BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 070052-EI

In the Matter of:

PETITION BY PROGRESS ENERGY FLORIDA, INC. TO RECOVER COSTS OF CRYSTAL RIVER UNIT 3 UPRATE THROUGH FUEL CLAUSE.
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VOLUME 2

Pages 177 through 381

PROCEEDINGS:	HEARING
BEFORE:	CHAIRMAN LISA POLAK EDGAR COMMISSIONER MATTHEW M. CARTER, II COMMISSIONER KATRINA J. McMURRIAN COMMISSIONER NANCY ARGENZIANO COMMISSIONER NATHAN A. SKOP
DATE:	Tuesday, August 7, 2007
TIME:	Commenced at 9:30 a.m. Recessed at 6:20 p.m.
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	MARY ALLEN NEEL, RPR, FPR
APPEARANCES:	(As heretofore noted.)

I N D E X

WITNESSES

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P R O C E E D I N G S

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CHAIRMAN EDGAR: Commissioner Skop, did you have questions?

COMMISSIONER SKOP: Yes, Madam Chair. Just briefly, as a point of information, I guess the question arose with respect to the Ten-Year Site Plans and the -- not putting the expected retirement dates in, and you mentioned that there were no assets to be retired. Were there anything -- I think it may be the Turner Plant or in Enterprise. Didn't they recently retire some generation there or some old oil-fired generation that was on Lake Monroe in the Enterprise area, Enterprise, Florida?

THE WITNESS: I'm not familiar with it. I would point out that this year in the 2007 plan, we would show the Bartow units, the existing Bartow units being retired as we repower the new units. The specific reference we were working from was the 2005 plan, and at that point we had no plan to retire units.

It is something we look at from time to time, and if it were economic to shut down and replace capacity, we would show that in the Ten-Year Site Plan. It's not that we never show it. It's just that we don't have any studies to confirm that that's the best choice going forward.

COMMISSIONER SKOP: Thank you.

CHAIRMAN EDGAR: Mr. Walls, did you have questions on cross?

MR. BREW: Yes, just real quick.

CROSS-EXAMINATION

BY MR. BREW:

Q. I guess it's good afternoon, Mr. Walls.

A. Good afternoon.

Q. Referring to the document that you've just been discuss -- it confused me too.

CHAIRMAN EDGAR: I apologize.

BY MR. BREW:

Q. If you could refer to the portion that Mr. McWhirter was discussing with you on the 2007 Ten-Year Site Plan, and you discussed what was Schedule 8.

A. Schedule 8.

Q. It would be the last page.

A. Okay.

Q. And that shows planned capacity additions and changes?

A. Yes.

Q. And it shows the Crystal River 3 uprate in terms of a 40-megawatt addition in '09 and a 140-megawatt addition in 2011; is that right?

A. That's correct.

Q. Does the Ten-Year Site Plan show the transmission addition that has been discussed in the company's testimony anywhere?

A. It does not, because as Mr. Roderick said, the study on that is not final. When we have a final project identified, it will go into the Ten-Year Site Plan.

Q. So currently there is no specific proposal and there is no budget for a transmission expansion?

A. That's correct.

MR. BREW: All right. Thank you. That's all I have.

CHAIRMAN EDGAR: Mr. Twomey.

MR. TWOMEY: Thank you, Madam Chair. Just a couple.

CROSS-EXAMINATION

BY MR. TWOMEY:

Q. Good afternoon, sir.

A. Good afternoon.

Q. Mr. Waters, in the summary of your testimony, you listed a number of benefits, correct, to be obtained by this project?

A. Yes.

Q. The 2.6 billion was -- tell me again, was that the lifetime projected fuel savings?

A. It's over the remaining life of the Crystal River 3 assuming a license extension, yes.

Q. Okay. How many years is that?

A. That takes us out to 2036.

Q. 2036. You said that, I guess, the net -- or did you say that the 321 million was the net present value benefit?

A. Again, to be clear, that 2.6 billion corresponds to 640 million net present value of fuel savings. The 320 million that I think everyone is referring to is the net savings when you subtract the costs of the project from the fuel savings.

Q. Okay. And you also pointed to increased fuel diversity; correct?

A. Yes.

Q. And additional reliability from base load generation?

A. Yes.

Q. You, if I remember correctly, referred to those as clear benefits; is that correct?

A. Yes.

Q. Okay. Now, Mr. Waters, isn't it true that these clear benefits that you've listed are achievable, that they will be obtained for the company to the benefit of the customers if the uprate is accomplished, irrespective of the method of cost recovery granted by this Commission?

A. Yes, that's true. The benefits would accrue if it were done.

Q. If it's done, irrespective of cost recovery, I mean, the amount and method of cost recovery?

A. The method of cost recovery, yes, I think that's correct.

Q. Now, apparently, according to Mr. Roderick, Progress management will consider abandoning all these -- the attainment of all these clear benefits, the 2.6 billion of fuel savings, et cetera, if it doesn't get its way with the fuel cost recovery sought in this petition. Is that true?

MS. TRIPLETT: Madam Chair?

CHAIRMAN EDGAR: Yes, ma'am.

MS. TRIPLETT: Object to lack of -- mischaracterization of Mr. Roderick's testimony.

CHAIRMAN EDGAR: Mr. Twomey, could you rephrase?

MR. TWOMEY: Well, Madam Chair, I will, but I'm not aware of how I mischaracterized his testimony, and it might help me if she would explain it.

MS. TRIPLETT: Certainly, Madam Chair. Mr. Roderick testified that he did not know what the management would do if the cost recovery request is denied.

MR. TWOMEY: Okay. Fair enough.

BY MR. TWOMEY:

Q. Were you in the room when I asked that question of Mr. Roderick?

A. Yes.

Q. Did you hear him say that if this petition was denied, he thought the company would re-examine its priorities?

A. I would not want to guess at what he said exactly. I would probably want to look at the transcript. But I remember the discussion, yes.

Q. Let me ask you, of your own knowledge, are you aware whether or not the company will put this project on hold if this petition is denied and re-examine its priorities?

A. I am not. And I guess I would go maybe one step further than Mr. Roderick. We don't enter these proceedings as far as -- I think I can speak for all the witnesses. We don't enter the proceedings assuming failure, so we have not laid out a course of action following this. It would be pure speculation on the part of any of us as to what we would do beyond this. And that's not to say that we would abandon the project or make any other judgments on what we would do. But we are here presenting what we believe is the right thing to do, and we're assuming that we'll go forward on that basis. We've made no other assumptions beyond that.

Q. So I hear you saying that you've assumed so thoroughly that you'll win and have this petition granted that you've made no contingent plans beyond that?

A. No, that's not what I said. I said I assume that we are presenting the right thing. We believe that we have a good case. We believe it's the right case. The Commission will ultimately decide, and after the decision is made, if we have to make contingencies, we will, but we're not going to assume contingencies at this point.

Q. I see. Now, let me ask you, if you know, isn't it true that if this plant is -- if the petition were denied and the company accomplished the uprate in any event, that roughly the same amount of money would be recovered from the customers through base rate recovery, if you know?

A. I don't know.

Q. Do you understand how base rate recovery normally works?

A. Basically, yes, but that's outside my area. And as I said before, in the analyses, we don't make an assumption on how -- the mechanism of recovery.

Q. Okay. Fine. But to the extent you understand basic rate regulation, isn't it true that through base rate regulation that the company would recover or return a reasonable return on its investment in this uprate?

A. I believe that's true, all other factors being equal.

Q. Right. And all other factors being equal, isn't it also true that the company would receive a -- once the plant was in service, it would receive the recovery of its necessary, reasonable, and prudent costs of operation?

A. That's a possible outcome of the rate case. You're getting into really what is the outcome of a rate proceeding if we went that path, and that's speculation. I wouldn't want to guess as to what the outcome would be.

MR. TWOMEY: That's all. Thank you.

CHAIRMAN EDGAR: Commissioners, any other questions?

MR. BREW: Excuse me, Madam Chairman.

CHAIRMAN EDGAR: Mr. Brew.

MR. BREW: Could I be permitted one additional question? It's not a follow-on to anything else.

CHAIRMAN EDGAR: Mr. Brew.

MR. BREW: Thank you very much.

FURTHER CROSS-EXAMINATION

BY MR. BREW:

Q. Mr. Roderick, could I refer you to your Exhibit SSW-1?

A. Yes.

Q. And I would like to point to the years 2017 and 2018.

A. Okay.

Q. And the row for nuclear production costs. Do you see that?

A. Yes.

Q. Between 2017 and 2018, your estimated nuclear production costs doubled in those years; is that right?

A. Yes.

Q. And is that due to a new nuclear unit coming online?

A. Yes, it is.

MR. BREW: Okay. That's all.

CHAIRMAN EDGAR: Thank you. Commissioners, any questions? None at this time. Questions from staff?

MR. YOUNG: Yes. Thank you, Madam Chairman.

CROSS-EXAMINATION

BY MR. YOUNG:

Q. Good morning, Mr. -- I mean good afternoon, Mr. Waters.

A. Good afternoon.

Q. Mr. Waters, can you please turn to page 9 of your amended direct prefiled testimony?

A. Okay.

Q. Starting on line 9 going through line 11, you stated that the increasing amount of nuclear energy available to Progress Energy Florida customers will lower the need of new capacity in the future; is this correct?

A. That's correct.

Q. And in that passage, you refer to additional nuclear energy from the CR3 uprate as a result of the project?

A. That's correct.

Q. Okay. Now, further down the line, further down on the same page, on page 9, lines 13 through 15, you stated that the additional energy from CR3 will displace energy from other higher cost generation sources; is this correct?

A. Yes.

Q. And the existing units that get displaced on the system when you look at the end result are primarily gas and oil-fired units?

A. Yes, that would be the -- the primary displaced energy on the system would be primarily coming from oil and gas units.

Q. Mr. Waters, what's being handed to you now is Staff Exhibit Number 22, which is a Progress Energy response to a staff interrogatory in Docket No. 060642-EI, the Crystal River 3 uprate need determination.

A. Yes.

(Exhibit 22 was marked for identification.)

BY MR. YOUNG:

Q. Do you recognize this document, Mr. Waters?

A. Yes, I do.

Q. How do you recognize this document?

A. This was produced by my staff in response to this request.

Q. Did you have any involvement in this document?

A. As I said, it was produced by my staff and under my direction in response to the question.

Q. Mr. Waters, can you identify in Staff Exhibit Number 22, looking at page 4, including the cover page?

A. Okay.

Q. Which units under this document will the CR3 uprate displace?

A. Well, actually, you have to go through --

Q. Well, let's walk through it.

A. Okay. Which year would you like to look?

Q. Starting in 2009, under steam-oil, will it displace the Bartow Units 1, 2, and 3?

A. No, we're not seeing any displacement from Bartow 1, 2, and 3.

Q. Suwannee 1, 2, and 3?

A. No, nothing there.

Q. Okay. Let's look at 2010. Will it displace any of those units?

A. Very little. There's just a little bit from Suwannee.

Q. Okay.

A. But there's 30 gigawatt-hours from Anclote, and there's 24 from Bartow repowering, which is a gas unit. The Hines units, which are gas units, show a substantial reduction. So as I said, I think most of the displacement is coming from oil and gas units.

Q. Attachment 2, same exhibit, looking at the purchased power of that exhibit --

A. Yes.

Q. This schedule shows the dollars associated with the purchased power contracts that will be displaced by the uprate; is this correct?

A. Let's see. You're looking at --

Q. Which is page 13 of 14.

A. Oh, I'm sorry. Okay. Yes, that is the dollars. I'm looking at Attachment 2, page 8 of 14. Is that the correct page?

Q. Okay. Yes.

A. Okay.

Q. Okay. And your answer? I don't think I heard your answer.

A. I'm sorry. I forgot what the question was.

CHAIRMAN EDGAR: Okay. Let's hold on a second. We've got a lot of numbers in these attachments. To staff, about how long a line of questioning do you have for this witness, approximately, approximately?

MR. YOUNG: I would say 30 minutes, Madam Chairman.

CHAIRMAN EDGAR: Okay. Let's go ahead and take a lunch break then. I'm seeing approximately 1:20, so let's come back at 2:15. 2:15. We're on lunch break, and we will continue then with staff questions to this witness.

(Lunch recess from 1:18 to 2:29 p.m.)

CHAIRMAN EDGAR: Okay. We will go back on the record. And when we took a lunch break, we were having questions from staff, so we will pick it up where we left off.

MR. YOUNG: Thank you, Madam Chairman.

BY MR. YOUNG:

Q. Mr. Waters, is it my understanding that you said that you didn't understand the question, the previous question; correct?

A. I didn't remember the previous question I think was the problem.

Q. All right. Looking at your response to Staff's Interrogatory No. 5, Attachment 2.

A. Yes.

Q. This shows the schedules of dollars associated with the purchased power contracts that will be displaced by the uprate of CR3; correct?

A. Yes, on page 8 of 14 of that attachment, yes.

Q. Page 8 of 14. Okay. Now, Mr. Waters, it is your testimony that you were intricately involved in the Ten-Year Site Plan for 2007; correct?

A. It was done under my supervision and control, yes. It was done by my staff.

Q. What about 2006? Are you familiar with those site plans?

A. Yes.

Q. Mr. Waters, could I ask to you turn to -- you received a handout of the 2006 and 2007 Ten-Year Site Plans.

A. Yes, I have those.

MR. YOUNG: Madam Chairman, I ask that for identification purposes -- two site plans were laid before you, which is 2006 and 2007. I ask that they be marked for identification purposes as Staff Hearing Exhibit Number 26 and Staff Hearing Exhibit Number 27 respectively.

CHAIRMAN EDGAR: Okay. So Progress Energy Florida's 2006 Ten-Year Site Plan. And I'm sorry. The number would be?

MR. YOUNG: The 2006 Ten-Year Site Plan would be Number 26.

CHAIRMAN EDGAR: Twenty-six. Okay. And then the 2007 Ten-Year Site Plan, 27.

MR. YOUNG: Yes, ma'am.

CHAIRMAN EDGAR: Thank you.

(Exhibits 26 and 27 were marked for identification.)

BY MR. YOUNG:

Q. Do you have those before you, sir?

A. Yes, I do.

Q. Okay. Looking at the 2007 Ten-Year Site Plan, starting on line 4 -- I'm sorry. Page 2 of your amended prefiled testimony. I'm sorry. I got ahead of myself.

A. Yes.

Q. Starting on line 4 of that amended prefiled testimony, you stated that you oversaw the completion of the most recent Ten-Year Site Plan, which is April 2007; correct?

A. That's correct.

Q. And you just stated that you were involved in the preparation of the 2006 Ten-Year Site Plan?

A. Yes.

Q. Okay. Before I ask some specific questions relating to these plans, I would like to ask you a few questions about how these plans were put together. Progress uses a program called Strategist to help develop its Ten-Year Site Plan; is this correct?

A. That's one of the tools, yes. Strategist is an optimization program that is used to identify the lowest cost portfolio of capacity additions, generally self-build additions.

Q. And I'm going to ask you about how these plans were put together. In basic terms, each year you begin with the load forecast as one of the basic inputs, the demand and energy forecasts; is this correct?

A. Yes.

Q. In compiling these plans?

A. Yes, that's one of the inputs. There are several, but that is one of the major inputs.

Q. Okay. And you also get inputs on a number of other parameters, including fuel price, the cost of technology, sometimes purchased power options, DSM, which is demand-side management programs, and so on; correct?

A. That's correct.

Q. In the years where you fall below the 20 percent service margin, the next step is to identify from all the alternatives available which of the alternatives would be the most cost-effective; correct?

A. That's correct, to meet the 20 percent.

Q. Mr. Waters, would you agree with me that when considering the most cost-effective alternative, you were looking at the total cost of options, the capital costs, the operation and management expenses, the fuel costs, and any fuel inputs on the system?

A. Yes. Just to be clear, operating and maintenance expense for the incremental units would be part of the fuel cost as a system, not just the fuel cost of the new units, and the incremental capital costs associated with the additions.

Q. Okay. So basically, Strategist produces the lowest cost combination of options to get through your planning horizon?

A. Correct.

Q. To the extent the assumptions PEF enters into the Strategist program regarding capital costs, operation and maintenance expense, fuel costs, et cetera, changes from year to year, the results that Strategist produces will change, correct, as well?

A. Yes, that's possible. As inputs change, the results we get may change.

Q. Thus, the forecasted amount of utility-owned generating capacity and the purchased power requirements for each can vary from year to year?

A. Yes.

Q. Okay. And the purchased power contract that appears in the Ten-Year Site Plans, this is purchased power that Progress already has under contract or may be negotiating at the time the Ten-Year Site Plan is put together; correct?

A. That's correct.

Q. Now, Mr. Waters, can you please turn to Schedule 8 in the 2006 Ten-Year Site Plan?

A. Okay. Page 3-7. I have that.

Q. And for the record, that's -- as you look at the bottom right-hand corner, that's hearing exhibit page number 000068. Do you have it in front of you, sir?

A. Yes, I do have it.

Q. Mr. Waters, looking at the plan, Progress's 2006 Ten-Year Site Plan makes no mention of the CR3 uprate; is this correct?

A. That's correct.

Q. Looking at the projects under column 10, there are six projects that go into commercial service in 2010 or later; correct?

A. Yes.

Q. Now, please turn your attention to column 13 of that plan.

A. Okay.

Q. Looking at the total megawatts associated with these six line items, the total megawatts would be 2,778 megawatts; correct?

A. Well, I don't have a calculator with me. I will accept that for the purposes of the discussion.

Q. Subject to check?

A. Subject to check.

Q. Okay. Now, turning your attention to the 2007 Ten-Year Site Plan, Schedule 8.

A. Okay. I have that.

Q. Looking at the projects that go into commercial service in 2010 or later under column 10 and the megawatt size of these additions under column 13, would you agree the net total megawatts associated with these seven line items is 2,335 megawatts, subject to check? I'm sorry 2,355 megawatts, subject to check?

A. Okay. I'll accept that subject to check.

Q. So, Mr. Waters, it appears that Progress Energy's 2007 estimate of planned and propsective generating capacity for the period of 2010 and beyond is approximately 423 megawatts less than its estimate for the same period in the 2006 report; correct?

A. Yes, based on this form alone. Just one word of caution. If you go back, I already discussed the extension of the UPS contract, the 424 megawatts, which is one of the differences. You have to go back and look at the plan as a whole and look at not only the self-build options, which is on this form, but the purchases, DSM changes. It all goes together. I think what you find is that in the two plans, the sum of all the resource options over a given period of time is very similar. It may not match exactly in megawatts, but it's close.

Q. That's fine. And I think -- Mr. Waters, I think I overheard you on cross-examination with other counsel that you estimate that approximately 200 to 250 megawatts per year is the expected increase that is needed for Progress Energy Florida; correct?

A. Roughly. Just due to load growth, we're looking at roughly 200 to 250 megawatts of capacity need each year.

Q. Okay. Please look at the bottom of the page on the 2007 Ten-Year Site Plan we've been discussing.

A. Yes.

Q. It shows a 1,125-megawatt unit going into commercial service in 2006; is this correct?

A. 2016.

Q. 2016, excuse me.

A. Yes.

Q. PEF doesn't -- Progress doesn't need all that, doesn't need the whole 1,125 megawatts in that year; correct?

A. Not in that year, that would be correct, based on the number I gave you previously. What that says is, based on our analysis of the whole portfolio, it's better to build a large unit that will carry us multiple years than to build several small units. It's more economic.

Q. And to the extent this new unit is less expensive than existing energy on Progress's system, this new unit would displace more expensive energy; correct?

A. Yes, based on energy alone. To the extent it produces lower cost energy, it would displace more expensive energy on the system.

Q. And Progress's customers would benefit from these savings; correct?

A. Well, I want to be very clear. On fuel alone, they would benefit. Remember, in this case, you have to account for the cost of that 1,125-megawatt unit. So if the question is would there be a net savings to customers, my answer is probably no.

Generally when we're adding units to meet the 20 percent reserve margin, as I discussed earlier, you very rarely have an option that pays for itself in fuel savings. That's the difference, I think, between the additions we see on this page, most of them, and the Crystal River 3 uprate. It actually does pay for itself in fuel savings.

Q. On the same schedule, line items 8 and 9, referring to the Bartow units.

A. Yes.

Q. Okay. Now, it appears that Bartow Units 1 through 3 will be retired in 2009. I think you said that.

A. Yes.

Q. And replaced by a larger Bartow Unit 1 also in 2009, June of 2009; is this correct?

A. That's correct.

Q. Now, looking under column 13 at the two line items dealing with the Bartow units, it appears that there will be a net increase of 715 megawatts as a result of the repowering of the Bartow unit site; correct?

A. Based on the summer rating, that's correct.

Q. And the repowering of the Bartow units will care Progress potentially for multiple years on load growth; correct?

A. Potentially. It's obviously more than needed for one year. The other factor that plays in here, we have to go and again look at the purchased power contracts. As they expire, they also have to be replaced. So while I'm giving some rather simplistic examples for load growth and so on, the total picture, you have to look at other things going on besides load growth to get a true picture of why we may need capacity in any given year.

Q. Okay. I think you might have said this. The Bartow unit will replace more expensive generation on

Progress's system; is this correct?

A. The energy from that unit, yes, will displace more expensive energy on the system.

Q. Also, the Bartow unit will displace more expensive purchased power on an energy basis; is this correct?

A. Yes. To the extent there are more expensive purchases on the system, it will displace those also.

Q. And Progress's customers will receive a benefit from these savings?

A. In terms of fuel, that's correct.

Q. How will Progress recover its investment in the repowered Bartow units?

A. Well, I would have speculate, because I'm not certain. Other things have been done in the past. But for the analysis purposes, we don't make any assumption on how it's recovered. But I think to get to your question, the normal assumption might be rate base treatment, but that remains to be seen.

Q. Okay. Who would better be served to answer that question, sir?

A. I think you could ask Mr. Portuondo how that would work.

Q. When Progress builds a new plant, new power plant, it does not necessarily match the capacity exactly with the load growth; correct?

A. That's true.

Q. In fact, PEF looks at building larger units that may meet several years' load growth because you can get an economy of scale; correct?

A. That's correct, yes.

Q. To the extent that the new units run efficiently, it will displace energy from any unit producing today that has a higher production cost or high fuel cost; correct?

A. Yes, it will displace that energy, that's true.

Q. Hines Unit 4 is scheduled to come online in December 2007; correct?

A. Correct.

Q. When the Hines unit comes online, this new energy will displace more expensive energy Progress is currently relying upon to meet its requirements; correct?

A. Yes, I think that's true.

Q. And Progress Energy's customers will receive a benefit from these savings?

A. In the fuel, in terms of fuel, that's correct.

Q. Would the recovery of the investment in Hines Unit 4 be another question for Mr. -- I'm sorry. How will Progress recover the investment in the Progress Energy Florida Hines Unit 4?

A. I'll go to your first question first. Yes, I think that would be for Mr. Portuondo to discuss.

Q. Okay. Now, looking at the 180 megawatts from the CR3 uprate, this capacity will displace 180 megawatts of other capacity in the long run; correct?

A. 180 megawatts in the long run, that's correct.

Q. Okay. Looking at the 2007 Ten-Year Site Plan, the sixth row down, Crystal River 5, does this line item indicate a 30-megawatt derate for CR5 due to the installation of an FGD scrubber on the unit?

A. Yes.

Q. And what is an FGD scrubber, sir?

A. It's flue gas desulfurization. The 30-megawatt derating is a recognition of the fact that putting cleanup equipment on the back end of a unit basically increases the load on the unit. There's a lot of equipment on the back end that basically siphons electricity from the unit, so the net rating to the system goes down.

Q. Now, please turn your attention to Schedule 7.1 of the 2006 Ten-Year Site Plan. That's 3-5.

A. Okay.

Q. Now, looking at the row for 2010 under column 3.

A. Yes.

Q. It indicates the company forecasted 1,093 megawatts of firm purchased power capacity for 2010; correct?

A. Yes.

Q. The same schedule, same column, but looking at the rows for 2011, it indicates the company was forecasting firm purchased power capacity of 890 megawatts for 2011; correct?

A. Correct.

Q. So according to the company's 2006 Ten-Year Site Plan, with no consideration of the CR3 uprate, the company forecasted a 203-megawatt decrease in reliance on the firm purchased power from 2010 to 2011; correct?

