BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

PETITION FOR INCREASE IN RATES BY PROGRESS ENERGY FLORIDA, INC. /	DOCKET NO. 090079-EI
PETITION FOR LIMITED PROCEEDING TO INCLUDE BARTOW REPOWERING PROJECT IN BASE RATES, BY PROGRESS ENERGY FLORIDA, INC. /	DOCKET NO. 090144-EI
PETITION FOR EXPEDITED APPROVAL OF THE DEFERRAL OF PENSION EXPENSES, AUTHORIZATION TO CHARGE STORM HARDENING EXPENSES TO THE STORM DAMAGE RESERVE, AND VARIANCE FROM OR WAIVER OF RULE 25-6.0143(1)(C), (D), AND (F), F. A. C., BY PROGRESS ENERGY FLORIDA, INC. /	DOCKET NO. 090145-EU

VOLUME 14

Pages 1902 through 2002

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PROCEEDINGS: HEARING

COMMISSIONERS PARTICIPATING:
CHAIRMAN MATTHEW M. CARTER, II
COMMISSIONER LISA POLAK EDGAR
COMMISSIONER KATRINA J. McMURRIAN
COMMISSIONER NANCY ARGENZIANO
COMMISSIONER NATHAN A. SKOP

DATE: Friday, September 25, 2009

TIME: Commenced at 9:33 a.m.

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: LINDA BOLES, RPR, CRR
Official FPSC Reporter
(850) 413-6734

PARTICIPATING: (As heretofore noted.)

I N D E X

WITNESSES

EXHIBITS

NUMBER:		ID.	ADMTD.
169	HWS-Appendix A	1910	2001
170	HWS-1	1910	2001
171	HWS-2	1910	2001
172	HWS-3	1910	2001

P R O C E E D I N G S

(Transcript follows in sequence from Volume 13.)

CHAIRMAN CARTER: Good morning. I'd like to call the hearing to order.

Before we begin, staff, are there any preliminary matters?

MS. FLEMING: Commissioners, I am not aware of any other preliminary matters. But I would like to note that we did hand out the updated schedule for today. The Commissioners and all the parties have received a copy of this.

CHAIRMAN CARTER: Okay. Is that correct, the parties have the, the Friday version of the list?

MS. KAUFMAN: Yes.

CHAIRMAN CARTER: Okay then. The Friday AM, yeah, the Friday AM version.

Call your next witness.

MR. REHWINKEL: The Citizens of Florida call Helmuth W. Schultz, III.

CHAIRMAN CARTER: Okay. I think Mr. Schultz has already been sworn. I saw him yesterday.

MR. REHWINKEL: Yes, he has.

THE WITNESS: That is correct.

CHAIRMAN CARTER: Okay.

HELMUTH W. SCHULTZ, III

was called as a witness on behalf of the Office of Public Counsel and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. REHWINKEL:

Q. Mr. Schultz, could you give your name, address and employer to the Commission, please?

A. My name is Helmuth W. Schultz, III. I'm employed by Larkin & Associates PLLC, 15728 Farmington Road, Lavonia, Michigan.

Q. Mr. Schultz, did you cause to be prepared prefiled direct testimony of 59 pages in this docket?

A. Yes, I did.

Q. Do you have any corrections or changes to make to that testimony?

A. I have a few.

Q. Could you tell those to the Commission at this time?

A. Yes.

On Page 22, Line 6 in the question, the word "adjustment" needs an N inserted into it.

On Page 37, in reviewing some information, I found that the sentence that starts on Line 21, "The pole inspection costs for 2010 are .8 million more than

2008," is incorrect. So I would just strike that sentence. And change the "Therefore approximately 7.7 million" should read "Therefore approximately 8.5 million."

On Page 42, based on further review, the sentence beginning on Line 3 that says, "Assuming the unit operates "and concludes with "six years," that sentence should be stricken.

On Page 44, Line 12, the word "be" should be "by ratepayers."

On Line, or on Page 45, Line 10, it begins by saying "Even though the a," the word "a" should be crossed off.

On Schedule C3 --

MR. REHWINKEL: We'll do the schedules at a later time.

THE WITNESS: Okay.

BY MR. REHWINKEL:

Q. Mr. Schultz, with those changes to your testimony, if I asked you the questions contained therein, would your answers be the same?

A. Yes, they would.

MR. REHWINKEL: Mr. Chairman, at this time I would ask that Mr. Schultz's prefiled direct testimony be admitted into the record.

CHAIRMAN CARTER: The prefiled testimony of the witness will be inserted into the record as though read.

BY MR. REHWINKEL:

Q. Mr. Schultz, did you also cause to be prepared several schedules, including an Appendix A with your qualifications, and Schedules HWS-1, HWS-2 and HWS-3?

A. Yes, I did.

Q. Do you have any changes or corrections to make to those schedules?

A. I noted on Schedule C-3, Page 2 of 2, again, I had a spelling error in the word "adjustment." There's an X -- there's a "Y" in there that does not belong. That's just above Line 6.

Q. This is in HWS-1?

A. HWS-1, Schedule C-3, Page 2 of 2. The title just above, description just above Line 6.

Q. Okay. Is that the only change you have?

A. Yes.

MR. REHWINKEL: Mr. Chairman, at this time I would ask that --

CHAIRMAN CARTER: What are those numbers for the, on staff's Comprehensive Exhibit List, Mr. Rehwinkel?

MR. REHWINKEL: This is 170, 171 -- no. 169, 170, 171 and 172.

CHAIRMAN CARTER: Thank you so much. Appreciate it.

MR. REHWINKEL: And those have already been given a number, so --

CHAIRMAN CARTER: Absolutely.

(Exhibits 169 through 172 marked for identification.)

DIRECT TESTIMONY

OF

Helmuth Schultz III

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

Docket No. 090079-EI

I. STATEMENT OF QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Helmuth W. Schultz III. My business address is 15728 Farmington Road, Livonia Michigan 48154.

Q. BY WHOM ARE YOU EMPLOYED?

A. I am a Senior Regulatory Analyst with Larkin & Associates P.L.L.C.

Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCITES, P.L.L.C.

A. Larkin & Associates, P.L.L.C. performs independent regulatory consulting primarily for public service/utility commission staffs and consumer interest groups (public counsels, public advocates, consumer counsels, attorney generals, etc.). Larkin & Associates, P.L.L.C., has extensive experience in the utility regulatory field as expert witnesses in over 600 regulatory proceedings including water and sewer, gas, electric and telephone utilities.

Q. HAVE YOU PREPARED AN APPENDIX WHICH DESCRIBES YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE?

A. Yes. Attached as Appendix I, is a summary of my background, experience and qualifications.

Q. BY WHOM WERE YOU RETAINED, AND WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. Larkin & Associates, P.L.L.C., was retained by the Florida Office of Public Counsel (OPC) to review the rate increase requested by Progress Energy Florida (the Company or PEF). Accordingly, I am appearing on behalf of the citizens of Florida ("Citizens") who are customers of PEF.

Q. ARE ANY ADDITIONAL WITNESSES APPEARING ON BEHALF OF THE FLORIDA OFFICE OF PUBLIC COUNSEL?

A. Yes. Kim Dismukes, of Acadian Consulting, is presenting testimony on affiliate transactions. Jacob Pous is presenting testimony on the over-recovery of depreciation expense and the associated excess depreciation reserve. Daniel J. Lawton will address the ratemaking policy and financial implications surrounding the Company's over-recoveries of depreciation expense and the associated excess depreciation reserve. Additionally, Dr. J. Randall Wooldridge is presenting testimony on the OPC's recommended rate of return.

<u>II. BACKGROUND</u>

Q. PLEASE BRIEFLY DESCRIBE THE GENESIS OF THIS PROCEEDING.

A. On March 20, 2009 Progress Energy Florida filed its Minimum Filing Requirements (MFR's) requesting a revenue increase of $499.997 million. Corrections have been made since the filing however the amount of increase has not been revised by the Company. We analyzed the Company's filing, issued discovery and evaluated the responses to PEF's discovery responses, including the Commission Staff (Staff). Based on the analysis performed and the recommendations of the OPC's other consultants it was determined that the Company's request for an increase of $499.997 million is excessive and should be denied. The Company should not be allowed an increase and instead rates should be reduced by at least $35.038 million. The results of the OPC witnesses findings are summarized on Exhibit HWS-1, Schedule A-1. Rate base and rate base adjustments are detailed on the B schedules and adjustments to operating and maintenance costs are detailed on my C schedules. The proposed capital structure is presented on Schedule D.

Q. PLEASE EXPLAIN WHY THE COMPANY'S REQUEST IS OVERSTATED?

A. The Company has proposed increases in costs that factor in inflation, an increase in the employee complement, business as usual pay increases, bonuses, a significant increase in operations and maintenance expenses, increased depreciation expenses that are not justifiable, as explained by Mr. Lawton and Mr. Pous, and an excessive rate of return as explained in detail by Dr. Woolridge. Given the current state of the economy and the difficulty that customers are experiencing the excesses requested are definitely inappropriate. Since the fall of 2008, companies and governmental agencies have been cutting costs, freezing and/or limiting pay increases and cutting benefits. Yet the Company has taken the approach that a similar belt tightening effort is not required largely because they are a regulated utility in a monopoly that is to some degree more sheltered from the economic conditions than non-regulated businesses.

Q. HOW IS THE COMPANY SHELTERED MORE THAN THE NON-REGULATED COMPANY?

A. The Company is a monopoly and its customers do not have the choice of looking elsewhere for lower cost energy. When costs go up, the customers are limited in how much they can reduce their demand for energy. When rates are set without regard to the state of the economy and the impact it has on the captive customer base, then those customers have only two choices; (1) pay the rate or (2) stop using electricity. The second choice is not much of an alternative. Non-regulated companies compete and if they do not cut costs, the cost increases will drive up prices to a level that will motivate the customer to either shop elsewhere or simply do without the unregulated company's product. In my opinion this filing does not reflect an attempt by the Company to minimize costs and to take into consideration the economic impact that its business as usual increases will have on customers. In fact this request compounds the inequity already imposed on customers because the Company is being compensated for costs for plant that is not even used and useful, which is in direct contradiction to the traditional general theory of ratemaking.

III. NUCLEAR FUEL BALANCE

Q. WHAT DID YOU DETERMINE FROM YOUR REVIEW OF THE COMPANY'S REQUEST FOR AN INCREASE IN THE NUCLEAR FUEL INCLUDED IN RATE BASE?

A. The Company's requested Net Nuclear Fuel of $155.017 million is not supported by the Company's witness and/or the filing. According to Company Schedule B-16 the witness responsible for the Nuclear Fuel amount included in rate base is Sasha Weintraub. In reviewing the testimony of Sasha Weintraub I was unable to find any discussion that would explain why the amount included in rate base increased from a net average of $86.294 million in 2008 to $155,017 million in 2010. In my review of the filing, the Company indicated in Supplemental Schedule F-8 that in 2009 the Company would acquire approximately $41 million of nuclear fuel. The Schedule F-8 for 2010 indicated that approximately $29 million of nuclear fuel is expected to be purchased. The sum of the purchases would increase the balance by $70 million but after accounting for the amortization that occurred in 2009 and 2010 there is an unexplained difference.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO THE NUCLEAR FUEL INCLUDED IN RATE BASE?

A. Yes. As shown on Exhibit HWS-1, Schedule B-3 the Company's requested for Net Nuclear Fuel of $155.017 million should be reduced $32.766 million ($26.752 million jurisdictional) to $122.251 million.

Q. HOW DID YOU DETERMINE YOUR RECOMMENDED ADJUSTMENT TO THE NUCLEAR FUEL INCLUDED IN RATE BASE?

A. In 2009 I started with the Company balance for December 2008 and each month I added to that one twelfth of the $41 million of nuclear fuel expected to be purchased and deducted one twelfth of the approximate $21.188 million of amortization included on Company Schedule B-16, Page 2 of 3. In 2010 I continued with the calculated balance as of December 2009 and then each month I added to that one twelfth of the $29 million of nuclear fuel expected to be purchased and deducted one twelfth of the approximate $36.283 million of amortization included on Company Schedule B-16, Page 1 of 3.

Q. WHY SHOULD THE COMMISSION ACCEPT YOUR RECOMMENDED ADJUSTMENT TO THE NUCLEAR FUEL AMOUNT INCLUDED IN RATE BASE?

A. The Company filing should support the amounts requested. The Company failed to even identify the change in the original filing. The amount requested was just included. The only attempt to correct the deficiency was the supplemental filing of Schedule B-5 on March 27, 2009. That supplemental schedule simply stated that in 2009 the balance increased by 50.67% to provide working stock and protection against supply interruption. The $68.723 million ($155.017 million - $86.294 million) increase in rate base is of the magnitude that requires sufficient justification in the filing. The Company is obligated to provide that justification when it files. Because the Company failed to justify the amount requested an adjustment is required. By not sending a signal to the Company for its failure to sufficiently explain the significant increases reflected would be the same as giving the Company a blank check for any increase in rates desired.

IV. STORM RESERVE ACCRUAL AND RESERVE BALANCE

Q. DID YOU REVIEW THE COMPANY'S REQUEST FOR AN INCREASE IN THE ANNUAL STORM ACCRUAL?

A. Yes, the Company's witness Peter Toomey recommends an annual accrual of $16 million on a system basis and $14.922 million on a retail basis. The intent is to maintain a reserve of approximately $150 million. The accrual amount and the requested reserve are based on an analysis performed by the Company's witness Steven Harris.

Q. ARE THERE CONCERNS WITH THE COMPANY'S REQUEST FOR AN INCREASE IN THE ANNUAL STORM ACCRUAL?

A. Yes. The Company's reserve has increased significantly over the past three plus years due to the collection of a surcharge from customers and also due to the low level of charges against the reserve. The Company's witness Mr. Toomey has stated the annual accrual of $16 million is "equivalent to the expected average recoverable storm loss" from Mr. Harris' study. There are concerns with the focus of the study, the assumptions made, recent history and the conclusions that resulted from the study. There is also a concern with what may not have been factored and/or identified in the study and Company testimony.

