BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of

DOCKET NO. 070001-EI

FUEL AND PURCHASED POWER
COST RECOVERY CLAUSE WITH
GENERATING PERFORMANCE INCENTIVE
FACTOR.
_______________________________________/

VOLUME 1

Pages 1 through 189

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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, November 6, 2007
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
TIME:	Commenced at 10:06 a.m.
REPORTED BY:	LINDA BOLES, CRR, RPR Official FPSC Reporter (850) 413-6734

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NORMAN H. HORTON, JR., ESQUIRE, Messer, Caparello & Self, P.A., Post Office Box 15579, Tallahassee, Florida 32317, appearing on behalf of Florida Public Utilities Company.

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APPEARANCES (Continued):

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I N D E X

WITNESSES

EXHIBITS

NUMBER:		ID.	ADMTD.
1	Comprehensive Exhibit List	33	33
2	Staff Composite Exhibit 2	33	33
3	(Confidential) Staff Composite Exhibit 3	33	33
4	WG-1T	34	34
5	WG-2T	34	34
6	WG-3T	34	34
7	LC-1R	46	46
8	LC-1P	46	46
9	JM-1T	87	87
10	JM-1P	87	87
11	RMO-1T	88	88
12	RMO-1P	88	88
13	GJY-1	104	166
14	GJY-2	104	166
15	***This exhibit was withdrawn***		
21	KMD-6	104	166
24	CMM-2	13	13

EXHIBITS

NUMBER:		ID.	ADMTD.
25	CMM-2	13	13
26	MK-1	13	13
46	Additional Stipulations	7	33
47	(Partial Confidential) Gulf's Responses to Staff's 1st and 4th Interrogatories	10	
48	(Late-Filed) FPL Hedging Percentages (Financial/ Physical) 2007	102	
49	(Late-Filed) PEF Hedging Percentages (Financial/ Physical) 2007	102	
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P R O C E E D I N G S

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CHAIRMAN EDGAR: And we will move on and take up the 01 docket. So with that, I open the record for the '01 docket. And we're ready.

MS. BENNETT: Staff would note, Madam Chair, that there are additional stipulations that were entered into by the parties after the Prehearing Order. You have a copy of those additional stipulations, as do all of the parties. It might be appropriate to ask if all the parties have seen these stipulations and continue to agree with them.

CHAIRMAN EDGAR: Okay. Realizing that we have a number of parties in this docket and, as Ms. Bennett has described, there have been, my phrase, recent changes to some of those proposed stipulations, do all counsel have what they need and are there any concerns, objections, issues? And I'm seeing none.

MR. BURGESS: No.

MS. BENNETT: Then I'm asked that this be entered into -- on the Comprehensive Exhibit List as Number 46. And when we take up the Comprehensive Exhibit List, I will ask that it be entered into the record as Exhibit Number 46.

CHAIRMAN EDGAR: Okay. So we will mark the document labeled Additional Stipulations as Exhibit Number 46.

(Exhibit 46 marked for identification.)

MS. BENNETT: Thank you, Madam Chair.

I want to note for the record also that there are several witnesses that have been excused in this proceeding. As we get to those witnesses, the parties' attorney will ask that those witnesses' testimony and their exhibits be moved into the record. Cross-examination has been waived for those witnesses excused.

I'd also like to note that because we have agreed to defer Issue 13A to 2008, Mr. Butler and Mr. Burgess would like to withdraw certain of the testimony that has been submitted into this record, and now would be an appropriate time to do that.

CHAIRMAN EDGAR: Mr. Butler.

MR. BUTLER: Thank you. For FPL, we would ask that the following testimony be withdrawn from the record and not inserted into the record as though read.

In rebuttal testimony, which is the easier ones, it would be the entire testimony of Witness William Avera and Korel Dubin. Then on direct testimony it would be for Witness Terry Jones, Page 8, Line 10, through Page 18, Line 12 of his direct testimony. And for Witness Korel Dubin it would be Page 5, Line 20, through Page 8, Line 4. Thank you.

CHAIRMAN EDGAR: Thank you.

Mr. Burgess.

MR. BURGESS: Thank you, Madam Chair. For the Public

Counsel's Office the testimony, the prefiled testimony filed by Aaron Rothschild we would ask be withdrawn in its entirety. Thank you.

CHAIRMAN EDGAR: Thank you.

MS. BENNETT: And then the Comprehensive Exhibit List, which includes the two staff composite exhibit lists as well as now Item 46, there have been no objections to the Comprehensive Exhibit List nor to entering the composite exhibit list into the record. When we get to the record on this proceeding, I will ask that they be admitted into the record. It is staff's understanding that Gulf will also be asking for additional exhibits to be entered into the record at that time. They would be composite Exhibit 47, and Mr. Badders might go ahead and identify that composite Exhibit 47.

CHAIRMAN EDGAR: Mr. Badders.

MR. BADDERS: Thank you. As composite Exhibit 47 Gulf would like to add Gulf's responses to staff's first and fourth set of interrogatories. The first set is numbered 1 through 10 and the fourth set is numbered 17 through 23. And copies of these were provided in discovery to all parties and we also have additional copies here today for the court reporter and any other parties.

CHAIRMAN EDGAR: Okay. The specific interrogatory responses noted by Mr. Badders will be marked as Exhibit 47 proposed by Gulf.

(Exhibit 47 marked for identification.)

MR. BADDERS: Thank you. And three of the items on the first set are confidential, and we will provide that to the court reporter.

CHAIRMAN EDGAR: Thank you.

MR. BUTLER: Madam Chairman, regarding the exhibit list, let me point out that Exhibit 15 on staff's Comprehensive Exhibit List is an exhibit to Witness Terry Jones' testimony that would be withdrawn along with his prefiled testimony.

MR. BURGESS: Madam Chair, as well, in a similar vein, Exhibit 45 by Witness Rothschild, the same category, I know it was implied as part of the withdrawal, but explicitly we would ask that that be withdrawn as well.

CHAIRMAN EDGAR: Thank you. And I appreciate you bringing that to our attention. And as noted on the Comprehensive Exhibit List, those exhibits listed as 15 and as 45 will be withdrawn.

MS. BENNETT: There are outstanding motions and petitions on confidentiality. They will be provided to the Prehearing Officer at a later date.

I do want to remind parties that at times we may be discussing confidential matters, and when we discuss confidential matters, especially in the hedging docket, there are some numbers that the parties provide that they deem to be confidential. We need to take great care to protect those numbers from being spoken aloud.

CHAIRMAN EDGAR: And, Ms. Bennett, just so we are clear, we have not entered the prefiled testimony of the witnesses that have been excused. Is it your recommendation that we do that as we come to those witnesses in order or in advance?

MS. BENNETT: I recommend that we do them in order because there are multiple witnesses who are excused but several who are not.

CHAIRMAN EDGAR: Okay. And so for, for the orderliness of the record we will enter the prefiled testimony of excused witnesses and any exhibits that are attached as we come. We will work our way through the witness list. And for the two parties that have prefiled testimony that we will be excerpting from what will be entered, if you'll help me when we come to those appropriate points as well so that we are all in the same place.

Any other matters, Ms. Bennett?

MS. BENNETT: Yes, Madam Chair. Major Damund Williams from the Federal Executive Agency has asked that he be excused from the proceeding on Wednesday. I'll let him speak to that matter.

CHAIRMAN EDGAR: Mr. Williams or Captain Williams -- Major Williams. I'm sorry.

MAJOR WILLIAMS: Yes, ma'am, Madam Chair. Given the stipulations, we do ask that we be excused from the rest of the proceedings. Actually if we could be excused for the rest of today, we'd appreciate it.

CHAIRMAN EDGAR: You don't want to join us for the rest of the day?

MAJOR WILLIAMS: I would like to. I enjoy you all's company immensely, but there are other matters that are pressing that I have to get back to.

CHAIRMAN EDGAR: I understand. You are always welcome here. The attorneys for the federal agencies will be excused from the rest of the proceeding. Thank you.

MAJOR WILLIAMS: Thank you, ma'am.

MR. HORTON: Madam Chairman.

CHAIRMAN EDGAR: Yes, sir.

MR. HORTON: I'm sorry. I believe that all of the issues for Florida Public Utilities have been stipulated. And if our witnesses, if we could insert their testimony now, I would also ask to be excused from the remainder of the proceeding rather than wait through other testimony.

CHAIRMAN EDGAR: Okay. Give me, give me a moment to get the right things in front of me and we'll see if we can address that. Okay. So that would be Witnesses Martin and --

MR. HORTON: Khojasteh.

CHAIRMAN EDGAR: Thank you.

MR. HORTON: Actually Mr. Khojasteh adopted the testimony of Ms. Martin, so we would insert that testimony as his, all of it.

CHAIRMAN EDGAR: Okay. Are there any objections or concerns from staff about going ahead and entering the prefiled testimony of Witness Martin and Khojasteh?

MR. HORTON: Khojasteh.

CHAIRMAN EDGAR: Khojasteh. Sorry.

MR. HORTON: That's all right.

CHAIRMAN EDGAR: With the accompanying exhibits into the record at this time?

MS. BENNETT: No, Madam Chair.

CHAIRMAN EDGAR: Okay. Seeing none, the prefiled testimony of the two FPUC witnesses will be entered into the record as though read at this time.

Are there exhibits?

MR. HORTON: Yes, ma'am.

CHAIRMAN EDGAR: And can you mention the right page -- they are numbered?

MR. HORTON: Yes, ma'am. Well, they're on the staff's comprehensive list, I believe. 24 and 25 and 26.

CHAIRMAN EDGAR: They are, I believe -- thank you. And Exhibits 24, 25 and 26 will be entered into the record at this time.

(Exhibits 24, 25 and 26 marked for identification and admitted into the record.)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

Docket No. 070001-EI
Fuel and Purchased Power Cost Recovery Clause

Direct Testimony of
Cheryl M. Martin
on behalf of
Florida Public Utilities Company

Q. Please state your name and business address.

A. Cheryl M. Martin, 401 South Dixie Highway, West Palm Beach, Florida 33401.

Q. By whom are you employed?

A. I am employed by Florida Public Utilities Company.

Q. Could you give a brief description of your background and business experience?

A. I graduated from Florida State University in 1984 with a BS degree in Accounting and I am a Certified Public Accountant in the state of Florida. I have been employed by FPU since 1985 and performed numerous accounting functions until I was promoted to Corporate Accounting Manager in 1995 with responsibilities for managing the Corporate Accounting Department including regulatory accounting (Fuel, PGA, conservation, rate cases, Surveillance reports, reporting), tax accounting, external reports and special projects. In January 2002 I was promoted to my current position of Controller where my responsibilities are the same as above with additional responsibilities in the purchasing and general accounting areas and Security and Exchange Commission (SEC) filings.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present the calculation of the final remaining true-up amounts for the period Jan. 2006 through Dec. 2006.

Q. Have you prepared any exhibits to support your testimony?

A. Yes. Exhibit________ (CMM-2) consists of Schedules M1 , F1 and E1-B for the Marianna and Fernandina Beach Divisions. These schedules were prepared from the records of the company.

Q. What has FPUC calculated as the final remaining true-up amounts for the period Jan. - Dec. 2006?

A. For Marianna the final remaining true-up amount is an over recovery of $74,131. For Fernandina Beach the calculation is an over recovery of $272,928.

Q. How were these amounts calculated?

A. They are the difference between the actual end of period true-up amounts for the Jan. - Dec. 2006 period and the total true-up amounts to be collected or refunded during the Jan. - Dec. 2007 period.

Q. What was the actual end of period true-up amount for Jan. - Dec. 2006?

A. For Marianna it was $242,460 under recovery and for Fernandina Beach it was $619,754 under recovery.

Q. What have you calculated to be the total true-up amount to be collected or refunded during the Jan. - Dec. 2007 period?

A. Using six months actual and six months estimated amounts, we calculated an under recovery for Marianna of $316,591 and an under recovery of $892,682 for Fernandina Beach.

Q. Does this conclude your direct testimony?

A. Yes, it does.

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION
DOCKET NO. 070001-EI
CONTINUING SURVEILLANCE AND REVIEW OF
FUEL COST RECOVERY CLAUSES OF ELECTRIC UTILITIES

Direct Testimony of
Mehrdad Khojasteh
On Behalf of
Florida Public Utilities Company

Q. Please state your name and business address.

A. Mehrdad Khojasteh, 401 South Dixie Highway, West Palm Beach, FL 33401.

Q. By whom are you employed?

A. I am employed by Florida Public Utilities.

Q. Have you previously testified in this Docket?

A. No.

Q. What is the purpose of your testimony at this time?

A. I will briefly describe the basis for our computations that were made in preparations of the various schedules that we have submitted to support our calculation of the levelized fuel adjustment factor for January 2008 - December 2008.

Q. Were the schedules filed by your Company completed under your direction?

A. Yes

Q. Which of the Staff's set of schedules has your company completed and filed?

A. We have filed Schedules E1-A, E1-B, and E1-B1 for Marianna and E1-A, E1-B, and E1-B1 for Fernandina Beach. They are included in Composite Prehearing Identification Number CMM-2. Schedule E1-B shows the Calculation of Purchased Power Costs and Calculation of True-Up and Interest Provision for the period January 2007 - December 2007 based on 6 Months Actual and 6 Months Estimated data.

Q. Please address the calculations of the total true-up amount to be collected or refunded during January 2008 - December 2008.

A. We have determined that at the end of December 2007 based on six months actual and six months estimated, we will under-recover $690,530 in purchased power costs in our Marianna division. In Fernandina Beach we will have under-recovered $915,677 in purchased power costs.

Q. What are the final remaining true-up amounts for the period January 2006 - December 2006 for both divisions?

A. In Marianna, the final remaining true-up amount was an over-recovery of $74,131. The final remaining true-up amount for Fernandina Beach was an over-recovery of $272,928.

Q. What are the estimated true-up amounts for the period January 2007 - December 2007?

A. In Marianna, there is an estimated under-recovery of $764,661. Fernandina Beach has an estimated under-recovery of $1,188,605.

Q. Does this conclude your testimony?

A. Yes.

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION
DOCKET NO. 070001-EI
CONTINUING SURVEILLANCE AND REVIEW OF
FUEL COST RECOVERY CLAUSES OF ELECTRIC UTILITIES

Direct Testimony of
Mehrdad Khojasteh
On Behalf of
Florida Public Utilities Company

Q. Please state your name and business address.
A. Mehrdad Khojasteh, 401 South Dixie Highway, West Palm Beach, FL 33401.
Q. By whom are you employed?
A. I am employed by Florida Public Utilities Company.
Q. Have you previously testified in this Docket?
A. Yes.
Q. What is the purpose of your testimony at this time?
A. I will briefly describe the basis for the computations that were made in the preparation of the various Schedules that we have submitted in support of the January 2008 - December 2008 fuel cost recovery adjustments for our two electric divisions. In addition, I will advise the Commission of the projected differences between the revenues collected under the levelized fuel adjustment and the purchased power costs allowed in developing the levelized fuel adjustment for the period January 2007 - December 2007 and to establish a "true-up" amount to be collected or refunded during January 2008 - December 2008.
Q. Were the schedules filed by your Company completed under your direction?
A. Yes.
Q. Which of the Staff's set of schedules has your company completed and filed?
A. We have filed Schedules E1, E1A, E2, E7, and E10 for Marianna

(Northwest division) and E1, E1A, E2, E7, E8, and E10 for Fernandina Beach (Northeast division). They are included in Composite Prehearing Identification Number MK-1.

Q. Were there any other schedules completed and filed that are pertinent to this docket?

A. Yes, Schedule E-1, A-2, M-1(Marianna only) and F-1(Fernandina Beach only) for both Marianna (Northwest) and Fernandina Beach (Northeast) were filed last month in Composite Prehearing Identification Number CMM-4 as part of FPUC's computation for its 2007 midcourse correction. These schedules support the calculation of the levelized fuel adjustment factor for January 2008 - December 2008. Schedules M-1 and F-1 show the Calculation of Purchased Power Costs and Calculation of True-Up and Interest Provision for the period January 2007 - December 2007 based on 6 Months Actual and 6 Months Estimated data.

Q. What was the purpose of filing for the midcourse adjustment and how is it relevant to the data presented in this testimony?

A. The under recovery for the Northeast Division, year-to-date June 30, 2007 is $803,546 and for the Northwest Division is $652,398. The under recovery is due in part to less demand for power than was projected in Docket 060001-EI, a situation which is expected to continue, and a significant under estimate of purchases. FPUC does not expect the under recovery to improve or reduce before year end. In August 2007, the Commission approved a midcourse to collect this underrecovery.

Q. In derivation of the projected cost factor for the January 2008 - December 2008 period, did you follow the same procedures that were used in the prior period filings?

A. Yes.

Q. Have there been any changes to the fuel contracts used to purchase electricity.

A. Yes, we will have a new contract in our Marianna (Northwest division) for the purchase of fuel beginning January 1, 2008

Q. Do the projections for fuel in the Marianna (Northwest division) reflect the anticipated prices of this new fuel contract?

A. Yes, the projections for Marianna (Northwest division) have utilized anticipated fuel costs in our fuel factors from our anticipated new fuel contract. The Commission received and approved this contract on June 6, 2007.

Q Why has the GSLD1 rate class for Fernandina Beach (Northeast division) been excluded from these computations?

A. Demand and other purchased power costs are assigned to the GSLD1 rate class directly based on their actual CP KW and their actual KWH consumption. That procedure for the GSLD1 class has been in use for several years and has not been changed herein. Costs to be recovered from all other classes are determined after deducting from total purchased power costs those costs directly assigned to GSLD1.

Q. How will the demand cost recovery factors for the other rate classes be used?

A. The demand cost recovery factors for each of the RS, GS, GSD, GSLD, GSLD1 and OL-SL rate classes will become one element of the total cost recovery factor for those classes. All other costs of purchased power will be recovered by the use of the levelized factor that is the same for all those rate classes. Thus the total factor for each class will be the sum of the respective demand cost factor and the levelized factor for all other costs.

Q. Please address the calculation of the total true-up amount to be collected or refunded during the January 2008 - December 2008.

A. We have determined that at the end of December 2007 based on six months actual and six months estimated and inclusive of the midcourse adjusted rates that will be effective on October 1, 2007, we will have under-recovered $3,856 in purchased power costs in our Marianna (Northwest division). Based on estimated sales for the period January 2008 - December 2008, it will be necessary to add .00109¢ per KWH to collect this under-recovery.

In Fernandina Beach (Northeast division) we will have under-recovered $5,040 in purchased power costs. This amount will be collected at .00147¢ per KWH during the January 2008 - December 2008 period (excludes GSLD1 customers). Page 3 and 10 of Composite Prehearing Identification Number MK-1 provides a detail of the calculation of the true-up amounts.

Q. What are the final remaining true-up amounts for the period January 2006 - December 2006 for both divisions?

A. In Marianna (Northwest division) the final remaining true-up amount was an over-recovery of $74,131. The final remaining true-up amount for Fernandina Beach (Northeast division) was an over-recovery of $272,928.

Q. What are the estimated true-up amounts for the period of January 2007 - December 2007?

A. In Marianna (Northwest division), there is an estimated under-recovery of $77,987. Fernandina Beach (Northeast division) has an estimated under-recovery of $277,968.

Q. What will the total fuel adjustment factor, excluding demand cost recovery, be for both divisions for the period?

A. In Marianna (Northwest division) the total fuel adjustment factor as shown on Line 33, Schedule E1, is 4.711¢ per KWH. In Fernandina

Beach (Northwest division) the total fuel adjustment factor for "other classes", as shown on Line 43, Schedule E1, amounts to 4.591¢ per KWH.

Q. Has FPUC taken any other steps to temper the effect of the anticipated increased fuel costs on its residential customers?

A. Yes, we are implementing a step-rate billing process where those residential customers whose consumption for any given month is 1,000 KWH or less will be billed at a reduced rate. We believe that this approach will help soften the impact of the increased costs on our customers as well as induce energy conservation.

Q. Please advise what a residential customer using 1,000 KWH will pay for the period January 2008 - December 2008 including base rates, conservation cost recovery factors, and fuel adjustment factor and after application of a line loss multiplier.

A. In Marianna (Northwest division) a residential customer using 1,000 KWH will pay $103.01, an increase of $23.20 from the previous period. In Fernandina Beach (Northeast division) a customer will pay $92.93, an increase of $2.80 from the previous period.

Q. Does this conclude your testimony?

A. Yes.

CHAIRMAN EDGAR: Mr. Horton, any other matters for you?

MR. HORTON: No, ma'am. I think with that I would ask that we be excused for the remainder of the hearing.

CHAIRMAN EDGAR: Mr. Horton is excused from the remainder of the hearing on behalf of his clients.

MR. HORTON: Thank you very much.

CHAIRMAN EDGAR: Thank you.

Ms. Bennett.

MS. BENNETT: That's all the preliminary matters staff has. I don't -- I'm not aware of parties having additional preliminary matters.

CHAIRMAN EDGAR: Are there any other matters from any of the other parties that you would like us to address at this time?

Yes, ma'am.

MS. BRADLEY: Yes. In light of the stipulations and the spinoff document, we would also ask to be excused from the remainder of the hearing.

CHAIRMAN EDGAR: And you had no witnesses; correct?

MS. BRADLEY: No, ma'am.

CHAIRMAN EDGAR: Okay. Then the Attorney General's Office is excused from the remainder of the hearing. Thank you.

MS. BRADLEY: Thank you. Appreciate it.

CHAIRMAN EDGAR: Okay. Seeing and hearing no other items to be addressed at this time, are we ready to move to opening statements?

MS. BENNETT: Yes, Madam Chair.

CHAIRMAN EDGAR: Okay. Then we will move to opening statements per the Prehearing Order, five minutes per party.

Mr. Butler.

MR. BUTLER: FPL waives opening statement.

CHAIRMAN EDGAR: Mr. Burnett.

MR. BURNETT: Progress Energy waives as well.

MR. BADDERS: Likewise, Gulf waives.

MR. BEASLEY: As does Tampa Electric.

MS. CHRISTENSEN: OPC has no opening statement.

CHAIRMAN EDGAR: Mr. McWhirter.

MR. McWHIRTER: Well, somebody ought to say something.

(Laughter.)

In the cost recovery dockets this year the utilities are going to collect around $11.9 billion, and it's a lot of money and there are a lot of things to go through in a very short period of time.