A. Yes.

Q. And the company continued to forecast annual firm purchased power of 890 megawatts in 2012 and in 2013 before the level dropped to 412 megawatts in 2014 and '15; is this correct?

A. That's correct.

Q. Looking at the 2007 Ten-Year Site Plan, Schedule 7.1.

A. Yes, I have that.

Q. Looking at the row for 2010 under column 3, it indicates the company's forecasted firm purchased power capacity of 1,253 megawatts for 2010; correct?

A. Yes.

Q. Now, the same schedule, same column, but looking down for 2012 -- well, in the row for 2011 -- excuse me. It indicates the company's forecasted purchased power capacity of 1,370 megawatts for 2011; correct?

A. Correct.

Q. So according to the company's 2007 Ten-Year Site Plan, the company forecasted a 117-megawatt increase in reliance on the firm purchased power for 2010 and 2011; correct?

A. That's correct.

Q. Same schedule, same column, but looking down, looking at the row for -- excuse me. Same schedule, same column, but looking at the row for 2012. Are you there, sir?

A. Yes.

Q. It indicates the company's forecasted firm purchased power of 1,530 megawatts for 2012; correct?

A. Correct.

Q. So the company forecasted this 1,530 level of firm purchased power through 2015; correct?

A. That's correct.

Q. So, Mr. Waters, it appears that Progress is now projecting 640 megawatts more of purchased power for 2012 in its 2007 forecast than it projected it would need for the same period in the 2006 Ten-Year Site Plan; correct?

A. Well, to be clear, this is not really a forecast in the same sense as load and fuel prices and so on. This is based on contracts. As I mentioned earlier, generally speaking, in the Ten-Year Site Plan, we either reflect actual contracts or contracts that are near completion in negotiation. So what 2007 does reflect versus 2006 is that we have signed contracts, signed additional contracts for purchased power.

Two that come to mind that account for most of the difference between the two years are the Southern UPS contract, which I mentioned before, which had expired in 2010 under the original contract, which we extended through '15, with an option to go through '17 for the combined cycle. And we've discussed that quite a bit today. And the other contract is about 470 or 480 megawatts from the Shady Hills facility, which we extended for an additional five years beyond the planning horizon. That in 2006 under the terms of the contract would have expired, but we extended that contract, so it is reflected in 2007 as running longer than what we had.

So this isn't so much a forecast of what we think purchased power will be. These are contracts that we've signed. Again, based on economics, it was more economic to purchase from these facilities than to build new facilities that we may have identified, and we have identified the final result of that in the site plan.

Q. Okay. Thank you, sir. Now, Mr. Waters, do you recall in your deposition I asked you a series of questions regarding your understanding of the methodology that Standard & Poor's used to evaluate the perceived impact purchased power contracts have on a utility's financial position?

A. Yes.

Q. And it is your understanding that -- you said that, if I can recall, that you were not the expert, but you are familiar with that methodology; correct?

A. That's correct.

Q. Okay. Isn't it your understanding that when Progress makes a long-term commitment to purchase power, that some portion of the contract is treated by the rating agency as imputed debt?

A. Yes.

Q. And is it your understanding that's an additional cost to the company as a result of the rating agency treatment on purchased power contracts; correct?

A. Yes. And because of that understanding, when we do an economic analysis of any purchase, we account for that additional cost as a cost of the purchase when we compare it to a self-build option. So when I say that the economics of purchasing are better than building, we have accounted for that additional cost represented in the -- we'll call it imputed debt for now.

Q. Specifically how did you account for that cost?

A. This is where I don't want to go too far beyond my expertise, because our finance people actually calculate the exact number. But basically, what is done is, based on the type of contract we're going to sign -- and just as an example, there are take-or-pay contracts, there are pay-for-performance contracts, different kinds of contracts.

Standard & Poor's recognizes that your fixed payment stream, basically the capacity charges, a certain portion of that they treat as debt looking forward on your books, and the percentage they treat as debt depends on the type of contract that you have. A take-or-pay contract would have a higher percentage imputed than a pay-for-performance contract. But a percentage of those fixed payments going forward are treated as debt.

What that does is to bring -- the way we look at it as an additional cost, to bring the balance sheet or the capital structure back in line, there would be a cost associated with additional equity to basically equalize back to where your balance sheet was before you made that purchase. That additional cost is what we're talking about basically in making the purchase.

Q. First, are you familiar with Progress's position regarding the need to increase its equity capitalization to offset the imputed debt associated with the purchased power? I think you just answered it sir.

A. I think --

Q. I just want it for the record.

A. When you say Progress Energy's position, I know it has been our position that that is an appropriate adjustment when we analyze purchased power, and we've done that consistently for some time, including in our analyses of requests for proposals we've done in the last couple of cycles where we've made capacity decisions. So I know it has been presented to the Commission I think consistently over some period of time.

Q. Progress included an equity adjustment in its calculation of the cost of additional purchased power when it revised its estimates for 2012; correct?

A. I'm sorry. I didn't put that together. Are you talking about in the revised site plan numbers?

Q. Yes.

A. Those are actual contracts, so in the analysis of those actual contracts, yes, we did include that additional cost in the analysis, if that's the question.

Q. Okay. Mr. Waters, please turn to the bottom of page 6 of your amended prefiled direct testimony.

A. Okay.

Q. On line 23 through the top of page 7, you said that altogether, purchased power resources account for approximately 12 percent of PEF's generation resources. Is this correct? Is this a true statement?

A. Yes.

Q. And this level of purchased power reflects all purchased power contracts for Progress as of the 2007 time frame; correct?

A. That's correct.

Q. Would you agree with me, sir, that subject to check, that in the 2006 Ten-Year Site Plan, the company projected that it will rely on purchased power for approximately 13.5 percent of its generation resources for 2012?

A. I think that's approximately correct. I'll accept that subject to check.

Q. And would you agree with me, sir, subject to check, that in the 2007 Ten-Year Site Plan, the company projects that it will rely on purchased power for approximately 18.6 of its generation resources for 2012?

A. Are you including qualifying facility purchases in the numbers?

Q. Yes.

A. Okay. Yes. Then I would agree with the numbers, yes.

Q. And finally, Mr. Waters, the additional cost that results from Progress's increased reliance on purchased power to meet its requirements, that has already been factored into the cost of these contracts in PEF's evaluation process?

A. Yes.

MR. YOUNG: No further questions, Madam Chairman.

CHAIRMAN EDGAR: Questions on redirect.

MS. TRIPLETT: Very brief, Madam Chair. Thank you.

REDIRECT EXAMINATION

BY MS. TRIPLETT:

Q. Mr. Waters, Mr. Young asked you several questions about other units planned in the 2006 and 2007 Ten-Year Site Plans. I believe he mentioned Hines 4 and the Bartow repowering. Can you explain the differences between those projects and the CR3 uprate?

A. The difference is how they enter the process. The Hines 4 project and the Bartow project -- going back to the discussion we had on the general planning process, we look at our load forecast, we look at existing resources, we look at where we fall short on the 20 percent reserve margin, and then we look at what alternatives we have that we can add to the system to get us back to 20 percent. We then identify what would be the lowest cost alternative to add on a self-build basis. That would be -- a Hines 4 or Bartow project would come out of that process.

The CR3 uprate was not developed as an alternative to meet some future need for capacity. It was developed as a potential fuel savings alternative, and it was fed into the process. As I mentioned earlier in one of the discussions, if we had no need for capacity at all, the Crystal River 3 project would still make sense, because it still pays for itself. It reduces cost to customers. The fact that it contributes

180 megawatts of capacity, I will not ignore that. I will certainly add that to the plan, but that is not its primary purpose, and that's not how it came about in the plan. That's not why we developed it and put it into our Ten-Year Site Plan.

So I think that's the basic difference.

Q. Mr. Waters, you were asked also a number of questions comparing different numbers between the 2005, 2006, and 2007 Ten-Year Site Plans. Can you simply compare by adding or subtracting various numbers among the different Ten-Year Site Plans?

A. No. I tried to caution as we were going through that. Taking any single column or any single form from the site plan and comparing it from one year to the next is something of a dangerous exercise, because really, from one year to the next, all the numbers change. Our load forecast changes. Our alternatives may change. The amount of DSM we have planned may change. The purchases will change, because we may have been negotiating contracts between one cycle and another. So you need to kind of look at the totals, you know, what is the total capacity added, the sum of the purchases, the new capacity, and even the DSM to make sure -- to see what really changed overall in the system. So just looking at one column or another I think may lead to an erroneous conclusion.

MS. TRIPLETT: Thank you. No further questions.

CHAIRMAN EDGAR: Okay. Let's take up the exhibits.

MS. TRIPLETT: We will move into evidence witness Exhibits SSW-1 and 2, and those are Hearing Exhibits 5 and 6.

CHAIRMAN EDGAR: Yes, ma'am. Thank you. Seeing no objection, Exhibits 5 and 6 will be entered into the record.

(Exhibits 5 and 6 were admitted into the record.)

CHAIRMAN EDGAR: Mr. McWhirter, I believe you had Exhibit 22.

MR. McWHIRTER: I would like to introduce 21 and 22. We've had argument about 21, so maybe I'll first go to 22 and then come back.

CHAIRMAN EDGAR: Let's start with 22.

MR. McWHIRTER: Okay.

MS. BENNETT: As a matter of record, it appears on the comprehensive exhibit list as 20 and 21, with 20 being the excerpt of the 2006 Ten-Year Site Plan, and 21 is --

CHAIRMAN EDGAR: Is the full document.

MS. BENNETT: Twenty-one is the site plans themselves.

CHAIRMAN EDGAR: Okay. Well, let's start with 22. Any objection to Exhibit 22? Seeing none, Exhibit 22 will be entered into the record. We can take up 20 and 21 together. Any objection?

MS. TRIPLETT: Progress Energy has no objection to 21, which is the actual Ten-Year Site Plans that Progress filed. However --

CHAIRMAN EDGAR: Okay. Then seeing no objection, we will enter Exhibit 21 into the record.

(Exhibit 21 was admitted into the record.)

CHAIRMAN EDGAR: And you have a concern about Exhibit 20?

MS. TRIPLETT: Yes, ma'am. Again, we would object to the relevance of Exhibit 20, as there has been no testimony as to the relevance of this particular document as it regards this proceeding. Again, we don't object to the authenticity of the document, just the relevance in this proceeding.

CHAIRMAN EDGAR: Mr. McWhirter?

MR. McWHIRTER: Madam Chairman, this is a document which we requested official notice under the provisions of Florida Statute 90.202, I believe it is. The Commission can take notice of things that are well known to it, as you know.

And with respect to the relevance, it's relevant because it refers to an existing continuing problem with the transmission system in the northern part of Florida. And the witnesses that are proffered in this case that have the burden of proving their case have no knowledge of the relationship to the general transmission problems and the problems that are created by the uprate, and I think that's evidence that the company's presentation is falling short of the mark with respect to whether this transmission line is exclusively for the uprate or for general transmission problems.

And our position is that probably what they're trying to do here is to get 34 miles of transmission line that normally would have come in under base rates into the cost recovery clause, and they purposefully didn't put forward any witness that talked about the transmission problem.

CHAIRMAN EDGAR: Okay. Ms. Helton, to the document.

MS. HELTON: Madam Chairman, I have to say that I agree again with Ms. Triplett that I'm not sure that a foundation has been laid upon which you can admit Exhibit Number 20.

CHAIRMAN EDGAR: Mr. McWhirter, from the

reasons you've given, I tend to agree. It sounded to me like again some rearguing and maybe some legal conclusions that were a little bit beyond the scope of the foundation for this document to be admitted with this witness, so could I ask you to speak again to that point?

MR. McWHIRTER: Well, she's talking about foundation, and she's talking about relevance.

MS. TRIPLETT: Well, I didn't --

MR. McWHIRTER: Foundation doesn't have to be dealt with, because it's official notice, and it's something that you can enter into evidence without the necessity of formal authentication.

MS. HELTON: Well, for whatever reason -- there was a motion for official recognition that Mr. McWhirter filed prior to the prehearing conference. For whatever reason, I don't know that that motion per se was ruled upon. I think that the ruling by the Prehearing Officer was that the parties stipulated that the items included in his list of official recognition would be entered into the record or entered on the list, exhibit list, and the parties reserved the right to object to the relevancy of each document. So I think that's where we find ourselves.

I think that before you can even -- as I understand evidence, before you can even get to the issue of whether a particular exhibit is relevant or not, you have to lay the foundation. In my mind, if we don't have a witness that can speak to the exhibit, I'm not sure how you can lay a foundation and how you can show the relevance.

CHAIRMAN EDGAR: Ms. Helton, have we not in the past at times taken administrative or judicial notice of documents which are well known and therefore do not need to be authenticated without entering them into the record through numbering, et cetera?

MS. HELTON: Yes, ma'am, we have.

CHAIRMAN EDGAR: Okay. How about we do it that way, Mr. McWhirter?

MR. McWHIRTER: Well, that's what I prefer to do. That's what I --

CHAIRMAN EDGAR: Then we're all on the same page. We're all on the same page. Okay. Exhibit 20 will not be admitted into the record. However, we will take administrative or judicial notice of this material.

And with that, I that think we have taken up all of the exhibits. Are there any other questions or items --

MR. YOUNG: Madam Chairman.

CHAIRMAN EDGAR: Who -- where are we? Oh, yes, sir, Mr. Young.

MR. YOUNG: Staff asks that we move Exhibits Number 22, 26, and 27 into the record.

CHAIRMAN EDGAR: Any objections?

MS. TRIPLETT: No, ma'am.

CHAIRMAN EDGAR: Okay. We will enter Exhibits 22, 26, and 27 into the record.

(Exhibits 22, 26, and 27 were admitted into the record.)

CHAIRMAN EDGAR: Any other matters before this witness is dismissed, excused? No other matters. Okay. The witness can be excused. Thank you very much.

MS. TRIPLETT: Madam Chairman, may he be dismissed from the proceeding?

CHAIRMAN EDGAR: He may be dismissed.

MS. TRIPLETT: Thank you.

CHAIRMAN EDGAR: And you may call your next witness.

MR. WALLS: Madam Chair, we call Javier Portuondo.

Thereupon,

JAVIER PORTUONDO

was called as a witness on behalf of Progress Energy Florida, and having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. WALLS:

Q. Mr. Portuondo, will you please introduce yourself to the Commission and provide your address?

A. My name is Javier Portuondo. My address is 410 South Wilmington, Raleigh, North Carolina.

Q. Who do you work for, and what is your position?

A. I am employed by Progress Energy Service Company in the capacity of Director of Regulatory Planning.

Q. And have you filed prefiled amended direct testimony and exhibits in this proceeding?

A. Yes, I have.

Q. And do you have any amendments to make to your prefiled amended direct testimony or exhibits?

A. No, I do not.

Q. If I asked you the same questions in your amended prefiled direct testimony today, would you give the same answers that are reflected in that testimony?

A. Yes, I would.

MR. WALLS: We request that the amended direct testimony of Mr. Portuondo be moved into evidence at this time as if read.

CHAIRMAN EDGAR: The amended direct prefiled testimony of Witness Portuondo will be entered into the record as though read.

IN RE: PETITION TO RECOVER THE COSTS OF THE CRYSTAL RIVER UNIT 3 UPRATE THROUGH THE FUEL CLAUSE

BY PROGRESS ENERGY FLORIDA

FPSC DOCKET NO. 070052

AMENDED DIRECT TESTIMONY OF

JAVIER PORTUONDO

I. INTRODUCTION AND QUALIFICATIONS

Q. Please state your name and business address.

A. My name is Javier Portuondo. My business address is 410 South Wilmington Street, Raleigh, North Carolina, 27601.

Q. By whom are you employed and in what capacity?

A. I am employed by Progress Energy Service Company, LLC, as Director of Regulatory Planning.

Q. What is the scope of your duties?

A. Currently, I am responsible for regulatory planning, cost recovery, and pricing functions for both Progress Energy Florida ("PEF" or the "Company") and Progress Energy Carolinas.

Q. Please describe your educational background and professional experience.

A. I received a Bachelors of Science degree in Accounting from the University of South Florida. I began my employment with Florida Power Corporation in 1985. During my 21 years with Florida Power Corporation and PEF, I have held a number of financial and accounting positions. In 1993, I became Manager, Regulatory Services, and I recently became Director, Regulatory Planning.

II. PURPOSE AND SUMMARY OF AMENDED TESTIMONY

Q. Did you previously file direct testimony in this proceeding?

A. Yes.

Q. What is the purpose of your previously filed direct testimony?

A. The purpose of my testimony is to support the Company's request for recovery of reasonably and prudently incurred costs of the Crystal River Unit 3 ("CR3") power uprate project. Specifically, I will explain why recovery of the power uprate costs, transmission-related project costs, and Point of Discharge ("POD") related project costs through the Fuel and Purchase Power Cost Recovery Clause ("Fuel Clause") is appropriate and consistent with established Commission policy.

Q. Why are you amending your previously filed direct testimony?

A. After further evaluation and meetings with the Nuclear Regulatory Commission ("NRC") regarding the proposed uprate project, the Company has determined that part of the uprate project work originally scheduled for the 2009 refueling and steam generator replacement outage can be accelerated and performed during the 2007 refueling outage. The reasons for this change are explained in the amended direct testimony of Daniel L. Roderick. I am amending my direct testimony to explain that, with the acceleration of part of the power uprate project to the 2007 refueling outage, the Company's customers will begin to receive an additional 12 MWe of nuclear power beginning in 2008, with the corresponding fuel savings, and the Company will need to recover the costs of this first phase of the CR3 power uprate project in the 2007 Fuel and Purchased Power Docket.

Q. Are you sponsoring any Exhibits with your direct testimony?

A. Yes. I am sponsoring the following exhibits that were prepared under my supervision:

- Exhibit No. ___ (JP-1), which is an excerpt of Schedule B-13 of the Minimum Filing Requirements ("MFRs") submitted in Docket No. 050078-EI.
- Exhibit No. ___ (JP-2), which is an excerpt of Schedule B-2 of the MFR's submitted in Docket No. 050078-EI.
- Exhibit No. ___ (JP-3), which is an excerpt of Schedule B-1 of the MFR's submitted in Docket No. 050078-EI.

These exhibits are true and correct.

Q. Please summarize your testimony.

A. The CR3 power uprate project will provide PEF's customers substantial fuel savings expected to be in excess of $2.6 billion by the end of 2036 with an expected net present value of savings to costs of $320 million to the retail customer. The power uprate project achieves these savings by displacing fossil fuel generation capacity with additional nuclear generation capacity and, thus, enhancing fuel diversity on the Company's system. The Commission has long sought to encourage innovative utility projects and programs that reduce total customer costs by providing the incentive of cost recovery under the Fuel Clause for such projects and programs. Under well established Commission precedent, cost recovery under the Fuel Clause is authorized when the costs (1) were not anticipated and included in current base rates and (2) generate fuel savings for customers. The costs of the CR3 power uprate project were not anticipated and they are not included in the Company's current base rates and the project costs generate substantial fuel savings for PEF's customers. As a result, under Commission precedent, the Commission should grant PEF's petition requesting that the Commission find that the CR3 power uprate costs are eligible for cost recovery under the Fuel Clause.

III. OVERVIEW OF THE PROJECT

Q. Please describe the CR3 power uprate project.

A. The CR3 power uprate project will increase the power output of CR3 by approximately 180 MWe, resulting in a capacity increase in the unit from about 900 MWe to 1,080 MWe. As discussed in more detail in the amended pre-filed testimony of Danny Roderick, the project has three major phases. The first part of the project will require modifications to plant instrumentation and associated calculations to allow measurement uncertainty recovery ("MUR"). These modifications are expected to increase output by approximately 12 MWe towards the end of 2007. The second part of the project involves replacement of the turbine line components to take advantage of greater steam efficiencies in the turbines and electrical generator. These modifications are expected to increase output by approximately 28 MWe at the end of 2009. The third part of the project will involve increasing the power or thermal megawatts ("MW's") produced in the reactor core by making changes to the core that will allow for use of more highly enriched uranium. The increase in CR3 capacity will require modifications to the transmission system and modifications to address POD thermal limit issues to reap the full benefit of the power uprate. The work required by the project will be completed during the CR3 fuel outages in the 2007 refueling outage, 2009 generator replacement and refueling outage, and the 2011 refueling outage at CR3.

Q. What are the projected costs of the CR3 power uprate project?

A. As Mr. Roderick explains in his testimony, the project is estimated to cost approximately \$381.8 million in total, with the power uprate itself requiring approximately \$250 million and the modifications to the transmission system and to address the POD issues caused by the additional power and heat generated by the power uprate estimated at \$89 million and \$43 million, respectively. The Company will continue to analyze the issues surrounding the CR3 power uprate project, in particular the transmission and POD impacts and available remedies, and refine its cost estimates as the time for work on the project draws closer.

Q. Why is the Company requesting Commission approval of the CR3 power uprate project at this time?

A. The Company began incurring expenditures in 2006 and is continuing to make expenditures to ensure that work necessary for the power uprate itself can be done during the 2007, 2009, and 2011 scheduled refueling outages for the CR3 unit.

Q. Why has the Company proposed this project?

A. The primary purpose of the CR3 power uprate project is to reduce fuel costs to customers by displacing energy from higher cost fossil fuel with low cost nuclear fuel. The power uprate at CR3 is not needed to meet a need for additional power to ensure customers a continued supply of reliable power, although the uprate will increase the base load power available to the Company. Rather, the CR3 power uprate meets an economic need for cheaper power and greater fuel diversity as nuclear fuel from the power uprate displaces more expensive fossil fuels and purchased power on the Company's system. The CR3 power uprate project generates substantial fuel cost savings for the Company's customers. The Company is proposing the CR3 power uprate project to give its customers the benefit of these substantial fuel cost savings.

Q. What are the results of the fuel cost savings analysis?

A. The CR3 power uprate project is expected to produce approximately $2.6 billion in fuel savings by the end of year 2036. With the expected net present value ("NPV") of fuel savings to the retail customers of $640 million and a NPV of the costs of only $320 million, this will result in a NPV savings to the retail customer of almost $320 million. These fuel savings benefits are further explained in the amended direct testimony of Samuel S. Waters.

IV. COST RECOVERY FOR THE PROJECT

Q. Are the costs of the CR3 uprate project recovered through the Company's base rates?

A. No. The CR3 power uprate project was not anticipated when PEF's current base rates were established in Docket No. 050078-EI. The costs of the project, therefore, were not included when the Company submitted its MFRs in its most recent base rate proceeding in Docket No. 050078-EI in April 2005. This is demonstrated by Exhibit No.___ (JP-1), Exhibit No. ___ (JP-2), and Exhibit No. ___ (JP-3).

Exhibit No. __ (JP-1) is an excerpt (page 1) from MFR Schedule B-13. That schedule presented the construction work in progress ("CWIP") for the projected 2006 test year. The only project for nuclear production on this schedule is for the Crystal River 3 Steam Generator replacement. The $230 million shown on line 11 for this project does not include any costs associated with the planned uprate. Further, Exhibit No. ___ (JP-2) is an excerpt (page 1) from MFR Schedule B-2. That schedule shows rate base adjustments. On line 28 of this schedule an adjustment is made to back out CWIP bearing an allowance for funds used during construction ("AFUDC"). The CWIP associated with the Steam Generator replacement is backed out of rate base on this line. Exhibit No. ___ (JP-3) is an excerpt (page 1) of MFR Schedule B-1. That schedule shows the adjusted rate base. It can be seen on line 31 of this schedule that the CWIP associated with the Steam Generator replacement is backed out of rate base for the 2006 test year. To summarize, the Crystal River uprate would have been associated with Nuclear Production. The only major project for nuclear production in the test year is the Steam Generator replacement. No costs associated with the CR3 power uprate project are included in the CWIP for the Steam Generator replacement. Even if there had been costs for the CR3 power uprate project on line 11 of MFR Schedule B-13, which is not the case, the entry on line 11 shows that all these costs were backed out of rate base on MFR Schedules B-1 and B-2, as I have explained above. With the approval of the rate case settlement agreement in Docket No. 050078-EI, the Commission approved the Company's MFRs for purposes of establishing the Company's baseline costs in its next base rate proceeding. Order No. PSC-05-0945-S-EI, Docket No. 050078-EI (Sept. 28, 2005), p. 2, Attachment A, ¶ 17.