Q. WHAT IS THE CONCERN WITH THE FOCUS OF THE STUDY?

A. Mr. Harris's testimony indicates that a focus was placed on four alternative reserve accruals, none of which made any assumption on what would happen if a lower annual accrual were made. This fact was confirmed in the response to OPC Interrogatory No. 365. That suggests that it was pre-determined that the only way to adjust the accrual was to increase it.

Next there was a focus on the historical storms, with an emphasis made on a 1921 storm that hit Pinellas County. Because of the magnitude of that storm it was estimated that the damage could reach $250 million. The worst case scenario is presented with no emphasis on other storms of similar magnitude or even the mentioning of the statistical probability that a comparable storm to the 1921 storm could strike that area. I believe that historical storm information is relevant but storm information should be specific to the PEF service territory. And while Pinellas County is the Company's most densely populated service territory, there are significantly larger geographical areas served by the Company with a statistically higher probability of landfall, where a major storm strike might not produce damage that would exceed the existing storm reserve.

Q. **WHAT ARE YOUR CONCERNS WITH THE ASSUMPTIONS INCORPORATED IN THE STUDY?**

A. Mr. Harris's testimony states that the study determined an average annual loss of $20.2 million. This assumption is a significant driver in the determination of the estimated reserve results. According to the study (Page 1-1) the loss was computed using the results of thousands of random variable storms. As indicated earlier, the use of storm data that may be applicable to areas outside of the PEF service territory could skew the results. There is also the concern that the study provides no indication as to what factors were used to determine an average annual loss rate of $20.2 million. The fact is that since 1994, with the exception of 2004 and 2005, the Company has only charged anywhere from $0 to $9.9 million to the reserve in any one year or an average of $3 million.

Based on Mr. Harris' testimony at page 11, the analysis took into consideration the 1921 storm and the fact that if that storm occurred there would be an estimated $250 million of damages to the current system. The reserve is not intended to recover costs for a storm of that significance because storms of that magnitude are not common and are unlikely to occur.

Q. WHY HAVE YOU EXCLUDED 2004 AND 2005 FROM THE AVERAGE YOU CALCULATED?

A. The year 2004 was an extraordinary year for hurricane costs and those costs are not costs that were charged against the reserve. In the Storm Cost Recovery proceeding (Docket No. 041272-EI) the decision stated that "PEF contends that the costs of severe storms like the 2004 hurricanes are too volatile, irregular in their occurrence, and unpredictable to be addressed in base rates." Yet, the Company has made its recommendations based on a study that did factor in the impact from those storms. This is despite the fact the Commission in its storm cost recovery decision stated that the 2004 hurricane season was "unprecedented and extraordinary in nature" and the incremental costs of the 2004 hurricanes do not constitute a base rate item.

The 2005 charges, if any, were not included here because the Company did not provide information for 2005 as they were requested to in OPC Interrogatory No. 109. Rather than assuming that the cost was zero for 2005 and thus arbitrarily reducing the average I elected to exclude 2005 from the computation.

Q. WHAT ARE YOUR CONCERNS WITH THE COMPANY'S CONCLUSION EXPRESSED REGARDING THE STUDY?

A. Mr. Toomey states in his testimony that, based on the updated study, the Company increased the annual accrual to $16 million on a system basis. The proposed accrual produces an expected reserve balance in five years of $152.5 million. The fact is the study indicates that based on a $16 million accrual there is a 90% chance that the reserve balance could be within the range of negative $53 million and a positive $231 million. A range of $284 million is significant, especially in today's economic climate. As indicated earlier the $16 million was a predetermined number intended to increase a already sufficient reserve balance, that is significant, given the recent history of storm costs charged against the reserve and taking into consideration that the 2004 and the 1921 storm factored into the study are storms that are not likely to occur and should not have been factored into the storm reserve determination.

Q. WHAT ARE YOUR CONCERNS WITH WHAT WAS NOT FACTORED INTO AND/OR IDENTIFIED IN THE STUDY OR COMPANY TESTIMONY?

A. The Company filing included a request that its storm hardening costs be charged against the reserve. While there is no indication that the study itself factored this request into the results, there is concern that the Company in its fixation on the $150 million reserve and the $16 million accrual had factored this in the determination that the $16 million and $150 million were reasonable numbers.

Based on the response to OPC Interrogatory No. 361 the study did not factor in to the model the impact that the recent storm hardening efforts directed by the Florida Public Service Commission would have on future storm costs. This should be considered a weakness in the development of a reserve cost estimate because the intent of the storm hardening efforts is to minimize damage and cost as the result of the storms. The response went on to state "Further, given that these recent additions and changes have been in place only a few years, it is anticipated that it will be a number of years before they would significantly impact the modeled study results." This assertion, if true, would raise some major concern as to whether the study data is appropriate. Significant dollars have been spent, both recently and over the lengthy history of the Company, to upgrade and improve the reliability of the system. The 1921 storm damage would likely be significantly different today given the improvements to the system over the years especially in recent years.

Mr. Harris on page 10 of his testimony links the $150 million reserve to the 1921 storm. Here Mr. Harris states that "with a $16 million accrual, the resulting reserve level of $152 million would be sufficient to cover storm damage of approximately a one in 35 year storm season." He then states "Thus, a $16 million annual accrual results in a storm reserve balance that will be adequate to cover losses during most, but not all, storm seasons." There are problems with this testimony based on the study results. First, in response to OPC Interrogatory No. 359 the only major storms that Mr. Harris could identify the level of impact on the Company in the last 35 years were the four hurricanes in 2004, and as indicated above all parties agreed those storms should not be factored into determining the reserve level.

On page 11 of his testimony Mr. Harris discusses the 1921 storm that affected PEF's service territory. In response to OPC Interrogatory No. 362, Mr. Harris states that no storms of similar strength and point of landfall have impacted the Company since 1921. He does again reference the 2004 storms as having similar strength and he indicates that the damage was significantly less. Again based on that information I would question the appropriateness of including that storm in the study.

Next, there is a concern that Mr. Harris' testimony on page 11 as referenced above suggests that he is concurring with the Company. Yet on page 10 he states that it was not his role to recommend an annual level of accrual or target reserve level. The testimony on page 10 as well as the Company's position is considered even more questionable when you read the disclaimer to the study on Exhibit No.__(SPH-1), page 4 which states that the study provides no guaranty of any kind, that the limited nature of data causes a level of uncertainty and that there is a "significant amount of uncertainty" in the storm severity and locations; asset vulnerabilities, replacement costs and other computational parameters. Simply put, anything can happen and the results could be significantly different from what is reflected in the study.

Finally, a major missing factor in testimony and in Mr. Harris' study is an explanation as to why a $150 million reserve would be better than $125 million or a $100 million reserve. The Company was requested in OPC Interrogatory No. 364 to explain why the $150 million would be better and the response was that the $150 million presents a lower probability that the reserve will be exhausted over a five year period, decreasing the likelihood of having to petition the PSC for an additional storm surcharge. This is not justification for a $16 million accrual or a reserve of $150 million. The surcharge may only be necessary when unusual storms occur such as those that occurred in 2004. Based on the study--that I question the reasonableness of--there is a 2.7% probability that the $150 million reserve could be exhausted by a storm and there is a 4.48% probability that a $100 million reserve would be exhausted by a storm. Ratepayers should not be required to continue to fund a reserve that is excessive especially in today's economic climate. Ratepayers should not be required to increase the funding so that maybe in 5 years the reserve could be as high as $231 million as indicated on page 24 of 31 of Exhibit No.__(SPH-1).

Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING TO THE COMPANY'S RESERVE ACCRUAL AND RESERVE REFLECTED IN THE FILING?

A. The Company's accrual should be reduced to zero because the reserve is sufficient at this time to cover storm costs that are likely to occur based on recent history. This recommendation reduces O&M expense $14.922 million and increases working capital and rate base $27.160 million as shown on Exhibit HWS-1, Schedule B-4.

Q. WOULD YOU EXPLAIN WHY YOUR ADJUSTMENT IS APPROPRIATE?

A. The Company has established a sufficient reserve to cover major storms in the future. As discussed earlier the calculated average cost of storms charged against the reserve excluding the unusual 2004 storm costs and any cost incurred in 2005 results is $3 million over a 13 year period. As shown on Exhibit HWS-1, Schedule B-4 , by charging the most recent three year average (2008 storm costs recorded in 2009 are reflected in 2008) of $6.590 million against the reserve without any additional accrual results in a December 31, 2010 reserve balance of $128,651,299. Using Table 3-1 in the study performed by Mr. Harris shows the probability that storm costs in a single year would eclipse the reserve to be approximately 3.4%. That's compared to the 2.7% relied on by the Company in establishing the $150 million reserve. After five years without any accrual and assuming an annual expense of $6.590 million the reserve would be $102,291,706. Again using Table 3-1 in the study performed by Mr. Harris the probability that storm costs in a single year would eclipse the reserve would be approximately 4.4%. The low probability that a more than major storm would occur and eclipse the reserve balance justifies the elimination of an accrual for the near future. Ratepayer contributions have essentially established an adequate and sufficient reserve as it exists today. Given the low level of recent charges against the reserve, ratepayers should not be required to contribute more to increase that reserve balance based on the excessive annual $20 million charge assumption used in the study and taking into consideration the overall impact the rate request will have on ratepayers in today's economy.

V. ARO ADJUSTMENT-WORKING CAPITAL

Q. DID YOU REVIEW THE COMPANY'S PROPOSED ARO ADJUSTMENT TO WORKING CAPITAL?

A. Yes. The Company increased the working capital requirement by $446.569 million ($371.128 million jurisdictional) and reduced plant in service $48.532 million for a total net increase to rate base of $398.038 million. This adjustment according to Schedule B-2, page 2, is "To remove recoverable Asset Retirement Obligations". There are multiple concerns with the proposed adjustment.

Q. WHAT ARE THE CONCERNS WITH THE COMPANY'S PROPOSED ARO ADJUSTMENT?

A. First, I could not find any detailed explanation in testimony or in the filing that would explain this adjustment beyond the statement on Company Schedule B-2. That is not appropriate given the significance of the amount in question.

Second, the Florida rules (25-14.014 Accounting for Asset Retirement Obligations Under SFAS 143) state that the implementation of the accounting shall be revenue neutral in the rate making process. The increase in the revenue requirement suggests the adjustment is not revenue neutral.

Next, the Company's financial statements state, that when the ARO requirement was adopted there was no impact on the income statement. That would mean that the entry or entries were all balance sheet related. The footnotes also stated that an amount equivalent to the liability recorded was added to the asset cost and was to be depreciated over the useful life of the asset. If the asset amount is not removed from rate base as the liability was then the ratemaking process is not revenue neutral as required by Florida rules. The entry made by the Company in this docket removes the liability from working capital and does not have an equivalent entry made to plant, accumulated depreciation and/or the deferred assets included in working capital. The entry appears to be a one sided entry. That clearly is not appropriate.

Finally, in the rate case with TECO, in Docket No. 080317-EI, the working capital calculation reflected a $27.111 million ARO obligation and no adjustment was made by TECO to remove the $27.111 million from working capital. That suggests that the adjustment proposed by PEF may be wrong.

Q. **ARE YOU RECOMMENDING AN ADJUSTMENT TO REVERSE THE COMPANY'S ADJUSTMENT TO WORKING CAPITAL?**

A. Not at this time. Because of the significance of the adjustment, I propose to defer any determination on my part to allow the Company to provide justification for their making the adjustment.

VI. COMPENSATION AND INCENTIVE PAY

Q. **WHAT DID YOU DETERMINE FROM YOUR REVIEW OF THE COMPANY'S REQUEST FOR PAYROLL IN THE FILING?**

A. The total payroll requested is $489,779,401 and the amount included in expense is approximately $354,600,286. The Company's request for compensation request is excessive and inappropriate. As shown on Exhibit HWS-1 Schedule C-3, Page 1 of 2, I am recommending a reduction of $53,831,980 ($47,540,636 on a jurisdictional basis) be made to compensation expense.

Q. **WHY ARE YOU RECOMMENDING THIS ADJUSTMENT TO THE COMPANY'S REQUEST FOR PAYROLL IN THE FILING?**

A. The Company's request totally ignores the state of the economy and the impact that the request will have on the citizens of Florida who are served by the Company. The request includes business as usual pay increases, an increase in payroll for employees that have not been hired yet and an increase in incentive compensation, when the current amount of incentive compensation is not justified.

Q. **WHY ARE YOU APPROXIMATING THE PAYROLL EXPENSE IN THE FILING?**

A. The Company's filing does not identify the amount of overtime included in the Company's request. The Company MFR Schedule C-35 entitled "Payroll & Fringe Benefit Increases Compared to CPI" does not reflect any overtime compensation. The Company has elected to bury the overtime costs in various other MFR schedules. This is contradictory to the purpose of the MFRs. The total amount of overtime in the projected test year was identified in the response to OPC Interrogatory No. 127. The portion expensed was estimated based on the expense ratio for the payroll costs as shown on MFR Schedule C-35 and the response to OPC Interrogatory No. 128 that identified the portion of payroll from MFR Schedule C-35 that was expensed in the projected test year.

Q. WHAT IS THE PROBLEM WITH THE BUSINESS AS USUAL PAY INCREASES?

A. The Company's response to OPC Interrogatory No. 124 indicates the budgeted increase for non-bargaining positions was 3.75% in 2009 and 2010. For bargaining positions the increases are budgeted at 3% for 2009 and 2010. In a follow up request the Company stated in response to OPC Interrogatories No. 301 and 302 that the increases identified in the response to OPC Interrogatory No. 124 is only the merit increase and that the budgeted labor as shown on MFR Schedule C-35 also includes promotions, off-cycle salary adjustments, market based adjustments and contractual step ups. As shown on Exhibit HWS-1 Schedule C-3 the average base pay reflected in the filing for a PEF employee increased 9.4% from 2008 to 2010. That is an increase of 4.7% per year. Simply put, that significant increase reflected in the projected test year compensation is a business as usual increase. The business as usual increase ignores the current economic climate and it ignores measures taken by other companies, both regulated and unregulated in curbing the amount of compensation and maintaining and/or cutting costs.

Late in 2008 and in early 2009 a number of companies were identified in the media that were either freezing compensation and/or cutting compensation in lieu of reducing employees. A study by Mercer dated June 17, 2009 indicated that 69% of companies surveyed had 2009 budgeted aggregate base pay equal to or below the 2008 budget. PEF is obviously not included in the 69%.