Cost recovery dockets as a whole this year, I'm pleased to report to you that cost recovery only accounts for about 58 percent of the total revenue of the utilities; whereas, last year it was over 70 percent. The area, of course, that is the largest is fuel cost, which is now around $9.7 billion. The good news is that this year the fuel cost increases are fairly modest. In fact, it's a reduction of less than 1 percent. FP&L's fuel cost increase goes up about 1 percent. Progress's fuel costs will go down for 2008. TECO's will go down. And Gulf, unfortunately, will go up, but it goes up a modest amount and it's related primarily to their growth in sales, not in the increase in cost.

In FIPUG's basic position, we took the position that right up to the hearing date you should carefully continue to examine what fuel costs are doing. And if there's an indicator that there's going to be dramatic changes for next year, you take it into consideration in these hearings. Nothing I've seen or read indicates that the cost figures for fuel are in disarray in any fashion and we have not objected, have no witnesses on the subject.

The other area, however, that we have put a position in has to do with hedging, and hedging has been around for over a hundred years and it's a very interesting device. We found in the testimony in these cases that the, the purpose of hedging by each of the utilities is not to save money but to keep the price from being volatile for the consumers. And the Commission by its orders a number of years ago has already pretty well eliminated the volatility for consumers with respect to fuel costs in that they have, we have an annual fuel factor now rather than changing it every 60 days as it started or six months as it grew into. So customers already have a good bit of stability.

I think when you evaluate the testimony what you see is that over time you come out at about the same place when you hedge as if you don't. In fact, that's how you come out if you're winning in your hedging activities. So you come out about the same place in the long-run. Customers already have stability, so do we really need hedging? I don't know. I think hedging is a good idea. The people that I represent engage in hedging. The question is whether it's a cost that should be borne by the customers who are the potential beneficiaries of it. And since the customers aren't really that much of a beneficiary of it in that the prices are already stable with the annual fuel factor, we ought to look at the costs.

And last year it was quite appalling, FP&L came in and I think the number was close to a half a billion dollars that hedging had cost, and it cost that in that year because prices came in lower than they had anticipated in the past. In the years they went up, the customers were winners. And as I understand they've been winners for the full five-year period. At least the prices have not been too bad.

But I think it's wise for the Commission from time to time to look into this information. And why should you look into it? Well, it's because of this. There's two kinds of hedging: There's physical contracts where you buy the fuel from a producer and then there are financial derivatives. And financial derivatives are a modern device and they're very effective, but they have been abused over time. So Enron and WorldCom who are utilities went down the tubes primarily because of their financial derivatives.

So the problem as a consumer we have is that most of this information is confidential. And it's confidential because when you're buying massive amounts of fuel, as the Florida utilities do, if the market knew what they were doing, it would affect the market and you would lose some of the benefits. So we consumers sitting on the sidelines say, hmm, there's a potential problem with financial derivatives. They've got to be secret. Do we know we're being treated fairly? Well, we have great admiration for the utilities and know that they try every effort to treat us fairly, but -- treat us fairly, but they deal with two masters. They have an obligation to their management and to their shareholders to make a profit and they have an obligation to customers to be fair. So what you have is kind of a difficult problem in the managing of a utility. So unfortunately by default, because there's a potential for grave danger with financial derivatives and misdoing unfortunately, because everything is secret and because utilities have an obligation both to be fair to consumers but also to make a big profit, the ball moves to your court.

And we think -- or as a consumer representative I would suggest to you that it is very important for the Commission and its staff that has access to the confidential documents to be sure that you go into those documents and you be sure that there's no hanky-panky going on. It would ill behoove me to suggest hanky-panky, but when money is involved even the most trusted people sometimes fall over the wall.

So I would suggest to you that maybe you ought to institute a new evaluation. Five years has transpired. We know that hedging is going on, we know that it's lost a lot of money last year, and it's going to lose money next year because of the contracts that were entered into, but that was more than made up when prices were going up. Prices are going to go up again, so everything may be okay. But that doesn't mean that you shouldn't look at it. So our position in this case, we presented no testimony, have not rigorously engaged in discovery, but we feel, I feel concerned that it's something that you need to take charge of, and I hope that you will do it.

That concludes my presentation.

CHAIRMAN EDGAR: Thank you, Mr. McWhirter.

Commissioner Argenziano.

COMMISSIONER ARGENZIANO: I'm glad you did speak up because I'm learning some of the, I guess, the ways of doing business in the utility business, and hedging, of course, being one of them. And it brought concerns to me because I don't know. And I'm not saying there's any hanky-panky. I understand the price, you know, trying to fix in and lock in a price and how important that is, but I can't really figure out if it's being done correctly.

And in the case of FP&L, I've looked at close to $400 million and I say, well, how, how come it's so far off the mark? And my concern is that consumers get to pay 100 percent of that. While the consumers, you know, are paying the higher price to begin with for the fuel than the actual costs, I guess, and then afterwards I guess because the company gambled by hedging, they gambled too high and way off the mark and now the consumer gets to pay the whole, the whole bill. That concerns me. And part of maybe a reevaluation would be to spread that -- because I think hedging is important, unless you can convince me that, as you say, there may be some customer stability that we already have in place. But I'm just not sure that maybe -- or maybe in a reevaluation we should consider maybe spreading that risk not just to the consumer but to the company and the shareholders also as I learn more about that.

But you talk about derivatives, financial derivatives. Are you -- I'm trying to figure out besides the obvious ones are you suggesting that there are financial derivatives in the hedging process?

MR. McWHIRTER: That's how they hedge their financial derivatives. They enter into agreements -- the things that I would ask about if I were concerned about it, you enter into what we call bilateral agreements with banks, not with people who sell gas and oil. And the deal is it's kind of a gambling deal. And if prices go up, you win the gamble. If prices go down, the bank wins the gamble. Well, a couple of months ago I read an article and it said the financial industry has done very well during the period of stock market growth, and one of the big areas they're doing very well in is in their energy activities. Well, their energy activities are financial derivatives dealing with hedging.

I think that not only the consumers benefit but the utilities benefit. So the question in my mind is why should the consumers bear the full cost if there's a dual benefit? Isn't there some way that the costs can be shared in hedging? I understand that with a true-up there's, you know, interest is charged if you're late and so forth, but that's certainly an area that could be looked into.

But financial derivatives is how it's done for the most part. There are fiscal contracts for coal. But with gas I think you'll see that they're not buying gas, they're buying -- they're gambling with a bank that they're going to come out. Are those banks doing business with utilities in other areas where they may be getting discounted rates? That's a question that I might like to ask sometime.

COMMISSIONER ARGENZIANO: Well, then basically the company takes the gamble on the hedging but the consumer is the one who pays if it goes wrong.

MR. McWHIRTER: It's not Las Vegas gambling. It's probably much worse.

(Laughter.)

COMMISSIONER ARGENZIANO: Got it. Got it. Thank you.

CHAIRMAN EDGAR: Commissioner McMurrian.

COMMISSIONER McMURRIAN: Thank you, Chairman.

I had one procedural question for Mr. McWhirter. I heard your discussion about the secret documents, and I guess I just wanted you to clarify for me because I understood that as parties to the, to the fuel clause that any, any party could sign nondisclosure agreements with the companies and see that information on behalf of your, the consumers you represent. Do I understand -- are you able to look at those documents or are those --

MR. McWHIRTER: Yeah. We -- the utilities have been very cooperative with us when we ask for confidential information. But, quite frankly, I'm a little bit reluctant to ask for those documents because the people I represent also engage in hedging, and it kind of puts me in the middle of keeping confidential information to myself when I don't understand it. So I've got to go to somebody who understands it and it's the people that are in competition with the utilities. So I've kind of tried to stay out of that except on a philosophical basis.

But you can get the confidential information and you've got a very bright, capable staff. And if you don't have, they can hire people that are bright and capable. So I recommend that you look at it very actively.

COMMISSIONER McMURRIAN: Thank you, Mr. McWhirter, for that clarification.

I just always get concerned when we start talking about secret documents and we're not really clear what we mean. That the parties on behalf of customers are able to at least look through those. Whether they choose to or not is entirely up to you. Thank you.

CHAIRMAN EDGAR: Mr. Twomey, did you waive opening?

MR. TWOMEY: Yes, ma'am.

CHAIRMAN EDGAR: You did. And, Ms. Christensen, you did as well? Mr. Burgess, you did. Okay. I just wanted to make sure that we don't miss anybody.

Ms. Bennett.

MS. BENNETT: Moving on to the exhibit list, I'd ask that you mark and move the Comprehensive Stipulated Exhibit List into the record, and also the list includes Exhibits 2 and

3, which are Staff's Composite Exhibit List, and 46, which is the additional stipulations. We'd ask that those be moved into the record, the exhibits themselves.

CHAIRMAN EDGAR: Okay. At this time we will move Exhibit 1, the Comprehensive Exhibit List, Exhibits 2 and 3 and 46 into the record.

(Exhibits 1, 2, 3 marked for identification and admitted into the record.)

(Exhibit 46 admitted into the record.)

MS. BENNETT: Thank you.

CHAIRMAN EDGAR: Excuse me. Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Would I have the opportunity to ask FPL some questions on that hedging?

CHAIRMAN EDGAR: Are you directing your questions to the witnesses or to --

COMMISSIONER ARGENZIANO: Probably going to be staff.

CHAIRMAN EDGAR: Actually if you have a question, just go right ahead.

COMMISSIONER ARGENZIANO: Well, I didn't know -- if we're moving on to that, I can wait for the proper time.

MR. BUTLER: We will have a witness, Mr. Yupp, who will be testifying on hedging.

COMMISSIONER ARGENZIANO: Okay. That'd be great.

CHAIRMAN EDGAR: Is that okay?

COMMISSIONER ARGENZIANO: Yes.

CHAIRMAN EDGAR: Okay.

MS. BENNETT: And at this point we're ready to swear the witnesses in, I believe.

CHAIRMAN EDGAR: My understanding is that we have four witnesses remaining. If those four witnesses would please stand with me and raise your right hand, we'll go ahead and swear you in as a group. One, two, three, four. Thank you.

(Witnesses collectively sworn.)

Should we take up Witness Garrett's testimony at this time?

MS. BENNETT: Yes, Madam Chair.

MR. BUTLER: Thank you, Madam Chair. John Burnett on behalf of Progress Energy Florida. At this time we would move Mr. Garrett's prefiled testimony as well as his exhibits, which I believe are 4, 5 and 6, into evidence.

CHAIRMAN EDGAR: Thank you. At this time we will enter the prefiled testimony of Witness Garrett into the record as though read, and the accompanying exhibits marked as 4, 5 and 6.

(Exhibits 4, 5 and 6 marked for identification and admitted into the record.)

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

Fuel and Capacity Cost Recovery
Final True-Up for the Period
January through December, 2006

DIRECT TESTIMONY OF
Will Garrett

March 1, 2007

Q. Please state your name and business address.

A. My name is Will A. Garrett. My business address is 299 First Avenue North, St. Petersburg, Florida 33701.

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

A. I am employed by Progress Energy Service Company, LLC as Controller of Progress Energy Florida.

Q. What are your responsibilities?

A. As legal entity Controller for Progress Energy Florida (PEF), I am responsible for all accounting matters that impact the reported financial results of this Progress Energy Corporation entity. I have direct management and oversight of the employees involved in PEF Regulatory Accounting, Property Plant and Materials Accounting, PEF Financial Reporting and General Accounting. I assumed the responsibilities for the various regulatory compliance filings, including this Fuel and Capacity Cost Recovery True-Up Filing, in February 2006 from Javier Portuondo.

Q. Please describe your educational background and professional experience.

A. I joined the company as Controller of PEF on November 7, 2005. My direct relevant experience includes 2 ½ years as the Corporate Controller for DPL, Inc. and its major subsidiary, Dayton Power and Light, headquartered in Dayton, Ohio. Prior to this position, I held a number of finance and accounting positions for 8 years at Niagara Mohawk Power Corporation, Inc. (NMPC) in Syracuse, New York, including Executive Director of Financial Operations, Director of Finance and Assistant Controller. As the Director of Finance and Assistant Controller, my responsibilities included regulatory proceedings, rates and financial planning, providing testimony on a variety of matters before the New York Public Service Commission. Prior to joining NMPC, I was a Senior Audit Manager at Price Waterhouse (PW) in upstate New York, with 10 years of direct experience with investor owned utilities and publicly traded companies. I am a graduate of the State University of New York in Binghamton, with a Bachelor of Science in Accounting and I am a Certified Public Accountant in the State of New York.

Q. Have you previously filed testimony before this Commission in connection with Progress Energy Florida's Fuel and Capacity Cost Recovery Clause?

A. No, I have not.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to describe PEF's Fuel Adjustment Clause final true-up amount for the period of January through December 2006, and PEF's Capacity Cost Recovery Clause final true-up amount for the same period.

Q. Have you prepared exhibits to your testimony?

A. Yes, I have prepared and attached to my true-up testimony as Exhibit No. __ (WG-1T), a Fuel Adjustment Clause true-up calculation and related schedules; Exhibit No. __ (WG-2T), a Capacity Cost Recovery Clause true-up calculation and related schedules; and Exhibit No. __(WG-3T), Schedules A1 through A3, A6, and A12 for December 2006, year-to-date. I have extracted schedules on which there was no sponsored testimony. Schedules A1 through A9, and A12 for the year ended December 31, 2006, were previously filed with the Commission on January 19, 2007.

Q. What is the source of the data that you will present by way of testimony or exhibits in this proceeding?

A. Unless otherwise indicated, the actual data is taken from the books and records of the Company. The books and records are kept in the regular course of business in accordance with generally accepted accounting principles and practices, and provisions of the Uniform System of Accounts as prescribed by this Commission.

Q. Would you please summarize your testimony?

A. Per Order No. PSC-06-1057-FOF-EI, the projected 2006 fuel adjustment true-up amount was an over-recovery of $46,480,257. The actual over-recovery for 2006 was $75,344,873 resulting in a final fuel adjustment true-up over-recovery amount of $28,864,616 (Exhibit No. __ (WG-1T)).

The projected 2006 capacity cost recovery true-up amount was an under-recovery of $5,380,565. The actual amount for 2006 was an under-recovery of $8,762,537 resulting in a final capacity true-up under-recovery amount of $3,381,972 (Exhibit No. __ (WG-2T)).

FUEL COST RECOVERY

Q. What is PEF's jurisdictional ending balance as of December 31, 2006 for fuel cost recovery?

A. The actual ending balance as of December 31, 2006 for true-up purposes is an over-recovery of $75,344,873.

Q. How does this amount compare to PEF's estimated 2006 ending balance included in the Company's estimated/actual true-up filing?

A. The actual true-up attributable to the January - December 2006 period is an over-recovery of $75,344,873 which is $28,864,616 higher than the re-projected year end over-recovery balance of $46,480,257.

Q. How was the final true-up ending balance determined?

A. The amount was determined in the manner set forth on Schedule A2 of the Commission's standard forms previously submitted by the Company on a monthly basis.

Q. What factors contributed to the period-ending jurisdictional over-recovery of $75,344,873 shown on your Exhibit No. __ (WG-1T)?

A. The factors contributing to the over-recovery are summarized on Exhibit No. __ (WG-1T), sheet 1 of 4. Net jurisdictional fuel revenues fell below the forecast by $54.4 million, while jurisdictional fuel and purchased power expense decreased $137.0 million. This $137.0 million favorable variance is primarily attributable to a favorable system variance from projected fuel and net purchased power of $150.9 M as more fully described below. The $75.3 million over-recovery also includes the deferral of $0.4 million of 2005 under-recovery approved in Order No. PSC-05-1252-FOF-EI. The net result of the difference in jurisdictional fuel revenues and expenses, plus the 2005 deferral and the 2006 interest provision calculated on the deferred balance throughout the year is an over-recovery of $75.3 million as of December 31, 2006.

Q. Please explain the components shown on Exhibit No. __ (WG-1T), sheet 4 of 4 which helps to explain the $150.9 million favorable system

variance from the projected cost of fuel and net purchased power transactions.

A. Sheet 4 of 4 is an analysis of the system dollar variance for each energy source in terms of three interrelated components; (1) changes in the amount (MWH's) of energy required; (2) changes in the heat rate of generated energy (BTU's per KWH); and (3) changes in the unit price of either fuel consumed for generation ($ per million BTU) or energy purchases and sales (cents per KWH).

Q. What effect did these components have on the system fuel and net power variance for the true-up period?

A. As shown on sheet 4 of 4, the dollar variance due to MWHs generated and purchased (column B) produced a cost decrease of $59.1 million. The primary reason for this favorable variance was lower system requirements. The unfavorable heat rate variance (column C) of $10.0 million is due to changes in the generation mix to meet the energy requirements. The favorable price variance of $101.8 million (column D) was caused mainly by lower than projected natural gas and heavy oil prices, partially offset by higher purchase power prices. Heavy oil averaged $6.36 per MMBtu, $0.91 per MMBtu (12.5%) lower than projected per the previously submitted A3, Page 3 of 4, Line 47. Natural gas averaged $7.41 per MMBtu, $1.91 per MMBtu (20.5%) lower than projected, also per the previously submitted A3, Page 3 of 4, Line 50. The variance related to Other Fuel is driven by the coal car investment (see Order No. 95-1089-FOF-EI.) This favorable $9.4 million Other Fuel price variance is offset by an unfavorable price variance in Coal. Due to a reporting difference between the projection and the actuals, components of the coal car investment fall within two lines, rather than one, on Exhibit No. __ (WG-1T), sheet 4 of 4.

Q. Does this period ending true-up balance include any noteworthy adjustments to fuel expense?

A. Yes. Noteworthy adjustments are shown on Exhibit No. __ (WG-3T) in the footnote to line 6b on page 1 of 2, Schedule A2. Included in the footnote to line 6b on page 1 of 2, Schedule A2, are the "2006 full revenue requirements of the installed cost of Hines Unit 2, excluding the unit's non-fuel Operations and Maintenance (O&M) expenses" of $36.6 million in accordance with Order No. PSC-05-0945-S-EI. These adjustments also include the return on coal inventory in transit of $3.4 million and the DOE crude oil refund of $3.9 million.

Q. Please explain the return on coal inventory in transit adjustment.

A: This $3.4 million adjustment represents the return on coal inventory in transit for the year in accordance with the approved Settlement and Stipulation in Docket No. 050078-EI, as discussed further in the *Other Matters* portion of this filing.

Q: Please explain the DOE crude oil refund adjustment.

A: As a result of a supplemental order issued in July 2006 by the Department of Energy, a crude oil refund was issued to PEF. The DOE ordered the $3.9 M refund to PEF and in August of 2006 this refund was returned to customers through a reduction in fuel expense recovered through the fuel clause.

Q. Did PEF exceed the economy sales threshold in 2006?

A. No. PEF did not exceed the gain on economy sales threshold of $5.6 M in 2006. As reported on Schedule A1, Line 15a, the gain for the year-to-date period through December 2006 was $2.0 million; which fell below the threshold. This entire amount was returned to customers through a reduction of total fuel and net power expense recovered through the fuel clause.

Q. Has the three-year rolling average gain on economy sales included in the Company's filing for the November, 2006 hearings been updated to incorporate actual data for all of year 2006?

A. Yes. PEF has calculated its three-year rolling average gain on economy sales, based entirely on actual data for calendar years 2004 through 2006, as follows:

Year	Actual Gain
2004	5,330,652

2005	1,703,378
2006	1,990,442
Three-Year Average	$ 3,008,157

CAPACITY COST RECOVERY

Q. What is the Company's jurisdictional ending balance as of December 31, 2006 for capacity cost recovery?

A. The actual ending balance as of December 31, 2006 for true-up purposes is an under-recovery of $8,762,537.

Q. How does this amount compare to the estimated 2006 ending balance included in the Company's estimated/actual true-up filing?

A. When the estimated 2006 under-recovery of $5,380,565 is compared to the $8,762,537 actual under-recovery, the final capacity true-up for the twelve month period ended December 2006 is an under-recovery of $3,381,972.

Q. Is this true-up calculation consistent with the true-up methodology used for the other cost recovery clauses?

A. Yes. The calculation of the final net true-up amount follows the procedures established by the Commission in Order No. PSC-96-1172-FOF-EI. The true-up amount was determined in the manner set forth on the Commission's standard forms previously submitted by the Company on a monthly basis.

Q. What factors contributed to the actual period-end capacity under-recovery of $8.8 million?

A. Exhibit No. __ (WG-2T, sheet 1 of 3) compares actual results to the original projection for the period. The $8.8 million under-recovery is due primarily to lower actual jurisdictional revenues of $6.7 million compared to projected revenues, due to lower than projected retail sales.

Q. Were there any items of note included in the current true-up period?

A. Yes. In Order No. PSC-02-1761-FOF-EI, issued in Docket No. 020001-EI, the Commission addressed the recovery of specific incremental security costs through the capacity cost recovery clause. In accordance with the Commission order, Exhibit No. __ (WG-2T, sheet 2 of 3, line 20) includes incremental security costs of $2,182,164 before jurisdictional allocation to retail customers.

OTHER MATTERS

Q. Were coal procurement and transportation functions transferred from Progress Fuels Corporation to PEF in 2006?

A. Yes. As part of a consolidation of PEF's coal procurement and transportation functions, ownership of railcars used to transport coal to Crystal River and coal inventory in transit were transferred from Progress

Fuels Corporation to PEF on January 1, 2006. In accordance with Order No. PSC-05-0945-S-EI, which approved the Stipulation and Settlement in Docket No. 050078-EI, PEF recovered its carrying costs of coal inventory in transit and its coal procurement O&M costs through the fuel recovery clause. Furthermore, consistent with established Commission policy, PEF recovered depreciation expense, repair and maintenance expenses, property taxes and a return on average investment associated with rail cars used to transport coal to Crystal River. In accordance with the approved Settlement and Stipulation in Docket No. 050078-EI, PEF used 11.75% as its authorized return on inventory in transit and coal car investment.

Q: Have you provided Schedule A12 showing the actual monthly capacity payments by contract consistent with the Staff Workshop on January 12, 2005?

A: Yes. Schedule A12 is included in Exhibit No. __ (WG-3T)).

Q. Does this conclude your direct true-up testimony?

A. Yes

CHAIRMAN EDGAR: And Witness Cross.

