated depreciation, is that correct?

A I would say, all of the things being equal, that's probably correct. It's a mathematical truism because of the way the calculation is done.

Q So if, and to the extent, FPL overstates the value of the cost of the deferred capacity, it would also overstate the amount of net savings and overstate the amount of accelerated depreciation taken, is that correct?

A Well, I can't accept the premise that FPL would overstate the capacity benefits, but if it were proven that they were overstated then certainly we would have higher deferral benefits.

Q The projections of the costs of Martin 3 and Martin 4 were based primarily on the parameters of a Bechtel contract dated 1979, is that correct?

A They were based on that design package, that is correct.

Q And they have been modified, as I understand it, by revisions to the assumed rate of inflation and by revisions to the assumed capital costs over time, is that correct?

A The installed cost estimate was updated for actual inflation and actual cost of capital, that's correct.

Q Okay. But the basic parameters remained those of the 1975 contract, except as modified by those two factors, is that correct?

A The basic design parameters, yes, sir.

Q Now, it's true that in the time frame 1979 to 1980 Florida Power and Light was planning the construction not only of the Martin Units but also of the St. Johns Power Park units, is that correct?

A There were discussions between FPL and Jacksonville at that time, negotiations going on, for a joint project to construct those units. What stage those were in, as far as design and contracting, I'm not certain. I don't believe the contract to construct St. Johns was done in that time frame.

Q Martin 3 was planned to be a base loaded coal-fired unit, is that correct?

A It was planned to be a coal-fired unit, that is correct. Base loaded is a result of many conditions, but we would assume that it would have run base loaded.

Q It was planned to be a 700 megawatt unit?

A Approximately. That was the original projection.

Q It was planned to utilize flue gas desulfurization?

A Yes, that was part of the design.

MR. McGLOTHLIN: I have a document that I would like to distribute at this point and have a number assigned to it.

CHAIRMAN WILSON: All right.

MR. McGLOTHLIN: And I'm not going to attempt to guess what the number is going to be. I will leave that to somebody else.

CHAIRMAN WILSON: I'm sorry, what?

MR. McGLOTHLIN: I'm not going to hazard a guess as to what the number is going to be. I will leave that to somebody else.

CHAIRMAN WILSON: Well, we have a lottery going up here so go ahead and guess. (Laughter)

COMMISSIONER BEARD: You can't do any worse than they are doing in Montana, they can't give their lottery away.

CHAIRMAN WILSON: What will the next number be?

MR. PRUITT: 213.

CHAIRMAN WILSON: 213?

MR. PRUITT: Yes, sir.

CHAIRMAN WILSON: All right, this will be Exhibit No. 213.

COMMISSIONER EASLEY: Hold on just a minute. Was this the one that was asked for yesterday by Mr. McWhirter? This is not the same one?

MR. McGLOTHLIN: No, Commissioner.

COMMISSIONER EASLEY: Okay, sorry.

COMMISSIONER GUNTER: This is part of the one -- if I'm not mistaken, isn't this part of the one that Commissioner Herndon talked about having some questions on?

COMMISSIONER HERNDON: Yes.

(Exhibit No. 213 marked for identification.)

Q (By Mr. McGlothlin) You have been handed a document identified as Exhibit 213 and captioned "1989 to 1998 Change of Power Plant Site Plan." Do you have that before you, Mr. Waters?

A Yes, I do.

Q Will you turn to what is marked as Page 38 of that document, please? (Pause)

A Okay, I have it.
Q And for the entry by the column for the St. Johns River Power Park, based upon the information shown there would you agree that the St. Johns Units were designed to be coal-burning, also?
A Yes, sir.
Q And do you agree that the in-service date is 1987 for that unit?
A That is correct.
Q Would that be applicable to the first of those two units, Mr. Waters, that the '87 date is entered twice? Do you know whether that is applicable to both units or just the first one?
A The March '87 date only applies to Unit 1. Unit 2 came in service in 1988.
Q And under the net capability there is 125 megawatts entered for each of the two units. Is it true that FPL's ownership interest is 250 megawatts in that site?
A FPL's ownership interest is 20% of the net rating. That results in the 125 shown in this table.
Q In fact, in terms of the overall size of the units, the St. Johns Power Units are about 600 megawatts, is that correct?
A They are nominally rated 600 megawatt units, that's correct.
Q Now, turn to the last page of the document that you

have. St. Johns River Power Park is shown as the last entry on the column there. Is it true that those units utilize flue gas desulfurization, also?

A Yes, sir. That's what is listed for the sulfur removal system.

Q Now, with respect to the size of units, do you agree that there are economies of scale at work such that the larger the unit the lower the cost per kW of that unit?

A There is a theory to that effect. I don't necessarily subscribe to it because there is no evidence at this time to show that 800 megawatt units in service today have actually come in service cheaper than the smaller unit. There is not enough data points to make that conclusion.

Q You say there is a theory in effect. Would you believe that other knowledgeable persons believe that relationship holds true?

A I know that a number of people believe that to be true. But I'm saying that from practical evidence to date, actual units in service, I don't think that there is enough data to draw that conclusion. Certainly in the smaller sizes, when we are talking about 200 to 400 megawatt units, and even up to the 600 megawatt class, that appears to have been the experience. But 800 megawatts I don't believe have been that much cheaper.

Q Turn to Page 40 of this document. In the far right-hand column it shows the total investment FPL has in its ownership share of the St. Johns River Park plans, is that right?

A The numbers shown there in building and equipment, it's difficult to say. That should represent FPL's ownership portion but that does not represent necessarily 20% of the total cost. There may be other facilities that may be accounted for separately.

Q Well, there is a total column of $306,530,000. Would you agree that that's FPL's investment in this ownership share?

A That's what we are showing to date, that's correct.

Q All right. Please divide that number by the 250 megawatts owned and see if you agree with me that the cost per kW of the St. Johns Unit, which had an in-service date of 1987 and 1988, was in the neighborhood of $1,225 per kW.

A Yes, sir, that's approximately what I get. However, we have to be very careful when comparing St. Johns to the Martin Units. We have to remember that St. Johns is a joint project; that it was financed differently, and much of the financing was done by Jacksonville. 80% of the financing, in fact, was done by Jacksonville at a lower debt rate than FPL would have been able to finance the project. The accounting is done through a separate entity. The St. Johns River Power Park has its own organization, its own management organization, its own accounting. So it's difficult to draw the conclusion here that this is exactly comparable.

Q How would the fact that the entity has a separate accounting group bear on the comparison of the investment costs?

A I'm not sure. I'm simply stating that it is accounted for differently, that there is a separate entity in existance that handles the management of the St. Johns River Power Park.

(Pause)

CHAIRMAN WILSON: Are you going to leave that piece?

MR. McGLOTHLIN: Yes, sir.

COMMISSIONER GUNTER: Let me ask you a question, and I'm trying to understand this now. It is my recollection that in the determination of need proceedings that the primary thrust of that project was, one, and I guess the primary, was that the only difference -- you know, because a plant is really a plant to plant except for where you site it and perhaps some transportation costs having to do with the fuel that you deliver and some differential there. But the primary thrust of that which was presented to the Commission was the uniqueness in the financing arrangement, which that was the last one that could be done that way because of the timing and the change in the law. Is my recollection of that correct?

WITNESS WATERS: That's my understanding, Commissioner. I was not involved in that proceeding.

COMMISSIONER GUNTER: So if we are looking at differentials and we really want, you know, to kind of get down with some preciseness, the only differential that would have occurred would have been the difference in the cost to finance the project?

WITNESS WATERS: That would be the primary difference.

COMMISSIONER GUNTER: All right, I just wanted to make sure I understood that because we are trying to get down now to address a question I think, and where Mr. McGlothlin is going and one that I think we have some interest in, is in the projected construction costs of Martin 3 and 4 in the same time period, the same general time period, that St. Johns Power Park would be. And we just want to make sure we understand where there could be any differences. And that would be the only material difference.

WITNESS WATERS: There is one other difference, Commissioner, that I would like to point out.

COMMISSIONER GUNTER: Is it a material difference?

WITNESS WATERS: I think it is a very material difference; that is, that the St. Johns Units, as originally projected, were 550 megawatts, not 625. That was the design basis; that was the basis for all projections until the units came in service. It was not until after they were in service that due to the fuel they used, due to the testing results, and so on, they were uprated to 625. So there is more than a 10% increase in the rating of that unit from its design basis. And we have no reason to suspect that it wouldn't be possible for the Martin Units to experience that same change which would, of course, lower the dollars per kilowatt that we are trying to compare here.

COMMISSIONER GUNTER: I know your recollection, I mean your information, is current, but I think I have down in my office the handouts that were given at the opening of St. Johns Power Park 1, of St. Johns 1, and I thought it was a 600 megawatt and had been upgraded to something like 638 or 643 or something like that. I thought those were the figures.

WITNESS WATERS: Well, we are talking basically the same thing here, but I tend to use net numbers because that's what comes out on the system.

COMMISSIONER GUNTER: I understand, but I was using the bus bar, you know.

WITNESS WATERS: St. Johns is a 600 megawatt nominal unit, that was the design basis, with 550 megawatts net to the system. That was uprated. I don't know the nominal uprating but I know the net uprating went from 550 to 625.

COMMISSIONER GUNTER: Okay. My recollection, you know, was a little different there. But still you have to build a plant recognizing the down rating or the derating with scrubbers, and what have you, and the internal use of the facility. But nobody gives you that; you have got to build it and pay for it.

WITNESS WATERS: That's right.

COMMISSIONER GUNTER: Okay.

Q (By Mr. McGlothlin) Mr. Waters, would you agree that in calculating the cost to FPL we didn't use 600, 575 or 625, we used its actual 250 megawatt ownership for that purpose?

A Well, calculating the cost to FPL, if the rating was originally 550 we would have owned 20% of that, so it would not be be 250 based on the original projections. That was the end result but we would have taken 20% of that 550, not 625.

Q Is it true that Florida Power and Light is using an assumption of 700 megawatts for purposes of calculating the deferral benefits applicable to Martin Unit No. 3?

