ORIGINAL

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FPL

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November 24, 2004

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COMMISSION CLERK

VIA HAND DELIVERY
Ms. Blanca S. Bayó, Director
Division of the Commission Clerk and
Administrative Services
Florida Public Service Commission
Betty Easley Conference Center
2540 Shumard Oak Boulevard, Room 110
Tallahassee, FL 32399-0850

Re: Petition for authority to recover prudently incurred storm restoration costs related to 2004 storm season that exceed storm reserve balance, by Florida Power & Light Company – Docket No. 041291-EI

Dear Ms. Bayó:

Enclosed for filing in the above-referenced docket are the original and fifteen (15) copies of the testimony and exhibits of Florida Power & Light Company's Witnesses K. Michael Davis, Rosemary Morley and Linda R. Whalin.

Please contact me if you have questions regarding this filing.

Sincerely,

Lynne A. Adams for
R. Wade Litchfield

CMP ____
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RWL:ec
Enclosures

Davis 12583-04
Morley 12584-04
Whalin 12585-04

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FPSC-BUREAU OF RECORDS

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by hand delivery(*) or United States Mail this 24th day of November, 2004 to the following:

Florida Public Service Commission
Cochran Keating, Esquire(*)
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By: Lynne A. Adams

for R. Wade Litchfield
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BEFORE THE FLORIDA
PUBLIC SERVICE COMMISSION

DOCKET NO. 041291-EI
FLORIDA POWER & LIGHT COMPANY

IN RE: FLORIDA POWER & LIGHT COMPANY'S PETITION FOR AUTHORITY TO RECOVER PRUDENTLY INCURRED STORM RESTORATION COSTS RELATED TO THE 2004 STORM SEASON THAT EXCEED THE STORM RESERVE BALANCE

NOVEMBER 24, 2004

DIRECT TESTIMONY & EXHIBIT OF:

K. MICHAEL DAVIS

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

TESTIMONY OF K. MICHAEL DAVIS

DOCKET NO. 041291-EI

I. INTRODUCTION AND CREDENTIALS

Q. Please state your name and business address.

A. My name is K. Michael Davis, my business address is 9250 West Flagler Street, Miami, Florida 33174.

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

A. I am employed by Florida Power & Light Company ("FPL" or the "Company") as Vice President, Controller and Chief Accounting Officer.

Q. Please outline your educational qualifications and experience.

A. I graduated from the University of Florida in 1968 with a Bachelor of Science degree in Business Administration, with a major in Accounting. In that same year I was employed by Deloitte Haskins & Sells (DH&S), Independent Public Accountants (presently Deloitte & Touche). I was promoted to manager in 1976 and was elected a Partner in 1981. During my tenure with DH&S, I participated in engagements involving services to a number of diverse industry groups including the utility industry. In addition, I was responsible for handling accounting questions concerning the utility industry during a three-year assignment in the DH&S executive office in New York. In December 1988, I was employed by FPL as comptroller. On July 1, 1991, I accepted my current position as Vice President, Controller and Chief Accounting Officer. I am a Certified Public Accountant in the State of Florida, and a member of the American Institute of Certified Public Accountants and the Florida Institute of Certified Public Accountants. I am a member and past chairman of the Accounting Executive Advisory Committee of the Edison Electric Institute (EEI). That group is composed of Chief Accounting Officers from utilities that are members of EEI and oversees the activities of the various accounting committees of EEI and advises senior EEI committees on accounting issues. **That committee meets annually with the Financial Accounting Standards Board to discuss accounting issues of interest to the membership and approves all comment letters issued by EEI on accounting matters.**

Q. What are your duties as Vice President, Controller and Chief Accounting Officer of FPL?

A. As Vice President, Controller and Chief Accounting Officer, I am responsible for the development, interpretation and implementation of FPL's accounting policies, procedures and related internal accounting controls, and for maintaining the accounting records in compliance with financial and regulatory accounting requirements. Also, I am responsible for ensuring the adequacy of the systems necessary to support the accounting process.

Q. Are you sponsoring an exhibit?

A. Yes. I am sponsoring Exhibit KMD – 1 which shows estimated storm damage costs by hurricane and cost category, net of expected insurance reimbursement.

