



**NORTH CAROLINA
PUBLIC STAFF
UTILITIES COMMISSION**

February 2, 2021

Ms. Kimberley A. Campbell, Chief Clerk
North Carolina Utilities Commission
4326 Mail Service Center
Raleigh, North Carolina 27699-4300

Re: Witness Summaries and Redirect Exhibits
Docket Nos. E-2, Sub 1262 and E-7, Sub 1243
Joint Petition for Issuance of Storm Recovery Financing Orders

Dear Ms. Campbell:

In response to the North Carolina Utilities Commission's ("Commission") November 6, 2020 Order Scheduling Hearing, Requiring Filing of Testimony, and Establishing Discovery Deadlines, attached for filing in the above-referenced dockets are the Public Staff's witness testimony Summaries read and/or moved into the record during the evidentiary hearing, including a listing thereof. Also attached for filing are the Public Staff's Redirect Exhibits introduced and moved into the record during the evidentiary hearing on Friday, January 29, 2021, including a listing thereof.

The Public Staff witness Summaries relate to Public Staff testimony and exhibits filed December 21, 2020. Corrections to testimony were filed for witnesses Fichera, Heller, Maness & Boswell, and Sutherland on January 6, 2021. Further corrections for witnesses Fichera and Heller were filed on January 13, 2021, at which time the fully-memorialized testimony (not exhibits) of witnesses Fichera, Heller, Maness & Boswell, and Sutherland was also filed.

If you have any questions, please do not hesitate to contact us. Thank you.

Sincerely,

Electronically submitted
/s/ William E. H. Creech
zeke.creech@psncuc.nc.gov

Attachments

c: Parties of Record

Executive Director
(919) 733-2435

Accounting
(919) 733-4279

Consumer Services
(919) 733-9277

Economic Research
(919) 733-2267

Energy
(919) 733-2267

Legal
(919) 733-6110

Transportation
(919) 733-7766

Water/Telephone
(919) 733-5610

Public Staff

Witness Testimony Summaries

Public Staff testimony Summaries were read and/or moved into the record on Thursday, January 28, and Friday, January 29, 2021, for the following witnesses, which are also attached:

- Abramson
- Fichera
- Heller
- Klein
- Maher
- Maness & Boswell
- Moore
- Schoenblum
- Sutherland

Public Staff
Redirect Exhibits

The Public Staff introduced and moved the following Redirect Exhibits into the record during the evidentiary hearing on Friday, January 29, 2021, copies of which are also attached:

- Public Staff Pre-Marked 38 introduced as:
 - **Public Staff Schoenblum Redirect Exhibit 1.**

- Public Staff Pre-Marked 69 introduced as:
 - **Public Staff Fichera Redirect Exhibit 1.**

- Public Staff Pre-Marked 42 introduced as:
 - **Public Staff Fichera Redirect Exhibit 2.**

Summary of the Testimony of Barry M. Abramson

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

CAREER COVERING UTILITIES

I have more than 40 years covering the utilities industry. I have covered the U.S. utilities sector from the investment side for more than 40 years. From 1977 through 2002, I worked for various Wall Street investment banking firms in the equity research department. From 2002 through 2016, I worked in two large money management firms as an analyst and portfolio manager, managing large portfolios that invested in the stocks and bonds of U.S. electric, gas and water utilities. I joined Saber Partners in 2016.

I have covered Duke Energy and its predecessor companies for more than 40 years.

UTILITY INVESTORS ARE RISK-AVERSE

Regulatory risk is always a consideration because investors understand that utilities are regulated monopolies. I believe that achieving the best outcome for ratepayers is good for relations between the utility and its regulators, and thus it is a positive for investors. Long-term investors understand the give-and-take of utility regulatory proceedings. This is of particular importance for investors in Duke Energy and its subsidiaries, because of the holding company's estimated \$58 billion 5-year capital spending program. I estimate that 40%-50% of this capital spending will be invested in Duke Energy's two North Carolina utilities, combined. I believe that such a large amount of rate base growth could require the North Carolina subsidiaries to file for rate increases on a regular basis.

**THE PUBLIC STAFF AND ITS INDEPENDENT FINANCIAL ADVISOR AS FULL AND
EQUAL PARTICIPANTS ON THE BOND TEAM**

Should investors be concerned that there might be an impact on the North Carolina regulatory relationship, if the holding company does not allow the NCUC and Public Staff's independent advisors to participate on the bond team, in the same way that the Florida public service commission and its independent advisors participated in the 2016 issuance of ratepayer-backed bonds for Duke Energy Florida?

I believe that the Public Staff and its independent financial advisor, should be a full and equal participant on the bond team. The Public Staff was directly created by law, to protect the interest of ratepayers in North Carolina. The principal and interest on ratepayer-backed bonds are the direct obligation of the ratepayers, and not an obligation of the utility that benefits from the proceeds of the bond sale.

PUBLIC STAFF ROLE

I don't regard the Public Staff as an intervenor. In more than 40 years of following the regulated utility industry in the U.S. I have looked at hundreds of utility rate cases and other regulatory proceedings. In nearly every case, there were outside intervenors, pursuing a narrow agenda. The Public Staff in North Carolina is not an outside intervenor. The Public Staff was established by law.

NC Gen. Stat. § 62-15 ("Office of executive director; public staff, structure and function") provides in-part:

6 (d) It shall be the duty and responsibility of the Public Staff to:

(3) Intervene on behalf of the using and consuming public, in all Commission proceedings affecting the rates or service of any public utility.

ROLE OF INDEPENDENT FINANCIAL ADVISOR(S)

Using an independent financial advisor, acting solely in the interest of ratepayers, would result in the greatest possible savings to ratepayers. Furthermore, this should satisfy the goals of the Commission and the Public Staff. The independent advisor is not a beneficiary of the bond offering, and thus can be truly independent.

This is the first of many storm damage cost-recovery bond issuances in North Carolina. Many studies by climate scientists and meteorologists predict that frequency and severity of storms will increase. I have included three exhibits that discuss this issue, including two that specifically focus on North Carolina and the Southeast Region of the U.S. I could have included dozens more.

Therefore it is important to get it right the first time and create a model for future issuances of storm damage cost-recovery bonds. I believe that the costs of damage from future storms will continue to increase, due to: Climate Change, Customer Growth, Inflation, Work From Home Trends, and Electric Vehicle Market Growth And EV Related Infrastructure.

Stock and bond investors have increased their analysis and concern of the risk of climate change. This is a major consideration for most institutional investors today, and it was not a major concern to most of them, only a few years ago. For coastal utilities, like DEP this is extremely important. For DEC, whose territory is not far from the coast, I believe it is also a key factor. I have included one exhibit in my testimony about how investors are incorporating climate change risks into their decision-making process.

The ability of a utility to use ratepayer backed bonds to recover storm damage costs is considered a factor that reduces overall investment risk. This is another

important reason why I believe that it is important to successfully complete this particular financing, the first such financing in the state of North Carolina.

RATEPAYER-BACKED BONDS ARE DIFFERENT FROM TRADITIONAL BOND

OFFERINGS

The Commissioners, the Commission Staff, and the Public Staff, all will benefit from being fully involved in the structure, pricing and marketing of this ratepayer-backed bond issue. This is the first of many such bond issuances likely in the state. Knowledge will be gained by all parties from full participation on the Bond Team. The active involvement of the Independent Advisor will facilitate the spread of knowledge and make the experience more worthwhile.

This concludes my summary.

Summary of Testimony of Joseph Fichera
Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

My testimony focuses on the unique situation this Joint Petition creates for the Commission to consider. Close to \$1 billion is proposed to be raised, and the natural question for the people who will be responsible for paying it back is — “at what cost”?

The Commission is being asked to use its powerful regulatory authority in ways that have not previously been done in North Carolina. It will create a bond of unusual strength, a completely separate credit from the Companies. The Companies do not pay back the bonds; the ratepayers do directly with an irrevocable charge on their monthly bill. Moreover, this proceeding will establish a template for future issuances of storm recovery bonds, as more damaging hurricanes are expected to occur in North Carolina.

In addition to my testimony, the Saber Team is presenting in-depth testimony from former top utility and corporate finance executives (former utility CEO, CFO and Treasurer), a former state utility regulator who oversaw establishment of another Ratepayer-Backed Bond program as well as from an independent modeler of Ratepayer-Backed Bonds and a former utility equity analyst. These people – with decades of experience - all agree that Ratepayer-Backed Bonds are unique and require certain best practices to achieve the lowest cost to the customer transaction. Our experience says that three simple “best practices” should be followed to achieve the lowest storm recovery charges for ratepayers.

1. Ratepayer representation
2. A clear decision-making standard
3. Independently verified written certifications

The goal of the financing order is for the Commission to get the lowest cost of funds available in the capital markets at the time any storm recovery bonds are priced. Cost matters. If cost did not matter, then the North Carolina General Assembly could have allowed the Companies to sell bonds at whatever rate the professional judgement of the underwriters and investors wanted. But the General Assembly did not say that because cost does matter.

The capital markets are often thought of as a “black box” of buyers and sellers rapidly exchanging millions of dollars. They are thought to produce efficient results because each market participant pursues its own economic interest, with full knowledge and understanding of each transaction, so that prices are determined through “perfect competition” based on a free flow of information. However, my experience is that this is not the case for the capital markets in general or in the market for securitized storm recovery bonds in particular.

Ratepayer Representation. All top-rated securities, even AAA-rated securities, do NOT price the same; there are differing views. Nothing is automatic in the capital markets except that self-interest rules. The economic interests of the Underwriters and the Companies will not necessarily align with the interests of ratepayers. As with any publicly-offered securities, the Underwriters will represent their own economic interests, and the Companies will represent their own interests. Unless the Commission acts to create a process involving Public Staff and the Commission, the results are likely to be skewed against ratepayers’ interests. This will affect the pricing, the transaction documents and every aspect of the deal.

Nothing will occur without the hard work and collaborative efforts of all parties involved. The Companies, the Public Staff and the Commission can work together. They can create the balance necessary to manage competition among Underwriters and investors. Decisions affecting ratepayers should be made in consultation with an independent advisor with experience in this unique segment of the capital markets and with a specific and direct fiduciary duty to ratepayers. Public Staff witness Schoenblum describes this best practice in more detail.

A clear decision-making standard. This is critical. The standard should be the best possible deal for ratepayers at the time of pricing, the lowest possible cost of funds that maximizes present value savings to customers. Anything less allows for less-than-optimal results. Why? Very simply, without a lowest cost, best price present value standard, there is little incentive for any additional effort and hard work. The bonds can be priced quickly and move on.

But, the simple facts are that unless a market participant negotiates hard on its own behalf with Wall Street, across the table from those sophisticated and large investors with differing views, that market participant will leave substantial amounts of money on the table. Each side is looking out for its own economic interests. The Underwriters and investors want the best deal for themselves. Other market participants must negotiate equally hard and be equally diligent to arrive at a fair transaction that achieves the lowest cost to ratepayers and is fair value to the investor.

So, without a clear standard and a negotiating position that includes potential for the issuer and ratepayer representatives saying “no” when evaluating offers, Underwriters and investors will have the negotiating leverage to dictate a final cost to ratepayers.

Remember, the best way for a homeowner to lose control of the sale price of her house is for her to tell prospective buyers that she must sell her house today because she really needs the money now. Pricing leverage quickly shifts.

The third and final element of “best practices” is a basic business principle — “put it in writing” — written certifications. The key transaction participants — the Companies, Underwriters, and an independent financial advisor — should deliver to the Commission independent written certifications, without material qualifications, confirming that what they have done has in fact led to the lowest cost of funds and the lowest storm recovery charges consistent with market conditions at the time of pricing. With these confirming certifications in hand, the Commission can make the final “go, no -go” decision.

Any prudent person would want it in writing. For example, investors want documentation before they give up their money. They do not rely solely on oral representations before investing. With Sarbanes Oxley and a heightened need to maintain public confidence in business, written certifications have become a part of normal business “best practices.”

These best practices were successfully implemented with Duke Energy for Florida ratepayers on a similar transaction. North Carolina ratepayers deserve no less.

This completes my summary.

Summary of the Testimony of Steven Heller

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

I am owner of Analytical Aid, Inc., a consulting company. I have approximately 25 years of investment banking experience at firms including Merrill Lynch, Credit Suisse, and Bank of America. My primary responsibilities were structuring asset-backed securities (ABS) such as mortgage (residential and commercial) and non-mortgage (student loan, pharma royalty, auto, property-assessed clean energy (PACE)) collateralized financings and developing models used in that structuring. I have also structured seven (7) issues of Ratepayer-Backed Bonds (4 while at an investment bank and 3 as a consultant). I was the structuring/financial modeler for the Duke Energy Florida \$1.294 billion Ratepayer-Backed Bond offering that received top ratings from Moody's, S&P and Fitch. It was also one of the longest duration bonds ever structured – 20 years to scheduled final maturity. I worked directly for Tom Heath of Duke Energy and interacted with Saber Partners as the financial advisor representing the ratepayers.

There are two items I want to highlight from my testimony:

- 1. It does a disservice to Ratepayer-Backed Bonds – and the ratepayers who must pay their costs - to treat them as ABS.** Ratepayer-Backed Bonds are different from traditional ABS in all material ways that are of concern to investors. ABS are typically described with scenario analyses that certainly include prepayment risk and might also include risk of loss. Even AAA-rated ABS with little or no risk of loss trade at a wider spread (higher) than AAA-rated corporate securities like Johnson & Johnson and Exxon, at least in part, because of variability in the timing of principal return. But, AAA-rated Ratepayer Backed Bonds have no material risk of loss or payment variability

because of the frequent legislatively-mandated and Commission-enforced true-up mechanism. Investors can expect to receive the scheduled cash flows with near perfect certainty.

2. **From my personal experience I have seen that ratepayers interests are best served when independent advisors are involved directly in overseeing the structuring process.** The lowest cost to the ratepayer may not be the desired structure for the underwriters. At an investment bank, we may have had prepared a preliminary structure with a 2-year weighted average life tranche of bonds, and I would go to my bank's traders and say "here's a structure with a 3-year weighted average life tranche of bonds with all-in execution that is 1 basis point lower." They're very likely to say something like: "We already see good appetite for the 2-year weighted average life tranche and 1 basis point is a rounding error" and I might not disagree with them. But somewhere, maybe at 2 or 3 basis points, they might still think we're at a "rounding error," and an independent advisor will be advocating for the lowest cost to the ratepayer. On short maturities, a few basis points may have limited impact, but with longer maturities like 10-, 15-, or 20-year scheduled final maturities, even one basis point can be significant.

Summary of Testimony of Rebecca Klein, Principal, Klein Energy LLC

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

Utility customers have the potential to realize meaningful savings if specific actions, practices and processes are undertaken through the life-cycle of stages of a Ratepayer-Backed Bond (RBB) program. The North Carolina General Statute contemplates a lowest storm recovery charge standard, very similar to the statutory provisions in Texas. Adherence to the lowest cost standard results in benefits to the ratepayer, at no cost to the utility. Texas completed three RBB transactions during my tenure as a commissioner of the Public Utility Commission of Texas (PUCT) for approximately \$2.5 billion. These transactions established the baseline for the program. The practices that we undertook resulted in an average ratepayer savings for the three transactions of \$23 million nominal and \$17 million net present value, as compared to the pricing of other RBBs during the same time frame. The actions and processes we developed and implemented that resulted in these bonds may be beneficial to the North Carolina Utilities Commission. In this spirit, I offer highlights below of the actions undertaken in Texas that resulted in a superior outcome in terms of transaction cost savings to ratepayers.

Ensuring Ratepayer Interests Are Represented at Every Stage of the Transaction

- The PUCT took an approach of being actively engaged in implementing the terms, conditions and provisions of each phase of the transaction process, *i.e.* the structuring of the bond; the marketing of the bond; and the pricing of the bond. To engage the utility, underwriters and investors effectively, the PUCT was supported by the special expertise of its financial advisor. This allowed the commission to receive timely information, and make decisions

in real-time on particular matters. For example, the PUCT noticed a hearing within two business days after pricing for the purpose of considering whether to issue a stop order if the PUCT was not convinced that the lowest transition bond charge objective in fact had been achieved. The PUCT reviewed the marketing and pricing information in real-time so that the PUCT's hands would not be tied as a practical matter. This enabled the commission to have a framework in which to make decisions on pricing optimally, in a timely way. Ex-post information was not satisfactory.

- In Texas, the PUCT was a joint decision-maker with the sponsoring utility in all matters relating to the structuring, marketing and pricing of the "transition bonds". We expected the utility to work in a collaborative basis with the PUCT staff as well as with the PUCT's independent financial advisor to help ensure a successful transaction at the lowest "transition bond charges" to ratepayers. There is no reason why ratepayer interests and the utilities' interests cannot be aligned in light of the fact that any savings that could benefit ratepayers do not affect what the utilities will receive as part of the securitization amount necessary to recover storm damage costs on behalf of its ratepayers. On the other hand, the interests of underwriters and investors are not aligned with the ratepayers, and therefore it is imperative that the ratepayers' interests be represented at the negotiating table.

Codifying Certain Provisions in the Financing Order

- The statutory requirements in Texas provided that the "structuring and pricing" of transition bonds result in the lowest transition bond charges consistent with market conditions. The PUCT went an extra step to require in its Financing Order that the *marketing* of the bonds also be incorporated. North Carolina has a statutory provision (N.C. Gen. Stat., Sec. 62-172(b)(3)b), which directs the North Carolina Utilities Commission, similar to the Texas commission, to include in its Financing Orders "[a]ny other conditions not otherwise inconsistent with this section that the Commission determines are appropriate." Given this authority, the PUCT felt that it was

important to insert “marketing” as a function of lowering transition bond charges because the manner in which the bonds would be marketed would have a strong impact on pricing, and ensure lower “transition bond charges.”

- The Financing Orders in Texas directed the financial advisor to be actively engaged throughout the transaction process in order to ensure the greatest opportunity to meet a lowest cost transaction standard. Examples of the proactive initiatives the independent financial advisor undertook to help us reach our “lowest transition charge” mandate include: 1) insisting that any servicing fees and administration fees in excess of actual incremental costs be rebated or credited to ratepayers; 2) identifying any potential conflicts that may arise between the utility, the underwriter and the utility’s advisor; 3) participating fully and in advance in all aspects of structuring, marketing and pricing the “transition bonds”; 4) challenging any decision it believes might not result in lowest transition bond charges to ratepayers; and 5) requiring certifications from the Companies, the bookrunning underwriter(s) and the PUCT’s financial advisor that the structuring, marketing and pricing of the transition bonds in fact resulted in the lowest bond charges consistent with market conditions at the time the transaction priced and the terms of the Financing Order.
- Although the financial advisor (Saber Partners) in this instance is not supporting the Commission, the financial advisor is supporting Public Staff who represents ratepayers. Similarly, the financial advisor in Texas lent its expertise to the PUCT given that the agency had purview to protect customers of electric services consistent with the public interest.
- The Texas Financing Orders also required the utility to file a detailed set of analyses and representations called an “issuance advice letter” (See Klein Exhibit 1) about the pricing of the bonds and documenting the benefits of the transaction to ratepayers.

Unity of Purpose

- There is no reason why the utilities, the underwriters, the Commission and the interests of the ratepayers cannot have a unity of purpose in striving to reach a “lowest storm recovery charge” standard. Any savings that inure to ratepayers materializing from an efficient RBB Program do not diminish the securitized costs that the Commission determines is required for storm reparations. Therefore, utility and ratepayer interests are not inherently in disharmony.
- Maximizing the chance of a collaborative and collegial process rests on the Commission clarifying that the ultimate decision-making authority for all aspects of structuring, marketing, and pricing the proposed bonds rests with a designated member of the Commission. In addition, the Commission should be clearly dedicated to having the day-to-day decision-making rest with an ensemble that includes designated Commission Staff, the Public Staff and its respective financial advisors, and the utilities. As a collaborative, this group would represent the voices of all interested parties and can, together, help achieve the “lowest storm recovery charge” mandate through robust and transparent negotiation.

This completes my summary.

Summary of Testimony of Brian A. Maher
Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

My main focus will be the appropriate relationship between (i) the North Carolina Utilities Commission (Commission) and the Public Staff and its independent experts and advisors, who I believe are best placed to be the main representatives of the ratepayers' economic interests, and (ii) the other key parties in the transaction, essentially Duke Energy Carolinas, LLC (DEC) and Duke Energy Progress, LLC (DEP and, together with DEC, the Companies), the Companies' advisors, and the investment banks that will likely underwrite the storm recovery bond issue.

A key concept for the Commission to consider is whether or not the parties involved have what is often referred to as a "fiduciary relationship" as opposed to companies', underwriters' or advisors' acting primarily in their own financial interest. In broad terms, a service provider that has a fiduciary responsibility to its client commits to act in the client's best interests to the exclusion of any contrary interests. Where a fiduciary relationship exists, the client should be comfortable that the service provider is looking out for the client's best interests. The issue of whether a fiduciary relationship exists impacts what the Commission should consider in deciding how to evaluate information it receives from different parties to the proposed transaction. In my experience, for example, underwriters claim they have no fiduciary relationship to issuers. Underwriting agreements prepared by counsel for the underwriters now typically include a specific declaration that the

underwriters have no fiduciary relationship with the issuer. Issuers frequently are asked to acknowledge this affirmatively in the underwriting agreement.