MR. BURNETT: Yes, ma'am. Similarly, we would move Ms. Cross's prefiled testimony into the record as read here today, along with her two exhibits, Exhibits 7 and 8.

CHAIRMAN EDGAR: The prefiled testimony of Witness Cross will be moved into the record as though read with Exhibits 7 and 8.

(Exhibits 7 and 8 marked for identification and admitted into the record.)

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

Fuel and Capacity Cost Recovery
Estimated/Actual True-Up Amounts
January through December 2007

DIRECT TESTIMONY OF
LORI CROSS

Q. Please state your name and business address.

A. My name is Lori Cross. My business address is 299 1st Avenue North, St. Petersburg, Florida 33701.

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

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

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present for Commission approval Progress Energy Florida's (PEF or the Company) estimated/actual fuel and capacity cost recovery true-up amounts for the period of January through December 2007.

Q. Do you have an exhibit to your testimony?

A. Yes. I have prepared Exhibit No.__(LC-1R) which is attached to my prepared testimony consisting of Commission Schedules E1-B through E9 which contain the calculation of the Company's true-up balances and the supporting data and Part A which contains the Company's reprojected capacity cost recovery true-up balance and supporting data.

FUEL COST RECOVERY

Q. How was the estimated true-up over-recovery of $169,376,547 shown on Schedule E1-B, Sheet 1, line 20, developed?

A. The estimated true-up calculation begins with the actual under-recovered balance of $147,350,329, taken from Schedule A2, page 2 of 2, for the month of June 2007. This balance plus the estimated July through December 2007 monthly true-up calculations comprise the estimated $169,376,547 over-recovered balance at year-end. The projected December 2007 true-up balance includes interest estimated at the June ending rate of 0.439% per month. The development of the actual/estimated true-up amount for the period ending December 2007 is shown on Schedule E1-B.

Q. What are the primary reasons for the projected December-ending 2007 over-recovery of $169.4 million?

A. The $169.4 million projected over-recovery is primarily attributable to two factors. First, oil and natural gas prices have been, and are expected to remain lower than the forecast used in the projection filing for 2007. Second, retail sales have been lower than projected through June, and this trend is expected to continue through the remainder of the year. While these lower system requirements result in lower fuel revenues, they also result in greater reductions in fuel costs due to lower peaking generation which has a higher than system average fuel cost.

Q. How does the current fuel price forecast for July – December 2007 compare with the same period forecast used in the Company's 2007 projection filed in October 2006?

A. Coal prices remain essentially constant. Natural gas prices decrease an average of $1.71/mmbtu or approximately 16%. Heavy oil prices decrease an average of $.66/mmbtu or 6.9%, while light oil prices decrease an average of $1.03/mmbtu or 6.5%.

Q. Does Progress Energy Florida expect to exceed the three-year rolling average gain on Other Power Sales?

A. Yes, Progress Energy Florida estimates the total gain on non-separated sales during 2007 will be $3,659,812, which exceeds the three-year rolling average for such sales of $3,008,157 by $651,654.

Q. What amount of this gain will Progress Energy Florida shareholders get to keep?

A. Consistent with Order No. PSC-01-2371-FOF-EI, PEF shareholders are entitled to keep 20% of the gains in excess of the current 3 year rolling average. For 2007 this value is expected to be $130,331.

Q. When is Hines 4 expected to go into commercial service?

A. Currently, Hines 4 is expected to go into commercial service in December of 2007.

Q. Have the revenue requirements associated with Hines 2 been removed from the estimated fuel and purchased power costs in December 2007 consistent with the Stipulation and Settlement Agreement in Docket No. 050078?

A. Yes, PEF has removed the revenue requirements associated with Hines 2 from the estimated costs in the Fuel and Purchased Power Clause beginning in December 2007 coincident with the expected in-service date of Hines 4. Upon the commercial in-service date of Hines Unit 4, PEF will begin recovering the revenue requirements for Hines 2, excluding the unit's non-fuel O&M expenses, through an increase in base rates in accordance with the provisions of PEF's base rate settlement agreement in Docket 050078.

Q. Does the projected over-recovery for 2007 indicate the need for a mid-course correction?

A. No. Order No. PSC-07-0333-PAA-EI in Docket No. 070001 indicates that a utility should file for a mid-course correction when the absolute value of the estimated end-of-period total net true-up divided by the current period's total actual and estimated jurisdictional fuel revenue applicable-to-period will be ten percent or greater. PEF's projected over-recovery of $169.4 million is only 8.3% greater than projected fuel revenues of $2,046.9 million for the period ending December 31, 2007.

CAPACITY COST RECOVERY

Q. How was the estimated true-up under-recovery of $14,799,865 shown on Part A, Line 50, developed?

A. The estimated true-up calculation begins with the actual under-recovered balance of $26,910,910 for the month of June 2007. This balance plus the estimated July through December 2007 monthly true-up calculations comprise the estimated $14,799,865 under-recovered balance at year-end. The projected December 2007 true-up balance includes interest estimated at the June ending rate of 0.439% per month.

Q. What are the major changes between the original projection for the year 2007 and the actual/estimated reprojection?

A. The $14.8 million under-recovery is primarily attributable to sales being lower than originally projected. 2007 Jurisdictional KWh sales are projected to be approximately 1.5 million lower than originally projected for 2007.

OTHER MATTERS

Q. Does this conclude your estimated/actual true-up testimony?

A. Yes.

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

Fuel and Capacity Cost Recovery Factors
January through December 2008

DIRECT TESTIMONY OF
LORI CROSS

Q. Please state your name and business address.

A. My name is Lori Cross. My business address is 299 1st Avenue North, St. Petersburg, Florida 33701.

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

A. I am employed by Progress Energy Service Company, LLC, in the capacity of Manager of Regulatory Planning Florida.

Q. Have your duties and responsibilities remained the same since your testimony was last filed in this docket?

A. Yes.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present for Commission approval the levelized fuel and capacity cost factors of Progress Energy Florida (PEF or the Company) for the period of January through December 2008.

Q. Do you have an exhibit to your testimony?

A. Yes. I have prepared an exhibit attached to my testimony consisting of Sections A through C. Section A contains our forecast assumptions on fuel costs. Section B contains fuel cost recovery (FCR) schedules E1 through E10, H1 and the calculation of the inverted fuel rate. Section C contains capacity cost recovery (CCR) schedules.

FUEL COST RECOVERY CLAUSE

Q. Please describe the fuel cost factors calculated by the Company for the projection period.

A. Schedule E1 shows the calculation of the Company's basic levelized fuel cost factor of 4.604 ¢/kWh. This factor consists of a fuel cost for the projection period of 5.00666 ¢/kWh (adjusted for jurisdictional losses), a GPIF reward of 0.00146 ¢/kWh, and an estimated prior period over recovery true-up of 0.40724 ¢/kWh. Utilizing this basic factor, Schedule E1-D shows the calculation and supporting data for the Company's final levelized fuel cost factors for service taken at secondary, primary, and transmission metering voltage levels. To perform this calculation, effective jurisdictional sales at the secondary level are calculated by applying 1% and 2% metering reduction factors to primary and transmission sales, respectively (forecasted at meter level). This is consistent with the methodology used in the development of the capacity cost recovery factors. The final levelized fuel cost factor for residential service is 4.611 ¢/kWh. Schedule E1-D shows the Company's proposed tiered rates of 4.278 ¢/kWh for the first 1,000 kWh and 5.278 ¢/kWh above 1,000 kWh. These rates are developed in the "Calculation of Inverted Residential Fuel Rate" schedule in Section B.

Schedule E1-E develops the Time of Use (TOU) multipliers of 1.379 On-peak and 0.824 Off-peak. The multipliers are then applied to the levelized fuel cost factors for each metering voltage level which results in the final TOU fuel factors to be applied to customer bills during the projection period.

Q. What is the amount of the 2007 net true-up that PEF has included in the fuel cost recovery factor for 2008?

A. PEF has included a projected over-recovery of $169,376,547. This amount includes a projected actual/estimated over-recovery for 2007 of $140,511,931 plus the final true-up over-recovery of $28,864,616 for 2006 that was filed on March 1, 2007.

Q. What is the change in the levelized residential fuel factor for the projection period from the fuel factor currently in effect?

A. The projected levelized residential fuel factor for 2008 of 4.611 ¢/kWh is an decrease of .528 ¢/kWh or 10.3% from the 2007 levelized fuel factor of 5.139 ¢/kWh.

Q. Please explain the reasons for the decrease in the levelized fuel factor.

A. The decrease in the levelized fuel factor between 2007 and 2008 is mainly driven by the 2007 expected over-recovery of $169.4 million. There is also a $35.4 million reduction from 2007 due to moving Hines 2 from the fuel clause to base rates. Changes in 2008 projected fuel costs per unit compared to 2007 projections are as follows: Coal 6.8% decrease, heavy oil 4.2% increase, light oil 1.6% increase and natural gas 3.1% increase. The fuel price increases for both oil and natural gas continue to be driven by the worldwide supply and refining capacity limitations coupled with increased global demand and geopolitical uncertainty. As discussed in more detail in the Direct Testimony of Joseph McCallister, the Company has entered into hedging contracts to mitigate the price volatility risk of natural gas and oil.

Q. Why is PEF proposing to continue use of the tiered rate structure approved for use in 2006?

A. In light of continually increasing fuel costs, the Company is proposing to continue use of the inverted rate design for residential fuel factors to encourage energy efficiency and conservation. Specifically, the Company proposes to continue a two-tiered fuel charge whereby the charge for a customer's monthly usage in excess of 1,000 kWh (second tier) is priced one cent per kWh more than the charge for the customer's usage up to 1,000 kWh (first tier). The 1,000 kWh price change breakpoint is reasonable in that approximately 2/3 of all residential energy is consumed in the first tier and 1/3 of all energy is consumed in the second tier. The Company believes the one cent higher per unit price, targeted at 1/3 of the residential class's energy consumption, will promote energy efficiency and conservation. This type of inverted rate design was incorporated in the Company's base rates approved in Order No. 02-0655-AS-EI.

Q. How was the inverted fuel rate calculated?

A. I have included a page in Section B of my exhibit that shows the calculation of the levelized fuel cost factors for the two tiers of residential customers. The two factors are calculated on a revenue neutral basis so that the Company will recover the same fuel costs as it would under the traditional levelized approach. The two-tiered factors are determined by first calculating the amount of revenues that would be generated by the overall levelized residential factor of

4.611¢/kWh shown on Schedule E1-D. The two factors are then calculated by allocating the total revenues to the two tiers for residential customers based on the total annual energy usage for each tier.

Q. What is included in Schedule E1, line 3, "Coal Car Investment"?

A: The $637 thousand on Line 3 represents the estimated return on average investment in rail cars used to transport coal to Crystal River.

Q. What is included in Schedule E1, line 4, "Adjustments to Fuel Cost"?

A. The $11.1 million credit on Line 4 represents the return on coal inventory in transit and the estimated refund plus interest based on Staff's Primary Recommendation in Docket No. 060658. The return on coal inventory in transit was calculated and included in accordance with the Stipulation and Settlement Agreement in Docket 050078-EI. I note, however, that to date, a final order has not been issued in Docket No.__060658-EI and adjustments may or may not need to be made in this area after such order is issued.

Q. Are there any costs associated with natural gas storage included in the 2008 fuel factor?

A. Yes. To further enhance system reliability, PEF has entered into gas storage contracts with Bay Gas Storage Company, LTD. and SG Resources Mississippi, L.L.C coming on-line in May of 2008. These contracts will primarily increase PEF's gas supply reliability and mitigate price risk.

Q. How do PEF's projected gains on non-separated wholesale energy sales for 2008 compare to the incentive benchmark?

A. The total gain on non-separated sales for 2008 is estimated to be $4,161,133 which is above the benchmark of $2,451,211 by $1,709,922. Therefore, 100% of gains below the benchmark and 80% of gains above the benchmark will be distributed to customers based on the sharing mechanism approved by the Commission in Order No. PSC-00-1744-PAA-EI. Further, consistent with this Order, $341,984 or 20% of the gains above the benchmark will be returned to the shareholder. The benchmark of $2,451,211 was calculated based on the average of actual gains for 2005 and 2006 and estimated gains for 2007 in accordance with Order No. PSC-00-1744-PAA-EI.

Q. Please explain the entry on Schedule E1, line 17, "Fuel Cost of Stratified Sales."

A. PEF has several wholesale contracts with SECI. One contract provides for the sale of supplemental energy to supply the portion of their load in excess of SECI's own resources. The fuel costs charged to SECI for supplemental sales are calculated on a "stratified" basis in a manner which recovers the higher cost of intermediate/peaking generation used to provide the energy. There are other SECI contracts for fixed amounts of base, intermediate and peaking capacity. PEF is crediting average fuel cost of the appropriate strata in accordance with Order No. PSC-97-0262-FOF-EI. The fuel costs of wholesale sales are normally included in the total cost of fuel and net power transactions used to calculate the average system cost per kWh for fuel adjustment purposes. However, since the fuel costs of the stratified sales are not recovered on an average system cost basis, an adjustment has been made to remove these costs and the related kWh sales from the fuel adjustment calculation in the same manner that interchange sales are removed from the calculation. This adjustment is necessary to avoid an over-recovery by the Company which would result from the treatment of these fuel costs on an average system cost basis in this proceeding, while actually recovering the costs from these customers on a higher, stratified cost basis. Line 17 also includes the fuel cost of sales made to the City of Tallahassee in accordance with Order No. PSC-99-1741-PAA-EI, as well as sales to TECO, Reedy Creek and the City of Homestead.

Q. Please give a brief overview of the procedure used in developing the projected fuel cost data from which the Company's basic fuel cost recovery factor was calculated.

A. The process begins with a fuel price forecast and a system sales forecast. These forecasts are input into the Company's production cost simulation model along with purchased power information, generating unit operating characteristics, maintenance schedules, and other pertinent data. The model then computes system fuel consumption and fuel and purchased power costs. This information is the basis for the calculation of the Company's levelized fuel cost factors and supporting schedules.

Q. What is the source of the system sales forecast?

A. The system sales are forecasted by Corporate Planning using normal weather conditions, population projections from the Bureau of Economic and Business Research at the University of Florida and economic assumptions from Economy.Com.

Q. Is the methodology used to prepare the sales forecast for this projection period the same as previously used by the Company?

A. Yes. The methodology employed to produce the forecast for the projection period is consistent with the Company's most recent filings and was developed with an econometric forecasting model.

Q. What is the source of the Company's fuel price forecast?

A. The fuel price forecasts for natural gas and fuel oil (residual #6 and distillate #2) and coal are based on observable market data in the industry and are prepared jointly by the Company's Enterprise Risk Management Department and Regulated Fuels Department. For coal, a third party forecast is used. Additional details and forecast assumptions are provided in Section A of my exhibit.

Q. Are current fuel prices the same as those used in the development of the projected fuel factor?

A. No. As we all know, fuel prices are very volatile particularly in the storm season and can change significantly from day to day. Since this projection run was completed, natural gas and oil prices have decreased somewhat. Consistent with past practices, PEF will continue to monitor fuel prices and update our projection filing as the storm season winds down if changes in fuel prices create a significant change in PEF's projected fuel costs.

CAPACITY COST RECOVERY

Q. How was the Capacity Cost Recovery factor developed?

A. The calculation of the capacity cost recovery (CCR) factor is shown in Section C of my exhibit. The factor allocates capacity costs to rate classes in the same manner that they would be allocated if they were recovered in base rates.

Q. **Please provide a brief explanation of Section C to your exhibit.**

A. Page 1, Projected Capacity Payments, provides system capacity payments to qualifying facilities and other power suppliers. The retail portion of the capacity payments is calculated using separation factors as agreed to in the Stipulation and Settlement Agreement under Docket 050078 as detailed in the Rebuttal Testimony of William C. Slusser Jr. Page 2, Estimated/Actual True-Up, which was also included in the exhibit to my direct testimony in the 2007 estimated/actual true-up filing, calculates the estimated true-up balance for calendar year 2007 of $14.8 million. This balance is carried forward to Page 1 to be collected during January through December 2008.

Page 3, Capacity Contracts, provides dates and MW associated with the various contracts.

Pages 4 and 5, Calculation of Capacity Clause Recovery Factor, provide the calculation of the capacity cost recovery factor for each rate class based on average 12 CP and annual average demand. The CCR factor for each secondary delivery rate class in cents per kWh is the product of total jurisdictional capacity costs (including revenue taxes) from Page 1, multiplied by the class demand allocation factor, divided by projected effective sales at the secondary level. The CCR factors for primary and transmission rate classes reflect the application of metering reduction factors of 1% and 2% from the secondary CCR factor.

Q. Please explain the increase in the CCR factor for the projection period compared to the CCR factor currently in effect.

A. The projected average retail CCR factor of 1.018 ¢/kWh is 5.6% higher than the 2007 factor of 0.964 ¢/kWh. The increase is primarily due to price increases in most base capacity contracts and a higher under-recovery over the prior year.

Q. Has PEF included incremental security charges in the 2008 projected capacity amount?

A. Yes. PEF has included $5.7 million of estimated incremental security costs for 2008 in accordance with the Stipulation and Settlement Agreement in Docket 050078-EI. Of this amount, $3.8 million is associated with the Nuclear Regulatory Commission, $1 million is associated with the Maritime Transportation Security Act, and $.9 million is associated with the North American Electric Reliability Council (NERC) Cyber Security Standards CIP-002-1 through CIP-009-1, effective June 1, 2006.

OTHER MATTERS

Q. Has PEF included any refund associated with Docket No. 060658 in the 2008 fuel factor calculation?

A. Yes. PEF has included a refund of $14,195,140 in the 2008 fuel factor calculation. This amount represents Staff's Primary Recommendation with interest through June of 2007 plus an estimate for interest that will accrue in the 3rd and 4th quarter of 2007. As noted previously in my testimony, however, a final order has not been issued in Docket No.__060658-EI and adjustments may or may not need to be made in this area after such order is issued.

Q. Does this conclude your testimony?

A. Yes.

MR. BURNETT: And, Madam Chairman, if appropriate at this time, Progress Energy Florida would call Joseph McCallister as its first witness.

CHAIRMAN EDGAR: Thank you.

MR. BURNETT: Madam Chair, may I proceed?

CHAIRMAN EDGAR: Yes, sir.

JOSEPH F. McCALLISTER

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

DIRECT EXAMINATION

BY MR. BURNETT:

Q Good morning, Mr. McCallister. Would you please introduce yourself to the Commission and provide your business address.

A Good morning, Commissioners. My name is Joseph F. McCallister. My business address is 410 South Wilmington Street, Raleigh, North Carolina 27601.

Q And, Mr. McCallister, correct me if I'm wrong, but I just saw you be sworn in as a witness; is that correct?

A Yes, sir.

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

A I'm employed by Progress Energy Carolina and I'm the Director, Gas and Oil Trading.

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

A Yes, I have.

Q Do you have a copy of your prefiled testimony and exhibits with you today?

A Yes, sir.

Q Do you have any changes to make to your prefiled testimony and exhibits?

A No, sir.

Q Mr. McCallister, if I asked you the same questions in your prefiled testimony today, would you give the same answers that are in your prefiled testimony?

A Yes, sir.

MR. BURNETT: Madam Chair, we request that the prefiled testimony of Mr. McCallister be entered into the record as if it were so read today.

CHAIRMAN EDGAR: The prefiled testimony will be entered into the record as though read.

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

Fuel and Capacity Cost Recovery
Final True-Up for the Period
January through December, 2006

DIRECT TESTIMONY OF JOSEPH MCCALLISTER

April 2, 2007

Q. Please state your name and business address.

A. My name is Joseph McCallister. 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 Carolinas in the capacity of Director, Gas & Oil Trading.

Q. Have your duties and responsibilities remained the same since you last testified in this proceeding?

A. Yes, my responsibilities for the procurement and trading of natural gas and oil on behalf of Progress Energy Florida (PEF or the Company) have remained the same.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to summarize the results of PEF's hedging activity for 2006 and to provide the information required by Order No. PSC-

02-1484-FOF-EI which approved the resolution of the hedging related issues pending before the Commission in Docket No. 011605-EI.

Q. Have you prepared exhibits to your testimony?

A. Yes. I have attached exhibit JM-1T which summarizes hedging information for 2006.

Q. What are the primary objectives of PEF's hedging strategy?

A. The primary objectives of PEF's hedging strategy are to mitigate fuel price risk and volatility and provide greater price certainty to PEF's customers.

Q. What hedging activities did PEF undertake during 2006 for fuel and wholesale power.

A. PEF continued to perform the daily management activities outlined in its Risk Management Plan and executed physical and financial transactions in accordance with established company risk management guidelines. With respect to hedging natural gas prices for 2006, PEF had fixed price physical contracts and financial instruments that resulted in net fuel cost savings to customers of approximately $62.1 million. With respect to hedging heavy and light oil prices for 2006, PEF had fixed price financial instruments that resulted in net fuel costs savings to customers of approximately $56.9 million. In total, the gas and oil hedging activity for 2006 resulted in net fuel cost savings to customers of approximately $119 million. In addition, during 2006 PEF made economic energy purchases and wholesale power sales to third parties that resulted in additional savings to customers of $24.4 million and $2 million, respectively.

Q. Does this conclude your testimony?

A. Yes

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

Fuel and Capacity Cost Recovery
January through December 2008

DIRECT TESTIMONY OF JOSEPH MCCALLISTER

September 4, 2007

Q. Please state your name and business address.

A. My name is Joseph McCallister. 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 Carolinas in the capacity of Director, Gas & Oil Trading.

Q. Have you previously filed testimony before this Commission?

A. Yes I have.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to outline PEF's Risk Management Plan for fuel procurement in 2008, outline PEF's hedging activities and objectives for 2008, and summarize PEF's actual hedging results for the period January through July 2007.

Q. Has PEF developed its Risk Management Plan for fuel procurement in 2007 in accordance with the Resolution of Issues proposed by Staff and approved by the Commission in Order No. PSC-02-1484-FOF-EI, Docket No. 011605-EI?

A. Yes. PEF's Risk Management Plan was prepared in accordance with the Resolution of Issues approved by the Commission and is attached to my prepared testimony as Exhibit No. ___ (JM-1P). Certain confidential information in the exhibit has been redacted, consistent with the Company's request for confidential classification of this information.

