ORIGINAL

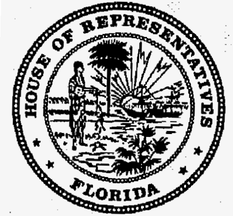
JAMES E. "JIM" KING, JR.
President

Harold McLean
Public Counsel

STATE OF FLORIDA
OFFICE OF PUBLIC COUNSEL

c/o THE FLORIDA LEGISLATURE
111 WEST MADISON ST.
ROOM 812
TALLAHASSEE, FLORIDA 32399-1400
850-488-9330

JOHNNIE BYRD
Speaker



Robert D. Vandiver
Associate Public Counsel

July 12, 2004

Ms. Blanca S. Bayó, Director
Division of the Commission Clerk
and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0870

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031033-EI

In re: Review of Tampa Electric Company's waterborne transportation contract with TECO Transport and associated benchmark

Dear Ms. Bayó:

Pursuant to Rule 28-106.307 Florida Administrative Code, enclosed are an original and twenty copies of the Joint Post Hearing Brief and Statement of Issues and Position of the Citizens of the State of Florida and Florida Industrial Power Users Group (FIPUG) in the above referred docket.

Please let me know if you have any questions. Thank you for your assistance.

Sincerely,

Robert Vandiver
Associate Public Counsel

cc: Parties of Record

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Review of Tampa Electric Company's 2004-2008 Waterborne transportation contract with TECO Transport and associated benchmark.
_______________________________________/

Docket No. 031033-EI
Filed: July 12, 2004

JOINT POST-HEARING BRIEF AND STATEMENT OF ISSUES AND POSITIONS

OF

THE CITIZENS OF THE STATE OF FLORIDA

AND THE FLORIDA INDUSTRIAL POWER USERS GROUP

Harold McLean
Public Counsel
Robert D. Vandiver
Associate Public Counsel

Office of Public Counsel
c/o the Florida Legislature
111 W. Madison Street
Room 812
Tallahassee, Florida 32399-1400
(850) 488-9330

Attorneys for the Citizens
of the State of Florida

John W. McWhirter, Jr.
McWhirter, Reeves, McGlothlin,
Davidson, Kaufman, & Arnold, P.A.
400 North Tampa Street, Suite 2450
Tampa, Florida 33602
(813) 224-0866

Vicki Gordon Kaufman
Timothy J. Perry
McWhirter, Reeves, McGlothlin,
Davidson, Kaufman, & Arnold, P.A.
117 South Gadsden Street
Tallahassee, Florida 32301
(850) 222-2525 (telephone)
(850) 222-5606 (fax)

Attorneys for the Florida Industrial
Power Users Group

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PRELIMINARY STATEMENT[1]

Pursuant to Rule 28-106.307, Florida Administrative Code, OPC and FIPUG file their Joint Post-Hearing Brief and Statement of Issues and Positions.

INTRODUCTION

The Commission must begin its analysis of the issues in this case[2] with the recognition that TECo, a monopoly provider of service to its captive customers, is required to enter into fuel arrangements, including those involving the transportation of fuel, which are prudent, cost-effective and in ratepayers' best interests.[3] The Commission may only permit recovery from ratepayers of prudently incurred costs for activities undertaken in the public service. As the evidence in this case demonstrates, TECo's contract with its sister company, TECo Transport, is antithetical to these well-established ratemaking principles.

The contract between TECo and TECo Transport, pursuant to which TECo Transport will carry TECo's coal on all three segments (river, terminal, ocean) of its journey to Tampa, contains inflated prices and terms which benefit TECo Transport, to the detriment of TECo's ratepayers. The contract is not in the public interest. Rather than trying to get the best deal it could for its *ratepayers*, TECo (with the assistance of the consultants it retained) attempted to get the most favorable rates it could for its *affiliate*, TECo Transport, with the dollars ultimately flowing to

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[1]The following abbreviations are used in this brief: the Florida Public Service Commission is referred to as the Commission. The Office of Public Counsel is called OPC. The Florida Industrial Power Users Group is called FIPUG. Tampa Electric Company is called TECo. The transcript is referred to as (Tr.) followed by the page number, and exhibits are referred to as Exhibit No. ____. Mr. Dibner's report (Exhibit No. 4) will be referenced by both original page number and Bates Stamp page number.

[2] The issues which the Commission will consider were "spun off" from the fuel adjustment proceeding. *In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.* Order No. PSC-03-1359-PCO-EI, Docket No. 030001-EI, (December 1, 2003). The Commission found that a separate docket "would allow both this Commission and the parties the opportunity to more fully evaluate the market rate analysis that Tampa Electric Company has offered to serve as the basis for the cost of waterborne coal transportation services to be charged to customer over the next five years." *Id.* at 5.

[3] Given the wide disparity between TECo's rates and that of the other utilities which this Commission regulates, further investigation of all of TECo's fuel procurement practices appears to be in order. (Exhibit No. 112).

TECO Energy, the parent company of TECo and TECo Transport.[4]

Through its contract with its sister company, TECo is attempting to overcharge ratepayers for transportation services it purchases from a related company. While TECo is not prohibited from entering into contracts with an affiliated company, it is not the ratepayers' role to fund such sweetheart transactions. All costs above those that are reasonable and prudent must be disallowed. The evidence in this case demonstrates, as will be discussed in detail below, that the amounts TECo seeks to recover are excessive and inure to the benefit of its parent company.

SUMMARY OF ARGUMENT

TECo's Request for Proposals (RFP) was not a serious attempt to solicit commercial bids but rather an instrument constructed to reach the preordained conclusion that TECo Transport would be the presumptive provider of transportation for all three legs of the transportation service. The right of first refusal, the short response time, the integration preference, the lack of dialogue with bidders, and the failure to take even the limited bids received back to TECo Transport to meet or beat demonstrate that TECo was not serious about the RFP process. The market reacted accordingly, as evidenced by articles written during the bidding process, (Exhibit No. 10), letters in response to the RFP itself (Exhibit No. 11), and, perhaps most telling, the almost total lack of bid responses (1 disqualified partial bid on the river, 1 terminal bid, 0 ocean bids). The Commission will never know if a properly constructed, unbiased RFP would have sparked interest from the marketplace because TECo tainted the process.

TECo then hired a consultant, Mr. Dibner, to produce a model (Exhibit No. 4) that was necessary because of the dismal failure of the RFP. The model, has never been used in a regulatory proceeding and suffers from two real world, fatal flaws – it fails to account for backhaul traffic and it adds a premium for preference trades. Neither of these items is reflective

[4] The dire financial circumstances of TECo Energy are a matter of public record.

of a competitive market. When compared to other TECo Transport rates, such as those JEA paid to TECo Transport, it becomes obvious that Mr. Dibner's model rates are excessive. In the case of JEA, Mr. Dibner's rates are more than that charged by TECo Transport to move coal twice the distance!

The sixteen-year old benchmark methodology is based on publicly available coal rail rates. Most coal in this country does not move under publicly tariffed rail rates but under confidential contract rates. In comparison to actual rail rates TECo paid in 2000, the benchmark is almost $10 higher per ton resulting in a $50 million[5] dollar difference between what the benchmark would permit and actual rail rates.[6] Thus, the benchmark has outlived its usefulness and should be eliminated.

ARGUMENT

LEGAL PRINCIPLES APPLICABLE TO THE COMMISSION'S DECISION

A. The Burden of Proof

The burden of proof in this case rests squarely with TECo. The rule that the burden of proof is on the utility in proceedings involving rates is so well recognized that this Commission has labeled it "universally established."[7] In an investigation into the shut down of Crystal River Unit No. 3, the utility attempted to argue that intervenors had advocated a "refund of rates" and thus the propriety of the utility's collections were to be presumed. The Commission quickly put that novel idea to rest:

> The rule that, in proceedings involving rates requested by a utility company, the burden of proof is upon the applicant utility, has been universally established.

[5] The $50 million figure is the product of multiplying $10 times TECo's full requirement of 5 million tons of coal per year. It is not based on the tons of coal TECo received by rail at the Gannon facility, which was much less than its full requirement. See discussion *infra* at 32-34.
[6] These rates were confidential in 2002, but have since been declassified.
[7] *In re: Investigation into forced shutdown of Florida Power Corporation's Crystal River No. 3 unit,* Order No. 8994 at 2, Docket No. 780732-EU, August 3, 1979.