Bond underwriters will typically propose an offering process, including bond pricing, whereby the underwriters use their “professional judgment” in establishing price guidance and change that price guidance “solely in their professional judgment.” This is what the Companies’ witness Atkins has testified. However, the underwriters act for their own benefit and cannot always be counted on to act solely on behalf of the Issuer. Pricing is arguably the most important component of offering securities in the market. I believe this is a compelling reason why bond issuers need to be very active in the offering process: to protect their own interests.

In response to data request questions inquiring if underwriters of securities have a duty to the issuer of those securities and if it is a fiduciary duty, the Companies’ witness Heath stated that the underwriters do not have a fiduciary duty to the issuer. In responding to PS DR 2-2(g), witness Heath acknowledges that the engagement letters between the Companies and Guggenheim Securities and Atkins Capital do not create a fiduciary relationship between the parties.

In contrast, as financial advisor to the Public Staff, Saber Partners considers itself as having a fiduciary duty to North Carolina ratepayers.

The storm recovery bond transaction is different from normal corporate debt issues in which the issuer has a direct interest in minimizing the cost of the transaction in order to maximize economics for its shareholders. For traditional utility debt issues, as well, incentives exist to minimize the costs of the transaction.

Here the Companies propose that the storm recovery bonds will be issued by special purpose entities (SPEs). This is simply a mechanism to facilitate the transfer of funds from the ratepayers to the Companies, while the ratepayers alone will ultimately bear all transaction costs and all costs of repaying the storm recovery bonds. The Companies will receive net proceeds of the bonds to recover previously incurred costs. While I do not doubt that the Companies would desire that its ratepayers incur low storm recovery charges, the Companies' main motivation is to receive the debt proceeds in a timely, efficient manner. Therefore, the Companies do not share the same incentives to achieve the lowest overall cost of funds. It is left to the Commission and the Public Staff to ensure that the ratepayers achieve the lowest overall cost of funds for the bonds and the lowest storm recovery charges consistent with market conditions at the time the bonds are priced. I believe that they need to be fully involved in working in a cooperative way with the Companies and the Companies' advisor to achieve that objective. That will require optimal structuring and marketing of the storm recovery bond issue.

I believe that the Bond Team for the storm recovery bond issue should consist of the Companies, the Companies' advisor (provided such advisor is not one of the banks acting as underwriter for the transaction), the Commission, either directly or through a designated staff member(s), the Public Staff, and the independent advisors and counsel. I believe it is very important for the lead Commission representative to be closely involved in the project. There are many complexities, and this is probably not the type of work that Commissioners

undertake on a regular basis. It is important that the Bond Team operate independently and entirely in the interest of the ratepayers and not include any of the underwriting banks due to their inherent conflict of interest discussed above. All members of the Bond Team should have a fiduciary relationship with either the Companies, the Commission, or the Public Staff. Decisions of the Bond Team should be a shared responsibility of its members, with the Commission's representatives in a position to make the final decision on a timely basis, often in real time during the final pricing process, in the event of any disagreements among Bond Team members.

In my many years overseeing ExxonMobil's capital markets activities, I learned that bond issues could almost always be done at lower rates than the best market preliminary indications given by the banks. This was true despite the fact that ExxonMobil was a well-known and coveted "AAA"-rated debt issuer. Active involvement by ExxonMobil to create competition among the banks and to demand the best execution consistently added value.

It is also true that all "AAA" and "AAA(sf)" rated debt is not viewed alike by investors in the debt capital markets. For example, when I worked at ExxonMobil, "AAA"-rated ExxonMobil or Federal Agency credits would command better pricing than most "AAA"-rated structured debt securities which were backed solely by a pool of intangible contract rights such as mortgages or credit card receivables.

In summary, the proposed storm recovery bonds should achieve a "AAA(sf)" rating and perform well in the market. But superior performance is not automatic since all "AAA" and "AAA(sf)" rated bonds do not trade alike. The key takeaway

should be that, while factors such as underwriters' professional opinions are valuable, underwriters do not have any fiduciary responsibility to the ratepayer. Similarly, the Companies' primary responsibility is to their own shareholders. Therefore, the Commission, the Public Staff and their independent financial advisor(s) are in the primary position of having to look out for the ratepayers' best interests. It is critical that they play an active role in all aspects of the transaction. They must be willing to invest all the time necessary in the structuring and take an aggressive stance during the marketing process to capture the lowest cost of financing and the lowest storm recovery charges for the ratepayers. This should involve full participation in the transaction with the Companies and the bond underwriters and, if required, timely decision making by the Commission to resolve any potential financing issues in the ratepayers' best interests.

This completes my summary.

Summary of the Joint Testimony of Michael C. Maness and Michelle M. Boswell

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

The purpose of our testimony is to present the Public Staff's position on certain matters related to Docket No. E-7, Sub 1243 and Docket No. E-2, Sub 1262, the Joint Petition for Financing Orders filed with the Commission by Duke Energy Carolinas, LLC (DEC) and Duke Energy Progress, LLC (DEP).

In our testimony, we addressed five basic topics: (1) Statutory Basis for the Petition and Specific Relevance to our Testimony; (2) Relevant General Rate Case Proceedings; (3) Costs to be Securitized; (4) Conditions of the General Rate Case Stipulations Affecting Test of Quantifiable Benefits; and (5) Application of the Net Benefit Test. The Petition was filed with the Commission pursuant to N.C. Gen. Stat. § 62-172. *Financing for certain storm recovery costs*, and includes the 2018 and 2019 storms originally proposed by the Companies for deferral and amortization in each Company's last general rate case, and subsequently removed from O&M and capital costs as part of Stipulations with the Public Staff in each case. Additionally, the Companies have included in the amounts to be securitized upfront and ongoing financing costs, servicing fees, and other costs related to the securitization of the storm costs as provided for in the Statute. The Public Staff has made several recommendations regarding the accounting for all of the costs proposed by the Companies for inclusion in the securitization filing, including (1) provisions if the Stipulations are not accepted by the Commission in each Company's general rate case

proceedings currently pending before the Commission, and (2) provisions to limit amounts charged to ratepayers to actual and reasonable storm recovery costs and financing costs.

Furthermore, our testimony details the conditions of each Company's general rate case Stipulations that affected the test of quantifiable benefits as well as the application of the net benefit test. We agreed that in the present case, securitization does provide quantifiable benefits to the ratepayers.

The Companies and the Public Staff have entered into an Agreement and Stipulation of Partial Settlement, which settles all accounting issues discussed in our testimony.

This concludes our summary.

Summary of the Testimony of William Moore

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

I retired in 2011 as President and CEO of Westar Energy after a 33-year career in the Electric Utility industry. Most of my career was in the Financial area as Finance Assistant, Treasurer, VP Finance, EVP Finance and CFO. During those years, I negotiated terms and conditions for the issuance of over \$3 billion of both investment grade and non-investment grade securities, \$1.5 billion of bank facilities, over \$1 billion of equity and several other ways of sourcing funds such as a power plant sale/leaseback, sale of accounts receivable, and floating rate pollution control bonds. My investor relations responsibilities included many meetings with analysts and investors to provide information on our company and to hopefully raise interest in our securities.

The purpose of my testimony, as a former utility CEO and CFO, I support the need for a Bond Team. It is the right thing to do for ratepayers. It is also common sense given the unique nature of these Ratepayer-Backed Bonds. The Bond Team should include active Commission, Staff and Public Staff representation with its independent advisor in all aspects of structuring, marketing and pricing the proposed storm recovery bonds.

Most importantly, the structuring, marketing and pricing of Ratepayer-Backed Bonds are more complex than that of "plain vanilla" utility bonds, such as first mortgage bonds. This is because ratepayers are directly responsible to repay the bonds and associated financing cost through a nonbypassable, automatically

adjustable rate component, in this case a “storm recovery charge,” with the Commission required to give up future review.

It is a good business practice, and common sense, that the party directly responsible for repaying the bonds (ratepayer) should be “at the negotiating table” throughout the many steps in structuring, marketing and pricing the Ratepayer-Backed Bonds. Everything that occurs in the structuring and marketing of the bonds leads into the most important part/bottom line of this transaction: **Pricing**.

My 33-year experience with Wall Street on many securities offerings has shown me it is not always wise to rely solely on the underwriters’ “professional judgment” when pricing bonds. Wall Street wants all sales force and investor inputs funneled through the Bookrunning Manager/Underwriter(s). Westar had an investor relations team that often talked to owners of our securities directly before and after securities offerings. For Ratepayer-Backed Bonds, ratepayer representatives should have eyes and ears on what the underwriters are saying to and hearing from potential investors before floating “price talk”.

Because the Financing Order is irrevocable, the Commission must give up its regular ongoing review of these costs. The Bond Team approach would provide independent confirmation that the lowest storm recovery charge in fact was achieved. A Bond Team that includes Commission, Staff, and Public Staff representatives should have the mandate to be involved in first-hand discussions with the sales force and investors to be effective in helping to achieve the lowest storm recovery charge benchmark.

This completes my summary.

Summary of the Testimony of Hyman Schoenblum

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

I am a Senior Advisor to Saber Partners, LLC (Saber). Saber is the independent financial advisor to the Public Staff in the proceeding regarding the issuance of Storm Recovery Bonds by Duke Energy Carolinas and Duke Energy Progress.

I have 35 years of utility financial experience. I was employed by Consolidated Edison Company of New York (Con Ed) in various senior financial capacities such as Treasurer, Controller and Vice President of Strategic Planning. I was also a key member of the investor relations team and met regularly with investors and bankers. I testified in numerous rate cases as well as proceedings relating to M&A transactions initiated by Con Ed.

With regards to Ratepayer-Backed Bonds, I submitted direct testimony in 2015 on the Duke Energy Florida (DEF) \$1.3 billion transaction which refinanced the unrecovered costs of a nuclear power plant. In 2018, I submitted testimony in a California proceeding regarding the risks and benefits of securitization.

My testimony in this proceeding addresses three major issues:

1. The need for Commission and Public Staff involvement in all aspects of the issuance of Ratepayer-Backed Bonds.
2. Differences between incentives that exist for standard utility bond issuances versus Ratepayer-Backed Bonds.
3. The need for a fiduciary relationship between the various participants in the issuance of Ratepayer-Backed Bonds.

Commission Involvement

I believe that all parties involved in the issuance of these Ratepayer-Backed Bonds should work collaboratively and in a cooperative fashion to structure the transaction. This will ensure investors and ratepayers that their interests are being protected and will produce a successful transaction with the greatest economic benefit. Since ratepayers are effectively the ones who will repay the debt to bondholders, the Commission must ensure that their interests are best served through enhanced regulatory oversight.

The most efficient manner to achieve these goals is through a “Bond Team” that includes all participants, including the Public Staff, its independent financial advisor and the Commission. This approach worked very effectively in the above-mentioned DEF transaction which was praised by the markets and the Florida Commission staff as being an efficient process, yielding superior results. It also worked well in other states as delineated in my testimony. My motto is: why tamper with success?

Differing Incentives

As a former Treasurer, I can attest to the regulatory incentives that standard utility debt issuances have. I was always worried that the New York Commission would second-guess Con Ed’s marketing or pricing in future rate proceedings. Thus, we were extremely careful that we should not be exposed to such potential oversight, both in terms of the interest rates and fees paid to underwriters.

Ratepayer-Backed Bonds do not have these regulatory incentives. The North Carolina Utility Commission (the “Commission”) cannot second-guess the most important aspects of the storm recovery bond transaction in future rate proceedings. The State has

pledged not to interfere. Recovery of issuance costs and interest costs are guaranteed. The True-up ensures full cost recovery.

As such, it is extremely important that “we get it right the first time”. The issuance needs to be handled in an efficient manner, yielding the lowest cost possible. Adopting the “best practices” recommended by Saber and having all parties work in a collaborative manner, will, in my opinion, create the appropriate incentives for a successful transaction. My testimony lists several states that have adopted these “best practices” in their financing orders. I recommend the same in the instant proceeding.

Fiduciary Relationship

I concur with Witness Maher that the various parties to this transaction should have a fiduciary relationship with either the utilities or the Commission. That entails that the Companies and the Commission need to receive conflict-free advice from the experts. The parties need to ensure that conflicts of interest are avoided. For example, utilizing an underwriter to also provide consulting advice might yield a conflict; even though Witness Heath believes that structuring advisors “are often in the best position” to be the lead underwriter.

Lastly, it is my opinion that the form of Issuance Advice Letters (IAL) outlined in the proposed Financing Order filed by the Companies needs to be strengthened to include certification that the structuring, marketing and pricing have, in fact, resulted in the “lowest storm recovery charge” consistent with market conditions at the time the storm recovery bonds are priced and based on information available through the date of pricing. Furthermore, while the IAL provides some assurance, the Commission should enhance the protections needed to ensure a conflict-free process by its involvement in the

complete process in issuing these bonds and in requiring certificates from not only the Companies, but also from the bookrunning underwriter(s) and the Public Staff's financial advisor. My testimony delineates a number of personal experiences where investment banker assurances were not sufficient in protecting the transaction.

This concludes my summary.

Summary of Testimony of Paul Sutherland
Docket Nos. E-2, Sub 1262 and E-7, Sub 1243

The purpose of my testimony is to discuss and demonstrate how ratepayers benefit from ratepayer backed bond (RBB) financing, and more specifically, ways in which that benefit can be measured and maximized through optimal structuring and application of “best practices” by a properly structured bond team. My testimony focuses on the quantitative analysis of structuring and pricing decisions. By comparing past RBB pricings both with and without best practices and also by pointing out some misleading testimony by Companies’ witnesses, my testimony demonstrates the importance of having on the bond team expert representation on behalf of the ratepayer.

With an undergraduate degree in electrical engineering from Cornell University and an MBA from the University of Chicago, I worked for over 20-years with Florida Power & Light Company, primarily in the area of corporate finance. I then spent another 20 years with Saber Partners, LLC involved in 13 utility securitization transactions raising over \$9 billion in an advisory role to public utility commissions on behalf of ratepayers. My particular role as Senior Advisor has been in the area of quantitative analysis.

The biggest net present value (NPV) savings in a utility securitization result from the fact that rating agencies (Moody’s, S&P, Fitch) generally treat utility securitization debt as off-balance sheet despite the fact that it may not be so for other accounting or regulatory purposes. This is important because utilities set their capital structure (i.e. their ratio of debt to equity) based on what is necessary

to maintain an acceptable bond rating by the credit rating agencies. This means that utilities can issue securitization debt without having to issue a similar amount of equity to maintain what the rating agencies consider the proper debt to equity ratio. Without the need for that amount of equity, there is no associated income tax expense. Another large contributor to NPV savings from securitization comes from the fact that the revenue requirements are generally structured to be levelized like mortgage payments rather than declining as is the case with traditional utility revenue requirements.

With these savings factors intrinsic to all RRB financings in mind, there are 2 major aspects with which the bond issuer has some ability to affect the amount of additional ratepayer savings resulting from a well-executed securitization financing. The first is the interest rate on the bonds, and the second is the structure of the financing. Decisions on structure might include the maturity or weighted average life (WAL) of the bonds and the number and size of tranches or series of bonds. Both the interest rate and the structure are determined as part of the pricing process of bond issuance. Consequently, the extent to which the pricing process results in savings is determined by the efforts of the bond team prior to and at the time of pricing.

Interest rates are established based on a spread (in basis points, or hundredths of a %) to the rate on a benchmark security. By convention, asset-backed securities (ABS) are generally priced relative to the rate for interest rate swaps, while traditional corporate debt is priced relative to U. S. Treasury bond rates. Utility securitization bonds have usually been priced like ABS, based off a

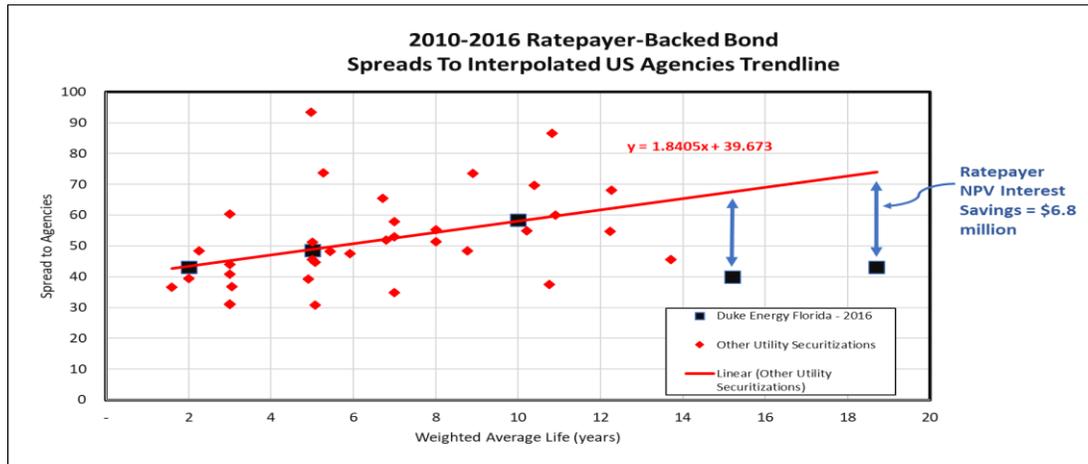
spread to swaps, but the Duke Energy Florida transaction of 2016 was priced using a spread to U. S. Treasury debt. In either case, the securitized debt should be priced relative to a security of the same WAL. If there is no such security, then it should be priced based on an interpolated rate between the 2 nearest (in years) benchmark securities.

While an issuer cannot control the interest rate on the underlying benchmark security at any point in time, the issuer has the ability to achieve attractive spreads to benchmark rates by effective marketing, educating investors about unusually attractive aspects of the RBBs, and by exercising good analytical and negotiating skills. However, in order to achieve the lowest cost for the ratepayer, the bond team should include a representative of the Public Staff or Staff's financial advisor, since that is who has the greatest incentive to protect ratepayer interests. This is most important with utility securitization issues because, unlike conventional utility debt, securitization debt is a direct obligation of the ratepayer and not the utility.

Interest rate savings relative to other securitization financings can be measured by comparing pricing spreads to benchmark rates for transactions over some reasonably stable period of time. Since the comparisons must be for similar WALs, a regression line can be used showing spreads versus WALs and then used to predict pricing spreads for any particular WAL tranche. The outcome for a transaction following best practices with active involvement of a ratepayer representative can be compared to the predicted pricing results based on all other

securitizations in the same general time frame to calculate the value (interest rate savings) from such best practices.

In addition to spreads used at time of pricing, spreads to other AAA debt securities, such as U.S. agency securities (e.g., the Federal Home Loan Bank or the Tennessee Valley Authority) can be used to judge success, both at the time of pricing and thereafter. Various exhibits to my direct testimony illustrate such



savings over a variety of transactions, as for example, Exhibit 7, below, showing interest savings in the Duke Energy Florida transaction in 2016 compared to all other RBBs from 2010 through 2016.

Sometimes additional savings can be generated simply by changing the number or size of the tranches in a securitization. An example is given from the Duke Energy Florida securitization in 2016 when, at the suggestion of the Commission’s financial advisor, a simple change from a 4-tranche to a 5-tranche structure resulted in an additional \$3 million NPV savings for ratepayers.

Another type of structural change involves extending the final scheduled maturity of the financing. In direct testimony, the Companies recommended a 15-year final scheduled maturity for both DEC and DEP despite the fact that a 20-year

structure offers substantially greater net present value savings. My testimony points out several problems with the Companies' analysis of a 20-year alternative structure and discusses why the Companies' financial advisor seems inclined to be dismissive of such alternative.

In addition to including Public Staff and/or their advisor as part of a bond team, there are three other changes suggested in the testimony. The first is to restrict the return on the capital subaccount held and managed by the bond trustee to just the actual earnings on investments made in the account rather than a return equal to the rate on the longest tranche of the financing. The second recommendation is to reflect in the financing order a requirement that all so-called "tail-end" collections of securitization revenues collected after the bonds have been paid off will be credited back to the ratepayers. The final recommendation is that, to the extent that actual, marginal servicing and administration costs incurred by the Companies are less than the assumed annual fee, those amounts will also be credited back to the ratepayer in a timely manner.

Besides these three recommendations, it is my recommendation that the Public Staff and its financial advisor have equal authority with the companies regarding all major decisions involving structuring, marketing and pricing the securities. Beyond that, the Commission should follow best practices as described by witness Fichera and other Public Staff witnesses.

This completes my summary.