Q. ARE YOU AWARE OF UTLITIES EITHER FREEZING COMPENSATION OR TAKING MEASURES TO AVOID ADDED HARDSHIP TO CUSTOMERS?

A. Yes. In a current rate filing in Vermont, Green Mountain Power has limited the increases in compensation to the contractual rate for bargaining employees and frozen wages for non-bargaining. Potomac Electric Power Company in it's current filing in Case 1076 has foregone any wage increase for non-bargaining employees in its request and has requested only a portion of the bargaining employees increase. People's Gas System in Docket No. 080318-GU eliminated the executive increase and reduced the employees' compensation increases.

Q. DID YOU INQUIRE AS TO WHETHER THE COMPANY HAD CONSIDERED THE CURRENT STATE OF THE ECONOMY?

A. Yes. In the response to OPC Interrogatory No. 303 the Company stated "During each budgeting process historical trends and economic conditions at that time are evaluated. The 3.75% budget for 2010 reflects recent historical trends of year-over-year increases and the current economic conditions by holding the increase from 2007 to 2008 flat for the three year period 2008-2010." I would interpret that response to the Company saying that economic conditions are such that an increase above the 2008 increase of 3.75% is not warranted. The response is insensitive to the ratepayers given the current state of the economy. When the economy was doing well back in 2006 and 2007 the increase was budgeted at 3.5%. As economic conditions deteriorated the budgeted percentage was increased to 3.75% in 2008. This action counters claims by the Company that they have tried to minimize costs and the request for an increase in rates charged to the customers of PEF.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO THE PERCENTAGE INCREASE THAT IS PASSED ON TO RATEPAYERS IN RATES?

A. Yes. Even though I believe that any pay increases granted should be excluded from rates at this time I do not believe that the Commission would approve such a recommendation. Therefore, I am recommending that the annual average increase be limited to 2.35% or one-half of the Company's 4.7% calculated increase in base pay. As shown on Exhibit HWS-1 Schedule C-3, Page 2 of 2 the reduction to an annual increase of 2.35% reduces the proposed average base salary from $75,170 to $71,979 and that reduces payroll expense by $12,209,439.

Q. DO YOU HAVE ANY FURTHER JUSTIFICATION FOR RECOMMENDING AN ADJUSTMENT TO THE PERCENTAGE INCREASE THAT IS PASSED ON TO RATEPAYERS IN RATES?

A. Yes. In the revised response to OPC Interrogatory No. 124 the Company provided the actual 2009 increase for non-bargaining positions. The increase is 2% for management and 3% for non-management employees. Despite the Company's assertion in the response to OPC Interrogatory No. 303 that the increases budgeted and included in this rate request are reasonable in today's economy there appears to be a different strategy when it comes to actual operations.

Q. WHAT ARE YOUR CONCERNS WITH RESPECT TO THE NUMBER OF *EMPLOYEES INCLUDED IN THE COMPANY'S REQUEST?*

A. The Company is requesting that the number of employees allowed in rates through capitalized and expensed labor be increased a net 370 positions from 4,929 Full Time Equivalents (FTEs) in 2008 to 5,299 FTEs in the 2010 projected test year. The increase again ignores the impact that will be reflected on customer bills in an economy that is already difficult. The request assumes that positions budgeted for will be filled and it assumes that future vacancies will not occur. The increase is not appropriate. As I indicated earlier a Mercer survey indicated that 2009 budgeted base pay would be equal to or less than the 2008 budget for 69% of the companies surveyed. For that to be accomplished for PEF there can be no pay increase and no additional employees added unless pay cuts are implemented. The record is clear that PEF is not reducing payroll, therefore the Company's plan to increase pay and add employees ignores the economic events that other companies and ratepayers are forced to recognize.

A second concern is that even though the Company budget is established based on current employees and proposed additions, the Company's human resource department does not maintain budgeted employee level detail. Month to month changes can be tracked but a comparison to budget can not be provided to evaluate how the Company projections are performing.

Q. **HAVE CHANGES OCCURRED WITH THE NUMBER OF EMPLOYEES SINCE 2008?**

A. Yes. Based on the response to OPC Interrogatory No. 297, the Company had 4,929 employees as of December 31, 2008 and 4,911 as of March 31, 2009. The decrease of 18 employees is evidence that the fact of vacancies cannot be ignored and raises concerns whether the increase projected is reasonable.

Q. **DID YOU INQUIRE AS TO WHERE IN THE FILING THE COMPANY JUSTIFIED THE INCREASE AND THE CURRENT STATUS OF THE ADDED POSITIONS?**

A. Yes. The response to OPC Interrogatory No. 299 indicates that in fact, 497 positions are proposed to be added and that 127 positions will be eliminated for a net increase of 370 positions. The Company response eliminates 416 positions from the explanation requirement by indicating that the 387 positions are "Clause Positions" and 29 positions are "Allocated Headcounts". Apparently the Company believes these positions do not require justification. The response continues by stating that after making the two adjustments there only 81 of the net addition of 370 positions that represent true position increases affecting base rates. The 81 positions consist of 36 new positions and 45 vacancies. Only 10 of the new positions have been filled and only 20 of the vacancies have been filled. However, based on the employee count as of March 31, 2009, more vacancies have occurred. The response also indicates that only 33 of the 36 new positions were identified and/or referenced in

Company testimony. That means that along with no justification being provide for the so called "Clause Positions" and the "Allocated Headcounts", the filing has failed to provide any justification for the other 48 positions (81-33) included in the Company's request.

Q. ARE YOU RECOMMENDING THAT AN ~~ADJUSTMET~~ ADJUSTMENT BE MADE TO THE ALLOWANCE FOR THE NUMBER OF EMPLOYEES INCLUDED IN THE FILING?

A. Yes. Based on the response to OPC Interrogatory No. 299 I am recommending that the allowance for 51 unfilled positions the Company classifies as true position increases be removed and the allowance for 29 service company positions be removed for a total adjustment of 80 positions. As shown on Exhibit HWS-1 Schedule C-3, Page 2 of 2, using my adjusted average base salary of $71,979 the payroll expense would be reduced $4,156,891.

Q. HAVE YOU TESTED YOUR ESTIMATE FOR REASONABLENESS?

A. Yes, I have. As I discussed earlier, in addition to not providing justification for the positions, the Company has ignored vacancies by assuming that vacant positions as of December 2008 would be filled. Since the Company would not provide monthly budgeted employee counts I interpolated the increase projected by the Company assuming a level increase from one month to the next. Using the March 2009 actual employee count of 4,911, I estimated a vacancy rate of 1.94%. Applying the 1.94% to the 5,299 projected positions, results in 103 vacant positions. Based on that result my adjustment related to funding these proposed 80 positions is conservative.

Q. WHAT IS YOUR CONCERN WITH INCLUDING INCENTIVE COMPENSATION IN THE COMPANY'S REQUEST?

A. Incentive compensation is compensation in addition to base pay that can only be justified if the performance of employees results in improved customer service, customer reliability and improved financial results. With those improvements there is a benefit to both ratepayers and shareholders. The cost for incentives should follow the benefit. Therefore, if the improvement in operations can be shown in service, reliability and earnings then it would be appropriate for shareholders and ratepayers to share the cost of that improved performance. If service and reliability does not improve, but profits do, then the shareholders are receiving a greater benefit and they should be responsible for the cost. It is not appropriate to assume that incentive compensation is a required part of a compensation package that makes it a cost that should automatically be passed through to ratepayers.

Next, taking into consideration the current state of the economy, the inclusion of the payment for incentive compensation in rates is even more inappropriate. The Company is requesting that an increased level of incentive compensation be included in rates as if the economy has not had a downturn. This is hypocritical when you take into consideration the fact that the pension costs requested by the Company reflect the downturn in the economy, yet base compensation increases and incentive compensation are treated as business as usual. To ask ratepayers who may be unemployed and/or who have had to make other concessions because of reduced or frozen compensation is not appropriate.

Q. DID YOU ASK THE COMPANY WHETHER THEY WOULD CONSIDER REMOVING THE INCENTIVE COMPENSATION FROM THE COMPANY'S REQUEST?

A. Yes. In OPC Interrogatory No. 376 the Company was asked if they would be willing to remove the cost of incentive compensation from the current request based on the current economic conditions and the Company's efforts to manage its cost. The response stated "No, the Company is not willing to remove these costs from the current rate request. These compensation structures are standard practice in the electric power industry and other industries. They are a necessary cost of doing business and are essential in attracting, retaining and properly motivating the highly skilled workforce needed to efficiently manage and operate today's electric utility. Customers benefit in that these employees are essential for the efficient and reliable service that customers have come to expect." This is a typical response that, along with the use of another misnomer, has in the past, convinced the Commission Staff and the Commission that incentive compensation is required to be included in rates. The reality is that while many companies do pay incentive compensation there are a number of jurisdictions that either do not allow and/or limit the amount of incentive compensation in rates.

Q. WHAT IS THE OTHER MISNOMER THAT YOU REFERED TO THAT YOU BELIEVE IS MISLEADING?

A. Typically a Company will state that the payment of incentive compensation is required to attract, retain and motivate and it follows a pay-for-performance philosophy. That is supplemented with reference to the compensation program being market-based at the 50th percentile of national and regional markets. The

Company's witness, Masceo DesChamps, essentially states this very position on pages 5 and 6 of his pre-filed testimony. *I have been analyzing rate requests for* more than 30 years and after incentive compensation came into play that is the most frequent argument that I have heard. In my experience, I have found very few companies that will state they are anywhere but in the 50^{th} percentile. My opinion, based on the numerous studies reviewed is that the compensation level referred to in the studies as being the 50^{th} percentile is skewed by a limited few organizations. But to reiterate the one fact that is missed by commissions when they accept the-attract and-retain argument, along with the 50^{th} percentile argument, is that the utility companies that are in those studies do not have all of the incentive compensation included in rates. Therefore, to allow the incentive compensation in rates in its entirety based on an inappropriate comparison puts Florida ratepayers at a disadvantage when compared to ratepayers in other jurisdictions.

There is also some question as to whether it is true that incentive pay is as significant a factor in attracting and retaining competent employees is as factual as the Company would lead you to believe. In response to OPC Interrogatory No. 284, the Company provided the top five drivers an employee uses to choose an employer based on a Towers Perrin survey. They are as follows:

1) Competitive Base Pay
2) Competitive Health care Benefits
3) Vacation/Paid Time Off
4) Competitive Retirement Benefits
5) Career Advancement Opportunities

Missing from the list is incentive compensation that is really added compensation. In fact in reviewing the response to OPC POD No.222, it was noted that incentive compensation was not included in any of the top 10 attraction drivers.

Q. ARE YOU SURE THAT THE COMPARATIVE COMPENSATION HAS NOT BEEN ADJUSTED FOR THE INCENTIVE COMPENSATION NOT ALLOWED IN OTHER JURISDICTIONS?

A. Yes. Based on my review of compensation studies over the past 30 years I have never found any study that indicated that the various companies' compensation levels within the studies have been adjusted to reflect the disallowance of compensation by a regulator. The Company confirmed this in the response to OPC Interrogatory No. 283.

Q. DOES THE COMPANY VIEW INCENTIVE COMPENSATION AS ADDED COMPENSATION?

A. The answer to this question is it all depends on who the Company is discussing the topic of incentive compensation with. In response to OPC Interrogatory No. 344 the Company stated that "Incentive compensation should not be viewed as an amount that is "added" to base salary, but rather as one variable component of a competitive total compensation program." In the Company Employee Cash Incentive Plan (ECIP) (Company response to OPC POD 31, page 156) a frequently asked questions is "How will the ECIP affect my annual base pay?". The response is clear "The ECIP is separate from, and <u>in addition to</u>, your base pay. Any award you receive will not affect either your base pay or future salary adjustments to your pay." (emphasis added).

Q. ARE THERE CONCERNS WITH THE PLAN ITSELF?

A. Yes, the incentive compensation plans are directed at improving the financial performance of the Company. PEF's emphasis, therefore, is the shareholders interest. The Management Incentive Compensation Plan (MICP) states first and foremost that the purpose of the plan "is to promote the financial interests of the Company". It continues with the rhetoric regarding attracting and retaining employees and motivating with goals through the payment of cash incentives. Therein lies more of the problem, the incentive compensation plan is based on goals that do not require above average performance.

Q. WHAT ARE YOUR CONCERNS WITH THE GOALS?

A. The plans emphasis is on financial performance of the Company which is directed toward shareholders. Companies argue that if there is financial success that ratepayers benefit. That assertion is not necessarily true. The financial success may be attributed to cost reductions in customer service areas. To add further concern, the results can be adjusted based on the CEO's discretion.

Next there are the operational goals which may not be real goals. For example:

- The Corporate Services 2006 employee incentive goal of less than 1.25 recordable injuries was not achieved and in 2007 the goal was relaxed to less than 1.37 recordable injuries. Not only was this goal change not appropriate, I observed that in 2006 of the ten operating goals listed for Corporate Services the OSHA goal was listed twice with a second goal level. This duplication was noticed elsewhere.

- Another example is the Sarbanes-Oxley "goal" of no material weakness of the internal controls for a number of groups. The employees' base pay has to have some performance requirements tied to it and one would expect that maintaining proper internal controls would be expected of all employees. To establish a goal for achieving a task that should be an expected duty falling under base pay compensation is redundant and inappropriate.
- The Transmission goal in 2006 for System Average Interruption Index (SAIDI) was less than or equal to 9.3 was not achieved, in 2007 the goal was changed to 9.48, lowering the performance requirement, and despite being achieved in 2007, the goal for 2008 was set at 10.2, again lowering the performance requirement. Compounding the problem is that the SAIDI goal was listed twice at different levels.
- In Power Operations, Company witness David Sorrick states that it is PGF's goal to have zero accidents yet the incentive compensation goal allows for accidents.
- A further illustration is where then there are the goals that are accomplished in one year and the next year the goal is the same. As an example, the response to OPC Interrogatory No. 255 shows that even though the environmental goal of greater than or equal to 4 was achieved in 2005, 2006, 2007 and 2008, the goal in 2009 remains at 4.