Q. How does the Company propose to recover the costs of the project?

A. PEF proposes to recover through the Fuel Clause all capital costs incurred for the CR3 power uprate, necessary transmission system changes, and any costs incurred to offset the POD impact for the project, including a return on average investment and taxes, to the extent such costs do not exceed cumulative expected fuel savings over the life of the project. The Company will not begin recovery through the Fuel Clause until the CR3 power uprate goes into commercial service. For phase one of the CR3 power uprate project, recovery is expected to commence at the beginning of 2008. PEF anticipates requesting recovery of these costs as part of the 070001 Fuel and Purchased Power docket. For phases two and three, recovery is expected to begin at the end of 2009 and 2011, respectively. Actual costs incurred for the CR3 power uprate project would be subject to Commission review for prudence and reasonableness as they are submitted for recovery through the Fuel Clause. PEF will submit follow-up testimony as the costs of the project become more firm to establish the proposed recovery under the Fuel Clause.

Q. Does Commission precedent support the recovery of the CR3 power uprate costs, transmission-related project costs, and POD-related project costs through the Fuel Clause?

A. Yes. There is a long line of Commission authority supporting the timely recovery through the Fuel Clause of costs that are necessary to reduce total costs and benefit customers. Beginning in 1981, in Order No. 9957 in Docket No. 810001-EU, the Commission granted Florida Power & Light Company's ("FPL") petition to revise the definition of costs which may be included within the Fuel Clause to allow the recovery of capacity costs associated with FPL's purchases of "coal-by-wire" from the Southern Company. Order No. 9957, Docket No. 810001-EU, 1981 Fla. PUC LEXIS 531 (April 20, 1981). FPL argued that such costs should be recovered through the Fuel Clause when they had the effect of lowering revenue requirements.

Excluding such costs from recovery under the Fuel Clause, FPL further argued, would penalize FPL's stockholders for making prudent management decisions that serve to reduce total costs. Order No. 9957, 1981 Fla. PUC Lexis 531, *3-*6.

The Commission agreed that the definition of recoverable costs under the Fuel Clause should be revised to permit the recovery of the capacity costs associated with FPL's economy purchases from the Southern Company when those transactions served to lower overall costs to ratepayers. The Commission noted that such purchases on many occasions "will have the effect of replacing expensive, oil-fired generation with cheaper "coal-by-wire", lessening the revenues required from ratepayers and also decreasing the need for imported oil." Order No. 9957, 1981 Fla. PUC Lexis 531, *5, *6. Accordingly, the Commission granted FPL's petition, recognizing that the capacity purchase costs were not recovered in FPL's base rates, and allowed FPL to recover the costs through the Fuel Clause.

Q. What policy did the Commission establish in Order No. 9957?

A. The Commission wanted everyone to understand that it intended to encourage innovative projects that reduced costs and benefited customers. As the Commission explained: "... [w]e wish to indicate that the <u>underlying principle</u> governing our decision --- <u>that utilities must be encouraged to take innovative actions designed to benefit customers and to lower overall costs</u> --- <u>has application elsewhere</u>." Order No. 9957, 1981 Fla. PUC LEXIS *7. (emphasis supplied). The Commission intended this principle to be broadly applied, i.e., by "application elsewhere", whenever necessary to ensure that utilities recovered their costs to provide savings to ratepayers. Indeed, the Commission pointed out that the subject of acquiring inexpensive "coal-by-wire" on an economical basis was just an example of the type of innovative "ideas and programs" that the Commission hoped to encourage utilities to pursue to take advantage of the opportunity to lower costs to customers. Id.

Q. What conditions did regulated electric utilities face in the early 1980's?

A. Following the oil embargo and crises of the mid- and late 70's, regulated utilities and their customers faced rising fossil fuel costs and increasing interest rates by the late 70's and early 80's. At the same time, utilities were experiencing continued growth in customers and customer demand for energy in Florida. This situation led to the passage of the Florida Energy Efficiency and Conservation Act ("FEECA") in 1980. FEECA emphasized conservation measures to control the growth rate of peak demand and reduce energy consumption and to reduce the consumption of expensive fossil fuel resources. One such conservation measure adopted by the Commission was the Oil Backout Rule, which provided cost recovery to utilities for the economic displacement of oil generation in Florida. Former Rule 25-17.016, F.A.C. Both the Florida Legislature and the Commission recognized the need for greater fuel diversity and the reduction in customer energy costs.

Q. Do similar conditions exist today?

A. Yes, they do, although they are maybe not as extreme as the late 70's and early 80's. While population growth in Florida has abated from the peak years in the 80's, the

State's population still continues to grow. Also, with this population growth, utilities are continuing to experience growth in customer energy usage. And, while Florida utilities, especially PEF, have made great strides on fuel diversity, fossil fuel resources remain a necessary, significant source of fuel for energy production in Florida. Unfortunately, PEF and other regulated utilities are again faced with rising fossil fuel costs and interest rates. These conditions prompted the Governor to issue an Executive Order in late 2005 directing the Department of Environmental Protection ("DEP") to develop a comprehensive energy plan for the State of Florida. One of the directives in that order was the development of options for diversifying Florida's electric generation capacity. The Commission, regulated utilities in Florida, and others were invited to provide input in the development of that plan.

One of the principle recommendations in the Florida Energy Plan is the promotion of fuel diversity. To this end, the Florida legislature passed legislation in 2006 amending the Florida Electrical Power Plant Siting Act ("PPSA") to include fuel diversity as one criterion for the installation of electrical power plants. In this way, the Florida Energy Plan intended fuel diversity to be a high priority in the Commission's decision-making processes.

Q. Is the CR3 power uprate project consistent with the goals of the Florida Energy Plan and the recent legislation?

A. Yes, it is. The CR3 power uprate will increase the contribution of nuclear fuel to the mix of resources available to PEF thereby improving the Company's fuel diversity. Indeed, to the extent that the power uprate displaces higher cost fossil fuels with lower cost nuclear fuel the fuel diversity is only enhanced. This enhancement is significant because, as I have noted, the total fuel savings from the CR3 power uprate project exceed $2.6 billion. Enhancement of PEF's fuel diversity will also enhance the fuel diversity state-wide, contributing to the goal established in the Florida Energy Plan and 2006 legislation.

Q. Is there any other Commission precedent for the recovery of the CR3 power uprate project costs through the Fuel Clause?

A. Yes. Both before and after Commission Order No. 9957 in 1981 the Commission has acted consistent with the principle laid down in Order No. 9957 by allowing cost recovery through the Fuel Clause for utility expenditures designed to benefit customers by reducing overall utility costs.

In early 1980 in Dockets Nos. 790898-EU and 74680-CI, the Commission allowed FPL to recover through the Fuel Clause capital, O&M, and fuel costs associated with an experimental project to determine the feasibility of burning a coal and oil mixture in a boiler originally designed to burn only oil in an effort to displace oil with other fuels. Order No. 9224, Dockets Nos. 790898-EU and 74680-CI, 1980 Fla. PUC LEXIS 519 (Jan. 30, 1980). Interestingly, the expected net savings to the customer from the project would be realized only if the modifications were successful. Id. at *3-*4. Yet, the Commission still granted FPL's petition, explaining that the Commission was "impressed by the initiative the company is taking in its search for more economical and more readily available sources of boiler fuel" and believed "the overwhelming importance of the task" of taking the initiative to pursue more economical energy production for the benefit of the customer justified including the costs within the Fuel Clause. Id. at *5.

Likewise, in 1985 in Commission Order No. 14546, the Commission again recognized that certain, unanticipated costs are appropriate for recovery through the Fuel Clause when they result in fuel savings to customers. Specifically, the Commission recognized that, prospectively, proper charges under the Fuel Clause included "fossil fuel-related costs normally recovered through base rates but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers." Order No. 14546, Docket No. 850001-EI-B, 1985 Fla. PUC LEXIS 531, *11-*12 (July 8, 1985). In subsequent orders, the Commission repeatedly has approved the recovery of costs through the Fuel Clause when those expenditures resulted in significant savings to the utility's ratepayers. See, e.g., Order No. PSC-98-0412-FOF-EI, Docket No. 980001-EI, 1998 WL 173332 (March 20, 1998); Order No. PSC-97-0359-FOF-EI, Docket No. 970001-EI, 1997 WL 199376 (March 31, 1997); Order No. PSC-95-0450-FOF-EI, Docket No. 950001-EI, 1995 WL 220901 (April 6, 1995); and Order No. PSC-94-1106-FOF-EI, Docket No. 940391-EI, 1994 Fla. PUC LEXIS 1126 (Sept. 7, 1994).

Q. Did the Commission limit the costs that may be recovered through the Fuel Clause to fossil fuel-related costs in Order No. 14546?

A. No, the Commission did not, if the reference to "fossil fuel-related costs" is intended to mean costs associated only with fossil fuel units and their related equipment, material, or facilities. Although the Commission used the term "fossil fuel-related costs" in its list of the proper future charges to the Fuel Clause, the Commission nowhere expressly limited the Fuel Clause recovery to costs associated with fossil fuel units and their related equipment, material, or facilities, that resulted in fuel savings to ratepayers.

Instead, the Commission's express finding approved the stipulation of the parties and adopted "the provisions therein as its own." Order No. 14546, 1985 Fla. PUC Lexis 531, *8. (emphasis supplied). In those provisions, the parties recommended a policy that "was flexible enough to allow for recovery through fuel adjustment clauses of expenses normally recovered through base rates when utilities are in a position to take advantage of a cost-effective transaction, the costs of which were not recognized or anticipated in the level of costs used to establish the utility's base rates." Id. at *8-*9. (emphasis supplied). In approving these provisions, then, the Commission's policy is a "flexible" one, allowing the recovery of "expenses" when they (1) were normally recovered in base rates but not anticipated and included in current base rates and (2) resulted in a "cost-effective transaction," i.e. generated fuel savings for ratepayers.

The reference to "fossil fuel-related costs" in the subsequent list of costs recoverable in the future might have come from the example the parties provided in the stipulation of an expense that met the test of a "cost-effective transaction" under the recommended flexible policy. They explained that "one example" was "the cost of an unanticipated short-term lease of a terminal to allow a utility to receive a shipment of low cost oil." Order No. 14546, 1985 Fla. PUC Lexis 531, *9. The example, therefore, was a cost related to the fuel supply for a fossil fuel generating unit, but the parties' stipulation and the Commission's subsequent adoption of the provisions of that stipulation as its own makes clear it was just an example and not intended to be a limitation.

Indeed, any such limitation is inconsistent with the "underlying principle" encouraging cost-saving innovation that the Commission followed before and after Order No. 14546. As I have explained, the Commission intended to encourage utilities to take innovative action benefiting customers with lower costs by providing them the incentive of cost recovery through the Fuel Clause. Denying cost recovery through the Fuel Clause for costs other than "fossil" unit, facilities, equipment, or material costs, even though they result in fuel savings to customers, discourages – not encourages – innovative, cost-saving projects.

Additionally, it simply makes no sense for the Commission to draw a distinction about the type of cost incurred when the real issue is whether the costs incurred result in fuel savings to customers and were not addressed in determining current base rates. The more logical and thus reasonable construction of the reference to "fossil fuel-related costs" in the list of recoverable costs under the Fuel Clause in Order No. 14546, then, is a shorthand reference to all costs that result in the reduction in use of, or replacement of, fossil fuels. This construction of the term "fossil fuel-related costs" is consistent with the fundamental purpose of the order by providing for the recovery of all costs associated with the generation of fuel savings for the benefit of customers.

Q. Has the Commission actually limited cost recovery under the Fuel Clause to costs associated with fossil fuel units and their related equipment, material, or facilities that result in fuel savings to customers?

A. No. In 1996, the Commission in fact approved the recovery of costs associated with a power uprate of FPL's nuclear units at Turkey Point through the Fuel Clause. Order No. PSC-96-1172-FOF-EI, Docket No. 960001-EI (Sept. 19, 1996). FPL estimated that, at a cost of approximately $10 million, FPL could obtain a 31 MW increase in nuclear capacity that would result in estimated fuel savings of $198 million, or a net present value of $97 million to FPL's customers. The Commission noted that the "savings are due to the difference between low cost nuclear fuel replacing higher cost fossil fuel." Order No. PSC-96-1172-FOF-EI, 1996 WL 554613, p. 6. In approving FPL's request, the Commission expressly relied on Order No. 14546 allowing "a utility to recover fossil-fuel related costs which result in fuel savings when those costs were not previously addressed in determining base rates." Id. This Order confirms that "fossil fuel-related costs" means any cost or expense that generates fuel savings by reducing the use of, or replacing the use of, expensive fossil fuels.

Likewise, while most proceedings involving requests for cost recovery through the Fuel Clause of costs that resulted in fuel savings to customers have involved fossil fuel units or their related facilities, equipment, or material, the Commission has never said that only these specific types of costs can be recovered under the Fuel Clause. In fact, in 1994 when FPL sought to recover the cost of converting its Manatee oil units to burn Orimulsion rather than oil under the Oil

Backout Rule or, alternatively, the Fuel Clause under Order No. 14546, the Commission granted FPL's request for recovery under the Fuel Clause and made no reference to whether the costs were "fossil fuel-related costs." Rather, the Commission emphasized that Order No. 14546 authorized recovery through the Fuel Clause of "costs 'normally recovered through base rates but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers.'" Order No. PSC-94-1106-FOF-EI, Docket No. 940391-EI, 1994 Fla. PUC LEXIS 1126, pp. *5-*6 (Sept. 7, 1994). Again, the Commission's emphasis was on whether the costs incurred resulted in fuel savings to customers and not on the exact type of costs that were incurred.

Q. Is the Company's cost recovery request in this proceeding consistent with the result in Docket No. 960001-EI involving FPL's nuclear uprate proceeding?

A. Yes, it is. FPL was permitted to recover through the Fuel Clause the cost of the thermal power uprate including a return on average investment at its current weighted average cost of capital as well as applicable taxes, subject to a true-up of original projections and to verify the prudence of the individual cost components for recovery. Order No. PSC-96-1172-FOF-EI, 1996 WL 554613, p. 7. PEF seeks a similar recovery here. The only difference is the magnitude of the thermal uprate and costs and the resulting fuel savings benefits to customers. While PEF's thermal uprate costs are higher, an estimated $381.8 million compared to FPL's $10 million for a 180 MWe versus a 31 MWe uprate, the fuel savings benefits are also more substantial, over $2.6 billion in PEF's thermal uprate compared to $198 million in FPL's thermal uprate.

Q. Has the Commission recognized the fuel cost savings benefits of nuclear generation in other Fuel Clause matters before the Commission?

A. Yes, it has. Beginning with its Order No. PSC-01-2516-EI, the Commission has authorized the recovery of security expenditures incurred in response to the terrorist attacks of September 11, 2001 through the Fuel Clause even though security costs were traditionally and historically recovered through base rates. In granting this cost recovery the Commission explained that "[w]e find that recovery of this incremental cost through the fuel clause is appropriate in this instance because there is a nexus between protection of FPL's nuclear generation facilities and the fuel cost savings that result from the continued operation of those facilities." Order No. PSC-01-2516-EI, Docket No. 010001-EI, 2001 WL 1677492, p. 3 (Dec. 26, 2001). The Commission was willing to allow the recovery through the Fuel Clause of the non-fuel related additional security costs because the Commission understood the fuel savings value of nuclear operations.

PEF, through the CR3 power uprate project, is actually seeking to enhance its nuclear operations to generate even more fuel savings for customers than currently exist from the operation of CR3. The recovery of the CR3 power uprate costs, transmission-related project costs, and POD-related project costs through the Fuel Clause is consistent with the Commission's understanding of the fuel savings value of nuclear operations in general and PEF's nuclear facility in particular.

Q. Do you believe the Commission still supports the underlying principle from Order No. 9957 that utilities should be encouraged to take innovative action designed to benefit customers by lowering their costs?

A. Yes I do, because the Commission says it does. In the Commission's Mission Statement the Commission explains that its mission in relevant part is to emphasize "incentive-based approaches, where feasible" with respect to rate of return regulated utilities. The "underlying principle" in Order No. 9957, where the Commission encouraged innovation that benefited customers by allowing recovery through the Fuel Clause of a utility's costs because they resulted in significant fuel savings to customers, is fully consistent with the Commission's current Mission Statement. Further, as I have explained in my testimony, the Commission has consistently followed this "underlying principle" in Order No 14546 and its subsequent rulings applying that Order by rewarding utility efforts to generate fuel savings for ratepayers through cost recovery for those efforts under the Fuel Clause.

Q. Should the Commission grant PEF's request for recovery of the CR3 power uprate costs, transmission-related project costs, and POD-related project costs through the Fuel Clause?

A. Yes. The costs of the CR3 power uprate and potential transmission and POD modifications for the project including a return on average investment at our current weighted average cost of capital as well as applicable taxes, clearly qualify for recovery through the Fuel Clause under the policy set forth in Orders Nos. 9957 and

14546 and their progeny. For the estimated $381.8 million cost of the CR3 power uprate transmission, and POD modifications for the project, PEF's customers will receive over $2.6 billion in fuel savings and the State and PEF's customers will receive added fuel diversity from the additional, low cost, base load nuclear power.

Q. Does this conclude your testimony?

A. Yes, it does.

BY MR. WALLS:

Q. Mr. Portuondo, do you have a summary of your prefiled direct testimony?

A. Yes, I do.

Q. Will you please summarize your amended prefiled direct testimony for the Commission?

A. Certainly. Good afternoon, Commissioners. The CR3 uprate project that is here before you today is an innovative project that will provide customers with approximately $2.6 billion worth of savings over the extended life of this unit. The power uprate project achieves these savings by displacing fossil fuel generation with additional nuclear generation. The project as a result also enhances fuel diversity for the company's system consistent with the objectives set forth in the 2006 Energy Act passed by the Florida Legislature.

This Commission established Order 14546 in 1985. The costs that can be recovered through the fuel clause under this order, in Item 10 of Order 14546, utilities can recover costs that, one, were not recognized or anticipated in the cost levels used during the utility's current base rates; number two, generate fuel savings for customers. PEF meets each part of this Commission test with this uprate project.

The CR3 uprate project costs were not recognized or anticipated in the cost levels used in FPC's current base rates. The MRFs for PEF's last rate case in 2005 did not include these costs. Second, the uprate project will generate fuel savings that exceed the project costs, providing savings to customers. The uprate project therefore satisfies the tests of the fuel clause recovery set out in Item 10 of Order 14546.

The company's request for recovery of the uprate costs through the fuel clause is consistent with the Commission's orders applying the tests in Item 10 over the last 20 years. The example -- for example, the Commission approved the FP&L request for cost recovery through the fuel clause for capital costs incurred for the thermal power uprate of FP&L's nuclear unit. The Commission pointed out that the fuel savings from FP&L's uprate results from the replacement of higher cost fossil fuel with nuclear generation.

This is exactly what the CR3 uprate project does. The difference is that PEF will incur more costs for more megawatts of cost-efficient nuclear fuel, nuclear generation, resulting in greater fuel savings. PEF requests similar treatment for the uprate as this Commission has awarded on other projects identified under Item 10.

The Commission recognizes that the utility must first take care of what they currently have to meet customer -- to meet customers' present energy needs in the most cost-efficient manner. As a result, the Commission has sought to encourage the development of innovative utility projects and programs that generate fuel savings for customers. This policy on Item 10, Order 14546, accomplishes that.

The policy works. PEF has converted several combustion turbines to dual fuel capability to achieve fuel savings and obtain -- and has obtained cost recovery through the fuel clause for these capital costs under this policy. FP&L, as I noted before, obtained cost recovery through the fuel clause for its power uprate at its nuclear unit under this policy. Similarly, we identified and pursued the CR3 uprate because we were aware of this policy and the Commission's consistent application of the policy over the last 20 years.

The CR3 uprate project -- the CR3 uprate is a project that benefits customers under this Commission's policy. We request that the Commission apply its policy here and approve our request for recovery of the CR3 uprate project through the fuel clause.

Thank you.

MR. WALLS: We tender Mr. Portuondo for cross.
CHAIRMAN EDGAR: Thank you. Mr. McGlothlin.

CROSS-EXAMINATION

BY MR. McGLOTHLIN:

Q. Mr. Portuondo, I'll begin with a question that I also posed to Mr. Waters. Would you agree, sir, that the accuracy of the calculation of fuel savings that has been offered in support for the proposal depends in a direct way on the accuracy of the estimates of the costs of the project?

A. Yes, absolutely. If the costs come in less than projected, the savings, the net savings that will result will be greater than have been projected.

Q. And is there another side of that coin?

A. Absolutely. If the costs are higher, the savings will be less. But we're talking about $2.6 billion worth of savings. I've got a tremendous amount of headroom there.

Q. That's $2.6 billion nominal; correct?

A. That's correct.

Q. Would you agree that the costs of the project are preliminary estimates at this point?

A. They are. Some of them are more preliminary than others, but that's really irrelevant, because the Commission will have on an annual basis the opportunity to review the actual costs incurred and analyze the savings achieved in every single fuel hearing until full recovery has occurred.

Q. But in terms of the ability of the Commission to get its arms around the accuracy of the numbers and in terms of describing where the company is today, these are very preliminary numbers, are they not?

A. Yes. This is a projection of what we believe the costs will be. And what is before the Commission is a request that they review this project under Item 10 of their Commission Order 14546 and allow us the opportunity to show the actual achieved savings, net savings resulting from this project. We believe they're there. We have reason to believe they're very significant.

And I think that's what Item 10 of the Commission's order was attempting to encourage the utility to bring these projects. Even though the costs are estimates, there will be sufficient time for the Commission, the staff, and intervenors to review the final costs and determine whether we have truly achieved net savings for the customer.

Q. In the same refueling outage in which the company intends to install a portion of the uprate project, Progress Energy also intends to replace the steam generator at Crystal River 3; correct?

A. That is correct.

Q. And is it true that the initial project estimate for the replacement of the steam generator was $170 million?

A. I remember you pointing me to something in the MRFs in our deposition, but I'm not 100 percent. I think we went over this in my deposition. I would have to be pointed to the 170.

Q. Okay. If you want to check, it's in your own Schedule JP-1, page 1. If you'll accept it subject to check, you indicate there that the initial project construction cost was on the order of 170 to $172 million.

A. That's correct. Column D shows $172 million was the estimate of the project.

Q. And is it true that the current estimate has increased to $239 million?

A. Well, that is the -- that's correct. Column E indicates that the total cost to complete is 230 million.

Q. Would you accept, subject to check, that's on the order of about a 40 percent increase over the original estimate?

A. That's fine. I don't see the relevance, but that's fine.

Q. Is it true, Mr. Portuondo, that currently Progress Energy Florida is before the Commission in Docket No. 0700 -- I'm sorry, 070290 with its request for permission to collect from customers the costs of Hines 4 that exceeded its original estimate?

A. That is correct. I think as part of the settlement, we had to present the final costs for Hines 4. They have exceeded the bid rules cap, and we have presented evidence in support of the prudency of those costs.

Q. Now, under the company's proposal under which fuel savings realized annually are applied to the costs of the project, to the extent that the company understates the -- let me strike that. To the extent that the costs of the project exceed the current estimates, that would have the effect of pushing out in time the point at which the project is paid for; is that correct?

A. Correct, fully paid for, yes. I guess I would add, the opposite is also true. I think you already knew that. It will shorten the recovery period if the costs are less.

Q. Is it true that the analysis of project costs that became a part of the calculation of fuel savings did not take into account the possible impact of the project on decommissioning expense?

A. We did not, no.

Q. And is it true that in your view, it is possible that Phase 3 of the project would increase the decommissioning expense?

A. It's hard to tell. It might, may not. A full study needs to be undertaken at the appropriate time. The current decommissioning expense is zero in base rates.

Q. Do you have available to you, Mr. Portuondo, the answer to Public Counsel's Interrogatory 19 that you sponsored?

A. This is OPC's first request?

Q. Second set of interrogatories, Number 19.

A. I do. Hold on. Yes, I do.

Q. 19(a) posed this question: Describe fully the manner in which each phase of the CR3 uprate project will affect the mode and/or costs of the decommissioning of Crystal River Unit 3. Would you read your answer?

A. "FPC has not evaluated the impact of the uprate on decommissioning, but would not" -- I'm sorry. "PEF has not evaluated the impact of the uprate project on decommissioning, but would not expect to see an increase caused by Phase 1 or Phase 2. Phase 3 could result in an increase in decommissioning due to the additional point of discharge cooling solution."