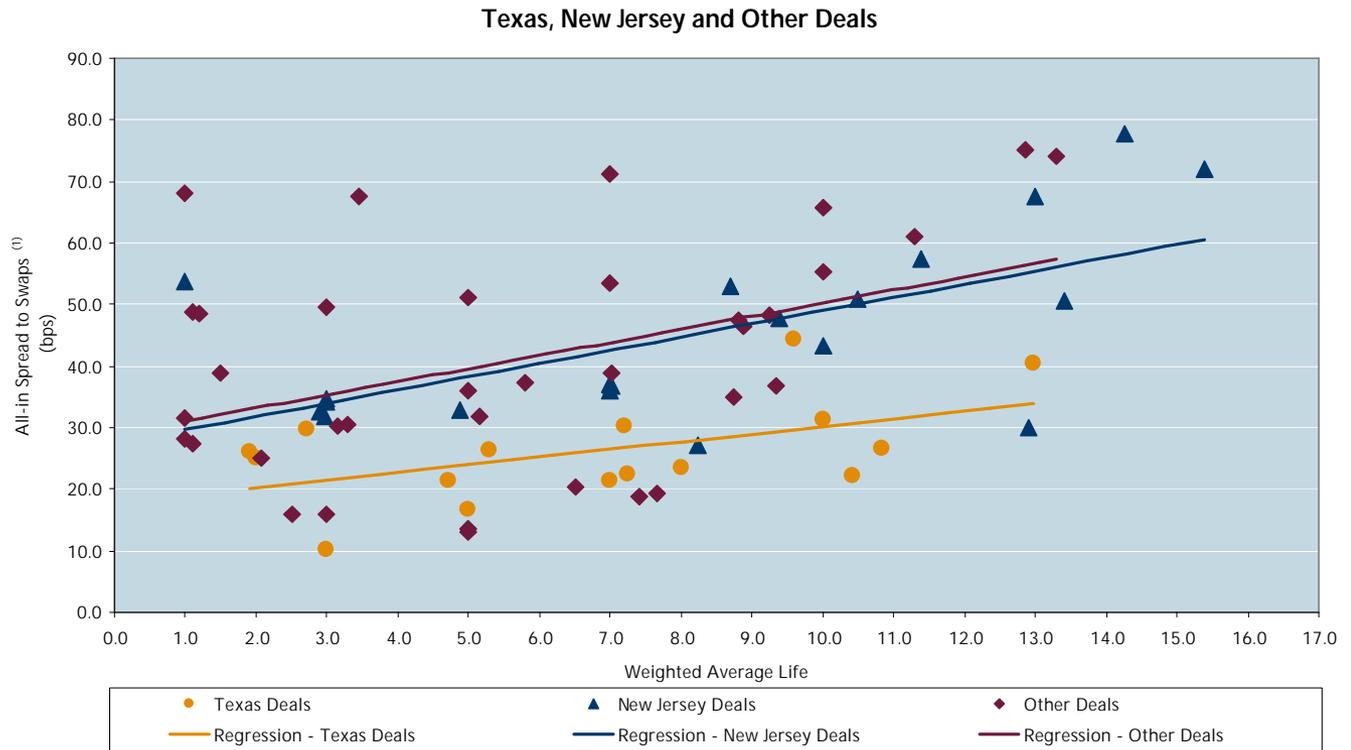


5. RRB Spread Summary

Offering Spread to Swaps vs. Weighted Average Life



All-in Spread to Swaps vs. Weighted Average Life



(1) All-in spreads include annualized underwriting and structuring fees.

Pre-marked Exhibit 69

Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

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In the Matter of:

4

DOCKET NO. 150171-EI

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PETITION FOR ISSUANCE OF
NUCLEAR ASSET-RECOVERY

6

FINANCING ORDER, BY DUKE
ENERGY FLORIDA LLC D/B/A DUKE
ENERGY.

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PROCEEDINGS: EMERGENCY MEETING

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12

COMMISSIONERS
PARTICIPATING:

13

CHAIRMAN JULIE I. BROWN
COMMISSIONER LISA POLAK EDGAR
COMMISSIONER ART GRAHAM
COMMISSIONER RONALD A. BRISÉ
COMMISSIONER JIMMY PATRONIS

14

15

DATE:

Thursday, June 16, 2016

16

PLACE:

Brevard County Government Center
Commission Room, Building C
1st Floor
2725 Judge Fran Jamieson Way,
Melbourne, Florida 32940

17

18

TIME:

Commenced at 12:33 p.m.
Concluded at 1:03 p.m.

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REPORTED BY:

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

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23

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25

1 APPEARANCES:

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4 Florida 33701, appearing on behalf of Duke Energy
5 Florida, Inc.

6 J.R. KELLY, PUBLIC COUNSEL, and CHARLES
7 REHWINKEL, DEPUTY PUBLIC COUNSEL, Office of Public
8 Counsel, c/o the Florida Legislature, 111 W. Madison
9 Street, Room 812, Tallahassee, Florida 32399-1400,
10 appearing on behalf of the Citizens of the State of
11 Florida.

12 ROBERT SCHEFFEL WRIGHT, ESQUIRE, Gardner Law
13 Firm, 1300 Thomaswood Drive, Tallahassee, Florida 32308,
14 appearing on behalf Florida Retail Federation.

15 SUZANNE BROWNLESS and ROSANNE GERVASI,
16 ESQUIRES, FPSC General Counsel's Office, and ANDREW
17 MAUREY, 2540 Shumard Oak Boulevard, Tallahassee, Florida
18 32399-0850, appearing on behalf of the Florida Public
19 Service Commission.

20 MARY ANNE HELTON, ESQUIRE, FPSC General
21 Counsel's Office, 2540 Shumard Oak Boulevard,
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23 the Florida Public Service Commission.

1 ALSO APPEARING:

2 JOSEPH FICHERA, SABER PARTNERS

3 DEAN CRIDDLE, ORRICK HERRINGTON

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P R O C E E D I N G S

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2 **CHAIRMAN BROWN:** Okay. Good morning and thank
3 you for joining us here today. This meeting is called to
4 order for the petition for issuance of the nuclear
5 asset-recovery financing order by Duke Energy. And at
6 this time I'd like to have staff read the notice.

7 **MS. BROWNLESS:** Thank you. By notice dated
8 June 14th, 2016, this time and place has been set for an
9 emergency meeting in Docket No. 150171-EI, petition for
10 issuance of nuclear asset-recovery financing order by
11 Duke Energy Florida, LLC.

12 **CHAIRMAN BROWN:** Thank you. And as I stated
13 just a second ago, there are people on the phone. I will
14 be taking appearances, so when we go to you, please -- if
15 you're on the phone, please note that you are appearing.
16 We'll take appearances starting with Duke Energy. And I
17 believe the microphone is working right there,
18 Ms. Triplett.

19 **MS. TRIPLETT:** Thank you. Good morning, Madam
20 Chairman, Commissioners. Dianne Triplett on behalf of
21 Duke Energy Florida.

22 **CHAIRMAN BROWN:** Thank you. We'll go with
23 Office of Public Counsel at this time.

24 **MR. REHWINKEL:** Charles Rehwinkel with the
25 Office of Public Counsel.

1 **CHAIRMAN BROWN:** Thank you. And you also have
2 J.R. Kelly here today.

3 **MR. REHWINKEL:** Yes, we do.

4 **CHAIRMAN BROWN:** Got to mention him.

5 (Laughter.)

6 Retail Federation.

7 **MR. WRIGHT:** Schef Wright on behalf of the
8 Florida Retail Federation. Thank you.

9 **CHAIRMAN BROWN:** Thank you.

10 PSC staff.

11 **MS. GERVASI:** Good morning. This is Rosanne
12 Gervasi appearing on behalf of Commission staff.

13 **MS. BROWNLESS:** Suzanne Brownless,
14 Commission --

15 **MS. HELTON:** Mary Anne Helton is also here with
16 Rosanne Gervasi on behalf of the Commission.

17 **CHAIRMAN BROWN:** Did you -- I didn't understand
18 that.

19 **COMMISSIONER BRISÉ:** It's Mary Anne.

20 **COMMISSIONER EDGAR:** Mary Anne.

21 **CHAIRMAN BROWN:** Mary Anne. Thank you. And go
22 ahead.

23 **MS. BROWNLESS:** Suzanne Brownless on behalf of
24 Commission staff.

25 **CHAIRMAN BROWN:** Thank you.

1 My understanding also is that we have Dean
2 Criddle on the phone. Is that correct? Dean Criddle,
3 are you on the phone?

4 (No response.)

5 And Joe Fichera.

6 **MR. FICHERA:** Joseph Fichera from Saber is
7 here, yes.

8 **CHAIRMAN BROWN:** Okay. Thank you. Is there
9 anybody else on the phone?

10 **MS. GERVASI:** Madam Chairman, Dean Criddle
11 should be appearing momentarily. We'll call him and make
12 sure he'll be calling in.

13 **CHAIRMAN BROWN:** Thank you. We will proceed,
14 though, to opening statements and Mr. Maurey.

15 **MR. MAUREY:** Madam Chairman, Commissioners,
16 thank you. Andrew Maurey on behalf of Commission staff.

17 **CHAIRMAN BROWN:** Andrew, could you please push
18 that closer and make sure it's on?

19 **MR. MAUREY:** How about this?

20 **CHAIRMAN BROWN:** Not that we can't hear you
21 right here.

22 **SPEAKER:** I have Dean Criddle on the line now.

23 **CHAIRMAN BROWN:** Thank you. Could you guys
24 please mute it while we hear opening statements by the
25 parties?

1 You may proceed.

2 **MR. MAUREY:** Thank you. Pursuant to the
3 financing order issued in this docket, the Commission has
4 had an opportunity to consider whether the structuring,
5 marketing, and pricing of the nuclear asset-recovery
6 bonds would result in statutory cost objectives, the
7 lowest nuclear asset-recovery charges consistent with
8 market conditions at the time of pricing, terms and
9 conditions of the financing order and other applicable
10 law, and the greatest possible customer protections.

11 If the Commission does not issue a stop order,
12 the Commission, without the need for further action and
13 pursuant to the authority under the financing order,
14 shall have determined that the requirements of Section
15 366.95, *Florida Statutes*, and the financing order have
16 been satisfied.

17 This meeting is optional. It will -- the deal
18 will go forward if we don't do anything, but we wanted
19 to have this opportunity to explain the work that went
20 into making this superior result possible. And with --
21 we have -- are in receipt of the opinion letter from the
22 financial advisor. I'd like to make a couple of
23 statements with respect to that.

24 **CHAIRMAN BROWN:** Please go ahead.

25 **MR. MAUREY:** Saber Partners is of the opinion

1 that the proposed structuring, pricing, and financing
2 cost of the bonds have a significant likelihood of
3 resulting in lower overall cost or would avoid or
4 significantly mitigate rate impacts to customers as
5 compared to the traditional method of financing and
6 recovering nuclear asset-recovery costs.

7 Saber Partners also is of the opinion that on
8 a reasonably comparable basis, the actual cost of the
9 nuclear asset-recovery issuance will result in the
10 lowest overall costs that were reasonably consistent
11 with market conditions at the June 15th, 2016, pricing
12 of the bonds and the terms of the financing order.

13 In addition, Saber Partners is of the opinion
14 that the transaction has achieved the greatest possible
15 customer protections reasonably consistent with the
16 terms of the financing act, the financing order, and
17 other applicable law.

18 Finally, Saber Partners is not aware of any
19 action or inaction which Saber Partners believes might
20 have caused the transaction not to achieve the statutory
21 cost objectives, the lowest nuclear asset-recovery
22 charges, and/or the greatest possible customer
23 protections. In summary, Saber Partners does not
24 recommend that the Commission issue a stop order.

25 With your indulgence, I would like to go

1 through a few slides that we've distributed prior to the
2 meeting.

3 **CHAIRMAN BROWN:** Thank you. I think now is the
4 appropriate time.

5 **MR. MAUREY:** All right. Thank you. Just go
6 over some of the details of this transaction that
7 resulted in significant savings to Duke Energy Florida's
8 customers.

9 On the first slide we talk about the total
10 financing cost of 2.72 percent. This is the lowest cost
11 in the history of investor-owned utility rate reduction
12 bonds. Now these bonds have maturities that went out.
13 Well, let me give you context. In the settlement that
14 allowed for the recovery of this regulatory asset, it
15 was contemplated that these charges would be recovered
16 over a period of 20 years through base rates. Through
17 this securitization, we were able to be true to the
18 20-year recovery period but significantly lowered that
19 cost to customers.

20 The investors that bought these bonds, they
21 bought -- did so at interest rates that were in line
22 with U.S. agency securities such as Tennessee Valley
23 Authority, Fannie Mae, Federal Home Loan Board, and some
24 of the largest, highest-rated global corporations such
25 as Johnson & Johnson and Exxon.

1 The transaction was benefited from an
2 extensive investor education effort, which included
3 contact both physically and over the phone with over
4 110 investors to build demand for this bond. This
5 effort involved Saber Partners, Commission staff, Duke
6 Energy Florida, and the underwriters that were brought
7 in.

8 The next slide shows a graphic presentation of
9 how this deal compared to other deals in this space. It
10 looked at all other ratepayer -- rate reduction bonds
11 that were issued between 2010 and 2015. And you can see
12 the higher line represents how those priced at the
13 various maturities relative to government agencies, and
14 the lower dotted line shows where the DEF bonds priced.
15 And I want to draw your attention really to the two
16 squares at the far right. You'll see that there are no
17 other dots out there for the other deals. That
18 represents the challenge that we faced in selling bonds
19 at the 15- and 18-year maturities to be true to the
20 terms of the settlement but build demand for those bonds
21 where others have not sold them in the past or at least
22 in the last five years.

23 The next slide, we wanted to highlight the
24 18-year maturity specifically because as -- when you
25 look at this, this is a comparison of how the DEF

1 project finance bonds priced relative to comparable
2 issues of these other names I mentioned. We priced
3 right on top of Tennessee Valley Authority. Tennessee
4 Valley Authority sells billions of debt. They're a
5 well-known issuer. DEF project finance didn't exist
6 more than six months ago. So we -- this was almost akin
7 to an initial public offering. We were able to do so
8 with the collaborative effort of Duke Energy Florida,
9 Saber Partners, staff, and the other outside counsels
10 that came together to make this successful. But this is
11 a strong signal that those efforts were successful.

12 And then finally I have two final pages. This
13 transaction was made possible due to a special
14 legislation that was enacted in 2015. When that
15 legislative process was ongoing, an illustrative example
16 was presented. And this page, page 4, is that example
17 where it was estimated that at that time the charge
18 would have been, through base rates, approximately
19 \$5.33 per thousand kWh. And if we did enter
20 securitization, we would have had a charge of
21 approximately \$2.91, resulting in nominal savings of a
22 little over 800 million and net present value savings of
23 a little over 600 million. Those were the expectations.

24 But on the last slide, when we got into the
25 issuance, we were able to motivate the underwriters to

1 challenge those spreads, to tighten the interest rates,
2 and we ended up resulting in a charge of \$2.84 per
3 thousand kWh, which resulted in comparable nominal
4 savings but higher net present value savings, net
5 present value savings of 684 million directly to the
6 benefit of customers.

7 So this was a, as I say, a very successful
8 effort. A lot of people were involved. And it -- we
9 would have not had this result, though, without the
10 tireless efforts of our financial consultants, Saber
11 Partners and Joe Fichera in particular, and our outside
12 counsel, Dean Criddle of Orrick Herrington. And I want
13 to thank them for their involvement on behalf of this
14 transaction. I'm available for any questions.

15 **CHAIRMAN BROWN:** Thank you, Mr. Maurey. And
16 just to close up your summary, your recommendation would
17 be --

18 **MR. MAUREY:** Oh, my recommendation is that you
19 do not issue a stop order. Thank you.

20 **CHAIRMAN BROWN:** Thank you. That was just for
21 the record.

22 And before we get to the parties to give them
23 an opportunity to speak, I do want to -- I mean, it goes
24 without saying -- to thank staff, the entire Bond Team,
25 Duke Energy, Saber Partners. Commissioner Graham has

1 been involved in this too on behalf of the Commission.
2 And I will tell you, you guys have just worked so
3 diligently, especially the fact that we had this
4 emergency meeting, which we really -- it was not
5 necessary to do, and we appreciate you bringing it forth
6 for our consideration. I think, even with a bad stock
7 market this past week, your fine marketing efforts have
8 really produced just an incredible result.

9 So with that, I'd like to kick this off and
10 give Duke an opportunity to make some statements.

11 **MR. MAUREY:** Thank you.

12 **CHAIRMAN BROWN:** Thank you, Mr. Maurey.

13 **MS. TRIPLETT:** It's so weird to be standing.
14 Thank you again. I'll be very brief. As you heard, this
15 transaction is great. It will save our customers
16 significant money. And before I start, let me say my
17 recommendation too is that you not issue a stop order
18 today.

19 This fantastic outcome is no accident. As you
20 pointed out, it is the culmination of months of hard
21 work. And I actually went and looked at my calendar,
22 and the first bond meeting was at the end of October,
23 and I don't even think the financing order had been
24 issued. So everyone hit the ground running. There were
25 several weeks where we had multiple meetings, lots of

1 emails, lots of review of documents, and I just wanted
2 to highlight just a few of the things. We included this
3 in our issuance advice letter that was filed today and
4 circulated to the parties yesterday, but I think it's
5 important to note some of the good work that was done.

6 We ensured that the registration statement
7 contained proper disclosures to communicate the really
8 superior credit features of these bonds. We hired a
9 diverse group of underwriters, including underwriters
10 with international and mid-tier expertise and those with
11 diverse ownership in order to attract a wide variety of
12 investors, and also potentially investors that may not
13 have bought these bonds or these types of bonds before.

14 We attended in-person and telephonic
15 premarketing investor meetings throughout 2016, in
16 addition to four road show cities and multiple other
17 meetings that happened after the marketing, you know,
18 went live, so to speak. We developed and implemented a
19 marketing plan designed to encourage each of the
20 underwriters to aggressively market the bonds to a broad
21 base of prospective investors, and we also adapted the
22 bond offering to market conditions and investor demand
23 at the time of pricing. It was -- it's been an exciting
24 last few weeks. I've certainly learned a lot. But it
25 was a great iterative process and, again, it resulted in

1 this great transaction and this great result. And,
2 accordingly, the company also certifies that the
3 statutory cost objectives set forth in the financing
4 order have been satisfied, and that also was included in
5 the issuance advice letter that was filed today.

6 And as Mr. Maurey noted, we reviewed the
7 opinion letter from Saber Partners, and it does not
8 contain any qualifications with respect to the opinions
9 that he was giving and compliance with the financing
10 order. So, again, all signs point to no stop order.

11 And I would be remiss if I did not thank your
12 staff, particularly Mr. Maurey, Mark Cicchetti, and
13 Rosanne Gervasi. They were in the trenches with us --
14 lots of late night phone calls, late emails -- really to
15 get a fantastic result. And also the signatories to our
16 settlement agreement: Mr. Rehwinkel, Mr. Wright, who
17 are both here today; Mr. Brew and Mr. Moyle, who could
18 not be here. But we ran into some things and it really
19 took -- they stepped up very quickly to address them and
20 really maintained the good value of the settlement.

21 So I'm available to answer any questions, and
22 I have Mr. Portuondo in case you want to ask about
23 numbers. And thank you very much.

24 **CHAIRMAN BROWN:** Thank you, Ms. Triplett. And
25 we'll go for Mr. Rehwinkel at this time.

1 **MR. REHWINKEL:** Thank you, Commissioners.

2 Charles Rehwinkel, Deputy Public Counsel. And on behalf
3 of J. R. Kelly, the Public Counsel, who is here at his
4 second meeting today, I would like to thank you for the
5 opportunity to address you on this matter on behalf of
6 all of Duke's customers.

7 My remarks today are premised on the notion
8 that the reasons for the retirement of the CR3 plant
9 were put to rest in 2013 when the Commission approved
10 the global settlement that resulted in over \$2 billion
11 of benefits to the ratepayers. Today we are here
12 instead to consider the net present value of
13 \$684 million in additional benefits that result from the
14 financing of the remaining cost of the retired nuclear
15 plant with the nuclear asset-recovery bonds.

16 The Public Counsel supports the proposal
17 contained in the issuance advice letter filed by Duke
18 and in the opinion letter filed by your advisor, Saber
19 Partners. No action is needed. We -- Mr. Kelly,
20 myself -- have been observers at almost all of the Bond
21 Team meetings and were allowed unparalleled visibility
22 into the pricing of the bonds as an observer on the
23 crucial calls in the last two weeks of this transaction,
24 all the way up to yesterday at 2:00 p.m. when the bonds
25 were finally priced. We have also reviewed thousands of

1 pages of material prepared in support of the transaction
2 for the Securities and Exchange Commission and European
3 regulators.

4 For all of these reasons, we can say to you
5 today that we agree that the transaction appears to have
6 met the statutory standards of achieving the lowest
7 overall costs that were reasonably consistent with
8 market conditions at the time of pricing, are consistent
9 with the applicable terms of the Revised and Restated
10 Settlement and Stipulation Agreement, or RRSSA, and will
11 result in substantially lower costs. As you've heard,
12 an additional 684 million less cost to the customers as
13 compared to the traditional method allowed by the RRSSA,
14 which notably had already a greatly reduced 30 percent
15 reduction in allowed shareholder profits. So what
16 you're approving today is a reduction even off of that.
17 The pricing proposal also results in the greatest
18 possible customer protections as required by the statute
19 and your order.

20 For these reasons, the Public Counsel urges
21 you to either affirmatively approve the pricing, which
22 you really don't need to do, or to take no action and
23 refrain from issuing a stop order.

24 Having said that, it's important for us to
25 thank Duke Florida President Alex Glenn for his

1 leadership in approaching the legislature with the
2 securitization proposal in the first place. Without him
3 taking this leadership, we would not be here talking
4 about saving nearly another \$700 million.