The term incentive means to stimulate. There is no stimulation if goals are not increased. Failure to raise the bar to promote improvement means that the plan can be little more than designed to provide added compensation at the expense of ratepayers. The Company payout for incentive compensation is further evidence that the plan is simply additional compensation that is expected by employees and not driven by an incentive to improve performance that will benefit ratepayers.

Q. HOW DO THE INCENTIVE PAYMENTS PROVIDE EVIDENCE THAT THE PLAN IS NOT DESIGNED TO IMPROVE PERFORMANCE?

A. The response to OPC Interrogatory No. 131 shows that in 2006 99.6% of eligible employees were awarded an incentive payment. In each of the years 2007 and 2008 the awards were made to 99.7% of the eligible employees. With approximately 5,000 employees I find it very hard to believe that performance was so high among the employees that almost everyone earned a payment. This is further evidence that this is just added compensation and not truly incentive pay.

Q. IS THERE CONCERN THAT THE FOCUS IS NOT ON RATEPAYERS IN DETERMINING WHETHER AN INCENTIVE PAYMENT SHOULD BE MADE?

A. A review of the plans and the changes in the plans that occurred failed to identify a reference to ratepayers. As indicated earlier the purpose is to promote the financial interest of the Company and share achievement with employees. Absent actual documented proof that the plan provides improved performance to ratepayers, there is no justification for ratepayers to bear any portion of the incentive compensation costs. Other jurisdictions have recognized this fact and have either totally disallowed incentive compensation or they have limited the recovery in rates. Florida should be no different.

Q. COULD YOU IDENTIFY SOME OTHER JURISDICTIONS THAT HAVE DISALLOWED INCENTIVE COMPENSATION IN TOTAL OR IN PART?

A. In New York the decision in Consolidated Edison Company, Case 07-E-0523 the Commission disallowed the cash incentive compensation, commonly referred to as variable pay and the stock based plan costs. Even though the Company argued that both incentive plans should be allowed, using the standard argument that it is necessary to attract and retain employees and it compensates for achievement of good service, reliability and safety, the Commission did not find the request justified. In a recent filing in Washington D.C., Potomac Electric Power Company removed its incentive compensation from its request because it was in accordance with a previous decision. In Vermont, Green Mountain Power in Docket No. 5983 had incentive compensation totally disallowed because the goals did not provide an incentive that would require an improvement above goals that were previously achieved. Currently in Vermont it is common practice that portions of incentive compensation is automatically excluded when a filing is submitted by the company. In Connecticut the Department has determined that various levels of incentive compensation should be excluded from rates. In Arizona cash based incentive costs are shared between ratepayers and shareholders and stock based incentive compensation is generally excluded in its entirety.

Q. WHAT ARE YOU RECOMMENDING BE DISALLOWED IN THIS RATE FILING?

A. The Company's request for $25,371,639 of incentive compensation expense and approximately $12,094,011 of long term incentive compensation expense should be disallowed in its entirety. The disallowance is based on the Company's failure to establish a plan that is designed to provide a tangible and/or quantifiable benefit to ratepayers. As stated earlier, the design and the goals are a simple formula for paying added compensation. If PEF's management believes that attaining goals that do not encourage improvement is sufficient for payment of added compensation to its employees, then shareholders, not its ratepayers, should pay for the related compensation.

Another reason the incentive compensation should be disallowed is it is not justifiable for the Commission to allow in rates this added compensation with dubious demonstrable benefits which will increase rates to customers who are already struggling to meet their own financial obligations in today's economy. People on fixed incomes, people who have lost their jobs and people who have made sacrifices so they can keep their jobs should not in good conscience be required to fund a better way of life for a Company that is insensitive to the current economic impact imposed on its customers just because the monopolistic environment in which it exists allows it to do so.

VII. EMPLOYEE BENEFITS

Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO EMPLOYEE BENEFIT EXPENSE?

A. Yes. At a minimum, an adjustment is required based on the recommended adjustment to the Company's employee complement. Based on a discrepancy between the initial filing and the revised filing another adjustment is required to account for a change reflected to MFR Schedule C-35. As shown on Exhibit HWS-1 Schedule C-4, I first reduced the $138,288,606 of expense reflected in the filing by

$9,376,809 for the change in total fringe benefits reflected in the revised MFR Schedule C-35. I determined the adjustment by multiplying the expense ratio for fringe benefits provided in response to OPC Interrogatory No. 128 by the total fringe benefit cost on Revised MFR Schedule C-35.

My next adjustment simply took the average benefit expense per employee by my recommended reduction of 80 positions in the employee complement. The result is an adjustment of $1,946,206.

Q. WHY DID YOU STATE THAT THE RECOMMENDED ADJUSTMENT IS "AT A MINIMUM"?

A. The Company's fringe benefit costs are projected to increase $79,676,684 (83.1%) from $95,825,556 in the 2008 base year to $175,502,240 in the projected test year 2010. The increase is driven by the $67,472,819 increase in pension costs and a $7,071,527 (26.3%) increase in medical costs. The pension increase is attributed to the significant downturn in the economy. The healthcare increase appears excessive and could be attributed to the fact that employee sharing has not kept pace with the cost increases the Company has projected. For example, in response to OPC Interrogatory No. 349 the employee contribution increased by 3% while according to the response to the response to OPC Interrogatory No. 136, health care costs are increasing at 10%-12% annually.

The Company has a wide array of benefits that include two retirement plans. The pension plan and the employee savings plan. Having two retirement plans is a luxury that I am confident most PEF ratepayers cannot enjoy. In addition there is a generous health care plan (i.e. general health plan, health savings plan pre tax, dental and vision), various miscellaneous benefits (including added bonuses) and retiree benefits. Again the ratepayers that are paying for this generous benefit package may themselves be uninsured and/or may not have any retirement plan. The Commission when evaluating the overall compensation request made by PEF should factor this fact into its decision process especially in today's economic climate.

VIII. RATECASE EXPENSE

Q. WHAT DID YOU DETERMINE FROM YOUR REVIEW OF THE COMPANY'S REQUEST FOR RATE CASE EXPENSE?

A. The Company's request is excessive, the amortization period is not acceptable and the rate base treatment is not consistent with rate making principles. As shown on Exhibit HWS-1 Schedule C-5, the Company's expense request should be reduced \$989,618 and the amount included in rate base should be reduced \$969,531.

Q. WHY IS THE TOTAL AMOUNT REQUESTED CONSIDERED EXCESSIVE?

A. The Company's request does not reflect the contractual terms of the consultants and lawyers. The consultant's costs are overstated by approximately \$70,090 and the lawyer's fees exceed the contract amounts by \$697,500, for a total overstatement of \$767,590.

Q. WHY IS THE AMORTIZATION PERIOD NOT ACCEPTABLE?

A. The Company has requested an amortization period of two years based on what Mr. Toomey says is a "long-standing Commission practice". When asked about the long-standing Commission practice the Company stated in response to OPC Interrogatory No. 381 that it was relying on the January 1999 DIGEST OF COMMISSION REGULATORY PRACTICES AS EXPRESSED IN RATE MAKING PROCEEDINGS AND CURRENT DECISIONS which referenced a 1982 decision. That ignores the period between rate cases in more recent years and it ignores recent rulings in other cases. Because of the time between rate cases and taking into consideration that lengthening the amortization period will help reduce the immediate impact on rate payers, a five year amortization period is recommended.

Q. WHAT IS THE RATE BASE TREATMENT REQUESTED THAT IS INCONSISTENT WITH RATEMAKING PRINCIPLES?

A. The Company has requested the full amount be included in rate base without factoring in amortization in the rate year and ignoring the fact that rate base is an average not a beginning of the year amount. Allowing the Company treatment would result in a double charge to ratepayers and ignores the fact that amortization in the rate year occurred. An adjustment to the average rate base amount in 2010 is appropriate.

IX. TRANSMISSION O&M EXPENSE

Q. DID YOU REVIEW THE COMPANY'S REQUEST FOR TRANSMISSION O&M EXPENSE?

A. To some degree I was able to analyze portions of the request based on the limited specifics included in testimony and budget information supplied. There is a general concern with the significant increase in the budgeted dollars. Based on the

Company's MFR C-4 the costs for transmission O&M between 2005 and 2008 ranged from $31.3 million in 2005 to $35.2 million in 2008. The 2009 budgeted cost is $35.1 million. In 2010, the projected test year, the costs spikes upward by $10.3 million for a total of $45.3 million. The Company's testimony identifies $6.9 million of added costs for FERC Order 890. Budget information shows an increase of $1 million for a line bonding and grounding program, and there is an increase of $2.7 million for vegetative management. All of these cost increases are of concern.

The FERC Order 890 cost estimate is not based on any historical costs. There is no explanation in the Company testimony and/or filing for the bonding and grounding program. Based on the explanation for 2009 benchmark comparison, it appears that the bonding and grounding is not a cost incurred on an annual basis. The vegetative management increase appears to coincide with the fact that the Company is in for a rate increase and ignores any potential cost savings resulting from this activity.

Q. WHY DO YOU BELIEVE THE VEGETATIVE MANAGEMENT INCREASE IS DRIVEN BY THE RATE REQUEST?

A. The storm hardening initiative has been in effect since 2006. According to the response to OPC Interrogatory No. 238 the Company spent $6.3 million in 2006, $6.9 million in 2007, $5.9 million in 2008 and have budgeted $6.6 million for 2009. The projected test year 2010 is set at $9.3 million. The Company's requested increase is excessive when compared to the historical spending and the 2009 budget. If the Company was required by the Commission to perform an increased level of trimming that increase should have been reflected in the 2009 budget. Without reflecting an increase in the 2009 budget there is concern that need for an increase in trimming does not exist. The cost increase in 2010 is not justified.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR VEGETATIVE MANAGEMENT EXPENSE INCLUDED IN THE TRANSMISSION O&M EXPENSE?

A. Yes, an adjustment of $1,717,043 is recommended on a jurisdictional basis as shown on Exhibit HWS-1 Schedule C-6. The adjustment assumes that vegetative maintenance will continue at the level the Company deemed appropriate over the period 2006-2009. The increase requested is not justified given the Company's historical spending level. The only justification provided for the increase is on MFR Schedule C-41; Page 8 where the Company simply states it is required to comply with FERC and Commission standards. The Company has not indicated that the historic spending and the budgeted 2009 spending level was insufficient to maintain compliance, so there is no justification for the increase.

Q. ARE YOU RECOMMENDING ANY ADDITIONAL ADJUSTMENTS TO THE COMPANY'S REQUESTED TRANSMISSION O&M EXPENSE?

A. Yes, an adjustment of $338,145 ($500,000 x .67629) is recommended on a jurisdictional basis to reflect a more normalized level of expense for line bonding and grounding. The $1 million included in the projected test year is reduced to reflect the average of an every other year expense. It is not appropriate to overload the projected test year to increase rates.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR THE FERC 890 COSTS INCLUDED IN THE TRANSMISSION O&M EXPENSE?

A. A specific adjustment is not being recommended but I will discuss how I took the Company's failure to adequately support the request for the FERC 890 cost elsewhere in my testimony.

X. DISTRIBUTION O&M EXPENSE

Q. DID YOU REVIEW THE COMPANY'S REQUEST FOR DISTRIBUTION O&M EXPENSE?

A. As with the transmission O&M request there was a limited amount of specifics included in testimony and budget information supplied. Company witness Jackie Joyner stated that the Company was requesting $145 million for distribution O&M expense in the projected test year 2010. The only specific discussion regarding O&M expense is the mentioning that PEF will spend $3.2 million for pole inspections and $34.4 million for vegetation management. The benchmark comparison on MFR Schedule C-41 adds little valuable information in identifying any other changes or programs. On MFR Schedule C-41 there are three costs described that net to a $400,000 increase. In 2008 there were $120.6 million in costs charged to Distribution O&M and as indicated the Company is seeking $145 million in the 2010 projected test year. Vegetation management accounts for $15.9 million of the $24.4 million increase. ~~The pole inspection costs for 2010 are $.8 million more than 2008~~. Therefore approximately $~~7.7~~ 8.5 million of the increase is essentially unexplained.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO THE COMPANY'S DISTRIBUTION O&M EXPENSE REQUEST?

A. Yes, a reduction of $8,924,197 is recommended on a jurisdictional basis, as shown on Exhibit HWS-1 Schedule C-7, for Distribution Vegetation Management. The adjustment factors in the trimming of the 18,341 primary conductor miles over a five year period using the Company $5,538 cost per mile and adds an estimated $5 million for trimming and treatment of the remaining 7,297 miles that consists of secondary conductors.

Q. WHY ARE YOU RECOMMENDING AN ADJUSTMENT TO THE COMPANY'S VEGETATION MANAGEMENT REQUEST?

A. The Company trimmed 3,419 miles in 2006, 4,303 miles in 2007 and 3,297 miles in 2008. Based on the response to OPC Interrogatory No. 272 the Company's projected expense for 2010 is based on trimming 5,080 miles. The significant increase suggests that the Company did not trim the required miles in the years 2006-2008 and is attempting to make up for the shortfall in the year rates are being set. Based on the response to OPC Interrogatory No. 270 the Company's 2009 budget is comparable to the amount expended in 2007. The significant increase in 2010 over 2009 further suggests that costs are being deferred to the projected test year. Limiting maintenance in previous years, for whatever reason, is not justification for passing the catch up costs on to ratepayers. The amount allowed in rates should be based on the annual requirement to trim the primary conductor miles of line. Furthermore, it would be inappropriate to defer costs properly attributable to 2009 since that period is covered by a revenue sharing mechanism that assumes that earnings are fairly presented for surveillance purposes.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR THE UNEXPLAINED COSTS INCLUDED IN THE DISTRIBUTION O&M EXPENSE REQUEST?

A. No specific adjustment is being recommended for the unexplained O&M expense but I will discuss this concern elsewhere in my testimony.