Mississippi Public Service Commission v. Mississippi Power Company, 337 So.2d 936 (Miss. S. Ct., 1976); Pennsylvania v. Laurel Pipeline Company, 19 PUR 4th 454 (Penn. Commonwealth Court, 1977); Re: Hawaiian Electric Company, Inc., 10 PUR 4th 1, 535 P2d 1102 (Hawaii S. Ct., 1975); North Carolina ex rel. Utilities Commission et al. v. Duke Power Company, 206 SE 2d 269, 6 PUR 4th 390 (N.C. St. Ct., 1974). In such proceedings, the burden is upon the utility to demonstrate the reasonableness of the operating expenses for which it should be compensated to enable it to realize a fair rate of return. This docket involves a single aspect or element of the utility's operating expenses, i.e. its fuel expenses, which are the subject of an ongoing review. Each month, regulated electric utilities apply for approval of the fuel expenses incurred by them to generate electricity. As in ratemaking proceedings generally, the burden of proof lies with the petitioning utilities to demonstrate the reasonableness and propriety of the expenses incurred.[8]

It is TECo that seeks permission from this Commission to recover through the fuel adjustment clause, on a dollar for dollar basis, the amounts it proposes to pay to its affiliated company. As in any case where a utility wants to impose charges upon its customers, TECo has the burden to prove that the costs it seeks are fair, just and reasonable. As this Commission has noted, the nature of the fuel adjustment is "continuous."[9] It has further held that:

> The burden of proof rests *solely* with the utility to document the reasonableness of its procurement practices and the resultant expenses from such practices.[10]

In addition, in its order on utility fuel procurement practices, Order No. 12645, discussed below, the Commission emphasized that the utility has the burden of proof:

> Any fuel or fuel related transaction which does not meet the above criteria *shall be denied recovery* through the fuel clause by the Commission, *unless the utility, which has the full burden of proof*, can demonstrate that the transaction is in the best interest of the ratepayer.[11]

---

[8] *Id.*

[9] *In re: Investigation of Fuel Adjustment Clauses of Electric Utilities,* Order No. 12645 at 11, Docket No. 830002-EU, November 3, 1983.

[10] *Id.* at 12, emphasis added. *See also, In re: Investigation of forced shutdown of Crystal River No. 3,* Order 9775 at 4, Docket No. 780732-EU, January 30, 1981 ("the burden is upon the company to demonstrate that the fuel expenses which it proposes to recover from ratepayers were reasonably and prudently incurred."); *In re: Investigation into extended outage at Florida Power and Light Company's St. Lucie Unit No. 1,* Order No. 15486 at 21, Docket No. 840001-EI-A, December 23, 1985 ("[U]tilities bear the burden of demonstrating that their fuel costs are reasonable and prudent.").

[11] *Id.* at 14, emphasis added.

No such demonstration has been made in this case.

B. The Commission's Ratemaking Obligations

TECo argues that the Commission has no choice but to approve the costs of the five-year contract between TECo and TECo Transport for full cost recovery from ratepayers due to Order No. 20298.[12] Order No. 20298 moved TECo's waterborne coal transportation from a "cost plus" method of regulation to a "market-based standard." The Order indicates that a "market pricing system" is the preferable mode of regulation and utilizes published rail rates to gauge the reasonableness of waterborne transportation costs. TECo says that because its new contract rates are below the rail benchmark established in this 1988 Order, the Commission must permit TECo to recover from ratepayers the rates contained in its new contract with its sister company.

Through this argument, TECo attempts to turn the Commission's ratemaking obligations – to ensure that ratepayers pay fair and reasonable rates – on its head. The Commission must reject any assertion that Order No. 20298 requires it to pass through patently imprudent rates. Order No. 20298 cannot, and does not, provide TECo with "rubber stamp" approval of its rates simply because those rates fall below the benchmark. Relegating the Commission's role to that of ministerial approval would result in an unlawful abrogation of the Commission's statutory duties,[13] which serve to protect the ratepayers.[14] A brief review of this Commission's orders

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[12] As a preliminary matter, it should be noted that TECo has been on notice since 2002 that the Commission was reviewing the validity of the waterborne benchmark. In Order No. PSC-02-1591-PHO-EI at 46, the Commission stated that as part of its continuing fuel and purchased power cost recovery proceedings, it would review the validity and reasonableness of the current waterborne coal transportation benchmark for transportation services TECo purchased from its affiliated company. Thus, TECo's lack of notice argument is without merit. It entered into the contract with its sister company at its own risk.

[13] A simple example illustrates the absurdity of TECo's position. What if TECo had sought approval of a contract with its sister company with a 50-year term rather than a 5-year term? If the contract rates were below the benchmark, would Order No. 20298 entitle TECo to maintain the contract and receive full cost recovery for the full 50 years, even if more cost-effective alternatives were available? Of course not; the Commission must establish rates that are fair, just and reasonable.

[14] *See*, *i.e.*, § 366.01, where the Florida Legislature declares the regulation of public utilities to be in the public interest and to be an exercise of the police power of the state for the protection of the public welfare; § 366.04(1),

demonstrates that the fuel adjustment proceeding is on going and shows TECo's argument is without merit.

In Order No. PSC-92-1048-FOF-EI,[15] this Commission clearly articulated its ability to ensure just and reasonable rates. In that case, ironically, TECo sought to change the benchmark. The Commission denied TECo's request and noted that it had an obligation to change rates when the rates were not fair, just and reasonable:[16]

> That is not to say that we could not modify the manner in which the benchmark is calculated if circumstances warranted such a modification. We are not precluded by any legal doctrine from considering Tampa Electric's petition, from reviewing the correctness and effectiveness of its market-based pricing method, or from modifying that method if we determine that it is in the public interest to do so. To the contrary, we are required to review and modify our rate decisions, on a prospective basis, by virtue of our continuing duty to regulate the rates and service of electric utilities. If we determine that the rates charged by a utility are not fair, just and reasonable, either to the company or to its ratepayers, we have the obligation to fix them. This continuing obligation applies to rates for fuel cost recovery as well as to other forms of rates. . . .
>
> Ratemaking is an ongoing, legislative function intended to be responsive to changing economic conditions. As the First District Court of Appeal recently stated in its order affirming the Commission's authority to correct, on a going forward basis, "an incorrect assumption" in a five-year-old rate order that had operated to the detriment of the utility's ratepayers:
>
>> Peoples Gas Systems, Inc. v. Mason, 187 So.2d 335, 339 (Fla. 1966), and Austin Tupler Trucking, Inc. v. Hawkins, 377 So.2d 679 (Fla. 1979), recognize an exception to the doctrine of administrative finality where there is a demonstrated public interest. Unlike the issues raised in those cases (authority to approve territorial agreements and the dormancy of transportation certificate), the issue of prospective rate-making is never truly capable of finality.
>> Sunshine Utilities v. Florida Public Service Commission, 577 So.2d 663 (Fla. 1st DCA 1991).

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which provides that the Commission shall have jurisdiction to "regulate and supervise each public utility with respect to its rates...."; § 366.05(1) which provides that, in the exercise of its jurisdiction, the Commission will prescribe fair and reasonable rates and charges for each public utility; and §§ 366.041(1), 366.06(1) which require the Commission to set just and reasonable rates.

[15] *In re: Petition for Clarification a [sic] Guidance on Appropriate Market Based Pricing Methodology for Coal Purchased from Gatliff Coal Company by Tampa Electric Company*, Docket No. 920041-EI, Sept. 23, 1992.

[16] TECo acknowledges that the Commission may only permit it to recover costs which are prudent and reasonable. (Tr. 500, 502).

See also Reedy Creek Utilities v. Florida Public Service Commission, 418 So.2d 249 (Fla. 1982), and Richter v. Florida Power Corporation, 366 So.2d 798 (Fla. 2d DCA 1979).

> We cannot modify our prior rate orders capriciously, without sufficient demonstration that the public interest requires the modification; but where the demonstration has been adequately made, we not only have the authority to make the appropriate modifications, we have the obligation to make them.[17]

In regard to the importance of its responsibility to ensure appropriate fuel adjustment charges, the Commission has also said:

> Because of the relative importance and impact of fuel costs upon the ratepayers, it is incumbent that electric utilities exercise all reasonable means to purchase the lowest costing fuel possible. Any deviation from this policy results in excessive monthly fuel adjustment charges, the majority of which are passed on to the ratepayers through the application of the fuel cost recovery clause. Where excessive charges for fuel are paid by a utility, *we find it to be our responsibility to correct such overcharges and take whatever measures are necessary in order to rectify that situation.*[18]

Substantial competent evidence in this case demonstrates that the benchmark mechanism of Order No. 20298 would cause ratepayers to pay more than the reasonable and prudent cost of fuel transportation. As this Commission has recognized and articulated, it has not only a duty, but an obligation to adjust rates when they are not fair, just and reasonable.

Also critical to the Commission's decision in this case is Order No. 12645. In Order No. 12645, the Commission discussed at length the fuel procurement policies regulated utilities must follow. Order No. 12645 includes Appendix A, entitled "Florida Public Service Commission Fuel Procurement Policy."[19] Many of these articulated policies are directly applicable to the Commission's decision in this case.

For example, Policy IA states:

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[17] Order No. PSC-92-1048-PCO-EI at 11-12, emphasis in original.

[18] *In re: General investigation and show cause order as to alleged overcharges paid by Florida Power Corporation for spot purchases of fuel oil*, Order No. 8205 at 1-2, Docket No. 770671-CI, March 1, 1978 (emphasis supplied).

[19] The fuel procurement policy was attached as an Exhibit No. 14 to Mr. Majoros' testimony.