II. PURPOSE

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to discuss FPL's accounting treatment for the storm damages in the Storm Damage Reserve. I will discuss the amount charged to the storm damage reserve and what FPL expects the reserve deficiency to be at December 31, 2004. I will discuss how FPL's treatment is consistent with Commission rules, Order No. PSC-95-0264-FOF-EI, issued February 27, 1995 in Docket No. 930405-EI and the terms and conditions of the settlement agreement approved in Order No. PSC-02-0501-AS-EI, issued April 11, 2002 in Docket No. 001148-EI. In addition, I will discuss the appropriate mechanism and the appropriate time frame for recovery of these costs.

III. HURRICANE COSTS AND ACCOUNTING TREATMENT

Q. What is the current amount of the storm damage from the hurricanes?

A. The total damages to date are approximately $818 million. The company expects to receive an insurance reimbursement of $108 million for non-transmission and distribution property. The $108 million has been recorded as a receivable from the insurance company. Consequently, the total amount charged to the reserve to date is $710 million on a total system basis.

Q. Please provide a breakdown of the $710 million charged to the Storm Damage Reserve for hurricane damages by storm.

A. The following is a breakdown by storm of the $710 million:

(in millions)

Charley	Frances	Jeanne	TOTAL
$209	$267	$234	$710

The $710 million is an estimate of the total uninsured hurricane damages. It is subject to adjustment as the actual invoices are received and paid.

Q. Please provide a breakdown of the $710 million by category.

A. Exhibit KMD – 1 shows the breakdown of the $710 million by category and by storm, net of the expected $108 million of insurance reimbursement.

Q. How was the $710 million (system) of storm damages recorded?

A. In accordance with Commission rule 25-6.0143 Florida Administrative Code (FAC) all costs incurred related to the hurricane were debited to the Storm Damage Reserve.

Q. What effect did the $710 million (system) have on the Storm Damage Reserve?

A. The $710 million (system) charged to the Storm Damage Reserve created a deficiency in the reserve which will be discussed in more detail later in my testimony.

Q. Is the deficiency in the Storm Damage Reserve recovered by any other recovery mechanism?

A. No. The annual accrual of $20.3 million will continue to be recorded by FPL. Because FPL proposes that the recovery of the deficit will be based on the reserve balance as of December 31, 2004, the continuation of the $20.3 million annual accrual, beginning January 1, 2005 would be used to begin rebuilding the reserve for future storm losses.

Q. Are the current accrual and the recovery of the deficit authorized by Commission orders?

A. Yes. The current accrual amount of $20.3 million was approved in Order No. PSC-95-1588-FOF-EI issued December 27, 1995, in Docket No. 951167-EI and reaffirmed by the Commission in Order No. PSC-98-0953-FOF-EI, issued July 14, 1998, in Docket No. 971237-EI. In this order the Commission stated that, "In cases of catastrophic loss, FPL continues to be able to petition the Commission for emergency relief." In addition, the settlement agreement approved by the Commission in Order No. PSC-02-0501-AS-EI, issued April 11, 2002 in Docket No. 001148-EI states, "In the event that there are insufficient funds in the Storm Damage Reserve and through insurance, FPL may petition the FPSC for recovery of prudently incurred costs not recovered from these sources."

Q. What is FPL proposing to recover at this time?

A. FPL is only requesting recovery of the deficiency.

Q. What is the history of FPL's Storm Damage Reserve?

A. FPL's Storm Damage Reserve started in 1946, and became a funded reserve in 1958. FPL has increased the reserve by the amounts authorized by the Commission. In addition, the reserve has been increased by the earnings from investments held in the related fund. The reserve has been reduced by amounts needed to repair damage caused by hurricanes and other named storms. As such, FPL's customers have benefited from the existence of the reserve. It is the catastrophic nature of the three hurricanes experienced in 2004 that has wiped out the entire reserve and created the deficit FPL is now seeking to address.

Q. Please describe the accounting entries to record the $20.3 million annual accrual.

A. Monthly accruals are recorded as a debit to Account 924 – Property insurance expense - and a credit to Account 228.1 – Accumulated provision for property insurance – Storm and Property Damage Reserve. Monthly accruals are equal to one-twelfth of the annual amount authorized. This accounting is consistent with Rule 25-6.0143 of the Florida Administrative Code and the Uniform System of Accounts prescribed by this Commission.