And again, in retrospect, I got carried away. Point of discharge would actually fall under fossil dismantlement to some degree. But it would be split, because you have one cooling tower that is allocated to more than one solution.

The impact there, again, as I stated, could be an impact to decommissioning, but without having done a decommissioning site-specific study, I don't know what that impact might be.

Q. Is it true that in the course of the uprate project, certain existing plant facilities will be retired?

A. Yes, they would. And the revenue requirements currently in rates for those component parts will be credited against the total costs of the project, to which then the fuel savings will be applied. That is consistent with how Item 10 has been applied in the past and how other capital cost recoveries have been applied in other clauses.

Q. Let me ask you specifically about the undepreciated portion of the existing plant that will be retired when the new plant is installed. Has the undepreciated portion of the investment been attributed to the project as a cost of the project?

A. No. We have not credited the costs with the revenue requirements of those retired facilities at this point to show the largest exposure that we would think of at the time. So the 320 million, or 440 with AFUDC, was trying to establish somewhat of an upper bound for the costs so that we could test to make sure that we were achieving the fuel savings sufficient to cover the costs.

But we would, as a matter of practice, in the annual fuel filings, once we know which assets will get retired -- we'll have to go to the plant records and find out what was the level of return in current base rates. And we would credit the costs for that year with that year's revenue requirements before we applied the savings to recover the balance.

Q. I want to see if I understood your answer. It was a long answer. It appears to me that but for the uprate project, the existing plant would continue to be depreciated and paid for by base rates; is that correct?

A. The existing plant is in base rates, and revenue requirements are received in base rates.

Q. As a result of the uprate project, some of those plant items will be retired before they have been completely depreciated; correct?

A. That is correct.

Q. And but for the uprate project, those original items of plant would remain in rate base, and the costs would be recovered through depreciation expense over time; correct?

A. Could you say that one more time?

Q. Yes. But for the uprate project, those original plant items would remain in service and would also remain in rate base, and the cost of the items would be recovered through depreciation expense over time through base rates?

A. Correct, just like any other component of any other power plant currently in base rates.

Q. Now, here comes the uprate project. New plant goes in, and the earlier plant, some of it is retired before it has been fully depreciated.

A. Correct.

Q. Is it not true that those undepreciated costs, to the extent the company intends to recover them, are costs of the uprate project?

A. Technically, I guess I -- I don't agree. I guess what I stated previously is, since those costs or the revenue requirements associated with those costs that are being retired are in base rates, and we don't wish to double recover -- I mean, that's kind of primary test number one. The revenue requirements associated with those assets that will be retired for which we're already collecting become a credit against the new costs, the replacement assets, to make sure that we're only recovering on the incremental costs attributable to the uprate project.

Q. And those revenue requirements would include the depreciation expense associated with the newly retired items?

A. Yes, it would.

Q. Okay. Is it true that the plant items associated with the measurement uncertainty recapture phase are expected to last through the end of the license agreement, license agreement through the year 2036?

A. Yes.

Q. Is it true that Progress Energy Florida proposes to recover the entire MUR investment in a single year?

A. Yes. We believe that the savings from that first year are more than enough to recover the costs.

Q. Would you agree, sir, that this proposal to recover the investment in the MUR in a single year appears neither in the company's petition nor in any of the witnesses' prefiled direct testimony?

A. I think our testimony says that we would recover the costs to the degree of fuel savings. So if the costs in that year are less than the savings, then we would apply the full recovery of those costs in that year.

Q. Now, the other items in Phases 2 and 3, and also the transmission and point of discharge facilities, the company proposes to recover those over a ten-year period; is that correct?

A. That's correct. Our initial calculations indicated that over a ten-year period, there would be sufficient fuel savings to allow the recovery of the costs incurred to achieve those savings.

Q. Would you agree that the ten-year period does not appear either in the company's petition or in any of the company witnesses' direct testimony?

A. Again, I think my testimony addresses to the extent of fuel savings. Ten just happened to be the period that our analysis indicated would be long enough to be able to recover. And again, if the estimate goes up or goes down, that will change. If the cost of fuel for fossil fuel-related items goes up, it would create even greater savings.

Q. When a capital item such as this investment in plant is placed in rate base under the normal fashion, is it true that typically such investment gives rise to deferred taxes under applicable tax law?

A. Yes.

Q. And again, under the normal ratemaking fashion, does the company use those deferred taxes collected from customers before they need to be paid as a source of cost-free capital?

A. It is included as part of the weighted average cost of capital, correct.

Q. Under the company's proposal, is it true that the lives for tax purposes are longer than the amortization period that the company proposes?

A. Yes. Assuming that the ten-year holds true, that would be a correct statement.

Q. As a regulated public utility, Mr. Portuondo, Progress Energy serves 100 percent of the retail customers in its service area, does it not?

A. Yes.

Q. If a new customer applies for service and the company determines that the amount of investment needed to reach that customer is such that the customer's expected revenues don't yield the authorized rate of return, is it true that the company can require the new customer to pay a contribution in aid of construction as a condition of service?

A. I believe the contribution in aid of construction is associated with facilities the customer may request beyond the standard facilities that the company offers. If they want redundant systems or something like that, that's where a contribution -- or undergrounding, if they want underground versus overhead, there would be a contribution in aid of construction.

Q. Do you know whether the concept of CIAC comes into play in other situations, such as an unusually large investment to reach and serve in the usual means?

A. For line extensions?

Q. Yes.

A. Yes.

Q. It's true, is it not, that under regulation in Florida, Progress Energy Florida and other regulated electric utilities can request the Commission to approve a projected test year for purposes of base rate review?

A. That is correct, yes.

Q. And it's true, is it not, that once an electric utility files for a rate base increase, it has the ability to request the Commission to grant an interim increase, and the Commission would act on that within 60 days of the filing?

A. Yes, there's an interim rule. I think it has been around for a long time.

Q. If you know, sir, has the Commission ever timed a decision in a base rate proceeding to coincide with the point in time at which the utility would be called on to recognize significant new costs such that the increase in rates is simultaneous with the increase in costs?

A. I think typically -- I would say that's true. Typically it would probably be initiated by the utility.

Q. But that's possible to do and has been done; isn't that true?

A. Yes. I think that has been around since Order 14546 has been around.

Q. Now, do I understand correctly that in your view, it would be inappropriate to seek to pass the cost of a new power plant through the fuel cost recovery clause?

A. Except through stipulation.

Q. All right.

A. Just kidding. I mean, that's how Hines 2 was in there. But typically, I think I would agree with you. A new power plant which is meant to meet the reserve margin, meet the demand of the state, would not be a fuel clause item. It's being driven by demand.

Q. Well, even if a power plant is also economically justified, it would not be appropriate to pass the cost of a new power plant through the fuel clause, would it?

A. I would say if the economics are such that under Item 10, the savings from its construction are fully funded by those fuel savings, I would say yes, it is appropriate. It's not typically the case, as I was listening to Mr. Waters testify to.

Q. What about a repowering project? Do I understand correctly that you regarded the repowering as something that should be recovered through base rates and not through the fuel clause?

A. Absolutely, if you're referring to Bartow. Bartow's repowering is being driven by a capacity requirement, reserve margin requirement. That was planned for in order to meet that need in the 2009 time frame.

MR. McGLOTHLIN: If I could have a moment in place, I think I can wrap up quickly.

CHAIRMAN EDGAR: Yes, sir.

(Pause.)

MR. McGLOTHLIN: That completes my questioning.

CHAIRMAN EDGAR: Mr. Wright.

MR. WRIGHT: Thank you, Madam Chairman. I just have a couple of questions.

CROSS-EXAMINATION

BY MR. WRIGHT:

Q. Good afternoon, Mr. Portuondo.

A. Good afternoon.

Q. You've been here all day; correct?

A. I have, yes.

Q. And I imagine you were paying attention when I asked Mr. Roderick questions about your cost estimates?

A. Yes.

Q. And I will ask you the same question I asked him. Is Progress willing to bear the risk of cost overruns associated with the uprate project?

A. I would say no.

Q. And will Progress implement the CR3 uprate project if the Public Service Commission does not grant advance approval of cost recovery through the fuel clause?

A. That's above my pay grade. Typically if we follow suit with the way dollars are allocated to Progress Energy, they are prioritized. There's not, you know, an endless amount of capital that we can go out in the marketplace and procure for every single project in every single year. It's just not good business sense. But we would have to simply go back and reprioritize and look at is there sufficient funding to be able to accomplish everything we need during this, you know, ten-year time period that we're talking about. So it's very difficult to say. There's a lot of things that need to be considered.

Q. Would it be a fair characterization of that response that you don't know and you can't commit one way or the other?

A. I cannot commit one way or another.

Q. Thanks. I'm not sure how long you've been around doing this stuff, but do you recall when Crystal River 5 came online?

A. Well, that was way before my time.

Q. Okay. Do you have any knowledge of what the company did with existing capacity that was already on its system when Crystal River 5 came online?

A. No, I really don't.

MR. WRIGHT: Okay. Then I'll not pursue that line. Thank you.

THE WITNESS: You're welcome.

CHAIRMAN EDGAR: Mr. McWhirter.

CROSS-EXAMINATION

BY MR. McWHIRTER:

Q. You probably weren't born when Crystal River 3 came online.

A. I was. I was just a wee lad, but I was here.
Q. Mr. Portuondo, are you familiar with the term "historic rate base" and how it's used in regulation?
A. Historic test year?
Q. Yes.
A. Yes.
Q. Would you explain what that is?
A. The historic test year is a representation of the accumulation of spending that has taken place since the beginning of time and the representation of that through the level of assets and liabilities that the company has at the close of the last set of books for a particular time period.
Q. And that was the policy of this Commission years ago, that when had you a rate case, you would use a historic test year; is that correct?
A. That's correct.
Q. And what is a year-end rate base?
A. Year-end versus 13-month average? Is that where you're -- year-end would indicate to me it would be the exact level of investment as of the year-end versus an alternative that's used currently, a 13-month average rate base, which is again just that. It's an average over the last 13 months.
Q. And a year-end rate base, this Commission used

an historic year-end rate base years ago, and the Supreme Court overturned that in the General Telephone case. Do you recall that?

A. That I do not.

Q. You do not?

A. I do not.

Q. And then you just mentioned a 13-month average rate base. Is that an historic test year, or is it a projected test year?

A. It's used for both currently.

Q. When do they use the historic 13-month average?

A. Well, since 1992, which was the last time we -- well, I would say the last time -- the very first time I was involved in a base rate proceeding was in the '92 rate case, and I know that for both the historic period and the projected period, we were using a 13-month average rate base.

Q. Now, in this case, as I understand it, you are seeking to get Commission approval in advance of expenditures that will be made five years from now?

A. No, sir, we are not.

Q. But you're seeking a policy that suggests that whatever the expenditure has been, it will be approved and recovered through cost recovery clause?

A. No, sir, I'm not.

Q. What is it precisely -- with respect to expenditures that occur in the years 2010 and 2011, what are you asking the Commission to do about those expenditures at this point in time?

A. I'm asking the Commission to approve this project as a legitimate, recoverable cost through the fuel clause. And if they approve that, in the year that the particular asset installed goes commercial and begins to create fuel savings, the reviewed, actual costs will then be recovered to the extent of fuel savings.

Q. And the number $381 million has been used, but that's not the number that you will ask to recover through the fuel clause, is it?

A. No. I mean, the other number that has been presented is the equivalent with AFUDC. And again, depending on how the expenditures are actually made, the level of AFUDC is going to differ. So again, it's an approximation.

Q. And that number on your most recent analysis was what? $428 million?

A. No. I think it was 440-something.

Q. $440 million?

A. Is the total with AFUDC.

Q. And that is your anticipated cost as of the year 2011?

A. That would be correct.

Q. And if the cost comes in more than that, irrespective of the return that you're then earning on base rates, you will seek to have the full cost recovered through the cost recovery clause?

A. Yes, sir.

Q. And that will be true even if at that point in time through base rates you are earning in excess of your authorized return?

A. Absolutely. The Commission would throughout this entire process be monitoring base rates, as they do, and if base rates get out of line, I'm sure I'll be up here explaining why. So I think the checks and balances are in place.

Q. So what you're saying is it's a possibility if you're earning in excess of your authorized return that the Commission might demand that you come in and file a rate case in the base rate proceedings? Is that what you're saying?

A. Absolutely.

Q. And how long does it take to process a case of that nature?

A. Eight months.

Q. So if the Commission determines through a surveillance report that you're overearning, it would direct you to make minimum filing requirements. And the eight months would run from the date that the surveillance report came in or from the date you got around to filing the minimum filing requirements?

A. No. I think the process, if I recall, would hold revenues subject to refund from the date of the surveillance that gave rise to the question in the Commission's mind of whether the company was over earnings, was overearning. And then the eight-month clock would actually start once the MRFs are filed and have been approved by the Commission.

Q. I guess they could enter an order and tell you to hold your rates subject to refund, and they could go back to the date that they filed their order. Is that the way it works?

A. Yes. What I'm recalling is, in the 2001 rate case, we had filed, you know, our projected surveillance report, which comes in -- I think it's due March 15th typically, and that was the demarcation point for revenues subject to refund.

Q. And that was because at that point in time, your earnings were exceeding the authorized return?

A. Actually, not at that point, but it was a projection for that coming year, and we were projected to be over our then-authorized ceiling. And that's why they said, "Well, let's look at everything." And also, it was around the time of the merger as well.

Q. And in fact, the savings came about as a result of the merger, and the end result was a settlement in which you reduced your base rates by $125 million?

A. That is correct.

Q. Now, also part of that agreement was that Hines No. 2 would go into the fuel clause at that time, and you could recover not your operating expenses, but your return and your depreciation on Hines 2 through the fuel clause; is that correct?

A. That is correct.

Q. But there was a caveat in that settlement agreement, and that was that you wouldn't collect it if the fuel savings did not materialize.

A. I do recall that.

Q. So if the fuel savings did not come about, you would not be able to recover a return on your investment except to the extent that there were savings, and you would not be able to recover a depreciation charge which would enable you to recover your investment; is that correct?

A. That is correct. The clause in that settlement provided for the cumulative -- over the cumulative period of the settlement, if the savings did not exceed the costs, then we would be limited to the level of savings.

Q. Now, you're not proposing that with respect to the CR3 uprate. In this case, you want to recover your costs irrespective of the fact that the savings materialize in the current year. For instance, in 2012, the capital costs and your return will be greater than the savings for that year, and that goes on for a number of years; is that correct?

A. I can't picture the schedule, but we would be recovering only to the level of savings. Any cost for that year that was not covered by the savings would flow into the next year and would be again calculated to see if the savings were sufficient to cover the costs.

Q. I see. And would you -- if you didn't recover the costs, would they -- would you get a interest payment on those costs that you didn't recover?

A. Well, we're earning the weighted average cost of capital, yes.

Q. So you would apply an AFUDC rate to the cost that was not recovered?

A. The weighted average cost of capital is slightly different than the AFUDC, but --

Q. Now, in this case, you have proffered an 11.75 percent after-tax return on the equity component of your investment; is that correct?

A. That is correct. That's the last authorized.

Q. And you haven't presented any testimony on that. You're just using some other vehicle for determining that an 11.75 percent return on equity is appropriate at this time?

A. It's the authorized cost of equity capital that the Commission last approved for our company.

Q. And that's the same that it approved in 2001 and reapproved in -- I mean in 1992 and then approved again in the 2001 and 2005 rate cases?

A. They approved this one in the 2005 rate case.

Q. What had it been before 2005?

A. 12 percent.

Q. And that's after taxes?

A. Correct. No, that's pre-tax. The 12 percent is pre-tax.

Q. It's 12 percent --

A. No, I'm sorry.

Q. It's after-tax?

A. It's after-tax, yes. It's been a long day.

Q. Now, Hines 2 will go into base rates in

January of this year? Is that what you project?

A. Hines 2?

Q. Yes, sir.

A. No, Hines 2 will go into rate base per the settlement in -- late November, early December, I believe is the in-service of Hines 4, and we agreed to move it in at the same time we moved in Hines 4.

Q. Have you done a preliminary study as to the amount of additional revenue you will collect from your customers as a result of this base rate increase?

A. For Hines 2 and Hines 4?

Q. Yes, sir.

A. I think it was part of the filing in the Hines 4 proceeding. We showed the Hines 4 revenue requirements. The Hines 2 revenue requirements are currently coming through the fuel clause, so that's readily available. I just don't have those numbers here today with me.

Q. Would it be fair to estimate that that cost would be in the range of a $90 million base rate increase when Hines 2 and Hines 4 come into base rates?

A. Well, yes, the sum of the two, but fuel would go down by the Hines 2 portion of the revenue requirements.

Q. And your current fuel cost factor that was established November of last year or December of last year for the year 2007 was -- what was that fuel cost?

A. For Hines 2?

Q. Yes, sir.

A. Don't hold me to this, but maybe like 36 --

Q. No, your total fuel cost that you collected.

A. Oh, my total fuel cost.

Q. It's in the range of $2.5 billion, isn't it?

A. Yes, yes.

Q. And you say that that will go down by $90 million, but --

A. No.

Q. Is that right?

A. No, that's not right. It won't go down by the whole 90. It will only go down by the CR2 portion, because that's what's in fuel today, the CR2 -- pardon me. The Hines 2. Forgive me. The Hines 2 is what's in fuel today. It will move out of fuel and go into base rates.

Q. Okay. And that's about $40 million a year?

A. Give or take.

Q. All right, sir. Now, Mr. Waters has put into evidence an exhibit that shows your anticipated fuel costs, excluding what you're asking for in this uprate case, will be $3.1 billion in 2008. Is that what you're going to come in and ask for in September and plan to start collecting in January?

A. I don't have those numbers yet. I mean, we file testimony in September. I don't have those numbers finalized yet.

Q. Are you familiar with that exhibit in Mr. Waters' testimony that the fuel costs that he's basing his savings on are going to be $3.1 billion, and that's $600 million greater than the current fuel costs including Hines 2?

A. I am familiar with his filing. I guess the reason I say that I don't know that to be the final number is because to do that, you have to apply the over- or underrecovery for the current year to get to kind of your net request for 2008.

Q. Are you familiar with the fuel cost information you filed for the month of June 2007?

A. I have not memorized it, no, sir.

Q. Would it be fair to say that you're currently projecting that your actual fuel costs are some $140 million less than you estimated they would be in December?

A. That I do, yes. In fact, I think our reprojection was filed here recently, and I think maybe 160 is what we're planning for year-end.

Q. Would you agree with me that if you can't project fuel costs any closer than that for a six-month period, it's going to be somewhat difficult to project fuel costs and savings for a 30-year period?

A. I don't disagree. I mean, we're at the mercy of changes in the market. The beauty of the Commission's policy is that they will have an opportunity to look at actual fuel costs and measure those savings to the actual costs incurred to achieve the savings from the uprate. So, you know, the issue around forecasting is really moot.

Q. Well, let's look at the year 2012. In the year 2012, the carrying costs on your investment in this plant is going to be somewhere around $100 million, but the fuel savings from the commercial operation will be less than that. Does that mean that customers will get some kind of refund, or does it just mean that you'll collect that later plus interest?

A. I will collect the difference in the following year.

Q. And that will carry interest at the -- guaranteed interest at your AFUDC rate, which is somewhat more than 8 percent?

A. Correct.

Q. And that's after taxes?

A. Correct. And I guess I would add that that is very much consistent with how all of our other capital projects have been recovered for the gas conversion. This petition was modeled exactly to comply with what we believed was the Commission's policy.

Q. What is this Commission's policy with respect to fuel underrecoveries and overrecoveries? What interest has it applied to the guaranteed recovery?

A. This Commission applies the commercial paper rate for fuel. The reason behind that is because fuel is procured utilizing commercial paper, unlike this project that will be funded with all sources of capital.

Q. You go back in history to when you were just getting out of high school, and Florida Power & Light did the coal-by-wire. Do you remember that part of your testimony?

A. Uh-huh.

Q. And they spent a billion dollars to bring coal that they purchased from the Scherer plant in Georgia down to the State of Florida, and they set aside the oil costs. And you're likening that concept to this present case?

A. Yes. I think the principle is the same, that those efforts undertaken by Power & Light were designed to try and reduce fuel costs, just like this project is attempting to do, is to help customers reduce fuel costs.

Q. And something unusual happened in that case, however, because natural gas became deregulated, and the price fell from $6 to $1.50, and the fuel savings did not materialize. As a consequence, the customers through their oil backout charge paid for this plant, and the fuel savings were nonexistent. Is that -- do you recall that?

A. Uh-huh. Again, that's a little bit -- that's one of the differences between that and how the Commission has applied this policy, where you'll recover to the extent you're demonstrating fuel savings on a cumulative basis. If you're not demonstrating the fuel savings, then you will have to wait on the recovery.

Q. One final question, Mr. Portuondo. You refer to Item 10 in Order No. 14546. And as I understand your testimony, there are only two criteria that are necessary for an investment to go into the fuel clause. The first criteria is that it wasn't anticipated in the last rate case, and the second criteria is that the investment which, if expended, will result in fuel savings to customers. Are those the only two criteria that apply in order to put an investment that saves fuel in the fuel clause?

A. Yes, sir.

Q. A capital investment?

A. Yes, sir.

Q. And so if you built a new base load plant, under that hypothesis, wouldn't it be fair to say that using those criteria, that base load plant would -- because it's going to save fuel costs on combustion turbines and so forth, should go through the fuel clause rather than through base rates?

A. No, sir, because it would not meet the second test. It would not produce fuel savings to the level that would recover the investment in that facility.

Q. I'm not sure I followed you. Would you mind saying that again in fourth grade language?

A. The second prong of the test is that the fuel savings achieved from the project are greater than the costs incurred to achieve those savings, and I don't think that that test would be met.

Q. I see.

A. And in fact, I believe that was Mr. Waters' testimony.

Q. The investment in that plant and the carrying costs on it would -- when they're added together wouldn't add up to the fuel savings? I mean, it would be greater than the fuel savings?

A. It would be greater.

Q. The fuel plus the return on the capital costs. What did Item 10 mean when it said recovery of such costs should be made on a case-by-case basis after Commission approval?

A. What I believe was meant by that phrase and how I've conducted myself in accordance with that phrase is that I am not permitted to charge the fuel clause for any item other than 1 through 9 without first getting the Commission's approval. One through 9 are kind of, okay, we know what those are, transportation, commodity; go ahead and charge those, and our auditors will review the prudency of the costs.

For Item 10, the Commission wants the company to come before it and show, you know, what's the projected cost, what are the projected savings, you know, what's the project. They want to know more about these types of efforts than simply, you know, go ahead and charge it and come to us later.

Q. But if you present credible evidence that -- your estimate of fuel savings over a 30-year period, the net present value of that, it's your opinion that it's mandatory for the Commission to approve it under the basis of that order that was issued back in 1985?

A. I believe so. I believe that's the intent of the order. That's the -- as I see it, that's the law under which I'm working today. That's the regulatory guidance that I've received from the Commission. And I believe that's what we're doing here today, is showing the credible evidence that we have a project that will create the potential for $2.6 billion worth of fuel savings at a cost of around 440-some million dollars, plus or minus.

Q. That's not required by statute, and it's not required by rule, but it's required by a 1985 order?

A. That's correct.

Q. And in your opinion, the Commission is obligated to follow that order?

A. I know I'm obligated to follow that order.

Q. Very good. Are you familiar with Financial Accounting Standard 133 dealing with derivatives?

A. I sure am.

Q. And in my confused mind, what that says is when you're financially reporting the value of a derivative such as a hedge contract, you put in your balance sheet the value of that contract if it's going to provide earnings in the future; is that right?

A. You have to recognize the fair market value and then recognize it through earnings over the period of the hedge.

Q. And as I recall it, Enron got into a lot of trouble because they were marking to market contracts that were maturing 10, 12 years into the future, so their earnings were not properly projected. Is that your -- do you know anything about that?

A. No.

Q. Would it be fair to say that in this case, by taking a net present value of savings that occur up to 30 years into the future, you're marking those future savings to market to justify this cost increase to customers?

A. No. I disagree. The net present value calculation, as was discussed with Mr. Waters, is simply a recognition of the time value of money over the period of time. I don't characterize it that way.