> The Public Service Commission requires that all expense associated with the procurement of fuel, fuel related handling services and *fuel transportation* which are recovered through the fuel adjustment clause *be prudently incurred*, *result from competitive procurement procedures*, *be reasonably competitive in cost or value* relative to what other buyers are paying under similar terms and conditions for fuel or services for comparable quality or specifications and result from sound administration of fuel supply agreements.[20]

Section II of the Commission's Policy Statement is entitled "Long-Term Agreements for Fuel, Fuel Handling Services, Fuel Transportation, Spot Purchase and Affiliate Transaction. Thus, it is particularly applicable to issues before the Commission. Policy IIB states:

> The Commission recommends that, to the extent practicable, such long-term contracts be negotiated in a *competitive* environment. It is recommended that the primary method employed should be an *open competitive bidding process* or some comparable alternative which produces the same result.[21]

Policy IID provides:

> Vendors should be selected on the basis of a *formal evaluation system* which is *neutral in its application* and capable of producing quantifiable ratings of individual suppliers. Considerations other than delivered price, fuel quality and vendor performance should be *thoroughly documented*.[22]

As to transactions with affiliates, Policy IIP provides:

> All utility transaction[s] with affiliated companies which provide fuel or fuel related services should be based on costs which are *consistent with or lower than* the costs a utility would incur if the utility received the fuel or services form an independent supplier in the *competitive market obtained through competitive bidding*.[23]

TECo's actions in this case flout the requirements of the Commission's policies set forth above.

Finally, in *GTE Florida, Inc. v. Deason,*[24] the Court reversed the Commission's decision to reduce costs arising from a transaction between GTE and its affiliates. The Court articulated the rule applicable to affiliate transactions: "We believe the standard must be whether the

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[20] Order No. 12645 at 12, emphasis added.
[21] *Id.* at 13, emphasis added.
[22] *Id.*, emphasis added.
[23] *Id.* at 14, emphasis added.
[24] 642 So.2d 545 (Fla. 1994).

transactions exceed the going market rate or are otherwise inherently unfair."[25] The TECo Transport rates here fail both the market rate test and the inherent unfairness test. TECo Transport's rates are not "market" rates because, as witness Majoros explained, in a competitive market, these inflated rates would not be paid. (Tr. 808–810, 815). And it is inherently unfair to assign the total cost of this movement to the ratepayers when the Commission knows that over 4.5 million tons of backhaul cargo are going back across the Gulf of Mexico and TECo Transport is pocketing this revenue. (Tr. 165). The evidence also reflects that significant tonnage is moving upriver. (Tr. 194, 808). To totally ignore this tonnage, as TECo urges, is inherently unfair.

The term "market," both as used in Order No. 20298 and in the *GTE* decision, means a *competitive* market. The *GTE* Court said as much: "the evidence indicates that GTE's costs were no greater than they would have been had GTE purchased supplies and services elsewhere."[26] Order No. 20298 also expressly speaks of *competitive* markets.[27]

Further, in Order No. 14782, the Commission recognized that net profits from backhaul of phosphate should be credited to the ratepayers.[28] Although this order was issued during the "cost-plus" regime, the reasoning the Commission used applies equally in a "market" context.[29] The Commission reasoned in Order No. 14782 that when a barge dedicated for utility use earns a profit carrying non-utility business, the ratepayers must be credited those profits to offset the cost of coal transportation. That case is factually indistinguishable from the instant case. The Commission should employ the same logic and credit ratepayers for the backhaul.

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[25] *Id.* at 547.
[26] 642 So. 2d at 547.
[27] Order No. 20298 at 12.
[28] *In re: Investigation of fuel adjustment clauses of electric utilities – Florida Power Corporation/Electric Fuels Corporation waterborne transportation charges*, Order No. 14782 at 6, Docket No. 850001-EI-A, August 28, 1985.
[29] *Id.* at 2-4.

TECo also claims that CSXT's bid demonstrates that a "market" for coal transportation exists between the mine and the generating plant. (Tr. 17-18). Yet TECo rejected CSXT's bids as not bona fide and "unreasonable, incomplete and unfeasible." (Tr. 418; 430). TECo cannot have it both ways: either CSXT is a viable bidder that must be considered or it is not. Given the duplicity of TECo's positions with respect to CSXT's bid, any reliance by TECo on the rail bid as evidence of a "market" must be ignored.

C. The Commission's Authority to Take Action in This Case

Commissioner Jaber asked several questions at hearing regarding the Commission's authority to take action in this case. (Tr. 1124-1125). For the reasons set forth above, the Commission has not only the authority, but the obligation, to assess only fair, just and reasonable rates. Thus, it has ample authority to make appropriate adjustments to the transportation services rates TECo seeks and to disallow imprudent costs. Further, given the extreme disregard TECo has shown for the appropriate practices and procedures to follow in devising and issuing an RFP that would fully test the market, this Commission also has authority to prescribe what actions TECo must take on a going-forward basis pursuant to its authority under § 366.07, Florida Statutes.

Section 366.07 provides:

> Whenever the commission, after public hearing either upon its own motion or upon complaint, shall find the rates, rentals, charges or classifications, or any of them, proposed, demanded, observed, charged or collected by any public utility for any service, or in connection therewith, or the rules, regulations, measurements, practices or contracts, or any of them, relating thereto, are unjust, unreasonable, insufficient, excessive, or unjustly discriminatory or preferential, or in anywise in violation of law, or any service is inadequate or cannot be obtained, the *commission shall determine and by order fix* the fair and reasonable rates, rentals, charges or classifications, and *reasonable rules, regulations, measurements, practices, contracts or service, to be imposed, observed, furnished or followed in the future.*[30]

[30] Emphasis added.

Section 366.07 not only sets forth the Commission's obligation to fix fair and reasonable rates for TECo's ratepayers, but also gives the Commission the power to require TECo to follow certain procedures on a going-forward basis.

Thus, the Commission should require TECo, in any subsequent RFP, to take, at a minimum, the following action:

> Prohibit an integration preference;

> Make it clear that bids for a portion of the movement will be accepted and considered on the same basis as full requirements bids;

> Eliminate any right of first refusal for TECo's sister company;

> Provide the RFP to Commission Staff and interested parties, at least six (6) weeks prior to its release for comment and clarification to ensure that the invitation to bid is not a closed process;

> Allow a minimum 8-week response time from the marketplace;

> Conduct a pre-bid meeting;

> Indicate in the RFP the scoring and evaluation methodology to be employed;

> Require any affiliate company to submit its bid on the same terms and conditions and at the same time as non-affiliate bidders;

> Provide the RFP to all potential bidders; do not eliminate one type of bidder (such as the rail) because the RFP document is limited to waterborne transportation.

ISSUE 1

IS TAMPA ELECTRIC'S JUNE 27, 2003, REQUEST FOR PROPOSALS SUFFICIENT TO DETERMINE THE CURRENT MARKET PRICE FOR COAL TRANSPORTATION?

OPC/FIPUG Position:* No. The RFP was flawed in numerous respects, as was the evaluation of the few bids received. The RFP cannot be used to determine the current market price for coal transportation.*

TECo's Request for Proposals (RFP) for transportation services was flawed and

discouraged bidding by non-affiliated providers. This is evidenced by the fact that despite the number of potential providers to whom the RFP was sent,[31] TECo received **one** bid on the river section[32] (which it rejected), **one** bid on the terminal portion (which it accepted without any price negotiation), and **no** bids on the ocean leg. (Tr. 80-81).[33] TECo did not provide the RFP to CSXT at all (Tr. 863); when CSXT requested the RFP, TECo reluctantly provided it and then rejected CSXT's bids out of hand.[34] Mr. Wells, former President and CEO of Electric Fuels Corporation (EFC), testified: "[A] successful RFP gets bids. If they don't get bids, it is not successful." (Tr. 872). For an RFP to be fair and provide an appropriate response from the marketplace, the bid process must encourage full participation. TECo's RFP contained provisions which discouraged independent bidders from submitting a proposal. (Tr. 862-864).

As a preliminary matter, the prior contract with TECo Transport contained a "right of first refusal." (Tr. 375-376). This allowed TECo Transport to "meet or beat" any offers which TECo got in response to the RFP.[35] TECo Transport was not subject to requirements of the competitive bidding process, but instead had the extraordinary advantage of being able to sit back and wait to see what others might do. (Tr. 866). TECo's own witness, Mr. Murrell, testified that the right of first refusal conveyed an inherent advantage to TECo Transport:

> Q. Would you agree that the right of first refusal conveys an advantage to TECO Transport in competing for this business?

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[31] TECo touts the number of providers to whom the RFP was sent (Tr. 1379); however, the proof of a successful RFP is not related to the number of potential bidders who **received** the bid package, but the number of providers who **responded** to the RFP.

[32] Mr. Dibner's characterization of responses to the river portion of the RFP as "disappointing" (Tr. 266-267) is understatement at its best.

[33] Despite the scarcity of bids, TECo made *no* effort to determine why more providers did not submit proposals. (Tr. 865).

[34] This behavior should be contrasted with a provider who is actually interested in soliciting competitive bids. Such a provider would have contacted CSXT to see if an optimal price for ratepayers was possible. (Tr. 877; 956). It appears TECo went out of its way to disqualify CSXT. (See, e.g., Tr. 1034; 1173).