A That's what we show in our calculations. The megawatts of deferral are really not that relevant to the calculation. It's basically the dollars when the unit comes in service. We show the 700 megawatts as simply a convenience on the form.

Q Do you have occasion to utilize a capacity value for PROMOD runs applicable to the unit?

A The rating we use in PROMOD I believe is 730 megawatts, which is the net rating we expected. That would be for a nominal 800 megawatt clash unit.

Q I think you said earlier that the most material difference between the St. Johns Plant and the Martin 3 Plant would be the financing cost, is that correct?

A Well, I have said that there are two material differences: One, of course, is financing, and the other is uprating, which we had no way of knowing what the final rating of Martin would have been. In a proper comparison between St. Johns and Martin it might be appropriate to use the original rating of St. Johns.

Q Would you agree that one of the principle components of financing is that of paid AFUDC?

A Well, if I can restructure your question a little bit, it's the result of the cost of financing is AFUDC, so that is the financing cost of the unit.

Q And incorporated in the calculation of AFUDC is an assumed return on equity, is that correct?

A That's correct.

Q So if we wanted to get some appreciation of the comparison between St. Johns and its financing costs and that assumed from Martin No. 3, would it be appropriate to look at the cost of equity that was assumed in calculating AFUDC from Martin 3 over time?

A We could make that comparison. Of course, the Martin estimates include the actual AFUDC experienced during the construction period so that would already be included in our estimates.

Q What do you mean by actual experience, Mr. Waters?

A It's the cost of capital to FPL in the given year of construction.

Q Over time what assumption of return on equity has been incorporated into AFUDC calculated for Martin plants?

A I'm not sure -- it was a year by year calculation. So I can't give you a number for return on equity. It would vary by year. During the construction period.

Q What is it currently?

A Well, currently it wouldn't be -- I don't know what the current number is, but that wouldn't be relevant because we're talking about AFUDC during construction here.

Q Do you also calculate post construction carrying cost applicable to the unit?

A I don't do that personally but it is done in the calculation.

Q If you know, what return on equity is applied to Martin 3 for post construction carrying costs?

A I believe the return on equity during post construction is 15.6.

COMMISSIONER GUNTER: What would be included in post construction costs, which you would still be allowed to capitalize?

WITNESS WATERS: There is -- the question I just answered was how the carring charge was done. So there is really no post construction cost being added, it's simply the return on the investment at that point. But there are typically post construction additions to particularly coal units, where there are upgrades, change outs, modifications to the unit, after it comes in service. So usually some capital charges associate with it, and we don't try and account for those in a -- what I'll call a planning unit of this nature.

COMMISSIONER GUNTER: Let me see if I understand the bookkeeping there a little bit.

If a plant is up running, if a coal plant, construction is completed and it's up running, any changes or modifications you make to it you use -- you capitalize AFUDC on it after the plant is in service?

WITNESS WATERS: I don't know that AFUDC is capitalized, Commissioner.

COMMISSIONER GUNTER: See I'm trying to understand the question and the response. Because my understanding of the question that you responded to from Mr. McGlothlin was AFUDC after construction is complete, and the term you used was post construction expenses. I'm trying to find out what kind of expenses are post construction if, in fact, it's been completed and the plant's in service. I'm trying to understand the bookkeeping.

WITNESS WATERS: If I led to the confusion, I'm sorry. AFUDC is only applied during the construction period up to the point where the unit comes in service. But, there are in calculating the carrying charges after the unit goes in service, the revenue requirements, there is a return.

COMMISSIONER GUNTER: All right. I understand that. I understand the response now. I didn't understand it with the question and the response. Excuse me, I apologize, Mr. McGlothlin.

MR. McGLOTHLIN: That's all right.

Q (By Mr. McGlothlin) Mr. Waters, just to make the comparison clear, even with the revised inflation assumptions and cost of capital assumptions, FP&L has utilized a value per kW of over $2,000 for Martin 3 in calculating the impact on net savings, is that correct?

A $2,000 a kilowatt for both units?

Q Yes.

A One unit. It's approximately $2,000 a kilowatt, total installed cost for the two units.

Q Are you aware of any other coal-fired units with scrubbers in the range of 600 to 800 megawatts that were installed in the 1987 time frame at over $2,000 per kW?

A I've not done that comparison to determine total installed costs on other units. I can say that as far as comparison to St. Johns, that comparison was done in 1987 by FP&L on a direct cost basis, without escalation in AFUDC, and that St. Johns costs, I believe, were within 2% of the Martin direct cost estimate. (Pause)

Q Mr. Waters, please turn to Page 31 of your rebuttal testimony.

A All right.

Q Your response at Line 7 says, "Based on your judgment, Martin 3 would have been the most economic choice to meet a required in-service date of 1987."

A That's correct.

Q The 1987 in-service date was an assumption which was carried forward from the 1982 qualification proceedings, is that correct?

A Yes.

Q And that was based upon the projections of load and the generation expansion plan that was performed at the time?

A Yes, sir. And that's really the only relevant comparison you can make, is what the decision would have been in 1982. That was at the point where we had to either defer the unit or proceed with this project.

Q Would you agree that a well run utility monitors its load growth and adjusts its expansion plan over time to account for any changes and to enable it to meet changes in the most economical fashion?

A I would agree with that as sort of a grand philosophical statement. However, I think it's important to realize that is a terrible oversimplification of what we do in the planning process. You don't simply change or defer units simply because your load forecast has changed. In this case, for example, in 1983 we would have, if we had been building Martin, spent a fair amount of money on the Martin unit. To say that we would simply defer it and keep incurring interest charges on the money that we had spent I think is an oversimplification. We would have had to do an analysis at that point to see what the most cost effective course would be.

Q But there would have been an ongoing analysis, is that correct?

A The planning process is continual.

Q And depending on the results of the analysis, the Company would have adjusted its plan and its expansion plan accordingly, is that correct?

A Well, without doing the analysis I can't say whether there would be any adjustments to the expansion plan or not.

COMMISSIONER EASLEY: Are you about to leave that, counselor? Are you about to leave that?

MR. McGLOTHLIN: I just wanted to confer a moment, Commissioner. (Pause)

CHAIRMAN WILSON: Do you have questions, Commissioners? Go ahead.

COMMISSIONER EASLEY: I'd like to clarify this area that we're talking about. Looking at Pages 18, 19 and 20 of the direct testimony, and particularly the question and answer on Page 19, beginning on Line 1, the question on Line 1, the answer on Line 3. Is the methodology or the computations that you all are talking about different now than were part of your answer on Page 19? I don't know how to phrase that any differently. There was a levelized oil backout recovery factor of .886 cents per kilowatt hour for the period of October of '88 through March of '89. In listening and looking back over some of this we're talking about the same plants, Martin's 3 and 4 and we're talking about St. Johns being in there at some point. What I'm asking is, are the methodologies and are the calculations that resulted in this .886 the same now?

WITNESS WATERS: Yes. The methodology has really never changed. The issue is when did capacity deferral benefits first appear in the calculation.

Technically there was always in the methodology an accounting for deferred capacity benefits but they did not appear until 1987.

COMMISSIONER EASLEY: But there were factors approved subsequent to that first appearance of deferral, without objection by anybody?

WITNESS WATERS: Yes.

COMMISSIONER EASLEY: Thank you.

Q (By Mr. McGlothlin) Mr. Waters, I believe it follows from your earlier statement, and also follows from a review of your testimony, that you have not, in this proceeding, submitted an analysis designed to identify the least cost generation expansion plan from '82-83 forward, assuming the absence of the Southern contract, to verify either the 1987, assumed 1987 in-service date or the least cost generation alternative that would have fallen out of that analysis.

A Let me disagree with that.

Q Excuse me, sir. Have you performed it or not?

A There is two pieces to your question. I can't answer it "yes" or "no" because part of it is yes, and part of it is no.

I have not done an analysis year by year through time to show the in-service date should be 1987. No, I've not performed that. However, in my rebuttal testimony, in Document 3, I have done a year-by-year analysis of the economics comparing Martin 3 to combined cycle units, which was implied in testimony that would be the least cost alternative. And what I've shown in Document No. 3, which I've distributed, is that it does not make sense to consider combined cycle as an alternative to Martin 3. We would not have done that in the period of '82-85. Due to the oil forecast and due to the sunk cost in Martin 3 that would have been incurred had we been building that unit. I guess I would take issue with the statement that I have not perform a least cost analysis. I have compared those two alternatives.

Q Is this the same kind of analysis you performed in the annual planning document, Mr. Waters?

A It's similar, but different. The annual planning hearing analysis is much more extensive than just one document, of course. But we do compare whole units to combined cycle units. However, there is one major difference in this analysis. This is showing the analysis based on incurring costs of an actual unit. This is not just a planning study where we are looking to provide need sometime in the future. This is looking at a scenario where we would have been incurring costs to build Martin 3.

Q Do you have Document No. 3 in front of you?

A Yes.

Q At the top, this statement appears; "Required in-service date, 1987." Is it true that the required in-service date was a given, an assumption in this analysis?

A It was a given for two reasons. First it was what appeared in Mr. Scalf's testimony in the original qualification proceedings.

Q When was that, Mr. Waters.

A That was in 1982. Also it's in Mr. Pollock's own testimony that our actual loads in 1987 and 1988 were within 4% of what was forecast in 1982. In fact, the 1988 actual load was to the megawatt what was forecast in 1982 So I have no reason to make any changes to the in-service date of Martin 3 and 4.

Q You assumed the in-service date in 1987 based upon Mr. Scalf's testimony in 1982 and a reference to Mr. Pollock's testimony in this proceeding?

A Yes.

Q Anything else?

A That's basically how I got there.

Q In making the comparisons which appear on Document No. 3 what return on equity did you incorporate?

A In Document No. 3?

Q Yes.

A In calculating the capital revenue requirements I've actually used a return on equity -- I'm trying to remember the exact number, it was not 15.6, it was lower. It was our 1988 projection so it was something more on the order of 13-1/2 but I'd have to check the exact number.

CHAIRMAN WILSON: Do you have a document that reflects that, or when do you need to check on that?

