BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

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In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.	DOCKET NO. 090001-EI FILED: October 5, 2009

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the Direct Testimony of Tomer Kopelovich and the Direct Testimony of Ronald A. Mavrides was furnished to the following, by U.S. Mail, on this 5th day of October, 2009:

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DOCKET NO. 090001-EI: Fuel and purchased power cost recovery clause with generating performance incentive factor.

WITNESS: **Direct Testimony Of Ronald A. Mavrides,** Appearing On Behalf Of Staff

DATE FILED: October 5, 2009

DIRECT TESTIMONY OF RONALD A. MAVRIDES

Q. Please state your name and business address.

A. My name is Ronald A. Mavrides and my business address is 4950 West Kennedy Blvd., Suite 310, Tampa, Florida 33609.

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

A. I am employed by the Florida Public Service Commission as a Professional Accountant in the Division of Regulatory Compliance.

Q. How long have you been employed by the Commission?

A. I have been employed by the Florida Public Service Commission since October 2007.

Q. Briefly review your educational and professional background.

A. In 1990, I received a Bachelor of Science degree from the University of Central Florida with a major in accounting. I am also a Certified Government Auditing Professional and a Certified Management Accountant.

Q. Please describe your current responsibilities.

A. I perform conservation, environmental, hedging, and staff-assisted rate case audits. Also, I perform various other financial audits of electric, gas, and water and wastewater utilities.

Q. Have you previously presented testimony before this Commission?

A. No.

Q. What is the purpose of your testimony today?

A. The purpose of my testimony is to sponsor the staff audit report of Progress Energy Florida, Inc. (PEF, company, or utility) which addresses the utility's August 1, 2008, through July 31, 2009, hedging activities. The audit report is filed with my testimony and is identified as Exhibit RAM-1.

Q. Was this audit prepared by you or under your direction?

A. Yes, it was prepared by me.

Q. Please describe the work performed in this audit.

A. We requested a listing of each futures, options, and swap contract executed by PEF for the 12-month period covered by the Hedging Information Report. We requested the volumes of each fuel the utility actually hedged using fixed price contract or instrument. In addition, we requested the types of hedging instruments the utility used and the average period of each hedge, options premiums, futures gains and losses and swap settlements. We tested 24 hedging transactions, choosing an array of transaction types for each hedged fuel type. We traced the transactions to the general ledger.

We reviewed the existing tolling arrangements, and tested all tolling transactions for one month by tracing the invoices to the general ledger. A tolling arrangement involves providing natural gas to generators under purchased power agreements, and receiving back the generated power for a fee.

We reviewed PEF's Hedging Information Report as filed on August 15, 2009. We examined the report for reasonableness and used it as a basis for our testing and prudency reviews. We verified that the accounting treatment from futures, options, and swap contracts between PEF and its counterparties are consistent with Order No. PSC-02-1484-

FOF-EI, in Docket No. 011605-EI, issued October 30, 2002, and as clarified by Order No. PSC-08-0316-PAA-EI. We recalculated and traced gains (losses) to the general ledger. We determined they flowed through the fuel and purchased power cost recovery clause as either a charge or a credit as required in Order No. PSC-02-1484-FOF-EI. When there was existing inventory, the inventory account was adjusted, and when there was no existing inventory, the gains (losses) flowed through the fuel expense account.

We verified that the gains (losses) associated with each financial hedging instrument that PEF implemented are consistent with Order No. PSC-02-1484-FOF-EI. Using the trade tickets, we recalculated the gains (losses) by multiplying the volume by the difference between the fixed price and the settlement price, and compared them to the recorded gains (losses) per books.

We compared the percentage limits of purchased power hedged in the Risk Management Plan with the actual volumes of hedged burns.

We reviewed the utility's written procedures for separation of duties related to hedging activities: front office, middle office, and back office. We reviewed the internal and external auditors' workpapers addressing the separation of duties.

Q. Please review the audit findings in this audit report, RAM-1, which addresses the hedging activities of PEF from August 1, 2008, through July 31,2009.