Q. What are the objectives of PEF's hedging activities?

A. The objectives of PEF's hedging activities are to reduce fuel price risk and volatility, and provide greater price certainty to PEF's customers by locking in fixed prices over time for a portion of its forecasted natural gas, heavy oil and light oil fuel requirements. PEF utilizes approved physical and financial agreements to meet these objectives.

Q. Describe PEF's hedging activities for 2008.

A. PEF executed its hedging strategy and objectives for 2008 consistent with prior years by entering into fixed price physical and financial transactions over time for natural gas, heavy oil and light oil. Given the volatility of natural gas and fuel oil prices, executing fixed price transactions over time provides an effective method to reduce the overall price risk and volatility associated with these fuels while providing greater price certainty for our customers. Based on current forecasts as of August 1, 2007, PEF has hedged approximately [redacted] of its forecasted natural gas requirements, [redacted] of its forecasted heavy oil requirements and [redacted] of its forecasted light oil requirements for 2008.

Q. What were the results of PEF's hedging activities for January through July 2007?

A. The Company's natural gas and fuel oil hedging activities for January through July 2007 have resulted in realized hedge losses of approximately $3.1 million. For the period 2003 through 2006, PEF's natural gas and fuel oil hedging activities have provided net fuel savings of approximately $380 million to its customers. Although PEF's hedging activity has achieved significant net fuel savings to date, the primary objective is to reduce price risk and volatility. As a result, there will be periods when realized hedge losses occur.

Q. Does this conclude your testimony?

A. Yes.

(REPORTER'S NOTE: Page 72 of Volume 1 inadvertently left blank.)

(REPORTER'S NOTE: Page 73 of Volume 1 inadvertently left blank.)

(REPORTER'S NOTE: Page 74 of Volume 1 inadvertently left blank.)

(REPORTER'S NOTE: Page 75 of Volume 1 inadvertently left blank.)

(REPORTER'S NOTE: Page 76 of Volume 1 inadvertently left blank.)

BY MR. BURNETT:

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

A Yes, I do.

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

A Good morning, Commissioners. My testimony specifically addresses Progress Energy Florida's hedging program and strategies. The objective of PEF's hedging strategy is to mitigate fuel price risk and volatility --

(Interruption.)

-- to provide greater price certainty to PEF's customers by locking in fixed prices over time for a portion of its forecasted natural gas and fuel oil requirements. PEF's hedging program has met the objective of reducing price risk and volatility to PEF's customers. I look forward to answering any questions you may have. Thank you.

MR. BURNETT: And with the request that Mr. McCallister keep it kind of slow like that from now on I will tender him for cross-examination.

THE WITNESS: I will try my best.

CHAIRMAN EDGAR: Are there questions from any party on cross for this witness? Mr. Burgess?

MR. BURGESS: No questions.

CHAIRMAN EDGAR: Mr. Twomey? No?

Mr. McWhirter?

MR. McWHIRTER: I feel constrained to ask a question or two.

CROSS EXAMINATION

BY MR. McWHIRTER:

Q Mr. McCallister, as I understand it, according to your testimony your hedging losses were $3.1 million for the period 2003 to 2006?

A That is correct, sir.

Q And --

A No. I'm sorry, sir. $3.1 million for January 2007 to September, I mean, to July 2007.

Q I see. But for 2003 through 2006 you're ahead of the game by $380 million?

A Approximately.

Q How do you come by that calculation?

A How do we calculate the number?

Q Yes.

A Well, in simple terms, and I'll speak specifically to gas and oil, the way that the, that you purchase gas and oil in the market is via spot index prices. So there's a prevailing market price and that's just the way you procure it. When we're hedging, we are actually locking in prices for those commodities. So for gas and oil we would be fixing the price whether it's through a physical transaction or through a financial transaction. So to calculate the gain or loss we're simply taking our fixed price, comparing it to the spot price we would have paid if we didn't hedge, and then taking that difference times the volume to get the net number.

Q And you do that by comparing the price you paid for a specific day of the year to the price as it's stated on the NYMEX or other commodity exchange?

A Yes. We would compare it to the actual price we would have paid if we didn't hedge. So if, if we did -- let me give you an example. If we hedged for December of '07 -- or let's go back, July of '07, we bought gas for $8 under a fixed price transaction, and say it's Florida Zone 3, we're buying a physical fixed price transaction, and let's say that Florida Zone 3 came out to $8 for that month, we would take that difference of a dollar times the volume we purchased under that hedge and that would be the gain, in this case the gain, but it could be a loss as well if the price was lower than that. Does that make sense?

Q What percentage of your contracts are physical contracts to buy the commodity as opposed to financial derivatives?

A Well, let me make sure I understand the question. All of our contracts to buy the commodity are going to be physical. You know, once again, we're buying those under standard contracts which are primarily index related. So it's going to be based on the prevailing market at the time that you've actually executed -- I mean, what you're buying it at and where you're buying it at. In terms of the percentage that we're -- is your question how much are we hedging physically versus financially?

Q Yes.

A I'd have to check some of these numbers. I think over time we've hedged more financially as we've gone through time because we've built up our financial contracts. You know, in our portfolio, our fixed price physical deal -- I mean, our index deals also allow us to convert to fixed price at any point in time, some of them do. So it can be a combination of both the financial and the physical. If you need an exact percentage, I can certainly get that for you. I don't --

Q That was what I was looking for, the ratio of financial to physical.

A Well, for oil it's almost predominantly financial. It has been since 2004. 2004, 2005, all of our oil hedges have been financial in nature.

For gas, once again this is from memory, but it's been a mixture and I'd have to get that number for you. But there is a mix of some physical fixed price deals and some financial fixed price deals.

Q Let me see if I get this right in my mind. You go to an oil producer and you enter into a contract with that oil producer. Do you enter into that contract at a fixed price or do you enter into it at a variable price with the producer?

A Well, with the actual supplier it would be at an index price. And once again, the reason for that is because that's the way the industry works. Most of the oil that is supplied, whether we're buying it on a spot basis or under a term contract, it is priced against a monthly price, the price, you know, on a given day when we actually take delivery. So financially we're able to go out to a variety of contracts. And maybe I should give you a little more background on our financial agreements.

We have a number of them. We have 20 to 25 financial agreements with various counterparties, some of them physical players in the market, producers, some of them, as you call them, banks or financial institutions. So we use a combination of those. But once again, because of the way the industry actually sells the physical products, they're sold under an index-based contract. So, therefore, we have to go out and execute a hedge kind of separately from that with a financial agreement or we, or we can convert some things to a physical fixed price deal.

Q So your alternative is to buy from a supplier and pay the amount that the exchange rate shows for that day on the spot market or you can fix your price by going to a bank or another institution and say we will pay you $8 an MCF for the gas. And if the price on the spot market comes in less than $8, you win, and if it comes in more than $8, we win. Is that the way it works?

A Let me, let me make sure I understand your question. There's two pieces. One is we're buying the physical product.

Q Right.

A The second is we're trying to manage the price risk and the volatility associated with that product over time. So we're doing a little bit of both. I mean, once again, we're really buying the product under an index-based contract because that's standard, standard practice in the industry.

Q Right.

A The financial piece of it, the piece we're really trying to manage that concerns us is the ups and downs in the prices. And that's the piece that we, we hedge, through your terminology, with the bank or even through another physical player we can hedge it financially.

And the other thing I kind of want to say here too is that a lot of these banks also have physical operations. I mean, they're not -- you know, if you look at some of the big banks, they also have groups that are moving natural gas and doing other things. So they're not pure, pure financial players. They're not just speculating and speculating. They may have a portfolio of business they're trying to manage as well, and that kind of makes the market right. You have buyers and sellers. So a lot of these financial players, as you've called them in the past, banks, they also do have in some instances a pretty large portfolio of physical supply and gas as well.

Q Well, if you already have a contract with a supplier and you go to a bank, you're committed on the supply from the supplier. And even though the bank may have its own supply, you don't take the bank's supply. You take it from your supplier and the bank fills in the difference in cost.

A Yeah. Because there are two different transaction types. One is a physical transaction. One is a, as you call it, a derivative transaction. So there are two separate transactions that, that serve different purposes.

When we're doing the financial derivative contract, we're actually exchanging a fixed price in exchange for the floating index price that we're trying to hedge that we're actually buying the fuel under. So by executing that hedge you eliminate that index risk with the supply you're actually buying.

Q So if the price comes in higher than the fixed price you bought with your derivative estimate, you win because you pay less, is that right, or the consumers win?

A Yeah. That, that, that extra, that gain would flow through the fuel clause and be a credit to the fuel cost.

Q And that's -- when you say that over the period of time you've had fuel savings of $380 million, you've had those fuel savings as a result of the fact that the price of natural gas or oil has been higher than the fixed price at which you were able to buy it.

A That is correct.

Q Do you strive to make money or do you just strive to obtain financial stability?

A Well, our primary objective is to, is to achieve reduction of price risk and volatility. So the, the result of making or losing money really isn't part of the objectives of the program.

Q Do the banks charge you a fee for this activity other than the price that you would pay for the commodity?

A We have not paid any fees associated with our over-the-counter transactions with financial institutions.

Q Does your company or the holding company that owns your company have any dealings with these banks other than in the financial derivatives for your hedging activity?

A I would, I would be speculating, but certainly on the, on the, the treasury side of the house I'm certain there's some relationships with some of the institutions that we deal with.

MR. McWHIRTER: That's all the questions that I have.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Yes. If I, if I may ask you. I think so far you may have better staff than the bank or whoever you deal with because it seems like you've come out on top and have done a good job. But I need to ask, why, why worry about the volatility then? Why not just go with the certainty, the physical fiscal certainty and worry then about what the ratepayers may, you know, have to deal with after with the higher risk?

THE WITNESS: That's a good question. I think I'll provide a very recent example.

You know, I was looking just this morning at December, December '07 natural gas prices and oil prices. Since September 4th natural gas has went up 15 to 20 percent for just December and oil has went up 25 to 30 percent. So these are, these are very volatile commodities that move a lot and they're driven by market-driven functions that we can't control.

So I think -- we're not advocating that we lock in 100 percent, but we sure are advocating that we take a prudent approach to it and a reasonable approach of layering in transactions over time to reduce some of that, that risk associated with that market because the market, it can move significantly and it can move significantly quickly.

COMMISSIONER ARGENZIANO: Madam Chair. Then that would go to the gentleman's questions about the ratio. I would think that would be important and I'd love to know what the ratio would be of the certainty versus the uncertainty, which could turn out to be better in the long-run. But --

THE WITNESS: Are you asking what our, what our percentages hedged are? Are you asking the difference between physical --

COMMISSIONER ARGENZIANO: I guess, yes.

MR. BURNETT: Commissioner, please excuse me. That is confidential information. If I could provide that to the Commission in a sealed capacity. We have it available. It just would be confidential. Please forgive my interruption.

COMMISSIONER ARGENZIANO: Absolutely. I understand. Thank you.

MR. BURNETT: Sure.

CHAIRMAN EDGAR: Are there questions from staff?

MS. BENNETT: No, there are no questions from staff.

Mr. Burnett, do you have the confidential information with you today that we could share with the Commission?

THE WITNESS: If I don't have it handy, I can get it very quickly.

MR. BURNETT: Perhaps at a break we could prepare that and submit it.

MS. BENNETT: Thank you.

Staff has no further questions.

CHAIRMAN EDGAR: Okay. Did you have anything on redirect?

MR. BURNETT: No, ma'am.

CHAIRMAN EDGAR: No. Anything further from the Commissioners? No.

Exhibits?

MR. BURNETT: Yes, ma'am. We would move into evidence witness exhibits JM-1T and JM-1P as Exhibits 9 and 10, please.

CHAIRMAN EDGAR: Exhibits 9 and 10 will be entered into the record.

(Exhibits 9 and 10 marked for identification and admitted into the record.)

MR. BURNETT: And may Mr. McCallister be excused?

CHAIRMAN EDGAR: And he may be excused. Thank you.

THE WITNESS: You're welcome.

MS. BENNETT: Madam Chair, did we move the testimony in also?

CHAIRMAN EDGAR: Yes, we did.

MR. BURNETT: If I failed to do so, I'd do so now.

And, Madam Chair, the last witness for Progress Energy would be Robert M. Oliver, and at this time, if appropriate, we would move his prefiled testimony and Exhibits 11 and 12 into the record.

CHAIRMAN EDGAR: Witness Oliver has been excused. The prefiled testimony will be entered into the record as though read with the accompanying Exhibits 11 and 12.

(Exhibits 11 and 12 marked for identification and admitted into the record.)

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

GPIF Reward/Penalty Amount for January through December 2006

DIRECT TESTIMONY OF ROBERT M. OLIVER

Q. Please state your name and business address.

A. My name is Robert M. Oliver. 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 Carolinas as Manager of Portfolio Management.

Q. Describe your responsibilities as Manager of Portfolio Management.

A. As Manager of Portfolio Management, I am responsible for managing the development and application of the model, analysis and data used for the short term generation planning. As relates to this process, my duties include responsibility for the preparation of the information and material required by the Commission's GPIF True-Up and Targets mechanisms.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to describe the calculation of PEF's GPIF reward/penalty amount for the period of January through December 2006. This calculation was based on a comparison of the actual performance of PEF's twelve GPIF generating units for this period against the approved targets set for these units prior to the actual performance period.

Q. Do you have an exhibit to your testimony in this proceeding?

A. Yes, I am sponsoring Exhibit No. _______ (RMO-1T), which consists of the schedules required by the GPIF Implementation Manual to support the development of the incentive amount. This 34-page exhibit is attached to my prepared testimony and includes as its first page an index to the contents of the exhibit.

Q. What GPIF incentive amount have you calculated for this period?

A. I have calculated PEF's GPIF incentive amount to be a reward of $607,201. This amount was developed in a manner consistent with the GPIF Implementation Manual. Page 2 of my exhibit shows the system GPIF points and the corresponding reward. The summary of weighted incentive points earned by each individual unit can be found on page 4 of my exhibit.

Q. How were the incentive points for equivalent availability and heat rate calculated for the individual GPIF units?

A. The calculation of incentive points was made by comparing the adjusted actual performance data for equivalent availability and heat rate to the target performance indicators for each unit. This comparison is shown on each unit's

Generating Performance Incentive Points Table found on pages 9 through 20 of my exhibit.

Q. Why is it necessary to make adjustments to the actual performance data for comparison with the targets?

A. Adjustments to the actual equivalent availability and heat rate data are necessary to allow their comparison with the "target" Point Tables exactly as approved by the Commission prior to the period. These adjustments are described in the Implementation Manual and are further explained by a Staff memorandum, dated October 23, 1981, directed to the GPIF utilities. The adjustments to actual equivalent availability concern primarily the differences between target and actual planned outage hours, and are shown on page 7 of my exhibit. The heat rate adjustments concern the differences between the target and actual Net Output Factor (NOF), and are shown on page 8. The methodology for both the equivalent availability and heat rate adjustments are explained in the Staff memorandum.

Q. Have you provided the as-worked planned outage schedules for PEF's GPIF units to support your adjustments to actual equivalent availability?

A. Yes. Page 33 of my exhibit summarizes the planned outages experienced by PEF's GPIF units during the period. Page 34 presents an as-worked schedule for each individual planned outage.

Q. Does this conclude your testimony?

A. Yes.

PROGRESS ENERGY FLORIDA

DOCKET NO. 070001-EI

GPIF Targets and Ranges for January through December 2008

DIRECT TESTIMONY OF ROBERT M. OLIVER

Q. Please state your name and business address.

A. My name is Robert M. Oliver. My business address is P.O. Box 1551, Raleigh, North Carolina 27602.

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

A. I am employed by Progress Energy Carolinas Inc. as Manager of Portfolio Management for Regulated Commercial Operations.

Q. What are your duties and responsibilities in that capacity?

A. As Manager of Portfolio Management for Regulated Commercial Operations, I oversee the management of energy portfolios for Progress Energy Florida, Inc. ("Progress Energy" or "Company"), as well as Progress Energy Carolinas, Inc. My responsibilities include oversight of planning and coordination associated with economic system operations, including unit commitment and dispatch, fuel burns, and power marketing and trading functions.

Q. What is the purpose of your testimony?

rates), the unplanned and planned outage factors (EUOF and POF) when added to the equivalent availability factor (EAF) will always equal 100%. For example, an EUOF of 15% and POF of 10% results in an EAF of 75%.

The supporting tables and graphs for the target and range rates are contained in pages 53-104 of my exhibit in the section entitled "Unplanned Outage Rate Tables and Graphs."

Q. Were adjustments made to historical unplanned outage hours to exclude the impact of performance anomalies?

A. Yes. Historical unplanned outage hours for Crystal River Units 1, 2, and 3 were adjusted to exclude the impact of certain performance anomalies.

Q. Please describe the performance anomalies at Crystal River Units 1 and 2.

A. Crystal River Units 1 and 2 experienced unplanned derations due to point of discharge (POD) during June, July, and August of 2005. In May 2006, Progress Energy installed temporary cooling towers to minimize future POD related derations. Based on the satisfactory experience with the temporary cooling towers to date, it is anticipated that this equipment will be retained for service in 2008. Thus, the historical outage hours for these events were excluded when setting the EAF targets for Crystal River Units 1 and 2.

Q. Please describe the performance anomalies at Crystal River Unit 3.

A. Crystal River Unit 3 experienced unplanned derations and outages due to a main transformer replacement during December 2005 and January 2006. As a result of replacing the main transformer, Crystal River Unit 3 is not expected to have main transformer related events in 2008, thus the historical outage hours for this event were excluded when setting the EAF target for Crystal River Unit 3.

Q. Please describe the overall impact of the adjustments on Crystal River Units 1, 2, and 3 equivalent availability targets.

A. The adjustments raise the equivalent availability targets for Crystal River Units 1, 2, and 3 making the target higher than using the unadjusted historical average.

Q. Please describe the methodology utilized to develop the improvement/degradation ranges for each GPIF unit's availability targets?

A. The methodology described in the GPIF Implementation Manual was used. Ranges were first established for each of the four unplanned outage rates associated with each unit. From an analysis of the unplanned outage graphs, units with small historical variations in outage rates were assigned narrow ranges and units with large variations were assigned wider ranges. These individual ranges, expressed in term of rates, were then converted into a single unit availability range, expressed in terms of a factor, using the same procedure described above for converting the availability targets from rates to factors.

Q. Have you determined the net operating heat rate targets and ranges for the Company's GPIF units?

A. Yes. This information is included in the Target and Range Summary on page 4 of my exhibit.

Q. How were these heat rate targets and ranges developed?

A. The development of the heat rate targets and ranges for the upcoming period utilized historical data from the past three years, as described in the GPIF Implementation Manual. A "least squares" procedure was used to curve-fit the heat rate data within ranges having a 90% confidence level of including all data. The analyses and data plots used to develop the heat rate targets and ranges for each of the GPIF units are contained in pages 32-52 of my exhibit in the section entitled "Average Net Operating Heat Rate Curves."

Q. How were the GPIF incentive points developed for the unit availability and heat rate ranges?

A. GPIF incentive points for availability and heat rate were developed by evenly spreading the positive and negative point values from the target to the maximum and minimum values in case of availability, and from the neutral band to the maximum and minimum values in the case of heat rate.

The fuel savings (loss) dollars were evenly spread over the range in the same manner as described for incentive points. The maximum savings (loss) dollars are the same as those used in the calculation of the weighting factors.

Q. How were the GPIF weighting factors determined?

A. To determine the weighting factors for availability, a series of simulations were made using a production costing model in which each unit's maximum equivalent availability was substituted for the target value to obtain a new system fuel cost. The differences in fuel costs between these cases and the target case determine the contribution of each unit's availability to fuel savings. The heat rate contribution of each unit to fuel savings was determined by multiplying the BTU savings between the minimum and target heat rates (at constant generation) by the average cost per BTU for that unit. Weighting factors were then calculated by dividing each individual unit's fuel savings by total system fuel savings.

Q. What was the basis for determining the estimated maximum incentive amount?

A. The determination of the maximum reward or penalty was based upon monthly common equity projections obtained from a detailed financial simulation performed by the Company's Corporate Model.

MR. BURNETT: Madam Chair, that would be the last witness for Progress Energy Florida. We would rest at this time.

CHAIRMAN EDGAR: I'm sorry?

MR. BURNETT: We would rest our case at this time.

CHAIRMAN EDGAR: Thank you.

MR. BUTLER: The next witness on the list is FPL's witness Gerry Yupp, and I would call him to the stand.

CHAIRMAN EDGAR: Thank you.

COMMISSIONER ARGENZIANO: Madam Chair.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Just if I could interrupt for a moment. I probably would like the same information that I asked of Progress from the other companies also, if that's acceptable.

CHAIRMAN EDGAR: From FPL, TECO and from Gulf? Thank you. And I'm seeing some nods.

MR. BUTLER: I'm sorry. That information was the percentage of the utility's total fuel volume that is hedged?

COMMISSIONER ARGENZIANO: Yes.

MR. BUTLER: Sort of broken down by physical and financial?

CHAIRMAN EDGAR: Physical and financial breakdown is what I'm hearing to understand. Yes. Is that something that could be similarly -- we will probably take a short break after this witness is what I was thinking, although we can do it sooner, if that's necessary. Okay. I'm seeing maybe a partial request. All right. On that point, and it probably is about that time, let's take about a 15-minute break, and we would ask each of the parties to please get with our staff as well to see how we can accommodate Commissioner Argenziano's request, and we'll take that up when we come back from break. Thank you.

(Recess taken.)

We will go back on the record from break. And before we go into hearing from our next witness, I know, Commissioner Argenziano, you had asked for some additional information from a few of the parties, and we had asked you to get with our staff. And are there questions or can we discuss when that information may be available?

MR. BUTLER: Thank you. For FPL, we are gathering the information. I think it can be made available fairly quickly.

One point of clarification I wanted to confirm is our intent is to provide the information on the hedging percentages for the, for 2007 to date. Is that an appropriate time period for the information to be presented?

COMMISSIONER ARGENZIANO: I think so. I guess --

CHAIRMAN EDGAR: I'm sorry, Commissioner. Can you make sure that you're -- for the record. Thank you.

COMMISSIONER ARGENZIANO: You're saying you could give me for 2007, the ratio for just 2007?

MR. BUTLER: Right. It would show the ratio of our hedging percentage of total fuel purchases in 2007 to date.

COMMISSIONER ARGENZIANO: That would be fine.