WITNESS WATERS: I can provide that, Commissioner. I don't think I have it with me. It's based on our financial forecast for 1988. And it goes into the calculation. In my Footnote 1 I have a levelized fix carrying charge rate of 17%. I have to go back and gather the assumptions that went into. But that's more of a current projection. That was not the original projection for Martin.

Q (By Mr. McGlothlin) Mr. Waters you've --

CHAIRMAN WILSON: Could we have a late-filed exhibit? When could we get that?

WITNESS WATERS: We can get that shortly. I just have to go back to some documents, make a phone call, and get the actual document, the financial forecast.

Q (By Mr. McGlothlin) Just to follow through on that last question, Mr. Waters, as I understand it, you've utilized a return on equity in the neighborhood of 13.5 or .6% which represents the company's forecasting assumption, is that correct?

A That's correct. I'm using the forecast assumption. It's an incremental cost of capital assumption that we use for planning purposes.

Q Would I be correct in assuming that the values for Martin Unit No. 3, which appear on Document 3, incorporate some sunk costs that reflect a 15.6 return on equity?

A The sunk costs reflected in these numbers are the actual cash flows reflected in the testimony we have been filing for oil backout. In other words, they reflect actual cost of capital incurred, so it's not a 15 6 assumption. It's actual year-by-year cost of capital during the construction period.

Q And what was that?

A Again I don't know. I'd have to check that since it changes year-by-year.

Q Is it something other than the authorized return on equity that's incorporated?

A I don't know. I'd have to look. It's the period 1980 through '86 and each year would be a different factor, so I'd have to get that information.

Q Would that information be available to you while you're here today? Is that something we can come back to and verify?

A Yes.

Q In your testimony you describe that Florida Power and Light Company first presented testimony concerning the deferral benefits in 1987, is that correct?

A That's correct. As far as calculating the oil backout factor, that's correct.

Q Isn't it true that the testimony presented at that time carried forward the 1982 assumption about the 1987 in-service date?

A I believe that would be correct.

Q The testimony submitted in 1987 did not include an analysis designed to verify the 1987 date assuming the absence of the Southern contract over time, is that correct?

A To my knowledge there was no analysis to show that '87 would be the in-service date. But that in-service date was not questioned in that proceeding or any other since, until this time.

Q You testified a few minutes ago that it's important not to oversimplify the planning process and that the planning process takes into account a variety of things.

Is it true that among those things are such considerations as the availability of capacity from other utilities adjacent to FP&L to meet the capacity needs?

A Yes, that's correct. We would look, of course, at sources of other power aside from constructing new units.

Q Would it also include some consideration of demand side alternatives such as interruptible rates to meet the system requirements?

A Yes, it would.

Q Would it include consideration of short-term alternatives like combustion turbines that could be used as a bridge to enable the Utility to defer larger units?

A To paraphrase an expression that's been used at FP&L, combustion turbines are a monument to poor planning. I would not like to think that using a bridge to fill in the gap would be a normal part of the planning process. That's how you react if you have not done the proper planning. So no, I wouldn't consider that part of the planning procession. Looking at installing combustion turbines over the life of the unit, yes, we would look at that.

Q Does FP&L have any combustion turbines on its system?

A Certainly.

Q Would the analysis include some consideration of deferring a unit even if construction had begun on the unit, if that were the economical thing to do?

A If an analysis showed that deferral of the unit was the economic thing to do, then that would be the recommendation to management, they would make that decision. But we've done no such analysis to show that that would have been possible in the time frame we're talking about here.

Q Would the analysis include some consideration of the impact on reliability of interties to other utility systems?

A The planning analysis or the deferral analysis?

Q The planning analysis.

A The planning analysis would account for any tie lines and availability of assistance from other systems.

Q Would such interties have the effect of reducing the reserve requirements on the individual system?

A No, not necessarily. It is possible that that could be one outcome. There are a number of factors. Since FP&L uses two criteria for planning, one is reserve margin and one is loss of load probability. It is possible to have a reduction in reserve margin due to many factors, including transmission ties. However, when you lower the reserve margin you're deferring capacity essentially or avoiding capacity. It's the same impact we're talking about here. So it's really not a separate effect as such. It is one and the same as what we have been talking about here, deferring Martin 3 and 4. That is one of the benefits of our ties to Southern, and we've always acknowledged that.

MR. McGLOTHLIN: Commissioners, I'm going to change subjects, and I could use two minute recess.

CHAIRMAN WILSON: Let's take about a 10 minute break. This will give you an opportunity to make those phone calls that you were going to make.

(Brief recess)

CHAIRMAN WILSON: Call the hearing back to order.

Q (By Mr. McGlothlin) Mr. Waters, would you agree that the choice a prudent planner would make to meet a system need requirement would depend in part upon the timing of that need?

A I'm not quite sure how to answer that question. If you're saying that the time required to construct, the time required to site and license, all those things would have to be considered in the prudent choice; yes, I'd say that would have to be considered.

Q The choices and the actions a planner would make would depend in part upon the time when the load materialized that you were planning to meet, is that correct?

A When the expected load developed a need, yes, and I think that is one of the problems with the assertion that we could have changed technologies, for example, in 1987.

We could not have reacted in 1985, for example, to change technologies to meet the need in 1987. We could not have changed from a Martin 3 and 4 to a combined cycle unit. You can't site license and construct a different kind of unit in two years; even combustion turbines, that's an awful short schedule. So we do have to account for the timing, which is one of the issues in my testimony, saying that we had to make the decision on Martin 3 and 4 in the early '80s; certainly by 1982 that decision would have been made.

Q Mr. Waters, in addition to Florida Power and Light's ownership interest in the St. Johns plants, FP&L purchases capacity from that site, is that correct?

A From the JEA units, yes.

Q And those purchases include a capacity charge, do they not?

A We are purchasing capacity. I don't know the form the payments take. I would assume there would be a capacity charge.

Q And there is no separate mechanism, rate mechanism for the recovery of those capacity charges so they are recovered in base rates, is that correct?

A I do not know how we're recovering any charges for Jacksonville right now.

Q Are you familiar with the fact that FPL purchased capacity from TECO during the '85 to '87 time frame?

A Yes, sir, we did purchase powe. from the Big Bend Unit at TECO.

Q Do you know whether those capacity costs were recovered through base rates?

A I believe the capacity costs were recovered through base rates for that purchase.

Q The predecessor in your position was Mr. Smith, is that correct?

A That's correct.

Q I'm going to distribute a document and ask the witness to refer to it. (Hands document to witness.)

CHAIRMAN WILSON: Do we need to give this a number?

MR. McGLOTHLIN: Yes, sir.

CHAIRMAN WILSON: What would be the next Exhibit number, Mr. Pruitt?

MR. PRUITT: 214.

CHAIRMAN WILSON: 214.

(Exhibit No. 214 marked for identification.)

MR. GUYTON: Joe, is this complete?

MR. McGLOTHLIN: I intend it to be. Let me check with Mr. Pollock. (Pause) Charles, we've obtained this through discovery as one of your response to request of documents and this is what we obtained at the time.

MR. GUYTON: Could you, just a minute to --

CHAIRMAN WILSON: Yes. (Pause) We'll take just a minute while he checks. It's a four-page documents and the last page is No. 10. It raises a question. They may number their documents the way we do our exhibits. (Laughter)

MR. GUYTON: Excuse me. Thank you, Commissioner. My apologies, Joe.

CHAIRMAN WILSON: Is this your complete response to their interrogatory request, or their production request?

MR. GUYTON: It doesn't appear to be. There appears to be a page missing from it.

CHAIRMAN WILSON: Oh, there does? Okay.

MR. McGLOTHLIN: I'm going to use this for a very limited purpose. Could I ask the questions to see if you have a problem with it?

MR. GUYTON: Sure.

Q (By Mr. McGlothlin) Mr. Waters, you have before you a document numbered 214 which is a memorandum from Mr. Whiting to

Mr. Meader.

A That's correct.

Q Would you turn to page marked No. 10 and review Paragraphs No. 2 and 3, Unit Power purchase from TECO, Unit Power Purchase from St. Johns. (Pause)

My question to you, after you review it, is whether you agree if based on this document, Florida Power and Light Company recovered -- is recovering the capacity costs of both those transactions with TECO and St. Johns JEA, the capacity costs are being recovered through base rates?

MR. GUYTON: I'm sorry. Have we established that Mr. Waters is familiar with this document? Have we?

A I have not seen this document before. The only thing I can assume here, it says, "assumptions used to develop forcasted data for '87, '88 and '89." I don't know that that indicates that actual recovery has occurred for any of these. This is a computer model used by the Company. So I still don't know whether actual recovery takes place through these clauses or not. I do believe Tampa was recovered through base rates but I don't know about St. Johns.

CHAIRMAN WILSON: All right.

Q (By Mr. McGlothlin) Mr. Waters, I'd like you to refer to Pages 23 of your rebuttal testimony and 17 of your direct testimony.

COMMISSIONER GUNTER: 17 and 23 was that?

MR. McGLOTHLIN: That's right. 17 of the direct, 23 of the rebuttal.

COMMISSIONER GUNTER: I've got you.

You would ask for a page they didn't give me a copy of. I ain't got Page 23 on rebuttal, I've got 22 and 24. That's all right. Some how Ms. Easley and I are getting short sheeted.

COMMISSIONER EASLEY: We don't need to know.

CHAIRMAN WILSON: It was a test.

Q (By Mr. McGlothlin) In the preparation of your testimony, Mr. Waters, you reviewed the oil backout rule with some care, did you not?

A Yes.

Q On Page 23 of your direct testimony you state that the rule explicitly defines what costs may be recovered. Do you see that statement?

A Yes.

Q And if you need for refer to the rule, is it true that you have delineated here in exact form those items of recovery which are explicitly authorized and defined by the rule?

A I've basically paraphrased or summarized the rule. It's not the exact wording in the rule.

Q Have you incorporated all the items of recovery there are contained in the rule?

A I believe so, correct, in Section 4-A of the rule.

Q And when you did that again in your rebuttal testimony, is the list the same?

A That's correct. That's what those pages show.

Q The straight-line depreciation of the project is the first item mentioned. Does that relate to the recovery of the investment in the transmission line project?

A Yes. The rule states that it's of the qualified oil backout project, which in this case would be the 500 kV line project.