XI. POWER OPERATIONS O&M EXPENSE

Q. WHAT DID YOU DETERMINE FROM YOUR REVIEW OF THE COMPANY'S POWER OPERATIONS O&M EXPENSE REQUEST?

A. The request appears excessive. As with the transmission and distribution submissions there was a limited amount of specifics regarding what the Company was including in the request. Beginning on page 24, Company witness, David Sorrick provides an explanation of the $53.1 million benchmark variance. The Company's request for Power Operations O&M expense is $175 million after excluding the payroll taxes, employee benefits and injuries and damages budgeted by the Power Operations cost center. The real budget total is $201 million. A very generic explanation of why the benchmark variance is $53.1 million does not constitute adequate justification for the $175 million identified by the Company's witness.

Q. WHY DO YOU BELIEVE THE COMPANY'S POWER OPERATIONS O&M EXPENSE REQUEST IS EXCESSIVE?

A. The Company's $175 million request has increased significantly when compared to the 2008 costs of approximately $138 million and the 2007 costs of approximately $127 million as shown on Company MFR Schedule C-6. Company testimony attempts to justify the increase by describing the various improvements in operations and efficiencies achieved. The problem is that the testimony does not provide an adequate explanation and it does not justify the cost increase requested. For example on page 15 of his pre-filed testimony Mr. Sorrick discusses the improvement in Equivalent Forced Outage Rates (EFOR) for unit CR2. A review of the response to OPC Interrogatory No. 248 indicates that in 2008 CR1, CR4 and CR5 EFOR increased. There are other increases also. In reviewing the response to OPC Interrogatory No. 247 it was observed that unit availability declined for a majority of the units in 2008. There is also discussion about costs savings and efficiencies but no indication as to how and/or whether any savings are reflected.

Q. ARE YOU RECOMMENDING SPECIFIC ADJUSTMENTS TO THE POWER OPERATIONS O&M EXPENSE REQUEST?

A. Yes. There is one specific adjustment and later in my testimony I will include some discussion regarding Power Operations in a proposed overall adjustment to the Company's request. As shown on Exhibit HWS-1 Schedule C-8 the Company's Power Operations Maintenance Expense should be reduced $17,741,309 on a jurisdictional basis.

Q. COULD YOU EXPLAIN HOW YOU DETERMINED THE ADJUSTMENT TO THE POWER OPERATIONS O&M EXPENSE REQUEST?

A First, the maintenance expense for power generation is projected to increase from $76.5 million in 2008 to $109.2 in 2010. After excluding company labor from the request, the maintenance is projected to increase $19 million (35.2%) from $54 million in 2008 to $73 million in 2010. Maintenance can fluctuate from year to year and basing the rate request on one high year is inappropriate. Therefore, some adjustment was required to smooth out the cost being passed onto ratepayers. The Company's 2010 projected cost was adjusted for certain increases to smooth out the 2010 maintenance overload.

One cost driver of the increase is the adding of major Clean Air equipment at Crystal River Unit 4. Based on the response to OPC Interrogatories No. 260 and 263 there are two concerns with the $15.1 million of added cost in this project. The first concern is this type of work is typically performed every 9 years. The second concern is the cost increase appears to include $5.3 million for a precipitator and if that response is correct, this a capital cost not an expense. Because the cost is not typical maintenance and will not be recurring, the cost for rate making purposes should be spread over at least 5 years. Spreading the $15.1 million over 5 years reduces the 2010 cost by $12 million.

Second, the Company was requested in OPC's Production of Document Request No. 213 to provide <u>all supporting documentation</u> that the company has for the $4.6 million cost estimate for 2010 under the Long Term Service Agreement discussed by Mr. Sorrick on page 26, of his pre-filed testimony. (emphasis added) The Company response was, to see the response to OPC POD Question #1, MFR Schedule C-41, page 3 of 18. The MFR as indicated earlier provides a generic explanation for the increase over the benchmark and the explanation for the $4.6 million consisted of a paragraph that concludes by stating "We estimate the costs of that maintenance work covered by the LTSA to be approximately $4.6 million for the completion of two combustion inspections and two Balance of Plant outages." Another request was made for a more detailed explanation of the cost estimate in OPC Interrogatory No. 261. The response indicated that the inspection requirement included for the two units occurs every 12,500 hours. ~~Assuming the unit operates 24-7 that would equate to an inspection every 6 years~~. Supporting documentation for a cost estimate is not a paragraph that says "we estimate the cost to be this". Because the Company failed to provide supporting documentation for the requested expense the cost estimate of $4.6 million should be disallowed. However because this is also an infrequent cost I am recommending that only half of the cost be allowed in rates. This reduces the maintenance expense by $2.3 million.

Finally the Company was asked about the $14.7 million increase for existing fleet maintenance. OPC Interrogatory No. 264 asked the Company to identify the supporting documentation for the $14.7 million cost estimate and the response simply referred to the benchmark comparison explanation. Once again documentation for costs is not a paragraph but an invoice or cost quote. The response also provided a summary listing of the cost estimate. This estimate only provides further verification that what has occurred in the 2010 projections is an overloading of maintenance expense. The fact that 2010 is the projected test year for setting rates is not coincidental. The $14.7 million should be reduced $7.35 million to smooth out the costs for maintenance being charged to ratepayers. Without this smoothing, rates could be set artificially high and in future year's shareholders will benefit from the over-collection.

XII. DIRECTORS AND OFFICERS LIABILITY INSURANCE

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR THE COST OF DIRECTORS AND OFFICERS LIABILITY INSURANCE?

A. Yes. The Company has included $2.2 million of expense in account 925 for Directors and Officer's liability insurance (DOL) based on the response to OPC Interrogatory No. 310. The response to OPC POD No. 272 indicates that the budget includes $2,750,650 allocated to PEF. This expense is for $300 million of coverage. This expense protects shareholders from the decisions they made when they hired the Company's Board of Directors and the Board of Directors in turn hired the officers of the Company. The question is whether this cost that the Company has elected to incur as a business expense is for the benefit of shareholders and/or ratepayers. The question also is whether the cost for $300 million of coverage is necessary and whether the cost for that level of coverage is appropriate to pass on to ratepayers.

Q. DID YOU JUST RECENTLY ADDRESS THIS ISSUE IN THE TAMPA ELECTRIC CASE AND THE PEOPLES GAS CASE?

A. Yes and in both cases the Commission allowed the cost to be included in customer's rates. The justification for allowing the cost was the cost was determined to be a legitimate business expense. In fact in the Agenda Conference for Peoples Gas Company, on May 5, 2009, at least one Commissioner opined that the decision to allow the cost should be applied consistently to all utilities electric, gas and water and sewer on the basis that the cost is a legitimate business expense.

Q. BASED ON THAT STATEMENT AND THE DECISIONS WHY ARE YOU RECOMMENDING AN ADJUSTMENT FOR THE COST ASSOCIATED WITH DIRECTORS AND OFFICERS LIABILITY INSURANCE?

A. The Florida Commission has in the past disallowed DOL insurance costs and I respectfully disagree with the staff's recommendation and the Commission's conclusion on this issue in recent cases. The issue is more than whether the cost is a legitimate business expense. The issue is whether the cost is one that is beneficial to ratepayers and that should be borne by ratepayers as opposed to shareholders. Contributions and lobbying are deemed legitimate business expenses but they are not deemed appropriate costs to be passed on to ratepayers. In fact other regulatory agencies have also determined that the cost for DOL insurance to be a legitimate business expense but that the cost should not be borne totally ~~be~~ by ratepayers. I believe that because the Staff concluded that the cost, in their opinion, is a legitimate business expense should not be the ultimate deciding factor as to whether the cost is appropriate to be borne by ratepayers. As a witness that is representing the ratepayers of Florida it is my responsibility to recommend to the Commission that ratepayers should not be required to pay for costs, that are solely for the benefit of the shareholders of the Company, especially when the cost have been disallowed from rates in other jurisdictions.

Q. COULD YOU PROVIDE SOME ADDITIONAL INFORMATION AS TO WHY OTHER JURISDICTIONS HAVE NOT REQUIRED RATEPAYERS TO BEAR THE COST ENTIRE COST OF DIRECTORS AND OFFICERS LIABILITY INSURANCE?

A. Yes. In Connecticut there has been multiple decision where the amount allowed to be recovered from ratepayers has been limited. For example in Docket No. 07-07-01 the Department limited the recovery by Connecticut Light and Power for DOL insurance cost from ratepayers to 30% because it was determined that ratepayers should not be required to protect shareholders from the decisions they make in electing the Board of Directors. On February 4, 2009 the Department determined that United Illuminating Company could only recover 25% of the cost of DOL insurance from ratepayers. In New York in Case 07-E-0523 the Commission did not disallow the cost recovery of DOL insurance based on the judges recommendation even though the disallowance of such cost could be made based on Commission policy. The issue was raised again when Consolidated Edison Company filed in Case 08-E-0539. In the final decision the Commission ruled that $300 million of coverage was excessive based on the comparisons to similar companies and disallowed the premium associated with $100 million excess and then disallowed 50% of the premium associated with the $200 million that was determined to be reasonable. In the discussion the Commission notes that D&O insurance provides substantial protection to shareholders who elect directors and have influence over whether competent directors and officers are in place while customers have no influence. The decision continued by stating "We find no particularly good way to distinguish and quantify the benefits of D&O insurance to ratepayers from the benefits to shareholders, especially taking into account the advantage that shareholders have in control over directors and officers. We believe the fairest and most reasonable way to apportion the cost of D&O insurance therefore is to share it equally between ratepayers and shareholders." (Page 91 of the decision)

Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO THE COST OF DIRECTORS AND OFFICERS LIABILITY INSURANCE INCLUDED IN THE COMPANY'S REQUEST?

A. I am recommending total disallowance of the $2,750,650 ($2,412,100 jurisdictional) because the cost provides a direct benefit and protection to shareholders. In each of the cases cited above the company argued that the cost is a necessary and prudent cost that is required to attract and retain competent directors and officers. There are regulatory decisions that have indicated that although DOL insurance is a necessary cost of doing business, the ratepayers should not be required to pay the full cost of coverage because the insurance primarily benefits shareholders. In ratemaking the cost should follow the benefit and the benefit of this insurance clearly inures first and foremost to shareholders. In fact, shareholders will likely be the one that makes a claim against the policy. I have never heard of a claim being filed by ratepayers against a D&O insurance policy.

Q. WHY ARE YOU PROPOSING THE ENTIRE COST OF DIRECTORS AND OFFICERS LIABILITY INSURANCE BE DISALLOWED AS OPPOSED TO A SHARING AS EXHIBITED IN THE CASES YOU IDENTIFIED?

A. I am recommending total disallowance for the same reason the Company is requesting that all the costs be allowed in rates. It is my belief that the entire cost is for the protection of shareholders. A common argument for the insurance is that it is required to attract and retain competent directors and officers chosen by shareholders. That argument may justify shareholders purchasing the insurance because they are the ones who hold the officers and directors accountable. There is no argument that would justify ratepayers bearing any of the cost. It is not my position that the Company should not have the insurance coverage, I just believe that the burden should follow the benefit and in this case the benefit is to shareholders. That being said I would not object to some form of sharing if some benefit to ratepayers could be shown.

XIII. INJURIES & DAMAGES EXPENSE ADJUSTMENT

Q. WHY ARE YOU RECOMMENDING AN ADJUSTMENT TO INJURIES & DAMAGES EXPENSE?

A. The Company's request in the filing is not supported by the record. The original filing as shown on MFR Schedule B-21, Page 1 of 4, showed there was no expense in the projected rate year for injuries and damages. The witness for Schedule B-21, Mr. Toomey does not discuss injuries and damages. As shown on Exhibit HWS-1 Schedule C-9, I am recommending an adjustment of $5,449,303 or $4,778,603 on a jurisdictional basis.

Q. IF THERE WAS NO EXPENSE IN THE PROJECTED TEST YEAR WHY WOULD YOU PROPOSE AN ADJUSTMENT TO INJURIES & DAMAGES EXPENSE?

A. There was an expense in the projected test year 2010. The Company was requested to verify whether the MFR was correct and if the MFR was not correct the Company was requested to provide the costs included in the projected test year 2010 by budget center. The response to OPC Interrogatory No. 342 indicated the MFR was not correct and that there was $2,694,313 in various budget centers and $1.7 million in the legal department's budget. However, it turns out that this information was also incorrect.

Q. *HOW DID YOU DETERMINE THAT THE RESPONSE TO OPC INTERROGATORY NO. 342 WAS NOT CORRECT?*

A. The Company was requested in OPC Interrogatory No. 386 to explain what the costs that were identified as either "Other" or "Purch" with the classification of "Salaries and Wages" were that were included in the budget provided in response to OPC POD No. 37. The response indicated that the "Salaries and Wages" identification was incorrect and should have been labeled "A&G Office Supplies & Expense". In addition the response indicated that the nuclear budget had misclassified $450,000 that should have been included in "A&G Injuries & Damages". That would mean that there was at least $4,844,313 ($2,694,313 +1,700,000 + 450,000) included in the 2010 projected year. My analysis of the budgeted costs actually revealed $5,020,063. As shown on Exhibit HWS-1 Schedule C-9, the legal budget included $1,825,000 plus another $50,750 not the $1,700,000 indicated by the Company. The $1,825,000 was verified in the response to OPC POD No. 274. As will be discussed elsewhere the Company budgeting is a concern and the costs included in that budget are of even greater concern since the Company apparently has problems identifying costs and has errors in the process itself.

Q. WHY WOULD YOU ELIMINATE THE ENTIRE AMOUNT REQUESTED FOR INJURIES AND DAMAGES IN THE PROJECTED TEST YEAR 2010?

A. The Company failed to provide any justification for any cost for 2010. This is important considering the fact that it appears that the 2008 did not have any expense. The Company provided the 2008 budgeted and actual cost for 2008 in response to OPC Interrogatory No. 389 and as shown on Exhibit HWS-1 Schedule C-9, there was a negative expense in 2008. It would not be appropriate for the Company to be allowed an expense in the projected test year when there was no expense in the base year 2008. This is especially true when there was initially an indication that zero expense was included in the projected year and when there is no testimony or justification for any amount in the projected test year 2010.

XIV. BUDGET ANALYSIS

Q. DID YOU REVIEW BUDGET DETAIL USED BY THE COMPANY IN THE DEVELOPEMNT OF PROJECTED TEST YEAR COSTS FOR 2010?

A. There was a review of budget information supplied in various responses to OPC discovery and there was a sample review performed in an attempt to determine what support existed for the Company projections. Based on my review I have some grave concerns about the costs included in the Company's rate request.