MR. BUTLER: And, Madam Chairman, would you like to go ahead and identify that as a late-filed exhibit or how should we handle that?

CHAIRMAN EDGAR: I think procedurally that makes sense. Commissioner -- yes. Let's go ahead and do that. So we will mark --

MR. BUTLER: I think it would be Exhibit 48; is that right?

CHAIRMAN EDGAR: Hang on. I'll get there. Yes.

MR. BUTLER: And entitle it "FPL Hedging Percentages (Financial and Physical) in 2007."

CHAIRMAN EDGAR: Okay. So we will label as Exhibit 48 information to be filed by FPL titled "FPL Hedging Percentages (Financial and Physical) 2007" to be late filed.

And, Commissioner Argenziano, you had also asked for similar information from the other companies; is that correct? Will we need to have separate late-filed exhibits or what is the best way to address that, Ms. Bennett?

MS. BENNETT: I believe we will need separate late-filed. Except I believe TECO at the break showed me that they have that available, so it won't be a late-filed. It will just be presented into evidence.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: I had asked staff in the interim for some additional questions to the original questions, and I think -- have you had the chance to get that to the companies?

MR. YOUNG: No, Madam -- no, Madam Commissioner. We're in the process of getting that to the companies.

COMMISSIONER ARGENZIANO: Madam Chair, this may sound silly, but could you read the questions that I gave you out loud so that they know ahead of time?

MR. YOUNG: With pleasure. The question is how much, how much of your total fuel purchase is hedging versus spot hedging versus long-term contracts? And that's total fuel purchases.

COMMISSIONER ARGENZIANO: Right. Thank you.

MR. YOUNG: And, Madam Chairman, for the, for the record, Gulf, as it relates to the previous question in terms of percentage financial versus physical, Gulf can answer that for the record. It's not confidential.

CHAIRMAN EDGAR: Mr. Badders.

MR. BADDERS: Yes. Our witness can respond to that question or I can tell you the number. I mean, either way.

COMMISSIONER ARGENZIANO: Okay. Whatever you prefer.

CHAIRMAN EDGAR: Mr. Badders, why don't we go ahead while we're on it.

MR. BADDERS: All right. Currently financial hedging for Gulf ranges between 40 and 60 percent. That's our target range. And with regard to the additional question, we can provide that information also with a late-filed exhibit.

CHAIRMAN EDGAR: Okay.

MS. BENNETT: So then, Madam Chair, the late-filed exhibit for Progress would be 49; is that correct?

CHAIRMAN EDGAR: Yes, ma'am.

MS. BENNETT: And it would be similar to Florida Power & Light's Hedging Percentage (Financial and Physical) for 2007; is that correct?

MR. BURNETT: Correct.

CHAIRMAN EDGAR: And we will so mark.

MS. BENNETT: And then for Gulf it would be Exhibit Number 50, and it would again be Gulf's Hedging Percentages (Financial and Physical) for 2007.

And then Exhibit 51 would be TECO. And again it would be TECO's Hedging Percentages (Financial and Physical) for 2007.

CHAIRMAN EDGAR: And we will mark Exhibits 48, 49, 50 and 51 as, to be late-filed unless they are to become available prior to the end of this hearing.

(Late-Filed Exhibits 48, 49, 50 and 51 identified for the record.)

Okay. Are we ready to move on?

Okay. Next witness.

MR. BUTLER: I would call Mr. Yupp to the stand.

GERARD YUPP

was called as a witness on behalf of Florida Power & Light Company and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. BUTLER:

Q And, Mr. Yupp, would you please state your name and address for the record?

A My name is Gerard Yupp. My business address is 700 Universe Boulevard, Juno Beach, Florida 33408.

Q And by whom are you employed and in what capacity?

A I am employed by Florida Power & Light Company as Director of Wholesale Operations.

Q Have you previously been sworn, Mr. Yupp?

A Yes, I have.

Q Okay. Do you have before you testimony, prefiled testimony of Gerard J. Yupp in this docket dated April 2, 2007, consisting of five pages and one attached exhibit, GJY-1?

A Yes, I do.

MR. BUTLER: Okay. I'd note for the record that GJY-1 has been identified as Exhibit 13 in the staff Comprehensive Exhibit List.

CHAIRMAN EDGAR: Thank you.

(Exhibit 13 marked for identification.)

BY MR. BUTLER:

Q Excuse me. Do you have any changes or corrections to this testimony?

A No, I do not.

Q Okay. Do you adopt this prepared testimony as your testimony in this proceeding?

A Yes, I do.

MR. BUTLER: Okay. I would ask that Mr. Yupp's testimony dated April 2, 2007, be entered, inserted into the record as though read.

CHAIRMAN EDGAR: The prefiled testimony will be entered into the record as though read.

MR. BUTLER: Thank you.

BY MR. BUTLER:

Q Mr. Yupp, do you also have before you prefiled testimony dated September 4, 2007, consisting of 17 pages and two attached exhibits?

A Yes, I do.

MR. BUTLER: Okay. And the first of those exhibits, Madam Chairman, GJY-2, is identified as Exhibit 14. And then the second is actually a portion of Ms. Dubin's Exhibit KMD-6, which has been identified in the Comprehensive Exhibit List as Exhibit 21.

(Exhibits 14 and 21 marked for identification.)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

TESTIMONY OF GERARD J. YUPP

DOCKET NO. 070001-EI

APRIL 2, 2007

Q. Please state your name and address.

A. My name is Gerard J. Yupp. My business address is 700 Universe Boulevard, Juno Beach, Florida, 33408.

Q. By whom are you employed and what is your position?

A. I am employed by Florida Power & Light Company (FPL) as Director of Wholesale Operations in the Energy Marketing and Trading Division.

Q. Have you previously testified in the predecessors to this docket?

A. Yes.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide a review of FPL's 2006 hedging activity, including the detail required by Item 5 of the Resolution of Issues in Docket 011605-EI approved by the Commission per Order No. PSC-02-1484-FOF-EI, which states:

"5. Each investor-owned utility shall provide, as part of its final true-up filing in the fuel and purchased power cost recovery docket, the following information: (1) the volumes of each fuel the utility actually hedged using a fixed price contract or instrument; (2) the types of hedging instruments the utility used, and the volume and type of fuel associated with each type of instrument; (3) the average period of each hedge; and (4) the actual total cost (e.g. fees, commissions, options premiums, futures gains and losses, swaps settlements) associated with using each type of hedging instrument."

Q. Are you sponsoring an Exhibit for this proceeding?

A. Yes. I am sponsoring the following Exhibit:

GJY-1:2006 Hedging Activity

Q. Please describe FPL's hedging objectives.

A. In Order No. PSC-02-1484-FOF-EI, the Commission approved the Resolution of Issues in the Hedging Docket. The first component of the Resolution states:

"Each investor-owned electric utility recognizes the importance of managing price volatility in the fuel and purchased power it purchases to provide electric service to its customers. Further, each investor-owned electric utility recognizes that the greater the proportion of a particular fuel or purchased power it relies upon to provide electric service to its customers, the greater the importance of managing price volatility associated with that energy source."

Accordingly, the primary objective of FPL's hedging program is to reduce fuel price volatility, thereby helping to deliver greater price certainty to FPL's customers. FPL does not execute speculative hedging strategies aimed at "out guessing" the market in the hopes of potentially returning savings to FPL's customers. FPL has implemented a well-disciplined, well-defined and controlled hedging program that is executed in compliance with FPL's risk management policies and procedures.

Q. Please summarize FPL's 2006 hedging activities.

A. FPL hedged its fuel portfolio for 2006 utilizing a mix of options and fixed price transactions. An "option" is a hedging instrument that gives the buyer the right, but not the obligation, to buy (call) or sell (put) a set commodity volume at a specific price for a specific period of time. The buyer of an option pays a premium to hold this right. A "fixed price transaction" locks in the price of a commodity for a set volume over a set period of time. In contrast to options, there is typically no separate premium charged for fixed price transactions.

The natural gas and heavy fuel oil markets experienced extreme price movements during the year. Natural gas settlement prices on the NYMEX ranged from a high of $11.43 per MMBtu in January to a low of $4.20 per MMBtu in October. Mild winter weather, above average natural gas storage levels and a relatively inactive hurricane season contributed to this significant downturn in the natural gas market. United States Gulf Coast (USGC) heavy fuel oil ranged from a high of $48.15 per barrel in July to a low of $32.83 per barrel in December. New York Harbor (NYH) heavy fuel oil ranged from a high of $50.76 per barrel in April to a low of $39.89 per barrel in December. In addition to the impact of a relatively inactive hurricane season, the significant downturn in heavy fuel oil prices can be attributed to increased supply resulting from relatively high refinery runs in order to meet growing U. S. gasoline demand. Because the natural gas and heavy fuel oil markets trended lower after FPL's hedge positions were in place for 2006, FPL's hedging activities for natural gas and heavy fuel oil resulted in losses on those positions of approximately $469 million. This situation was a complete reversal of prior years in which FPL's hedge positions resulted in significant savings as the fuel markets continually trended higher after FPL's hedge positions were in place. On a cumulative basis, since its inception, FPL's expanded hedging program has resulted in net gains of $471 million. While the cumulative impact of FPL's hedging program will vary and, at times, may show either net savings or net losses, FPL expects that the cumulative, long-term impact of its hedging program will not result in significant savings or losses to FPL's customers. FPL continues to monitor the fundamentals of the energy markets and, as conditions change, FPL will make further adjustments to its hedging program to meet FPL's objective of reduced fuel price volatility.

Q. Does your Exhibit GJY-1 provide the detail on FPL's 2006 hedging activities required by Item 5 of the Resolution of Issues?

A. Yes.

Q. Does this conclude your testimony?

A. Yes, it does.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

TESTIMONY OF GERARD J. YUPP

DOCKET NO. 070001-EI

SEPTEMBER 4, 2007

Q. Please state your name and address.

A. My name is Gerard J. Yupp. My business address is 700 Universe Boulevard, Juno Beach, Florida, 33408.

Q. By whom are you employed and what is your position?

A. I am employed by Florida Power & Light Company (FPL) as Director of Wholesale Operations in the Energy Marketing and Trading Division.

Q. Have you previously testified in this docket?

A. Yes.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present and explain FPL's projections for (1) the dispatch costs of heavy fuel oil, light fuel oil, coal and natural gas, (2) the availability of natural gas to FPL, (3) generating unit heat rates and availabilities and (4) the quantities and costs of wholesale (off-system) power and purchased power transactions. Additionally, I provide a review of FPL's hedging program and present FPL's Risk Management Plan for fuel procurement in 2008.

Q. Have you prepared or caused to be prepared under your supervision, direction and control any exhibits in this proceeding?

A. Yes, I am sponsoring the following exhibits:

- GJY-2 - Appendix I
- Schedules E2 through E9 of Appendix II

FUEL PRICE FORECAST

Q. What forecast methodologies has FPL used for the 2008 recovery period?

A. For natural gas commodity prices, the forecast methodology relies upon the NYMEX Natural Gas Futures contract prices (forward curve). For light and heavy fuel oil prices, FPL utilizes Over-The-Counter (OTC) forward market prices. Projections for the price of coal and the availability of natural gas are developed internally at FPL. The forward curves for both natural gas and fuel oil represent expected future prices at a given point in time and are consistent with the prices at which FPL can transact its hedging program. The basic assumption made with respect to using the forward curves is that all available data that could impact the price of natural gas and fuel oil in the future is incorporated into the curves at all times. The methodology allows FPL to execute hedges consistent with its forecasting method and to optimize the dispatch of its units in changing market conditions. FPL utilized forward curve prices from the close of business on July 24, 2007 for its 2008 projection filing. This was the most recent date that allowed FPL adequate time to complete its filing.

Q. What are the key factors that could affect FPL's price for heavy fuel oil during the January through December 2008 period?

A. The key factors that could affect FPL's price for heavy oil are (1) worldwide demand for crude oil and petroleum products (including domestic heavy fuel oil), (2) non-OPEC crude oil supply, (3) the extent to which OPEC adheres to their quotas and reacts to fluctuating demand for OPEC crude oil, (4) the political and civil tensions in the major producing areas of the world like the Middle East and West Africa, (5) the availability of refining capacity, (6) the price relationship between heavy fuel oil and crude oil, (7) the price relationship between heavy oil and natural gas, (8) the supply and demand for heavy oil in the domestic market, and (9) the terms of FPL's fuel supply and transportation contracts.

The major driver for crude oil and petroleum product prices during the remainder of 2007 and 2008 will be the continued tensions in the Middle East, West Africa (in particular Nigeria) and other producing regions in the world. With limited spare OPEC production capacity, refineries running near capacity, and growing worldwide demand, any perceived or actual loss of supply due to political or civil unrest in these regions have been, and will continue to be, a major factor in the price of oil to FPL's customers.

World demand for crude oil and petroleum products is projected to increase slightly in 2008 over 2007 average levels, primarily due to increases in demand in the U.S., China and other Pacific Rim countries. Although crude oil production and worldwide refining capacity will be adequate to meet the projected increase in crude oil and petroleum product demand, general adherence by OPEC members to its most recent production accord, and limited spare OPEC production capacity, should prevent significant overproduction of crude oil which, in turn, will result in the continued tight supply of crude oil and petroleum products during most of 2008.

Q. Please provide FPL's projection for the dispatch cost of heavy fuel oil for the January through December 2008 period.

A. FPL's projection for the system average dispatch cost of heavy fuel oil, by month, is provided on page 3 of Appendix I.

Q. What are the key factors that could affect the price of light fuel oil?

A. The key factors are similar to those described above for heavy fuel oil.

Q. Please provide FPL's projection for the dispatch cost of light fuel oil for the January through December 2008 period.

A. FPL's projection for the system average dispatch cost of light oil, by month, is provided on page 3 of Appendix I.

Q. What is the basis for FPL's projections of the dispatch cost of coal for St. Johns' River Power Park (SJRPP) and Plant Scherer?

A. FPL's projected dispatch costs for both plants are based on FPL's price projection for spot coal, delivered to the plants.

Although FPL has historically burned petroleum coke at SJRPP, current and projected delivered petroleum coke prices have risen above the delivered price of coal, resulting in a projected 2008 fuel mix of 100% coal for SJRPP.

Q. Please provide FPL's projection for the dispatch cost of SJRPP and Plant Scherer for the January through December 2008 period.

A. FPL's projection for the system average dispatch cost of coal for this period, by plant and by month, is shown on page 3 of Appendix I.

Q. What are the factors that can affect FPL's natural gas prices during the January through December 2008 period?

A. In general, the key physical factors are (1) North American natural gas demand and domestic production, (2) LNG and Canadian natural gas imports, (3) heavy fuel oil and light fuel oil prices, and (4) the terms of FPL's natural gas supply and transportation contracts.

The major drivers for natural gas prices during 2008 are expected to be: (1) projected natural gas demand in North America will continue to grow moderately in 2008, primarily in the electric generation sector; and (2) with continued increases in domestic rig activity in the U.S. over the past few years, 2008 domestic natural gas production is expected to be slightly higher than average 2007 production levels, as a continued decline in the Gulf of Mexico region is more than offset by increases in Rocky Mountain and Mid-Continent regions. The remaining balance of supply will come from increased LNG imports.

Q. **What are the factors that FPL expects to affect the availability of natural gas to FPL during the January through December 2008 period?**

A. The key factors are (1) the capacity of the Florida Gas Transmission (FGT) pipeline into Florida, (2) the capacity of the Gulfstream Natural Gas System (Gulfstream) pipeline into Florida, (3) the limited number of operational receipt points into the Gulfstream pipeline, (4) the portion of FGT and Gulfstream capacity that is contractually committed to FPL on a firm basis each month, (5) the assumed volume of natural gas which can move from the Gulfstream pipeline into FGT at the Hardee and Osceola interconnects, and (6) the natural gas demand in the State of Florida.

The current capacity of FGT into the State of Florida is about 2,030,000 million BTU per day and the current capacity of Gulfstream is about 1,100,000 million BTU per day. For 2008, FPL has firm natural gas transportation capacity on FGT ranging from 750,000 to 874,000 million BTU per day, depending on the month, and 350,000 million BTU per day increasing to 535,000 million BTU per day on July 1, 2008 of firm natural gas transportation on Gulfstream. FPL projects that during the January through December 2008 period between 155,000 and 605,000 million BTU per day of non-firm natural gas transportation capacity (varying by month) will be available into the state. FPL projects that it could acquire some of this capacity, if economic, to supplement FPL's firm allocation on FGT and Gulfstream. This projection is based on the current capability and availability of the two interconnections between Gulfstream and FGT pipeline systems, as well as the availability of capacity on each pipeline.

Q. **Please provide FPL's projections for the dispatch cost and availability of natural gas for the January through December**

2008 period.

A. FPL's projections of the system average dispatch cost and availability of natural gas, by transport type, by pipeline and by month, are provided on page 3 of Appendix I.

PLANT HEAT RATES, OUTAGE FACTORS, PLANNED OUTAGES, AND CHANGES IN GENERATING CAPACITY

Q. Please describe how FPL developed the projected the Average Net Heat Rates shown on Schedule E4 of Appendix II.

A. The projected Average Net Heat Rates were calculated by the POWRSYM model. The current heat rate equations and efficiency factors for FPL's generating units, which present heat rate as a function of unit power level, were used as inputs to POWRSYM for this calculation. The heat rate equations and efficiency factors are updated as appropriate based on historical unit performance and projected changes due to plant upgrades, fuel grade changes, and/or from the results of performance tests.

Q. Are you providing the outage factors projected for the period January through December 2008?

A. Yes. This data is shown on page 4 of Appendix I.

Q. How were the outage factors for this period developed?

A. The unplanned outage factors were developed using the actual historical full and partial outage event data for each of the units.

The historical unplanned outage factor of each generating unit was adjusted, as necessary, to eliminate non-recurring events and recognize the effect of planned outages to arrive at the projected factor for the period January through December 2008.

Q. Please describe the significant planned outages for the January through December 2008 period.

A. Planned outages at FPL's nuclear units are the most significant in relation to fuel cost recovery. Turkey Point Unit 4 is scheduled to be out of service for refueling from March 30, 2008 until May 4, 2008 or 35 days during the period. St. Lucie Unit 1 is scheduled to be out of service for refueling from October 10, 2008 until November 30, 2008 or 41 days during the projected period.

Q. Please list any changes to FPL's generation capacity projected to take place during the January through December 2008 period.

A. There are no significant changes to FPL's generation capacity in 2008.

<u>WHOLESALE (OFF-SYSTEM) POWER AND PURCHASED POWER TRANSACTIONS</u>

Q. Are you providing the projected wholesale (off-system) power and purchased power transactions forecasted for January through December 2008?

A. Yes. This data is shown on Schedules E6, E7, E8, and E9 of Appendix II of this filing.

Q. In what types of wholesale (off-system) power transactions does FPL engage?

A. FPL purchases power from the wholesale market when it can displace higher cost generation with lower cost power from the market. FPL will also sell excess power into the market when its cost of generation is lower than the market. Purchasing and selling power in the wholesale market allows FPL to lower fuel costs for its customers because savings on purchases and gains on sales are credited to the customer through the Fuel Cost Recovery Clause. Power purchases and sales are executed under specific tariffs that allow FPL to transact with a given entity. Although FPL primarily transacts on a short-term basis (hourly and daily transactions), FPL continuously searches for all opportunities to lower fuel costs through purchasing and selling wholesale power, regardless of the duration of the transaction. FPL can also purchase and sell power during emergency conditions under several types of Emergency Interchange agreements that are in place with other utilities within Florida.

Q. Please describe the method used to forecast wholesale (off-system) power purchases and sales.

A. The quantity of wholesale (off-system) power purchases and sales are projected based upon estimated generation costs, generation availability, expected market conditions and historical data.

Q. What are the forecasted amounts and costs of wholesale (off-system) power sales?

A. FPL has projected 1,840,000 MWh of wholesale (off-system) power sales for the period of January through December 2008. The projected fuel cost related to these sales is $117,801,650. The projected transaction revenue from these sales is $140,663,083. The projected gain for these sales is $19,100,677.

Q. In what document are the fuel costs for wholesale (off-system) power sales transactions reported?

A. Schedule E6 of Appendix II provides the total MWh of energy; total dollars for fuel adjustment, total cost and total gain for wholesale (off-system) power sales.

Q. What are the forecasted amounts and costs of wholesale (off-system) power purchases for the January to December 2008 period?

A. The costs of these purchases are shown on Schedule E9 of Appendix II. For the period, FPL projects it will purchase a total of 1,490,963 MWh at a cost of $106,086,827. If FPL generated this energy, FPL estimates that it would cost $123,453,148. Therefore, these purchases are projected to result in savings of $17,366,322

Q. Does FPL have additional agreements for the purchase of

electric power and energy that are included in your projections?

A. Yes. FPL purchases coal-by-wire electrical energy under the 1988 Unit Power Sales Agreement (UPS) with the Southern Companies. FPL has contracts to purchase and sell nuclear energy under the St. Lucie Plant Nuclear Reliability Exchange Agreements with Orlando Utilities Commission (OUC) and Florida Municipal Power Agency (FMPA). FPL also purchases energy from JEA's portion of the SJRPP Units.

Capacity that FPL purchases through short-term agreements will be lower in 2008 compared with 2007, as FPL's agreements for the output of 2 combustion turbines with Southern Power Company (Desoto) and 3 combustion turbines with Reliant Energy Services (Shady Hills) expired on May 31, 2007 and February 28, 2007 respectively. FPL's 2008 short-term capacity contracts involving the output of specific generating units are with Southern Power Company (Oleander) for the output of 1 combustion turbine and with Reliant Energy Services (Indian River) for the output of three conventional steam units totaling 576 MW. The Southern Power Company (Oleander) agreement expires on May 31, 2012. The Reliant Energy Services (Indian River) contract expires on December 31, 2009.

Additionally, FPL has two short-term capacity arrangements with Williams Power Company and Constellation Energy Commodities Group, Inc. The transaction with Williams Power Company began on March 3, 2006 and runs through December 31, 2009. This transaction is for 106 MW of capacity. The transaction with Constellation Energy Commodities Group, Inc. began on May 1, 2006 and runs through April 30, 2009. The capacity of this transaction is projected to range from 48 MW to 93 MW depending on the availability of transmission service. Lastly, FPL purchases energy and capacity from Qualifying Facilities under existing tariffs and contracts.