Q The cost of capital of the project, would that be the cost of capital associated with the transmission line?

A That's correct.

Q The actual tax expense, would that be the tax expense associated with the building of the transmission line?

A That's the way the rule reads, that's correct.

Q The oil and the non-oil O&M expense differential, what would that consist of?

A Well, I believe it's really a matter of how the Commission has interpreted this. In Order 11210 I've stated they've allowed recovery of capacity charges and wheeling charges from Southern Company, and I would suspect that this particular item is how the Commission interpreted, or how they came to the conclusion that we could recover capacity and wheeling charges. That what we're comparing is a case where we are burning oil to a case where we're not burning oil, and the difference in expenses in those two cased includes capacity and wheeling charges.

Q So your contention is that the capacity charges constitute an O&M expense?

A I believe it's been interpreted that way. Again you're asking me to interpret a Commission ruling since it is in the order that we can recover those charges. And I'm not sure it's explicit in that ruling, in that order, as to which of these components the Commission used to authorize that recovery.

Q Is it possible that it is not in any of the components?

A Well, if what you're asking is did the Commission authorize something that's not allowed according to the rule, I can't answer that question. I don't think that's the case.

Q In your opinion is capacity charge paid to Southern Company a form of O&M expense?

CHAIRMAN WILSON: A form of what?

MR. McGLOTHLIN: O&M expense.

WITNESS WATERS: I think as applied in this case it is.

MR. McGLOTHLIN: Very good.

Q Mr. Waters, one possible resolution of the issues in this proceeding is the decision by the Commission to make no adjustment with respect to the amount of accelerated depreciation taken. In that event is it true that the investment in the transmission line will have been recovered as of August 1989?

A That's my understanding, that's correct.

Q Is it true that the oil backout rule requires that once the investment in the project is recovered and depreciation achieved, that the application of the charge will terminate?

A No, I don't think that's what's required by the rule at all. I think the rule requires that charges be -- of course, the collection of capital for the project would terminate, but the expenses associated with the project would continue under the oil backout clause until such time as it's put in the company's base rates.

Q Would you point us to the language in the rule that you think supports that?

A In Section 4-C of the rule it states that, "Upon full depreciation of the qualified oil backout project, cost recovery pursuant to 25-17.15 Section 4-(a)(1)," which I think is a typo. I don't think that there is a 1 to be applied here -- "shall terminate and only the actual oil, non-oil, operating and maintenance expense differential exclusive of fuel expense of the qualified oil backout project, which would normally be included in base rates, shall be recovered through the oil backout cost recovery factor until such time as these costs are included in the base rates of the utility."

Q Tell me again what you think is incorporated in the oil, non-oil, operating and maintenance expense differential which would continue to be recovered?

A We would have O&M expenses of the transmission line itself, and I think the capacity and wheeling charges associated with the Southern purchases would be included in that.

Q How are the capacity charges of the Southern purchases related to the O&M expenses of the transmission line?

A I'm not sure I understand the question. I don't think there is a direct relationship other than the megawatts we buy may have some impact on how much maintenance and operating expense we incur on the lines. But I don't think there is a direct correspondence between the dollars.

Q If Florida Power and Light Company built the transmission line and not enter the UPS contracts, would the O&M expenses of the line have been materially different from those which you are calculating today?

A Possibly not. I have no way of determining that. But that's not one of the scenarios under analysis here. The qualification proceeding really compared two cases: The with-the-project case and the without-the-project case, and those are the differentials we're talking about here. This was covered in the qualification proceeding. In fact, the issue of whether the lines would have been built without oil backout factor was completely covered in the original 1982 qualification proceeding.

Q Yes, sir. But your contention that FP&L would be entitled to recover capacity charges, even if investment in the line had been fully depreciated, is dependent upon your assertion that the capacity charge paid for the capacity of the Southern plants is included in the O&M differential identified in the rule, is that correct?

A It's not really my assertion. That's my reading of what the Commission has allowed us to do since the inception of the factor.

Q You do not assert that the capacity charges belong in the O&M entry then, is that correct?

A I'm simply agreeing with the Commission. If you want to call it my assertion that's fine. I think since the original, the first oil backout recovery factor we have been recovering those charges through a backout recovery factor.

CHAIRMAN WILSON: The distinction, though, is capacity charges are not an O&M expense.

WITNESS WATERS: Not normally.

CHAIRMAN WILSON: They may have been recovered through oil backout recovery clause, but you would not ordinarily consider --

WITNESS WATERS: Ordinarily, no, sir, and if we stick to that definition, though, there would be no recovery of capacity charges at all because of the way the rule is written. And I'm simply assuming that the Commission has interpreted that particular section to allow capacity charges in the oil backout cost recovery factor.

Q (By Mr. McGlothlin) You were making that interpretation, but you personally do not believe that it's an O&M expense, correct?

A Under normal circumstances, normal firm capacity purchases to provide capacity for the system would not be. However, these capacity purchases were not intended to primarily displace load on the system. The primary purpose of this project, including the purchases from Southern, was to economically displace oil-fired generation.

Q So you don't interpret, you don't contend that capacity charges constitute O&M expense, and you cannot point me to any statement by the Commission in its order that would support that same interpretation, can you?

A I don't believe the Commission explicitly stated that. But they did state that they believe that the energy savings of this project required that we pay capacity and wheeling charges to Southern and that's why they have been included in this particular project.

MR. McGLOTHLIN: Those are all the questions I have.

CHAIRMAN WILSON: Did you discover what rate of return was assumed in your chart, I think was it six or three? Your revised Document No. 3 Mr. McGlothlin was asking you some questions about and we asked you what --

WITNESS WATERS: The entire capital structure is what I've asked for; it's on the way. I still don't have those numbers.

CHAIRMAN WILSON: They didn't tell you when you called and asked what the number was for equity?

WITNESS WATERS: No, I had someone call for me, so I didn't talk to the person direct.

I did learn as far as AFUDC rates are concerned on the Martin project, although I don't have those numbers yet, that what was used was the Commission-approved return on equity in each year of the construction period, so in calculating AFUDC for the Martin units that would have come on line in '87 and '88, that was the methodology.

CHAIRMAN WILSON: But you don't have that number?

WITNESS WATERS: No. Those are on the way also. Should be here shortly.

CHAIRMAN WILSON: Ms. Rule, do you have any questions?

MS. RULE: Yes, I have a few questions.

CROSS EXAMINATION

BY MS. RULE:

Q Mr. Waters, are you familiar with FPL's current power supply expansion plan?

A Yes, I am.

Q And that's set forth in FPL's petition to determine need for electrical power plant 1993 to 1996 which is currently pending before the Commission, is it not?

A Yes.

Q The expansion plan currently calls for two units designated Martin Units 3 and 4, doesn't it?

A Yes. Those shouldn't be confused with the Martin Units 3 and 4 we're talking about here. The numbering system is simply what's built next at Martin gets the number Unit 3 and one following that one Unit 4. And in this case you're referring to combined cycle units.

Q And those in-service dates for the new -- I'll call them the new Units 3 and 4, would be 1994 and 1995, correct?

A For the combined cycle units, that's correct.

Q The Martin 3 and 4 units for which FP&L currently receives deferral benefits were to serve essentially the same function as these newer Martin 3 and 4 units, is that correct?

A If you mean that the deferred units were to meet system load growth, I guess in general philosophically you're correct, but obviously we're not serving the same load. Martin Units 3 and 4 you're referring to, of course, are after the Southern purchases of 2,000 megawatts, and there are a number of other changes at this point.

Q But both the current planned Martin 3 and 4 and the earlier planned Martin 3 and 4 were intended to serve base load, were they not?

A To serve base load? We don't look at a unit as serving a particular segment of load, but Martin Units 3 and 4 are expected to run at a high capacity factor, if that's your question.

Q Why does FP&L now propose combined cycle technology rather than traditional base load coal capacity?

A There are several reasons for that. Let me delineate a couple of important ones. Of course, one is the economic analysis which shows that with the reduced oil and gas forecast we expect the combined cycles to provide better economics. But beyond that, and maybe the most important reason, is this very proceeding shows how uncertainty in the planning process causes us to look for solutions that offer the most flexibility in addition to the best economics. Here we have made a decision to backout oil, we've made a decision to buy coal-fired energy and that decision has been called into question here.

The decision to build a combined cycle running on natural gas may be called into question at some later date. But the combined cycle offers us the option of burning natural gas or coal, and we consider that to be a very important factor in developing the expansion plan is flexibility. We need to be flexible, not only in the fuel sources but in load growth. One of the issues that's been raised here is load forecast, changing year-by-year. Combined cycle offers us some flexibility in responding to load growth also, we can build it in phases. We can put segments in, like combustion turbines, and follow with a steam system later. So it's a very flexible type plan.

Q The Utility should continually adapt generation expansion plans to reflect not only improved technology but changed conditions?

A To the maximum extent possible, yes. And, of course, I've qualified that by saying you have to look at the economics of trying to respond and many other factors in doing that.

Q Mr. Waters, the combined cycle plants that are planned and currently designated as Martin Units 3 and 4 in the expansion plan, how would you characterize the operation? Would they be serving peak load, intermediate or base load capacity?

A Well, again I don't like to use those terms. It implies that each unit serves a particular part of the load shape. But we do expect them to run at a high load factor. Megawatts are megawatts. Once they are on the system they are all mixed up; you can't say that megawatt from a particular unit went to a particular customer.

Q Does a high load factor imply base load?

A That's the way most people interpret it, that's correct.

Q So although plans for Martin 3 and 4 now incorporate improved generating technology, FP&L still plans Martin Units 3 and 4 to serve base load capacity?

A You keep trying to hook me in on that phrase. They will run at a high capacity factor. In fact, the combined cycles would run at a higher capacity factor than the Martin units due to the higher availability of a combined cycle unit, which is, of course, another factor in the analysis. But they would both run at very high capacity factors, yes.

MS. RULE: Thank you. No further questions.

CHAIRMAN WILSON: Did you get what you wanted, finally?

MS. RULE: I think so.

CHAIRMAN WILSON: When will you have those numbers available for us?

WITNESS WATERS: The return on equity used in that Document No. 3 is 14-1/2%.