[35] Ms. Wehle could think of no instance in which a company with a right of first refusal actually made a better offer (that is, beat) the offer presented to it. (Tr. 504). And what incentive would any company have to offer a lower price than what the other party was willing to accept?

A. I would, yes. I think there is an inherent advantage there. I agree with that.

(Tr. 1419-1420). TECo did not even require TECo Transport to negotiate the price of the deal. (Tr. 482).

TECo attempts to justify the right of first refusal as a way to encourage a supplier of long standing that has invested significant capital to invest more capital, whether "affiliated or not." (Tr. 410). But TECo's own actions in dealing with suppliers shows this is not the case. While affiliate TECo Transport enjoys the advantage of the right of first refusal, (Tr. 410), unaffiliated companies do not fare as well. For example, CTL Trucking (CTL) has been a TECo transportation partner since 1995 or 1996, trucking coal from TECo's Big Bend plant to the Polk facility. (Tr. 473). To do so, CTL has invested in specialized equipment to make the haul, consisting of approximately ten trucks. (Tr. 473-474). TECo recently renewed its contract with CTL but did not include a right of first refusal. (Tr. 474). TECo attempts to justify its right of first refusal with TECo Transport as a reward for TECo Transport's capital investment; however, CTL was not commensurately "rewarded" for its capital investment. (Tr. 410). TECo apparently has one set of standards for affiliates and another for non-affiliates. Put differently, TECo Transport gains significant advantages from its affiliate relationship with TECo, which work to the ratepayers' detriment.

In addition, since the inception of the TECo transportation system, the contract has *always* been awarded to TECo's sister company, TECo Transport. (Tr. 268). Mr. Dibner admitted that more vendors would respond to a TECo RFP if they thought they actually had a chance to win the business. (Tr. 269). Mr. Dibner further admitted that without the restrictive provisions included in the RFP, it is likely that more bids would have been received. (Tr. 270).

From the outset, the RFP document was problematic. Prior to the issuance of the RFP,

Staff requested a meeting with TECo to discuss the RFP's terms. TECo ignored this request and issued the RFP before meeting with Staff. (Exhibit No. 9).

Staff subsequently held a meeting with TECo on July 1, 2003, after the RFP was issued. At the meeting, Staff made a number of suggestions regarding ways the RFP could be improved and subsequently provided suggestions in written form to TECo. Staff noted that:

> . . .In staff's opinion, such [clarifying] statements are necessary to clarify certain ambiguous aspects of the RFP which may otherwise limit the number and type of bids that Tampa Electric receives in response to the RFP as issued. . . . Staff believes it would be prudent for the utility to [issue these clarifications] in order for staff's concern to be adequately addressed.[36]

TECo refused to make any of the changes Staff suggested to improve the RFP. TECo responded to Staff's letter by stating:

> . . . Tampa Electric reaffirms its belief that the RFP the company has issued is fully descriptive of Tampa Electric's waterborne coal transportation needs, particularly for those who compete in the waterborne transportation industry. Based on its own knowledge and experience and the advice of its expert consultant, Tampa Electric is confident that its RFP will generate a *significant interest and consideration from potential transportation providers*, and the resulting proposals will be afforded careful consideration as it state in the RFP.
>
> . . . The company believes that, as this process is concluded, the Staff and the Commission will be satisfied that the company's RFP was, in fact, *informative and productive.*[37]

TECo's prediction of *significant* interest and a *productive* process turned out to be hollow.

The marketplace was well aware that the transportation business would go to TECo's sister company. The market's disinclination to waste time responding to an RFP whose outcome was preordained is illustrated by information appearing on a well-known industry website, Platts. Shortly after the RFP was issued, this item appeared:

> Tampa Electric is taking bids to transport solid fuels – including coal, coal-based synfuel and petroleum coke – to the Big Bend station, but some in the industry are

[36] Exhibit No. 9.
[37] Exhibit No. 7, Bates Stamp No. 75, emphasis supplied.

skeptical about the offer. Bids are due Aug.1, and the utility expects to award a five-year contract, beginning in 2004 and running through 2008. TECO is seeking bids to move the fuels from midwestern supply sources convenient to the Mississippi and Ohio river systems. Minimum annual tonnage requirements for 2004-2006 range from 3.25 million tons on the inland river system to 4 million tons on the Gulf.

. . . Industry sources, however, downplayed the solicitation as *"an exercise in futility." "We went through this same process six years ago," said on industry executive. "They'll take bids and then award the contract to their sister company, TECO Transport.* It's all a game to keep the Public Service Commission happy." TECO solicited in 1997 for a five-year contract and awarded it to TECO Transport.[38]

One of the largest and most reliable river barge companies, (Tr. 864), expressed similar concerns in a letter to TECo in which it explained why it did not bid:

After serious consideration, [name of company deleted as confidential] has elected not to provide rates in response to your Request for Waterborne Transportation Services Proposals WB-2004.

I can assure you that if TECo had proceeded to divest itself of the barge line, our response would be different. However, our impression from bidding on this business in the past is that our response, along with others', does nothing more than establish the rate structure at which *your in-house carrier will continue to move your tonnage.*[39]

These exhibits indicate exactly what the RFP itself, with its restrictive conditions, clearly conveyed to the marketplace: don't bother to bid, TECo Transport is getting the business. What is amazing is that the RFP garnered even the limited, anemic response it did. There was no surprise in the marketplace when this contract was awarded to TECo Transport.

TECo's witness, Ms. Wehle, testified that the RFP was "an information gathering tool that provides market price data." (Tr. 674). It is hard to envision many companies expending time on a proposal in light of the statement that their proposals would be used to gather market data rather than to award the business.

[38] Exhibit No. 10, emphasis added.
[39] Exhibit No. 11, emphasis added.

The RFP states: "Tampa Electric prefers proposals for integrated waterborne transportation services. . . ." (Exhibit No. 111). Thus, TECo sought one provider for all its transportation services. (Tr. 370-371). Mr. Murrell testified that TECo Transport was the *only* carrier that could fulfill this "preference." (Tr. 1418). TECo notes that while it "preferred" an integrated system, it was willing to consider other proposals. (Tr. 370; 510). However, the RFP gives no clue as to how TECo's integration preference would be scored (Tr. 510), so bidders had no idea what value to place on TECo's "preference." The necessity for an "integration preference" is belied by the fact that Florida Progress receives coal by water via a system very similar to that TECo uses. (Tr. 1365), but does not have an "integrated" delivery system. (Tr. 1413).

The "integration" requirement inappropriately tilts the playing field excessively toward a large integrated company, like TECo Transport, which provides all three legs of the service (river, terminal and Gulf). (Tr. 863). Smaller, more efficient players on one leg or another may decide not to bid due to this integration preference, especially when they do not know how much weight this "preference" will receive in the bid evaluation. (Tr. 863).

Ms. Wehle testified that if the TECo waterborne transportation system was not integrated, it would be more expensive for ratepayers. (Tr. 511). However, Ms. Wehle's testimony does not quantify this additional expense in any way.[40] This "preference" was yet another signal to potential bidders that this contract was destined for TECo Transport.

The five-week time frame to submit a bid was unnecessarily truncated. (Tr. 863; Exhibit No. 10). This truncated time frame suggests TECo really was not serious about getting bids. TECo was well aware of when the contract would expire, yet provides no reason for this very

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[40] While Ms. Wehle touted the "administrative efficiencies" of integration (Tr. 370), she failed to analyze the value of such efficiencies (such as perhaps the salary of an extra clerk) versus the savings for ratepayers in transportation costs.

truncated response time. (Tr. 863). This is especially the case if TECo really expected multiple carriers to get together and submit one "integrated" bid.

Mr. Wells testified that eight weeks was the minimum time for an RFP of this complexity. (Tr. 863). The movement of coal at issue here is the largest in the country involving an ocean leg. (Tr. 151). It is comparable to the Florida Progress movement, although the Florida Progress move is differentiated by the tonnage received and the size of its port. (Tr. 1365-1366; 1405). Mr. James Heller, a nationally recognized expert on transportation matters, filed testimony in the Florida Progress waterborne transportation docket.[41] In Mr. Heller's opinion, a minimum of eight weeks would be necessary for the cross-Gulf RFP given the magnitude and complexity of the move. (Tr. 1407).

TECo's time frame for completion of the competitive bid process was also unreasonable. Although TECo witnesses testified that the six-month time frame for the bid process was reasonable, (Tr. 1368-1369), the actual time frame was much shorter. For TECo to seek cost recovery during 2004 for the new contract, it had to file testimony prior to the November 2004 fuel hearing. Therefore, the actual amount of time TECo allowed for the procurement process was three months – the time between when it issued its RFP (June 27, 2003) and when the fuel testimony was filed (September 2003). (Tr. 514-515). Three months is insufficient to complete the procurement process.