Q. Please provide the projected energy costs to be recovered through the Fuel Cost Recovery Clause for the power purchases referred to above during the January through December 2008 period.

A. Under the UPS agreement, FPL's capacity entitlement during the period from January through December 2008 is 931 MW. Based upon the alternate and supplemental energy provisions of UPS, an availability factor of 100% is applied to these capacity entitlements to project energy purchases. The projected UPS energy (unit) cost for this period, used as an input to POWRSYM, is based on data provided by the Southern Companies. UPS energy purchases are projected to be 8,134,439 MWh for the period at an energy cost of $194,489,000. The total UPS energy projections are presented on Schedule E7 of Appendix II.

Energy purchases from the JEA-owned portion of SJRPP are projected to be 3,015,121 MWh for the period at an energy cost of $78,569,000. FPL's cost for energy purchases under the St. Lucie Plant Reliability Exchange Agreements is a function of the operation of St. Lucie Unit 2 and the fuel costs to the owners. For the period, FPL projects purchases of 458,617 MWh at a cost of $2,164,800. These projections are shown on Schedule E7 of Appendix II.

FPL projects to dispatch 545,523 MWh from its short-term capacity agreements at a cost of $43,345,850. These projections are shown on Schedule E7 of Appendix II.

In addition, as shown on Schedule E8 of Appendix II, FPL projects that purchases from Qualifying Facilities for the period will provide 5,929,307 MWh at a cost of $188,840,508.

Q. What are the forecasted amounts and cost of energy being sold under the St. Lucie Plant Reliability Exchange Agreement?

A. FPL projects the sale of 66,877 MWh of energy at a cost of $1,807,900. These projections are shown on Schedule E6 of

Appendix II.

Q. How does FPL develop the projected energy costs related to purchases from Qualifying Facilities?

A. For those contracts that entitle FPL to purchase "as-available" energy, FPL used its fuel price forecasts as inputs to the POWRSYM model to project FPL's avoided energy cost that is used to set the price of these energy purchases each month. For those contracts that enable FPL to purchase firm capacity and energy, the applicable Unit Energy Cost mechanisms prescribed in the contracts are used to project monthly energy costs.

HEDGING/ RISK MANAGEMENT PLAN

Q. Please describe FPL's hedging objectives.

A. The primary objective of FPL's hedging program has been, and remains, the reduction of fuel price volatility. Reducing fuel price volatility helps deliver greater price certainty to FPL's customers. FPL does not engage in speculative hedging strategies aimed at "out guessing" the market.

Q. Does FPL expect that its hedging program will deliver fuel savings each year?

A. No. This is a point that I have emphasized in all my prior testimony on hedging. While FPL is extremely pleased when its hedging program generates net savings for its customers, it does not engage in hedging for this purpose. FPL's hedging strategies are aimed at reducing fuel price volatility. Speculative hedging strategies aimed at "out guessing" the market in the hopes of potentially returning savings to FPL's customers will lead to increased volatility in prices to FPL's customers. FPL cannot predict future fuel prices as there is no certainty in predicting the main drivers of fuel price, such as weather, hurricanes or unstable conditions around the world. What FPL can continue to do is execute a well-disciplined, independently controlled hedging program that reduces fuel price volatility and delivers greater price certainty to FPL's customers. As a consequence of volatility reduction, the hedging program will show savings in some years and losses in others, with the expectation that, over time, the cumulative impact of FPL's hedging program will be neutral and not result in significant savings or losses to FPL's customers. FPL does expect, however, that over time its customers will experience more stable rates as a result of FPL's hedging activities. These objectives and consequences of hedging were recognized and supported by Staff during last year's fuel hearing in Docket No. 060001-EI, where Staff stated in reference to FPL's hedging program (Hearing Transcript, Volume 8, Page 1076): "Their objective is to minimize price volatility. And there are going to be times due to the uncertainty of gas prices when there will gains and losses. Staff will continue to monitor those activities. We believe overall the minimization of price volatility as a goal is appropriate and will produce customer benefits."

Q. Has FPL prepared a risk management plan for 2008, as required by Order PSC- 02-1484-FOF-EI issued on October 30, 2002?

A. Yes. FPL's 2008 Risk Management Plan is provided on pages 5 and 6 of Appendix I.

Q. Is FPL seeking to recover projected incremental operating and maintenance expenses with respect to maintaining an expanded, non-speculative financial and/or physical hedging program for the January through December 2008 period?

A. Yes. FPL projects to incur incremental expenses of $513,425 for its Trading and Operations Group and $83,700 for its Systems Group. By "incremental," I mean that these expenses are not reflected in FPL's base rates. The expenses projected for the Trading and Operations Group are primarily for salaries of the three personnel who were added to support FPL's enhanced hedging program. The expenses projected for the Systems Group are for incremental annual license fees for FPL's volume forecasting software.

Q. Does this conclude your testimony?

A. Yes it does.

BY MR. BUTLER:

Q Mr. Yupp, would you please summarize both of your testimonies, particularly with respect to the subject of hedging?

A Yes, I will.

Good morning, Madam Chairman and Commissioners. The objective of FPL's hedging program is to reduce fuel price volatility. FPL does not engage in speculative hedging strategies aimed at outguessing the market as FPL cannot predict future fuel prices. Instead, FPL executes a well-disciplined, independently controlled hedging program that reduces fuel price volatility and delivers greater price certainty to FPL's customers.

As a consequence of volatility reduction, the hedging program will show savings in some years and it will show losses in other years; however, with the expectation that over time the cumulative impact of hedging will not result in significant savings or losses to FPL's customers. FPL does expect, however, that over time its customers will experience more stable rates as a result of FPL's hedging activities. And that concludes my summaries, or my summary, and I would be happy to answer any questions.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Thank you. And I'm not sure if maybe you can answer the question and then maybe staff can follow up on this one.

We have annual fuel proceedings, and wouldn't those -- or doesn't the annual fuel proceeding reduce volatility?

THE WITNESS: I would answer that to a certain extent I think they do. With an annualized fuel factor, yes, that in and of itself has, does stabilize prices for customers.

However, if we recall back to 2001 when hedging really first was discussed, what, what led to the discussion was the unprecedented rise in natural gas prices going into the winter of 2000/2001. And within that 2001 period we were back up here for midcourse corrections due to underrecoveries because of that rise in fuel prices. And so I think you can say yes, that a yearly factor does stabilize fuel prices to a certain extent; however, it does not eliminate the mechanism where utilities can come back to the Commission and make changes intrayear in the form of a midcourse correction. If fuel prices go up and that puts a utility potentially more than 10 percent out from budget of their, of their budgeted fuel costs for that year, then the utility is obligated to come here, notify the Commission of that fact and potentially make a change to the rate intrayear, to the fuel rate intrayear.

So given that fact, you cannot -- a levelized factor just does not simply stabilize prices for the whole year. With the mechanism of coming back here for midcourse corrections, then there is volatility on an intrayear basis with our fuel expenditures.

COMMISSIONER ARGENZIANO: Madam Chair, a follow-up.

But if you, if -- and I'm trying to grasp all this because I know it's an important issue. But at some point if the cost to the consumer is higher, then at what, you know, at what cost then do you start to change and say this is not worth it? Does it outweigh -- because I still think the annual fuel proceedings overall at the end of the year you're going to minimize the volatility, just not month to month.

THE WITNESS: I think the levelized factor does minimize the volatility as long as there is not a move in the fuel markets on an intrayear basis that would cause a utility to become more than 10 percent either over or underrecovered warranting a change in the fuel factor for that year. If that occurs, that in and of itself is volatility to the customer on an intrayear basis.

As far as whether the cost ultimately at the end of the day is warranted, again, going back to 2001 and really the entire effort moving forward of hedging and what the benefits of hedging would be and is it something we should do for our customers, we spent, we spent quite a bit of time working with staff and the parties on that question. And I think at that period in time, given the unprecedented moves in the fuel markets, we all agreed collectively as a group that our customers wanted stability in their fuel prices. They, they -- when 2001 occurred and gas, you know, went up $2 or $3 or $4 or $5 dollars an MMBtu, the first time we had seen that, that was the main discussion: What do our customers want? Do they want that stable price over a long period of time? And it's been mentioned here today already that at the end of the day or at the end of the, of a long period of time, I think Mr. McWhirter mentioned it, that we believe there will be, and as I summarized, there will be no significant savings or significant losses to our customers, but that what we will have done over that period of time is stabilize fuel prices. So whether we hedge or whether we don't hedge, we would believe that over that given period of time our customers will end up paying the same for their fuel price.

The question is how do they want to pay for it? Do they want to pay for it in more stable rates or do they want to take the swings in the market, being that some years could be very high, some years could be very low? So it's a difficult question. But, but, again, when we went down this road of hedging, it was because everybody believed that customers wanted that stability in their fuel prices, given the fact that volatility appeared that it was here to stay and it was not going anywhere and we were going to go through a period of time where fuel prices were going to move intrayear pretty significantly.

COMMISSIONER ARGENZIANO: Madam Chair. If it's customer stability then, and I guess until I see the ratios, wouldn't it be more stable to physically buy that fuel on a larger percentage than to risk the possibility? Because as you say, it can go either way. And I don't think the customers see volatility now. I think that's what you're saying.

THE WITNESS: I think customers have seen volatility. And I can, I guess I can put it in terms of prior to when our hedged program, I would say, was fully up to speed. In other words, the issue, the order on the hedging resolution was issued in October of 2002, and by sometime mid-2003 or slightly thereafter we had implemented our expanded hedging program.

Prior to 2003 or from 1986 through 2003 FPL had filed for 15 midcourse corrections, all at the end of the day relatively equal. There were, I think, eight filings for underrecoveries and seven for overrecoveries, so we increased and we decreased within that period.

Since mid-2003 we have not had a midcourse correction. And so while hedging does not eliminate the potential, completely eliminate the potential for midcourse corrections, it does mitigate the potential for it. And as we have seen since 2003 with really coming through one of the most volatile periods in fuel prices, particularly natural gas in September of 2005 when Hurricane Katrina came through the Gulf and we saw production shut-ins and really volatile prices, FPL has not been back here for a midcourse correction. And so, so that is the stability that we're talking about to our customers. And I'm not sure I fully answered because I know you talked about physical, and, and I might need a little bit more clarification on that.

COMMISSIONER ARGENZIANO: Well, I mean -- Madam Chair. Actually going in with certainty today to a company that supplies and you say, this is what I'm going to pay you, here's a contract for five years, this is what I'm going to pay, and have some type of certain physical and fiscal commitment, I mean, to me that's stability. And I'm not so certain -- I understand what you're saying since 2003, but isn't it FPL that's $400 million off the mark this time around?

THE WITNESS: Yes. Off, off the mark is, is a strong term. I -- prior to last year, at one point in the first three years of our hedging program it had saved the customers $930 million. And, yes, last year fuel prices did come down and our hedges were in place. And so as you say, we are, we are -- at the end of last year we were net $470 million positive, and by the end of this year we will be in the other direction.

But that, that is not -- it's hard to say that we missed the mark. We are, we are trying to reduce fuel price volatility and we do not speculate on where fuel prices are going. So in order -- there is a trade-off. If you believe that stability for customers is the most important thing that customers want, then, then you will hedge. And you cannot speculate when you're hedging, so you need to lock in your fuel prices, whatever percentage that may be, however you're trying to quantify what your fuel costs could be around a certain range, and you live with the result. There will be years that there are gains that the market goes up from the time you put your hedges on, there will be years when, when customers will have otherwise paid more than they should have or would have had you not hedged. So -- and I'm sorry. I may not be fully answering your question.

On the, on the physical side of it though, I think going back to what, what you had asked there, and maybe an important distinction that was brought up between financial and physical, I don't see a lot of difference between the two from a hedging perspective. We've talked about using financial derivatives. We could, we could simply do that with physical fuel, with physical contracts and lock in the price. There's more liquidity in the financial market; it's easier to transact in that market. And so to go back to, to what another witness had said is most of our physical, of our fuel procurement, FPL's, speaking on behalf of FPL, is, is physical fuel procurement based on an index. And what we do to lock in our price then is use the financial market, whether it be fixed price or whether it be call options. Although call options don't necessarily lock in a price, but they are an instrument that can be used to help mitigate volatility. But we use the financial market to lock in that fixed price.

But our physical fuel procurement is the same as it always has been. We contract with suppliers over various terms of contracts, whether that be one-year, two-year, three-year supply contracts that are based at an index price, and then the financial derivatives will help us secure what that fixed price will be.

COMMISSIONER ARGENZIANO: Madam Chair, if I may. So you don't believe there is less stability in, I guess, the financial versus the physical?

THE WITNESS: Less --

COMMISSIONER ARGENZIANO: Stability as far as the consumer. I guess, I guess what it comes down to is is it the goal to minimize the volatility or minimize the price to the consumer?

THE WITNESS: There is only one goal and that is to minimize volatility. With our hedging program we, we cannot look at whether we're minimizing costs to the customer or whether the customer, customer is, is paying more than they otherwise would have had we not hedged. We can't have it both ways, so to speak.

In reducing volatility you are going to fix a certain percentage of your fuel portfolio. FPL, as a matter of practice, rebalances its hedge positions on a weekly basis. So, in other words, we set a target for the year where we would like to be each month, a percentage of both natural gas and fuel oil that we have hedged. As the market moves during the year, we rebalance our position. So if gas goes down and oil goes up and we project that we're going to burn more gas during the year, then we will rebalance our portfolio to get back to the, to the target levels, you know, that we had originally assumed or wanted to be at.

COMMISSIONER ARGENZIANO: Madam Chair, if I may, just a couple of other questions very quickly because I'm trying to learn a lot about this very quickly.

What happened to your projections? I mean, I understand that hurricane season, the projections there, but it seems that the other companies did something different. And I guess what I'm concerned with is that at what point does the, the, the risk to minimize volatility outweigh the cost to the consumer?

THE WITNESS: In regard to what happened to our projections, I would say this. We do not make projections. We do not make guesses as to where the fuel, where fuel prices will go during the year. Our fuel filing is based off of a forward curve, which, which at that time that we picked that forward curve and for this filing, it happens to be July 24th's forward curve. We believe that forward curve has everything built into it that the market sees occurring right now. And so at that time that is our best guess of, or our best estimate of where the market will be, in this case, in 2008.

So we do not make projections. I think making projections as to, and maybe in this light, as to, okay, well, fuel prices in the summer of 2008 are $7 an MMBtu for natural gas. FPL doesn't believe that. Maybe we think it's going to be $5 an MMBtu, so let's not hedge for the summer period. We do not do that type of hedging. That is what I refer to in my summary as speculative hedging. And I think if you engage in speculative hedging trying to outguess where the market will be, what you will ultimately do at the end of the day is really increase fuel price volatility to your customers. Because I'm not smarter than the market, FPL as a whole is not smarter than the market, and I don't -- and nobody in this room technically is either.

We just don't, we don't know what is going to happen. We don't -- we have projections for weather this winter. We don't know what the winter really holds for us. Will it be warmer than normal? Will it be colder than normal? That will have a great impact on where fuel prices go. Will there be storms in the hurricane season of 2008 as there have not been in 2006 and 2007? Those are tremendous drivers of the market. And to sit here today and say we made a guess of where prices would be, that's not correct. We believe what the forward market says, we believe it incorporates all relevant information, and then the market moves from there and the drivers occur. There are no hurricanes and gas prices come down. Overall that's a good thing for our customers. To the extent that you're not 100 percent hedged, then that unhedged piece of your portfolio, your customers can take advantage of the market coming down.

So I guess long story short, we don't make projections of where the market will be. We implement what we believe is an appropriate level of hedging to manage our fuel costs within 10 percent around our original budget, and we stay that course throughout the, the period, the recovery period.

COMMISSIONER ARGENZIANO: Okay. Just my last comment. And I guess I'm trying to understand what you're saying in a business perspective. But I don't know how you enter into a contract without having some kind of a, of a, of an understanding or idea of where things are going to go. How do you then bargain for the best contract if you do not look into the future? And obviously something, FP&L did something differently than the other companies did when it came to projecting or not projecting the actual fuel prices. And I know that's hard to do, but I just don't understand how you can go into a contract. How do you -- where is the bargaining? How do you know that you're not going too high or too low or --

THE WITNESS: Yeah. And I really wouldn't know what we did different than the other companies, except to say we actual probably hedge at different percentage levels. FPL is predominantly gas and oil and have a very significant portfolio of gas and oil. And so, you know, you're going to see our, our portfolio or our hedge position swing quite significantly during the year for a 10-cent move in the market or whatever, or whatever it may be, 10 cents or a dollar.

And maybe you can just repeat it for me one more time because I do want to answer your question. I don't -- to the contract, while we are hedging financially, we're entering into a contract for a period of time, and maybe that's for a month or for three months. There really is not negotiation that takes place, so to speak. We do negotiate our physical natural gas, in this case procurement contracts. We negotiate, you know, where the delivery point is and, and what, what index we're going to use to set that price. But from a financial derivative standpoint, and if we go back to talking with banks, there is a market. There is a market number that's posted every day. There is not negotiation that goes on in that. That is the number at which the market is willing to transact for that period of time, for, for whatever period of time it is at that given point in time. And so I don't like to use the word "price taker," but there is a market on that day which the banks in the example we're using are willing to sell at and that's what we would, that's what we would take.

Once we have set our hedge percentages, we try to execute in a pretty rigid process. So we have targets that we want to hit. Let's say we're assuming we're going to hedge for 2008. We have, we have targets that we would like to hit at the end of each month during 2007 to say, okay, hypothetically if we wanted to be 60 percent hedged, then by the end of June we would be 10 percent and the end of July 20 percent. And I'm using hypothetical examples. So we have a rigid, we have a pretty rigid process with a lot of checks and balances. And so there are -- we are in the market numerous days and there is a market on that given day and that is the price that we, that we implement our hedges at. I hope that sheds a little more clarity on it.

COMMISSIONER ARGENZIANO: Thank you.

CHAIRMAN EDGAR: Are there questions on cross for this witness? Mr. McWhirter.

CROSS EXAMINATION

BY MR. McWHIRTER:

Q Mr. Yupp, did you hear the questions I asked of Mr. McCallister about hedging activities?

A Yes, I did.

Q If I asked you the same questions, would your answers be the same?

(Laughter.)

A If you could ask me the same questions right now, they might be.

Q I forgot. Schedule H1 attached to Ms. Dubin's exhibit shows that you estimate in, if you'll accept this subject to check, in 2008 you're going to buy 90 million MCF of natural gas. Is that right according to your analysis?

A In two thousand --

Q 2008.

A In 2008 total?

Q Yeah.

A I believe in 2008 total our burn projections are approximately 496 billion cubic feet of gas.

MR. BUTLER: Mr. McWhirter, could you refer to a page in whatever exhibit it is you are referencing just so Mr. Yupp can look at that and hopefully it'll make the discussion clearer?

MR. McWHIRTER: It's Schedule H1 attached to Ms. Dubin's, and it has units of fuel burned and it has MCF and it compares 2005, 2006, 2007 and 2008.

THE WITNESS: Oh, okay. Okay. I am on Schedule H1.

MR. BUTLER: Just for clarity, this has a Number 69 at the bottom of the page. Is that right, Mr. McWhirter?

MR. McWHIRTER: Well, I don't know. Could be.

THE WITNESS: That's -- I have 69 at the bottom of the page, Schedule H1.

MR. BUTLER: Okay. That's fine.

THE WITNESS: And, again, I don't, I don't see the 90 million that you were referring to.

BY MR. McWHIRTER:

Q I was -- about a third of the page down it has -- oh, I guess I'm looking at Btus as opposed to -- okay. Units of fuel burned and then you have barrels of heavy oil, tons of coal, gas MCF, and if you take that out through the fourth column I see 90,566,107.

A I see 496,692,663 on MCF of gas burn projected in 2008.

Q Okay. Well, I must have extracted a page from another year. But irrespective of that, that's a lot of natural gas, isn't it?

A Yes, it is.

Q And what impact would those purchases have on market prices if people knew what you were paying for gas?

A Impact on the market if people knew what we were paying?

Q Yes.

A I'm not sure I follow. Knew what we were paying on our hedge?

Q Knew what you were paying to purchase natural gas, whether you were paying $10 an MCF as opposed to $6 an MCF. Would that affect the market?

A Well, I don't believe it would affect the market. It doesn't quite happen like that.

When we are out for physical procurement for our baseload supply, and we do participate in a spot market on a daily basis to balance our needs as opposed to what we procured upfront going into a month, our physical procurement is done as, as I described before, at index. And so there is no, there is no $10, $6 per MMBtu price tied with it. We are procuring at a, at a physical index when that month settles, that is the price that we are going to pay for physical natural gas.

The financial side of it, the hedging piece of it, is kind of the addition or the subtraction to that index that was used to set the price of the physical natural gas.

Q Is it confidential information the percentage of your contracts you hedge as opposed to just straight physical contract?

A We have kept the, the percentages that we hedge, whether it be financial or even if we will participate in physical, we've kept a percentage of what we're hedging in relation to our entire portfolio confidential. We do believe that speaks to strategy. We do not want to notify the market of, okay, here's FPL and here's what they're going to hedge for this year. And as you pointed out, that's, that's a lot of gas that we project to burn on a yearly basis. And even if we decided to hedge 50 percent, half of that is a lot. To the extent that, that counterparties, counterparties knew, you know, roughly the time frames that we were going to hedge in and how we were going to hedge, we feel that it could be a detriment to our customers that we, that we potentially may not get the, the best value for our customer.

And I go back to there's not a lot of wiggle room, so to speak, when you're dealing with banks or whoever it may be, over-the-counter market. The market is what it is. But we don't want to see prices coming up just because people are aware that Florida Power & Light is in the market hedging on that day because everybody had that information and kind of made the guess that, that we were going to do that.

MR. BUTLER: May I ask for clarification, Mr. McWhirter? Was your question going to the percentage of the total volume that is being hedged or, let's say, if FPL had five contracts, you know, what number of those contracts were hedged using financial derivatives in a spot price versus the number that were on a sort of physical long-term contract fixed price basis?

MR. McWHIRTER: It's the former.

BY MR. McWHIRTER:

Q I wanted to know what percentage of your total purchases you hedge. And if that's confidential, you don't divulge it.

A That is, that is confidential.