MR. McWHIRTER: Okay. I tender the witness.

CHAIRMAN EDGAR: Mr. Brew.

CROSS-EXAMINATION

BY MR. BREW:

Q. Good afternoon, Mr. Portuondo.

A. Good afternoon.

Q. I have just a quick question about limits, if any, on your position. Let's assume in 2012 that the project hasn't exactly gone as planned, and the core upgrades to the steam generators aren't running, and the unit is down for the year. You don't have fuel savings. In fact, you've got substantially increased fuel costs. Do I understand correctly that under your proposal, the company would defer what it would have amortized in that year from its schedule, plus carrying charges, and customers simply pay the higher fuel costs and then carry on the next year? Is that right?

A. Yes. I mean, the event that gave rise to those replacement costs more than likely is going to get the scrutiny of this Commission in the fuel proceeding, and they will through that process adjudicate the prudency of those replacement costs and whether they will be recovered or not.

Q. Well, let's leave the prudency of the fuel costs aside for the moment. But in terms of the costs of the uprate project, there are no fuel savings for that year from the project, so you would simply defer what you would have amortized per your schedule, plus carrying charges, to be collected or offset later from future fuel savings; right?

A. Correct. The event was not driven by the uprate.

Q. Okay. And if, as described in your testimony, you weren't shut down altogether, but either costs were higher or fuel savings were less, and there was some underrecovery, the company will absorb all of the fuel savings for the year and then carry any balance forward; is that right?

A. You're going to have to restate that one.

Q. Page 25 of your testimony. You state it better than I do. Lines -- this is of your rebuttal. Not -- yes, your rebuttal, page 25 --

CHAIRMAN EDGAR: Let me break in. Just for clarity, we are not on rebuttal. Mr. Portuondo is going to join us again at the end of the proceeding, so you may want to hold that question until we get to that point.

MR. BREW: I can do the question --

CHAIRMAN EDGAR: Differently?

MR. BREW: Differently.

CHAIRMAN EDGAR: Okay.

BY MR. BREW:

Q. If the fuel savings were 80 million for the year and your amortization was going to be 100 million, under this proposal, you would absorb the entire fuel savings and carry 20 million plus carrying charges forward to the next year; right?

A. Correct.

Q. Okay. Is the company's proposal the same if the cost of the project turns out to be 800 million instead of 420?

A. Wow. That's a good question.

Q. I'm hoping for a good answer.

A. Yeah, me too. You know, that's a pretty significant increase. I think we would have to really assess what drove us there. We're pretty comfortable today with the power plant portion. As Mr. Roderick has testified to, he's got his fixed price contracts. There's protection. We're getting our hands around the POD and the transmission. I guess today, at this moment, I don't know that I could answer it.

Q. Let's take that a step further. On the transmission, you're doing studies now, but you don't have a firm estimate, proposal, or budget; is that right?

A. No, we do not. We won't have that until later in the fourth quarter.

Q. And the same goes for the POD?

A. The same for the POD, yes.

Q. Okay. According to Mr. Roderick's testimony, he's looking at pinch point analysis for equipment changes and upgrades that they may need to do that is still evolving; is that right?

A. Correct.

Q. So at this point, there's a lot of room for maneuvering on where the final costs are going to come out; would you agree?

A. To an extent. In the transmission and the POD, I think there's wiggle room there. The power block, Mr. Roderick appears pretty comfortable with those numbers. And again, we try to -- as he indicated, we try to give ourselves that upper bound with what we put in there for transmission and POD. Hopefully we've done the right thing.

Q. I guess I have one question two different ways. One is, is there a point at which you could tell the Commission when you would be willing to commit to a firm price estimate for the project?

A. We'll provide it to the Commission as soon as we have it, absolutely.

Q. No, but is that something that can be decided by the end of the year? When could we expect to see a firm commitment as to what the project should cost?

A. Standing here today, I can't tell you when the POD portion of the analysis is going to be completed. I'm expecting the transmission here before the end of this year, but the POD may take a little longer, until next year. So I can't give you a precise date. But it will be -- the minute we have it finalized, the Commission will have it finalized.

Q. Okay. Once you have it finalized, would you be willing to commit to that estimate for rate recovery purposes?

A. I think that was Mr. Wright's question, and I don't think I can do that.

Q. So no matter what the level of final cost would be in terms of overruns, your position doesn't change?

A. Well, as I mentioned before, the Commission in every fuel hearing will have the opportunity to review how we managed those contracts. And to the extent that we have done something incorrectly or imprudent, that would be the opportunity for the Commission to say, "No, no. Stop. This portion is not recoverable. It didn't comply with the application of the contract," or whatever, like they would do for any other contract that we enter into. So if it's found imprudent or inappropriate, we would not recover those through the fuel clause.

Q. Only in a separate docket, not in limits or conditions in this case?

A. I don't understand the question.

Q. In the Commission's order in this case, you're proposing there to be no limits as to how high the costs could be in terms of recovery through the fuel clause?

A. The only thing that I'm asking this Commission to vote on associated with this petition is that this project is recoverable through the fuel clause. The prudency of the costs incurred will be adjudicated by them at every fuel hearing during the recovery period.

MR. BREW: Okay. That's all I have. Thank you.

CHAIRMAN EDGAR: Mr. Twomey.

MR. TWOMEY: Yes, ma'am. Thank you.

CROSS-EXAMINATION

BY MR. TWOMEY:

Q. Do you have a copy of Order 14546?

A. I do. Give me a moment. Yes.

Q. Okay. As reflected on the first page of that order, you recognize then that the order was published on July 8th of 1985, a little over 22 years ago; correct?

A. Correct.

Q. Now, you've discussed in your various testimony, I think, the fact that there have been five relevant applications of Item 10 of the order by the Commission since -- in the 22 intervening years; correct?

A. Correct.

Q. Now, the prior applications, I'm looking at a table that Mr. Walls passed out, but maybe it's intended for your rebuttal, but it's convenient for me if you have it. I'm not sure if the Commissioners have it or not. But I would like to refer you to it just because it has the dates and the numbers there. Do you have it?

A. I do.

Q. Thank you, sir. Looking at the five prior applications of Item 10 of that order, it strikes me that the middle three, if you will, there for your predecessor company, Florida Power Corporation, averaged about $2.5 million. Do you see the 2.6, 2.5, 2.45 million projects, on the project costs?

A. Yes. The 7.5 is ours as well.

Q. Yes, sir. But just referring to those three that are in the 2.5 million range, I pulled out my phone that wasn't supposed to ring and used the calculator function of it, and it struck me that those projects -- that your project at $381 million that's being considered in this instant case is roughly 152 times larger than the projects averaging 2.5 million. Would you agree with that subject to check?

A. It's very large compared to those projects, yes.

Q. Right. And then I looked at your other project in the second row of 7.5 million project cost and used the old trusty calculator, and it appeared to be 1/51 the size of this current project. Does that sound about right to you, that is to say, the current project that we're considering here is 51 times larger than the 7.5 million project?

A. That's correct.

Q. Okay.

A. You could do that same calculation on the savings as well. It's quite significant.

Q. I suppose you could.

A. Yes.

Q. Maybe that's rebuttal. I'm not sure.

And then I looked at the Florida Power & Light Turkey Point 3 and 4 project, and it was $10 million, as reflected in that third row, the project cost column. And your current project is 38 times larger than the FP&L project if my math is correct; right?

A. Yes, it is.

Q. Now, going to the -- I'm leery of doing this now since you brought it up, but looking at the projected ratio of savings to costs over the recovery period, your current project considered here is greater than two of those other five Item 10 applications, but less than three of them; is that correct?

A. Say that again.

Q. Well, if I understand your numbers correctly in that table, you're projecting that the ratio of savings to costs over the recovery period for the instant project for $381 million is 2.7 times; correct?

A. Oh, yes, yes.

Q. Okay. And so my question is, looking at the other five previous applications, the 2.7 is a greater ratio -- and the greater the ratio the better; right?

A. Yes.

Q. Is a greater ratio than the 1.3 immediately above it, and as well, it's a greater ratio than the 1.9 ratio for FP&L's project; correct?

A. That's correct. I just didn't hear you.

Q. Okay. I'm sorry. And then just to finish the point, it is substantially less than 8.8 times, 6.2, and then it's just a little bit less than the 2.9 times; correct?

A. That's correct.

Q. Okay. Now, I would like to refer you back to Order 14546, which I believe was in -- I don't know if this is your composite exhibit or the staff's. I'm not sure. I think it's staff's. Anyway, it's Item 6 of one of the composite exhibits. In any event, I wanted to ask you, would you please read just the first sentence of that order following the title "Background"?

A. Sure. "As a result of issues raised by staff in the February 1985 fuel adjustment hearing, this docket was created to consider the proper means of recovery of fuel-related expenses."

Q. I'm sorry. Did you just drop a word?

A. I'm sorry. Fossil fuel-related expenses.

Q. Fossil fuel-related expenses.

A. That's correct.

Q. Now, I was just curious --

CHAIRMAN EDGAR: Mr. Twomey, I'm sorry. I apologize for interrupting, but we've had a couple, and I think it would be time for about a 10-minute stretch. So I would like to take a break, and then we'll come back and pick up right where you are.

MR. TWOMEY: Of course.

CHAIRMAN EDGAR: Okay. Thank you very much. We will come back, Commissioners, in about 10 minutes.

(Short recess.)

CHAIRMAN EDGAR: Okay. We are back on the record. Thank you all.

Mr. Twomey, before we go back to your questioning, you had passed out, or somebody had passed out this chart shortly before we took a break, and I thought that you said that it was in one of the composite exhibits, but I could not find it.

MR. TWOMEY: I apologize. I was confused in my statement. No, the exhibit is the company's. It's Mr. Walls', and I think he planned to use it during rebuttal; correct?

MR. WALLS: That's correct. I had actually planned to use it in redirect, because staff had put in a similar exhibit. And we were just adding some numbers to what staff had done, and then Mr. Twomey went ahead and asked questions about it, which I'm fine with.

CHAIRMAN EDGAR: Okay. Again, I just wasn't sure what it was.

MR. TWOMEY: What I referred to as being in the staff composite was the order that we're speaking to. And I would be happy if you want to number it --

CHAIRMAN EDGAR: 14546.

MR. TWOMEY: -- now, or however you want to --

CHAIRMAN EDGAR: Okay. Why don't we go ahead and do that if that works, Ms. Helton. Okay. Why don't we go ahead and number it and label it, and that help me keep track and hopefully will help with the record as well. So this would be Number 28. Mr. Twomey, can you give me a title?

MR. TWOMEY: Well, I think "Prior Application of Item 10 Under Order No. 14546" was the title.

CHAIRMAN EDGAR: All right. Then we will so label and mark as 28. Thank you.

(Exhibit 28 was marked for identification.)

MR. TWOMEY: I don't think it makes any difference, but really, it's a company witness -- I mean a company exhibit, is what I'm saying.

Okay. I can start again?

CHAIRMAN EDGAR: Yes, sir.

MR. TWOMEY: Thank you.

BY MR. TWOMEY:

Q. Okay. I think when we left off, you had in the reading of the first sentence dropped the word "fossil", but then found it again; is that correct?

A. Yes.

Q. Thank you. And I was curious about that, because I think you didn't use the word "fossil" in the summary of your testimony either when you discussed the two factors that are required for the application of Item 10; is that correct?

A. I probably did not.

Q. Now, is that because despite the language of this order, the Commission on one occasion has used the item with respect to a nuclear power plant?

A. No, sir. I think what we are saving is fossil fuel-related costs. To achieve those savings, you're having to install capital costs. As you can see from

Exhibit 28, in every single application of Item 10, what the Commission has authorized recovery of has been capital costs.

Q. Well, perhaps. But you don't deny that that first sentence says, that is, the first sentence of Order 14546, "to consider the proper means of recovery of fossil fuel-related expenses"?

A. Correct. I don't disagree with you at all. I think the premise of what gave rise to this order was getting clarity around the items that are recoverable in the fuel clause, which Item 1 through 10 are fossil fuel-related costs, or Item 1 through 9, I should say. Item 10 was to address savings of fossil fuel-related costs.

Q. Well, you recognize the distinction, do you not, between an expense and a return on investment?

A. Oh, I do.

Q. Okay. Now, let me ask you to turn to page 4 of that same order, please. And I don't want to belabor this, but let me ask you to briefly read, just Item 10 in its entirety, please.

A. "Fossil fuel-related costs normally recovered through base rates but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers. Recovery of such costs should be made on a case-by-case basis after Commission approval."

Q. Okay. Again, the reference, am I correct, of course, in fossil fuel-related costs; right?

A. That's correct.

Q. Now, the Commission used an illustration of what they were talking about on the previous page, did they not, with reference to Item 10?

A. Yes, they did.

Q. In fact, if we turn to page 3, let me read part of it. We can trade off here a little bit. Okay. The first full paragraph in the rightmost column of page 3 says, "In addition to stipulating to the foregoing applications of policy, the parties also recommended to the Commission that the policy it adopts be flexible enough to allow recovery through fuel adjustment clauses of expenses normally recovered through base rates when utilities are in a position to take advantage of a cost-effective transaction, the costs of which were not recognized or anticipated in the level of costs used to establish the utility's base rates. One example raised was the cost of an unanticipated short-term lease of a terminal to allow a utility to receive a shipment of low cost oil," close quote.

Now, I want to ask you, Mr. Portuondo, the

$381 million project you have to uprate the Crystal River 3 unit is, would you agree with me, somewhat of a far cry from an unanticipated short-term lease of a shipping terminal?

A. No, I don't agree. I think it's a fuel savings. It's a different approach to achieving the same end result that the Commission was striving for. In the introduction to that example, nowhere did they say fossil fuel expense. So again, sometimes they use those words; other times they don't. I think the end game or what the parties to the workshops that gave rise to this in the final order, what they were trying to do is reduce fossil fuel expenses, and the leasing of this tank achieved it. That's one example. I mean, they say this is one example.

Q. Well, let me --

A. I'm presenting to the Commission Number 5, or Number 6. They've had previous examples of capital expenditures that have given rise to fuel savings for the benefit of customers.

Q. Okay. Let me read the rest of the paragraph quickly and then ask some more questions. "The parties suggest that this flexibility is appropriate to encourage utilities to take advantage of short-term opportunities not reasonably anticipated or projected for base rate recovery. In these instances, we will require that the affected utility shall bring the matter before the Commission at the first available fuel adjustment hearing and request cost recovery through the fuel adjustment clause on a case-by-case basis. The Commission shall rule on the appropriate method of cost recovery based upon the merits of each individual case," close quote.

Now, is there anything to your mind short-term about the CR3 uprate?

A. No. On the contrary, it's providing savings for many, many years.

Q. Well, would you characterize it as a short-term opportunity?

A. No. I think it's a long-term opportunity to create fuel savings.

Q. Okay. Now, you have anticipated this project, right, because you're here requesting it, and you have not accomplished it yet; is that correct?

A. I guess I don't understand.

Q. Well, the Commission --

A. The project -- I'm sorry. Go ahead.

Q. Go ahead.

A. No, go ahead.

Q. The Commission in its discussion I just quoted says to encourage utilities to take advantage of short-term opportunities not reasonably anticipated or projected for base rate recovery. And my question to you is, one, you could project this for base rate recovery in your next rate case, could you not, this project?

A. No. I think that the question put forth here is that it had not been anticipated or put forth in rates at the time. Absolutely, I don't disagree with you. At some future rate case, whenever that may be, any capital investment that we make could be sought through base rates.

This project here is one that, but for the fuel savings, would not have been considered. Just like the dual fuel conversion of our peakers, it was the fuel savings that drove it. And it's the utilization of the Commission's policy that we're trying to -- or we're trying to comply with the Commission's policy on the recovery of these types of projects.

Q. Okay. But I want you to help me here, okay, because I'm thinking to myself that the Commission didn't include this illustrative language in the order, the illustration, the example they gave here for no good purpose. I mean, wouldn't you agree with me that there must have been some purpose intended when they gave this example?

A. It was an example of something that would create fuel savings. It's just one.

Q. Right, I understand. But in the example they've given, wouldn't you agree with me what they've said here is, "Okay. We've got a company. They have an opportunity to get a shipment of oil, maybe a barge or a tank load of oil at lower costs than prevailing, and they need to lease a terminal to take delivery of the oil, and that's something that's short-term, that was unanticipated, and we're going to go ahead and do that because it makes sense." Don't you agree they're talking about something that's short-term by definition, and it involves a lease, and something small, by definition, in terms of dollars?

A. It's simply one example.

Q. I see. Well, in fact, it's the only example in this order, isn't it?

A. It is the only example. And I think by virtue of how many projects in the last 20 years have come before the Commission, you can see that they don't occur very often. It's difficult to find these opportunities.

Q. Now, going back to what has now been identified as Exhibit 28, let me ask you, would you agree with me that if the Commission, if this Commission wanted the opportunity to distinguish this specific case from the five other cases that occurred under this Item 10 application over the last 22 years, would you agree with me that an excellent thing for them to get their hands around to distinguish this case would be the order of magnitude of the project's cost, your cost versus those that came before?

A. I agree. That is a distinction, but so is the level of savings of this project versus the others.

Q. Now, the Commission entered this order that covers a lot of other areas, correct, regarding fuel cost recovery?

A. Correct.

Q. And we have this Item 10 that is but one small part of a much larger order, and it has only been used on five previous occasions over the course of 22 years; correct?

A. Correct.

Q. Four of the five involves fossil-fired generation plants; right?

A. Correct.

Q. The fifth remaining admittedly involved a nuclear power plant, but in fact it involved two plants, the uprate of two plants, Turkey Point 3 and 4, at a project cost of $10 million; right?

A. Correct.

Q. Now, you said earlier I think in response to Mr. McWhirter's questioning that you felt obliged to obey this order, or words to that effect; right?

A. No. I think what I said is I have to follow this order.

Q. Okay. Which you are saying means you have to come in and, based on the facts of this case, ask that it be cost recovered through the fuel adjustment clause?

A. What I'm saying is that this order provides for the recovery of this type of project, and to seek recovery, I cannot simply just put it in fuel, but I have to bring it to the Commission for their review.

Q. Okay. Now, I want to know if you think that if the Commission said no -- I mean, each and every customer, body, or party that's here is urging the Commission to say no, to just say no. Okay? If the Commission were to say no, would you feel that you've detrimentally relied upon this order?

A. I guess I would, personally.

Q. Well --

A. I mean, I'm trying to do the right thing. I'm trying to follow the Commission's direction through its orders, and that's what brings us here today.

Q. Yes, sir. I understand that. But let me contrast it to another situation. Okay? Let's say that you've gone ahead and spent $381 million on this project and then came in and said to the Commission, "Look way deep in the bowels of this order, whatever number it is, and in Item Number 10, it says this is how we should have done it, fuel adjustment clause," and they say, "Time out. You're wrong." Contrast that situation to now. You haven't spent the $381 million in reliance upon getting fuel cost recovery for the project; right?

A. That's correct. But I wouldn't -- your scenario wouldn't happen, because the practice has been in the fuel clause that if there's anything unusual, you seek permission first before you start spending dollars. That's actually the practice in all the clauses, is to seek approval first, get an acknowledgement from the Commission that the project does comply with the clause, and then costs from the point at which time you've petitioned can be recoverable, but not after the fact.

Q. Yes, sir. And that was my point, because you're here pursuant to the long-established policy that you ask first, generally get permission and do it?

A. Correct.

Q. In these type of matters. And my point is, and I want to ask you to agree with me hopefully, is that aside from the preparation you put in this case, you're not put out financially because you haven't spent the money yet; right?

A. Well, I think we have spent some dollars.

Q. Yes, sir, but you haven't spent the $381 million on the project. You have spent moneys in preparation of making your case here.

A. Well, and scheduling -- maybe a couple million dollars. But, yes, you're right, I haven't spent the bulk of the dollars.

Q. And I think you were probably going to say that you've actually ordered some rotors and that kind of stuff. Were you going to say that?

A. Well, I don't know whether the order has been placed yet.

Q. But even if they had been ordered and you had expended funds on it, you could go ahead and still use the rotors and make the uprate even if you didn't get fuel cost recovery in this case; right?

A. I can't agree to that. I don't know whether -- I can't agree. I don't know whether the company would pursue the project or not.

Q. My question isn't whether the company would go ahead and do this project that would bring huge benefits, clear benefits, Mr. Roderick's language, clear benefits to the customers if they didn't get their way on the recovery. But in terms of a practical, actual possibility, you could go ahead and do the entire project if you elected to under rate base recovery; right?

A. I don't know whether we would pursue the project or not. I mean, I've answered that question before as posed by different intervenors, and I just don't know what the company would do.

Q. Okay. Now, as I said a minute ago, you recognize that everybody here on this side of the table, which is usually your side, strongly opposes fuel cost recovery in this case; right?

A. Yes.

Q. That is all your customers, because Public Counsel statutorily represents all of your customers by law, and then the rest of us are in here helping. We all oppose this methodology. And yet you still want to go ahead and do it; right?

A. Yes, I do.

Q. Now, isn't it reasonable to conclude that if we don't want you to do it and you want to do it anyway, you're doing it for your own purposes, to your own advantage?

A. No. I'm doing it because that was the encouragement of the Commission, to think innovatively.

We've done that. We've thought innovatively. We're bringing a project with the potential of $2.6 billion, and I think we're entitled to the treatment under today's regulations.

If you want to change that going forward, I think Mr. Walls in his opening comments said the utility has no objection for pursuing a workshop to change things prospectively if that's what is the desire of the intervenors and the customers. But I think what makes the regulatory compact and the efficient operation of a regulated utility is to know what the rules are and to follow those rules, and that's what we're doing here today.

And I think that we are bringing benefits to the customer. I think the customer's rates remain the same or go down during that period of time, and I think that's a win-win. The company is able to recover that investment and be able to redeploy it back into other projects. We have a lot of projects over the next ten years. So that is an important criteria to keep in mind.

Q. Yes, sir. But we're telling you en masse here that we don't think the project as petitioned for here benefits us to our advantage. You are saying, as I understand what you're saying anyway, and correct me if

I'm wrong, is that we think it benefits you, and we know better than you what's good for you. Is that what you're saying?

A. No, I'm not.

Q. Well, then if that's not the case, it stands to reason, at least to me, that you want to do it despite the fact that we don't want you to do it because it has advantages to the utility. And I want to ask you about some advantages and see if they exist.

The recovery to you for this project through fuel cost recovery would start when?

A. It would start upon the commercial in-service of the respective component.

Q. Through fuel?

A. Correct.

Q. So there is -- arguably, if you didn't have a rate case, a base rate case concluded by the time this goes in service, the fuel would result in a faster recovery of your costs than the base rate treatment; correct?

A. Well, I think to the extent that any asset goes commercial, it goes into rate base, and you're assumed to be recovering it to the extent revenues allow it, yes.

Q. Yes, sir, precisely. It's in rate base, but it wouldn't be reflected in new rates in a rate case?

A. Unless we've petitioned. I mean, that was a potential when the '85 order was approved, that any petitioner could come and petition for a project to be recovered in base rates.

Q. Let me be sure I understand you. You're telling the Commission that if you didn't get the fuel cost recovery and had to go the base rates methodology, not base rate case, but base rates, that the unit would go into rates on the same in-service date, approximately, that it would be recovered through fuel, because it would be in rate base and it would be in rates on the in-service date irrespective of whether you had a new rate case or not?

A. Just like any other asset of the company.

Q. But it would be in -- what I'm saying is, to be clear, it would be in rates. It would be covered by your rates?

A. Correct, to the extent we pursued that -- if in the Commission's -- if the Commission denies our request and we were to continue with the project, it would be treated like any other project of the company. It would go into base rates.

Q. Right. And it's kind of like the -- I had a handout, and I just mentioned it briefly in my -- it's not an exhibit, but in my opening statement. There was an article in that. I don't know if you saw it, but there was an article in the paper that said that utilities, including Progress Energy, were large beneficiaries of the property tax reductions in the counties, and that Progress Energy was going to have $1.4 million savings. Are you aware of that?

A. I saw what you handed out.

Q. And the question was, by the reporter, apparently, would that be reflected in rates, in a rate reduction. And I think the answer given was proper, as I understand ratemaking, is that, no, because you have a rate settlement to 2009, and that would just be one of the reductions, perhaps of many, that you have in expenses to offset maybe new plant coming in, which happens all the time; right?