5 We also want to thank Senator Jack Latvala for
6 championing the effort in the legislature to save these
7 \$700 million for the customers and for the inclusion of
8 the provisions that allowed for the Commission to hire
9 experts in bond finance and bond finance law to advocate
10 for customers alongside with your staff, your expert
11 staff, and we also want to thank the legislature and the
12 Governor for the law.

13 We owe a special thanks to your staff on the
14 Bond Team led by Andrew Maurey and including Mark
15 Cicchetti and Rosanne Gervasi. They were vigorous and
16 very knowledgeable advocates for the customers'
17 interests and obviously had the full support of the
18 Executive Director and the General Counsel in their
19 advocacy, and we deeply appreciate it.

20 But the OPC saved its best thanks for the
21 Commission's advisor, Saber Partners and especially Joe
22 Fichera, and the Commission's bond counsel, Dean
23 Criddle, who brought impressive expertise, experience,
24 and discipline to the transaction and, without question,
25 were instrumental in saving many millions of dollars for

1 the customers in current and future costs through their
2 dogged and expert advocacy to achieve the optimum lowest
3 cost for customers at the outset. At the outset we
4 reviewed -- we viewed their deep involvement to be
5 vital, and having observed firsthand their guidance in
6 the transaction, we are firmly convinced that they
7 brought tremendous value to the customers.

8 And I want to thank Duke and the team they put
9 together, Dianne Triplett, Javier Portuondo, Steve --
10 Bryan Buckles (sic) -- I think I said that right.

11 **MS. TRIPLETT:** Buckler.

12 **MR. REHWINKEL:** Buckler. I am so sorry. Bryan
13 Buckler, Tom Heath, Jack Sullivan, and Steve De May to
14 structure and price and issue these bonds. Their sincere
15 expert and cooperative efforts greatly facilitated this
16 transaction, not only the final process, but in the
17 Commission's proceeding leading up to the financing order
18 and the amendments to the RRSSA.

19 And finally, we want to thank you, the
20 Commissioners, for your support for this and your
21 approval of the pricing today.

22 I would like to also say that I am authorized
23 by Jay Brew, who represents PCS Phosphate, to state that
24 he concurs in these remarks. So thank you for your
25 indulgence.

1 **CHAIRMAN BROWN:** Mr. Rehwinkel, thank you.

2 Those were great remarks, and we appreciate hearing -- I
3 appreciate hearing all of those. Thank you.

4 **MR. REHWINKEL:** Thank you.

5 **CHAIRMAN BROWN:** Mr. Wright.

6 **MR. WRIGHT:** Thank you, Madam Chair and
7 Commissioners. I'll be as brief as I can. The real
8 thing here is that there's so many people to thank, it's
9 going to take me a bit. I think less than two minutes,
10 but here we go.

11 **CHAIRMAN BROWN:** The Academy Awards here.

12 **MR. WRIGHT:** Pardon?

13 **CHAIRMAN BROWN:** I'm just saying it's like the
14 Academy Awards here. Go ahead.

15 (Laughter.)

16 **MR. WRIGHT:** Rather, rather, and appropriately
17 so, because everybody involved in this process deserves
18 really, really, really big awards and really big thanks.

19 I'll start by saying that the Florida Retail
20 Federation strongly supports the staff's recommendation
21 that you not issue a stop order. Whether you
22 affirmatively vote to affirm the pricing or just not
23 issue a stop order is fine. It gets to the same exact
24 result.

25 We support Duke's issue in its advice letter.

1 We support Saber's opinion letter. We are profoundly
2 grateful for the \$684 million of additional savings over
3 and above what you already approved in the 2013 global
4 settlement.

5 And now here's where the thanks really start.
6 I thank the legislature, Senator Latvala. Thank the
7 Governor for signing this into law. Thank you all for
8 your support; thank you for issuing the financing order
9 and for hiring the right people to make this happen.
10 Thank Duke, especially Alex Glenn, Diane Triplett,
11 Javier Portuondo, and everybody else, the long list that
12 Charles read off, for their hard work. Big, big, big
13 thanks, Oscars to your staff, especially Andrew,
14 Rosanne, and Mark, for their extraordinary hard work and
15 support for everything throughout this process. Thanks
16 to Saber Partners. Thanks to Mr. Criddle and Orrick
17 Herrington for their hard work to bring this in. And
18 thanks again to y'all for approving it.

19 Again, we would join Duke and the Office of
20 Public Counsel and PCS Phosphate and others in urging
21 you to approve the pricing or refrain from issuing an
22 advice letter.

23 I'm profoundly impressed, the federation is
24 profoundly impressed with and by all the work that went
25 into this and even more so by the result. This is just

1 really, really great. I'm going to close with three
2 words: Wow and thank you.

3 **CHAIRMAN BROWN:** That's great. I appreciate
4 those words.

5 All right. Mr. Maurey, do you want to
6 readdress the Commission?

7 **MR. MAUREY:** Only if you have some questions.

8 **CHAIRMAN BROWN:** No. It obviously goes without
9 saying, a huge thank you. All of you have worked above
10 and beyond, many, many hours of overtime, driving down
11 here for this emergency meeting and all that.

12 And I'm going to open it up to the
13 Commissioners to provide some comments, questions. You
14 may begin, Commissioner Edgar.

15 **COMMISSIONER EDGAR:** Thank you, Madam Chairman.

16 As always, some of the comments that I wanted
17 to make have already been made, but I also would like to
18 acknowledge the foresight of those who worked on the
19 legislation in providing the resources and the direction
20 for the Commission to be able to hire outside bond
21 counsel and outside financial advisor. I do believe
22 that was a very important part of the process and an
23 important part of the success of the result, working
24 closely, of course, with our staff and all of the
25 involved parties.

1 You know, this is truly a good news story, and
2 I hope that that goods news gets out that although it is
3 a complex financial transaction, it is an innovative
4 financing mechanism to address a very unique situation.
5 And I do believe that the result that we have before us
6 is consistent with the statutory objectives, that the
7 lowest charges consistent with the prevailing market
8 conditions have been achieved, and that we were also
9 able to achieve the greatest possible consumer
10 protections. Lots of moving pieces, lots of moving
11 parts obviously requiring SEC review, the investor
12 education effort, but ultimately I do believe that we
13 have achieved the lower overall cost to mitigate,
14 minimize costs to the ratepayers and attract capital.
15 It is my understanding that a vote or a specific formal
16 action is not required for this to move forward, but I
17 certainly would like to endorse the process and the
18 result.

19 **CHAIRMAN BROWN:** Excellent. Thank you,
20 Commissioner Edgar.

21 I'm going to go to Commissioner Graham and
22 then Commissioner Brisé.

23 **COMMISSIONER GRAHAM:** Well, first of all, I
24 want to thank all the parties. My role in all this was
25 just more impasse resolution than anything else. And I

1 have to say the first couple of -- first couple of
2 meetings that I listened in to, I thought to myself that
3 I was going to be very busy. And come to find out, as
4 things went on, it started to ease itself up.

5 I'm going to steal a line from Charles
6 Rehwinkel. He said earlier, he says, "It's like sausage
7 because it's usually real good when you're eating it,
8 but you don't want to see it getting made." And I think
9 that's what this process was. A great outcome at the
10 end of it all, but it wasn't -- sometimes it was very
11 strained. You know, you're listening on the phone to
12 the teleconference, so you can hear the stress in the
13 voices, you can see some of the patience that went into
14 all of that, but -- and all the work that went into it
15 all. I mean, basically all I was doing was a fly on the
16 wall listening to what was going on and it was stressing
17 me, so I can imagine the people that were actually in
18 the trenches that were throwing things back and forth.
19 And I do appreciate the patience. I do appreciate
20 nobody letting the process stop or halt, that everybody
21 knew what the desired outcome was going to be and
22 everybody stayed diligent and made it all happen. It
23 didn't come easy by any means, but it did get all the
24 way through.

25 I guess one of the questions I have to staff

1 is I want to make sure that this result, this end result
2 that we have is -- actually addresses what that law was
3 that passed, that we're sure that it checks all the
4 boxes of what we're supposed to accomplish and everybody
5 is good with that.

6 **MR. MAUREY:** Yes, sir, it does.

7 **COMMISSIONER GRAHAM:** Okay. I just wanted to
8 make sure. I didn't want for anybody else to come to us
9 later on and say, well, the law said this and you did
10 that or the law was quiet to this or what we really
11 wanted was that. But just as long as we're sure that we
12 did everything we're supposed to have done, then I think
13 this is absolutely fantastic, and I thank you all for the
14 efforts that you put forth.

15 **CHAIRMAN BROWN:** Thank you, Commissioner
16 Graham.

17 Commissioner Brisé.

18 **COMMISSIONER BRISÉ:** Thank you, Madam Chair.

19 I just want to chime in and thank all the
20 parties for working together to come to this point. I
21 think that we have met the statutory requirements,
22 recognizing this is a good example of the legislature
23 and the Commission and all the parties working together,
24 looking at a situation, and trying to figure out what is
25 the best outcome for the citizens here in the state of

1 Florida, and I think this is a shining example of that
2 happening.

3 But one thing that is near and dear to my
4 heart personally is that in addition to meeting the
5 statutory requirement, we also addressed the issue of
6 opening the pot so that we can have a diverse group of
7 financial institutions as participants, and I think that
8 that's an important factor. And I think we've done all
9 of that, and that continues the public interest
10 component of this as well. So I want to commend all of
11 you and commend our staff because I know that when we
12 were working on the finance order, that was a lot of
13 work. And to continue all of that work, we are greatly
14 appreciative of our staff, of your expertise, and of
15 your willingness to put all that extra time in to get us
16 to this point. So thank you.

17 **CHAIRMAN BROWN:** Thank you, Commissioner Brisé.
18 Commissioner Patronis.

19 **COMMISSIONER PATRONIS:** Thank you, Madam
20 Chairman.

21 Just mainly thank you to staff. Couldn't
22 have this been -- this couldn't have been possible
23 without the efforts and works and fruit of your labor.
24 And really this is absolutely my best day as a
25 Commissioner today. I didn't have to do a thing. Thank

1 you.

2 (Laughter.)

3 **CHAIRMAN BROWN:** And we get positive results,
4 positive results. So seeing that we do not need to have
5 a motion and we don't need any further discussion, if no
6 one has any further discussion, a big thank you again in
7 closing, and this meeting is adjourned.

8 (Meeting adjourned at 1:03 p.m.)

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1 STATE OF FLORIDA)
 : CERTIFICATE OF REPORTER
2 COUNTY OF LEON)

3
4 I, LINDA BOLES, CRR, RPR, Official Commission
5 Reporter, do hereby certify that the foregoing
6 proceeding was heard at the time and place herein
7 stated.

8 IT IS FURTHER CERTIFIED that I
9 stenographically reported the said proceedings; that the
10 same has been transcribed under my direct supervision;
11 and that this transcript constitutes a true
12 transcription of my notes of said proceedings.

13 I FURTHER CERTIFY that I am not a relative,
14 employee, attorney or counsel of any of the parties, nor
15 am I a relative or employee of any of the parties'
16 attorney or counsel connected with the action, nor am I
17 financially interested in the action.

18 DATED THIS 20th day of June, 2016.

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25


LINDA BOLES, CRR, RPR
FPSC Official Hearings Reporter
(850) 413-6734

Not Part of Actual Transcript:

Link to video of June 16, 2016
Open Meeting of Florida Public
Service Commission (with
printed transcript captioned
throughout):

<https://www.youtube.com/watch?v=Jt0fUs3Ujo8&t=3s>

State of Florida



Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: May 8, 2006

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Economic Regulation (Maurey, Ballinger, Baxter, Brennan, Draper, Haff, Hewitt, Kaproth, Kummer, Kyle, Lee, Lowe, McNulty, M. Roy, Marsh, Redemann, Rieger, Romig, Slemkewicz, Springer, Stallcup, Trapp, Willis)
Office of the General Counsel (Keating, Brubaker, Gervasi, Helton)
Division of Regulatory Compliance & Consumer Assistance (Vandiver)

RE: Docket No. 060038-EI – Petition for issuance of a storm recovery financing order, by Florida Power & Light Company.

AGENDA: 05/15/06 – Special Agenda – Posthearing Decision – Participation is Limited to Commissioners and Staff

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Deason

CRITICAL DATES: May 15, 2006 (120 days after filing of petition)

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\060038.RCM.DOC

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Case Background

On January 13, 2006, Florida Power & Light Company (“FPL” or “the Company”) filed a petition for issuance of a storm recovery financing order or, in the alternative, an order approving the establishment of a storm cost recovery surcharge. This Commission has jurisdiction pursuant to Chapter 366, Florida Statutes, including Sections 366.04, 366.05, 366.06, and 366.8260, Florida Statutes.

Historical Background

Like other Florida investor-owned electric utilities, FPL operates under a self insurance program for its distribution and transmission facilities. This became necessary when insurance became cost prohibitive as a result of the devastation caused by Hurricane Andrew in 1992. In 1993, the Commission authorized FPL to implement this self insurance approach through annual contributions from base rate revenues to its Storm and Property Insurance Reserve Fund (referred to as “Reserve”, “Storm reserve”, or “Storm damage reserve”). From 1995 until 2005, FPL annually accrued \$20.3 million to its Reserve.

At the start of the 2004 hurricane season, FPL’s Reserve balance had reached approximately \$354 million. As a result of Hurricanes Charley, Frances, and Jeanne in 2004, FPL incurred storm-related costs of approximately \$890 million, net of insurance proceeds, which resulted in a deficit of approximately \$536 million in its Reserve at the end of December 2004. In November 2004, FPL filed a petition seeking authority to recover \$533 million of this estimated deficit through a monthly surcharge to apply to customer bills based on a 36-month recovery period. By Order No. PSC-05-0937-FOF-EI, issued September 21, 2005, in Docket No. 041291-EI, In 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 (“2004 Storm Order”), the Commission approved the initiation of a surcharge to recover prudently incurred storm restoration costs in excess of FPL’s Reserve balance (“2004 storm costs”). For residential customers, this surcharge amounts to \$1.65 for monthly usage of 1,000 kilowatt hours (kWh), with the surcharge expected to last three years or less. The Order did not address the replenishment of FPL’s Reserve.

In its 2005 session, the Florida Legislature established a new financing vehicle by which investor-owned electric utilities can quickly recover their storm restoration costs and replenish their Reserve funds. This mechanism, referred to as “securitization,” allows utilities to access low-cost funds through “storm-recovery bonds” issued pursuant to financing orders issued by the Commission. This new provision of Florida law is codified in Section 366.8260, Florida Statutes.

Also in 2005, FPL initiated a base rate proceeding before the Commission. The parties to that proceeding ultimately reached a settlement which provided, among other things, that FPL would, as of January 1, 2006, cease making any annual accrual to its Reserve. Instead, FPL would be permitted to recover its reasonable and prudently incurred storm restoration costs and to seek approval to replenish its Reserve (to a Commission-approved level) pursuant to the new securitization law and/or through a more traditional surcharge like the one approved in the 2004 Storm Order. The Commission approved the settlement by Order No. PSC-05-0902-S-EI, issued

September 14, 2005, in Docket No. 050045-EI, In re: Petition for rate increase by Florida Power & Light Company (“2005 Rate Case Order”).

Following approval of the settlement in 2005, FPL’s service territory was impacted by multiple tropical storms and hurricanes, including Dennis, Katrina, Rita, and Wilma. According to FPL’s petition in this docket, FPL incurred storm-related costs of approximately \$879.9 million, net of insurance proceeds.

FPL’s Petition

Through its petition in this docket, FPL requests that the Commission approve the issuance of up to \$1.05 billion of storm-recovery bonds pursuant to Section 366.8260, Florida Statutes. According to FPL’s petition, this would enable FPL to: (1) recover the remaining unrecovered balance of its 2004 storm costs; (2) recover its prudently incurred 2005 storm costs, less capital costs and insurance proceeds; and (3) rebuild its Reserve to a level of approximately \$650 million. FPL notes that the bonds would be issued for the after-tax value of these amounts to recognize the tax benefit received when storm restoration costs are deducted for income tax purposes. The following table, reproduced from information in Exhibit A to FPL’s petition, summarizes these amounts:

SUMMARY OF STORM COSTS AND AMOUNT OF PROPOSED BOND ISSUANCE		
(\$000s)		
	2005 System Amount	2005 Jurisdictional Amount
Total Estimated 2005 Storm-Recovery Costs	\$906,404	
Less: Estimated Insurance Proceeds	(26,533)	
2005 Storm Costs (Net of Insurance Proceeds)	\$879,871	
Less: 2005 Estimated Capital Storm Costs	(63,855)	
Net 2005 Storm-Recovery Costs	\$816,016	\$815,372
Interest Incurred Through Estimated Bond Issuance Date		11,481
Unrecovered 2005 Storm-Recovery Costs		\$826,853
Unrecovered 2004 Storm-Recovery Costs (as of July 31, 2006)		\$213,307
Replenishment of Reserve		\$650,000
Total Storm Costs		\$1,690,160
Estimated Up-front Bond Issuance Costs		11,425
Total Costs Requested for Recovery		\$1,701,585
Less: Income Taxes		(651,979)
Total Amount of Storm-Recovery Bonds		\$1,049,606

Under FPL’s proposal, the amount financed through storm-recovery bonds would be paid over approximately twelve years through charges applied on a per kilowatt-hour (kWh) basis to all applicable customer classes. In addition, any tax liabilities associated with collection of the new charges would be paid through another charge to the extent such liabilities are not recovered

through other rates or charges. In sum, these proposed charges are estimated to be \$1.58 for residential monthly usage of 1,000 kWh. If a financing order is issued to include FPL's unrecovered 2004 storm costs, the surcharge approved in the 2004 Storm Order would be terminated on the effective date of the new charges.

In the event that the Commission issues a financing order and the issuance of storm-recovery bonds is delayed for any reason, FPL asks that the Commission authorize a surcharge to apply to bills rendered on and after August 15, 2006, to recover the 2005 storm costs over approximately three years. FPL estimates that this surcharge would amount to \$2.98 for residential monthly usage of 1,000 kWh, in addition to the existing surcharge for 2004 storm costs. As proposed by FPL, this surcharge would terminate upon issuance of the bonds and the amount of the bonds would be adjusted to reflect collections made under the temporary surcharge.

If the Commission does not grant FPL approval to issue storm-cost recovery bonds, FPL asks that the Commission approve a surcharge effective for bills rendered on and after June 15, 2006, that would allow FPL, over a three year period, to recover its estimated 2005 storm costs plus \$650 million toward the replenishment of its Reserve. FPL estimates that this surcharge would amount to \$5.19 for residential monthly usage of 1,000 kWh, in addition to the existing surcharge for 2004 storm costs.

The following table provides a summary of the rate impacts associated with FPL's primary and alternative requests:

SUMMARY OF RATE IMPACTS (Monthly Residential Bill for 1,000 kWh)		
	Primary Request (Securitization)	Alternative Request (Short-Term Surcharge)
Existing Surcharge for 2004 Costs	No separate surcharge; included in total charge	\$1.65 ¹ (approx. 20 months)
New Surcharge for 2005 Costs	No separate surcharge; included in total charge	\$2.98 ² (approx. 3 years)
New Surcharge for Replenishment of Reserve	No separate charge; included in total charge	\$2.21 ³ (approx. 3 years)
Storm Bond Repayment Charge and Storm Bond Tax Charge	\$1.58 (approx. 12 years)	Not applicable
Total Rate Impact	\$1.58 (over approx. 12 years)	\$6.84⁽¹⁺²⁺³⁾ (over approx. 20 months) \$5.19⁽²⁺³⁾ (over remaining approx. 16 months)

Procedural Background

On March 1-3, 2006, the Commission held customer service hearings in the portions of FPL's service territory that were most affected by the 2005 storm season: Ft. Myers, West Palm Beach, Ft. Lauderdale, and Miami. The Commission took testimony from several persons at these service hearings concerning FPL's restoration efforts, its quality of service, and its petition in this docket.

On April 19-21, 2006, the Commission conducted a technical hearing on FPL's petition. Along with FPL, the Office of Public Counsel ("OPC"), Florida Industrial Power Users Group ("FIPUG"), Florida Retail Federation ("FRF"), AARP, Federal Executive Agencies ("FEA"), and the Office of the Attorney General ("AG") (sometimes referred to collectively as "Intervenors") participated as parties to the proceeding.¹ During the hearing, the Commission accepted the prefiled testimony of 20 witnesses, heard cross-examination of most of those witnesses, and admitted 172 exhibits into evidence. Following the hearing, each party filed a post-hearing brief and/or statement of issues and positions.

Pursuant to Section 366.8260(2)(b)1., Florida Statutes, the Commission is required to make a decision on FPL's petition no later than 120 days after the date the petition was filed. Hence, this matter has been scheduled for a special agenda conference on May 15, 2006. Further, pursuant to the same law, the Commission is required to issue a financing order or an order rejecting FPL's petition no later than 135 days after the date the petition was filed – May 30, 2006, in this case.