Finally, TECo did not establish any dialogue with prospective bidders. As Mr. Wells testified, much can be learned through discussions with the bidders. (Tr. 865). Mr. Wells, who has many years of experience as CEO and President of Electric Fuels Corporation, explained:

> [Dialogue with bidders provides] the opportunity for more improvement in bids, not just price, but in operational procedures, and many other factors of importance

[41] *In re: Review of Progress Energy Florida, Inc.'s benchmark for Waterborne Transportation Transaction with Progress Fuels*, Docket No. 031057-EI.

> in such a contract. To me, not meeting with the bidders is a huge indicator of TECo's lack of "seriousness" about awarding this business to anyone but its affiliate.

(Tr. 865). TECo even *refused* to meet with the barge company whose bid it rejected. (Tr. 865).

In addition, a meeting with the bidders is helpful in "selling" the RFP to potential bidders, thereby soliciting more bids. "Selling" the RFP is particularly important if one supplier has been providing the service for a long period of time or if there is a perception in the marketplace that the business cannot be obtained through the RFP[42] – both conditions were present with TECo's RFP. (Tr. 872-873). If TECo's intent was truly to gauge the market, why not engage the very participants one seeks to deal with? Again, this indicates TECo was not serious about awarding the contract to anyone but TECo Transport.

The actions TECo took in regard to the terms and conditions of the RFP, the truncated response time, the lack of any scoring or evaluation mechanism, its failure to engage in any dialogue with prospective bidders, and its failure to document in any way "non-price" considerations demonstrate that TECo did not comply with even the minimum requirements of this Commission's fuel procurement policies. Thus, the Commission must find that the RFP has no bearing on its determination of a competitive price for coal transportation.

ISSUE 2

ARE TAMPA ELECTRIC'S PROJECTED COAL TRANSPORTATION COSTS FOR 2004 THROUGH 2008 UNDER THE WINNING BID TO ITS JUNE 27, 2003, REQUEST FOR PROPOSALS FOR COAL TRANSPORTATION REASONABLE FOR COST RECOVERY PURPOSES?

<u>OPC/FIPUG Position</u>: *No. The rates TECo seeks to collect from ratepayers do not reflect competitive market rates; they are thus excessive and inflated. The Commission should make Mr. Majoros' recommended adjustments, which will result in a competitive rate.*

[42] Exhibit Nos. 10 and 11 confirm the industry-wide perception. (Tr. 881).

The transportation of coal to Big Bend can be divided into three segments: the river leg, the terminal piece, and the ocean or Gulf leg. (Tr. 150-151). On the river leg, coal comes out of the mine[43] and is trucked or put on rail cars to take to a river dock for loading onto river barges. (Tr. 69). The barges are towed by tugboat to the terminal facility at the mouth of the Mississippi River for transloading, storage or blending. (Tr. 151). Finally, the coal is shipped across the Gulf of Mexico to the Big Bend facility. (Tr. 72).

Due to the paucity of bids received pursuant to the RFP, TECo had to "construct" market prices. TECo claims to have done this through Mr. Dibner's prices (Exhibit No. 4) that were presented to TECo Transport to "meet or beat." Despite the fact that TECo has a fiduciary duty to its ratepayers, it reviewed Mr. Dibner's report only for "mathematical accuracy"; it did not evaluate his assumptions. (Tr. 656-657).

Mr. Dibner's prices are not reflective of a competitive market; they do not represent prices that non-affiliated competitors would have offered to TECo in the real world. Mr. Dibner's prices (now embodied in the TECo Transport contract) are excessive in two principal areas – failure to recognize backhaul and the preference trade adder[44] – especially when compared to other movements. Further, the terminal rate is unfair and must be adjusted.

A. Fairness and Consideration of a Competitive Market Require an Adjustment to Reflect Backhaul

In 2002, TECo carried <u>4,652,335 tons</u>[45] of backhaul across the Gulf on the <u>same</u> TECo Transport ships that carried coal to Tampa. (Tr. 165). Despite this undisputed fact, TECo, through Mr. Dibner, avers that ratepayers should be obligated to pay the <u>entire cost of the round</u>

[43] TECo purchases its coal from suppliers in the Midwest. (Tr. 69-72).

[44] Mr. Majoros' discussion of only these two adjustments does not represent his endorsement of the Dibner model. (Tr. 811). There may well be other necessary adjustments, as to the cost of capital. (See, Exhibit Nos. 72-74). However, Mr. Majoros' adjustments are so significant as to cast grave doubt on the efficacy of the entire model. (Tr. 811).

trip from mine to plant without any credit for these millions of tons of backhaul.[46] These revenues flow straight to the bottom line of TECo Transport and then to TECO Energy stockholders, courtesy of captive ratepayers. (Tr. 168).

Mr. Dibner unabashedly admits that he ignored backhaul in the prices resulting from his model. (Tr. 165-167). Mr. Dibner opined that: "[a] consideration of backhaul is not for outside conjecture, interference, confiscation or reallocation in setting market rates." (Tr. 110). Mr. Dibner could not be more wrong.

First, this Commission's ratemaking authority is clearly implicated in this transaction. Ratepayers have paid the cost of this entire trip. Under this approach, backhaul revenues are credited to a non-regulated entity, TECo Transport, at the captive customers' expense.

Second, the notion that consideration of backhaul would amount to "confiscation" or "interference" is ludicrous on its face. In *Bluefield Waterworks and Improvement v. Public Service Commission of W. Va.,*[47] the United States Supreme Court discussed confiscatory rates. The Court found that fair rates must be paid for assets "being used for the public."[48] There can be no claim that on the backhaul,[49] the TECo Transport ships are being used for the benefit of the public. It would be confiscatory from the ratepayers' perspective if the Commission did not take backhaul into consideration. This Commission has the authority to consider the amount of backhaul to reflect a fair cost of transporting this tonnage.

Backhaul is critical to the analysis of this case because, as Mr. Majoros explained, in a competitive market, backhaul restricts the ability to assign 100% of the costs to the originating

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[45] The Port of Tampa data and the amount of backhaul reflected therein is undisputed. (Tr. 164).
[46] Mr. Dibner actually claims there is no marginal backhaul. (Exhibit No. 64).
[47] 262 U.S. 679 (U.S. 1923).
[48] *Id.* at 690.
[49] It is also interesting to note that backhaul is often in the eye of the beholder. On many voyages, the tonnage on the return trip is greater than on the trip transporting the coal. (See, Exhibit No. 18).

movement. (Tr. 809). Even Mr. Dibner conceded that with competition one might have to take backhaul into account. (Tr. 217). That is the point. TECo Transport, because it was successful in eliminating competition, blithely ignored the backhaul.[50]

The backhaul has two parts – the ocean backhaul and the river backhaul. Mr. Majoros calculated the ocean backhaul adjustment using the uncontroverted Port of Tampa data.[51] (Tr. 203; Exhibit Nos. 15, 18). Mr. Majoros determined, by vessel, the actual percentage of roundtrips from Louisiana to Tampa and back on which TECo Transport carried backhaul cargo. Mr. Dibner's ocean model calculations were adjusted to account for the backhaul percentage. (Tr. 811-812).

The river backhaul component must also be considered. TECo Transport's website touts its success in northbound shipping while TECO Energy's 2002 10K Report notes that TECo Transport is expected to move increased volumes of fertilizers and petroleum coke northbound on the river system. (Tr. 808).

To conservatively estimate the appropriate adjustment for the river backhaul, Mr. Majoros used a figure of 34.67%. This number was derived by reducing the ocean backhaul amount by 50%. (Tr. 812; Exhibit No. 99).[52] These adjustments must be made to avoid putting windfall profits on the backs of captive customers.

B. The Preference Trade Adder is Not Reflective of Competitive Market Prices

In addition to ignoring backhaul traffic, Mr. Dibner also included an additional amount in

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[50] The Commission should disregard Mr. Dibner's that Mr. Majoros' adjustments are inappropriate because they fail to capture incremental backhaul costs. (Tr. 123). Mr. Dibner conceded at the hearing that such incremental backhaul costs are already captured in the backhaul rates TECo Transport charges. (Tr. 168).

[51] TECo's response to the uncontroverted existence of this traffic is that it is variable and it is unclear what the tonnage of such traffic will be in the future. (Tr. 123). The same is true of every assumption Mr. Dibner uses! However, unlike Mr. Dibner's assumptions, the record reflects *actual*, historic backhaul data which provides a firm evidentiary basis for the adjustments Mr. Majoros recommends. (Exhibit Nos. 15, 16 and 18).

[52] Mr. Dibner cited a figure of 26%, which included some of the same products from the website. (Tr. 194-195). Dr. Hochstein's data suggests that the Mississippi river backhaul dry bulk tonnage is approximately 30%. (Tr. 733).

the TECo Transport rates to account for "preference trade" business TECo Transport was *not* engaging in because it was carrying coal for TECo. Mr. Dibner provides a premium for "lost opportunity costs." (Tr. 810).

The preference trades are a series of federal programs that involve the supply of food commodities to foreign countries. (Tr. 189). American flag vessels bid for this seasonal, variable spot trade. (Tr. 189-190). Such business is less certain than a five-year contract with TECo. (Tr. 190). In a competitive market, no carrier would be able to extract a premium for business it was *not* performing. (Tr. 810). That TECo Transport was able to do so here is simply more evidence of the advantages it gains from its affiliate relationship. Mr. Majoros eliminated this rate "adder" by removing the preference trade premium.[53] He used TECo's time charter rate in the calculations rather than the average of the TECo time charter rates and preference time charter rates. (Tr. 811).