A. To offset new plant? Well, it could offset a thousand different things. You have rising medical costs for your employees. You have rising material costs. I mean, there are up and downs from year to year on your normal recurring costs, and that would have been a normal recurring cost that was anticipated in rates. This particular project is really not akin to something like that, normal recurring type level of capital expenditure.

Q. Yes, sir. And you also have a possibility, hopefully, of increased revenues as well; right?

A. Not attributable to this project --

Q. No, I don't --

A. -- no, sir.

Q. I'm sorry. I didn't mean to interrupt you. Not to this project. I mean customer growth, increased consumption, per capita consumption of customers and that kind of thing. That's something you would like to see, and it's certainly a possibility; right?

A. Typically that revenue comes with a cost associated with connecting up those customers, extension of lines, new generation to support those customers, additional manpower to respond to customer needs in the customer service center. You know, that's kind of base rates. As you add more customers, hopefully the addition of revenues will help the normal recurring costs of your business. And to the extent that those are matching, you can avoid a rate case. You can avoid raising rates to customers.

What this order helped to do is to provide cost recovery for those unique things, that ingenuity to address issues that didn't have a corresponding new revenue stream. In fact, this serves to reduce customer costs through the fuel savings. So I think that's what the Commission was trying to encourage by Item 10.

Q. Okay. But let me ask you now -- I'm near the end here. Typically, in the base rate review of this, you would have maybe an insurance cost, property insurance -- not insurance, property tax going down 1.4 million a year. You might have revenue growth here. You would have new plant installed, generating, or transmission, whatever. And absent a settlement, from month to month, the company would look and see whether you were earning within your last approved range; right?

A. Correct.

Q. And the customer groups and the Commission, the Commission staff would be looking to see if you were fortunate enough to be earning above the range; right?

A. Correct.

Q. In which case we could call for a rate reduction case. If you were below your last authorized return because of -- whatever the circumstances that went into the rate base mix, then you could request a rate increase; right?

A. Correct.

Q. Now, if you know, where are you going to be -- you're in a rate settlement now, right, with most of us?

A. Correct.

Q. Through 2009, or into 2009.

A. Through the end of 2009, with potential extension through mid-2010.

Q. Okay. If you know, how would a plant, a capital plant expense or cost of the order of $381 million, where would it put you in your earnings vis-a-vis your last authorized range of equity?

A. I do not know. I mean, there's a lot of new costs coming into the business. The Bartow repowering goes in service around that time. The steam generator goes in service around that time. I mean, you've got to consider that since Bartow is going in because of a capacity need, there's probably growth in revenues there to offset some of that. So there's a lot of variables.

Unlike those, this one doesn't have a corresponding revenue stream. The basis for the recovery, we're fortunate that we have fuel savings we can use to fund this one without having to include it in a base rate proceeding and get base rate recovery of it.

Q. Yes, sir. One last line here and I'll stop. I think Mr. McWhirter asked -- he touched on this. It's possible, is it not -- I'm not saying that you know or that I can know, because I don't think either one of us do, but you're in a better position, of course. But it's possible, isn't it, that if you went ahead and completed this project, which you unanimously have said has great benefits or clear benefits for the customers in terms of fuel savings, reduced greenhouse gases, greater fuel diversity, greater base load generating capacity, if you went ahead and did it even if the Commission didn't authorize fuel clause recovery, that you expend the $381 million and get to the end of your settlement and find that you were still in -- for whatever the circumstances, still in the middle of the range of your last approved return, and then you couldn't come in and ask for any more rates; right? That's a possibility?

MR. WALLS: I'm going to object that it calls for speculation.

MR. TWOMEY: Madam Chair, I don't think it -- it calls for "isn't that a possibility." I'm not saying is it going to happen this way or that way. But the clear fact is that if, as I outlined it, they got there, if they're in the middle of their last authorized range, for whatever reasons, they wouldn't be able to ask for rate relief. I'm just asking him to confirm that. I suppose I could just call it a hypothetical.

MR. WALLS: Hypothetical or not, he's still asking the witness to speculate.

CHAIRMAN EDGAR: Sounds like speculation to me.

MR. TWOMEY: Well, you're the boss, Madam Chair, so I'll leave it there and stop.

CHAIRMAN EDGAR: Okay.

MR. TWOMEY: Thank you.

CHAIRMAN EDGAR: Any -- I believe we are at the time for Commissioner questions. Commissioner Skop.

COMMISSIONER SKOP: Thank you, Madam Chair. I think Mr. Twomey kind of stole a little bit of my wind in terms of questioning that he raised with respect to Order No. 14546, but I had a couple of questions for the witness.

Would you agree that the request to recover the uprate costs via the fuel clause substantially builds upon the existing precedent to the extent of the order of magnitude that's requested in comparison to the Turkey Point precedent that he referenced?

THE WITNESS: No. I don't think order of magnitude is relevant in the application of the order. I think the order was trying to encourage the utilities to find fuel savings. It just happens that, you know, this one requires a significant expense in order to achieve significant savings.

COMMISSIONER SKOP: And as a follow-up to that, in Mr. Twomey's cross-examination, he mentioned a win-win scenario. Do you remember that?

THE WITNESS: Yes, I do.

COMMISSIONER SKOP: But you would agree, would you not, that the situation is only win-win to the extent that -- only if you deliver on time, on budget, and achieve the projected benefits; is that correct?

THE WITNESS: Well, it's a win-win if I deliver, you know, 2.6 billion less, you know, the costs. I think at the end of the day, we'll be able to show that customers have received benefits in excess of the costs of the project.

COMMISSIONER SKOP: And excuse me if it wasn't you, but I believe on your direct testimony you mentioned that -- well, actually it was probably on cross, but you mentioned that if the costs went up substantially -- like right now they're projected, I think, at 440 million all in, but if they went up to like 800 million, the speculation as to whether this would be ultimately a cost-effective or cost-beneficial project came into a little bit of concern; is that correct?

THE WITNESS: That's correct. I think the point I was trying to make in response to that question is that the Commission will have an opportunity to review the costs incurred on an annual basis. The Commission and its staff and the intervenors will have an opportunity to see what drove those cost overruns, are they reasonable, were they, you know, reasonable scope changes, or was it something that we may have not managed as efficiently as we could have. But I think what I was getting at is that the opportunity to review those costs is ongoing by the Commission every year.

COMMISSIONER SKOP: Just two quick more -- two additional questions. Are you familiar with the need determination for this project that was approved by the Commission?

THE WITNESS: I've given the order a cursory review, yes.

COMMISSIONER SKOP: And having been approved for the project via a need determination, can you offer any reason why a utility would not pursue that project irrespective of what the cost recovery mechanism would be?

THE WITNESS: Well, it was approved as a capacity need -- as an economic need. I think procedurally a project of this nature has to go through that -- through those procedural steps.

And as I've responded before, it's difficult to say whether we ultimately proceed or not, because there's a number of projects that are on the table that will need to be re-evaluated. We can't just look at this project in isolation. There's limited -- there's limitations to how much indebtedness, how much equity the utility can go after in any one year to pursue the necessary bread-and-butter type projects. This is one of those projects that has to compete alongside with making sure that the system hardening is accomplished correctly on schedule, that the power plants are operating efficiently and humming and providing the reliable service to our customers. So I think all those things need to be taken into consideration.

That's not to say that this one, you know, wouldn't hunt, but I think that's not the way we looked at it. I think we saw this as kind of a win-win, that we could provide for more timely cost recovery and then be able to go back into the capital markets and get more of that capital to apply to the other projects that are coming up in the horizon. I mean, we've got -- you know, CAIR is a billion dollars. We've got future base load needs. The hardening is going to be an investment as well. So I think we have to look at it holistically.

COMMISSIONER SKOP: Thank you.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Thank you. I'm just having a hard time grasping your argument for, I guess, relying on Order No. 14546. I understand where you're trying to go. So I'm just going to ask a couple of questions, because most of them have been asked already.

I guess the one that sticks out in my mind -- and I won't even go into the fossil fuel one. But maybe you can help me by clarifying what your definition of short-term is, because I just see it as a clear differentiation between what I'm interpreting from that and maybe what you are.

THE WITNESS: Certainly. I think the reference on page 3 to short-term, that was trying to provide a flavor around the example that was being provided, that this was a short-term opportunity in this particular example. I don't see that being part of the definition in Item 10. I guess I didn't read it as that being a restriction for the application under Item 10.

COMMISSIONER ARGENZIANO: Not maybe as the intent?

THE WITNESS: It was difficult for me to make that leap, because I know how important striving for fuel savings is. So I would have been surprised if they were looking so narrowly, you know, in deciding that this would be something appropriate for the fuel clause.

COMMISSIONER ARGENZIANO: Okay. And just a couple of others. And I know I've heard it several times here, and I think I wrote it down the way you said it, "I don't know whether the company would pursue the project." And, of course, how would you know unless they told you personally? But I can ask you this question, because I think it's important for me to hear it. Would you or do you believe that PEF does have an obligation to obtain the lowest costs, fuel costs?

THE WITNESS: Sure. And we strive for that every year in our procurement of fuels, the transportation as well as the commodity. I think that, again, as I've tried to articulate, maybe not as effectively -- I mean, it's a struggle, because you do have limited abilities in any one year, and there could be thousands of things that you would want to accomplish, but you just can't go out and create such a debt that you end up, you know, creating a bad situation for the utility going forward. So you do prioritize your projects. You prioritize your O&M projects. You prioritize your capital projects.

And this opportunity that was considered in this order I think recognized that to some degree, to say, "Okay. We know you've got to keep the lights on, the bread and butter, and we know you're doing the right thing in your procurement of fuel and your transportation, but we want your employees and everyone to keep imagining what else could be done, and we'll give you this opportunity to recoup that investment utilizing the fuel savings so that you can keep redeploying those dollars and thinking of more things to do." And it is hard. I know I continually in the 22 years I've been at this trying to get people to think of ideas like this, and it is very hard.

COMMISSIONER ARGENZIANO: Certainly -- Madam Chair. Certainly that's very important, and I think everybody would agree with that. But still with the obligation to obtain the lowest costs and I guess to protect the ratepayers also; right?

THE WITNESS: Correct.

COMMISSIONER ARGENZIANO: And maybe one other question, to answer maybe the best as you can. Do you think that if the company did not pursue this project that it kind of contradicts what PEF's position in last week's -- I think it was in the $143 million coal refund case. One of the witnesses testified that they were under an obligation to obtain the lowest cost fuel that meets reliability needs. Do you think there would be a contradiction if the company didn't pursue it?

THE WITNESS: No, I don't. As I mentioned, I think we're going to procure fuel at the least cost possible. This is an opportunity not in the procurement arena, and that's what makes it more creative. It's an ability to try and avoid the need to use a more costly fuel altogether through this uprate.

So I think we're definitely prudently procuring the least cost commodity for the fleet as seen necessary based on the dispatch of that fleet. What else can we do? And that's kind of what this order tried to get at. What else could there be out there?

We have in base rates our maintenance dollars to make sure that the plant is running efficiently, therefore producing the least cost to customers. This is kind of the stretch goal, you know, because it's not something -- as Mr. Roderick articulated, it's not something that's been done to a B&W plant. So we're trying to go the extra mile.

And we did that, I think, in thinking about our gas conversion projects as well. The market -- we saw the potential to play off the spread between oil and gas. That was only possible if we were able to modify equipment of the turbines to be able to switch between oil and gas. So again, we came to the Commission, we were able to get recovery, and then we immediately took that capital and reinvested it in the next couple of units and again until we ran out of units where that would really make sense.

And it's been a while since we've been able to think about or identify other beneficial projects like that. And this one just happened to be a whopper, you know, both from the cost and the savings.

But at the end of the day, I think customers are not harmed by this methodology the Commission has established. Rates remain the same or, you know, may slightly go down in the years over which we're recovering these dollars, and then they get a huge pop once the cost has been fully recovered. They get 100 percent of the benefits of this uprate.

COMMISSIONER ARGENZIANO: Madam Chair, if I could just bring it back to the question, because you said a lot in there. And I guess what I'm asking you, and I may ask it one more time -- I think you partially answered it. I just don't remember now from what you first said. According to witnesses that testified from PEF, you're still saying that you would think that PEF is under an obligation to obtain the lowest cost in whatever you pursue?

THE WITNESS: The lowest cost purchase of fuel, yes.

COMMISSIONER ARGENZIANO: Thank you.

CHAIRMAN EDGAR: Commissioner Skop.

COMMISSIONER SKOP: Thank you, Madam Chair. Just one quick follow-up question. I noted that when you were pressed to committing to moving forward with the project without the granting of the request to put it in the fuel clause that you were hesitant, and you were likewise hesitant towards committing to bring the project in at a specified cost to the extent that there is some cost risk uncertainty.

So in that regard, and noting that you mentioned the win-win scenario, has any thought been given to making approval of your request contingent upon overcoming the cost and technical risks associated with implementing the uprate that was approved via the need determination in a manner analogous to the pay for performance concept that's in the corporate world? Again, because we are looking at win-win solutions, and I do think that, having been approved by the need determination, there's certainly merit to the project, the question is how do you implement and capture that need in the manner you mentioned as win-win. So could you please comment upon that?

THE WITNESS: I think that's an interesting concept. I think it merits some thinking on the part of the company. I have not thought about it in that way.

COMMISSIONER SKOP: Thank you.

CHAIRMAN EDGAR: Are there questions from staff?

MS. BENNETT: Yes. Thank you, Chair. I have whittled down the questions.

CROSS-EXAMINATION

BY MS. BENNETT:

Q. I wanted to start with Issue 2, which is, if the Commission authorized clause recovery of the CR3 uprate project, which cost recovery clause, fuel or capacity, is appropriate for capitalized costs attributable to the uprate. And on page 6 of your amended direct testimony, you state that the purpose or the primary purpose of the CR3 uprate project is to reduce fuel costs to customers by displacing energy from higher cost fossil fuel with low cost nuclear fuel; is that correct?

A. That's right.

Q. Is it correct to state that fuel costs are recovered through the fuel clause?

A. Yes.

Q. And is it true that customers who experience the fuel savings by seeing a reduction in their fuel -- is it true that customers will experience a fuel savings by seeing a reduction in the fuel factor?

A. Would you repeat that?

Q. Sure. Is it true customers will experience fuel savings by seeing a reduction in their fuel factor?

A. During the period that the costs are being recovered?

Q. Yes.

A. No, because we're using those savings to recover the costs. Once the costs have been fully recovered, they will see a significant decrease. I think we were projecting, you know, maybe $90 million in some years worth of fuel savings. So once the recovery is complete, then customers would see 100 percent of the benefits.

Q. And those benefits would be seen through the fuel clause or through the capacity clause?

A. Yes, ma'am, through fuel clause.

Q. Thank you. How are fuel costs allocated? Are they allocated on an energy or demand basis?

A. Energy basis.

Q. And how does the capacity cost recovery clause allocate costs?

A. On a demand basis.

Q. And is it correct to state in general that a demand allocation assigns more responsibility to the residential class?

A. That is correct.

Q. So if costs are being recovered through the capacity clause, then the residential class would see a larger assignment of the costs than if the costs were recovered through the fuel clause?

A. That is correct.

Q. Okay. I want to turn to Issue 5, which is if, again, the Commission authorizes Progress Energy Florida to recover through the clause, what return on investment should the Commission authorize PEF to include. And some of my questions will focus on Issue 5.

First of all, if PEF is permitted to recover the costs of the CR3 project through the fuel cost recovery clause, I understand it's PEF's position that the last authorized weighted average cost of capital approved by the Commission should be used for purposes of determining the appropriate return; is that correct?

A. Yes, it is.

Q. And that return on equity is 11.75 percent; is that correct?

A. Yes, it is.

Q. And your position, Progress's position is based on prior Commission decisions; is that correct?

A. It's also based on the -- I guess that is a decision too, the settlement reached with the parties and approved by the Commission in the 2005 rate case.

Q. But it's also true that you cannot cite any rule or statute that specifies that a currently authorized return on equity is the only return the Commission can use for calculating the return on capital items recovered through the fuel cost recovery clause; is that correct?

A. That is correct. Unlike the other clauses, the fuel clause does not have a corresponding rule to point to.

Q. And then I'm going to turn our attention to Issue 7, which is, if the Commission again authorizes clause recovery of the CR3 uprate project, what reports, if any, should Progress be required to file with the Commission. It's my understanding that if the Commission allows clause recovery, the company will attach an exhibit to its testimony each year in the fuel clause which will show the calculation of fuel savings and costs of the project; is that correct?

A. That is correct.

Q. This exhibit will be like exhibits you've filed for prior projects that have been recovered through the fuel clause; is that correct?

A. Yes, it will be.

Q. The costs of past projects that received fuel clause recovery are reviewed by PSC auditors; is that correct?

A. Absolutely.

Q. Let's assume that the cost of the project is approved for clause recovery. And fuel savings that you will report will be calculated by comparing PEF's system with and without the additional nuclear megawatts; is that correct?

A. That is correct.

Q. If the project costs are approved for clause recovery, for reporting purposes, you will report project costs, amortization, allocation between retail and wholesale, and return on investments; is that correct?

A. That is correct. We will also -- to the extent that co-owners have taken some of that, we will acknowledge that as well.

Q. In your direct testimony on page 7, line 10, and continuing on to the next page -- I'll give you a minute to get there.

A. You said page 7?

Q. Page 7, beginning on line 10 and continuing to the next page.

A. Yes, ma'am.

Q. Isn't it true that if there was no CR3 uprate project, the steam generator project would still take place? I believe you've also testified to that.

A. Absolutely.

Q. In your deposition, you stated that Progress Energy owns approximately 90 percent of the CR3 power plant; is that correct?

A. Yes.

Q. Who are the other owners?

A. Seminole, and a handful of cities represented by FMPA, Tallahassee, City of Tallahassee. I believe GRU also owns a piece.

Q. If the other owners elect not to share in the costs, would retail customers get the entire benefit of the 180-megawatt increase?

A. Absolutely.

Q. Would there be any situation when PEF's retail customers would pay for 100 percent, but receive less than 100 percent of the uprate?

A. No, ma'am.

Q. Issue 6 deals with the allocation of the CR3 uprate costs between the wholesale and retail jurisdictions. The joint owners that we discussed before are considered the wholesale jurisdiction; is that correct?

A. No, ma'am. No, they're actually equity owners in the power plant. They also happen to be wholesale customers, but the wholesale jurisdiction is more encompassing than just the co-owners.

Q. Let's assume a joint owner agrees to pay a share of the costs of the uprate. How will Progress determine how much the joint owner will pay?

A. My understanding is that there is an ownership percent for each co-owner, and they would be entitled to that same percent ownership in the uprate. So like we said, we own 90. The sum of the others let's say is 10, so they would be entitled to a 10 percent investment share and corresponding megawatts of this project.

Q. I also believe you testified that you were presenting testimony on Commission policy and that you believed it was the Commission's policy to approve the types of capital cost recovery when they have fuel cost savings; is that correct? You are the policy witness?

A. Yes, I am.

Q. Do you believe that providing additional nuclear generation for Florida is good public policy?

A. I think it was articulated through the passage of the 2006 Energy Act, yes.

Q. In your opinion, should the Commission encourage investor-owned utilities to provide additional nuclear generation?

A. I think so.

Q. Isn't it good regulatory policy to have all utility stakeholders on board at the commencement of an important public policy?

A. I think they were through the passage of the legislation.

Q. Back to the allocation between retail and wholesale costs. Can you explain how Progress Energy will show the Commission the allocations between the retail and wholesale costs?

A. In the schedule or exhibit that will be attached to our testimony, there's a section I believe towards the bottom of that schedule that shows the energy allocation amongst the stratified customers and then in turn the average energy customers, wholesale and retail. So you'll see the -- you'll be able to walk through the calculation of the allocators on that schedule.

Q. Okay. And finally, I'm going to turn back to -- Mr. Roderick testified, and I believe you've also filed amended testimony based upon the MUR going into effect in 2007. I'm not sure we heard, what date did Progress Energy Florida discover that the MUR project should be done -- could be done separately or should be done separately from the steam generation?

A. I probably heard later than Danny, Mr. Roderick did, but I think it was earlier this year, the first quarter of 2007.

Q. Okay. And how did Progress Energy learn that the MUR should be done first?

A. That was a question for Mr. Roderick.

Q. Can you -- do you know how long the refueling outages will be in 2007?

A. This is a typical outage, so I would say 32 days is the -- usually around that, plus or minus five, is your typical refueling outage.

Q. And the refueling outage in 2009, do you know how long that will be?

A. Again, I believe again that would be better answered by Mr. Roderick, but I think it's in the 80-something days. It's a pretty long one.

Q. And if you can answer this question, could the MUR project be put into 2009, when it would be tested at that time, and then the stream uprate also subsequently put into place during that time frame?

A. That's a question for Mr. Roderick. I think he actually did answer that question. He was asked that.

MS. BENNETT: And that's at all questions I have.

CHAIRMAN EDGAR: Thank you. Commissioner McMurrian.

COMMISSIONER McMURRIAN: Thank you, Chairman.

I had one. I'm not sure if this has been asked or not. I know we talked about this quite a bit. We have spoken about how the company can't make the call, at least not here today, about what would be done if the project were not approved for recovery as requested in the petition through the fuel clause. But when could the company make that call as to whether it would pursue this project even if it were not approved for fuel recovery?

THE WITNESS: I couldn't tell you. I would have to go check with senior management.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Just another question. And I don't know that you really can answer it, but maybe your opinion. Do you think the company would share the savings by only recovering half of the costs to the customers?

THE WITNESS: I don't know that I can answer that today.

COMMISSIONER ARGENZIANO: Okay. Thank you.

CHAIRMAN EDGAR: Redirect?

MR. WALLS: Yes. I'll try to be brief.

REDIRECT EXAMINATION

BY MR. WALLS:

Q. Mr. Portuondo, you were asked a number of questions by the intervenor parties regarding the cost estimates. What happens if natural gas or oil prices are higher in the future than they've been projected by the company?

A. Our projection of the 2.6 billion would go up.

Q. And Mr. McWhirter was asking you a number of questions about the fuel costs in December -- as of December 2008 or in 2008 compared to 2007. What happens at the end of November or December 2007 that can affect fuel costs, and particularly gas costs?

A. Could you say that again?

Q. Yes. Mr. McWhirter was asking you a number of questions comparing the fuel costs between 2007 and 2006, current and projected, and the 2008 period, pointing out that 2008 was significantly higher. What happens at the end of November or December 2007 that can affect the fuel costs, and particularly natural gas costs?

A. The projected underrecovery Mr. McWhirter was alluding to could disappear pretty quickly should we be impacted by a hurricane in the Gulf of Mexico. So again, we definitely caveat that our reprojection is assuming normal weather and that no such event occurs.

Q. I was actually thinking of something more basic, like don't we have a unit coming online?

A. Okay. Well, you're referring to Hines 4. The fuel cost of Hines 4 is already incorporated in that reprojection. So, you know, hopefully we got some good price projections based on normal weather. That would be the only thing that I could envision impacting the commodity prices between now and the end of the year.

Q. My next questions are about the Hearing Exhibit Number 28 that Mr. Twomey was asking you about, if you have that in front of you.

A. I do.

Q. He was asking you a number of questions to compare the cost factors of the other five projects on this exhibit that have been approved by the Commission under Order 14546 and the CR3 uprate. I was wondering if you could give us the savings factors of the other five projects compared to the uprate.

A. I can. One moment.

Beginning with the first project, our projected savings during this period is 57 times greater than the FP&L project. If you go to the next approved project, that one is -- our current project is 46 times greater. The next one, the 16 million, our current project is 64 times greater. The 20 million savings for the next dual fuel conversion, we are 51 times greater. And lastly, with the Suwannee project, we're 314 times greater.

Q. And Mr. Twomey was also asking you a number of questions about return versus expense under Order 14546. In every prior application that's identified in Exhibit 28, did the utility earn a return?

A. Yes, they did.

Q. A couple of final questions. Mr. Twomey was focusing you in on language in the order that talked about the example of a short-term lease. Looking at Exhibit 28, is the thermal uprate at Turkey Point a short-term or a long-term savings project?

A. Long-term.

Q. And what about the other ones? Would they be characterized as short-term or long-term?

A. They're all long-term.

MR. WALLS: That's all the questions I have.