Standard of Review

Section 366.8260(2)(b)1.b., Florida Statutes, provides the standard of review applicable to a petition for issuance of a financing order:

The commission shall issue a financing order authorizing financing of reasonable and prudent storm-recovery costs, the storm-recovery reserve amount determined appropriate by the commission, and financing costs if the commission finds that the issuance of the storm-recovery bonds and the imposition of storm-recovery charges authorized by the order are reasonably expected to result in lower overall costs or would avoid or significantly mitigate rate impacts to customers as compared with alternative methods of financing or recovering storm-recovery costs and storm-recovery reserve. Any determination of whether storm-recovery costs are reasonable and prudent shall be made with reference to the general public interest in, and the scope of effort required to provide, the safe and expeditious restoration of electric service.

(Emphasis added.) FPL does not assert that granting its request for a financing order is reasonably expected to result in lower overall costs as compared to imposition of a short-term, "traditional" surcharge. Rather, FPL's petition is based on the mitigating effect that its proposed

¹ The AG was granted leave to intervene at the Prehearing Conference held April 13, 2006. All other parties, except FPL, were granted leave to intervene by separate orders.

storm-recovery charges would have on rates as compared to continuing the existing surcharge in addition to implementing another short-term surcharge.

Summary of Recommendation

None of the parties except FIPUG support implementation of a traditional, short-term surcharge. Instead, the parties appear to support the lower but longer-term charges associated with the issuance of storm-recovery bonds. Still, a number of disputed issues remain concerning the appropriate amount to be recovered from ratepayers. To the extent the Commission authorizes FPL to finance any portion of this amount through storm-recovery bonds, several issues remain concerning the process of issuing the bonds.

With respect to the amount to be recovered from ratepayers, there are three main groups of disputed issues, which are outlined in the Table of Contents and addressed below: (1) issues related to the appropriate charges to FPL's Reserve (Issues 1-26); (2) issues related to the prudence of FPL's system maintenance activities prior to and during the 2005 storm season (Issues 27-36); and (3) issues related to the funding of FPL's Reserve (Issues 37-38).

Charges to the Reserve

An important issue with respect to the first set of issues is the methodology by which 2005 storm costs should be charged to the Reserve (Issue 6). The Commission addressed this issue in its 2004 Storm Order and found that a "modified incremental cost" approach should be used. Under that approach, storm-recovery expenses incremental to those already being recovered through FPL's base rates were charged to the Reserve. Capital items were not charged to the Reserve. In determining the appropriate amount to charge to the Reserve for 2004, the Commission considered that FPL did not collect normal base rate revenues – due to outages resulting from the storms – to cover its normal (i.e., non-incremental) costs during that period. Thus, the Commission allowed FPL to recover those normal costs that it found were not recovered by base rate revenues.

In this case, FPL supports the use of an approach slightly different from the "actual restoration cost" approach it supported last year. Under FPL's approach, all direct and indirect costs incurred to safely restore service and to return plant and equipment to its pre-storm operating condition are charged to the Reserve. FPL's approach in this docket differs from the approach it supported last year in that FPL has not charged capital items to the Reserve for the 2005 storms. Intervenors support use of the modified incremental cost approach used in the 2004 Storm Order, but assert that there should be no adjustment for undercollection of normal base rate revenues because such revenues exceeded budgeted revenues during the affected months in spite of the storm-related outages in 2005.

In this recommendation, staff recommends that the evidence supports continued use of the modified incremental cost approach as suggested by Intervenors (Issue 6). Based on the evidence presented, staff will recommend that there should be no adjustment for "lost revenues" for the Commission to consider in this case (Issue 17). Further, staff will advise that the 2004 Storm Order does not establish a precedent that binds the Commission's determination of the methodology to use in this docket (Issue 5). The table below provides a summary, by issue, of Staff's recommended adjustments consistent with the modified incremental cost approach.

Prudence of System Maintenance

The next set of issues concerns whether FPL adequately inspected and maintained its distribution and transmission system prior to and during the 2005 storm season (Issues 27-33). Intervenors assert that FPL did not adequately inspect and maintain its system for deterioration and overloading of poles, did not adequately control vegetation around its system, and did not adequately maintain facilities on two particular transmission lines that failed during the 2005 storm season. In this recommendation, staff will recommend that certain adjustments should be made under these issues. Staff's recommended adjustments are set forth in the table below.

Another controversial issue concerns whether FPL's 2005 storm-recovery costs should be shared between FPL's ratepayers and shareholders (Issue 35). This issue was addressed in testimony by Staff witness Jenkins, who suggested that shareholders be responsible for up to 20 percent of FPL's prudently incurred 2005 storm costs. Of the Intervenors, only the AG has supported application of this concept. All of the Intervenors were parties to the settlement approved in the 2005 Rate Case Order. As discussed in the recommendation, staff believes that the settlement was clearly intended to preclude the parties from proposing or supporting such a sharing, although the Commission is not entirely bound by the terms of the settlement. Staff believes that the Commission can honor the settlement but still require a sharing of costs by making the adjustments recommended in Issues 27-33 and by not considering "lost revenues" in determining the 2005 storm-recovery costs appropriately charged to the Reserve.

Funding of Reserve

There is also controversy surrounding the appropriate level of funding to replenish FPL's Reserve. FPL requests a level of \$650 million. Intervenors support a level of approximately \$150-200 million. The Commission has wide latitude in determining the appropriate amount. If future storm-recovery costs exceed the balance of FPL's Reserve, nothing prohibits FPL from seeking recovery of those costs through the issuance of storm-recovery bonds or a "traditional," short-term surcharge. In this recommendation, staff will propose that the Reserve should be funded to a level of \$200 million through this proceeding.

**SUMMARY OF ADJUSTMENTS TO FPL'S PROPOSED STORM-RECOVERY
 COSTS AND RESERVE FUNDING LEVEL**

Unrecovered 2004 Storm-Recovery Costs (as of July 31, 2006)	\$213,307,000
<u>Less: Staff Recommended Adjustments</u>	
Issue 1 – Nuclear Storm Damages	(6,100,000)
- Legal Claims And Lawsuits	(2,664,038)
- Other Parties' Poles Reimbursements	<u>(5,432,966)</u>
Subtotal	(14,197,004)
2004 Jurisdictional Factor	<u>99.525%</u>
Jurisdictional Adjustments	(14,129,568)
Issue 3 – Interest Adjustment	<u>(497,000)</u>
Total 2004 Adjustments	<u>(14,626,568)</u>
Adjusted Unrecovered 2004 Storm-Recovery Costs	<u>\$198,680,432</u>
FPL Estimated Unrecovered 2005 Storm-Recovery Costs (Net of Capital Costs and Insurance Proceeds)	\$826,853,000
<u>Less: Staff Recommended Adjustments</u>	
Issue 7 – Condenser Tubes	(2,785,364)
- Hydrolasing	(221,000)
- Proceeds from Others	(3,468,593)
Issue 8 – Payroll Expense	(17,925,918)
Issue 9 – Exempt Employee Overtime	(768,000)
Issue 11 – Tree Trimming	(1,100,000)
Issue 12 – Fleet Vehicles	(5,738,000)
Issue 13 – Telecommunications Expense	(520,264)
Issue 14 – Advertising	(1,143,916)
Issue 15 – Uncollectibles	(3,582,000)
Issue 16 – Normal Replacements	(8,745,000)

Issue 18 – Landscaping	(3,816,864)
Issue 19 – Lawsuit Settlement Charges	(2,849,571)
Issue 20 – Contingencies	(26,253,351)
Issue 22 – Other Entities’ Poles	(10,564,384)
Issue 24 – Employee Assistance	(245,025)
- Warranty Repairs	(316,250)
Issue 27 – Inspect & Maintain System (also \$1,440,000 Rate Base Adj.)	(4,460,000)
Issue 28 – Vegetation Management (also \$850,000 Rate Base Adj.)	(2,550,000)
Issue 33 – Transmission Failures ((\$12,000,000 Rate Base Adj.)	<u>0</u>
Subtotal	(97,053,500)
2005 Jurisdictional Factor	<u>99.921%</u>
Jurisdictional Adjustments	(96,976,828)
Issue 34 – 2005 Jurisdictional Interest Adjustment	<u>(1,365,500)</u>
Total 2005 Adjustments	<u>(98,342,328)</u>
Adjusted 2005 Storm Damage Costs To Be Charged Against Storm Reserve	<u>\$728,510,672</u>
FPL Requested Level of Reserve	\$650,000,000
<u>Less:</u> Staff Recommended Adjustment – Issue 37	<u>(450,000,000)</u>
Staff Recommended Reserve Level	<u>\$200,000,000</u>
TOTAL AMOUNT TO RECOVER – PRE-TAX BASIS	<u>\$1,127,191,104</u>
TOTAL AMOUNT TO RECOVER – AFTER-TAX BASIS	\$692,377,136
Up-Front Bond Issuance Costs	<u>11,425,000</u>
TOTAL AMOUNT SUBJECT TO SECURITIZATION	<u>\$703,802,136</u>

Terms and Conditions of Financing Order

As noted above, all parties but FIPUG appear to support the use of storm-recovery bonds to finance the amounts approved for recovery in this proceeding, and staff is recommending issuance of a financing order in this case. With respect to the terms and conditions to be included in a financing order for these amounts, there is still disagreement among the parties on several issues (see Issues 45-76). The major issues in dispute involve (1) whether or not the Commission should use a "lowest cost" standard with regard to interest rates achieved on the bonds and other issuance costs (Issue 61) and (2) the level of involvement that the Commission should have in the structure, marketing, and pricing of the bonds (Issues 61-68, 71, 74, 74A, and 74B). Staff will recommend that the Commission adopt a lowest cost standard with active Commission involvement in the pre-issuance process through final pricing.

Discussion of Issues

CHARGES TO STORM RESERVE

2004 Storm Costs

Issue 1: Did FPL stop charging 2004 storm-related costs to the storm reserve by July 31, 2005, for restoration work related to the 2004 storm season, as required by Order No. PSC-05-0937-FOF-EI? If not, what adjustments should be made?

Recommendation: No. The 2004 storm-related costs should be reduced by \$14,197,004. (Slemkewicz)

Position of the Parties

FPL: Yes. As of July 31, 2005, total storm costs of \$890.0 million were reflected in FPL's accounting records. Subsequent to this date, adjustments were made pursuant to the referenced order to remove \$91.9 million resulting in \$798.1 million of storm costs approved for recovery. As to estimated costs recorded as of July 31, 2005, for work not completed at that date, differences that would result in actual costs exceeding \$798.1 million will be absorbed by the Company. If actual costs are less than \$798.1 million, FPL proposes that the difference be credited to the Storm Reserve.

OPC: No. FPL added accruals to the 2004 storm reserve items not requested or identified in testimony, exhibits or other evidence in the record in Docket No. 041291-EI. FPL disregarded the Commission's cut off point for charges to the storm reserve. The Commission should adjust the reserve by \$51,264,919.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC as to appropriate adjustments.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis stated that FPL did stop charging 2004 storm-related costs to the storm reserve by July 31, 2005 as required by the order and that no adjustments are required at this time. (TR 1592)

OPC witness DeRonne presented a schedule (DD-2) in her direct testimony that calculated her recommended reduction of \$51,396,811 to the 2004 storm cost estimates. (EXH 86) However, OPC has accepted FPL witness Davis' rebuttal testimony that OPC's proposed adjustment related to reimbursements for work on poles owned by others should be reduced by \$131,892. (OPC BR at 6) Therefore, OPC's recommended adjustment is a reduction of \$51,264,919. (OPC BR at 1)

ANALYSIS

OPC's proposed \$51,264,919 adjustment is comprised of the following four components: (1) \$21.7 million charged to the Storm Reserve in the 2004 Storm Cost Recovery Order; (2) \$21,467,915 of various nuclear storm damages; (3) \$2,664,038 of legal claims and lawsuits; and (4) \$5,432,966 for reimbursements for repairs on poles owned by other parties.

\$21.7 Million Charged to the Storm Reserve in the 2004 Storm Cost Recovery Order

The 2004 Storm Order included a \$21.7 million (\$21,597,000 jurisdictional) reduction to FPL's requested 2004 storm damage recovery costs. (page 20) The effect of this adjustment transferred the \$21.7 million from storm costs recoverable through the surcharge back to the storm reserve. In essence, the \$21.7 million was deferred, not disallowed.

FPL agrees that \$21.7 million was excluded from the 2004 Storm Restoration Surcharge. However, witness Davis stated that the inclusion of the \$21.7 million in the Reserve, pending recovery, is consistent with the 2004 Storm Order. (TR 604, FPL BR at 18) In its brief, FPL stated that the \$21.7 million was the subject of a special staff supplemental recommendation, to which all parties to the 2004 Storm Cost Recovery proceeding agreed (including OPC), after which the Commission adopted Staff's proposed accounting treatment resulting in the \$21.7 million being charged to the Reserve rather than included in the amounts subject to the 2004 Storm Restoration Surcharge. (FPL BR at 18) Witness Davis testified that the \$21.7 million had been inadvertently removed from the 2004 storm costs. He further testified that rather than going back and revisiting the amount already approved for 2004, the \$21.7 million was charged back to the reserve and was not recovered at that time. (TR 537)

OPC witness DeRonne stated that the 2004 Storm Order indicated the \$21.7 million was included as part of storm restoration costs, but was not included in the calculation of the surcharge approved in that docket. In other words, the Order ultimately resulted in the addition of the \$21.7 million to the allowed charges to the storm reserve for future recovery, but it was not factored into the determination of the surcharge allowed in that case. Once this \$21.7 million is factored in, the net amount that effectively was approved for recovery in the 2004 Storm Cost Recovery Order is \$819,800,000 (\$798,100,000 + \$21,700,000). (TR 980) FPL agreed that the effect of the \$21.7 million adjustment contained in Exhibit 19 sponsored by FPL witness Davis is the same as if that amount were added to the amount contained in the Commission's 2004 Storm Order. (TR 536) Based on the information that she had received from FPL, witness DeRonne testified that it was her opinion that the \$21.7 million had been spent. (TR 1012)

Although the \$21.7 million was not included in the 2004 storm costs to be recovered through the surcharge, it was not disallowed. If it had been deemed to be a disallowance, FPL

would have been required to write off the \$21.7 million as an O&M expense. Instead, the \$21.7 million was charged against the reserve as an incurred storm cost. Staff believes that this is the appropriate time to seek recovery of this amount. In staff's opinion, the \$21.7 million represents 2004 storm costs that were deferred and that are now eligible for recovery. Staff recommends that the 2004 storm costs not be reduced by the \$21.7 million.

Various Nuclear Storm Damages (\$21.5 million)

Witness Davis testified that FPL included approximately \$21.5 million in nuclear storm damage costs as part of the \$890.0 million it requested in Docket No. 041291-EI. (TR 1593) He further stated the \$21.5 million was reduced in February 2006 due to the correction of an error in recording storm costs in 2005. A storm related payment had been incorrectly charged to a non-storm work order due to a transposition error in the work order number. The effect of correcting this error was to reduce the balance available for the uninsured nuclear costs to \$20.5 million. (TR 1594 Davis) Witness Davis testified that a further adjustment was made to reduce the \$20.5 million by \$5.1 million was based on a revised estimate in March 2006. The current estimate of \$15.4 million in uninsured 2004 costs was based on discussions with Nuclear Electric Insurance Limited ("NEIL") concerning the scope of damages to be repaired and the costs subject to insurance. (TR 1595) FPL witness Warner testified that the remaining \$15.4 million for uninsured 2004 nuclear plant storm damage reflects the most accurate and reliable information available concerning 2004 storm cost repairs still to be conducted at the St. Lucie Plant. (TR 388) The necessary adjustment of \$5.1 million is shown in FPL witness Davis' Exhibit 119.

OPC witness DeRonne testified that the 2004 storm costs should be reduced by \$21,467,915 (\$21.5 million) to remove various nuclear storm damages. Witness DeRonne stated that the response to OPC Interrogatory No. 108 (EXH 155) indicated that the costs were an estimate of uncompleted work subject to change based on insurance recoveries. Witness DeRonne further testified that these were future estimated costs that should not be included in the 2004 storm recovery costs. Witness DeRonne also stated that it appears that these costs were not presented in the prior case and were estimated after July 31, 2005. (TR 984-985)

Staff believes the timing of the nuclear unit repairs warrants economic and operating considerations. Because of the high replacement power costs incurred when a nuclear unit is off-line, damage assessment and repairs to certain equipment can only be performed during refueling outages, which occur approximately every 18 months. (Warner TR 389) FPL maintains that the repairs, including repairs to the intake and discharge canals, repair of coatings in various areas of the plant, and canal dredging, are critical to ensure the long-term reliability of plant operations, but due to the nature of nuclear operations it may take several years before the units can be fully restored to pre-storm conditions. (TR 390; FPL BR at 81) Staff believes FPL has justified the reasons for the delay in starting the nuclear unit repairs.

Based on the foregoing discussion, staff recommends that the estimated nuclear storm damage repair costs should be included in the 2004 storm costs. However, staff recommends that the amount be reduced by \$6.1 million to reflect FPL's latest estimate of the uninsured portion of the repairs. This represents the difference between the \$21.5 million original estimate and the \$15.4 million revised estimate.

Legal Claims and Lawsuits (\$2.7 million)

FPL witness Davis testified that the 2004 litigation costs included in FPL's March 31, 2006 accrual are directly related to storm restoration and are thus recoverable storm costs. FPL is a member of the Edison Electric Institute, and the Southeastern Electric Exchange, where the members of these organizations have a mutual aid agreement to help each other when disasters such as hurricanes occur. These organizations have guidelines as to what companies can charge each other for their assistance. The general framework of the mutual aid assistance agreement is that each company is entitled to recover all reasonable costs incurred for providing assistance to the host utility. (TR 1587) In addition, FPL is required to "indemnify, hold harmless and defend" foreign crews assisting FPL in restoration efforts from any and all lawsuits or claims that result from furnishing emergency assistance. (TR 1588) Witness Davis said that this means that FPL is responsible for reimbursing the assisting utility for its costs when that utility's employee causes an accident or injury during storm restoration. (TR 1589)

Witness Davis testified that the removal of these costs from storm cost recovery would attribute them to base rates. He also testified that hurricane litigation reimbursements are extraordinary and non-recurring costs that are excluded when setting base rates, because the hurricanes that give rise to them are extraordinary in nature. (TR 1589) However, witness Davis did testify that the amount of the costs should be reduced by \$635,000. (TR 1590; EXH 119)

OPC witness DeRonne testified that the 2004 storm recovery costs should be reduced by \$2,664,038 for claims outstanding and pending lawsuits. (TR 984) She testified that such costs are not directly related to the storm. (TR 984) She also stated that these costs were not presented previously as part of the storm costs. She further stated that this type of cost is considered in the determination of base rates. (TR 984) OPC stated in its brief that FPL witness Davis testified that he removed \$2.2 million of these costs. (OPC BR at 6; TR 1615) However, a review of the transcript shows that witness Davis was referring to 2005 costs rather than 2004 costs. (TR 1615)

Staff agrees with witness DeRonne that these costs should be not be included in the 2004 storm costs. Although the events associated with these pending actions occurred during storm damage restoration activities, they were not themselves storm damage restoration activities. There is also considerable uncertainty associated with estimating the final outcome of outstanding claims and pending lawsuits. For these reasons, staff recommends that the 2004 storm costs be reduced by \$2,664,038 to remove the outstanding claims and pending lawsuits resulting from the actions of other utilities' employees.

Reimbursements for Work on Other Parties' Poles (\$5.6 million)

FPL billed \$7,419,810 to other parties for replacing joint use poles owned by others. OPC, in Exhibit 86, recommended that 2004 storm costs be reduced by \$5,564,858 based on the assumption that 25 percent of the \$7,419,810 billed to outside parties would have been normal capital costs for the poles removed and thus already excluded from the amounts charged to the storm reserve. On rebuttal, FPL witness Davis identified the amount billed net of the normal capital costs of the poles as \$5,432,996, which is \$131,892 less than OPC's recommended adjustment. OPC has accepted FPL's position that \$5,432,966 is the appropriate amount. (OPC

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BR at 6) FPL agrees that the 2004 storm recovery costs should be reduced by \$5,432,966. (FPL BR at 20) Accordingly, staff recommends this adjustment be made.

CONCLUSION

Based on the above discussions, staff recommends that the 2004 storm-related costs be reduced by \$14,197,004, calculated as follows:

\$21.7 Million Amount Charged Back to Storm Reserve	\$ 0
Various nuclear storm damages	(6,100,000)
Legal Claims and Lawsuits	(2,664,038)
Other Parties' Poles Reimbursements	<u>(5,432,966)</u>
Total Adjustment	<u>\$(14,197,004)</u>

Issue 2: Should the 2004 storm costs be adjusted for other items? If so, what is the appropriate adjustment?

Recommendation: This is a moot issue because all of the proposed adjustments have been addressed in Issue 1. (Slemkewicz)

Position of the Parties

FPL: No. FPL has agreed to certain adjustments specified in Mr. Davis's rebuttal testimony, which should be addressed in a final true-up process. No adjustments other than those specified by Mr. Davis should be made.

OPC: Yes, the 2004 storm costs should be adjusted to remove the estimated amounts for reimbursements for repair and restoration of poles owned by other parties.

FIPUG: Adopts the position of OPC.

FRF: Yes. Agree with OPC as to appropriate adjustments.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: This is a moot issue because all of the proposed adjustments have been addressed in Issue 1.

Issue 3: Should an adjustment be made to reflect the actual December 31, 2005 storm cost deficiency related to the 2004 costs? If so, what is the amount of the adjustment?