CHAIRMAN WILSON: What about the AFUDC calculations?

WITNESS WATERS: I still haven't received those numbers.

CHAIRMAN WILSON: You haven't got those yet.

COMMISSIONER GUNTER: When you do that -- when you provide that AFUDC calculation, because you do it on a year-by-year basis, could you give us the capital structure of each individual year that gave rise to that AFUDC figure rather than just having a flat figure?

CHAIRMAN WILSON: We should have those calculations here at the Commission, shouldn't we?

MR. GUYTON: It's just now being provided to the witness. We can identify that as an exhibit. If you'd like we can do that at this time.

WITNESS WATERS: Okay. Yes, I have those now.

CHAIRMAN WILSON: You have those now.

WITNESS WATERS: Yes, I have those now. It's year-by-year, and it shows the capital structure and the cost of capital for each component by year.

MR. GUYTON: Mr. Chairman, should we give that an exhibit number?

CHAIRMAN WILSON: I'm sorry, what?

MR. GUYTON: Should we give that an exhibit number?

CHAIRMAN WILSON: Yes, we should.

MR. PRUITT: 215.

CHAIRMAN WILSON: Exhibit 215.

(Exhibit No. 215 marked for identification.)

COMMISSIONER GUNTER: Let me ask you a question. This does not include all of the items. I'm just looking at 1979. This does not include all of the items that is used by this Commission in calculating your overall cost of capital, is that correct?

WITNESS WATERS: I'm not familiar with that, Commissioner.

COMMISSIONER GUNTER: Let's just walk down that piece. If you only have debt preferred and common, which all have a cost component, it would tend to have an increase in the overall cost of capital if you exclude, for purposes of your calculation, those components such as deferred income taxes, tax credits and what have you that carry a zero cost in the capital structure, would it not?

WITNESS WATERS: That's true.

COMMISSIONER GUNTER: Now, would it not be more appropriate to include -- to separate and include all of the components that are included for regulatory purposes, would it not be more appropriate to include all of the line items rather than just a pick and choose kind of thing?

WITNESS WATERS: It might be, Commissioner. This is a convention we use --

COMMISSIONER GUNTER: And let me give you an example.

Year ended 1987, your overall rate of return would be 9.31%. One of the problems I have with this sheet that was just passed out is that it doesn't really run the complete spread, it doesn't have the percentage of, for instance, year end 1987, 17.98% of the total from deferred income taxes, which carries a zero cost component. And, you know, 18% of a total at zero certainly has a dampening effect, and I don't think an unrealistic dampening effect because I'm not asking for a presentation that's different than this Commission has used, at least since I was here, and we began in '79 and '80 of including all of those items. Is that unfair to say you've got to do it the same way all the time? Or is there a rule or a pronouncement, one of those administrative bulletins which says you do it differently?

WITNESS WATERS: Not that I know of. I can only give you my perspective as a system planner, which is the limit of my expertise.

But we use in the planning process, and here what we've used incremented cost of capital. It's looking at if we went out and financed the project on a incremental basis what would the cost be and that's why these numbers appear this way.

COMMISSIONER GUNTER: In other words, you've come down to the point that you can identify money. You can identify dollars to a specific project. I've always been told that once -- that it's virtually impossible to do and usually it's spread over the total cost.

WITNESS WATERS: I think in practice that's true, but looking at planning, it's a planning convenience, if you will. Looking at specific projects and trying to compare Project A to Project B we look at the incremental cost of those two projects rather than trying to get into some of the factors.

COMMISSIONER GUNTER: We're allowing AFUDC and you're changing -- for instance, you've had a substantial, over a time period cost of debt. Those change, you know, as times change. When you start it, if we wanted to say fine, we'll just keep you where you are when you start at an equity percentage of 37.35 and a debt of 52.15 at those cost elements, I think you'd be screaming like a mashed cat when you got over into situations where your debt was over 15%, and at least 50% of it, you know, you're talking 126 basis points difference. As versus on a cost component you just went down 15 basis points. You know, if we wanted to play that game, and I'm just trying to get some realism in the calculation of AFUDC is to where -- you know, what's the appropriate methodology. Do you understand my concern?

WITNESS WATERS: Yes.

COMMISSIONER GUNTER: Okay.

WITNESS WATERS: Okay. Commissioner, it appears that in the actual AFUDC rate what we haven't included here on this sheet is the deferred taxes and ITC. But I'm told that we do include that in the calculation of AFUDC, but it's not here on this exhibit, so we would have to add that.

COMMISSIONER GUNTER: If we get an exhibit that gave us, and we could take -- have you got Mr. Pollock's exhibits there?

WITNESS WATERS: I believe so.

COMMISSIONER GUNTER: If you don't, I'd imagine somebody could run you one over real quick.

WITNESS WATERS: I think I've got them all here.

COMMISSIONER GUNTER: Just run him over your copy, Mr. Pollock, you've got it laying right there before you.

Schedule No. 13 is the last page in his exhibits, the last page.

WITNESS WATERS: Okay. I have that.

COMMISSIONER GUNTER: If he used his calculation, just say for walking around, would your AFUDC rate be 9.31%? Assume you accepted that calculation.

WITNESS WATERS: Okay.

COMMISSIONER GUNTER: Would that be your AFUDC rate?

WITNESS WATERS: I would guess so, based on these numbers.

COMMISSIONER GUNTER: All right. Then we would assume that your figures were the same as theirs. I don't know whether they are right or not.

WITNESS WATERS: Right.

COMMISSIONER GUNTER: But do you think we would have the same AFUDC rate with your 1987 figures for either Martin 3 or Martin 4, do you think the math would work out the same?

WITNESS WATERS: If we've included ITC and deferred taxes properly we should -- I don't know. Seems to match --

COMMISSIONER GUNTER: You understand? This to me is just doesn't tell me enough.

WITNESS WATERS: Right. Doesn't have all the information on it.

COMMISSIONER GUNTER: I just have to tell you all the information is not there for me to make any judgment or, you know, any logical conclusion. I might reach the wrong conclusion if that's what I had to use.

WITNESS WATERS: Okay. We can provide the fuller list.

COMMISSIONER GUNTER: One of my colleagues just said, "Pickey, pickey, pickey." (Laughter)

MR. GUYTON: Commissioner Gunter, Is that Late-filed Exhibit 216?

COMMISSIONER GUNTER: Well, I would think we're going to need that, and it would have to be a late filed. I certainly need it before I could go much further.

CHAIRMAN WILSON: What are you asking for, Commissioner Gunter, is that the calculation of the AFUDC rate for those years, or the calculation of the capitalization rate that was used in the calculation of the oil backout?

COMMISSIONER GUNTER: I would like to see the calculation that was used -- both; AFUDC rate for the company should have been the same AFUDC rate that was used for oil backout; it should be the same. Your cost of capital should be the same. You don't have two po.s over here, and the cost to the Company is what I'm interested in, ana I'd like to see all the cost components. I think that's fair. So that you get an indication of what the AFUDC rate that was calculated each year was. Because for instance, on this sheet that's handed out, you know, one of the questions that was asked is what was the AFUDC rate each year and what was the capital structure that supported that. Well, I don't even see the AFUDC rate each year.

WITNESS WATERS: The bottom line is not on there. We can provide that as a late-filed.

COMMISSIONER GUNTER: Both those pieces, and I don't think that's unfair.

MR. GUYTON: Commissioner Gunter, if I may point out to the rule, as to the incremental nature of the AFUDC rate of this project. Subsection 6-C of the rule --

COMMISSIONER GUNTER: Wait a minute. 6?

MR. GUYTON: C of the rule, oil backout rule.

COMMISSIONER GUNTER: 25-17.106.

MR. GUYTON: Yes, Subsection C. This speaks of capitalizing costs of capital on the project, the allowance for funds used during the construction, "rates shall be computed using the cost of capital used to fund the project," which has been treated, I think, consistently by this Commission as an incremental cost of capital during the course of the years that the project was funded. I just raised that --

COMMISSIONER GUNTER: I understand, but then I want to say now if you want to shoulder that burden, if you want to be able to shoulder that burden of tracing dollars through the life of the process, I might give you what you want; be careful what you ask for because folks tell me, and I imagine shivers are running up and down the backs of some of the folks sitting in the audience, if you go back and say you want complete tracibility of all the funds, I don't believe you can do that. Joe Howard probably just fell over.

MR. GUYTON: Well, I think if you go back to Mr. Howard's exhibits he tried to identify the incremental nature of the funds that would be used.

COMMISSIONER GUNTER: I understand, and once you get started -- after you've once started, then it becomes an impossible task. I think we beat that horse about trying to trace funds ever since I've been here. Thus far nobody has been able to do that. And that's an interesting thing is that's without addressing the incremental cost of equity as we zip down the road.

CHAIRMAN WILSON: Any further questions of this witness? Any redirect?

MR. GUYTON: I do have some redirect.

CHAIRMAN WILSON: All right.

REDIRECT EXAMINATION

BY MR. GUYTON:

Q Mr. Waters, is FP&L using the same cost estimate for the Martin 3 and 4 units as it used in the oil backout qualification proceeding?

Q Why did FPL use the original Bechtel, GE and CE estimates as construction cost base for direct costs?

A FPL had signed contracts with Bechtel, with General Electric, with Combustion Engineering for the Martin Units 3 and 4, so we had some fairly good idea of what those units would have cost. We signed the Bechtel contract in 1979, and I believe General Electric and Combustion Engineering within the 1980-81 time period. So those costs were firmed up to some extent.

Q Subsequently to entering the Martin contracts in the '79 through '81 time period what, if anything, happened to the market for power plant construction costs?

A Well, based on some of the issues we have discussed here today, like declining load forecasts, and so on, there are a number of factors that contributed to a general decline in the power plant market. That allowed us, for instance in trying to compare St. Johns, which is what we have attempted to do today, the contracts at St. Johns we received a very favorable bid experience due to the depressed market. There weren't that many coal plants built, and there are not that many coal plants being built today, which leaves us in more of a buyer's market when looking for AEs and component suppliers.

Q Is that because the JEA units were started later than the Martin units would have been?