Ratepayers should not be forced to pay excessive "premiums" because TECo's flawed RFP process failed to garner any bids on the ocean leg. The Commission must ensure that the rates paid reflect what would occur in a competitive market. The backhaul and preference trade adder adjustments are necessary to reflect prices in a competitive market. (Tr. 812). Confidential Exhibit No. 99 quantifies the adjustments that must be made to arrive at competitive rates.

C. The Terminal Rate Should be Lowered to at Least $1.97

The terminal rates TECo proposes are unfair when compared to the price Progress Energy pays for terminal services just across the river. Progress Energy moves 1,677,095 tons at the terminal across the river from the TECo Transport terminal at a rate of $1.97 per ton. (Tr.

[53] In contrast, Mr. Dibner used time charter earnings to establish a trend curve by which each size vessel could have a preference time charter rate assigned to it. He then assigned a maximum time charter rate for each vessel. Those maximum rates were averaged with the model's time charter rates to arrive at the rate for each vessel. (Tr. 810).

173, 183; Exhibit No. 65). TECo moves about 5,500,000 tons through its affiliated terminal, at a much higher rate per ton. (Tr. 183; Exhibit No. 4 at 68, Bates Stamp No. 138). Such a rate disparity is unusual in the terminal business because shippers receive a decreased rate, or "volume discount," when they use more terminal services. In fact, TECo's own witness testified that based on the tonnages handled, he would expect TECo to pay less than Progress Energy for terminal service because of the volume discount:

Q. Okay. Let me ask you, the – do you recall discussing the volume discount feature –

A. Yes, I do.

Q. -- for terminal rates?

A. That's right.

Q. And I think specifically you said that 5 million tons would get a more favorable rate than, say, 2 million tons?

A. In theory that would be my expectation.[54]

However, TECo Transport's terminal rates are higher because it does not give a volume discount for *over twice* the tonnage moved. Its charges are significantly higher than the non-affiliate located across the river.[55] (Exhibit No. 4 at 68, Bates Stamp No. 138).

The Commission must consider the audited $1.97 Progress Energy terminal rate. Had TECo negotiated with the terminal bidder or TECo Transport, the terminal rate might well have been considerably lower. A prudent company would have engaged in negotiations; TECo's failure to do so should result in disallowance to $1.97, which is conservative given the volume discount factor.

[54] Tr. 172-173.

[55] TECo Transport also charged more than $1.97 between 1998 and 2003 under the old contract with TECo. (Exhibit No. 4 at 68, Bates Stamp No. 138)

D. The Affiliate Relationship Leads to Excessive Ratepayer Costs[56]

The rates TECo proposes to pay its sister company under the five-year contract are colored throughout by the affiliate relationship. (Tr. 800). Affiliate transactions are problematic because the incentive to overcharge always exists. (Tr. 800) There are endless opportunities for the unregulated affiliate to derive cross-subsidies from customers of the regulated affiliate. (Tr. 800). These problems are further compounded in this case because of the dollar-for-dollar nature of the fuel cost recovery clause. (Tr. 800-801). This cost recovery mechanism provides a very strong incentive for TECo Transport to overcharge TECo to improve the parent company's bottom line. (Tr. 800-801).

TECo's own consultants (paid for by the ratepayers) helped facilitate these abuses. (Tr. 802-803). Mr. Dibner recommends rates that clearly favor TECo Transport, rather than TECo's ratepayers, whose interests he is supposed to protect. (Tr. 802-803). Mr. Dibner's proposed rates are based on his model, which overstates the prices one would encounter in a competitive market. (Tr. 802-803). Mr. Dibner's rates unjustly enrich TECo Transport, by allowing it to maximize its profits, (Tr. 828), while harming TECo's ratepayers.[57]

TECo acted imprudently when it failed to aggressively pursue the lowest possible competitive price from all available sources. TECo acted imprudently when it failed to engage in hard negotiations to get the best deal for its ratepayers, who bear all of the risk associated with these costs. TECo acted imprudently when it rejected competitive bids from the marketplace. TECo acted imprudently when it failed to negotiate for lower prices with the one bidder it did not

[56] It appears that TECo's desire to use its affiliate for coal transportation has resulted in TECo's failure to enter into the most cost-effective coal contracts for ratepayers. (Tr. 1055-1060). Further, TECo does not synchronize its coal supply procurement and coal transportation procurement leading to mismatches between the contracts, (Tr. 1060), and it does not have a least cost coal purchasing strategy. (Tr. 1096).

[57] Similarly, TECo's other expert, Sargent & Lundy (S&L), went to extreme lengths to reject the two CSXT bids. It appears that S&L's sole focus was to discredit bids that were less than Mr. Dibner's proposed rates. (Tr. 1069-1071; 1079; 1192-1194).

reject. (Tr. 517-520). And TECo acted imprudently when it offered inflated rates to TECo Transport. (Tr. 482, 505, 516).

1. TECo Failed to Negotiate on Ratepayers' Behalf

Putting aside the flaws in Mr. Dibner's proposed prices discussed above, TECo's failure to negotiate resulted in unreasonably high rates. The failure to negotiate was imprudent and provides separate and distinct grounds for disallowance. In each case, when TECo was presented with a bid on price, TECo meekly accepted the bid and *did nothing* to secure a better rate. TECo's inaction defies common sense, but worse, it is an abrogation of TECo's responsibility as a regulated utility.[58]

The following exchange between Commissioners Jaber, Deason and TECo witness Wehle makes the point:

> Q And in your experience you never negotiate bid prices?
>
> A Typically we don't negotiate bid prices unless at the table there's some kind of something that may come-up. We will go back and possibly negotiate terms, timing, other things like that. But typically the – they're going to sharpen their pencil and provide us with the best, best price. That's how we do business. We don't – if I do that with every single person who provides me a bid, then it's not an open, fair bid process. I'm going to have to go back to every single person that offered me a bid and ask them to sharpen their pencil.
>
> Q I'm not asking to –
>
> COMMISSION JABER: Excuse me. I'm sorry. And the problem with that would be what exactly?
>
> THE WITNESS: Well, I think if you become – if you get a reputation for expecting room in a price, then no one is going to give you their best price up-front, and you're going to have to assume that you're always going to negotiate it down. And not everyone is going to necessarily know that.
>
> COMMISSIONER JABER: And the problem with that would be what exactly?

[58] See discussion *supra* at pages 5-10.

THE WITNESS: That everyone wouldn't be on equal footing. You may have someone who may come in and say this is my best offer. But, again, if I get five or ten bids. I would have to go back – wouldn't I have to go back to every single party and ask them, could you lower it by $5 or $2?

COMMISSIONER JABER: And the problem with that would be what exactly?

THE WITNESS: It would just be a very arduous process, I think.

COMMISSIONER JABER: And the problem with that would be what?

THE WITNESS: I think that it would be – it would just belabor the process, Commissioner.

COMMISSIONER JABER: And that's the only reason you didn't go back and ask TECO Transport to sharpen their pencils?

THE WITNESS: We felt like the model that Mr. Dibner had provided was the best Market rate that we could get, and under the right of first refusal they could meet or beat it and they chose to meet it.

. . .

COMMISSIONER DEASON: Yea. Now would be a good time to ask it. As I understood Mr. Perry's question, it has to do with the bid that was provided by the alternative terminal provider.

THE WITNESS: That's correct.

COMMISSIONER DEASON: And as I understood the testimony yesterday, there was one bid and , in fact, there is only one other entity other than TECO Transport that could even respond to that bid. Is that your understanding?

THE WITNESS: Yes.

COMMISSIONER DEASON: So you got one bid from one potential provider, and you did not think that it was appropriate to discuss with that provider whether there was some way to improve their bid?

THE WITNESS: Before – if I understand your question, before we offer it to Mr.—to TECO Transport?

COMMISSIONER DEASON: Yes.

THE WITNESS: That's correct.

COMMISSIONER DEASON: You chose not to do that?

THE WITNESS: We chose not to do that.

(Tr. 517-520). This exchange is even more amazing when one considers that on the terminal segment, TECo got *one* bid. How "arduous" is it to contact *one* bidder to see if a more favorable price can be negotiated for a five-year contract?[59] The answer is obvious: TECo, knowing the contract was going to its affiliate terminal to meet or beat the price quoted by the non-affiliate terminal, had no incentive to negotiate lower rates for the consumer and so no negotiation took place. (Tr. 516). A dollar saved in negotiation would be a dollar that TECo's parent company, TECo Energy, would not receive.[60]

This failure to negotiate becomes even more imprudent when one considers that this very same terminal charged Florida Progress $1.97/ton in 2003 for less tonnage than will be terminalled under the new contract, though TECo should have expected (and demanded) a volume discount. (Tr. 172-173; Exhibit 65).[61] If TECo had been a tough negotiator on the terminal segment, ratepayers would have saved money. Instead, TECo was content to present the bid to its affiliate and call it a day.