Recommendation: Yes. The 2004 reserve deficiency should be reduced by \$14,626,568 (jurisdictional) to match the recommendations made by staff in Issue 1 and the related interest expense. The December 31, 2005 difference between the general ledger and FPL witness Davis' Exhibit 19, along with other month-to-month variances attributable to actual interest accrued and billed revenues, should be addressed as part of a final true-up. (Romig)

Position of the Parties

FPL: No. There are some small differences between the deficiency balance and General Ledger due to rounding down the amount of 2004 storm costs approved for recovery, and differences between estimated and actual interest incurred and billed revenues as 2004 storm cost amounts have been recovered. Any differences remaining as of July 31, 2006 should be addressed as part of the final true-up.

OPC: Yes, the 2004 reserve deficiency should be reduced \$51,264,919 to reflect the adjustments discussed in response to issue 1, with a corresponding reduction in interest expense accrued at the pre-tax commercial paper rate on the account.

FIPUG: Adopts the position of OPC.

FRF: Yes. Agree with OPC that the 2004 reserve deficiency should be reduced by \$51,396,811.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

In his rebuttal testimony, FPL witness Davis stated that FPL believes that adjustments to the 2004 storm costs are appropriate. (TR 1584) As presented on Document No. KMD-11, witness Davis proposed adjustments of \$11,147,166 related to legal claims and lawsuits, various nuclear storm damages, and reimbursement for work on other parties' poles. (EXH 119) Each of these adjustments is analyzed as part of Issue 1, resulting in a \$14,197,004 recommended adjustment to 2004 storm-related costs.

In addition, FPL witness Davis testified that Audit Finding No. 11 of the Commission Staff's Audit Report (EXH 2) states the amount of unrecovered 2004 storm costs on FPL witness Davis' KMD-3 (EXH 19) is different than what is recorded in the general ledger as of December 31, 2005. However, witness Davis does not believe that any action is required at this time. Witness Davis explained the reason for the difference between the \$293,930,364 unrecovered

2004 storm costs in the General Ledger as of December 31, 2005 and the \$294,680,000 amount shown on Exhibit 19. Witness Davis described the \$749,636 difference as being attributable to three factors: The beginning deficiency balance on the general ledger was \$441,634,351, while the amount shown on Witness Davis' Exhibit 19 was \$441,990,525, the amount approved in the 2004 Storm Cost Recovery Order. In turn, this difference is because the beginning deficiency balance reflected in Exhibit 19 is different than what was recorded on the general ledger due to the rounding of actual storm funds available to offset the amount of 2004 storm costs approved for recovery from \$354,357,874 to \$354,000,000. (TR 1584-85; EXH 19) The remaining two factors relate to interest and billed revenues. Witness Davis' Exhibit 19 is based on actual interest and billed revenues to November 30, 2005 and estimated interest and revenues for December 2005, whereas the general ledger is based on actual interest and billed revenues through December 2005. Witness Davis testified that the month-to-month variances between actual and estimated unrecovered storm costs remaining as of July 31, 2006 should be addressed as part of a final true-up. (TR 1585)

In its Brief, OPC states that the reserve deficiency should be reduced by \$51,264,919 to reflect the adjustments discussed in Issue 1, with a corresponding reduction in interest expense accrued at the pre-tax commercial paper rate on the account. (OPC BR at 8)

Staff witness Welch testified that the actual general ledger amount of 2004 storm costs at December 31, 2005 for 2004 storm costs was \$293,930,364, whereas the amount of the ending deficiency on Exhibit 19 was estimated to be \$294,680,000. She also testified that the difference relates to the estimate of the beginning balance from the 2004 Storm Order being different from actual, the December interest calculation being different from actual, and an adjustment for the 2004 Storm Order related to taxes on the interest. (TR 1092)

ANALYSIS

The analyses and conclusions for the individual components of the \$51,264,919 at issue are addressed in Issue 1.

The remaining \$749,636 at issue is related to the difference between the estimated December 31, 2005 balance for 2004 storm costs and the amount recorded on FPL's general ledger on December 31, 2005. As pointed out by witness Davis, this variance was due to a rounding difference between the general ledger and the 2004 Storm Order as well as differences between estimated and actual interest incurred and billed revenues as the 2004 storm surcharge was collected.

In addition, in the 2004 Storm Order the Commission determined, "For the sake of simplicity and administrative efficiency, that annual revisions to storm recovery factors to reflect actual sales are not necessary" and "total revenues will be subject to the cumulative true-up at the end of the recovery period." (2004 Storm Order, p. 38) Finally, no party took a position on the \$749,636 at issue.

CONCLUSION

Based on the foregoing, the 2004 reserve deficiency should be reduced by \$14,626,568 (jurisdictional) to match the recommendation made by staff in Issue 1. Based on removing the

staff's proposed \$14,129,568 adjustment from the \$441,991,000 beginning balance for the unrecovered 2004 storm-recovery costs on Exhibit 19, the amount of interest on the outstanding balance should be reduced by \$497,000. The December 31, 2005 difference between the general ledger and FPL witness Davis' Exhibit 19, along with other month-to-month variances attributable to actual interest accrued and billed revenues, should be addressed as part of a final true-up. Staff's recommended adjustments are calculated as follows:

<u>ISSUE</u>	<u>DESCRIPTION</u>	<u>\$</u>
	Estimated Unamortized Jurisdictional 2004 Storm Costs as of July 31, 2006	<u>213,307,000</u>
1	July 31, 2005 Stop Date for 2004 Costs	
	- Various Nuclear Storm Damages	(6,100,000)
	- Amounts Not Incurred	0
	- Legal Claims and Lawsuits	(2,664,038)
	- Reimbursements for Other Parties' Poles	(5,432,966)
2	Other 2004 Storm Cost Adjustments	<u>0</u>
---	Total Adjustments to 2004 Storm Costs	(14,197,004)
---	Jurisdictional Factor	<u>99.525%</u>
3	Jurisdictional Adjustments to 2004 Storm Costs	(14,129,568)
3	Interest Expense Adjustments	<u>(497,000)</u>
3	Total 2004 Storm Cost Adjustments	<u>(14,626,568)</u>
---	Adjusted Unamortized Jurisdictional 2004 Storm Costs as of July 31, 2006	<u>198,680,432</u>

Issue 4: Has FPL properly accounted for the after-tax effects of interest on unrecovered storm costs?

Recommendation: Yes, FPL has properly accounted for the after-tax effects of interest on unrecovered storm costs. (Lowe, Kyle)

Position of the Parties

FPL: Yes. FPL has properly reflected the effect of deferred income taxes related to storm costs in its computation of storm costs to be securitized.

OPC: Interest should be reduced to reflect the reduction to the 2004 storm costs included in the reserve as discussed in response to issue 1.

FIPUG: Interest should be reduced to reflect the reduction to the 2004 storm costs included in the reserve as recommended by OPC witness DeRonne.

FRF: No position as to accuracy of accounting or as to the amount of any adjustment. Agree with OPC that interest should be reduced to reflect the reduction to 2004 storm costs included in the reserve.

AARP: Agree with FIPUG.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The Utility and two Intervenors addressed this issue. The Utility argues that it has properly accounted for the after-tax effects of interest on both unrecovered 2004 and 2005 storm costs in the computation of the storm costs to be securitized. FPL witness Davis shows the calculation for the 2004 interest expense (EXH 19) and for the 2005 interest expense. (EXH 20)

OPC argues that adjustments need to be made to the interest expense associated with the 2004 and 2005 storm costs. OPC witness DeRonne testified that the beginning balance of the unrecovered 2004 storm costs should be reduced by \$51,264,919. (OPC BR at 9) However, she did not provide testimony that the interest calculation should be reduced as a result of the adjustment. OPC further argues in its brief that interest on the 2005 storm costs should also be reduced. Again OPC provided no testimony to support this assertion.

FIPUG argues that interest should be reduced to reflect the reduction to the 2004 storm costs included in the reserve, as recommended by OPC witness DeRonne. (FIPUG BR at 11) Again, witness DeRonne did not testify as to the reduction of interest in the calculation of the level of allowable 2004 storm damages. There is no record support for this assertion.

Staff agrees with the Utility. Witness Davis testifies that FPL properly accounted for the after-tax effects of interest on both unrecovered 2004 and 2005 storm costs in the computation of the storm costs to be securitized. (EXH 19 and 20) This testimony was not refuted. However, staff also believes that interest should be adjusted if other adjustments are made to the allowable

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unrecovered 2004 and 2005 storm damages. We believe these are fall-out mathematical adjustments. Exhibits 19 and 20 show the mathematical calculation.

2005 Storm Costs

Issue 5: What is the legal effect, if any, of Order No. PSC-05-0937-FOF-EI on the decisions to be made in this docket?

Recommendation: The 2004 Storm Order does not operate as binding precedent with respect to the decisions to be made in this proceeding, including determinations of the appropriate accounting for 2005 storm costs and whether any “sharing” of 2005 storm costs should be required. The decisions in this docket should be made based on the record evidence in this proceeding. (Brubaker, Gervasi, Keating)

Position of the Parties

FPL: In accordance with fundamental principles of ratemaking, the Commission approved recovery by FPL of all costs of storm restoration that it deemed to be reasonably and prudently incurred. Nothing has changed that would alter the propriety of approving recovery of all reasonably and prudently incurred storm costs.

OPC: Order No. PSC-05-0937-FOF-EI contains some precedent for the Commission's decision in this case. However, the Commission can amend its policy decisions on issues such as lost revenues and the treatment of amounts FPL claims are uncollectible because such changes are supported by expert testimony and other evidence appropriate to the nature of the issues involved.

FIPUG: Adopts the position of OPC.

FRF: Order No. 05-0937 is non-binding precedent. Because all ratemaking is inherently prospective and legislative, as an exercise of the police power, the Commission is free to make any reasonable decision supported by competent substantial evidence of record with regard to the ratemaking issues (including cost allocation and prudency issues) in this case.

AARP: Same position as FIPUG.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

With respect to the accounting methodology to be used in this proceeding, FPL suggests that Order No. PSC-05-0937-FOF-EI (the 2004 Storm Order) established as Commission policy a methodology that can only be modified if a party presents evidence demonstrating a change in circumstances that warrants a modification. FPL asserts that application of the methodology it advocates in this docket – the actual restoration cost approach with an adjustment to remove capital costs – would result in the same total amount of 2005 storm-recovery costs as application

of the modified incremental cost approach used in the 2004 Storm Order, but in a more reliable manner. Thus, FPL argues, it has presented evidence to justify use of its proposed methodology instead of the methodology used in the Commission's 2004 Storm Order. FPL contends that Intervenor, who argue for the use of a different version of the modified incremental cost approach used in the 2004 Storm Order, have not provided evidence justifying use of their proposed methodology. (FPL BR at 23-24)

Further, FPL notes that in the 2004 Storm Order, the Commission rejected arguments that FPL should share some portion of its 2004 storm costs with ratepayers. FPL asserts that the rejection of these arguments demonstrated the Commission's support of "the fundamental principle of recoverability of prudently incurred costs." FPL states that it reasonably relied on this portion of the 2004 Storm Order, and earlier instances where the same principle was recognized, in planning its operations. FPL contends that any change at this point, i.e., a decision to require some sharing, would be retrospective and punitive. (FPL BR at 22-23)

OPC asserts that the 2004 Storm Order contains some precedent for the Commission's decision in this case. However, the Commission can amend its "policy decisions" concerning the appropriate accounting methodology to use in this case to the extent that such amendments are supported by expert testimony and other evidence appropriate to the nature of the issues involved. (OPC BR at 9-10) OPC's position is joined by AARP, FIPUG, FEA, and the AG.

FRF asserts that the 2004 Storm Order is non-binding precedent. FRF contends that because all ratemaking is inherently prospective and legislative, the Commission may make any reasonable decision supported by the evidence of record in this case. (FRF BR at 55)

ANALYSIS

In the 2004 Storm Order, the Commission addressed several substantive issues. In summary, the Commission determined the following: (1) the manner in which 2004 storm-recovery costs were to be charged to FPL's Reserve; (2) the prudence of the 2004 costs; (3) the recoverable amount of the 2004 costs; and (4) the means by which the 2004 costs would be recovered. Pursuant to the doctrine of administrative finality, these decisions – which related only to 2004 storm costs – may be modified only if there is a significant change in circumstances or if modification is required in the public interest.²

Staff's understanding is that this issue was intended primarily to address whether, and to what extent, the Commission may be bound by its determination in the 2004 Storm Order that a particular methodology – the modified incremental cost methodology – was the appropriate manner in which to account for the 2004 storm-recovery costs. As explained below, the Commission is not bound by that determination with respect to the accounting for 2005 storm-recovery costs.

In the 2004 Storm Order, the Commission evaluated different methodologies for charging items to FPL's Reserve. Based on its evaluation of the evidence presented in that case, the

² See *Florida Power Corp. v. Garcia*, 780 So.2d 34 (Fla. 2001), citing *Austin Tupler Trucking, Inc. v. Hawkins*, 377 So.2d 679, 681 (Fla. 1979).

Commission found that a modified incremental cost approach was appropriate for accounting for the 2004 storm-recovery costs. The doctrine of administrative finality provides that this finding should be final with respect to the specific matter at issue – the 2004 storm-recovery costs. The Commission’s decision with respect to the 2005 storm-recovery costs should be based on the evidence of record in this proceeding. Thus, while the Commission may find some guidance in the rationale supporting this finding, the finding does not operate as legally binding precedent with respect to the manner in which 2005 storm-recovery costs should be charged to FPL’s Reserve. This result was envisioned by the Commission when it voted to approve the modified incremental cost approach for 2004 costs, as reflected in the following exchange during the Commission’s July 19, 2005, Agenda Conference:

CHAIRMAN BAEZ: . . . [D]oes our decision today remedy [the fact that there is no established accounting methodology for costs charged to the Reserve] by saying this is the methodology that we are going to be using, or is it still, or does it still continue with the flexibility that I think forms the basis of the recommendation? . . .

COMMISSIONER DEASON: . . . I will be glad to share my views on that. I think until this Commission sets out a policy, preferably in a rulemaking as to what the specific accounting treatment is going to be, we retain our case-by-case flexibility. And that whatever decisions we make on the subsequent issues that follow Issue 1, that that is case-specific, based upon the facts of this record, and that we are not in the process of trying to establish an in-concrete procedure, accounting mechanisms, or whatever you want to call it that are going to be adhered to in the future. I think that really needs to be done in a rulemaking docket.

(Transcript of Item 17, July 19, 2005, Agenda Conference.) No further discussion followed this exchange prior to the Commission’s vote on the issue.

A rulemaking proceeding was initiated in November 2005 to attempt to establish a uniform and standardized methodology for identifying and charging costs of storm damage restoration to the utilities’ reserve accounts. That rulemaking proceeding is ongoing.

For the same reasons that the 2004 Storm Order does not operate as binding precedent with respect to the accounting methodology to be used in this case, it also does not operate as binding precedent with respect to the sharing of 2005 storm costs proposed in this case. As previously noted, the 2004 Storm Order addressed only 2004 storm costs. Thus, the findings in that order could not be reasonably relied upon by any party to be determinative of the treatment of 2005 storm costs.³

³ Staff witness Jenkins has proposed a sharing of prudently incurred 2005 storm costs. Witness Jenkins’ sharing proposal is addressed in Issue 35 of this recommendation, where the policy and legal questions surrounding the proposal are more fully addressed.

CONCLUSION

Based on its analysis, staff concludes that Order No. PSC-05-0937-FOF-EI does not operate as binding precedent with respect to the decisions to be made in this proceeding, including determinations of the appropriate accounting for 2005 storm costs and whether any “sharing” of 2005 storm costs should be required. The decisions in this docket should be made based on the record evidence in this proceeding.

Issue 6: What is the appropriate methodology to be used for booking the 2005 storm damage costs to the Storm Damage Reserve?

Recommendation: The incremental cost approach, including an adjustment to remove normal capital costs, is the appropriate methodology to be used for booking the 2005 storm damage costs to the Storm Damage Reserve. (Slemkewicz)

Position of the Parties

FPL: FPL recommends using the Actual Restoration Cost Method addressed in Docket No. 930405-EI with an adjustment to remove normal capital costs. It should be noted that FPL's proposed methodology yields the same result as the Modified Incremental Cost Approach approved by the Commission in the 2004 Storm Cost Recovery Order, Order No. PSC-05-0937-FOF-EI.

OPC: The risk shouldered by ratepayers in compensating companies for storm damage costs should be limited to the incremental costs incurred by utilities in restoring service to ratepayers that were prudently incurred, reasonable in amount, and otherwise properly charged to the storm reserve account. Because the storm reserve should be limited to incremental costs of restoring the system, so-called "lost revenues" have no place in the Commission's determination, whether directly or indirectly.

FIPUG: Adopts the position of OPC.

FRF: The appropriate methodology is the incremental cost methodology advocated by the witnesses for the Citizens of the State of Florida.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL filed its case using the Actual Restoration Cost Method with an adjustment to remove normal capital costs. As stated by witness Davis, this methodology includes all of the costs that were incurred to restore electric service or return assets to their pre-storm condition. These costs, however, have been reduced by insurance proceeds and by the normal cost of capital items. The remaining costs represent the operations and maintenance expenses that were incurred to restore service to FPL's customers. (TR 437) The intervenors support OPC's position that an incremental cost recovery method should be utilized in this proceeding. Witness Larkin testified that this methodology would limit recovery to those additional costs incurred to restore service that exceeded costs that were already considered and reflected in rates. (TR 890)

ANALYSIS

In prior proceedings concerning the recovery of storm damage restoration costs, the Commission approved variations of the incremental cost approach. This is true whether the methodology was approved after an adversarial proceeding⁴ or was the result of a stipulation.⁵ However, the methodologies used in those dockets did not establish any precedence for use in later dockets or as a continuing standard for charging costs to the storm reserve.

FPL's proposed methodology is the Actual Restoration Cost Method with an adjustment to remove normal capital costs. Witness Davis testified that some of the key attributes of this methodology are as follows:

This method, excluding an adjustment to capital costs, was utilized by the Company between 1993 and 2003 to determine the storm restoration costs to be charged against the Reserve. For this proceeding, FPL's proposed method includes all costs which are incurred to safely restore electric service or return plant and equipment to its pre-storm condition. The adjustment to remove capital costs will be at "normal cost" and recorded to rate base. What is left after adjusting for insurance recoveries represents the operations and maintenance expenses the Company has incurred to restore service to its customers.

(TR 437)

Witness Davis stated that:

FPL believes that its proposed method should be adopted for several reasons. First and foremost, this method is by far the most accurate way to account for storm restoration costs. Also, it is totally consistent with sound and commonly accepted cost accounting principles, procedures and practices. Accordingly, it results in accounting and recovery of the actual costs incurred to restore electric service.

(TR 438)

As witness Davis testified, the purpose of FPL's proposed method is to replicate the cost recovery that FPL would receive under a hypothetical third party replacement cost insurance policy. (TR 439)

On rebuttal, FPL witness Gower supported FPL's proposed Actual Restoration Cost Method with an adjustment to remove normal capital costs. Witness Gower also refuted the individual adjustments proposed by OPC witnesses Larkin and DeRonne. (TR 1516-1563)

OPC's proposed methodology is the incremental cost approach including an adjustment to remove normal capital costs. OPC witness Larkin testified that:

⁴ Docket No. 041272-EI, Progress Energy Florida, Inc.; Docket No. 041291-EI, Florida Power & Light Company.

⁵ Docket No. 050093-EI, Gulf Power Company; Docket No. 050225-EI, Tampa Electric Company.

The Company's cost accumulation under storm damage work orders results in the accumulation of all payroll and all materials, supplies and other costs charged to the work order being accumulated as storm damage costs. This is so even though some of the payroll costs and some material and other costs are reflected in rates and collected from ratepayers during the normal course of business or are costs that are part of the business risk which the Company should bear.

(TR 892-893)

In essence, witness Larkin is stating that the recovery from ratepayers should be limited to incremental costs incurred to restore service. Witness Larkin also stated that “. . . incremental cost should reflect only those additional costs incurred by the company in restoring service which exceed costs already considered and reflected in rates.” (TR 890)

Commenting further on incremental costs, witness Larkin testified:

FPL storm accounting system does not account for only incremental costs. It accounts for total cost of any employee, material, contract cost, supplies, etc. charged to a storm work order. The accounting process utilized by FPL does not account or attempt to account for the portion of the cost charged to storm work orders that are incremental to the Company's normal operating expense. The accounting process, which FPL labels as accurate, merely charges every cost associated with employees' work on the storm, rather than trying to segregate only that cost which is incremental to normal payroll, maintenance and other expense.

(TR 894-895)

Witness Larkin stated that granting FPL's requested storm costs would result in customers paying twice for the same cost: once in base rates, and once through a storm restoration charge. (TR 932) Witness Larkin stated that the approach advocated by OPC, on the other hand, allows FPL to recover all reasonable and prudent incremental storm costs, but only once. (OPC BR at 12)

CONCLUSION

The purpose of this issue is to establish the basic methodology to be utilized to determine the amount of storm damage restoration costs that should be charged against the storm reserve. The validity and appropriateness of the amounts, and the method for developing those amounts, in any of the individual adjustments addressed in the subsequent issues must be decided on their own merits.