A Yes, they were. The construction period was started somewhat later than Martin. The Martin units, we did begin expenditures in 1980. We would have, but for this project, continued through the '81-82 time period to incur some significant expenditures. St. Johns started somewhat later.

Q In response to a question by Mr. McGlothlin I think you had indicated that FPL had had an occasion to compare the cost elements, the direct cost elements, of Martin Units 3 and 4 used in FPL's computation of actual net savings be recovered through the factor with cost estimates for the JEA units?

A Yes, sir. A detailed comparison was done in 1987; in fact, there is a letter issued by Mr. Robert Stein in 1987, August of 1987, doing a detailed item-by-item construction cost comparison between the two units. The conclusion of that letter is that the direct costs to St. Johns are within 2% of the costs associated with Martin Units 3 and 4. It was also Mr. Stein's recommendation, I believe in that same letter, that for the purposes of oil backout we use the original cost estimates associated with the Bechtel package and adjust them for actual inflation and cost of capital.

Q Is that the same R. E. Stein that Mr. Pollock is quoted in his rebuttal testimony?

A Yes, it is.

MR. McWHIRTER: Mr. Chairman, I would like to object to this testimony as being hearsay unless the document upon which he is relying is placed into evidence.

MR. GUYTON: We will be happy to do so, Commissioner.

(Distributed)

WITNESS WATERS: It's Page 3 of that letter that I am referring to, entitled at the top of the page "Comparison of Martin Unit 3 and 4, Backout Estimates versus SGRPP Unit No. 1 and 2 Project Estimates."

MR. GUYTON: Chairman Wilson, may we have this document identified, please?

CHAIRMAN WILSON: Yes. Would that be number --

MR. PRUITT: 217.

CHAIRMAN WILSON: Exhibit 217.

MR. GUYTON: It's an August 10th, 1987 letter to Mr. Carlos A. Suastegui from Project Management Department, signed by Mr. Robert E. Stein.

(Exhibit No. 217 marked for identification.)

Q (By Mr. Guyton) Now, this comparison is a comparison of direct costs of the two units?

A Yes. This would be a comparison of direct costs only. I don't believe Mr. Stein has tried to compare any AFUDC charges, or any other component of the total installed costs.

Q How would the AFUDC element of cost compare for the JEA units and the FPL Martin 3 and 4 units used in this proceeding?

A I would imagine the AFUDC component of Martin would have to be slightly higher, since construction was started earlier and the construction period was somewhat longer, so they would incur both higher rates and, due to the longer construction period, more interest in that final installed cost for Martin 3 and 4.

Q Would there be as much equity in the JEA units as there is in the Martin assumptions?

A No. As I mentioned before, the JEA units were a joint project with Jacksonville Electric Authority. 80% of the unit was financed using JEA funds. They were able to issue, I guess, municipal bonds at a lower rate total debt financing on their part, which should have contributed significantly to lowering the overall installed cost.

Q Mr. Waters, you were asked earlier about an analysis of the deferral of units in the planning process. Do you recall those questions?

A Yes.

Q Has FPL performed any analysis of whether or not it should defer a coal-fired unit during the period 1983 through 1986, when FIPUG points out that load forecasts had dropped?

A Yes, sir. That precise analysis was requested by the Commission in, I believe it was, the 1983-1984 annual planning workshop proceedings. We were asked to look at the St. Johns unit which, of course, has the same projected in-service dates and has, in fact, come in service in '87 and '88. We were asked to look at deferring or cancelling Unit No. 2 in that proceeding.

MR. GUYTON: Mr. Chairman, we are going to hand out a document that I think Mr. Waters is referring to here, and ask that it be identified. (Supplied)

CHAIRMAN WILSON: The number?

WITNESS WATERS: There are two pages which I think are significant in this overall --

CHAIRMAN WILSON: Let's give this an exhibit number, and is that 218?

MR. PRUITT: Yes, sir.

CHAIRMAN WILSON: All right. "Florida Power and Light Company Total Project Investment in St. Johns River Power Park Units 1 and 2," is given the designation of Exhibit No. 218.

(Exhibit No. 218 marked for identification.)

Q (By Mr. Guyton) Mr. Waters, the document that is now identified as Exhibit 218, is this the deferral study that you were referring to previously?

A Yes, it is.

Q All right. Would you explain the results of the study?

A The basic purpose of the study was to look at delaying or cancelling, and/or cancelling Unit No. 2 at St. Johns River Power Park. Several cases were run to determine what would be the most economic choice at that time. The cases basically involved immediate cancellation of the unit, and by "immediate" I'm referring to January of 1984, which is the time roughly that the study was done. Looked at delaying the unit and deferring a decision on cancellation to 1986. And these cases are all summarized on the third page of the document.

There was also a third case run looking at delaying the unit and then resuming construction.

Now, the bottom line of all the results is shown on what is identified as Page 3 of 10 of the exhibit, and it's actually the fifth page in the handout, where net savings of the different scenarios are compared. One and two are considered a base construction schedule; in other words, complete the project at its then projected schedule, finish it on time.

The difference between the two cases, the encumbrances really has to do with commitments to the project for work not completed, so there was some expense that would have been incurred after delay or cancellation of the project anyway. And what we have attempted to do in 1 and 2 is show the difference in those expenses.

But in any event, with or without those expenses, Items 1 and 2 produced the most savings of any of the scenarios and, interpreted, that means that the delay or cancellation of those units would be an additional cost to FPL customers.

So the decision to defer would not have been a good one at this point. And this is the analysis that I mentioned before; this is the type of thing we would actually do, rather than simply looking at the load forecast and saying that the load has dropped, let's delay the unit, we have to look at what the costs associated with the deferral would be.

In this case you are incurring extra interest expense for money spent by delaying the unit, and there is a significant cost, or can be a significant cost associated with that.

Q Mr. Waters, you were also asked if you, as a planner, would consider the availability of other utilities' resources in your planning efforts. Do you recall that question?

A Yes, sir. We do look at that in the planning process to see if capacity is available for purchase.

Q Do you know what, if any, capacity was available from Tampa Electric Company for FPL in 1987?

A Actual experience, looking at actual loads and so on, I believe Tampa had a summer peak reserve margin below 15% for the years '87 and '88, which translated to practical terms means that they would not have had anything to sell to FPL during that period. It's also my understanding that Tampa has actually asked

FPL to provide emergency assistance to them several times during the past two years.

Q And was that 15% reserve margin before or after the conclusion of the capacity sales by TECO to FPL?

A The reserve margin shown in '88, of course, there were no capacity sales to FPL so that's just simply their reserve margin without sales. In 1987 they would have included that in maintenance, any maintenance to units on the system, in that reserve margin.

Q Now, you were also asked about planning criteria, mentioned planning criteria that were used for the additional generating units. How long has FPL used the loss of load probability, and the dual criteria of loss of load probability and reserve margin?

A The dual criteria -- in a general sense the dual criteria has been used for some time, but the targets and the standards have changed. Since 1985, approximately the middle of 1985, FPL has used the dual standards of 15% reserve margin and one day in ten years of loss of load probability. Prior to that time the criterion used by FPL was basically 20 to 25% reserve margin based on summer peak load.

Q You also spoke in an earlier answer of the tie capability to Southern presenting a capacity deferral benefit in and of itself by allowing you to lower your planning reserve margin?

A It's one of the factors that does allow us to lower reserve margin criteria. There are several others, but it does have the effect of providing a sort of backup role to our own capacity, and in that respect it improves system reliability. The bottom line of that, though, is that if what it is providing is basically the same as a type of capacity referral or capacity avoidance, which we have not included in any of the analyses done to date on the net benefits of the project, we have not even attempted to take into account the fact that we can operate at lower reserves.

Q Would it be reasonable, if that were quantifiable, to include that capacity deferral benefit associated with this project?

A Certainly, the way the cumulative present value test is done it's basically trying to include all costs and all benefits. And if we could quantify that, or if we did quantify that, I think it would be property included in the test as a benefit.

Q Mr. Waters, you were also asked about capacity charges and whether they were typically thought of as O&M expenses. Do you recall those questions?

A Yes, sir.

Q Do you know where purchased power costs are recorded, in what accounts?

A No, I don't, I'm not familiar with that. I know that purchased power can sometimes be recovered in the fuel clause, but I'm not sure what account it's normally credited to.

Q Have you had occasion to look at the FERC Uniform System of Accounts before?

A I have looked at the FERC forms but not in enough detail that I know the FERC System of Accounts.

MR. GUYTON: Commissioners, that's all I have on redirect.

CHAIRMAN WILSON: Any questions, Commissioners?

COMMISSIONER GUNTER: No.

MR. GUYTON: Commissioners, we would move Exhibits 208, 209, 211, 212, 215, 216, 217 and 218.

CHAIRMAN WILSON: All right. Without objection, those exhibits are admitted into evidence.

(Exhibit Nos. 208, 209, 211, 212, 215, 216, 217 and 218 admitted into evidence.)

MR. McWHIRTER: With respect to the exhibit dated August 10th, 1987, I believe that is Exhibit 215 and exhibit --

CHAIRMAN WILSON: That's 217, I think.

MR. McWHIRTER: 217?

CHAIRMAN WILSON: Yes, 217. That's the one to Mr. Carlos A. Suastegui.

MR. McWHIRTER: It's the one that says "Page 7" at the top?

CHAIRMAN WILSON: Yes.

MR. McWHIRTER: All right, and I don't have a number on

"Florida Power and Light Total Project investment, St. Johns River Power Park."

CHAIRMAN WILSON: That's 218.

MR. McWHIRTER: We would object to those two exhibits on the following grounds: FIPUG submitted a discovery request to Florida Power and Light requesting the Company to provide us with all information concerning their generation planning with respect to these particular sites, Martin and -- well, their generation planning in its entirety. We were furnished a document dated October 10th, 1984, on which Mr. Pollock based his testimony. We were not furnished with the two documents that have been proffered into evidence today. We think they are ligitmate discovery requests, and we think that Florida Power and Light failed to adhere to the discovery requirements, and we think that fatally flaws these two exhibits.