A. There are two audit findings in the audit report.

<u>Audit Finding No. 1</u>

We compared the percentage of natural gas and oil burned for the period August 1, 2008, to July 31, 2009, to the percentage range provided for in PEF's Risk Management Plan. Per the Risk Management Plan, the natural gas and No. 6 oil burn percentage ranges are 50%-80%. The hedged percentage exceeded the limits in the Plan during 2008 and 2009 for natural gas and 2008 for No. 6 oil. This was due to less natural gas and No. 6 oil usage than was originally forecast. As the generation requirements were reduced from prior forecasts, the percentage of hedged volume increased when compared to actual burns.

Per PEF's Risk Management Plan, the percentage range for No. 2 oil is at least 25%. For 2009, the actual amount burned was only 23%. As the percentage range for No. 2 oil calls for a minimum hedged volume, a slight increase in burn activity for this commodity over prior estimates leads to the decrease in hedged volume as a percentage of total burns during this period.

Audit Finding No. 2

We reviewed the utility's written procedures for separating duties relating to hedging activities: front office, middle office, and back office. We reviewed the internal auditor and external auditor workpapers. The external auditors mentioned no deficiencies in their report. However, the internal auditors reported one "Ineffective Exception" to the contracting procedures. This involved a control activity that required contract negotiations, once completed and prior to final execution, to be internally routed for appropriate approval or comments with the Contract Review Form. Two out of five contracts tested did not have appropriate approval with the Contract Review Form.

Q. Does this conclude your testimony?

A. Yes.

FLORIDA PUBLIC SERVICE COMMISSION

DIVISION OF REGULATORY COMPLIANCE
BUREAU OF AUDITING

Tampa District Office

PROGRESS ENERGY FLORIDA, INC.

2009 HEDGING ACTIVITIES

12-Month Period Ended July 31, 2009

DOCKET NO. 090001-EI
AUDIT CONTROL NO. 09-189-2-2

Ron Mavrides, Audit Manager

Joseph W. Rohrbacher, District Audit Supervisor

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DIVISION OF REGULATORY COMPLIANCE
AUDITOR'S REPORT

September 11, 2009

TO: FLORIDA PUBLIC SERVICE COMMISSION

We have performed the procedures described later in this report to meet the agreed upon objectives set forth by the Division of Economic Regulation in its audit service request dated June 23, 2009. We have applied these procedures to the Hedging Activities of Progress Energy Florida, Inc. (PEF) in Docket No. 090001-EI.

This audit is performed following general standards and field work standards found in the AICPA Statements on Standards for Attestation Engagements. This report is based on agreed upon procedures and the report is only for internal Commission use.

OBJECTIVES AND PROCEDURES

Objectives: To verify that the hedging transactions for fuel purchases from August 1, 2008 to July 31, 2009, were prudent.

Procedures: We requested a listing of each futures, options, and swap contract executed by PEF for the 12-month period covered by the Hedging Information Report. We requested the volumes of each fuel the utility actually hedged using fixed price contract or instrument. In addition, we requested the types of hedging instrument the utility used and the average period of each hedge, options premiums, futures gains and losses and swap settlements. We tested 24 hedging transactions, choosing an array of transaction types for each hedged fuel type. We traced the transactions to the general ledger.

Objectives: To determine if there are any tolling arrangements, and if there are, review them and determine if the are prudent. A tolling arrangement involves providing natural gas to generators under purchased power agreements, and receiving back the generated power for a fee.

Procedures: We reviewed the existing tolling arrangements, and tested all tolling transactions for one month by tracing the invoices to the general ledger.

Objectives: Review and verify the information presented in PEF's Hedging Information Report filed on August 15, 2009.

Procedures: We reviewed PEF's Hedging Information Report as filed on August 15, 2009. We examined the report for reasonableness and used it as a basis for our testing and prudency reviews.