Q. WHAT CONCERNS HAVE YOU IDENTIFED?

A. Initially the Company was requested in OPC POD No. 15 to provide the 2009 and 2010 budget in the most detailed format available. The response included 46 documents and on each document were numbers that do not provide any added information beyond what was already reflected in the filing. If you could identify a number that was in the filing you still were unable to determine what the factors were that made up the number. I have attached one of the documents as Exhibit HWS-2 as an example. In an attempt to derive some use from the documents provided the Company was requested in OPC Interrogatory No. 315 to provide a mapping that would allow for the tracking of the budget information supplied to the MFRs. The response did not provide any additional assistance.

The Company did provide in response to OPC POD No. 37 a more detailed budget that did have some information that was useful. As discussed above, the report provided did allow me to identify the problem with the Company's MFR for injuries and damages and served as source for identifying the concerns that I have with the budget. The report is by budget center and identifies cost by type and account. In my review I selected twenty-eight line items totaling $62.5 million for further review. With the exception of OPC POD Nos. 272-274, my request clearly stated "Provide the supporting detail for the budgeted costs and documentation for the budgeted costs". Of the nineteen line items that documentation was requested only two had what would be considered documentation. Detail of what was included in the line item amounts was provided for fourteen of the nineteen line items. There was not sufficient detail or documentation for five of the line items. If detail was provided it had numbers on it that could not be tied to the line item is was supposed to detail. The concern is, the information supplied was detail that provided in some cases more information as to what the different cost components were but there was no supporting documentation for the numbers on the detail page.

Q. WHAT WAS DIFFERENT WITH THE REQUESTS OPC POD NOS. 272-274?

A. The request stated "Provide the supporting documentation and/or detail for the budgeted costs". The "and/or" may have been interpreted to mean that either was sufficient. Such a reading would be contrary to the instructions accompanying the discovery. The Company provided detail for each of the nine line items identified. What could be considered as further detail or documentation was provide for one line item that allowed me to see how a cost was determined. Here again detail did in some case provided additional information but without supporting documentation for the cost, the numbers are just numbers on a piece of paper.

Q. **WHAT IS SUPPORTING DOCUMENTATION?**

A. Supporting documentation would be a quote, an invoice or an estimate from a third party that could justify a cost estimate included in the budget. Some costs like injuries and damages or labor for a certain type of project could be supported with actual historical cost detail. Numbers on a piece of paper is not supporting documentation. If an auditor or the IRS would ask for supporting documentation for a $1,200,000 line item in A&G Office Supplies and Expense they would not accept a piece of paper that says "Corporate Managed Account".

Q. **WHAT DOES THE COMPANY CONSIDER SUPPORTING DOCUMENTATION TO BE?**

A. I cannot answer that. The response to OPC Interrogatory No. 394 state that "PEF considers documentation to have the meaning given to it by applicable orders, rules, and statutes in Florida". The Company response did not provide any specific cite that could be relied on. Just like the costs there is no support provided for the Company response.

Q. **ARE THERE CONCERNS WITH THE DETAIL INFORMATION SUPPLIED?**

A. Yes. Even though there may have been a detailed listing of various costs included in the cost estimate, the detail did not provide any real information. For example, the response to OPC POD No. 272 provided four pages of "detail" for the $1,780,000 of

General Advertising Expense included in the budget. The detail simply labeled the cost as "other" and as "Utility Advertising". That really is not very informative. No indication is provided showing the type of advertising or the media used for the advertising. Another example is the response to OPC POD No. 267. The detail for the $1,789,440 is reference to a contract for $1,611,778 plus burdens of $177,662. The word contract is not support in anyway for costs, it is simply a word and a number. A third example, are the costs detailed in the response to OPC POD No. 268. There is $315,521 for which no detail was provided and then there are two combustion inspections each with an expense of $1.6 million. The concern is the detail indicates that the total project cost for each inspection is $2.158 million, with $558,000 being capitalized. There is a concern that the amount being capitalized is understated and there is also a concern that the documentation that was supplied indicates the expense is high. The documentation supplied for these two line items is the only real documentation supplied, it is confidential, and it is less than the projected expense. That fact raises my concern even more with the cost estimate for which no supporting cost documentation was supplied.

Q. ARE YOU RECOMMENDING AN ADJUSTMENT FOR ANY OF THE COSTS YOU ATTEMPTED TO REVIEW?

A. Yes. As shown on Exhibit HWS-1 Schedule C-10, I am recommending a specific adjustment of $2,688,677 ($2,331,755 on a jurisdictional basis) for cost included in A&G Office Supplies and Expense that are not appropriate costs to be included in rates especially in today's economy. With respect to the Company's failure to provide sufficient supporting documentation for the remaining costs I have factored that into my Productivity discussion and adjustment as will be discussed next.

Q. WHAT ARE THE COSTS THAT YOU ARE RECOMMENDING AN ADJUSTMENT FOR BECAUSE YOU BELIEVE THEY ARE NOT APPROPRIATE?

A. On Exhibit HWS-1 Schedule C-10, lines 1 and 2, I adjusted out $2,688,677 of costs. The first adjustment of $1,488,677 consists of $1,268,677 for events such as the Tampa Bay Lightning for $59,900, the Tampa Bay Buccaneers for $139,527, the Orlando Magic for $20,000 and more. The two listings of events and costs are included as Exhibit HWS-3. The remaining $220,000 is for service awards. Typically the Commission would allow the payment of service awards if the amount were determined to be reasonable but I believe at this time this cost should not be passed on to ratepayers.

The second adjustment is $1,200,000 for what is described as "Corporate Managed Account". This appears to be a large petty cash account for the president's budget center. The Company did not provide any supporting documentation for this expense as requested therefore the cost is not justified and should be excluded from rates.

Q. ARE YOU SURE THAT THE COMPANY DID NOT REMOVE THE COSTS IN QUESTION FROM ITS RATE REQUEST?

A. There is no evidence that the cost have been removed. The costs were budgeted in account 921 "A&G Office Supplies and Expense". In response to OPC Interrogatory No. 391 the Company supplied a reconciliation that links the budget costs reviewed to MFR Schedule C-1 and in turn to MFR Schedule C-2. The only adjustments O&M Expense reflected that remove budgeted costs are the aircraft adjustment and the advertising. The costs are not aircraft costs and the advertising adjustment of $3.388 million relates to labor costs in account 920 and advertising costs in account 9301.

XV. O&M EXPENSE PRODUCTIVITY ADJUSTMENT

Q. ARE YOU RECOMMENDING A PRODUCTIVTY ADJUSTMENT TO THE COMPANY'S O&M EXPENSE REQUEST?

A. Yes. The Company's request is excessive because it reflects an overloading of unsupported costs into the test year, and it does not reflect the cost savings that should be generated from any increase in maintenance and improvements in operations. In addition the Company can be expected to undertake every effort after rates are established to minimize its future costs so the corporate strategy can be achieved.

Q. IS THE COST SAVINGS AND UNSUPPORTED COSTS THE CONCERNS YOU HAD IDENTIFIED EARLIER AND YOU INDICATED WOULD BE DISCUSSED AT LATER TIME?

A. That is correct. The unsupported FERC 890 cost request of $6.9 million, the unidentified distribution increase of $7.7 million are examples and the budgeted costs that were not supported with documentation as requested. The Company's testimony identifies a number of improvements without any explanation as to where the cost savings are reflected. For example, the testimony of David Sorrick, at page 15, indicates that there will be cost savings from the Hines Power Block 4 Combustion Optimization Package in the future and, on page 16, the Anclote Cooling Tower project is expected to reduce maintenance cost in the future. There has to be some benefit to ratepayers from the significant increase in spending being requested that will offset the cost. If that cost savings is not reflected then there is the risk that it will flow through to shareholders absent a regular earnings adjustment filing by the Company. If rates are set based on the significant spending without recognition of the benefits that are forthcoming, when the cost savings occur there is no way for ratepayers to receive that benefit.

Q. WHAT IS THE CORPORATE STRATEGY TO WHICH YOU REFERRED?

A. In response to OPC Production of Documents No. 5, the Company provided a copy of the 2009 Progress Energy Florida Strategic Plan. An important point in the strategy commitment is the following statement "The overall mission of Progress Energy is to reward its investors by providing above-average total shareholder returns over a continuous timeframe." This thought process is further emphasized in the financial objectives that include "Annual EPS growth (4-5%)", continue dividend growth and an annual TSR of 8-10%. Part of the strategy is discussed on page 12 in the customer price analysis where it is indicated that the base rate filing in 2009 will add significantly to the 2010 price. There is also a reference to pursuing wholesale customers and consider the opportunities to expand generation, transmission, distribution and/or customer service to support other utilities in Florida. And then there is the commitment to annual productivity gains of at least 3%-5%. This emphasis on productivity gains is mentioned on pages 7 and 27. The strategy mentioned is noteworthy given the current rate request because it focuses on shareholders and is not concerned with the fact that the plan mentions that a weakness is customer rates generally are higher than peers.

Q. *WHAT IS YOUR INTERPRETATION OF THE CORPORATE STRATEGY YOU JUST DISCUSSED?*

A. The Company is requesting a $500 million rate increase. The increase reflects significant cost increases over historical cost levels that appear to have been controlled in the past by the Company. The significant increase requested includes costs such as payroll increases and incentives that many other companies are freezing, reducing or in the case of utilities minimizing the amounts requested in rates. PEF has not followed what many other companies are doing. The overall mission as clearly stated by PEF is to provide "above-average total shareholder returns". This mission is not only insensitive to ratepayers during theses difficult economic times but it also reflects a mentality that through regulation this company is free to ignore the economic realities of the day. It is clear that the focus is an increasing return for shareholders at the expense of ratepayers. Even though the plan identifies an objective of customer satisfaction and affordable rates, the rate request suggests that PEF has a different interpretation of what affordable rates are based on customer concerns presented in public hearings.

Q. ARE YOU QUESTIONING THE COMPANY'S EFFORT TO MINIMIZE RATEPAYER COSTS YET ACHIEVE THE MISSION TO REWARD SHAREHOLDERS WITH ABOVE-AVERAGE RETURNS?

A. Yes. As indicated earlier the Company goal is to award shareholders with above-average shareholder returns. There is no goal to minimize the rate request and that is substantiated with the business as usual pay increases, increased incentive compensation and the other significant cost increases that are recorded above the line. Mr. Toomey states, on page 13, of his testimony that the Company understands the tough realities of the current economic conditions and I believe the Company does but from a shareholders perspective. This is substantiated by the increases requested for above the line test year costs while 2010 budgeted shareholder costs have declined. In response to OPC Interrogatory No. 309 the Company stated that the declining economic condition was the reason that donations and civic expenses were less in the 2010 budget than in 2008. A budget reduction of approximately 20% of below the line costs for civic functions and donations is an important fact when you take into consideration the increase in above the line costs. Business as usual for above the line costs and belt tightening for shareholder costs in my opinion is evidence that the focus is on shareholder returns.

Q. HOW CAN THE CORPORATE STRATEGY ACHIEVE THE MISSION TO REWARD SHAREHOLDERS WITH ABOVE-AVERAGE RETURNS?

A. As stated above the Company has requested a $500 million rate increase. The increase is based on significant projected increases in cost estimates. The corporate strategy to achieve productivity gains of at least 3%-5% is the second step to achieving the success desired. If rates are increased based on the significant cost increase requested and then afterwards the productivity gains are achieved, the benefit will flow solely through to shareholders. This is not the time to be seeking excess earnings at the expense of ratepayers. This is the time to tighten the belt, contain costs and make concessions that will help ratepayers deal with today's economic downturn. This filing does not do this.

Q. WHAT ARE YOU RECOMMENDING FOR A PRODUCTIVITY ADJUSTMENT?

A. As shown on Exhibit HWS-1, Schedule C-11, the adjustment I am recommending is a reduction to O&M expense of $13.034 million. My adjustment takes the Company's requested 2010 O&M Expense net of labor and assumes a 3% productivity factor. The 3% is the low end of the Company strategy.

Q. IS THIS TYPE OF ADJUSTMENT APPROPRIATE FOR THE COMMISSION TO MAKE?

A. Most certainly. The Commission has to determine a fair cost of service that will produce a reasonable opportunity for the Company to achieve a reasonable rate of return. The Company has set a productivity goal of 3%-5% that means there is a good possibility of achievement of that goal and it would be inappropriate to ignore that fact. In New York, when Consolidated Edison Company files for a rate increase it incorporates a 1% productivity adjustment to payroll as previously directed by the commission. In the decision in Case 08-E-0539 the Commission determined that because of the increased investment in plant (similar to PEF's reflecting an increase in plant investment) there would be an increase in productivity and ruled that the productivity adjustment should be 2% instead of 1%. After evaluating the issues, the Commission made an additional adjustment reducing O&M cost by $60 million. This adjustment factored in the downturn in the economy and the impact the company's request would have on ratepayers. In the decision the company was ordered to implement austerity programs to constrain costs and tighten belts to limit discretionary spending. The adjustment I am recommending is reasonable and pales in comparison to the adjustment ordered by the New York Commission.

XVI. OTHER OPC WITNESS ADJUSTMENTS

Q. HAVE YOU REFLECTED ADJUSTMENTS PROPOSED BY OTHER OPC WITNESSES IN YOUR EXHIBITS?

A. Yes. The impact of adjustments to the reserve for accumulated depreciation and the change in depreciation expense has been reflected on Exhibit HWS-1, Schedule B-5. The impact on deferred income taxes was calculated by me based on the average change to the reserve for accumulated depreciation.

On Exhibit HWS-1, Schedule D, Page 2, I have reflected the capital structure ratios and the weighted cost rates as recommended by Dr. J Randall Woolridge. On Exhibit HWS-1, Schedule D, Page 1, I have reflected a revised capital structure that changes the capital structure ratios after reflecting the change in deferred income taxes that resulted from the adjustment proposed by OPC witness Jacob Pous.

On Exhibit HWS-1, Schedule B-2 and Schedule C-2, I have reflected the adjustments proposed by Ms. Kimberly Dismukes.