CHAIRMAN WILSON: Do you have a copy of the discovery request here? (Supplied)

MR. McWHIRTER: It's Discovery Request No. 14 dated the 22nd of February, 1989. We requested all documents pertaining to the 1987 decision to claim deferral benefits based on the assumption that the project deferred Martin coal unit rather than the alternative -- and an alternative in generation expansion option. 16: "All documents pertaining to the capacity deferral benefits and net savings associated with the project under assumption that a generation option other than the Martin 700 coal-fired units were units deferred by the construction of the project."

MR. GUYTON: Mr. Chairman, if I may respond.

CHAIRMAN WILSON: Those are the two requests that you are referring to?

MR. McWHIRTER: I think there's something else, Mr. Chairman, but we haven't identified it yet. (Pause)

Item 34 of the document request dated June 19th, we requested FP&L to provide the most recent transmission planning studies. (Pause) We think those are the two items. In addition, Mr. Pollock went to Miami and requested all information concerning the generation and planning and was not furnished with the two documents that are offered into evidence today.

MR. GUYTON: First off, I've noticed that the JEA deferral analysis, which this Commission has in its own files and could notice anyway, does not fall within the scope of either one of those discovery requests. It's a question that came up here today about an analysis of what you would do as a result of a reduction in load forecast between '83 and '86, and whether he, Mr. Waters, as a planner, would consider deferral of analysis in the planning process. We did anticipate the question might be asked but it wasn't asked on discovery and doesn't fall within either of the questions.

Now, quite frankly, I don't know how to respond to the other one other than to say that I have the two boxes of documents that were provided to Mr. Pollock -- let me back up. Mr. Pollock was provided some 20 to 30 transfer boxes of documents when he went to Miami on the 6th and 7th of June. They were in response to some 34 requests to produce, including a request to produce having to do with this interrogatory that you have been referred to. In that box of documents is the August 10th, 1987 letter from Mr. Stein to Mr. Carlos Suastegui. Quite frankly, the document has been produced. (Pause)

COMMISSIONER GUNTER: What say you? They're saying that it was given to Mr. Pollock.

CHAIRMAN WILSON: It was in a box of documents that were provided to Mr. Pollock in Miami?

MR. McWHIRTER: He denies that. I can put him on the stand to do it. I don't think it --

MR. GUYTON: I will be glad to put somebody on the stand to say that it was produced to him.

COMMISSIONER GUNTER: Do you all have a deal in this process -- and I'm trying to understand the procedure now -- where you sign for an inventory of what you got?

CHAIRMAN WILSON: Was there an index of the documents that were in the boxes that were given to the witness?

COMMISSIONER GUNTER: That's what I am talking about.

MR. GUYTON: There is an index that we compiled after the production that indicates the documents that were produced. I have kept my copy of the documents that Mr. Pollock identified and asked that we copy and send to him. I kept them intact, and that is where I just pulled this file folder out of. Not only did he review it in Miami on the 6th and 7th, he asked that we copy it and send it to St. Louis. We did so and sent it expeditiously to St. Louis to Mr. Pollock's office in a box.

CHAIRMAN WILSON: You are referring to the Exhibit 217?

MR. GUYTON: Yes, sir. (Pause)

CHAIRMAN WILSON: Let's just stand in informal recess for a moment while they discuss this.

(Brief recess.)

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CHAIRMAN WILSON: All right, what has happened here?

MR. GUYTON: Well, I am in the process of trying to satisfy Mr. Pollock that we provided this both in Miami and then we sent it to him. He is unconvinced and I am equally convinced. I'm not quite sure how to proceed.

CHAIRMAN WILSON: Well, then give it to me and I'll make the decision.

COMMISSIONER GUNTER: Go out into the parking lot.

COMMISSIONER EASLEY: Mr. Chairman, while you are waiting for that, I am really surprised to find out that there isn't an index that the receiver, either party receiving has to sign in response to the production of these documents. And I would hope in the future that when we have got this number of documents being produced that there be some kind of a sign-off list so that we don't run into this swearing match.

MR. McWHIRTER: I think that's a good idea.

CHAIRMAN WILSON: Now, tell me what this is that you have handed me. These are the documents that --

MR. GUYTON: That's part of the two boxes of documents that were sent to Mr. Pollock as a result of his review of the documents in response, FPL's Response to FIPUG's First Request for Production. Let me show you the boxes that I pulled them out of.

CHAIRMAN WILSON: These are copies of the documents that Mr. Pollock asked you to give him from those boxes of documents that he reviewed in Miami? Do I understand that correctly?

MR. GUYTON: That is correct.

CHAIRMAN WILSON: And when you made copies of those documents you kept a set of those same copies of documents in this folder?

COMMISSIONER EASLEY: In those boxes.

MR. GUYTON: And in those boxes.

CHAIRMAN WILSON: And in those boxes.

MR. GUYTON: One copy was kept at Florida Power and Light Company and the other copy was sent to their attorney, and that box has remained intact.

CHAIRMAN WILSON: You just removed this from the box?

MR. GUYTON: Yes, sir, I just removed it from the box.

COMMISSIONER EASLEY: The problem, Mr. Chairman, that you have got is that it doesn't make any difference, you've got a swearing match. (Pause) Mr. Chairman, there have been --

CHAIRMAN WILSON: First of all, I see no problem with Document No. 218 because this is a document that is on file with the Commission and this was filed in a proceeding 830377, and should have been easily discoverable by any of the parties and not necessarily had to be provided by Florida Power and Light. So I don't see any problem with that document, and that Document No. 218 will be admitted into evidence.

(Exhibit No. 218 admitted into evidence.)

COMMISSIONER EASLEY: On the other document, Mr. Chairman, there were questions and answers on the other document. I don't know whether legally that precludes an objection at this point but that document has been discussed on the record now.

MR. GUYTON: That's a good point, and I think probably the objection has been waived.

MR. McWHIRTER: Mr. Chairman, I think part of our problem is that Mr. Pollock relied on certain information that was given to him by FP&L in preparing his testimony.

CHAIRMAN WILSON: Uh-huh.

MR. McWHIRTER: In the redirect examination Mr. Pollock's testimony has been impuned using another document, which Mr. Pollock says he has never seen for some reason or other. I think what we might do to clarify the record is make that statement, that his testimony was not based upon these two documents which he has not seen, and place into evidence the document which he has seen and which his testimony was based upon, so there can be that clarification. I think that would --

COMMISSIONER BEARD: Can I ask a question? You said you kept an index?

MR. GUYTON: We have an inde. of the documents that were provided, yes.

COMMISSIONER BEARD: Did by chance you mail a copy of that index to him as well?

MR. GUYTON: No, we did not.

COMMISSIONER BEARD: So much for that idea.

MR. McWHIRTER: I presume the documents aren't that inconsistent, or if they are inconsistent that the inconsistencies would --

COMMISSIONER GUNTER: They would stand on their own bottom.

CHAIRMAN WILSON: So what you are saying is that go ahead and admit 217 and then provide, in addition, the document that Mr. Pollock did rely upon to prepare his testimony?

MR. McWHIRTER: Yes, sir.

CHAIRMAN WILSON: We do not have that at this time?

MR. McWHIRTER: That is correct.

CHAIRMAN WILSON: All right, and you are going to provide that to us?

MR. McWHIRTER: Yes, sir.

CHAIRMAN WILSON: And what would be the number for that exhibit?

MR. PRUITT: 219.

CHAIRMAN WILSON: All right. Does the Company have any objections to that? I would assume not.

MR. GUYTON: Probably not, but I would like to see the document to make sure that we know what's in it.

CHAIRMAN WILSON: I assume it's one of your documents.

MR. GUYTON: I assume so, too, but I know better than to -- (Pause) We have no object to this. This was quoted extensively in Mr. Pollock's rebuttal testimony.

CHAIRMAN WILSON: All right. That will be given the number 219, and if you will provide copies of that to the parties, Mr. McWhirter.

MR. PRUITT: We need a title.

CHAIRMAN WILSON: Identify the document for me, please.

MR. McWHIRTER: The document is on FPL letterhead. It's a document to Mr. E. Hoffman, and at the top of it it says, "Location, Juno Beach. Date of October 11th, 1984. Subject, Revision of Oil Backout Estimates, Martin 3 and 4, and Unsited 1 and 2."

CHAIRMAN WILSON: All right, thank you.

MR. McWHIRTER: We will copy that and supply it to you.

CHAIRMAN WILSON: All right.

(Exhibit 219 marked for identification.)

CHAIRMAN WILSON: All right, without objection, that document 218 is admitted into evidence -- 219 -- and Document 217 is also admitted into evidence. And 218 was admitted into evidence.

(Exhibits 217 and 219 admitted into evidence.)

MR. McWHIRTER: Mr. Chairman, FIPUG would also like to offer into evidence the exhibits that we proffered during Mr. Waters' testimony.

CHAIRMAN WILSON: I need to have the numbers of those, Mr. McWhirter.

MR. McWHIRTER: It would be the omitted numbers, I think it's 211 -- it's 213 and 214.

CHAIRMAN WILSON: All right. Exhibits 213 and 214, and the Commissioner had requested 215, which we can admit our own exhibit, I guess.

(Exhibit Nos. 213 and 215 admitted into evidence.)

MR. GUYTON: Commissioner, we have an objection to Exhibit 214.

CHAIRMAN WILSON: All right, let me find it, let me find 214. (Pause) All right, I've got it.

MR. GUYTON: This was a document that Mr. Waters said that he had not seen before and was not familiar with. The document has not been thoroughly authenticated and, more importantly, its purpose and why and what it was used for has not been established. There is an insufficient predicate for the exhibit.

CHAIRMAN WILSON: All right. Mr. McWhirter?

MR. McWHIRTER: Mr. Chairman, it appears on the face of the document, and from the responses to questions by the witness, Mr. Waters, that this is part of the official records of Florida Power and Light Company and is a document that was extracted from those records, and therefore under the business records rule it would be admissible into evidence.

CHAIRMAN WILSON: As I recall, though, Mr. Waters said that he had never seen the document before.

MR. McWHIRTER: He recalled that --

CHAIRMAN WILSON: And really at that point cross examination on the document ceased, if my recollection is correct.