Staff agrees with FPL that its cost accounting system tracks all of the costs that it believes are incurred for storm damage restoration activities. Some of these costs, by necessity, are estimates until the activities can be completed. The cost accounting system, however, is driven by the activities and costs that FPL specifies are to be included as storm damage restoration costs. Reasonable people can disagree whether any particular cost or activity is actually related to storm damage restoration. The issue at hand, however, is not whether the costs were actually

incurred, but how those costs should be apportioned for recovery. FPL's Actual Restoration Cost Method, with capital cost adjustment, assumes that none of the costs have been recovered through base rates. Therefore, all costs not recovered through base rates are to be charged to the reserve and any significant shortfalls should be recovered from the ratepayers. Staff believes that OPC has demonstrated that some of the storm damage restoration costs are already being recovered through base rate revenues, resulting in a double recovery. Although staff does not agree with all of OPC's proposed adjustments, staff does agree that the use of an incremental cost approach, with an adjustment for normal capital costs, is the appropriate methodology to use in this proceeding.

Issue 7: Has FPL charged to the storm reserve any costs associated with replacements or improvements that would have been needed in the absence of 2005 storms, and so should be charged to regular O & M or placed in rate base and accounted for accordingly? If so, what adjustments should be made?

Recommendation: Yes. The 2005 storm-related costs should be reduced by \$6,474,957. (Slemkewicz, Haff)

Position of the Parties

FPL: No. FPL has only charged storm-related costs to the Storm Reserve. Therefore, no adjustments should be made.

OPC: Yes. FPL has charged several items to the 2005 storm recovery costs that were maintenance projects planned prior to the damage incurred in 2005 by the storms, normal maintenance costs or offsets to O&M expenses which are recovered through base rates. These items include condenser tube repairs, hydrolasing costs, and amounts received from other utilities.

FIPUG: Adopts the position of OPC.

FRF: Yes. Agree with OPC as to the amounts to be adjusted for such items, including condenser tube repairs, hydrolasing, and loan of FPL personnel and equipment to other utilities.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that only storm restoration costs and costs needed for repairs to return the Company's equipment and facilities to pre-storm condition were charged to the storm reserve. (TR 452) Therefore, no adjustments need to be made.

OPC witness DeRonne testified that FPL had charged several items, totaling \$6,474,975, to the 2005 storm recovery costs that were planned maintenance, normal maintenance, or offsets to base rate O&M expenses. Witness DeRonne said that these costs should be removed from the 2005 storm costs.

ANALYSIS

Condenser Tube Repairs (\$2.8 million)

FPL witness Davis testified that the condenser tube repair costs of \$2,785,364 are a capital item and should be removed from the 2005 storm costs. (TR 1610) OPC witness DeRonne agreed that the condenser tube repairs should not be included in the 2005 storm costs. (TR 970) Therefore, staff recommends that the 2005 storm costs be reduced by \$2,785,364 to remove the condenser tube repair costs.

Hydrolasing Costs (\$221,000)

FPL witness Davis testified that FPL's review of necessary repairs identified the need for hydrolasing the condenser tubes. The need for this work was caused by storm debris passing through the tubes, and was necessary to enable a proper assessment of the condition of the tubes after the hurricane. As such, the \$0.2 million in hydrolasing costs were not part of normal maintenance activities and are properly included in FPL's 2005 storm costs. (TR 1611)

OPC witness DeRonne said that FPL's 2005 storm cost estimate also includes \$144,000 for hydrolasing the Martin Unit 1 and 2 condenser tubes and \$77,000 for hydrolasing the Martin Units 3 and 4 condenser tubes. The hydrolasing was conducted to clean the tubes to prepare for testing and is a normal, recurring maintenance item included in base rate recovery. Even without any storm activity, FPL had projected to perform condenser tube hydrolasing at Martin Units 1 and 2 in the spring of 2006, at Unit 3 in Fall of 2007 and Unit 4 in Spring 2008. (TR 971-972)

Based on the evidence presented, the hydrolasing would have been done in any event, so it should be treated as regular maintenance and not charged to the storm reserve. Staff recommends that the 2005 storm costs should be reduced by \$221,000 to remove the hydrolasing costs.

Proceeds from Other Power Companies (\$9,095,845)

During 2005, FPL billed \$9,095,845 for the loan of Company personnel and equipment to other power companies for storm restoration activities. FPL witness Davis said that FPL has properly accounted for costs and reimbursements for emergency aid it provided to other utilities during 2005. These costs and reimbursements have nothing to do with the 2005 storm restoration costs charged to the Reserve. Because FPL's costs for sending employees to help other utilities were never charged to FPL's Reserve, it is not proper to seek to disallow such costs or to seek to apply reimbursements for any such costs against the Reserve charges for the 2005 storms. (TR 1618-20)

Witness Davis further testified that:

When FPL sends its personnel to assist others, it captures actual costs incurred in a job order. When the assistance is complete, FPL applies appropriate loaders to the job order, as it would for any third party billing, and then provides an invoice to the host utility. Under the terms of the mutual aid agreements, FPL is not

allowed to bill the host utility for overtime it pays its remaining crews to maintain work schedules due to the absence of personnel sent to assist the utility. Those costs are charged to normal operations and maintenance expenses by FPL and offsets the payments received from other utilities.

(TR 1618-1619)

OPC witness DeRonne said that the majority of the reimbursements received by FPL for assisting other utilities in storm recovery efforts should be used as an offset to FPL's restoration costs. If this offset is not made, then FPL would recover the costs both in base rates and from the other utilities' reimbursements. Witness DeRonne would reduce the \$9,095,845 by the \$2,227,252 pertaining to travel and other costs not considered in base rates. (TR 975-976) In its brief, OPC agreed with another reduction to the \$9,095,845 in the amount of \$3,400,000. According to FPL witness Davis, the \$3,400,000 represents overtime payroll and materials that were not included in base rates or the 2005 budget. (TR 1620) This would leave a net adjustment of \$3,468,593. Witness Davis said that a further reduction of \$300,000 was warranted for back-fill work. (TR 1620)

Although FPL does not agree that this adjustment should be made, it did propose reductions to the adjustment if it was made. Staff agrees with OPC that this adjustment should be made in the amount of \$3,468,593. As discussed in Issue 17b, staff does not believe that back-fill work should be included.

CONCLUSION

Based on the above discussion, staff recommends that the 2005 storm costs be reduced by \$6,474,957, calculated as follows:

Condenser Tube Repairs	\$(2,785,364)
Hydrolasing Costs	(221,000)
Proceeds from Other Utilities	<u>(3,468,593)</u>
Total Adjustment	<u>\$(6,474,957)</u>

Issue 8: Has FPL quantified the appropriate amount of non-management employee labor payroll expense that should be charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. Non-management employee labor payroll expense and the employee benefits charged to the storm reserve for 2005 should be reduced by \$17,925,918. The Company should also be required to provide substantiation of the reassignment of the \$2,730,000 from clause activity to the storm reserve in its clause true-up filings. (Romig, Willis)

Position of the Parties

FPL: Yes. FPL correctly quantified and included all regular payroll as a direct result of the 2005 storms for exempt, non-exempt and bargaining personnel, subject to an adjustment to remove normal capital costs. Because FPL tracks payroll costs by exempt, non-exempt and bargaining unit personnel, FPL does not separately quantify amounts of "non-management employee labor payroll expense." No adjustments should be made.

OPC: No. Adjustments are necessary to ensure that the amount of payroll and labor related costs already recovered by FPL through base rates is not also recovered a second time through the recovery of the 2005 storm costs. The following adjustments are appropriate:

Remove Estimated Regular Employee Salaries	(\$26,092,000)
Less: Payroll Normally Charged to Clauses	2,730,000
Less: Capital Payroll in Regular Salaries	8,000,000
Remove Employee Benefits - Already in Base Rates	(9,213,514)
Total Incremental Salary/Payroll Related Adjustments	(\$24,575,514)

FIPUG: Adopts the position of OPC.

FRF: No. Agree with the \$24,575,514 in adjustments calculated and advocated by OPC's witnesses.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS & ANALYSIS

Because FPL tracks payroll costs by exempt, non-exempt, and bargaining unit personnel, FPL does not separately quantify amounts of non-management employee labor payroll expense. (TR 1596-97) Based on FPL's "Actual Restoration Cost" method as filed, FPL proposes to include \$26,092,000 in the 2005 storm reserve costs for regular payroll and \$60,334,000 for

overtime payroll. (EXH 13, p. 1) However, FPL concedes that in the event the Commission decides to apply its 2004 Storm Cost Recovery Method, then it should consider offsets to the \$26,092,000 million adjustment of \$2,730,000 for labor ordinarily charged to clauses, \$8,000,000 for labor ordinarily charged to capital, \$2,237,000 of additional capital payroll in regular salaries, and \$2,490,800 of nuclear payroll expected to be recovered through insurance. In addition, FPL agrees that under this method, an adjustment to remove payroll loadings related to the ordinary payroll removed is appropriate. (TR 959; EXH 121; FPL BR at 44-50) FPL testified that a reduction of \$10,634,200, excluding payroll loadings, and \$11,833,766, including a calculated payroll loading of \$1,692,566 to the requested 2005 Storm Costs, should be made if the 2004 Storm Cost Recovery Method is applied.

OPC advocates using the Incremental Cost Approach. (OPC BR at 15) Witness DeRonne testifies that using the incremental approach, the \$26,092,000 in regular employee salaries that should be removed from 2005 Storm Recovery Costs should be offset only for capital payroll of \$8,000,000 and payroll normally charged to clauses of \$2,730,000. (TR 959) Witness DeRonne further testified that in addition to the removal of \$26,092,000 of regular payroll, FPL's 2005 Storm Recovery Costs also should be reduced by incremental employee benefits of \$9,213,514. (TR 960; EXH 85, pp. 1-2) OPC witnesses DeRonne and Larkin testified that a reduction of \$24,575,514 to the requested 2005 Storm Costs should be made.

SUMMARY

Under the incremental approach, both FPL and OPC agree that ordinary payroll costs included in the petition are \$26,092,000, and that offsets of \$8,000,000 and \$2,730,000 for capital payroll and clause payroll are appropriate. In addition, FPL argues that nuclear payroll expense of \$2,490,800 should offset the \$26,092,000 adjustment, so as not to double-deduct; OPC argues that offsetting is not appropriate as it would give double-recovery. FPL proposed an offsetting adjustment of \$2,237,000 for payroll included in the 2005 estimated capital storm costs as of March 31, 2006; OPC argues that there is no evidence supporting that this is in addition to the \$8,000,000 adjustment for capital payroll and the \$2,237,000 offsetting adjustment should therefore be rejected. OPC argues that payroll loading costs of \$9,213,514 should be in addition to the \$26,092,000 adjustment; FPL argues a payroll loading adjustment of \$1,195,000 is appropriate based on its proposed payroll adjustments that were calculated based on the 2004 cost recovery order approach.

1. Capitalized Payroll Costs (\$8,000,000)

Under the incremental cost approach, FPL and OPC agree that an \$8,000,000 offset to the \$26,092,000 regular payroll adjustment is appropriate. FPL states that regular payroll charged to the storm reserve that would have ordinarily been charged to capital should be allowed to be recovered through the storm reserve since they are not being recovered through base rates. Because normal payroll has a capital component, the assumption that all regular payroll charged to storm is related to operations and maintenance work is incorrect. The regular payroll dollars in the 2005 storm costs include payroll dollars for employees that under normal working conditions would charge their time, or a portion of their time, to capital projects. Therefore, those costs should not be disallowed under the incremental cost methodology. (EXH 126, pp. 1-2) OPC agrees with this offset. (EXH 85) Staff believes that this offset should be accepted. To disallow this offset would effectively disallow recovery as there is no provision to recover it in

base rate operation and maintenance costs and it cannot be assigned to non-existent capital projects. For this reason, staff recommends that the \$26,092,000 regular payroll adjustment be offset by \$8,000,000.

2. Payroll Normally Charged to Clauses (\$2,730,000)

Under the incremental cost approach, FPL and OPC agree that a \$2,730,000 offset to the \$26,092,000 regular payroll adjustment is appropriate. FPL states that regular payroll charged to the storm reserve that would have ordinarily been charged to clauses should be allowed to be recovered through the storm reserve since they are not being recovered through a cost recovery clause or through base rates. (EXH 126, pp. 1-2) OPC agrees with this \$2,730,000 offset. (EXH 85) Staff believes that this offset should be accepted. To disallow this offset would effectively disallow recovery as there is no provision to recover it in base rate operation and maintenance costs and it cannot be assigned to clause activity. For this reason, staff recommends that the \$26,092,000 regular payroll adjustment be offset by the \$2,730,000. However, to insure that the \$2,730,000 is not double-recovered, i.e., recovered through clause activity, staff recommends that follow-up work be accomplished to ascertain that reduced clause costs have been reflected in the clause proceedings. To insure that the \$2,730,000 in normal payroll costs were reassigned from clause activity to storm cost activities, staff recommends that the Company be required to provide substantiation of the reassignment of the \$2,730,000 from clause activity to the storm reserve in its clause true-up filings.

3. Nuclear Payroll Expected to be Recovered through Insurance (\$2,490,800)

FPL witness Davis testified that if the Commission determines that the regular payroll of \$26,100,000 should be removed from the 2005 storm costs, \$2,490,800 should offset these costs. Witness Davis states that nuclear payroll expected to be recovered through insurance should not be included in the regular payroll adjustment. If it is, then it will be subtracted twice from 2005 storm costs: once through the \$26,100,000 adjustment and then again when insurance proceeds are removed from 2005 storm costs. Witness Davis contends that this would be a double disallowance. Further, in its response to the Staff Audit Report (EXH 126, pp. 1-2) FPL stated:

The amount of regular employee salaries charged to the Reserve of \$26,092,000 included an estimate of \$2,490,800 related to nuclear Powerblock repairs, which is expected to be recovered through insurance. Under the incremental cost approach, nuclear payroll expected to be recovered through insurance should not be included in any such payroll adjustment. If it is, then it will be subtracted twice from the total amount of 2005 storm cost to be recovered.

(TR 1603; EXH 121; EXH 126; OPC BR at 46)

FPL witness Warner testified that removal of the \$2,490,800 from 2005 storm recovery costs associated with nuclear employee base salaries is not appropriate, since the \$2,490,800 is not part of the \$17.9 million of nuclear division storm costs requested in this proceeding. Therefore, this amount should not reduce FPL's storm costs since it is not a part of those costs. (TR 391)

On cross-examination, staff witness Welch agreed that FPL adjusted the amount of regular payroll charged to the reserve to account for amounts that it expected to recover through insurance. She agreed that the \$2,490,800 of nuclear payroll expected to be recovered through insurance was not charged to the reserve and that the \$26,100,000 regular payroll adjustment should be reduced by the \$2,490,800. (TR 1100-01)

Witness DeRonne testified that FPL's calculations under the incremental cost approach included a \$2,490,800 offset to the regular employee salary adjustment to reflect the fact that a portion of these payroll costs had already been removed from the 2005 estimated storm recovery costs in the adjustment to remove the estimated insurance proceeds. (TR 959) Witness DeRonne does not believe that the \$2,490,800 offset to the regular employee salaries is appropriate. She testified that if this adjustment is reflected, FPL would recover the associated amount twice, once from the insurer and again from ratepayers. Witness DeRonne believes that the regular employee salary amount included in FPL's storm recovery costs that is being removed under the incremental cost approach, totaling \$26,092,000, is already being recovered in base rates. If the Company both recovers the \$2,490,800 of nuclear employee base salaries from insurers and also offsets the adjustment to remove base salaries from the storm costs by the same \$2,490,800, it will recover these costs both from the insurer and from the customers in base rates. (TR 960)

Staff believes that even though the \$2,490,800 has been removed from the reserve, FPL is still going to recover the amount twice, once from the insurer and once from the ratepayer. The issue of double recovery of the normal payroll due solely to the storms still exists because it is now being recovered through the insurer. Staff is persuaded by witness DeRonne's testimony and therefore the \$2,490,800 should be credited to the reserve and used to reduce storm costs.

4. Additional Capital Offset (\$2,237,000)

FPL witness Davis testified that the \$8,000,000 offset to normal payroll costs of \$26,100,000 that both FPL and OPC agreed was appropriate and was understated by \$2,237,000. FPL witness Davis represents that as of March 31, 2006, the total amount of estimated capital expenditures recorded by FPL is \$72,553,747. Of this amount, \$2,237,000 has been categorized as FPL regular payroll. (EXH 123) Witness Davis has shown this amount as an additional offset to the \$26,100,000 normal payroll cost adjustment. (EXH 121, p. 2)

OPC argues that there is no evidence that the capital offset proposed by FPL has not already been factored into FPL's \$8,000,000 adjustment to offset the salary adjustment by the amount of payroll normally charged to capital. OPC states that the additional \$2.2 million offset under the incremental approach proposed by FPL should not be accepted by the Commission. (OPC BR at 16)

Although staff is unable to ascertain whether the \$2,237,000 is part of the \$8,000,000 capital payroll offset, staff has found no evidence that the \$2,237,000 was not factored into the \$8,000,000 offset. Therefore, staff is uncertain whether the \$2,237,000 should be an offset. Further, staff calculates that the \$8,000,000 capital payroll offset agreed to by both FPL and OPC represents 31 percent of the normal payroll charged to 2005 storm costs. Based on this uncertainty as well as the percentage of capital payroll represented by the \$8,000,000, staff recommends that this offset not be made.

5. Applied Pensions and Welfare (OPC, \$9,213,514; FPL, \$1,195,000)

OPC witness DeRonne proposed an additional adjustment reducing FPL's storm costs based on a claim that FPL has erroneously included \$9,213,514 in "Applied Pensions and Welfare." (TR 960-61) Witness DeRonne states that these costs are already included in base rates and budgets and "would not increase as a result of a storm event," and therefore, should not be included in the 2005 storm costs. She also states that the \$9,213,514 in benefits are not incremental costs resulting from the storms and therefore should not be allowed. (TR 960-61)

FPL witness Davis contends that OPC witness DeRonne's claimed adjustment is incorrect, and the supposition upon which it is based is faulty, even if one were to implement the "incremental approach" advocated by OPC. (TR 1606)

On rebuttal, witness Davis provided a calculation to support that the sum of payroll loadings included in the 2005 storm costs is \$8,391,100, not \$9,213,514. Witness Davis states that the difference of \$822,414 is attributable to adjustments either not reflected or not fully explained in FPL's response to OPC's 9th Set of Interrogatories, No. 184. FPL witness Davis claimed that the \$8,391,100 consists of \$4,354,755 of payroll overhead related to regular payroll based on an overhead rate of 16.69 percent and \$4,036,345 pertaining to overtime payroll based on an overhead rate of 6.69 percent. FPL also claimed that in addition to the items included in the response to OPC for pensions, welfare and insurance, the payroll overheads also include payroll taxes. With regard to the application of payroll overheads associated with overtime payroll, FPL claims that the 6.69 percent overhead rate is lower as it only includes social security taxes. (TR 1606-07; EXH 124)

Witness Davis testified that the payroll overhead applicable to regular payroll included in the 2005 storm costs is \$4,354,755 (\$2,610,000 at 16.69 percent), which is the same overhead rate applied to regular payroll in the ordinary course of business. The payroll overhead applicable to overtime payroll included in the 2005 storm costs is \$4,036,345 (\$60,334,000 at 6.69 percent). The lower overhead applied to overtime payroll is based on the assumption that only social security taxes apply to overtime payroll. (TR 1606-07; EXH 124)

Witness Davis testified that therefore, if the Commission disallows recovery of any portion of the regular payroll, then the applicable payroll overheads associated with this amount should be computed and reduced using the appropriate percentage discussed above instead of removing the entire amount. The applicable percentage should also be applied to any regular payroll offsets approved by the Commission. (TR 1607)

OPC contends that the appropriate adjustment to 2005 storm recovery costs is \$9,213,514. (OPC BR at 18)

Based on the arguments set forth by both FPL and OPC, the 2005 storm recovery costs include an amount for payroll loading related to normal and overtime payroll. Staff believes that there is persuasive evidence indicating that the payroll loading costs related to normal payroll approximate \$4,354,755 (16.69 percent of \$26,092,000) and the payroll costs for overtime payroll approximate \$4,036,345, (6.69 percent of \$60,334,000).

In general, payroll loadings follow the payroll. If payroll is capitalized, the payroll loadings are also capitalized. If payroll is charged to a clause, the payroll loadings are charged to the clause. Therefore, if one removes a piece of payroll from the 2005 storm recovery costs, it follows that the related piece of the payroll loading should also follow and be removed. In this issue, staff is recommending removal of a net \$15,362,000 in regular payroll (\$26,092,000 – (\$8,000,000 + \$2,730,000)). Applying 16.69 percent to the amount of normal payroll that staff is recommending be removed results in the recommended decrease of \$2,563,918 for the related payroll loadings (.1669 * \$15,362,000).

CONCLUSION

In conclusion, the normal payroll of \$26,092,000 should be removed with offsets for capital payroll of \$8,000,000 and clause payroll of \$2,730,000. This results in allowing \$10,730,000 in regular payroll in the 2005 storm recovery costs, and excluding \$15,362,000. In addition, related payroll loadings of \$2,563,918 should be removed. The payroll loadings were calculated consistent with FPL's .1669 factor. Therefore, staff's recommended adjustment to 2005 storm costs is \$17,925,918.