CHAIRMAN EDGAR: Thank you. Okay. Let's take up the exhibits.

MR. WALLS: We would move into evidence the Witness Exhibits JP-1, JP-2, and JP-3, which are Hearing Exhibits 7, 8, and 9, as well as Hearing Exhibit 28.

CHAIRMAN EDGAR: Okay. Seeing no objection, let's enter 7, 8, and 9 into the record. Any objection, concerns or comments about Exhibit 28? Seeing none, okay, Exhibit 28 will be entered into the record as well.

(Exhibits 7, 8, 9, and 28 were admitted into the record.)

CHAIRMAN EDGAR: Okay. The witness is excused for now.

MR. WALLS: Yes, excused for now.

CHAIRMAN EDGAR: With the understanding that he will be coming back on rebuttal. Thank you, Mr. Portuondo.

THE WITNESS: Thank you.

CHAIRMAN EDGAR: Okay. Commissioners, I recognize that the hour is late, but we did have a request for one more witness today, so we will make every effort to push through a little bit, with the understanding that after we are concluded with this witness, then we will break and come back tomorrow. Tomorrow had been listed on our calendar as a day for this hearing, if needed, and it looks like it will be needed.

So, Mr. McWhirter, your witness.

Thereupon,

JEFFRY POLLOCK

was called as a witness on behalf of Florida Industrial Power Users Group, and having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. McWHIRTER:

Q. Would you state your name for the record, please, sir.

A. Jeffry Pollock.

Q. Have you previously been sworn in this case?

A. Yes.

Q. Have you prefiled testimony in this case?

A. I have.

Q. And do you have that before you?

A. Yes.

Q. Do you have any amendments or corrections that would you like to make to the testimony that you prefiled?

A. I have one correction, and that would be on page 20 of the testimony at line 1. I want to correct the order number. It should read 23573. That's the only correction.

Q. Mr. Pollock, would you summarize your testimony very briefly and rapidly?

A. Rapidly, yes, sir. Thank you and good evening, Commissioners. I appreciate you accommodating my schedule.

This case is not about denying cost recovery. It's all about recognizing that the company has several options to recover the nuclear uprate costs that provide a greater balance than proposed recovery through the fuel clause. For example, growth in sales is one opportunity. The company can also file a base rate case on or after July 2009 to recover the uprate costs if the company's earnings become deficient despite the revenue growth.

With respect to the revenue growth, the company's sales are projected to grow by over 5,800 gigawatt-hours for the period 2006 to 2011. At current base rates, that will generate over $240 million of additional revenues, not including the additional revenues associated with Hines Units 2 and 4 to be moved into base rates later this year. To put this into perspective, the 240 million is more than four times the revenue requirement of the uprate through 2011.

If the company is still unsatisfied with 240-plus million in additional base revenues, it still has a second option. A rate case filed in mid to late 2010 would allow timely recovery, because the vast majority of the investment will not be used and useful until the 2010, 2011 time frame. The filing of a rate case is also consistent with the settlement of the 2005 rate case, in which base rates would remain frozen through the end of 2009 unless the company agrees to a six-month extension.

In that settlement, the company agreed to not seek recovery of costs normally recovered in base rates through any new surcharges, but this is precisely what the company is seeking to do here. By adding capital costs to the fuel cost recovery clause, the result is higher fuel charges than if the costs were not recovered through the fuel cost recovery charges. Therefore, it is a surcharge.

FIPUG strongly believes that a deal is a deal. We urge you to uphold the 2005 settlement as a matter of equity and fairness to ratepayers.

In any event, the fuel clause recovery for over $440 million of capital costs would be unprecedented. All prior exceptions involved investments of $10 million or less with five-year or shorter amortization periods.

And there's no precedent to recover transmission costs through fuel clause. These costs account for about 89 million of the 380 million cost before AFUDC. The proposed transmission system upgrades are needed to maintain the reliability of the Florida grid and do not produce any fuel savings.

The same may be said about the 43 million of environmental costs that the company is also seeking fuel recovery. These costs also do not produce fuel savings. They're not recoverable through the fuel clause, but they are necessary to keep the plant in operation to provide reliable service.

The company's proposal should also be rejected because it will cause both intergenerational and interclass cost shifting. A fundamental tenet of ratemaking is to match cost recovery with the customers that receive the service. The nuclear uprate is projected to have a 28-year useful life, yet the company proposes to recover the capital costs in approximately ten years. This would create intergenerational inequity and should be rejected. At the very least, both the transmission and environmental costs should be amortized over long time periods, longer periods of time, consistent with the treatment of other similar costs.

Another fundamental ratemaking principle is that costs should be recovered in a manner consistent with cost causation. When examined in isolation, just about every new generation capacity addition will result in fuel savings just by virtue of improved technology. However, every capacity addition will enhance system reliability and meet projected demand growth. The nuclear uprate is no different. It will result in increased capacity and greater reliability. It will lessen the company's future needs to purchase power or to build additional generation capacity, and these facts are not in dispute.

There is no reason to alter how these costs are recovered from all other nuclear and non-nuclear investments, which are primarily recovered on the basis of a demand allocation. The Commission agreed with this reasoning when it adopted Rule 25-6.0423, Nuclear Plant Cost Recovery, earlier this year. Recovering capital costs through the fuel clause would shift the allocation from a demand allocation to an energy based allocation. However, all other similar costs are allocated to demand and recovered primarily through demand charges.

Thus, to prevent interclass cost shifting, if the Commission wants to go ahead and proceed with clause recovery, it should do so through the capacity cost recovery clause. However, our primary recommendation is to deny the petition. The company should not require extra incentives to do right by its customers.

That concludes my summary.

MR. McWHIRTER: I tender the witness for cross-examination.

CHAIRMAN EDGAR: Okay. Mr. McWhirter, would you like to enter the prefiled testimony into the record?

MR. McWHIRTER: Yes.

CHAIRMAN EDGAR: Okay. Let's go ahead and do that then, enter the prefiled direct testimony as amended by witness into the record as though read.

Before the
Florida Public Service Commission

In re: Petition to Recover Costs of Crystal River Unit 3 Uprate through the Fuel Clause	DOCKET NO. 070052-EI Submitted for filing: June 19, 2007

Direct Testimony of Jeffry Pollock

I. INTRODUCTION AND QUALIFICATIONS

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Jeffry Pollock; 12655 Olive Blvd., Suite 335, St. Louis, MO 63141.

Q WHAT IS YOUR OCCUPATION AND BY WHOM ARE YOU EMPLOYED?

A I am an energy advisor and President of J.Pollock, Incorporated.

Q PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A I have a Bachelor of Science Degree in Electrical Engineering and a Masters in Business Administration from Washington University. Since graduation in 1975, I have been engaged in a variety of consulting assignments including energy procurement and regulatory matters in both the United States and several Canadian provinces.

Q ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A I am testifying on behalf of the Florida Industrial Power Users Group (FIPUG). The participating FIPUG members are customers of Progress Energy Florida (PEF) and take service under various rate schedules.

II. PURPOSE AND SUMMARY OF TESTIMONY

Q **WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

A My testimony addresses PEF'S proposal to recover the Crystal River Unit 3 (CR3) uprate costs through the fuel clause.

Q **DO YOU HAVE ANY EXHIBITS TO YOUR TESTIMONY?**

A Yes. I have supervised the preparation of, or prepared the four exhibits to my Direct Testimony listed on the Table of Contents.

Q **PLEASE SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS IN THIS PROCEEDING.**

A PEF's proposed fuel clause recovery should be rejected for the following reasons. First, it would be a direct violation of the Settlement in PEF's 2005 base rate case (Docket No. 050078). Among other things, the Settlement required that base rates remain frozen through December 2009. Second, the proposed uprate does not qualify for cost recovery through the fuel clause because (a) the costs are not fuel-related and they are not volatile; (b) nuclear uprates are neither new nor innovative; and (c) the additional capacity to be provided by the uprate is needed by PEF to meet its projected peak demands and to maintain the required reserve margins. Third, collecting these costs through the fuel clause would create a double–recovery, because PEF's base rate already reflects the recovery of nuclear capacity costs. Fourth, the proposed fuel clause recovery is improper because (a) the costs at issue are properly classified as demand-related; (b) it would result in cost shifting because demand-related costs would be recovered on an energy, or kWh basis, and (c) the proposed 10-year amortization period would fail to match the costs of the uprate (which is expected to last through 2036), with the projected benefits, which are also projected to occur through 2036 the projected remaining life of CR3, (if PEF's planned license extension is granted).

Should the Commission, nevertheless, allow special cost recovery, the nuclear uprate costs properly allocable to PEF's retail customers should be recovered through the Capacity Cost Recovery Clause (CCRC). With the exception of the transmission portion of PEF's request, the costs should be amortized over the expected remaining life of CR3. Additional transmission costs should be amortized over a period not less than 40 years, consistent with the expected useful life of PEF's transmission facilities.

III. DOCKET NO 050078 SETTLEMENT

Q DID YOU PARTICIPATE IN DOCKET NO. 050078?

A Yes. I participated in this matter on behalf of FIPUG. Specifically I advised FIPUG on the relevant issues and supported the negotiations that ultimately resulted in the Stipulation and Settlement Agreement. Thus, I am familiar with the terms of the Agreement.

Q PLEASE EXPLAIN YOUR ASSERTION THAT PEF'S PROPOSED RECOVERY OF NUCLEAR UPRATE COSTS THROUGH THE FUEL CLAUSE WOULD BE A DIRECT VIOLATION OF THE DOCKET 050078 SETTLEMENT.

A The Agreement requires that PEF's base rates remain frozen through December 31, 2009 (or June 30, 2010, if PEF elects to extend the Agreement). Specifically it states that:

"PEF may not petition for an increase in base rates and charges that would take effect prior to the first billing cycle for January 2010 (or that would take effect prior to the first billing cycle for July 2010, if PEF elects to extend this Agreement pursuant to Section 1), except as otherwise provided for in Sections 7 and 10 of this Agreement. During the term of this Agreement, except as otherwise provided for in this Agreement, or except for unforeseen extraordinary costs imposed by government agencies relating to safety or matters of national security, PEF will not petition for any new surcharges, on a interim or permanent basis, to recover costs that are of a type that traditionally and historically would be, or are presently recovered through base rates." (*Stipulation and Settlement Agreement* at 4-5)

The proposed nuclear uprate costs are clearly those that would traditionally and historically be recovered in base rates. PEF may not circumvent the requirement by recovering base rate costs through the fuel clause. Further, as explained later, PEF's base rates already recover nuclear capacity-related costs. Thus, further recovery of these costs through the fuel clause would be double-recovery.

Q **ARE THERE ANY EXCEPTIONS TO THE BASE RATE FREEZE PROVIDED FOR IN THE AGREEMENT?**

A Yes, but none of those exceptions permit the recovery of CR3 uprate costs in fuel charges. The Agreement provides that PEF could petition the Commission for a base rate increase if its retail base rate earnings fall below a 10% return on equity, as reported on a Commission-adjusted or pro-forma basis, on a PEF monthly earning surveillance report. Next, PEF could petition for a base rate increase in the event that it was unable to recover costs associated with any catastrophic storms. Finally, PEF was allowed, by the Commission approved settlement agreement, to adjust base rates to recover the full non-fuel cost of Hines Unit 4, and at the same time, it would be allowed to roll-in to Hines Unit 2's 2006 full revenue requirements (excluding non-fuel O&M expense) to base rates. This adjustment would occur when Hines Unit 4 begins commercial operation, which is currently planned for December 2007.

Q WHAT WERE SOME OF THE OTHER ASPECTS OF THE SETTLEMENT AGREEMENT?

A. The 2005 base rate case initiated by PEF sought a base rate increase of $206 million. After full discovery the Commission approved a settlement which added Hines Unit 3 into the rate base with no increase in rates. The settlement has apparently had no serious adverse impact on PEF. **Exhibit ___ (JP-1)** is a copy of PEF's Rate of Return report for the 12 months ended December 31, 2006. Referring to page 11, PEF had sufficient cash flow to pay $235 million in dividends to its parent public utility, add $734 million in new construction to its rate base from operating revenues, and have $123 million left over while still earning 11% after taxes on the equity component of its capital structure. It would be very difficult to characterize the nuclear uprate as an extraordinary circumstance giving rise to the need for new cash to preserve PEF's financial integrity.

Q **IS PEF EARNING LESS THAN A 10% RETURN ON COMMON EQUITY FROM ITS RETAIL OPERATIONS?**

A No. As can be seen in **Exhibit ____ (JP-1)**, PEF's earned return on common equity was 11.00% in 2006. Thus, PEF does not qualify for a base rate adjustment under the terms of the Stipulation in Docket No. 050078.

Q **ARE ANY OF THE OTHER EXCEPTIONS THAT ALLOW PEF TO ADJUST BASE RATES RELEVANT?**

A No. PEF could seek higher base rate recovery of costs associated with any catastrophic storms. However, this particular exception is not relevant to the issues in this proceeding. The other exceptions are to allow the recovery of Hines Unit 2 and Unit 4 costs when the latter unit begins commercial operation. I shall discuss the relevance of these further exceptions later in this testimony.

IV. FUEL CLAUSE RECOVERY IS IMPROPER

Q **WHAT IS THE BASIS FOR YOUR ASSERTION THAT THE NUCLEAR UPRATE COSTS DO NOT QUALIFY FOR FUEL CLAUSE RECOVERY?**

A First, the nuclear uprate costs are not fuel-related and they are not volatile. Specifically, the nuclear uprate costs consist of three capital components:

Power uprate	$250 million
Transmission system modifications	$ 89 million
Modification to address point of discharge (POD) issues	$ 43 million

Total	$382 million

None of the above components are fuel-related costs as previously defined by the Commission. Fuel-related costs eligible for recovery through the fuel clause include:

1. The invoice price of fuel.
2. Any revisions to the invoice price.
3. Any quality and/or quantity adjustments to the invoice price.
4. Transportation costs to the utility's system, including detention or demurrage.
5. Federal and state taxes and purchasing agents' commissions.
6. Port charges.
7. All quantity and/or quality inspections performed by independent inspectors.
8. All additives blended with fuel prior to burning or injected into the boiler firing chamber along with fuel.
9. Inventory adjustments due to volume and/or price adjustments.
10. Fossil fuel-related costs normally recovered through base rates, but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers. Recovery of such costs should be made on case-by-case basis after Commission approval. (*In re: Cost recovery Methods for Fuel-Related Expenses, Docket No. 0850001- EI-B; Order No. 14546* dated July 8, 1985.) The Commission also found that costs eligible for fuel clause recovery must be volatile. Clearly, capital investments associated with generation and transmission

capacity additions are not volatile.

Q **WOULDN'T THE NUCLEAR UPRATE COSTS QUALIFY FOR FUEL COST RECOVERY UNDER ITEM 10 ABOVE?**

A No. Clearly, the proposed modifications anticipated to the transmission system are only incidentally related to the uprate project itself. However, it is a mis-leading and inaccurate over-simplification to assert that the sole purpose of the CR3 power uprate project is to reduce fuel costs. In its April 2007 *Ten-Year Site Plan* PEF has included the CR3 power uprate project as capacity that will be used to provide a reasonable reserve margin. Thus, PEF forecasts that this additional capacity is needed.

Further, the Stipulation in Docket No. 050078 anticipated that PEF would continue to make substantial investments in new electric generation and other infrastructure, and that the Stipulation would mitigate the impact of high energy prices. Specifically, the Stipulation states:

> WHEREAS PEF and the parties to this Agreement recognize that this is a period of unprecedented world energy prices and that this Agreement will mitigate the impact of high energy prices; (*Stipulation and Settlement Agreement* at 1).
>
> WHEREAS, the company must make substantial investments in the construction of new electric generation and other infrastructure for the foreseeable future in order to continue to provide safe and reliable power to meet the growing needs of customers in the state of Florida: (*Stipulation* and Settlement Agreement at 3).

Q PEF ASSERTS THAT THE CR3 POWER UPRATE PROJECT IS INNOVATIVE. DO YOU AGREE WITH PEF'S CHARACTERIZATION?

A No. Nuclear uprate projects are neither new nor innovative. As such, it is unnecessary to provide incentives, such as fuel clause recovery of the nuclear uprate capital costs, to encourage a utility to act in a prudent manner for the benefit of its ratepayers.

Q ARE NUCLEAR PLANT UPRATES NEW AND INNOVATIVE MEASURES?

A No. The Nuclear Regulatory Commission (NRC) published a report in June 2005 entitled, *Power Uprates for Nuclear Plants*. A copy of this report is enclosed as **Exhibit ____ (JP-2)**. As can be seen, the Report lists all of the nuclear uprate projects that the NRC has approved. As can be seen, the NRC has approved more than 100 uprates since 1977. This includes a 24 MW uprate of CR3 in 2002 (see Item 90). An additional 11 uprate projects are under review. Given that over 100 nuclear uprate projects have been approved, it would be misleading at best to claim that the pending CR3 uprate is new and innovative. For this reason, and because the settlement in Docket No. 050078 anticipated additional construction expenditures, PEF's request for fuel clause recovery should be denied.

V. DOUBLE-RECOVERY

Q YOU PREVIOUSLY STATED THAT THE PROPOSED FUEL CLAUSE RECOVERY OF THE CR3 POWER UPRATE PROJECT WOULD BE A DIRECT VIOLATION OF THE SETTLEMENT IN DOCKET NO. 050078. WOULD THAT STILL BE THE CASE, EVEN IF THE SPECIFIC CR3

POWER UPRATE-RELATED COSTS WERE NOT REFLECTED IN PEF'S BASE RATES?

A Yes. The Settlement does not require that nuclear uprate costs specifically be recognized in base rates as a condition for the base rate freeze. Specifically, it states that:

> "PEF will not petition for any new surcharges, on an interim or permanent basis, to recover costs that are of a type that traditionally and historically would be, or are presently, recovered through base rates." (Settlement and Stipulation Agreement at 4-5)

The CR3 power uprate costs are the same as other costs that PEF is currently recovering in base rates. For example, PEF is recovering a full return on and a return of the CR3 plant, which includes capitalized labor, equipment and cooling towers to dissipate the heat generated by the nuclear reactor. In addition, PEF's base rates also recover a return on and a return of transmission costs. Thus, all three components of the CR3 power uprate project are similar in nature to costs that PEF is currently recovering in its base rates. Any attempt to recover the same type of costs through the fuel clause would circumvent this specific provision of the rate case settlement and result in a double-recovery.

Q **DOES IT NECESSARILY FOLLOW THAT, BECAUSE NUCLEAR UPRATE COSTS WERE NOT SPECIFICALLY CONSIDERED IN PEF'S 2005 BASE RATE CASE, PEF IS SOMEHOW NOT RECOVERING THEM THROUGH BASE RATES?**

A No. The fact that a particular cost component may not have been specifically recognized in setting base rates does not mean that the utility is not recovering any new costs, such as the CR3 power uprate project.

Q **PLEASE EXPLAIN**

A A utility's base rates are set to recover non-fuel costs during a specific test year based on the amount of test year electricity sales. Base rate recovery includes equipment and labor costs, including both internal and third-party providers. However, once set, revenues and costs will change. Revenues will increase because of customer growth and higher sales. Capital additions will be made to serve that growing demand for electricity. However, these will be offset to some extent by the depreciation and retirement of existing investments. Operating expenses will also change. Some will increase while others will decrease.

To the extent that the company experiences sales growth, the additional sales will generate additional base revenue, thus offsetting further increases in base rate costs—such as the costs associated with projects that were not specifically recognized in the prior base rate case. This fundamental ratemaking principle is illustrated in **Exhibit____ (JP-3)**. This exhibit assumes that when base rates are set the utility has a base rate revenue requirement of $50,000 and electricity sales of 1,000 megawatthours (MWh). This results in an average base rate cost of $50 per MWh. Subsequent to the rate case, the utility's sales grow by 3%, from 1,000 MWh to 1,030 MWh. Because base rates are fixed at $50 per MWh, base rates generate $5,150. This is $1,500 above the level of base rate recovery assumed during the test year. In Year 2, the utility continues to experience a 3% growth in sales. This means it will recover

over $3,000 of additional base rate costs not otherwise reflected in the test year—when the utility's base rates were last set.

Thus, the application of fundamental ratemaking principles clearly demonstrates that a utility can recover increased base rate costs without the need for separate cost recovery. Because nuclear uprate costs are no different than the costs that were used to set PEF's current base rates, and because PEF is selling more electricity than during the test year in its last rate case, and recognizing PEF's recent earnings, allowing PEF to collect CR3 nuclear uprate project costs through the fuel clause would result in a double-recovery.

Q WOULD REJECTING PEF'S PROPOSAL TO COLLECT NUCLEAR UPRATE COSTS THROUGH THE FUEL CLAUSE DENY PEF THE OPPORTUNITY TO RECOVER NUCLEAR UPRATE COSTS?

A No. Given the ratemaking dynamics as discussed earlier, there is no rational basis to assert that piecemeal recovery (through the fuel clause) of particular new investments (e.g., CR3 nuclear uprate costs) is needed to allow a utility to recover these costs.

Q DO YOU HAVE ANY PEF-SPECIFIC EXAMPLES WHERE ADDITIONAL INVESTMENT WAS ADDED WITHOUT THE NEED TO IMPLEMENT HIGHER RATES?

A Yes. The Settlement and Stipulation in the 2005 rate case contemplated both sales and revenue growth and continuing rate base investment to serve the growing load. Acknowledging these terms, PEF agreed to continue the existing base rates despite the many additions to rate base, such as Hines Unit 3, that had occurred since the prior case. Despite the additional investments, PEF's actual ROE was still above the 10% ROE floor. This clearly demonstrates that PEF has sufficient revenues to recover nuclear uprate costs without fuel clause recovery.

Further, PEF will have more than ample cost recovery due to the ratemaking treatment of Hines Units 2 and 4. As previously stated, Hines Unit 2 will be rolled-in to base rates at its 2006 cost of service, while Hines Unit 4 will be rolled-in to base rates at 100% of its cost of service on its commercial operation date, which is estimated to occur this December. However, between 2006 and 2008, when Hines Unit 2 costs would be reflected in base rates, PEF will have depreciated a portion of Unit 2 investment, thereby reducing the associated revenue requirement. By holding base rates constant while reducing the revenue requirement, PEF will generate additional margins, which can be used to offset higher costs. A similar benefit will be realized with Hines Unit 4 after it begins commercial operation.

Given the dynamics of ratemaking and these specific facts applicable to PEF, PEF does not need a "piecemeal" rate increase to recover nuclear uprate costs just because they were incurred subsequent to its last rate case. If PEF is unable to earn at least a 10% ROE, then the door is open to a base rate adjustment. Further, PEF will have an opportunity to seek cost recovery after the termination of the base rate freeze. Most of the costs will be incurred after 2010.

VI. PEF'S PROPOSED COST RECOVERY IS IMPROPER

Q PLEASE EXPLAIN WHY PEF'S PROPOSED COST RECOVERY OF CR3 NUCLEAR UPRATE PROJECT COSTS IS IMPROPER.

A First, all of the proposed uprate costs are fixed costs and relate directly to the rated capacity of the nuclear unit. Thus, they are properly considered demand-related costs. Demand-related costs should be allocated and recovered on a demand basis under all accepted conventions of cost causation, cost of service ratemaking, and long standing Commission practice.

PEF is proposing to recover these costs through the fuel clause. Under the fuel clause, costs are recovered relative to loss-adjusted MWh sales. In effect, this would allocate demand-related costs on an all energy basis. Such an approach is improper because it would shift cost responsibility among customer classes that is inconsistent with basic cost causation principles. Further, it would be inconsistent with PEF's allocation of other nuclear and transmission base rate costs, which are allocated among customer classes on a demand basis. The second reason for rejecting PEF's cost recovery proposal is that it proposes to amortize the CR3 nuclear uprate project costs over 10 years. However, despite the 10-year amortization period, the company is projecting fuel savings through 2036, or 28 years. This claim assumes that the Company will be successful at extending the life of CR3 to 2036. PEF admits (in response to OPC's 1st set of Interrogatories 5, 7 and 8) that the MUR modification, the transmission upgrades, and the cooling towers are designed for the extended life of the plant. Thus, it would be fundamentally improper to allow PEF to recover capital costs over 10 years for plant investment and related capacity that will be in service through 2036 because it would require current ratepayers to subsidize investments that will benefit ratepayers well into the future. These capital costs should be recovered over the expected remaining life of the assets.