Since the monthly accrual to Account 924 is not deductible for income tax purposes, a credit to above-the-line deferred tax expense and a debit to a deferred tax asset Account 190 – Accumulated deferred income tax - is recorded to recognize the future tax deductibility at the time actual storm losses are incurred. In addition, because FPL's reserve is a funded reserve, entries are required to recognize the investment of the after-tax accruals in a special fund. Monthly contributions are made to the fund on an after tax basis equal to the gross accrual less current federal and state income tax payable. The amount contributed to the fund is recorded as a debit to Account 128.3 – Other special funds – storm and property damage fund. The use of the fund is restricted to un-insured losses that are covered by the storm and property damage reserve. To date, actual withdrawals from the fund have been limited to losses resulting from storm damages.

Q. How does FPL account for the earnings from investments held in the Fund?

A. In accordance with prior Commission orders, earnings from investments held in the fund, less any applicable income taxes, are reinvested in the fund resulting in an increase in the fund balance and a corresponding increase (credit) to the reserve. Fund earnings and applicable income taxes are recorded to below-the-line non-operating income accounts. FPL also accrues a below the line expense equal to the pre-tax value of reinvested earnings and records a credit to the reserve for a like amount. Since the expense representing the reinvestment of the fund earnings is not deductible for income tax purposes, a credit to deferred tax expense, Account 411 and a debit to deferred tax asset, Account 190 is also recorded. Fund income, current tax expense, accrual for earnings charged to the reserve, and deferred tax expense are all recorded to below-the-line accounts and net to zero on a monthly basis. Therefore, there is not an impact on FPL's net income resulting from reinvestment of fund earnings. The benefit accrues to the customers as an increase in the available reserve balance to offset storm damages.

Q. What is the effect of hurricane damages on the expected balance in the Storm Damage Reserve at December 31, 2004?

A. The balance in the Storm Damage Reserve excluding the $710 million (system) of charges would have been a credit (positive) balance of approximately $354 million (system). The storm reserve is expected to have a debit (deficit) balance of approximately $356 million (system) at December 31, 2004. This deficit balance is the direct result of charging the reserve, as directed by the Commission, with $710 million (system) of storm related costs. FPL has continued to increase the reserve on a monthly basis with one-twelfth of the annual accrual. In addition, earnings from investments held in the storm fund have continued to have a positive effect on the reserve balance. In order to minimize any negative effect on investment earnings from the liquidation and withdrawal of funds, the funds are being withdrawn over the October through December period. Any earnings realized from investments held in the fund during this period have been and will continue to be credited to the reserve until all funds have been withdrawn and the balance in the fund is reduced to zero. The continuation of monthly accruals and recognition of fund earnings through the end of the year have been applied to reduce the deficit resulting from the $710 million (system) of storm damage costs charged to the reserve.

Q. Is FPL's methodology for accounting for the storm fund consistent with Commission Rules and Orders?

A. Yes. FPL's methodology for accounting for the storm fund is consistent with Commission Rule 25-6.0143 Florida Administrative Code for establishing and maintaining a reserve. All costs incurred in connection with the three named hurricanes which hit FPL's service territory in 2004, both capital and O&M, have been charged to the storm reserve. The accounting treatment used was approved by the Commission in Order No. PSC-95-0264-FOF-EI, issued February 27, 1995 in Docket No. 930405-EI.

Q. How does FPL capture costs related to Storm Restoration?

A. When a storm threatens FPL's service territory 72 hours prior to landfall the General Office Command Center (GOCC) is activated and FPL establishes a work order unique to that storm. All costs related to the storm are charged to this work order, including preparation and restoration costs. FPL's main purpose for utilizing a unique work order is to simplify the accounting as the main focus of the Company's effort is on storm restoration. The use of work orders captures all costs by source, e.g., payroll, vehicle, cash voucher, etc., and allows the Company to maintain the appropriate audit trail.

Q. How does FPL propose to collect the Storm Reserve deficiency?

A. Upon Commission approval, FPL proposes to initiate recovery of the jurisdictional portion of the estimated Storm Reserve deficiency of $356 million (system), or $354 million (jurisdictional), through a monthly surcharge "Storm Restoration Surcharge" to apply to customer bills based on a twenty-four month period or until the $354 million (jurisdictional) amount is collected commencing January 1, 2005, or as early as practicable. The recovery of the $354 million (jurisdictional) will only allow FPL to recover the deficiency.