Q. DOES THAT CONCLUDE YOUR TESTIMONY?

A. Yes.

BY MR. REHWINKEL:

Q. Mr. Schultz, mindful of the -- are you aware of the five-minute rule for opening -- for summarizing testimony?

A. I am.

Q. Okay. And mindful of that, do you have a summary of your testimony to give?

A. I do have a summary. I'll try to get it within the five minutes and try to do it slow enough so it doesn't affect the court reporter.

Progress Energy is requesting that rates be increased by 499 million. The Office of Public Counsel has recommended a reduction of at least 35 million.

Based on the various OPC witness review of information, the request by the company is not substantiated by the record. The request is not only excessive from a general rate case perspective, but is even more inappropriate given the impact it will have on customers when taking into consideration the current state of the economy.

Progress Energy has ignored the economic impact that has affected ratepayers, other companies throughout the country and even other utilities by requesting that compensation be increased by an annual average of 4.7 percent; by requesting incentive compensation be fully funded by ratepayers, even though the goals do not create an incentive to perform at a level that would benefit customers; by requesting the full cost of directors' and officers' liability insurance that other commissions have recognized as costs that should be borne in part by shareholders; by requesting operating and maintenance costs that are higher than typically incurred; by requesting ratepayers to continue to build up a storm reserve that is already more than sufficient given recent history; by ignoring the productivity gains that are proposed to be achieved in the company's strategic plan; and by requesting an excessive return on equity.

This Commission has the unenviable task of sorting through the various arguments that are being made to determine whether the requested increase is reasonable or not.

Ratemaking principles require the company to provide sufficient evidence to support the increase requested, and the Office of Public Counsel is of the opinion that the burden has not been met. The company has failed to provide justification for increases in employees beyond the current levels; increases in compensation levels, especially since the actual increase in 2009 is below what was in the filing; and the inclusion of incentive compensation to the 99.6 percent of its employees for performance that provides no identifiable benefit to ratepayers.

The company failed to show why a storm study that ignores specific pertinent facts and includes emphasis on facts that should be given less weight should be considered as justification for an increase in the storm accrual.

The company failed to justify spikes in O&M costs when compared to historical costs. For instance, in vegetation management the increases are suggested to be supported by NERC and Commission standards, as if those standards did not exist before 2010.

The company failed to identify in prefiled testimony increases in nuclear fuel, injuries and damages, and an ARO adjustment.

The company failed to provide supporting detail for 1.2 million of budgeted office supplies expense when they supplied a document that simply identified it as corporate managed account, CHWS-3.

A number of companies around the country have taken some initiative to address the current economic impact on them because they do not fall under the protective umbrella of regulation. Even utilities have done this.

One thing the company did ignore -- did not ignore is the economic impact on pension costs.

Based on the evidence, the Office of Public Counsel recommends the company's request be denied.

MR. REHWINKEL: Mr. Schultz is tendered for cross-examination.

CHAIRMAN CARTER: Thank you, Mr. Rehwinkel.

Ms. Bradley.

MS. BRADLEY: Just a couple of quick questions.

CROSS EXAMINATION

BY MS. BRADLEY:

Q. I think I asked Mr., well, one of the folks yesterday whether or not they had seen an *Orlando Sentinel* article that talks about the decline in household income for Florida. Have you seen that?

A. I didn't see that specific article, but I've seen a number of other articles.

Q. Are you aware of the fact of what this article is talking about, that the, Florida has suffered between 2007 and 2008 the nation's worst decline in household income, and it mentioned the median income falling by about 3.9 percent?

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Ms. Bradley asked this witness if he had seen that article. He stated no. And now she's asking is he aware of certain assumptions made in the article that he says he has not seen. So I object. Lack of foundation.

CHAIRMAN CARTER: Ms. Bradley, to the objection.

MS. BRADLEY: Actually what he said was that he has seen several other articles, and I was asking him if he was aware of the information that's provided in this.

CHAIRMAN CARTER: Ms. Cibula.

MS. CIBULA: I think it should be allowed.

CHAIRMAN CARTER: Okay. You may proceed.

MS. BRADLEY: Thank you.

THE WITNESS: While I haven't seen the specific numbers that you've talked, are referencing, I've seen quotes of the increase in unemployment in Florida in certain articles, and I've, I've seen the talk about, you know, the economic impact. And I'm familiar with some of the activities within the real estate down here through other means.

BY MS. BRADLEY:

Q. Is that something that you took into consideration when you were forming your opinion in this case?

A. I took into consideration the impact in Florida. I took into consideration the impact across the country. I testify in many jurisdictions and evaluate a lot of rate cases. So I've seen the impact it has around the country. And I am aware of what it is like in Florida too.

Q. Is there anything in your area of expertise that says when you're considering, you know, a request for rate increases that you should not consider the state of the economy?

A. My opinion is, is that you have to take into consideration the state of the economy. I mean, first of all, you're asking the ratepayers of your state that you service to pay additional costs. Now that, that increase can have an impact not only on those ratepayers, but it can ultimately have an impact on the company, and then a snowballing effect on ratepayers even more. Because if those ratepayers aren't able to pay their bills, you have an increase in bad debts, which if those come up, the company's got the option of coming in and saying, hey, we need more money. Look at how our bad debts have increased. And then there you go again, another increase, and the ratepayers suffer more.

And I know that it's been considered in

jurisdictions because I've seen, based upon economic conditions, where commissions have, despite what a company may have put in rates or put in their rate filing as the projected increase or even actual increases, where they limited the amount of increase that was allowed for payroll in there.

And one specific case is in New York after the commission made an adjustment, not only for payroll, to reflect the impact of the economy, they made what they called a $60 million austerity adjustment to Consolidated Edison's rates to say, you know, the economy is bad. You have to take some measures to make sure that the costs of service that you're providing to ratepayers is reasonable. So it's my opinion and I've seen it done by commissions.

CHAIRMAN CARTER: Mr., on this -- excuse me, Ms. Bradley. Is this on the infamous 264? Do you, do you have that?

Would you show him? Mr. Rehwinkel, do you have your copy?

MR. REHWINKEL: Is that the ROE?

CHAIRMAN CARTER: This is the -- yes. I wanted to ask him, since he mentioned ConEdison. I saw it on there. I was going to ask him was it this case here.

MR. REHWINKEL: It's deep in my stack here. Maybe --

CHAIRMAN CARTER: Ms. Kaufman usually has hers handy.

MS. KAUFMAN: Yes. I'm looking for it.

MR. REHWINKEL: It's always the last one.

CHAIRMAN CARTER: Thank you.

You mentioned ConEdison in your response to Ms. Bradley?

THE WITNESS: Yes, sir.

CHAIRMAN CARTER: On, about three-quarters of the way down here on this sheet you'll see New York.

THE WITNESS: Yes, sir.

CHAIRMAN CARTER: It's the ConEdison. Is the case that you're talking about, where they went back and did a 60 -- I think -- what was the term you used, a 60 thousand, a 60 million --

THE WITNESS: $60 million austerity adjustment is what they called it.

CHAIRMAN CARTER: Was that in this case here?

THE WITNESS: That was in this case. Yes, sir.

CHAIRMAN CARTER: Okay. And the reason they did that was because of the economy? Is that --

THE WITNESS: That -- right. The economy was addressed frequently in that case. I, I testified in that case.

CHAIRMAN CARTER: Okay. You don't happen to remember the -- staff, can we get that, that case number so we can have that when we go through our deliberations? Just make a note. Get the case number.

MR. SAYLOR: Yes, sir. We'll find that, Mr. Chairman.

CHAIRMAN CARTER: Okay. Ms. Bradley, you may continue.

MR. REHWINKEL: That, that case, I think --

CHAIRMAN CARTER: Have you got the cite?

MR. REHWINKEL: It was provided as a late-filed exhibit to Mr. Schultz's -- it was, it was provided in discovery to staff very late. It is a very thick order. It's about a 400-page order. But I know we can, we can locate it. Yes, sir.

CHAIRMAN CARTER: Okay. Thank you.

Ms. Bradley.

MS. BRADLEY: Thank you.

BY MS. BRADLEY:

Q. Have you had an opportunity to review any of the information from the service hearings, or has anybody conveyed to you some of the testimony from the customers at those hearings?

A. I, I just call them little snippets, but I reviewed a lot of clippets.

Q. Okay.

A. Or whatever you guys were calling it yesterday from the newspapers that had to do with them. I'm very familiar with a lot of, a lot of those, yes.

Q. Did you see anything about the testimony from consumers that talked about having to -- that either they had lost their jobs or their pay had been cut or their hours had been cut and that type of testimony?

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Objection. Friendly cross. I would struggle to see how this is in any way hostile to Mr. Schultz.

CHAIRMAN CARTER: Move it, Ms. Bradley. Move it. Objection sustained.

MS. BRADLEY: I don't believe anyone has asked this question yet to this witness, sir.

CHAIRMAN CARTER: The objection is sustained. Move on.

BY MS. BRADLEY:

Q. Well, I was going to ask you a different question. That was kind of a foundation for it. Maybe you can answer it without the foundation.

I asked Mr. Toomey yesterday if he thought the fact that so many customers are having to sacrifice, if it was reasonable for them to expect the company to make similar sacrifices.

A. I heard the question.

MR. BURNETT: Mr. Chair? Objection. Friendly cross, and that was not a question at all. That was a declarative, not an interrogatory.

MS. BRADLEY: Well --

CHAIRMAN CARTER: Just restate it. Just restate it. Restate the question. Rephrase, rather.

BY MS. BRADLEY:

Q. The testimony at the customer service hearings stated there were a number of customers that, and I believe you indicated you were aware that customers were complaining about various things, including loss of jobs and having to cut back on pay and hours and this type of thing. And I -- my question to you is is it reasonable for those customers to expect a company to make similar sacrifices in bad economic times?

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Mischaracterization of evidence. Counsel is testifying. I believe she's in defiance of your prior ruling. It's still friendly cross.

CHAIRMAN CARTER: Ms. Bradley, to the objection.

MS. BRADLEY: To the objection, it's in the record, and I was merely stating some of the evidence in the record, trying to lay a foundation for the question.

CHAIRMAN CARTER: Ms. Cibula.

MS. CIBULA: I agree that it is friendly cross-examination.

CHAIRMAN CARTER: Objection sustained. Move on.

BY MS. BRADLEY:

Q. Do you think it's reasonable for customers to expect companies to make sacrifices and cutbacks in salary and bonuses during a time when customers are suffering, may be suffering? As you indicated, the economy was very poor.

A. I think that's what I've said in my --

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Objection. She has now removed her characterization and testimony but asked the same question again. Friendly cross.

CHAIRMAN CARTER: To the objection, Ms. Bradley.

MS. BRADLEY: There is no such thing as friendly cross. It's not redundant, it's not immaterial, it's not irrelevant, and it hasn't been asked of this witness. So I think we're entitled to ask the question. We asked it of their witness, and I think we're entitled to ask it of this witness as well.

CHAIRMAN CARTER: Ms. Cibula.

MS. CIBULA: I believe that it is friendly cross. And Ms. Bradley needs to show how her interest is adverse to this witness's interest.

CHAIRMAN CARTER: Ms. Bradley?

MS. BRADLEY: I have no idea. I haven't asked him the question. I won't know until I ask him.

CHAIRMAN CARTER: The objection is sustained. The objection is sustained. Move on.

MS. BRADLEY: I think I'd like to make a proffer, Your Honor.

CHAIRMAN CARTER: You're recognized.

BY MS. BRADLEY:

Q. Going back to my question, sir. Are you aware of the testimony where the customers came in and testified that they are having to make sacrifices, such as they've lost jobs, they've had their hours cut back, they've had their pay cut back, and various sacrifices that they're facing right now?

A. I'm aware of that. In fact, I alluded to that in my testimony to some extent, that the company has not recognized the fact that customers have made cuts, that companies around the country have had to cut costs, that other utilities have even done so, and that the company has come in with pay as, pay as usual increases, incentive comp as business as usual, and that they've just failed to recognize that fact.

Q. When customers are making these type of sacrifices, do you think it's fair for them to expect their public utility to make similar sacrifices as far as bonuses and raises and that type of thing?

A. I think I alluded to that also in my testimony, that, yes, they should. I mean, the company, the company has an obligation to provide the service at a fair and reasonable rate. And given the economic conditions, they should be willing to make the similar sacrifices that people are making across the whole country.

Q. Do you feel like that puts the company at risk, cutting back on things that are, such as executive compensation packages, I mean, as far as freezing the pay or not having bonuses?

A. I don't believe it does. Because in fact there's a number of companies that, utility companies that have compensation that isn't fully included in rates. This company is asking for everything in rates. They're asking for their full compensation, their full benefits.

And like I said, there's, there's companies out there. ConEdison is a prime example. No incentive comp. And in addition to that, they had a limitation on their, their compensation increase that was granted to them, and, on top of that, a productivity adjustment of 2 percent was made in that very case that we discussed earlier.

I mean, so other companies are having to make that. And I identified companies within my testimony that have foregone increases in pay levels, or even though -- in particular one had the increase that was granted for union employees, they only asked for a portion of what was granted to union, union employees in their rate case.

So there, there are companies out there who are taking into consideration this economic impact. I mean, unregulated companies have no choice, because if they don't, it's really going to hurt them. A regulated company has that umbrella that I've discussed that kind of protects them to some extent because they, they can come in and ask for that increase in rates. And, and if it's granted at the level they want, then they're fine.

I mean, how many companies are going to be given the alternative to be able to earn a return?

And there's companies out there who don't even have good credit ratings. I'm very familiar with a company in Vermont that is below credit grade. They've been below credit grade for five years. They've never cut their dividend. They've continued to pay incentive comp, but they only have part of it -- they only get 50 percent of the employees included in rates, and they only -- they don't have any of the executive incentive comp in rates.

So to think that they'd be so financially strapped that they wouldn't be able to exist I think is a little farfetched in my opinion.

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Although I know we are on a proffer now for appellate purposes, I would just preserve my objection, just for the, for the proffer record, that that lacks foundation beyond the scope of direct testimony. And I would forgo a voir dire for this witness's qualifications to opine on those, just, since we are on an appellate record at this point.

CHAIRMAN CARTER: Okay.

MR. BURNETT: Thank you, sir.