COMMISSIONER GUNTER: With the exception, Mr. Chairman, I think there were two questions that were asked -- and I don't have that before me -- but the two questions that were asked, one of them was TECO and the other one was the one on the bottom. TECO was 107 megawatts, I believe, that I read that was through 1987. And I think that the question that was asked had to do with the last footnote, and I apologize, one of them was C and one of them was D, I think, as to the recovery of the capital of the capacity component.

CHAIRMAN WILSON: Yes.

COMMISSIONER GUNTER: And I think the question was asked, after review of the methodology was the capacity cost recovered through base rates, period, end of conservation. That was my understanding or recollection.

COMMISSIONER EASLEY: One addition to that, Mr. Chairman. The witness pointed out that these were assumptioins, as based on the title of Page 10, and that based on that he read the document on its face.

COMMISSIONER GUNTER: That's right, within the four corners of the page.

MR. McWHIRTER: That would go to the weight of the evidence, if it please the Commission, and the issue is are these records of the Company. And he acknowledged that Mr. Smith was his supervisor and that they were records of the Company, and on that basis I think they would be admissible.

COMMISSIONER EASLEY: Mr. Chairman, the argument that I raised on that last one would apply to this one as well. The document has now been discussed on the record.

COMMISSIONER GUNTER: That's right.

CHAIRMAN WILSON: Well, that sort of thing, you may waive objections and you may not. There are always motions to strike that are available to correct that sort of thing, so that's not necessarily going to be determinative.

MR. GUYTON: I would point out the fact that Mr. Smith might be Mr. Waters' predecessor has no relevance to this document. I don't think Mr. Smith's name appears on it. But aside and apart from that, Mr. Waters has said he is unfamiliar with it, and we don't even have the predicate established that this is a business record of Florida Power and Light Company. The custodian of the record hasn't been called to show that it is kept in the regular order of business but, more importantly, we don't know the purpose for which this was used.

COMMISSIONER WILSON: Well, I think Commissioner Gunter just went over -- as I understand what it was offered for, it was to demonstrate how capacity charges were recovered by the Company and in what fashion.

MR. McWHIRTER: That's the principal purpose.

COMMISSIONER GUNTER: And one of the things that happened, Mr. Guyton, either way, one of the things that happens and that I can't divorce in my mind is immediately when we got this some folks ran and checked and came back and said, "Well, that's not all the pages." So by your own actions that would say, "You know, that's something you gave me."

MR. GUYTON: I don't deny that it was something that we had given them, Commissioner Gunter. You know, it's all for the limited purpose that has been set out here, and we --

CHAIRMAN WILSON: I am going to admit that into evidence as well, Exhibit 214.

(Exhibit No. 214 admitted into evidence.)

CHAIRMAN WILSON: Is there anything else?

MR. McWHIRTER: No, sir.

MR. GUYTON: We would ask that any exhibits that we may not have identified be moved at this time.

CHAIRMAN WILSON: We don't allow catch-all moving of exhibits anymore, Mr. Guyton.

MR. GUYTON: Well, I tried.

CHAIRMAN WILSON: We have been severely chastised by the court reporter and we no longer do that.

THE REPORTER: How about Exhibit 210?

CHAIRMAN WILSON: All right, 210. (Pause) Can you refresh my memory? What is Exhibit 210, Carol? Can you tell me what that is?

THE REPORTER: I don't have the title but it was submitted through Mr. Babka by Mr. McWhirter.

CHAIRMAN WILSON: Mr. McWhirter, I believe that's -- Mr. McWhirter, I believe that's your exhibit, 210. It's a schedule of oil backout revenue requirements projected for October '89 to March 1990.

MR. McWHIRTER: Yes, sir. I thought I proffered that at the time.

CHAIRMAN WILSON: All right, so you move the admission of that exhibit?

MR. McWHIRTER: Yes, sir.

CHAIRMAN WILSON: All right, Exhibit 210 is moved into evidence without objection.

(Exhibit No. 210 admitted into evidence.)

CHAIRMAN WILSON: All right. The transcript is due on September the 14th, briefs are due October 5th, and agenda on November 7th. Everybody has that schedule.

All right, is there anything further in this phase of the docket?

MR. GUYTON: I think Mr. Waters was identified as an oil backout witness but I understand -- I think everything he was going to be asked to testify to has now been addressed in this proceeding and we would ask if he can be excused from 001.

CHAIRMAN WILSON: All right. Without objection of the parties he may be excused.

WITNESS WATERS: Commissioner, if I might ask, I know that Commissioner Herndon had some questions about the site plan, and if he has those questions I am probably the one to ask before I leave.

COMMISSIONER HERNDON: It has been taken care of, thank you.

CHAIRMAN WILSON: Thank you.

(Witness Waters excused.)

CHAIRMAN WILSON: All right. If there is nothing further then this hearing will be adjourned, 89 -- yes?

MS. WALSH: We have a question from Staff regarding the stipulation Commissioner Gunter mentioned yesterday.

COMMISSIONER GUNTER: Oh, that's right. Where are we, since you are the witness sitting there -- you know, this is called "Let's Make a Deal," and that's sort of characterizing the TV thing where folks get down there and negotiate. We've got all the parties sitting here in the room, and the parties would either be party to the stipulation, which the Commission could accept or reject, would be on an item in the Prehearing Order as to the appropriateness of the rate of return on equity. We went through a process where I guess we just thought we had all the items covered, but apparently we missed one. Now, for the purposes of the oil backout, do you know, or are you authorized to speak for the Company?

WITNESS WATERS: I think Mr. Childs has the answer to the --

COMMISSIONER GUNTER: As to whether we could reach a stipulation on that item that was in the Prehearing Order.

CHAIRMAN WILSON: I guess the real question is why wouldn't you use, when you are doing a current recovery of costs such as you are on this, why wouldn't you use a more current cost of capital such as has been used in the tax rule?

MR. CHILDS: Commissioner, I can't debate the merits of that. Where we are, and we took the message to heart, is to attempt to get a resolution and a response as to what I could represent to you. I hope to have that but I don't have it yet.

Now, if you would like, we would try to be able to have a response very shortly after lunch, but I'm just not sure where we stand on that. We need to check with some people.

CHAIRMAN WILSON: Well, if you don't have an answer right now, we don't have an answer right now.

MR. McWHIRTER: I would suggest that we can do it with a written stipulation which we can circulate after this hearing and submit to you in due course.

COMMISSIONER GUNTER: Well why don't you just continue the hearing, if there is an assurance that we're going to have it after lunch? I don't think those of us who are not on the fuel panel, you will be here and all of the parties are still going to be here. You know, you weren't going to stay, probably, but you are billing by the hour so you would like to stay. (Laughter)

COMMISSIONER HERNDON: Mr. McGlothlin will be here.

COMMISSIONER GUNTER: Mr. McGlothlin will certainly be here through that process, to see if a stipulation could be reached, and we can put it to bed, one way or the other, today. I, for one, would like to see it put to bed today and I'll hang around, I'll be here.

MR. McWHIRTER: As I see it, there are three aspects to it that need to be considered, and one is they have been using the higher return on equity for the whole history of this project. The stipulation to go to 13.6 was in January of '87, so your first issue is do you apply it only for this particular section, or do you apply it back to 1987 and make the correction there. There would have to be significant calculations.

COMMISSIONER GUNTER: You see, part of the problem that we have is without a stipulation the alternative that is open to the Commission then is to initiate a proceeding on a prospective basis. And you start beginning to wonder then -- and I'm sure that the folks are calculating -- is to, you know, if you establish a new rate of return, would the new rate of return, if you had to have that kind of proceeding in order to do that, would that be for all purposes. You know, that's sort of like computing regret. Remember when you were a little boy, and I don't know if it every happened to you or not, but if you walked down one street going home you knew you were going to have to pass the bully. And it's just whether you wanted to walk four or five extra blocks not to pass the bully. Because on the best day I ever had I couldn't whip the bully. (Laughter) So that's sort of the situation they find themselves in, whether they want to go ahead or face the bully.

CHAIRMAN WILSON: I couldn't ever whip the bully, either.

COMMISSIONER GUNTER: Sometimes it's easier to walk around the block. So, see, the alternatives that are open to us, that's the reason I would like to put it to bed as to where we are, whether it's back to the 13.6 when it was started, whether it's prospective from this point, and see where we are. Because the Commission's hands are somewhat tied in the decisions that we can make, you know, as to retroactivity. You are aware of those kind of things better than I am.

COMMISSIONER BEARD: I think the bottom line is that you all bring forward a stipulation and we'll look at it; or you don't bring forward a stipulation and we do whatever it is we do best.

MR. McWHIRTER: That's obviously something you want to do at this particular proceeding because it pertains to the oil backout and --

CHAIRMAN WILSON: Well, if it comes back to us this afternoon, and if it doesn't we can't. But what I suggest that we do is that we adjourn this proceeding subject to reconvention at the call of the Chairman this afternoon.

COMMISSIONER BEARD: We can not rule on the stipulation this afternoon, too.

MR. McWHIRTER: That's for sure.

COMMISSIOENR GUNTER: I think that's fair.

CHAIRMAN WILSON: All right, with that, this hearing is adjourned and we will reconvene at 1:15 to take up 890001.

(Thereupon, lunch recess was taken at 12:15 p.m., and Docket No. 890148-EI was concluded.)

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FLORIDA)
:
COUNTY OF LEON)

CERTIFICATE OF REPORTERS

We, CAROL C. CAUSSEAUX, CSR, RPR, and JOY KELLY, CSR, RPR, Official Commission Reporters

DO HEREBY CERTIFY that the hearing in the captioned matter, Docket No. 890148-EI, was heard by the Florida Public Service Commission at the time and place herein stated; it is further

CERTIFIED that we reported in shorthand the proceedings held at such time and place; that the same has been transcribed under our direct supervision, and that this transcript, consisting of 493 pages, Volumes I through III, inclusive, constitutes a true and accurate transcription of our notes of said proceedings; it is further

CERTIFIED that we are neither of counsel nor related to the parties in said cause and have no interest, financial or otherwise, in the outcome of this docket.

IN WITNESS WHEREOF, we have hereunto set our hands at Tallahassee, Leon County, Florida, this 12 day of September, A.D., 1989.

Carol C. Causseaux
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