Q As I recall the Commission rule when it was being evolved, there was a recommendation that it be at a certain percentage. Do you recall that, or is my recollection as bad as it was about H1?

A I won't say your recollection is bad. But, no, when the order was issued in 2002 there was no, there were no percentages set. There was no recommendation ultimately as to whether financial or physical hedging was best, one better than the other. Basically the order stated that, that the Commission believed hedging was good. It was something that could be beneficial to the customers. The approval to, to increase our hedging programs or expand our hedging programs was granted in there. It was made very clear that transaction fees and other fees associated with hedging were recoverable through the fuel clause, as were gains and losses, and that at the end, at the end of each year we would submit what our hedging transactions were for that entire year and they would be reviewed by the Commission.

Q You mentioned the market. Is -- does the New York Mercantile Exchange, NYMEX, reflect the market that you deal with?

A Yes. I mean, that is one market mechanism for the underlying natural gas market. Yes.

Q Are there other commodities exchanges in which you deal?

A Not commodities exchanges. But I think it was mentioned before and, in fact, even submitted in a response to one set of interrogatories that we had received, we buy our natural gas at least on the physical side at numerous pricing points, whether that be FGT Zone 1, Zone 2, Zone 3 index, inside FERC, beginning of the month. There are a lot of different indices that are used to set the price of our natural gas. It is not just NYMEX. Do we do some NYMEX related contracts? Yes, we do. But our natural gas procurement comes from a wide variety of indices that we use.

Q You establish your price by the indexes. Do these, the people that set these indexes, do they have an exchange like the New York Stock Exchange where you just, you buy from an unknown person and sell to an unknown person or --

A No. For example, in let's just take a Gas Daily, which is a publication in the industry, a Gas Daily FGT Zone 3 Index. Those numbers -- that index is compiled by market information. So at the end of the trading day procurers, for lack of a better word, are polled as to, as to the transactions that they did. And, and I'm not exactly sure how the mechanics of it work, but whether averages are done and there's a high and a low and a mean, that all goes, that actual market data goes to set what the index was for that day.

Q And that deals with the spot market for current purchases.

A Uh-huh.

Q Does it work the same way if you're buying for next July?

A I believe so. And I'm not 100 percent sure of the exact indices that we use for that. Again, we could use NYMEX, we could use an inside FERC number, another publication for, for, you know, setting the monthly settlement. Again, numerous, numerous types of publications.

Q My question may be based upon ignorance of the circumstances, so please forgive me if that's the case. But if I wanted to buy a share of FPL stock, I would go to a stock broker. And let's say I want to buy a share of FPL stock, he would put in a bid at the New York Stock Exchange and, wah-la, some unknown seller would sell me a share of stock at the then market price. Does the commodities market work the same way? You could go to a commodities broker and buy gas futures for July of 2008 from the market from an unknown purchaser?

A I think --

Q Or seller rather.

A -- and I'm not involved in the mechanics of it, but, yes, I mean, it's fairly similar. If I was looking to procure July of 2008 and I wanted one contract in July of 2008 and I called a bank, in the example that we've used, yes, there would be a, there would be a price at which they were willing to sell gas or to fix the price of gas.

Q Well, that was my point. It seems to me that you have exchange transactions and you have bilateral transactions. A bilateral transaction would be one on one between your company and a bank; whereas, an exchange transaction would be from an unknown seller through an exchange. Do both of those, are both of those devices available to you?

A Yes, they are. And I, I think I would say that we use, typically tend to use a lot of bilateral or over-the-counter, as we call it, because of the liquidity in that market, and the ability to transact may be easier in that market.

Q Well, if transactions moved away from an exchange and toward bilateral circumstances, it would appear to me that it would deflate the value of the exchange itself because that doesn't truly reflect the market. The market would be reflected by a combination of both the exchange and the bilateral deal.

A Yes. But I think the, the exchange really does represent the market, and the bilateral market should be a reflection of what the exchange is. That is the, you know, the value of gas on that day.

Now, you know, there obviously could be premiums built into a, an over-the-counter or bilateral transaction by the, by the selling party, you know, to cover what their risk is going out that far in time and locking in the price. But I would say they should mirror each other, with the NYMEX being the underlying, you know, Henry Hub market.

Q What does that mean, "premiums"?

A Maybe premium is, is the wrong term. But there is a bid/ask spread when you're, when you're buying from -- bid/ask spread, there's a bid/ask market. What somebody is willing to buy, what somebody is willing to sell it at.

Ultimately do -- in the over-the-counter market is there a premium -- I say premium. You know, does a bank charge a little bit extra in selling their product because of the risks that they are taking on? They are transferring that risk of where the market may move to them and in exchange you are getting a fixed price for that period of time. I don't, I don't have any numbers to quantify what that may be or whether it really truly does exist. But potentially I think you could, you could see that there may be those types of premiums in that over-the-counter market, which is a compensation for the risk that that counterpart is taking on.

Q Do those premiums exist in the exchange transactions?

A Not that I'm aware of. But, again, I'm not in the mechanics of actually transacting in the market, so I probably can't speak very knowledgeably on that.

Q Do you know why your company tends to favor bilateral contracts over exchange type transactions?

A I think again it's liquidity, the ability to do transactions. Again, we are transacting quite a bit to the extent that we are hedging when you look at our potential gas burns. And so my understanding has always been that there is more liquidity, easier to transact in the over-the-counter market than it would be NYMEX because at times we are doing large volumes of transactions.

Q That would seem counterintuitive to me that you would have greater liquidity in dealing in the bilateral than you would by going to an exchange that has hundreds and maybe thousands of participants.

A And I'm not sure it's exactly like that. So I, again, that starts to get out of my area since I don't transact in that. But, again, just my understanding.

Q Are you familiar at all with your company's conservation programs?

A Not, not in-depthly enough to speak on them, I don't believe.

Q Do you know what the purpose of the conservation programs are?

A I would believe the purpose of a conservation program is to conserve electricity usage.

Q Are you familiar with the term -- I've forgotten what the term was. (Laughter.)

What is it when -- oh, I guess it's elasticity, price elasticity. Are you familiar with that term?

A Somewhat.

Q As I understand the term, it means that people react to prices and they would buy less if the price were higher and buy more if the price were lower. Is that --

A That's generally how I understand it.

Q Do you know from your observation of your customers' habits whether or not they are price elastic?

A I, I do not know that.

Q Do you know how many of your customers have, residential customers have signed up for demand-side management programs where they would be, their service would be interrupted as opposed to buying electricity during certain peak periods?

A I do not know those numbers, no.

MR. McWHIRTER: That's all the questions I have. Thank you.

CHAIRMAN EDGAR: Commissioner Skop. No? And nobody else had questions on cross.

Are there questions from staff?

MS. BENNETT: I have three areas that I'd like to follow up with.

CROSS EXAMINATION

BY MS. BENNETT:

Q My first is I understand that we are also going to get a late-filed exhibit that compares the total fuel purchased in hedging versus spot, and then also hedging versus long-term contracts in comparison; is that correct?

MR. BUTLER: I thought we would probably answer that question as part of what we've identified as the single late-filed exhibit, what was that, 48?

MS. BENNETT: So that would be included in Late-Filed Exhibit 48.

BY MS. BENNETT:

Q Then my next set of questions, Mr. Yupp, I want to understand -- we talked about the goal being stability of prices for customers. When you're talking about stability, are you talking in the year or from year to year price stability? What is Florida Power & Light's goal?

A For us, because of the way we currently hedge, which is, which is really one year out, it's intrayear price stability.

Q Forgive me for not understanding. Intrayear means within the year?

A Within the year. I'm sorry.

Q Okay. And so we don't look in 2007 at the price stability from 2007 to 2008; is that correct?

A Well, in 2007 we are, we are now transacting or hedging for 2008 or we have done that. So, yes, during 2007 we are looking at 2008, but, again, with, with FPL's -- currently the way we hedge being one year at a time, then, then there can be year-on-year volatility. So, you know, predominantly with one year at a time we are looking at that, you know, within the year managing price volatility.

Q Okay. And I think I understood you to say that since you've begun hedging you've not had midcourse corrections; is that correct?

A We have not had a midcourse correction since approximately mid-2003, which is right about the time that I think our hedging program probably reached its fully expanded level. Yes.

Q But isn't it true in 2005 that you had a significant underrecovery in the fuel docket and could have had a midcourse correction in 2005?

A I don't recall the numbers exactly off the, off the top of my head. I know 2005 was, was, you know, an unprecedented year as far as with hurricanes that we had in the Gulf of Mexico and so gas prices were extremely high. I don't recall the exact numbers though of where we were from an underrecovery standpoint.

MS. BENNETT: That's all the questions I have.

CHAIRMAN EDGAR: Commissioners?

Anything on redirect?

MR. BUTLER: Just a few on redirect.

REDIRECT EXAMINATION

BY MR. BUTLER:

Q Mr. Yupp, I'd ask you to consider two alternatives for hedging -- we'll just pick, say, hedging the price of fuel in July of 2008. The first would be to enter into a contract that was actually for physical delivery of fuel at a fixed price in July of 2008. The second would be a contract to purchase fuel from a supplier at the index price for fuel in 2008, but then coupled with a financial instrument that would assure that FPL paid net the same price that it would under my first example of the fix priced contract. Do you understand the difference between the two I'm proposing?

A Yes. Yes.

Q Would there be any difference in the extent of volatility control between those two approaches to hedging?

A No, there would not. You could fix the price on a physical basis and that would be the price you receive, or you could procure your physical gas at an index and lock in that same physical price you did on one side with a financial instrument.

Q And would there be any difference in the utility's and its customers' exposures to potential gains and losses compared to where the spot market ended up between those two approaches to hedging?

A No, there would not.

Q Okay. Does FPL and/or its shareholders make any profits off of its participation in its hedging program?

A No. There is, there is no benefit to, to shareholders. Everything that occurs because of the hedging program, whether that is gains or losses, is, is a pass-through through the fuel clause. I think it was stated earlier, to the extent that there are gains, those, those gains are credited to the fuel clause and ultimately reduce the cost, fuel cost to customers. And, likewise, if there are losses or customers have, would pay more than they otherwise would have had we not hedged, that is also run through the fuel clause and shows up under total fuel expenditures. So there is -- that is it. There is, there is no impact or no gain or benefit related to shareholders. This is -- hedging is done on behalf of the customers for the customers, and all gains and losses go to customers.

MR. BUTLER: Thank you. That's all the redirect that I have.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: May I ask a question? I'm not sure what his first question really asked the witness, and if he could repeat that. Your first question to the witness, I didn't really get that. Were you asking if there was, that I guess there was insurance in either buying physically or, or financially, is that, was that the gist of your question?

MR. BUTLER: Yes.

COMMISSIONER ARGENZIANO: Insurance as a result --

MR. BUTLER: That was the gist of the hypothetical I was setting up. I was trying to compare on the one hand that just hypothetically one buys from a physical supplier of fuel, you know, fuel for delivery in July 2008 at a fixed price. And then the second was that you buy from the supplier of the fuel at the index price in July 2008, so you're going to pay whatever it is when July 2008 arises or arrives. But then you also acquire a financial derivative that would have the effect of FPL paying net under that arrangement the same price that it would have paid under this fixed price long-term contract. That was the idea of the comparison.

COMMISSIONER ARGENZIANO: Okay. And, Madam Chair, if I may. And I guess the answer was that it was basically all the same, it's equal. And I'm not sure how that can be. Because it would -- there's a lot of other things that would go into that, wouldn't there be?

I mean, if you had bought at a fixed price and you were right on target, then it would be the gamble -- it's a gamble either way, isn't it? If you went with financial, as FPL has this time around and has not been close to the mark, I don't know how it would be the same as if -- I guess it would all depend on the decision, what you bought it on a fixed rate for physical versus financial. So I'm not sure they're the same.

MR. BUTLER: Well, what I was trying to illustrate, and you may want to pose the question to Mr. Yupp as well, but just to give you my perspective on it is that -- let's just put some numbers on it. Let's say that one buys gas at a price of $7 per MCF in July. And the first, first alternative was that you actually buy a contract, we'll just say for 100 MCF of gas at $7 per MCF, and that supplier is going to deliver the gas to you in July 2008 and you're going to pay $7 per MCF for it. That's one way you can achieve sort of a hedging effect, which I think would generally be called a physical hedge.

The other thing you can do is to buy the 100 MCF of gas, but under a contract where you're going to pay whatever the market is in July 2008, but then you also go and buy from the bank this derivative instrument that basically says you, FPL, will end up paying $7 per MCF and we, the bank, will make up the difference. We'll either have a nice gain in our pockets if it turns out that the gas was, you know, less expensive than that or we'll end up taking the hit if it's more expensive than that. But you, FPL, will pay, you know, the $7 in either case. Those are the two examples I was trying to compare. As I say, you may want to follow this up with the witness. But in my understanding both the degree of volatility control and the exposure to this idea of a mark-to-market gain or loss would be the same either way. That what we pay, FPL would pay would end up being the $7 whether it's paid directly to the physical supplier of the gas or we pay a certain amount to the physical supplier and then we get this true-up, as it were, from the bank or whatever it was that we entered into the financial derivative with. That was the point that I was trying to get to.

COMMISSIONER ARGENZIANO: Okay. Okay. Thank you.

CHAIRMAN EDGAR: Commissioners, any further questions? Commissioner Skop.

COMMISSIONER SKOP: Thank you, Madam Chair. I'm going to just chime in just as a point of clarification for my behalf. I just want to make sure I've got the facts straight because I by no means have any expertise in hedging.

But just for the witness, I just want to be clear that the fuel is a pass-through cost; is that correct?

THE WITNESS: That is correct.

COMMISSIONER SKOP: Okay. And I think you, I believe you mentioned that the purpose of hedging is to mitigate the risks associated with fuel price volatility; is that correct?

THE WITNESS: That is correct.

COMMISSIONER SKOP: Okay. And I think from 2001 you stated that historically natural gas and oil has been relatively volatile during that period; is that correct?

THE WITNESS: Correct.

COMMISSIONER SKOP: Okay. And with respect to the generation mix specifically for your utility, my understanding is you guys are heavily dependent upon natural gas and oil for your generation; is that correct?

THE WITNESS: That is correct.

COMMISSIONER SKOP: Okay. And noting the historical volatility and dependence upon that, do you feel in your opinion, is it in the customers' best interest to continue with hedging programs?

THE WITNESS: I'll answer that this way. We, we can continue hedging. I think our hedging program has been beneficial to date in reducing fuel price volatility. I think the evidence is there through the midcourse corrections and even some subsequent interrogatory responses where we, where we plot market prices of fuel versus where our charge out cost has been.

As far as whether we should continue or not, the only reason I hesitate on that, and I'm not hesitating on the answer, is that I don't think that, that I could make that decision, so to speak, in a vacuum. I think that's a, a common decision among all of us here. Hedging started, as, as I said, back in 2001. It was a joint effort between the Commission with staff, with all the parties. And I think if we, if we were to now reevaluate, as I think has been brought up, then that should be something that should be done between all of us. What is most beneficial? Do customers want stability? And along with that stability we understand that there will be gains in some years, there will be losses in others. And over the life of the program we believe that there will be no significant impact to customers from a savings or a loss perspective. Or is that not that critical to customers anymore and are customers willing to, to see fuel prices being high and understand that their bill will be high in that period and maybe next year it's low because prices have come down? I think that's a collective decision that would be, that would need to be studied and that decision made amongst all of us here, what is most important and what do customers really want? And I'm not trying to avoid your question and I apologize if that's what it sounds like.

COMMISSIONER SKOP: No, not at all.

Follow-up, Madam Chair. Thank you.

With respect to the volatility of natural gas in particular, because I know that's been a big issue and it's been one of the issues raised for the need to diversify our generation mix into other technologies, has any consideration been given to what price increase would result in terms of natural gas going up from, say, 5 to 7 or to 8 or a sharp spike in volatility, what specific price increase would cause, in the absence of hedging, would cause a midcourse correction?

THE WITNESS: That has been done on the analytical side, and those, that analysis goes into each year the decisions we make on the percentage of fuel to hedge, particularly natural gas. I say particularly, but both natural gas and fuel oil.

I'm not in-depthly involved in the analysis, but, yes, that goes into it because, again, our primary goal in, in managing price volatility is to try to, to manage our fuel expenditures to within 10 percent of what we originally forecast, obviously weighing though that there's a cost associated with hedging. And so where is that balance between the expenditures made and still trying to stay within 10 percent? So, yes, the answer to your question is that most likely has been done within the company.

COMMISSIONER SKOP: Madam Chair, one additional follow-up.

And where I was going with that is just strictly related to the volumes in question. I think that the volumes are substantial, as has been raised on cross-examination. And when you have that much volume and combined with volatility, you know, can send a huge price swing. So, again, it was more towards, I guess, from my own perspective looking at the value of hedging when you're so heavily dependent upon certain commodities for generation. So thank you, Madam Chair.

CHAIRMAN EDGAR: Commissioner Carter.

COMMISSIONER CARTER: Thank you, Madam Chairman.

This is just a historical question. It has probably nothing to do with -- well, maybe tangentially related. In the process -- I think you were involved when they went through the process in '02, '01. Were you involved?

THE WITNESS: Yes.

COMMISSIONER CARTER: What were the rates of increase for the ratepayers at that point in time that led to this? Any, any historical perspective on that?

THE WITNESS: I'm going to say, subject to check, but I think at least in 2001, I believe, and maybe I even have the data with me, but I believe that our first increase was very quick into the 2001 period because the end of 2000 was extremely cold, prices began to run up in the winter of 2001. And I believe that the first time that we were here ball park it was probably $500 million I think was our underrecovery, and that was within, or projected to be within the first two months of the year.

I don't have the particular data with me, but in that year I seem to recall somewhere in that area of, of a couple of times where we were a half a billion dollars. So they were not insignificant. It was an unprecedented rise in gas prices that we had never seen before in that period of time and, given our heavy reliance on natural gas, it had a major impact. So very -- I think that answers your question. At least in 2001 it was significant. I don't have figures here. In 2003 we witnessed the same type of events with a colder than normal winter. And in March of 2003 we saw natural gas prices reach a level to where our combined cycle units at an efficiency of 7,000 heat rate were no longer the most economical units on our system and it was cheaper to burn residual fuel oil. So very large magnitudes of increases.

COMMISSIONER CARTER: And subsequent to that with the implementation of the hedging procedures and program, what -- and I know you said it's primarily volatility is the, is the hallmark. It's probably unfair to ask this question because I think you said that you're not privy to the analysis or anything like that, but -- I won't ask it. Thank you, Madam Chair. I won't ask it.

CHAIRMAN EDGAR: Commissioner Argenziano.

COMMISSIONER ARGENZIANO: Just another question in regards to the stability to the consumer, and I'm not sure how to phrase it, but is it worth the risk of $400 million as you're looking at now not to come in for midcourse corrections?

THE WITNESS: I'm not sure I --

COMMISSIONER ARGENZIANO: I don't know if I'm phrasing that -- it's right now, right now for stability's sake you have -- you're saying that you felt stability was important, you felt the consumer wanted stability intrayear. So this -- the, the hedging that FP&L has, has, have before them now has a $400 million impact; am I correct?

THE WITNESS: Yes. Our net result through 2006 for the life of the hedge program, and we term it from 2002 through 2006, was a positive $470 million.

COMMISSIONER ARGENZIANO: Right. Madam Chair.

But I'm going back to your intrayear. So for this year, $400 million --

THE WITNESS: Right. Uh-huh.

COMMISSIONER ARGENZIANO: -- is it worth -- to me, I'm not sure it doesn't outweigh that risk of that $400 million for the sake of stability, as you say, in coming in for a midcourse correction. I'm trying to figure out was it beneficial or was it not?

THE WITNESS: Well, let me make sure I understand the question. As far as whether we should be in or not, when we make our original projection filing, let's say, for 2008, the hedge positions that we have on at the time, the mark-to-market either gain or loss of those positions is rolled into the factor. And so if your question is should we be in because of the $400 million, the answer would be, no, we project, and I'm not exactly sure what the final number was rolled into '08, but we do not project to end the year at a significant under or -- underrecovery.

I think maybe your, maybe your question is given the fact that it was that loss, was it really worth it then or would it have been better to just buy at spot market and come in and make an adjustment when we had to?

COMMISSIONER ARGENZIANO: Madam Chair. That's exactly my question.

THE WITNESS: Okay. And the answer to that again, I'll go back to my previous answer, I don't know that for sure. I think that that, again, is a collective study of what our -- what do we really want to accomplish here and what is most important to not only FPL's customers but all customers? Is it price stability? Because back in 2001 it was price stability, and that's why we went down the hedging, the hedging road. I referenced the magnitude at least of FPL's underrecoveries in that period of time. And, yes, our customers at that time, we believed they wanted stability. We all studied it and said, yes, hedging can do that. Hedging can deliver price, more price certainty to us. But understanding that customers will at times have paid more than they should have or would have had we not hedged and at times, and at times less. So, again, I'm not avoiding it. I think it would warrant further evaluation as to what now is most important to us.

COMMISSIONER ARGENZIANO: And, Madam Chair.

That's what I'm trying to get at because I see the benefits of hedging but I also see the negatives. And I'm not sure that this year especially that it was not a negative. I mean, there's not a benefit to the consumer even for the sake of stability because at what point does stability outweigh $400 million to the consumer? You know what I'm saying? I understand that there's a place for hedging, and I think, I think maybe in my mind, Commissioners, at some point we need to think about maybe a certain percentage in a fixed -- you know, maybe, maybe adding some, some, some comfort zone to making sure that hedging stays available for the, for the benefits that you obviously see many of the times, but also some protections for when, you know, I think in percentages there may be something that we could think about in the future and maybe have staff look into, see what the benefits could be of changing the percentages or maybe looking at it a little bit. And I'm not saying that it's not a good thing to have the hedging because I see where it can be a benefit. I'm just a little bit worried that maybe at some point if it outweighs the benefit, we need to take a second look at it.

THE WITNESS: And if I may, just, just to further that point though, in the position, in reference to the position we are in now, I would reiterate that we do believe that over a long period of time, and whether that be 20 years or 30 years, if we were to continue hedging with the normal ups and downs in the market, that we don't believe the customer will be impacted significantly. So all the -- you know, from a gain or loss perspective. And although right now we're on the other side of it from where we had been over a billion dollars to the positive, we don't believe the impact would be significant one way or another. But I do understand the, the point you're making.