This same "no negotiation" posture continued when TECo *did not even discuss price* with its sister company; the contract was simply presented to TECo Transport. (Tr. 482; 505; 516). This happens consistently in the TECo Transport/TECo relationship. For example, on the river leg, a barge company offered a bid for substantial savings over the TECo Transport contract for several origins. TECo did not meet with the barge company prior to rejecting its bid. (Tr. 865; Exhibit No. 12). Nor did TECo bother to take the lower offer back to TECo Transport to

[59] Put another way, isn't that what ratepayers pay Ms. Wehle to do?
[60] In Mr. White's view, TECo would not negotiate with CSXT because it was afraid it might have to accept a number lower than its current contract with TECo Transport. (Tr. 923).
[61] See discussion at 22-23, supra.

meet or beat under the right of first refusal. (Tr. 868). *Real* negotiation should have taken place, done with the goal of striking the best deal for ratepayers.

CSXT submitted two bids to TECo.[62] TECo maintained its "don't call us, we'll call you" stance, despite the fact that TECo witness Wehle admitted that the rates CSXT offered were very favorable. (Tr. 552). TECo rejected such bids out of hand and gave CSXT the cold shoulder every time rather than attempting to negotiate a deal for ratepayers' benefit. CSXT witness White explained that CSXT wanted to meet with and expected to negotiate with TECo:

> Q. Well, then isn't it true that your bid proposal was not a firm bid?
>
> A. It is a firm bid. If you want to take it that way, we will certainly sign it, but the point is you have the opportunity to negotiate those terms. Ms. Wehle said the other day, when she was asked a question about why didn't you go back and push IMT for a lower number, and she state that, well, you know, we usually don't push back on the number, but the other things in the contract, you know, we do negotiate on those.
>
> . . . We fully expected them [TECo] to come back on these other ancillary items and push back and say, hey, what about this. And the idea was let's sit down and talk about it. That is what a negotiation is.

(Tr. 948).

> Q. Well, then, if these are things that you expect Tampa Electric to negotiate with CSXT, did you expect Tampa Electric to evaluate your proposal based upon what you included in the proposal or not?
>
> A. I think we expected them to evaluate the proposal in the most prudent way they felt they should. I think that, you know, they need to think about what -- where they want to go in a negotiation. You know, I can't speculate on what they should do, but I would think that a prudent company would look at a bid and say the number looks good, what problems do we have with it. Let's sit down and talk to them.

(Tr. 956).

TECo's witness, Mr. Murrell, admitted that CSXT's proposal was very attractive and he

[62] Such bids were submitted after CSXT itself had to request the RFP. (Tr. 916). Further, CSXT witness Mr. White details in his testimony CSXT's rebuffed attempts to meet with TECo to discuss possible rail service. (Tr. 914).

hoped TECo would follow through on it. (Tr. 1421-1422). He also noted that discussion with CSXT regarding its proposal would be appropriate. (Tr. 1422). But TECo did not talk to CSXT nor did it take either of CSXT's proposals back to its affiliate to meet or beat. (Tr. 867).[63]

2. TECo Transport's "Forgiveness" of Multi-Million Dollar Dead Freight Debt

Inexplicably (at least from an arms' length business perspective), TECo Transport forgave a debt of approximately $10-12 million TECo owed to it. Although Ms. Wehle provided two different dates in her sworn testimony as to when this occurred,[64] the most reasonable interpretation of this generosity appears to be that TECo Transport decided to waive the $10-12 million in dead freight charges TECo owed it sometime between October 6[65] and October 20, 2003. (Tr. 487–489). Ms. Wehle testified that the $10-12 million debt would not have been waived if TECo Transport had not been awarded the new five-year contract. (Tr. 484).[66] Allegedly, there was no consideration for this debt forgiveness and it was not mentioned in the contract negotiations, despite the fact that Ms. Wehle's TECo Transport colleagues "constantly reminded" her of the debt. (Tr. 485).

It is not normal commercial behavior for a company to waive a $10-12 million debt for nothing. If one accepts that the debt forgiveness was not part of the contractual negotiations, it appears that TECo Transport made an independent decision to waive $10-12 million to which it was contractually entitled. Why? Was it a *quid pro quo* for being awarded a firm five-year

[63] The TECo witnesses expressed "fear" that if TECo did business with CSXT, it would become captive to the railroad. However, Ms. Wehle could not provide a single real world example where this "fear" became reality. (Tr. 601).

[64] In Ms. Wehle's deposition taken May 12, 2004, she stated that TECo Transport waived the dead freight debt in early January 2004. (Tr. 486; Exhibit No. 76). In Ms. Wehle's deposition taken October 20, 2003, she also stated that TECo Transport had waived the dead freight charges. (Exhibit No. 77). Obviously, the October 2003 deposition puts the waiver of dead freight decision by TECo Transport back much earlier than January 2004.

[65] The contract with TECo Transport was executed on October 6, 2003.

[66] TECo Transport's waiver of the dead freight charge is analogous to a car dealer offering to pay market value for a customer's trade-in, but offsetting the amount by charging the customer full sticker price for a new car.

transportation contract again? Perhaps the profits from the contract are so large that $10-12 million can simply come off the top?

TECo did no comparison of the value of the debt forgiveness verses lower cost transportation services. A review of the adjustments various intervenor experts suggest makes it obvious that such adjustments far outweigh the debt forgiveness. (Tr. 788). The affiliate relationship is quite troubling when an RFP is awarded by a sister company with $10-12 million in debt and within two weeks of the contract award, the debt mysteriously disappears.

3. JEA Rates Are Much Lower for Cargo Traveling Twice the Distance

JEA pays $9.00 per ton to ship petroleum coke from East Texas and Mississippi to Jacksonville, Florida. (Tr. 813; Exhibit No. 17). The carrier is TECo Transport, but the shipper is not an affiliate. Mr. Dibner's cost model (and thus the rates incorporated into the new contract) would charge ratepayers significantly more to transport similar cargo than the rate from East Texas to Tampa, which is half the distance! (Tr. 813; Exhibit No. 4 at 66, Bates Stamp 137). TECo attempts to dismiss the JEA transaction as a "spot" movement; however, the record shows significant tonnage moving for well over a year at a constant price of $9.00 per ton.[67] (Exhibit No. 17).

The JEA/TECo Transport rate also illustrates the unreasonableness of Mr. Dibner's cross-gulf rate to carry coal from the terminal in Davant, Louisiana to Tampa, Florida. (Exhibit No. 4 at 68, Bates Stamp 138). The distance from Davant to Tampa is also about half the distance of the voyage TECo Transport makes when it carries coal for JEA. Since TECo Transport charges JEA $9 per ton to go to Jacksonville, one would expect that Mr. Dibner's ocean rate would be about half that amount. However, Mr. Dibner's rate does not compare favorably to the JEA/TECo Transport rate. (See, Exhibit No. 4 at 68, Bates Stamp 138). The JEA/TECo

[67] These eight transactions encompass 13 months and over 280,000 tons. (Tr. 521-522; Exhibit No. 17).

Transport rate demonstrates that Mr. Dibner's petroleum coke and cross-gulf transportation rates are excessive.

4. TECo's Transportation Costs are Higher than Gulf Power's Costs

Gulf Power transports coal from International Marine Terminals (IMT), near the TECo Bulk Terminal in Davant, Louisiana, to its Crist Electric Generating Plant in Pensacola via the Intercoastal Waterway. (Tr. 318). To safely navigate the Intercoastal Waterway, Gulf Power ships its coal in four-barge tugs that are only capable of carrying approximately 6,000 to 7,000 tons of coal per trip (Tr. 313; 315); TECo, on the other hand, ships its coal in large ocean-going vessels carrying about 45,000 tons each. (Tr. 72).

Mr. Dibner recognized that one would expect that an arrangement similar to Gulf Power's would result in higher costs than those TECo would incur:

> Q. Okay. If [Gulf Power], in fact, receive their coal on the Intracoastal through tows of only four barges, one would expect that they would have higher cost and/or rates than what TECo pays, would you not?
>
> A. One would expect that if the comparison is fair, yes. (Tr. 313).

Even though TECo enjoys economies of scale and cost over Gulf Power, the amount Gulf Power pays for waterborne coal transportation from Davant, Louisiana, to Pensacola, Florida is $5.17, less than what TECo pays to transport coal from Davant to Tampa, Florida. (Compare Tr. 317-318; Exhibit No. 92 to Exhibit No. 4 at 68, Bates Stamp 138).

E. A Rate Adjustment Will Not Affect TECo's Reliability

Reliability is, and should be, an important issue for all parties. The Commission expressed concern during the hearing about the possibility that TECo Transport might utilize its fleet elsewhere and leave TECo ratepayers without a reliable source of coal transportation. (Tr. 829-834).

The record and history supply a ready answer. TECo and TECo Transport have already signed a contract for the next five years. (Tr. 390). Thus, TECo Transport will receive the rates under that contract unless the sister companies renegotiate the contract. What this proceeding is about, however, is TECo's recovery of dollars under the fuel clause from ratepayers. To the extent TECo fails to recover all of the amounts it has agreed to pay its affiliate, it is the result of its own imprudence.