Objectives: Verify that the accounting treatment from futures, options, and swap contracts between PEF and its counterparties are consistent with Order No. PSC-02-1484-FOF-EI, in Docket No. 011605-EI, issued October 30, 2002, and as clarified by Order No. PSC-08-0316-PAA-EI.

Procedures: We recalculated and traced gains (losses) to the general ledger. We determined they flowed through the fuel and purchased power cost recovery clause as either a charge or a credit as required in Order No. PSC-02-1484-FOF-EI. When there was existing inventory, the inventory account was adjusted, and when there was no existing inventory, the gains (losses) flowed through the fuel expense account.

Objectives: Verify that the gains (losses) associated with each financial hedging instrument that PEF implemented is consistent with Order No. PSC-02-1484-FOF-EI.

Procedures: Using the trade tickets, we recalculated the gains (losses) by multiplying the volume by the difference between the fixed price and the settlement price, and compared them to the recorded gains (losses) per books.

Objectives: Verify that the quantities of gas, residual oil, and purchased power hedged are within the percentage range, as represented in the utility's Risk Management Plan.

Procedures: We compared the percentage limits of purchased power hedged in the Risk Management Plan with the actual volumes of hedged burns. There were discrepancies. See Audit Finding No.1.

Objectives: Review the utility's procedures for separation of duties related to hedging activities: front office, middle office, and back office.

Procedures: We reviewed the utility's written procedures for separation of duties related to hedging activities. We reviewed the internal and external auditor's workpapers addressing the separation of duties. The external auditor made no comment on this, but the internal audit staff reported one deficiency involving the appropriate approval for the Contract Approval Forms. See Audit Finding No.2.

Objectives: Review the new transportation fuel hedging program.

Procedures: We reviewed the "PEF Fuels & Power Optimization Risk Management Guidelines". The transportation fuel has been added as an "approved product", and volumetric limits have been set.

AUDIT FINDING NO. 1

SUBJECT: PERCENTAGE RANGE OF PURCHASED FUEL HEDGED

AUDIT ANALYSIS:

We compared the percentage of Natural Gas and Oil burned for the period August 1, 2008 to July 31, 2009 to the percentage range provided for in the Risk Management Plan. The percentages burned deviated from the Plan as shown below.

	Natural Gas	**#6 Oil**	**#2 Oil**
Per Risk Management Plan	50 %-80 %	50 %-80 %	at least 25 %
Actual Amount Burned 2008	83% (Note #1)	96% (Note #1)	
Actual Amount Burned 2009	87% (Note #1)		23% (Note #2)

Note #1. The hedged percentage of natural gas and #6 oil burned exceeds the limits prescribed in the hedging plan due to less natural gas and #6 oil usage than was originally forecast. As the generation requirements have been reduced from prior forecasts, the percentage of hedged volume will increase when compared to actual burns.

Note #2. As the percentage range for #2 oil calls for a minimum hedged volume, a slight increase in burn activity for this commodity over prior estimates leads to the decrease in hedged volume as a percentage of total burns during this period.

EFFECT UPON GENERAL LEDGER IF THE FINDING IS ACCEPTED:

None

EFFECT UPON THE FILING IF THE FINDING IS ACCEPTED:

None, provided for information only.

AUDIT FINDING NO. 2

SUBJECT: SEPARATING DUTIES, HEDGING ACTIVITIES

AUDIT ANALYSIS:

We reviewed the utility's written procedures for separating duties relating to hedging activities: front office, middle office, and back office. We reviewed the internal auditor and external auditor workpapers. The external auditors mentioned no deficiencies in their report. However, the internal auditors reported one "Ineffective Exception" to the contracting procedures. This involved a control activity that required contract negotiations, once completed and prior to final execution, to be internally routed for appropriate approval or comments with the Contract Review Form. Two out of five contracts tested did not have appropriate approval with the Contract Review Form.

EFFECT UPON GENERAL LEDGER IF THE FINDING IS ACCEPTED:

None.

EFFECT UPON THE FILING IF THE FINDING IS ACCEPTED:

None, provided for information only.