COMMISSIONER ARGENZIANO: And my final comment to that would be, well, there's still 2008 to come, so.

THE WITNESS: Yes, there sure is.

COMMISSIONER ARGENZIANO: Thank you.

(Laughter.)

CHAIRMAN EDGAR: I think we're on the exhibits.

MR. BUTLER: Thank you. I would move Exhibits 13, 14 and 21.

CHAIRMAN EDGAR: Seeing no objection, Exhibits 13, 14 and 21 will be entered into the record at this time.

(Exhibits 13, 14 and 21 admitted into the record.)

MS. BENNETT: Madam Chair.

CHAIRMAN EDGAR: Yes, ma'am.

MS. BENNETT: The late-filed exhibits, I need to mention to the utilities that this is a bench decision today. And in order to make that decision, we need to have all of the exhibits in so that we need to have a time certain for those late-filed to be to the Commissioners for review.

MR. BUTLER: Madam Chairman, I think that we will be able to provide the exhibit for FPL sometime fairly shortly after the lunch break, which I assume will be sometime in the not too distant future.

CHAIRMAN EDGAR: A little later than I had predicted, but, yes.

MR. BUTLER: So that's -- we're hopeful that actually by the time we resume, but certainly if not that, you know, shortly thereafter that we would be able to provide it.

MR. BADDERS: Madam Chair, I could provide them in about two seconds, if the Commission would request an oral notice of intent for request for confidential classification as well as accept that it is handwritten. We prepared a handwritten, the information in a handwritten form. But I do have it now, if the Commission would like.

CHAIRMAN EDGAR: Commissioners, what is your pleasure? Now orally or, if you want something in writing, we can take it all up after lunch. I have no preferences.

COMMISSIONER ARGENZIANO: How about after lunch.

CHAIRMAN EDGAR: After lunch. Okay. How about we take it all up after lunch, if we can. That would be our goal so that we have it together and neat and orderly. Okay.

MR. BADDERS: We will endeavor to have it after lunch also.

CHAIRMAN EDGAR: Okay.

MR. BEASLEY: As will Tampa Electric Company.

CHAIRMAN EDGAR: Wonderful. Thank you. Okay. So we will plan to address that after the lunch break. And I believe the witness can be excused. Thank you. If we can, Mr. Butler --

MR. BUTLER: Yes.

CHAIRMAN EDGAR: -- I'm sorry -- can we go ahead then and go through the testimony and exhibits with the next witnesses that had been yours that have been excused, and then we can go on lunch break and then begin with the next witness after break.

MR. BUTLER: Okay. That would be fine.

CHAIRMAN EDGAR: Okay.

MR. BUTLER: The next witness for FPL would be Witness Terry Jones. And with the, you know, adjustment to his testimony, the withdrawal of certain portions of it related to the subject of Issue 13A, we would ask that his testimony be inserted into the record as though read.

CHAIRMAN EDGAR: Okay. Can you go ahead and give me, just so we have it all together, if you have it there available, those portions of the testimony that you had referenced previously to be removed prior to admittance?

MR. BUTLER: Oh, geez. Yes. There it is. That was Page 8, Line 10, through Page 18, Line 12, would be the portions that would be deleted or withdrawn.

CHAIRMAN EDGAR: So the prefiled testimony of Witness Jones will be entered into the record as though read, with the removal of the portions that Mr. Butler has described.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

TESTIMONY OF TERRY O. JONES

DOCKET NO. 070001-EI

September 4, 2007

Q. Please state your name and address.

A. My name is Terry O. Jones. My business address is 700 Universe Boulevard, Juno Beach, Florida 33408.

Q. By whom are you employed and what is your position?

A. I am employed by Florida Power & Light Company (FPL) as the Vice President of Nuclear Plant Support.

Q. Please describe your educational background and business experience in the nuclear industry.

A. I received my technical training in the U.S. Naval Nuclear Propulsion Program, serving for eight years. I received my Bachelor of Science degree in Administration from Barry University and my Masters in Business Administration from the University of Miami. I joined FPL at Turkey Point Nuclear Power Plant in 1987 and served in various roles of increasing responsibility until 2007. The positions held included Operations Manager, Maintenance

Manager, Plant Manager, and Site Vice President. Early this year I was appointed Vice President of Nuclear Plant Support. In my present position, I have accountability for Emergency Preparedness, Nuclear Security, Turbine Services, and Reactor Services.

Q. **What is the purpose of your testimony?**

A. My testimony presents and explains FPL's projections of nuclear fuel costs for the thermal energy (MMBTU) to be produced by our nuclear units and the costs of disposal of spent nuclear fuel. I am also updating the status of certain litigation that affects FPL's nuclear fuel costs; plant security costs and new NRC security initiatives; events that occurred during the Turkey Point Unit 3 outage extension in 2006; outage events; and the inspections and repairs to the reactor pressure vessel heads since the issuance of NRC Bulletin (IEB) 2002-02. Both nuclear fuel and disposal of spent nuclear fuel costs were input values to POWERSYM used to calculate the costs to be included in the proposed fuel cost recovery factors for the period January 2008 through December 2008.

Q. **Have you prepared, or caused to be prepared under your direction, supervision or control, an exhibit in this proceeding?**

A. Yes, Exhibit TOJ-1 – Corporate Security Investigative Report is attached to my testimony as a confidential exhibit.

Nuclear Fuel Costs

Q. What is the basis for FPL's projections of nuclear fuel costs?

A. FPL's nuclear fuel cost projections are developed using projected energy production at our nuclear units and their operating schedules, for the period January 2008 through December 2008.

Q. Please provide FPL's projection for nuclear fuel unit costs and energy for the period January 2008 through December 2008.

A. FPL projects the nuclear units will produce 268,189,146 MMBTU of energy at a cost of $0.4233 per MMBTU, excluding spent fuel disposal costs, for the period January 2008 through December 2008. Projections by nuclear unit and by month are in Appendix II, on Schedule E-4, starting on page 15 of the Appendix II.

Spent Nuclear Fuel Disposal Costs

Q. Please provide FPL's projections for spent nuclear fuel disposal costs for the period January 2008 through December 2008 and explain the basis for FPL's projections.

A. FPL's projections for spent nuclear fuel disposal costs of approximately $22.3 million are provided in Appendix II, on Schedule

E-2, starting on page 9 of the Appendix. These projections are based on FPL's contract with the U.S. Department of Energy (DOE), which sets the spent fuel disposal fee at 0.9285 mills per net kWh generated, including transmission and distribution line losses.

Litigation Status Update

Q. Is there currently an unresolved dispute under FPL's nuclear fuel contracts?

A. Yes.

Spent Fuel Disposal Dispute. This dispute arose under FPL's contract with the Department of Energy (DOE) for final disposal of spent nuclear fuel. In 1995 FPL, along with a number of electric utilities, states, and state regulatory agencies filed suit against DOE over its obligation to accept spent nuclear fuel beginning in 1998. On July 23, 1996, the U.S. Court of Appeals for the District of Columbia Circuit (D.C. Circuit) held that DOE is required by the Nuclear Waste Policy Act (NWPA) to take title to and dispose of spent nuclear fuel from nuclear power plants beginning on January 31, 1998.

On January 11, 2002, based on the D.C. Circuit's ruling, the Court of Federal Claims granted FPL's motion for partial summary judgment in favor of FPL on contract liability. There is no trial date scheduled at this time for the FPL damages claim.

The Court of Federal Claims ruled on May 21, 2004 that another nuclear plant owner, Indiana Michigan Power Company, was not entitled to any damages arising out of the Government's failure to begin disposal of spent nuclear fuel by January 31, 1998. On appeal, the U.S. Court of Appeals for the Federal Circuit upheld the Court of Federal Claims decision on September 9, 2005. The impact of this decision, if any, on FPL's claims against the Government remains unknown at this time.

<u>**Nuclear Plant Security Costs**</u>

Q. Please provide an update of the nuclear plant security costs to comply with NRC's requirements.

A. FPL has completed its initial Design Basis Threat (DBT) modifications and continues to maintain the ongoing modifications to comply with the NRC Orders.

Q. What is FPL's projection of the incremental security costs for the period January 2008 through December 2008?

A. FPL presently projects that it will incur $29.5 million in incremental nuclear power plant security costs in 2008.

Q. Please provide a brief description of the items included in this projection.

A. The projection includes adding security personnel as a result of implementing NRC's Order EA03-038, which limits the number of hours security personnel may work in a week; additional personnel training; additional regulatory initiatives for fires, aircraft threat strategy; protection of spent fuel pools and containments and impacts of NRC Part 26 and 73 rulemaking initiatives.

Q. Is there a possibility of further NRC security-related initiatives in 2008 and beyond, in addition to those included in FPL's projection?

A. Yes. As FPL has explained in prior testimony to the Commission, FPL is aware of NRC regulatory initiatives to revise requirements regarding fires, propose aircraft-threat strategy revisions, make potentially significant changes in requirements for protection of spent fuel pools, conduct a study in conjunction with The Department of Homeland Security to evaluate potential threats to nuclear facilities from land, sea and air attacks, and conduct a study of buffer zones around nuclear sites. There is also a NRC initiative to review and update the Enhanced Adversary Characteristics (EAC) of the Design Basis Threat (DBT). The DBT is the measure that all nuclear stations are designed to defend against. Some of these

EAC/DBT enhancements could require extensive engineering support and significant modifications to station security defensive positions.

In addition, FPL is aware of two new NRC security-related initiatives. The NRC is in the process of revising the current fatigue order by issuing a rule under Part 26. The new rule will mandate "days off" for the security officers at the St. Lucie and Turkey Point sites. The Part 26 rulemaking impacts costs are unknown in the industry at this time, but may result in the need to add additional officers to meet this revised requirement.

NRC Part 73.55 rulemaking may involve the need for significant modifications to various areas of the site. Some examples include redundant features for Central Alarm Station (CAS) and Secondary Alarm Station (SAS), enhanced weaponry, Owner Controlled Area (OCA) detection, and possible enhancements to assessment and interdiction. Currently, the industry and the NRC view the impact differently since the industry believes a literal interpretation of the proposed rule varies greatly from the NRC's stated intent. Nuclear Energy Institute (NEI) has 200 pages of comments discussing the impact of this rule. NEI estimates that the cost of rulemaking, based on literal interpretation, could range from $20-60 million per site.

It is not feasible for FPL to estimate at this time the future costs that will be required to comply with these various developing regulatory requirements, but the Commission should be aware that nuclear security costs could increase significantly based on the issues mentioned above.

~~2006 Turkey Point Outage Extension (Pressurizer Piping Incident)~~

Q. Please provide a brief description of the outage extension at Turkey Point Unit 3 in March and April of 2006.

A. Toward the end of Turkey Point Unit 3's spring 2006 refueling outage, FPL personnel identified a small drilled hole in the pressurizer piping on Unit 3 during of a series of tests and inspections that were conducted to ensure that equipment was operating properly prior to plant heat-up and restart. FPL conducted an extensive review of the unit to ensure no other systems were damaged. Prompt and effective corrective actions were taken by plant personnel to repair the pressurizer piping and provide the appropriate assurances of safety for restart. Unit 3 was restarted on April 10, 2006, which was an extension of approximately 5 days to the planned refueling outage.

The FBI and FPL's Corporate Security Department have both conducted investigations to determine who drilled the hole and under what circumstances. Those investigations commenced immediately after the drilled hole was discovered on March 31, 2006. FPL arranged to log access suspensions in the Nuclear Energy Institute's Personnel Access Data Base ("PADS") for all personnel who had entered the Turkey Point nuclear unit containment area during the period March 9-31, 2006 and to reinstate access for each person only after he or she had completed an FBI interview and psychological screening tests. This was an extraordinary measure, because it temporarily removed a large number of qualified nuclear personnel from the pool of available workers for plants around the country and hence required a high level of cooperation from all levels of the nuclear industry, including plant licensees and service vendors. The investigations were extremely thorough and, as a result, lasted more than a year. Both investigations are substantially complete at this time. FPL's Corporate Security Department issued an Investigative Report summarizing both its and the FBI's investigation, which is attached as confidential Exhibit TOJ-1.

Q. What conclusions have the FBI and FPL reached about how the hole was drilled in the pressurizer piping?

A. FPL's and the FBI's investigations have reached the same conclusion: the hole was drilled by a single individual, working alone. The individual was employed by a contractor FPL hired to perform services in support of Unit 3's Spring 2006 refueling outage. The individual had been granted unescorted access to the Turkey Point nuclear plant in early March 2006 after completing FPL's comprehensive access authorization and fitness-for-duty screening. Neither investigation has identified a definitive motive for this individual's actions.

Q. What is "unescorted access"?

A. "Unescorted access" means that a person is permitted to enter specified portions of a nuclear unit's protected area in order to perform assigned work, without having to be accompanied by a security guard. The system of granting personnel unescorted access upon successful completion of appropriate screening is universally accepted and used within the nuclear industry. It is logistically essential if the complex activities undertaken at the time of a refueling outage are to be performed promptly and efficiently.

Q. What actions has FPL taken with respect to the individual that FPL's and the FBI's investigations identified as having drilled the hole in the pressurizer piping?

A. The individual's access to FPL's nuclear plants was revoked promptly upon discovery of the drilled hole and will not be renewed in the future.

Q. Has the NRC also investigated this incident?

A. Yes, it has. The NRC formed an Augmented Inspection Team (AIT) that investigated this incident thoroughly. The AIT did not focus on the specifics of how the hole was drilled, but rather on the adequacy of FPL's security processes at Turkey Point and how FPL ensured that Unit 3 was ready for restart once the drilled hole was found.

Q. What were the findings of the AIT?

A. The AIT concluded that FPL's identification, classification, and response to the damage event were appropriate. In addition, the AIT found that the planned actions to ensure restart readiness for Unit 3 and continued operation of Unit 4 were effective and thorough. The AIT also noted that FPL appropriately positioned security officers at access points leading into containment, that access authorization personnel were knowledgeable in the area of access authorization, and that personnel were appropriately cleared before gaining unescorted access to the site. No findings or violations were issued by the NRC. The NRC informed FPL that it had reacted well in a difficult situation.

Q. Please describe the process used by FPL to screen personnel who will have unescorted access to protected areas within its nuclear plants.

A. Pursuant to NRC regulations, FPL has access authorization and fitness-for-duty (FFD) programs that apply to all persons who are granted unescorted access to nuclear power plant protected areas. FPL requires all personnel with unescorted access to nuclear facilities to pass a rigorous security screening. These processes are consistent with the standards and processes used across the nuclear industry and pursuant to applicable NRC requirements. Specifically, each individual who seeks unescorted access to an FPL nuclear plant (whether an FPL employee or contractor employee) is subjected to the following screening:

- Plant access authorization approval in advance by an FPL supervisor. The FPL supervisor reviews the work requirements of the individual and selects access to only those areas of the plant that are necessary to accommodate the individuals' work requirements.

- Each individual is subject to a detailed background investigation, including verification of employment history, credit check, and a character verification including reference checks, and where applicable, education and military checks.
- Each individual is required to pass a rigorous psychological examination consisting of nearly 600 questions, with the responses screened for psychological stability and other characteristics. As required, individuals may be subject to further psychological review including interviews by a licensed psychologist.
- Each individual is required to successfully complete an FBI criminal history verification, including fingerprints, with no disqualifying criminal background.
- Each individual must successfully complete drug and alcohol screening and is then subject to random drug and alcohol testing during the period of unescorted access.

Failure to successfully complete any of these steps will result in the individual being denied unescorted access to FPL's nuclear facilities.

Q. **Had all personnel who access to Turkey Point Unit 3 during the Spring 2006 refueling outage been screened prior to that outage in accordance with these procedures?**

A. Yes. In total, 1137 personnel entered the containment of Turkey Point Unit 3 during the outage. Each of these personnel, including the individual identified as having drilled the hole in the pressurizer piping, was subject to and successfully completed FPL's rigorous access and fitness for duty screening processes.

Q. What measures does FPL have in place to control access to nuclear power plant protected areas once unescorted access is granted?

A. FPL carefully controls access to its nuclear plants, especially within the vital areas such as the containment structure where the pressurizer piping is located. Each individual granted unescorted access to a nuclear plant is also screened by their supervisor for access to vital areas. Even after access is granted through the process that I described earlier, the access level for each individual is reviewed monthly thereafter by their supervisor. In addition, all individuals are subject to an ongoing behavioral observation program. This program is specifically designed to detect and require the reporting of behaviors which are not consistent with unescorted access, and also to identify changes in behavior, mood and other relevant criteria which are reported to security and are the subject of additional evaluation and management action, as may be required. Additionally, each person with unescorted access to the plant is required to complete re-qualification Plant Access Training for unescorted access as well as access to radiation controlled areas. During refueling outages, FPL deploys security officers to verify access into the containment structure. FPL also utilizes cameras to monitor work activities throughout the refueling outage.

All of the processes I have described were in full force and effect and were applied to all personnel who had unescorted containment access during the Spring 2006 Turkey Point Unit 3 refueling outage, including the individual who drilled the hole in the pressurizer piping. He had been authorized to have unescorted access to the area in Unit 3 where the pressurizer piping is located. There was no report of aberrant behavior by that individual that would have warranted revoking or limiting his access.

Q. In addition to access control and worker screening, does FPL have other security measures in place to protect the nuclear plant site from damage or theft?

A. Yes. FPL has an extensive security program to protect against acts of radiological sabotage and to prevent theft of nuclear material. The specifics of these programs constitute safeguards information, so I cannot discuss those specifics publicly. However, I can confirm that these programs conform in all respects to NRC requirements, are inspected periodically by the NRC, and are internally audited by FPL Nuclear Assurance in order to assess and determine compliance with the security requirements. At all relevant times, including during the Spring 2006 Turkey Point Unit 3 refueling outage, FPL maintained these programs consistent with NRC requirements. Of course, it is infeasible to monitor the location and activities at all times for each of the hundreds of personnel who have unescorted access during a refueling outage.

Q. Has the NRC or FPL Nuclear Assurance identified any deficiencies in FPL's security program that contributed to this event?

A. No. None of the previous NRC inspections or FPL Nuclear Assurance audits identified any uncorrected deficiencies that could have contributed to the drilled hole incident that occurred at Turkey Point Unit 3.

Q. From the results of the NRC's, the FBI's and FPL's internal investigations, do you conclude that FPL had appropriate measures in place to provide a high degree of protection for Turkey Point against the risk of criminal acts such as that which occurred?

A. Yes. FPL's security programs clearly provide a high degree of protection and represent a prudent response to the risk of such criminal acts taking place. However, it is important to recognize that no security program – at a nuclear plant or elsewhere – is infallible. Even the most rigorous access-control, worker-screening and security programs, can identify and prevent only a high percentage of potential personnel problems; they can never provide 100% protection against deliberate criminal acts, carried out by individuals with no prior history of such acts. That is why both the security systems and plant safety system have many layers of defense to ensure the health and safety of the public. This is called "Defense in Depth".

Q. Does FPL need to take additional measures to prevent recurrence of tampering incidents?

A. As I mentioned previously, FPL will exclude the individual who drilled the hole from ever working at any FPL nuclear plant in the future. Beyond that, given the rigor of our existing security processes, FPL does not believe that systemic changes are warranted. The NRC has concurred in that conclusion.

Q. Should FPL be held responsible for the replacement power costs incurred as a result of the Turkey Point Unit 3 outage extension?

A. No. FPL witness Dubin discusses the regulatory policies associated with recovery of replacement power costs, but speaking from the

~~perspective of nuclear operations, I see nothing that could warrant criticism in FPL's actions before or after the drilled hole was discovered. FPL management took extensive, reasonable and rigorous actions that complied fully with NRC requirements and industry standards in order to prevent improper access and deliberate criminal acts. FPL is not aware of, nor has anyone else indicated, any reasonable actions that could have been taken to prevent the criminal act that extended the Unit 3 outage. FPL took extensive actions to swiftly and effectively investigate and inspect both Turkey Unit 3 and Unit 4 after the criminal act was discovered, enabling FPL to expeditiously return the plant to service with minimal disruption in production.~~

<u>2007 Outage Events</u>

Q. Has FPL experienced in unplanned outages at its nuclear plants in 2007?

A. Yes. In June 2007, Turkey Point Unit 3 was shut down due to repetitive problems with the output signals from its rod position indicators (RPIs). These problems were traced to failures in a set of electrical connectors providing signals from the RPIs to the control room. The connectors were replaced and, because similar connectors had been used in Unit 4, that unit was shut down in July

2007 and the connectors were replaced proactively there as well. The outages were for 17 days at Unit 3 and 6 days at Unit 4.

St. Lucie Unit 2 shut down in August 2007 to investigate and repair a leak in the reactor coolant system. Upon shutdown, the leak was traced to a crack in the seal injection line that supplies the 2B1 Reactor Coolant Pump (RCP) seal.

FPL is in the process of investigating and evaluating these outages.

<u>Reactor Pressure Vessel Head Inspection Status</u>

Q. What is the status of the reactor heads for the St. Lucie and Turkey Point Units?

A. As FPL has explained in prior testimony to the Commission, the NRC issued IEB 2002-02 on August 9, 2002 to address concerns related to visual inspections of the reactor heads. This NRC Bulletin resulted in all four FPL units being categorized as high susceptibility, requiring ultrasonic testing in addition to visual inspections until the reactor heads are replaced. St. Lucie Unit 1 replaced the reactor vessel head during the refueling outage beginning on October 17, 2005. The St. Lucie Unit 2 reactor vessel head will be replaced in the Fall of 2007 at the same time the Unit 2 steam generators are replaced. The Turkey Point Unit 3 and 4 reactor vessel heads were replaced during the refueling outages beginning on September 26, 2004 and April 10, 2005 respectively.

Q. Does this conclude your testimony?

A. Yes it does.

STATE OF FLORIDA)
: CERTIFICATE OF REPORTER
COUNTY OF LEON)

I, LINDA BOLES, RPR, CRR, Official Commission Reporter, do hereby certify that the foregoing proceeding was heard at the time and place herein stated.

IT IS FURTHER CERTIFIED that I stenographically reported the said proceedings; that the same has been transcribed under my direct supervision; and that this transcript constitutes a true transcription of my notes of said proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorneys or counsel connected with the action, nor am I financially interested in the action.

DATED THIS 16th day of November, 2007.

Linda Boles

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