CHAIRMAN CARTER: Okay. For the record.

Ms. Bradley, you may continue.

BY MS. BRADLEY:

Q. There was testimony from Mr. Toomey last night that they had laid off something like 150 witnesses -- employees, and yet they were still unwilling to freeze executive salary increases and bonuses. Is that consistent with good business practice?

A. Well, my understanding, first of all, is the 150 that I'm familiar with was done in 2008. So it isn't something that they're doing currently. I mean, in fact they've asked for an increase in employees above what they already have. And since the date that they filed, through the most recent information I have, they actually had a decline in employees. So that increase isn't justified in the first place.

But as to the increase in compensation, I don't believe it's justified. In fact, it's -- I recently received an update to a response in a New York case where it shows that the budgeted salary increases overall -- now this isn't just your step increase or your merit increase or anything -- overall for 2009 was 3.8 percent, but the actual came in at 1.8 percent for 2009. That's a big drop from what they were predicting would occur in December of 2008 to what actually occurred. And they're forecasting in that study a 2.7, I think it is, for 2010. Those aren't even close to what the company is asking. The company is way above that.

MR. BURNETT: Mr. Chair?

CHAIRMAN CARTER: Mr. Burnett.

MR. BURNETT: Again, just to preserve my objections on this proffer, I'd move to strike everything to from the words "I recently received" to ending with "above that" for outside the scope of direct testimony. Thank you.

CHAIRMAN CARTER: Okay.

MR. REHWINKEL: Mr. Chairman, I understand Mr. Burnett is preserving his objection, and I understand, at least until we understand the termination point of the proffer, that that's where we are. But I would also like to make it clear that -- or make sure there is an understanding that because this is testimony on proffer, that once we get into, we become not in the proffer mode, that Mr. Schultz's answers to the extent they cover the same ground will not be subject to an asked and answered objection.

CHAIRMAN CARTER: Okay.

Ms. Bradley, you may proceed.

MS. BRADLEY: That was the end of my proffer, sir.

CHAIRMAN CARTER: Okay.

Mr. Burnett, the proffer is terminated.

MR. BURNETT: Thank you, sir.

Mr. Schultz, please turn to Page 59 of your direct testimony.

CHAIRMAN CARTER: This is in reference to the proffer, Mr. Burnett?

MR. BURNETT: Oh, no, sir. I thought I was recognized for cross.

CHAIRMAN CARTER: No. You're not recognized.

MR. BURNETT: I'm sorry. Forgive me. I have nothing else to add on the proffer. I'm sorry.

CHAIRMAN CARTER: Okay.

Ms. Bradley, you completed your proffer?

MS. BRADLEY: Yes, sir.

CHAIRMAN CARTER: Anything further for this witness?

MS. BRADLEY: I don't guess I should try.

CHAIRMAN CARTER: Is that a no?

MS. BRADLEY: That's a no.

CHAIRMAN CARTER: Okay. Thank you. Ms. Kaufman.

MS. BRADLEY: Under the circumstances.

CHAIRMAN CARTER: I beg your pardon?

MS. BRADLEY: That's a no in light of the circumstances.

CHAIRMAN CARTER: Ms. Kaufman.

MS. KAUFMAN: I have no questions for this witness, Mr. Chairman.

CHAIRMAN CARTER: Mr. Lavia.

MR. LAVIA: Good morning, Mr. Chairman. No questions.

CHAIRMAN CARTER: Mr. Burnett, you're recognized for cross.

MR. BURNETT: Thank you, sir. Sorry for jumping the gun.

CROSS EXAMINATION

BY MR. BURNETT:

Q. Mr. Schultz, Page 59 of your direct testimony, please, Lines 1 through 2.

A. Yes, sir.

Q. You state there that you have reflected adjustments proposed by other OPC witnesses in your exhibits; is that correct?

A. That is correct.

Q. Is that a true statement as you sit here today, sir?

A. To the best of my knowledge, yes. I've reflected the adjustments proposed by Mr. Pous, I reflected the return on equity by Mr. Woolridge, and I reflected an adjustment proposed by Ms. Dismukes.

Q. Thank you, sir. Please turn to Exhibit HWS-1, Schedule A-1, Page 1 of 1, Line 8.

A. Line 8?

Q. Yes, sir.

A. I'm there.

Q. Do you see the number reflected there in parentheses reflecting a negative $35,038,000?

A. Yes, I do.

Q. And that number reflects the approximate $35 million rate reduction that OPC advances in this case; correct?

A. That is correct.

Q. Please turn back to the cover page of your testimony, sir, while keeping your finger on that exhibit.

A. Yes, sir.

Q. Are you there, sir?

A. Yes, sir.

Q. Would you agree with me that your testimony reflects that it was filed in this proceeding on August 10, 2009?

A. Yes, sir.

Q. Would you please flip back to HWS-1, Schedule

A-1, Page 1 of 1, sir?

A. I'm there.

Q. You would then of course agree with me that since your testimony was filed on August 10, 2009, that the $35 million reduction reflected on Line 8 necessarily and logically cannot reflect the consideration of any evidence that took place after August 10, 2009, because that would be a date after your testimony; correct, sir?

A. I don't understand --

MR. REHWINKEL: I want to object to the characterization of the word "evidence." I don't, I don't think it's clear. I think it's vague as to what evidence means. Are we talking about evidence that has been admitted into this hearing or, or facts?

MR. BURNETT: I can rephrase, Mr. Chair.

CHAIRMAN CARTER: Rephrase.

BY MR. BURNETT:

Q. Mr. Schultz, you would agree with me that August 11th chronologically comes after August 10; correct?

A. That's correct.

Q. And you would agree with me that any subsequent dates preceding after August 10, 2009, would be dates that happened in history after your testimony;

correct?

A. That's correct.

Q. And you would then agree with me that with regard to any of the facts or information in your testimony that were filed with this Commission on August 10, that facts or circumstances that happened after August 10 necessarily could not be considered in your testimony because they would have happened after the date you filed it; would you agree with that, sir?

A. I would agree that my testimony is based upon the facts and circumstances that existed as of August 10th, 2009.

Q. Thank you.

A. But there are other events that have happened subsequently.

Q. Yes, sir.

A. And the company has made information added to their position based upon those events that have occurred, and you can't ignore what has happened after August 10th.

Q. I see, sir. And so are you suggesting in the advancement of your testimony that this Commission should consider facts and circumstances that have taken place after August 10, 2009?

A. What I'm saying is the Commission has the option to evaluate events that have occurred after August 10th, just as they have the option of considering any events that happened subsequent to the company's initial filing of their testimony and their exhibits. And those things are already on the record. The company filed revised schedules and those are on the record. The company has taken and answered questions. Those are on the record.

So there are things that happened after the fact that get included and have to be considered. To the extent that the Commission decides to, to consider them, that's their, their option. My understanding is you, you take in the facts -- when I reference you, I'm referring to the Commission -- and they can, they can decide what, what is relevant and what is not.

Q. Mr. Schultz, let me try again. Is it your personal contention that this Commission should consider all relevant facts and circumstances from today until the time they issue their order in this matter in coming to their opinion?

A. As I indicated, they can decide what are the relevant facts that have happened subsequent to the different filing dates.

Q. Mr. Schultz, are you contending -- I know what the Commission can do. I'm asking you, sir. Are you contending that as part of your testimony in summarizing the other OPC witnesses in this case to yield a $35 million reduction, are you, sir, contending that this Commission should consider all relevant evidence from the time of today until they issue their order in this case in making a decision in this matter?

A. My personal opinion? I'm kind of confused on your question because I've tried to elicit what my position is: That the Commission has the ability to evaluate whatever they deem relevant. What my opinion is as to what is relevant may not be relevant to them. So I'm a little confused as to where your question is coming from.

Q. Sure. Let me try to help you, Mr. Schultz. In your opening summary you said that the Commission should take consideration of the current state of the economy; is that correct?

A. And I said that in my testimony also, yes, sir.

Q. Yes, sir. By use of the term "current," what, what does that mean in a temporal scope?

A. The current state of the economy would have been the state of the economy on August 10th, 2009. And if they decide that the state of the economy on September 30th is relevant, then they can evaluate it as of September 30th. If they decide as of October 1st, then they can decide October 1st. That's their decision, not mine.

Q. Mr. Schultz, you also stated that you had been aware of certain articles regarding the economy and real estate in Florida when you were talking with Ms. Bradley earlier. Do you recall that?

A. Yes, sir.

Q. What are the dates of those articles?

A. I couldn't give you the specific dates. I just, like I said, I saw the snippets that were being put in papers throughout the hearing process when they had all the customers come in. And, I mean, I saw the debates where some customers said, hey, we can't, we can't afford this. I saw where some customers came in and said Progress should have it. And then I saw the follow-up articles that says these people aren't, aren't independent. So, you know, I've seen the realm of articles that have gone different ways.

Q. Do you recall if those took place in the month of August 2009?

A. I can't tell you exactly how far back those went. I can't, I can't even tell you the first date that, that the first hearing for customers was specifically.

Q. By offering testimony on your reflection of these articles that you can't remember the date on, are you suggesting that the Commission should base their decision on any of your testimony regarding those, sir?

MS. BRADLEY: Objection, Your Honor.

CHAIRMAN CARTER: Yes, ma'am.

MS. BRADLEY: He's crossing on a proffer, which is not permissible.

CHAIRMAN CARTER: Mr. Burnett, to the objection.

MR. BURNETT: Yes, sir. That was -- my recollection was the discussion of the articles was before the proffer. But if, if Ms. Bradley is suggesting that it was within, I'm happy to withdraw.

CHAIRMAN CARTER: Okay. Withdraw and move on.

BY MR. BURNETT:

Q. Mr. Schultz, were you here yesterday?

A. Yes, I was.

Q. Did you hear some questioning on Mr. Toomey regarding recent comments made by Chairman Bernanke?

A. I recall that, yes.

Q. Do you think that -- as an expert offering opinion testimony in this case, do you think that the Commission should consider those comments of Chairman Bernanke in reaching a decision in this case?

A. That's their choice. I'm not going to -- I can't really tell them to make that. It's something that I think that they have to give some consideration to. I mean, they have to have the latitude to be able to evaluate what's going on. And I'm sure if the economy suddenly took another nosedive, the Commission would have to take that into consideration. And I'm sure if the economy all of the sudden took some kind of spike upwards, that everything got better, that that also would have to be reflected somehow. I mean, you just can't ignore some of the events that are happening.

Q. Thank you, sir. And I'm fully aware of what the Commission's authority and prerogative is on what evidence they consider, so if I could just keep focused on your opinion as an expert offering testimony.

Do you think that this Commission should consider the current unemployment rate in the State of Florida as we sit here on 9/25/09?

A. I think they may, may take it into consideration. My testimony, as you indicated, was as of August 10th. I said that they had to consider things as of the date of my filing. I don't think things have changed that significantly. So whether they look at it as of September 25th or August 10th, that's, you know, that's their choice again.

In my opinion, again, I say it's up to them to make the decision. I'm here to proffer some information to them. I'm here to make my recommendations. And I take into consideration the level of what I think may be important, and whether that's important to them, that's, that's a different story.

Q. Thank you, Mr. Schultz. And if the Commission did consider evidence that, looking, as you say, at the big picture and keeping in mind everything going on in the present day, you'd agree with me that it would be fair for them to consider all relevant facts and circumstances, particularly if there was evidence that showed that my company was $95 million more in the hole due to recent sales and load?

MR. REHWINKEL: Mr. Chairman, I'm going to object.

MR. BURNETT: I can withdraw that, Mr. Chairman.

CHAIRMAN CARTER: Okay.

MR. BURNETT: Thank you. I have nothing further for Mr. Schultz.

CHAIRMAN CARTER: Thank you.

Staff.

MR. SAYLOR: Mr. Chairman, we have a couple of questions, and I'll make them really quick.

CROSS EXAMINATION

BY MR. SAYLOR:

Q. Good morning. How are you doing, Mr. Schultz? How are you?

A. I'm fine, thank you.

Q. All right. If you'll turn to Page 34 of your direct testimony, Lines 11 through 18. It is where you discuss making an adjustment for rate case expense.

A. Yes, sir.

Q. All right. And you asked that the Commission make an adjustment for rate case expense; is that correct?

A. That is correct.

Q. All right. And at your deposition I asked you about a couple of recent orders or rate cases that the Commission issued orders in, the TECO rate case and also the Florida Public Utilities Company electric, or gas rate case, and I asked you if you were familiar with those orders.

A. I was familiar with the orders. I wasn't totally familiar with the discussion on them.

Q. On rate case expense?

A. That's correct.

Q. All right. And since the deposition have you become more familiar with those orders and what they say about those --

A. The amortization period was four years.

Q. Right. And the question that I have for you is is it your testimony that the Commission should exclude the entire amount of the amortized rate case expense from the working capital in an effort to reflect a sharing of rate case expense between the shareholders and the ratepayers, since both would be benefiting from the rate, the pending rate case?

A. And as I said in my deposition, I wouldn't be opposed to that. It's, you know, it's treated various ways. And so I'm, I'm not going to -- in fact, I wasn't even sure that they were treated the same way in both of those cases. So if the Commission decides to exclude it, I'm fine with that.

MR. SAYLOR: All right. Thank you. That ends staff's questions.

CHAIRMAN CARTER: Thank you.

Commissioners, anything from the bench?

Redirect, Mr. Rehwinkel?

MR. REHWINKEL: No redirect.

CHAIRMAN CARTER: Exhibits?

MR. REHWINKEL: The Citizens move Exhibits 169 through 172.

CHAIRMAN CARTER: Are there any objections?

MR. BURNETT: No, sir.

CHAIRMAN CARTER: Without objection, show it done.

(Exhibits 169 through 172 admitted into the record.)

And we don't have to go to the back pages because we don't have any; right?

Okay. Anything further for this witness?

Thank you, Mr. Schultz. You may be excused.

THE WITNESS: Thank you very much.

MR. REHWINKEL: Mr. Chairman, I -- my witness is, is in the back there. I need to get him.

CHAIRMAN CARTER: Let's take a break. Let's take ten, everybody.

(Recess taken.)

(Transcript continues in sequence with Volume 15.)

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 30th day of September, 2009.

Linda Boles

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