Q **PLEASE EXPLAIN HOW FUEL CLAUSE RECOVERY OF CR3 NUCLEAR UPRATE COSTS WOULD RESULT IN IMPROPER COST SHIFTING BETWEEN CUSTOMER CLASSES.**

A Nuclear base rate costs are allocated to customer classes using a methodology which reflects primarily the coincident peak demands of the different classes. Specifically, PEF uses the Twelve Coincident Peak and One-Thirteenth Average Demand (12CP&1/13th AD) method to allocate nuclear base rate costs. This is the same method PEF uses to allocate all production demand-related costs. **Exhibit ___ (JP-4)** (which is an excerpt from PEF's CCRC filing in Docket No. 060001-EI) comparison between the demand allocation factors (column 10) and the energy corresponding allocation factors if nuclear uprate costs were recovered through the demand fuel clause (shown in column 8 under Annual Average Demand). As can be seen, the demand allocation factors are significantly different than the energy allocation factors, for all customer classes. The differences 16% (for the General Service Demand Class) to 83% (for the Lighting Class). Thus, fuel clause recovery would not be consistent with the cost-causation that is reflected in PEF's demand allocation method. PEF's fuel clause recovery proposal would create significant and inappropriate shifts in the cost responsibility of all customer classes.

Q **DOES THE COMMISSION DIFFERENTIATE BETWEEN THE ALLOCATION OF NUCLEAR BASE RATE COSTS AND OTHER**

TYPES OF PRODUCTION DEMAND-RELATED COSTS?

A No. The Commission has previously authorized the recovery of post-9/11 security measures through the Capacity Cost Recovery Clause (CCRC). Under the CCRC, these costs are allocated in the same manner as all other production base rate costs; that is, using the allocation methodology previously approved in the utility's most recent base rate case.

In addition, the Commission recently adopted a new rule authorizing the recovery of pre-construction and construction costs of new nuclear plants. Under this new rule, pre-construction and construction costs of new nuclear plants would be recovered through the CCRC. (Docket No. 060508-EI - Proposed Adoption of New Rule Regarding Nuclear Power Plant Cost Recovery.) This rule was adopted on March 20, 2007 and became effective April 8, 2007.

There is no justification to treat nuclear uprate costs any differently than all other nuclear base rate costs. Because recovery through the fuel clause would unnecessarily shift cost responsibility by customer class and would be inconsistent with the Commission's treatment of post-9/11 security costs and nuclear pre-construction and construction costs, PEF's proposal should be rejected.

Q WHY ELSE IS IT INAPPROPRIATE TO RECOVER NUCLEAR BASE RATE COSTS ON THE BASIS OF LOSS-ADJUSTED SALES?

A As previously stated, the capacity of the proposal uprate is needed to enable PEF to meet its projected peak demands and to provide appropriate reserve margins. Thus, this cost should be treated no differently than any other production demand-related costs.

Q PEF ASSERTS THAT THE NUCLEAR UPRATE COSTS WILL SAVE FUEL COSTS. IS THIS A REASON FOR RECOVERING THE NUCLEAR UPRATE COSTS THROUGH THE FUEL CLAUSE?

A No. The concept of allocating base rate costs (which are traditionally allocated using a demand-based cost allocation method) on the basis of fuel savings has not only been rejected by the utility that originally proposed such an allocation, but it has also been rejected by the Commission.

Specifically, Florida Power and Light Company (FPL) initially allocated its investment in St. Lucie Unit 2 relative to loss-adjusted kWh sales on the grounds that the unit would produce substantial fuel savings. However, in its last base rate case (Docket No. 050045-EI), FPL rejected that approach and allocated the St. Lucie 2 base rate costs using the same methodology as all other production demand-related costs. (Docket No. 050045-EI, *Testimony of Rosemary Morley* at 17-18.)

This Commission has also rejected the concept of allocating production demand-related costs relative to fuel savings. This was the premise underlying the Equivalent Peaker (EP) method of allocation. Under the EP method, capital costs in excess of the cost of a combustion turbine were assumed to be related to fuel cost savings and thus, were allocated on energy. However, in Docket No 891345-EI, the Commission stated that:

> "The equivalent peaker method implies a refined knowledge of costs which is misleading, particularly as to the allocation of the plant costs to hours beyond the break-even point. (Gulf

Power Company, Order. No. ~~234573~~ 23573 at 48)".

In other words, the Commission recognized that the extra plant costs associated with generating units that provide fuel cost savings is at odds with the planning process because all production from a specific plant (i.e., kWh sales) is not the critical factor in deciding what type of capability to install.

Q **WHY ELSE SHOULD THE COMPANY'S COST RECOVERY PROPOSAL BE REJECTED?**

A PEF concedes that the nuclear uprate costs will last for the duration of the extended life of CR3, which is projected to have a 28 year remaining useful life. This assumes that the company is successful in extending the life of CR3 to 2036. Thus, its proposal to recover these costs over just 10 years would fail to match the costs of the nuclear uprate project with the associated life long benefits. The mismatch would be even more severe with the projected transmission upgrades. Transmission investments typically have useful lives ranging from 40 to 58 years. Thus, by accelerating cost recovery to only 10 years, current ratepayers would be paying the entirety of the costs while the vast majority of benefits would inure to future ratepayers (for an additional 18 years). The failure to match the recovery of the costs with the benefits, thus, would create intergenerational inequities and should be rejected.

Q **WHAT CONSIDERATION HAS PEF GIVEN TO THE FACT THAT CR3 IS JOINTLY OWNED WITH SEVERAL MUNICIPALITIES?**

A PEF witness, Mr. Waters, acknowledges at page 6 of his testimony that actually the CR3 capacity dedicated to retail service is 788 MW not the

900 MW alleged in the petition. In other words, retail customers are responsible for approximately 88% of the CR3 capacity. Nevertheless, PEF is proposing to recover 100% of the CR3 uprate costs from retail customers. In his deposition, Mr. Waters indicated that the issue of participation by the other CR3 owners had not yet been resolved.

Q **IF THE COMMISSION WERE TO ALLOW PEF TO RECOVER CR3 NUCLEAR UPRATE PROJECT COSTS THROUGH A SEPARATE COST RECOVERY MECHANISM, HOW SHOULD PEF'S PROPOSAL BE MODIFIED?**

A If the Commission, nevertheless, approves PEF'S request for a separate cost recovery of CR3 nuclear uprate costs, then its proposal should be modified in several respects. First, the nuclear uprate costs should be amortized over the remaining useful life of CR3. This would property match the cost recovery with the associated benefits, which are projected to occur through 2036. Regardless of the treatment accorded to the nuclear uprate and POD costs, transmission costs should be amortized over a period not less than 40 years, consistent with the useful life of transmission facilities. Second, only the portion of CR3 costs allocable to retail customers should be collected. Finally, consistent with this Commission's treatment of other nuclear-related base rate costs, recovery should be through the CCRC, rather than the fuel clause. This would provide a more appropriate allocation of these cost-shifting among PEF's various customer classes.

Q **DOES THE CONCLUDE YOUR DIRECT TESTIMONY?**

A Yes, it does.

APPENDIX A

<u>Qualifications of Jeffry Pollock</u>

Q **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A Jeffry Pollock. My business mailing address is, 12655 Olive Blvd, Suite 335, St. Louis, Missouri 63141.

Q **WHAT IS YOUR OCCUPATION AND BY WHOM ARE YOU EMPLOYED?**

A I am an energy advisor and President of J.Pollock, Incorporated.

Q **PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.**

A I have a Bachelor of Science Degree in Electrical Engineering and a Masters in Business Administration from Washington University. At various times prior to graduation, I worked for the McDonnell Douglas Corporation in the Corporate Planning Department; Sachs Electric Company; and L. K. Comstock & Company. While at McDonnell Douglas, I analyzed the direct operating cost of commercial aircraft.

Upon graduation, in June 1975, I joined Drazen-Brubaker & Associates, Inc. (DBA). DBA was incorporated in 1972 assuming the utility rate and economic consulting activities of Drazen Associates, Inc., active since 1937. From April 1995 to November 2004, I was a managing principal at Brubaker & Associates (BAI).

During my tenure at both DBA and BAI, I have been engaged in a wide range of consulting assignments including energy and regulatory matters in both the United States and several Canadian provinces. This includes preparing financial and economic studies of investor-owned, cooperative and municipal utilities on revenue requirements, cost of service and rate design, and conducting site evaluation. Recent engagements have included advising clients on electric restructuring issues, assisting clients to procure and manage electricity in both competitive and regulated markets, developing and issuing request for proposals (RFPs), evaluating RFP responses and contract negotiation. I was also responsible for developing and presenting seminars on electricity issues.

I have worked on various projects in over 20 states and in 2 Canadian provinces, and have testified before the Federal Energy Regulatory Commission and the state regulatory commissions of Alabama, Arizona, Colorado, Delaware, Florida, Georgia, Illinois, Iowa, Louisiana, Minnesota, Mississippi, Missouri, Montana, New Jersey, New Mexico, Ohio, Pennsylvania, Texas, Virginia and Washington. I have also appeared before the City of Austin Electric Utility Commission, the Board of Public Utilities of Kansas City, Kansas, the Bonneville Power Administration, Travis County (Texas) District Court, and the U.S. Federal District Court.

Q **PLEASE DESCRIBE J.POLLOCK, INCORPORATED.**

A J.Pollock assists clients to procure and manage energy in both regulated and competitive markets. The J.Pollock team also advises clients on energy and regulatory issues. Our clients include commercial, industrial, and institutional energy consumers. Currently, J.Pollock has offices in St. Louis, Missouri and Austin, Texas.

CHAIRMAN EDGAR: And as always, I would ask that friendly cross be limited.

Mr. Brew, any questions for this witness on direct -- excuse me, on cross? I apologize, on cross.

Mr. Twomey? No.

Mr. McGlothlin? No.

Mr. Wright? No questions.

Ms. Triplett.

MS. TRIPLETT: I have some friendly cross.

THE WITNESS: Friendly cross or friendly fire?

CROSS-EXAMINATION

BY MS. TRIPLETT:

Q. Before I begin, do you have a copy of your deposition transcripts?

A. I did not bring one.

Q. Okay. I'm going to give those to you.

To begin with, I want to ask some questions about PEF's CR3 uprate project and its benefits, setting aside the method of cost recovery. First, you would agree that if the CR3 uprate produces the expected 180 megawatts of capacity, that it will be beneficial to ratepayers; is that correct?

A. I would agree with that, yes.

Q. And you would also agree that if the CR3 uprate works to produce the fuel savings that PEF has presented, the project will be beneficial to ratepayers; is that right?

A. If the company can rely on the additional capacity, then it should produce significant fuel savings.

Q. And you have no reason to dispute Progress Energy's cost estimates presented in this case; is that right?

A. No.

Q. And you also have not done any independent analysis of Progress Energy's fuel saving projections; is that right?

A. I've done a brief analysis, but, no, I've not tried to remodel the system to determine the reasonableness of the assumptions.

Q. So you have no reason to dispute the methodology used to determine those fuel savings forecasts; is that right?

A. No, I have no dispute with the methodology.

Q. Okay. Next, Mr. Pollock, I would like to discuss Commission Order 14546, which is the order pursuant to which the company is requesting fuel clause recovery; is that right?

A. Yes.

Q. And in fact, you discuss this order on pages 8 through 10 of your prefiled testimony. I'll let you get there.

A. Okay.

Q. And you would agree with me that Item 10 in that order is designed to allow recovery of costs that would normally be recovered through base rates, but which were not anticipated in current base rates, that will result in fuel savings; is that right?

A. That's exactly what the language says, yes.

Q. And Item 10 refers to recovery on a case-by-case basis; is that right?

A. That's right. The Commission is free to evaluate the facts and circumstances of every application that comes before it to determine whether to apply the fuel clause recovery.

Q. So it is your position that when the Commission is reviewing petitions under Item 10 that it can consider all facts and circumstances surrounding the utility and its request; is that right?

A. I believe that's implicit in any interpretation of a past Commission order, particularly one of such vintage as this particular order. As the Commission is well aware, circumstances change, and the Commission and others should be responsive to changes in circumstances. So I think the Commission is free to interpret its order differently. It's free to modify its order. It's free to do whatever is appropriate to serve the public interest.

Q. And you think that the Commission can consider whatever evidence is presented to it and make a decision based on that evidence; is that right?

A. Yes. I believe the Commission has broad authority to consider all the facts and circumstances in every application that comes before it.

Q. And you are not aware of any limit to what the Commission can consider in doing this case-by-case analysis; is that right?

A. I'm not sure what limit means. It depends on whatever facts and circumstances are relevant or the Commission deems relevant.

Q. Well, if you can turn in your deposition to page 13, lines 11 through 13. I asked you the question, "Is there any limit to what the Commission can consider in doing its case-by-case analysis?" And you answered, "I'm not aware of any limit"; is that right?

A. Right. As I stated, the Commission can decide what the limits are. The Commission is not bound to only look at narrow circumstances. They can define what facts and circumstances they want to look at in order to approve an application.

Q. So you believe that the Commission adopted a policy under Item 10 of Order 14546 that provides no express standard to guide utilities?

A. I think it provides at least an indication of what the Commission might allow, but I think the Commission is again free the interpret its order or apply its order differently, depending upon the circumstances surrounding a specific application.

Q. If that's your position, can you give me an order that the Commission considered any other factor in its analysis of a utility's request under Item 10 other than factors listed in Item 10 itself?

A. I don't think in any of the six or seven previous applications that we were talking about issues of the kind of magnitude that we're talking about here, so I would say that that is a clearly different situation than the Commission has ever addressed.

Q. So that's no, you cannot point me to an order?

A. I cannot point you to a specific order where the Commission took anything into account other than the fact that they felt this was a good deal and the amount of money was small and the payback was very quick. And that's a circumstance that's totally different in this case.

Q. Okay. Now, moving on to the cost allocation issues, it is your position that recovery of the CR3 uprate costs should be allocated through the capacity clause rather that the fuel clause; is that right?

A. Well, let me get that straight. If the Commission says that they're going to permit clause recovery as opposed our primary recommendation, which is to deny the petition, then we think it makes more sense and is consistent with the way nuclear capacity costs are handled to recover it through the capacity clause.

Q. But cost allocation is not addressed specifically in Order 14546; is that right?

A. That's correct. The presumption is that the Commission decides based on the merits of the case to allow fuel clause recovery.

Q. And that's because Order 14546 really addresses fuel cost recovery issues and not base rate cost allocation issues; is that right?

A. I would agree. That's the fundamental issue in this case.

Q. And you would also agree that Order 14546 does not address a cap on the total amount of costs or that the costs not be above a certain amount; is that right?

A. Well, I think there's certainly nothing in the order that suggests any cap. I think that's what the case-by-case decision means. The Commission can decide if it wants to impose a cap.

Q. But again, there's not an express cap specified in the order; is that correct?

A. No, but again, the Commission has broad authority to interpret its orders.

Q. Mr. Pollock, I would now like to ask you some questions about your testimony beginning on page 10 relating to PEF's 2005 rate case settlement.

A. Okay.

Q. You relied on PEF's 2005 rate case settlement agreement in preparing your testimony; is that right?

A. I referred to it extensively, yes.

Q. And this settlement agreement was signed in 2005; is that correct?

A. Yes.

Q. Order 14546 was issued in 1985; is that right?

A. Yes.

Q. And Order 14546 was in effect when the rate case settlement agreement was signed; is that right?

A. Yes.

Q. And the rate case settlement agreement does not explicitly stop the policy or rule in Order 14546 from applying; is that right?

A. I think that's a matter of interpretation, the interpretation being what does the provision mean in the settlement that says that you're not going to try to recover costs that are normally recovered in base rates through a separate cost recovery mechanism. I think that's the fundamental issue in this case.

Q. Okay. Well, let's just turn to page 17 of your deposition transcript.

A. Okay.

Q. And on lines -- starting on line 21, I asked the question, "And the rate case agreement does not explicitly preclude the application of Order No. 14546; is that right?"

Answer: "I don't know that I would agree with that." And then you say, "No, it doesn't stop the rule from applying." Did I read that correctly?

A. That's correct.

Q. Mr. Pollock, can you turn with me to page 9, line 17, of your testimony?

A. Okay.

Q. And this is where you cite Item 10 of Order 14546. And the first part of that item states, "Fossil fuel-related costs normally recovered through base rates." Did I read that correctly?

A. Yes.

Q. If a cost qualifies under Item 10 of Order 14546, it is your position that the settlement agreement does not preclude recovery; is that right?

A. Say that again, please.

Q. If a cost qualifies under Item 10 of Order 14546, it is your position that the settlement agreement does not preclude recovery of that cost?

A. Recovery how?

Q. Recovery through the fuel clause.

A. I think the settlement does.

Q. Well, let's go to page 19 of your deposition transcript.

A. Okay.

Q. And starting on line 2, I asked you the question, "So even if it's a cost that qualifies under Item 10 of Order 14546, it's your position that the settlement agreement precludes recovery under Order 14546?"

And your answer, "I don't think it precludes recovery."

A. Right. That's what that says. And the interpretation of that is, it doesn't preclude you from recovering the cost. It wasn't specifically saying it doesn't preclude recovery through the fuel -- it specifically doesn't say that it -- fuel clause recovery. In that context, we're saying you can still recover the cost even if you don't have fuel clause recovery.

Q. Mr. Pollock, let's discuss your testimony regarding the need for the CR3 uprate and the 2007 Ten-Year Site Plan. That's on page 10 of your prefiled testimony.

A. Okay.

Q. Lines 5 through 10.

A. Yes.

Q. Is it your position that because the CR3 uprate megawatts were included in the 2007 Ten-Year Site Plan, that the sole purpose of the uprate must be for reliability?

A. No, I'm not taking that position. However, I think it's an oversimplification to say that the sole purpose of the investment is for fuel savings, because as the Commission has heard testimony today, every megawatt of capacity provides reliability. This uprate will be no different than any other plant that also provides fuel savings that also provides reliability.

Q. But you do agree that the need for this project was granted on the basis of an economic need?

A. I understand the order said that, and if you look at it in isolation, yes, there seems to be an economic need. However, that's not to suggest that there aren't other factors involved in determining what causes a plant to be built. Once it is built, it will provide capacity, it will provide reliability, and it will help the company to meet the 20 percent reserve margin criteria in light of any additional load.

Q. In fact, the order granting the need determination for this project stated, "The need for the CR3 uprate is an economic need, not a reliability need"; is that right?

A. Yes. And looking at that in isolation and understanding that at that time, the company had other plants on the books that it was going to build to provide the reliability, one could come to that conclusion. However, as we've heard testimony today, the company's plans are not static. The company changed its plans. It now doesn't need 180 megawatts of capacity that it was planning to install in the later years because it will have this 180 megawatts associated with the nuclear uprate.

Q. In support of your opinion as to why PEF did this project, you only reviewed the 2007 Ten-Year Site Plan; is that right?

A. Primarily, yes.

Q. And you don't recall whether you reviewed the 2006 site plan when you prepared your --

A. After my deposition I did review it, yes.

Q. Well, at the time of your deposition, you did not know whether the uprate was included in the 2006 Ten-Year Site Plan.

A. Yes, that's right.

Q. Do you know now?

A. Yes. It was not identified in the 2006 plan.

Q. You've cut out a lot of questions.

A. Just the facts.

Q. All right. The last topic is the subject of innovative uprates. You have concluded that uprates are relatively common and therefore not new or innovative; is that right?

A. Yes.

Q. You are not a nuclear engineer, are you, Mr. Pollock?

A. I am not.

Q. And these other uprates that I believe you list in your Exhibit JP-2 to your testimony, you were not involved in any of those uprates; is that right?

A. I was not, no.

Q. And beyond the comparisons that are in the report attached to your testimony, you did not conduct any comparisons of CR3's uprate to these other uprates; is that right?

A. Well, I wouldn't quite go that far. I think if you look at that exhibit, specifically Exhibit 17, and you look at the amounts of megawatts associated with uprates at various plants, you're going to see that there are several uprates there that in terms of total megawatts exceed the 180 megawatts that we're talking about in this proceeding. So I would say based on that analysis and observation of the various uprates -- for example, you can look at a number that are over 200 megawatts. If you turn over to page 8, there's two pressurized water reactor plants that are looking to upgrade 211 megawatts.

Uprates have been done for years, and there have been some uprates that have been of a similar or same or greater magnitude than the uprates we're talking about now. And I think it's a little incomplete to say that those uprates weren't driven by changes in technology and things that made this stuff possible. In that sense, this uprate is really no different than any of the ones that have preceded it, based on this analysis.

Q. Okay. Let me just ask you to turn to page 24 of your deposition.

A. Twenty-four.

Q. Yes.

A. Okay.

Q. And starting at line 9, just so the record is clear, in your deposition I asked you, "And you did not conduct any comparisons of the other uprates to the CR3 uprate; is that right?" And your answer was, "Not beyond the comparisons that are in the report attached to my testimony."

A. That's correct. That's the comparisons that I just made.

Q. And in fact, you've not done a formal comparison from an engineering perspective of those uprates to the CR3 uprate; is that right?

A. No. But in reading the NRC material, it's very obvious that technology is driving a lot of these changes, particularly the ones where you see the letter E by the -- in the uprate code, which stands for an extended outage. Those are not things that are done quickly or without a lot of money. They're done because you're talking about major changes in technology in specific components of the plant, which again is similar to what we're talking about here.

MS. TRIPLETT: Okay. I have no further questions. Thank you.

CHAIRMAN EDGAR: Commissioners, any questions? Commissioner McMurrian.

COMMISSIONER McMURRIAN: I have one or two.

If the Commission ultimately did not allow recovery through the fuel clause of this project, do you think the company should pursue this project anyway?

THE WITNESS: Absolutely. I think that to the extent that it's shown that customers will benefit, I think customers should always come first in the decision as to whether or not to proceed with a project or not. And clearly, these customers deserve to come first. Yes, the project should be done.

COMMISSIONER McMURRIAN: And I guess there's just one clarification to that. Even if that would result in base rate recovery, you would still have that same opinion?

THE WITNESS: Yes. If the Commission decided that the company needed a base rate adjustment and the company went through the process of determining that a base rate adjustment was appropriate, we would obviously scrutinize the filing as the Commission staff and all the parties. But, yes, if that was the appropriate determination, then that's where the money would go, and that's were it should go.

COMMISSIONER McMURRIAN: Thank you, Mr. Pollock. That's all.

CHAIRMAN EDGAR: Questions from staff?

MS. BENNETT: No.

CHAIRMAN EDGAR: No questions. Okay. Mr. McWhirter?

MR. McWHIRTER: No redirect.

CHAIRMAN EDGAR: No redirect. Okay. Let's take up the exhibits.

MR. McWHIRTER: I would like to offer the Pollock exhibits. I believe they're 16, 17, 18, and 19, if I remember correctly.

THE WITNESS: Sounds right to me.

CHAIRMAN EDGAR: Yes. Seeing no objections, we will enter Exhibits 16, 17, 18, and 19 into the record.

(Exhibits 16, 17, 18, and 19 were admitted into the record.)

CHAIRMAN EDGAR: Any other matters for this witness? Seeing none, the witness is excused.

THE WITNESS: Thank you for your time.

CHAIRMAN EDGAR: Thank you. Okay. We have three remaining witnesses we will take up tomorrow, OPC witnesses Merchant and Lawton, and then Mr. Portuondo on rebuttal. We will come back and begin with witness Merchant at 9:30 tomorrow morning.

Before we adjourn for the day, any other matters that we need to discuss?

Seeing none, okay. Thank everybody for their patience and cooperation, and we will be back tomorrow morning at 9:30.

(Proceedings recessed at 6:20 a.m.)

(Transcript continues in sequence in Volume 3.)

CERTIFICATE OF REPORTER

STATE OF FLORIDA:

COUNTY OF LEON:

I, MARY ALLEN NEEL, Registered Professional Reporter, do hereby certify that the foregoing proceedings were taken before me at the time and place therein designated; that my shorthand notes were thereafter translated under my supervision; and the foregoing pages numbered 177 through 380 are a true and correct record of the aforesaid proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor relative or employee of such attorney or counsel, or financially interested in the foregoing action.

DATED THIS 14th day of August, 2007.

Mary Allen Neel

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