Q. Why is a 24 month recovery period appropriate?

A. In an effort to limit the impact to FPL's customers while still recovering the Storm Reserve deficiency in a timely manner, FPL proposes to recover the deficiency over a 24 month period or less. FPL has already incurred an extraordinary cost of $818 million ($710 million after expected insurance recovery of $108 million) to restore electrical power to its customers. Immediate recovery of these costs through FPL's storm reserve fund, insurance proceeds and customers would restore FPL's financial position to what it was before the hurricanes. In addition, it would provide the best match between the timing of the incurrence of the extraordinary costs with the timing of their recovery. Because of financing costs, the longer the recovery period, the more costly it is for FPL's customers.

Q. How will the $356 million (system) or $354 million (jurisdictional) be amortized over the proposed recovery period?

A. FPL will amortize the $356 million (system) or $354 million (jurisdictional) as a regulatory expense over the 24 month period or less. The amount amortized will be equal to the amount recovered from customers each month. The remaining unamortized balance will accrue interest at the 30 day commercial paper rate.

Q. What is the revenue requirement amount used to determine the Storm Restoration Surcharge?

A. The estimated 2005 annual revenue requirement amount is $183,179,800.

Q. Please describe how you calculated the estimated annual revenue requirement amount of $183,179,800.

A. The estimated 2005 annual revenue requirement amount of $183,179,800 was calculated by making the assumption that the deficit amount of $356 million (system) would be recovered ratably over a 24 month period of time. In addition, FPL accrued interest on the declining balance at the assumed 30 day commercial paper rate. The calculation does not take into consideration the monthly variation in sales. Any variances in any of the components will be included in the calculation of the final true-up amount.

Q. Will the recovery of the jurisdictional portion of the estimated Storm Reserve deficiency be subject to a true-up?

A. Yes. Within 60 days following expiration of the recovery period, FPL will file the final actual hurricane costs underlying the Storm Reserve deficiency. Any actual over-recovery of the Storm Reserve deficiency based upon such filing would be refunded on customer bills as soon as practicable following a final Commission order accepting the proposed true-up, such refund to be allocated in the same manner as the surcharge was applied. For any under-recovered portion of the Storm Reserve deficiency, FPL would propose the means by which it would be recovered at that time. In addition to identifying the actual, final Storm Reserve deficiency in its filing, and any under or over-recovered amounts, FPL would supply the revised Storm Recovery Factor corresponding to the refund or recovery, as appropriate, in connection with the true-up. As an alternative, the Commission may choose to apply any over-recovered amounts to the storm reserve. This would benefit our customers by increasing the funds available for future storm damage.

IV. CONCLUSION

Q. Can you please summarize your testimony?

A. Yes. As previously discussed, FPL maintains a funded reserve. Absent the hurricanes this funded reserve would be expected to reach $354 million at December 31, 2004. Due to unprecedented storm damage from Hurricanes Charley, Frances and Jeanne, FPL sustained $818 million ($710 million after expected insurance recovery of $108 million) in damages. FPL's expected insurance reimbursement is $108 million and as a result the Storm Damage Reserve was charged with $710 million on a total system basis. After application of the expected $354 million in the funded reserve, FPL expects to have a deficit of $356 million (total system) for which it is seeking recovery of $354 million (jurisdictional) over 24 months. FPL's treatment is consistent with Commission rules and orders and is consistent with a settlement agreement reached by various parties and approved by the Commission.

Q. Does this conclude your direct testimony?

A. Yes it does.

Exhibit No. ______
KMD -1
Docket No. 041291-EI
FPL Witness: K.M. Davis

November 24, 2004

Hurricane Restoration Costs by Storm and Cost Category*

Cost by Category	Charley	Frances	Jeanne	TOTAL
FPL Payroll	**$ 35,754,550**	**$ 48,024,667**	**$ 27,156,010**	**$ 110,935,227**
Contractor & Foreign Utility	**114,803,374**	**151,411,773**	**145,833,572**	**412,048,719**
Vehicle & Fuel	**5,964,257**	**4,770,307**	**8,652,257**	**19,386,821**
Materials	**20,186,257**	**16,337,301**	**11,000,000**	**47,523,558**
Logistics	**20,981,035**	**23,981,505**	**18,468,451**	**63,430,991**
Other	**11,459,686**	**22,645,159**	**22,569,839**	**56,674,684**
TOTAL	**$ 209,149,159**	**$ 267,170,712**	**$ 233,680,129**	**$ 710,000,000****

*** These costs are net of the expected insurance reimbursement of $108 million.**

**** Estimated costs included in Petition.**