Moreover, both OPC/FIPUG witnesses testified that an alternative to market-based rates would be actual costs verified by audit. (Tr. 816, 868). The Commission would then know the actual facts of this case. The Commission has authority to hold dollars subject to refund and to audit TECo Transport to find out the truth of where the actual revenues and costs lie. The Commission could then make reasonable allocations based upon the audit or could return to rate base regulation if there was real concern that TECo Transport might actually exit the market. This record supports a return to rate base type regulation if the Commission decides to pursue this option. (Tr. 742-743).

ISSUE 3

SHOULD THE COMMISSION MODIFY OR ELIMINATE THE WATERBORNE COAL TRANSPORTATION BENCHMARK THAT WAS ESTABLISHED FOR TAMPA ELECTRIC BY ORDER NO. PSC-93-0443-FOF-EI, ISSUED MARCH 23, 1993, IN DOCKET NO. 930001-EI?

OPC/FIPUG Position: *Yes. The waterborne coal transportation benchmark is outdated and does not provide information to judge the reasonableness of transportation prices. To continue to use the benchmark would result in inflated rates.*

The true test of the value of the benchmark is how it has functioned over time. The benchmark is a tool – a "sanity check" – intended to ensure that prices paid for transportation

services do not increase unreasonably without justification.[68] The benchmark has consistently been much higher than the rates TECo has paid TECo Transport, (Tr. 815), and is far out of line with reality when compared even to TECo Transport's inflated waterborne rates and the CSXT rail bids. (Tr. 814-815).

The benchmark has not served the ratepayers' interest because it is a misleading indicator. (Tr. 1086-1087). It compares only the rates TECo pays with publicly available rail rates. However, the public rail rates are higher than the actual rates the shipper's pay to the railroad, which are confidential. (Tr. 1409). TECo's witness, Mr. Murrell, testified that most coal moved by rail today moves under confidential contract rates, and those rates are lower than public tariff rates. (Tr. 1409). Thus, the benchmark is not an effective indicator of fair, just and reasonable rates.

Moreover, the benchmark compares only waterborne rates to publicly available rail rates; it does not compare the reasonableness of the rates paid to TECo Transport to the waterborne transportation market. If the Commission approved as reasonable all rates paid to TECo Transport that fall below the benchmark, it is possible that those rates would be much higher than the competitive market price for waterborne transportation services. And in fact, the evidence shows exactly that in this case: the prices contained in the October 6, 2003, contract between the two affiliate companies are above market because TECo failed to negotiate with TECo Transport or the terminal bidder, failed to consider backhaul revenues in the rates, and added an inappropriate preference trade premium. If the Commission approves the rates TECo proposes under the current contract, based on the fact that they are below the benchmark, it will

[68] Order No. 20298 at 8; Tr. 669.

be approving rates that are not fair, just or reasonable to the detriment of the ratepayers.[69]

The evidence reflects further problems with the benchmark when benchmark information is compared to now public FERC Form 423 data. Between the years 1992 and 2000, the difference between the benchmark rate and the rate paid to TECo Transport fluctuated from $4.91 per ton in 1993 (Tr. 669) to $9.61 per ton in 1998. (Tr. 672). This represents a swing of $24 million to $47 million per year in the "range of reasonableness" established by the benchmark. (Tr. 670-672). This swing shows how ineffective the benchmark is at serving as a "sanity check" for competitive market rates.

The discrepancy between the rail rates that TECo paid for the *actual* delivery of coal to its Gannon station and the benchmark rate further illustrates the benchmark's irrelevance to the real market. For example, in 2000, TECo paid CSXT $16.35 per ton to deliver coal to Gannon. (Tr. 1091). During this same timeframe, the benchmark was $26.23, a difference of almost $10 per ton or $50 million[70] a year when compared to actual rates paid. (Tr. 1092). The large swing of between $24 and $50 million between the benchmark and the actual prices paid is further proof that the benchmark must be eliminated. Dr. Sansom put it succinctly when he enumerated the reasons the benchmark should be eliminated:

> [I]t is based on data that cannot be audited, it is based on data that excludes volume discounts; it is based on data that miscalculates the allowed charges for rail car ownership, and it is based on data that is not public and not reviewable.

(Tr. 1080).

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[69] Dr. Sansom pointed out another flaw in the benchmark related to how TECo calculates it: TECo fails to include *all* transportation costs. TECo does not include the cost of moving the coal from the mine to the barge. (Tr. 1052, 1090).

[70] The $50 million figure is the product of multiplying $10 times TECo's full requirement of 5 million tons of coal per year. It is not based on the tons of coal TECo received by rail at the Gannon facility, which was much less than its full requirement.

CONCLUSION

TECo's RFP suffered from a variety of problems. Within two weeks after the RFP was issued, an industry website announced to the market: don't bother to bid, the contract is destined for TECo's affiliate, TECo Transport. The RFP stated a preference for an integrated provider, and the only provider capable of meeting this RFP term was TECo's affiliate. In addition, TECo's affiliate had an "ace-in-the-hole" – a right of first refusal. The Commission Staff offered its input on how to improve the RFP but TECo ignored them. Five weeks later, TECo received a meager response to its RFP: one partial river bid, one terminal bid, no ocean bids, and an "unsolicited" rail bid.

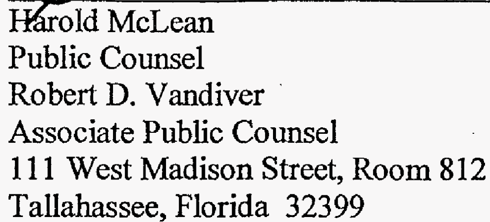
TECo rejected the river bid and dismissed the railroad's effort to win the business; none of the bids were taken to TECo Transport to meet or beat. The one bid TECo accepted, the terminal bid, was for a higher rate than TECo paid under its prior contract! Moreover, the terminal rate is higher than the rate Progress Energy pays for the same service just across the river, although TECo should pay less by virtue of a volume discount. TECo made no effort to negotiate with any of the bidders.

TECo's consultant then constructed a model for the ocean and river portions of the coal transportation journey which overstated the price for these services in a competitive market. When intervenors pointed out the existence of significant backhaul business that should reduce the rate, the consultant claimed that backhaul was irrelevant. He also added a "preference trade premium," as a lost opportunity cost on top of the high rates already constructed. In addition, he charged ratepayers more for a service that TECo Transport provided to another utility for less, even though the other utility is located twice as far away. Finally, TECo consistently failed to

negotiate lower rates for its customers when dealing with TECo Transport, thereby costing customers money.

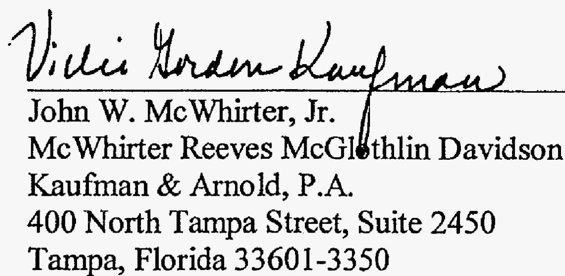
This Commission must set rates which are just and reasonable. It is TECo's obligation to prove that the rates it proposes are prudent. TECo has failed to do so and the Commission must disallow cost recovery as OPC/FIPUG witness Majoros recommends. (Exhibit No. 18). The Commission should also order TECo to change its waterborne coal transportation solicitation practices on a going-forward basis.

Finally, the Commission should eliminate the benchmark. The record overwhelmingly demonstrates that the benchmark is an outdated and irrelevant tool that fails to check the "sanity" of the rates.



Harold McLean
Public Counsel
Robert D. Vandiver
Associate Public Counsel
111 West Madison Street, Room 812
Tallahassee, Florida 32399

Attorneys for the Citizens of the State of Florida



John W. McWhirter, Jr.
McWhirter Reeves McGlothlin Davidson
Kaufman & Arnold, P.A.
400 North Tampa Street, Suite 2450
Tampa, Florida 33601-3350

Vicki Gordon Kaufman
Timothy J. Perry
McWhirter Reeves McGlothlin Davidson
Kaufman & Arnold, PA
117 South Gadsden Street
Tallahassee, Florida 32301

Attorneys for the Florida Industrial
Power Users Group

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Joint Post-Hearing Brief and Statement of Issues and Positions of the Citizens of the State of Florida and the Florida Industrial Power Users Group has been furnished by (*) hand delivery or U.S. Mail this 12th day of July 2004, to the following:

(*) Wm. Cochran Keating IV
Florida Public Service Commission
Division of Legal Services
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399

Lee L. Willis
James D. Beasley
Ausley & McMullen
227 S. Calhoun Street
Tallahassee, Florida 32302

R. Sheffel Wright
Landers & Parsons
301 West College Avenue
Tallahassee, Florida 32301

Mike Twomey
Post Office Box 5256
Tallahassee, Florida 32314-5256

Robert D. Vandiver