Issue 9: Has FPL quantified the appropriate amount of managerial employees payroll expense that should be charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. Managerial employees payroll expense charged to the storm reserve for 2005 should be reduced by \$768,000 to remove exempt employee overtime pay. (Romig)

Position of the Parties

FPL: Yes. FPL correctly quantified and included all regular payroll as a direct result of the 2005 storms for exempt, non-exempt and bargaining personnel, subject to an adjustment to remove normal capital costs. Because FPL tracks payroll costs by exempt, non-exempt and bargaining unit personnel, FPL does not separately quantify amounts of “managerial employees payroll expense.” No adjustments should be made.

OPC: No. The storm recovery cost is not a basis on which to provide extra compensation to employees who are salaried and have accepted that salary as full compensation for all time that they are required to put in. The 2005 storm costs should be reduced by \$768,000 to remove exempt employee overtime incentives.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that FPL's 2005 storm costs should be reduced by \$768,000 to remove exempt employees' overtime incentives.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

Because FPL tracks payroll costs by exempt, non-exempt, and bargaining unit personnel, FPL does not separately quantify amounts of management labor payroll expense. (FPL BR at 50) In its 2005 storm recovery costs, FPL included \$768,000 for exempt employee overtime incentives. FPL witness Davis explained that the salaries of the exempt employees who received the overtime pay are based on normal job requirements, not extraordinary storm restoration. Prohibiting any incentive payments made to employees who are involved in storm restoration that do not get paid overtime is inappropriate. These payments were determined in a manner consistent with the manner in which overtime payments were computed for other employees and was limited to the amount necessary to avoid inequities. (TR 1617)

FPL states that its policy for paying overtime to these employees during certain storm restoration efforts is a reasonable and appropriate storm cost. FPL witness Williams testified that, in general, the decision to pay or not pay for overtime is primarily based on the length of the

restoration effort. For Wilma, an eighteen-day restoration effort, many of FPL's employees worked sixteen-hour days continuously for the entire restoration period. During storm work, it is possible for two people, who normally are in different pay grade classifications, to be performing the same function during the restoration period. As a result of their normal pay grade classification, one might be eligible for overtime while the other is not. It would not be reasonable for only one to be compensated for their extraordinary overtime. These overtime payments were limited to the amount necessary to avoid inequities, and accounted for only 1.3 percent of total storm related overtime. (TR 1403-04)

FPL witness Davis testified that the record shows that the \$768,000 of overtime costs are reasonable and directly caused by the need to perform storm restoration duties and, accordingly, should be approved by the Commission. (TR 1617) Moreover, witness Davis testified that the exclusion of overtime pay proposed by OPC would provide management level personnel with a disincentive to work on storm restoration. The nature of storm restoration is such that all available personnel, without regard to pay grade classification, are asked to report for storm duty to ensure the prompt restoration of service to FPL's customers. (TR 1617)

FPL concludes that this is an equity issue to compensate employees that performed the same storm duties, but who are compensated differently per "contract."

OPC witness Larkin claims that exempt employee overtime pay should be removed from FPL's 2005 storm costs because an assertion that such employees' regular pay is "full compensation for all time that they are required to put in." (TR 915-16) Witness Larkin testified that salaried employees receive their compensation for the level of work that is required of them. They are not compensated based on a fixed number of hours of work. When overtime is required of salaried employees, they are responsible for providing that additional work for the salary they agreed to accept. The Company does not compensate these employees for additional time they might put in when work load requires that they spend additional hours, such as month end accounting closings or special projects with short due dates. The storm recovery cost is not a basis on which to provide extra compensation to employees who are salaried and have accepted that salary as full compensation for all the time that they are required to put in. (TR 916)

ANALYSIS

Staff agrees with OPC that salaried exempt employees generally should not be compensated for overtime that is charged to the ratepayers. Staff also believes that there can be an equity issue during hurricanes, which are extraordinary events. Hurricanes can cause day-to-day job duties to differ from one's normal duties. However, staff agrees with witness Larkin that salaried employees are not compensated based on a fixed number of hours of work and they are responsible for providing that additional work for the salary they agreed to accept. For this reason, staff recommends that 2005 Storm Recovery Costs be reduced by the \$768,000 for exempt employee overtime.

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CONCLUSION

Based on the foregoing, staff recommends that managerial employees payroll expense charged to the storm reserve for 2005 be reduced by \$768,000 to remove exempt employee overtime pay.

Issue 10: WITHDRAWN

Issue 11: Has FPL properly quantified the cost of tree trimming that should be charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. The cost of tree trimming charged to the storm reserve for 2005 should be reduced by \$1,100,000. (Romig, Lee)

Position of the Parties

FPL: Yes. FPL's storm restoration costs only include the reasonable costs of removing vegetation as a result of the storms. Routine tree trimming is not charged to the Storm Reserve. No adjustments should be made.

OPC: No. Adjustments are necessary to ensure that costs recovered by FPL through base rates are not recovered a second time through recovery of storm costs. A \$1,100,000 reduction to the tree trimming costs is appropriate to reflect that FPL's actual expenditures for non-storm related tree trimming were less than it included in its budget for 2005 tree trimming.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that FPL's claimed tree-trimming costs should be reduced by \$1.1 million.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

Based on the 2004 Storm Restoration Costs Order approach, one of FPL's 2005 adjustments to its 2005 storm costs removes \$1,100,000 for incremental tree trimming expenses. (EXH 121) Although the basis for the 2005 tree trimming adjustment is consistent with the basis for the tree trimming adjustment made by the Commission in the 2004 Storm Order, FPL does not believe the 2005 adjustment for \$1,100,000 is appropriate. The basis for the 2004 adjustment and the 2005 adjustment relies on FPL's actual tree trimming expenditures being less than budgeted. FPL does not believe the adjustment is appropriate because the reasons for the variance between budget and actual are not known. (TR 1020-21)

FPL argues that relying upon the budget variance as a basis for the proposed disallowance lacks logic and should be rejected, as the reason for the budget variance may be

attributable to the change in scope of tree trimming or other reasons that may have been discussed in budget meetings concerning vegetation management. (FPL BR at 54; TR 1020-21)

According to FPL:

OPC's overall theory of denying storm cost recovery based upon the so-called incremental approach has been discussed elsewhere in this brief, and shown to be unsound and unnecessary because of the absence of any double recovery of costs by FPL. In addition, it is clear that at the detailed implementation level of OPC's disallowances using the so-called incremental method, there is an utter lack of logical connection between the costs sought to be disallowed and whether the budget variance was caused by the storm.

Where, as here, OPC's proposed adjustment is contrary to extensive evidence in the record that FPL's storm vegetation removal expenses were reasonably managed and prudently incurred, the Commission should allow FPL's storm costs and deny OPC's requested adjustment.

(FPL BR at 54-55)

OPC witness DeRonne testified that in its Incremental Cost Methodology calculation provided in its supplemental response to OPC Interrogatory No. 30, and as shown on Exhibit 121, p. 2, FPL witness Davis included a reduction to tree trimming costs for the amount under budget. (TR 958)

FPL's actual expenditures for non-storm related tree trimming were \$1.1 million less than it included in its budget for 2005. (TR 961) Witness DeRonne testified that the \$1.1 million adjustment is reasonable and should be made. (TR 958; EXH 85) OPC argues that since customers have already paid for the full level of FPL's budgeted tree-trimming expense in base rates, an adjustment of \$1.1 million should be made to storm related tree-trimming expense so that customers do not pay twice for the same expense: once through base rates, and a second time through a hurricane surcharge. (OPC BR at 20)

ANALYSIS

As stated by FPL, the reason for the 2005 tree trimming budget variance is unknown and may be attributable to the change in scope of tree trimming or other reasons that may have been discussed in budget meetings concerning vegetation management. (FPL BR at 54; TR 1020-21) Disallowing a cost from recovery based solely on budget variances may not be preferred. However, absent evidence concerning the reason for the variance, it cannot be determined with certainty if the variance was attributable to hurricane activity. FPL offered no evidence to substantiate that it was not attributable to the hurricane activity. Therefore, staff recommends that 2005 Storm Costs be reduced by \$1,100,000. This is consistent with the 2004 treatment.

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CONCLUSION

Based on the foregoing, staff recommends that 2005 Storm Recovery Costs be reduced by \$1,100,000, the amount under budget for 2005 tree trimming costs.

Issue 12: Has FPL properly quantified the costs of company-owned fleet vehicles that should be charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. Staff recommends that \$5,738,000 should be removed from the 2005 storm costs. (Marsh)

Position of the Parties

FPL: Yes, the actual costs have been correctly quantified. No adjustments should be made.

OPC: No. Adjustments are necessary to ensure that costs recovered by FPL through base rates are not recovered a second time through recovery of storm costs. A \$5,738,000 reduction is appropriate to remove a portion of the vehicle costs FPL indicates would have been incurred in the normal course of business, even absent the storms.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that FPL's claimed costs should be reduced by \$5,738,000 to ensure that vehicle costs are not inappropriately recovered through both base rates and through storm surcharges.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Williams testified that actual 2005 costs for fleet vehicles exceeded the budget by \$3.2 million. (TR 1408) She stated that about \$1.2 million of that amount was due to increased maintenance as a direct result of the 2005 storms. (TR 1408) She said that the incremental work was performed through the addition of a second shift and through the use of overtime hours at FPL's maintenance facilities. (TR 1408) She also testified that more parts and materials were also needed above the budgeted amount. (TR 1408)

FPL witness Davis testified that the incremental cost approach would include an adjustment to remove fleet vehicle costs that are included in base rates, as well as an adjustment to remove the normal cost of capital from the amount of storm costs to be recovered. (TR 1607) He stated that both adjustments include an amount for the estimated capital portion of fleet vehicle costs. (TR 1607) He said that if both the fleet vehicle costs and the capital amounts are adjusted, the capital portion of fleet vehicle costs will be removed twice. (TR 1607-1608) He testified that FPL applied the same "capital/operations and maintenance split" that FPL normally uses to determine the \$2.8 million capital amount associated with the storm costs. (TR 1608) He

stated that the adoption of OPC's budget-based incremental cost approach would necessitate consideration of the year-end operations and budget variances for Fleet Services. (TR 1608) Witness Davis also testified that the \$1.2 million in additional maintenance costs discussed by witness Williams partially offsets fleet vehicle costs as shown in his exhibits. (TR 1608; EXH 121, p. 2)

OPC witness DeRonne stated that she removed \$5,738,000 of vehicle costs because FPL would have incurred these costs during the normal course of business. (TR 961) She testified that her calculation represents only a portion of the total vehicle costs included in the storm recovery amounts and that the number is based on the monthly vehicle rates charged to the storm accounts. (TR 961-962) She said that certain incremental vehicle costs will remain in the storm recovery amount for both company owned and non-company owned vehicles after her adjustment is applied. (TR 962)

Witness DeRonne testified that FPL, in determining the vehicle costs using the incremental approach, offset the vehicle costs that would have been incurred in the normal course of business by 48 percent, or \$2,767,000 that FPL argues would otherwise have been charged to capital costs and not to base rates. (TR 962) She testified that she did not reflect this offset because it was not supported by FPL. (TR 962) The witness stated that a similar offset was proposed in FPL's 2004 storm recovery case. (TR 962) She said that the Commission recognized that OPC objected to FPL's rationale in the 2004 Storm Order. (TR 962) She testified that the Commission did not reflect FPL's proposed capital offset in that case, but removed "the entire amount identified by FPL as costs it would have incurred for the Company owned vehicles whether or not the storm occurred." (TR 962)

ANALYSIS

There are three pieces to the figure to be determined in this issue.

Amount Of Normal Costs

FPL indicates in its brief that \$5,738,000 is the amount to remove fleet vehicle costs from base rates and that OPC uses the same figure, so there is no dispute on that point. (FPL BR at 55) Staff believes the record is clear that this cost would have been included in base rates but for the storms. Accordingly, since it is already covered by the rates FPL's customers pay, staff agrees with OPC that it should be removed from the storm costs.

Incremental Maintenance Costs

It appears to staff that some amount of incremental costs may have been incurred by FPL for vehicles. FPL witness Williams stated that \$1.2 million was incurred due to increased maintenance as a result of the storms. There may be support for additional costs in FPL's response to Staff's Interrogatory No. 96, where FPL states that, in addition to the amount included in storm costs ". . . there are also incremental fuel and maintenance costs incurred in direct support of storm restoration efforts which are not forecasted nor included [in the figure]." (EXH 4, p. 64) Staff notes that the additional amount is not stated in the exhibit. FPL argues that this adjustment is not disputed in the record. (FPL BR at 55)

OPC witness DeRonne testified that there are incremental vehicle cost amounts remaining in the record after her adjustment of \$5,738,000. (TR 962) Further, OPC argued in its brief that FPL did not “demonstrate that the \$1.2 million for additional maintenance was not included in the vehicle costs included in the 2005 storm recovery costs presented by FPL.” (OPC BR at 21) Staff disagrees with FPL that this amount is undisputed. Although she does not state a dollar amount, OPC witness DeRonne makes it clear that she believes her adjustment leaves other vehicle costs remaining in storm costs. (TR 962)

Staff believes that if the incremental amount was included in FPL’s original filing, as OPC believes, it should remain in the storm recovery costs. However, if it was not included, given there is no explanation as to why it was not included, staff does not believe it should be added back to the vehicle costs as proposed by FPL. Staff does not believe it is plausible that FPL would have included only the normal amount of vehicle costs without including the amount that was over budget. Accordingly, no offsetting adjustment should be made.

Capital Costs

FPL witness Williams testified:

Under the incremental cost approach, there is an adjustment to remove fleet vehicle costs that are already included in base rates and another adjustment to remove the normal cost of capital from the amount of storm costs to be recovered. Included in both of these adjustments is an amount for the estimated capital portion of fleet vehicle costs. Therefore, if both the total amount of fleet vehicle costs and capital adjustments are made, then the estimated amount of the capital portion of fleet vehicle costs has been subtracted from the amount of storm costs to be recovered twice.

(TR 1607-1608)

Staff notes an apparent discrepancy in the amount of capital cost associated with vehicles. While FPL witness Davis indicated that an allocation of \$2,767,000 was made to capital costs, his exhibits show only \$1,525,159 of capital associated with vehicles. (TR 1608; EXH 123) The record is silent as to the reason for the difference. (EXH 121, p. 2; EXH 123) The most recent exhibit amount shows the breakdown of the total capital adjustment proposed by FPL, but does not indicate which amounts were included in the original filing, nor does it show whether the capital adjustment for vehicles is a part of the \$2,767,000. (EXH 123)

FPL’s EXH 123 shows only \$1,525,159 in capital adjustments associated with vehicles. Further, staff cannot determine whether this figure is part of the original filing. Staff agrees with FPL witness Williams that if the total fleet vehicle costs and FPL’s proposed total capital adjustment are both made, it would result in double counting. Nevertheless, in this circumstance, staff believes it is inappropriate to add back the capital cost when it is not clear whether it was part of the filing in the first place.

CONCLUSION

Staff recommends that \$5,738,000 should be removed from the 2005 storm costs.

Issue 13: Has FPL properly quantified the costs of call center activities that should be charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. An adjustment of \$520,264 should be made to reduce telecommunications expense. No other adjustment to call center expense should be made. (Marsh)

Position of the Parties

FPL: Yes. FPL's has quantified and charged to the Reserve call center incremental costs directly related to storm restoration. No adjustment should be made.

OPC: No. The actual operation and maintenance expenses for telecommunications costs in 2005 were \$520,264 less than budgeted. The proposed 2005 storm recovery costs should be reduced by this \$520,264 so that only the incremental telecommunications costs beyond those factored into base rates are included.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that FPL's claimed costs should be reduced by \$520,264.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: There are two components to this issue: call center costs and telecommunications costs.

PARTIES' ARGUMENTS

FPL witness Davis testified that the call center budget appears to be overspent for October and underspent for November 2005. (TR 593) He said that there was misbudgeting of payroll for that period. (TR 593) He explained that certain months have two biweekly payrolls, while other months have three. (TR 593) The witness testified that the budget was planned for three payrolls in November when there were three in October instead. (TR 593) He stated that FPL's normal costs exceeded the budget for September, October, and December, but he did not know the specific reason for the September and December variances. (TR 594)

Witness Davis stated that the variances in telecommunications costs include amounts for local and long distance service, cellular service, leased lines, pagers, and equipment maintenance. (TR 1609) He testified that the variances were not associated with the storm restoration during 2005. (TR 1609) He said that two specific items that reduced telecommunications costs were the negotiation of a lower long-distance contract rate, and a revision of FPL's cellular phone policy. (TR 1609) He stated that "FPL should not be penalized for its efforts at managing costs solely because storms affected its service territory." (TR 1609)

OPC witness DeRonne testified that she did not take issue with FPL on call center amounts because FPL indicated only incremental costs were included in the filing. (TR 958) She stated that a comparison of budget to actual costs did not show the company was under budget for the call center during the storm period. (TR 958)

Witness DeRonne testified that FPL's proposed 2005 storm recovery costs for telecommunications expenses were \$520,264 less than budgeted. (TR 962-963) She said that the storm recovery amount should be reduced "so that only the incremental telecommunications costs beyond those factored into base rates are included." (TR 963)

OPC witness Larkin testified that FPL ". . . had a savings associated with telephone rates that had nothing to do with any productivity gains, rates were just decreased." (TR 941) He stated that FPL wants to keep a gain that they "did nothing for" but expects ratepayers to pay for any communications with the company about storms. (TR 941) He said that any under-budget spending for 2005 should automatically be considered a storm savings. (TR 940)

OPC argued that, because the full budgeted amounts are already included in base rates, FPL customers would pay twice: once in base rates and once through the hurricane charge. (BR at 22) OPC argued that customers should be credited for the full amount included in base rates. (BR at 23)

ANALYSIS

Staff's comparison of FPL's 2005 call center costs to the budget for September through December 2005 shows that the normal costs were \$9,033,776, while the budget was \$8,535,211. Staff noted similar variances for other months during the year. The amount of \$6,187,253 that FPL included in its storm costs is incremental to the normal costs of \$9,033,776. Thus, staff agrees that only an incremental amount of call center costs is included in the storm costs. (EXH 4, p. 188)

The record is not clear whether the telecommunications expense amount of \$520,264 that OPC recommended for removal is included in storm costs. Staff has identified amounts of telecommunications expenses that are included. (EXH 4, pp. 180-183) Staff agrees with OPC that the inclusion of the \$520,264 in storm costs would mean that customers pay twice. (OPC BR at 23) Staff notes that, while FPL provides plausible reasons for the fact that the normal telecommunications expense was under budget, no FPL witness denied that it was included in the storm costs. FPL's approach for other costs has been to include those storm costs that were above the "normal" costs, as discussed for the call center portion of this issue. Where the normal costs are less than budget, this would translate to an amount being recovered both through base rates and through the storm costs. Staff agrees with OPC that it is inappropriate to require the ratepayers to pay twice. Thus staff believes that \$520,264 of telecommunications expense should be deducted from the storm costs.

CONCLUSION

Staff recommends that an adjustment of \$520,264 should be made to reduce telecommunications expense. No other adjustment to call center expense should be made.

Issue 14: Has FPL appropriately charged to the storm reserve any amounts related to advertising expense or public relations expense for the 2005 storms? If not, what adjustments should be made?

Recommendation: No. The Commission should disallow \$1,143,916 in image enhancing and conservation expenses that FPL charged to the 2005 storm reserve. This amount represents \$577,272 in thank you ad expenses, \$144,068 in public relations expenses and \$422,576 in employee campaign radio, web cam, and conservation advertisements. (Kaproth)

Position of the Parties

FPL: Yes. FPL has identified an adjustment of \$422,576 and recommends that this amount be included as part of the final true-up process. No other adjustments should be made.

OPC: No. Advertising costs for safety and other customer services are incorporated into the determination of base rates. Additional expenditures made informing the public of the Company's efforts to restore service are either covered in base rates or do not provide a direct benefit to ratepayers and are not directly related to the storm restoration efforts. As such, advertising and communications costs of \$2,528,196 and \$144,068 for a public relations invoice should be removed from the 2005 storm costs.

FIPUG: Adopts the position of OPC.

FRF: FPL has inappropriately charged advertising and public relations costs to its 2005 storm costs. Agree with OPC that \$2,528,196 in advertising and communications costs, and \$144,068 for public relations costs, should be removed from FPL's claimed 2005 storm costs.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: FPL included \$2,528,196 in advertising costs and \$144,068 in promotional costs in the 2005 storm reserve costs. This information was provided in response to Staff's Second Set of Interrogatories, Interrogatory No. 100 and Audit Finding No. 7. (TR 972-973)

OPC witness Larkin testified that only costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. Witness Larkin further explains that other costs the Company may claim to relate to storm recovery should be excluded such as advertising costs. (TR 912-913)

OPC witness DeRonne, testified that advertising, media relations or public relations costs should not be included in storm restoration costs because these costs are generally image

building type expenditures and are not related to the restoration of service to the customers. (TR 972)

Witness DeRonne further states that in response to Staff Interrogatory No. 100 (EXH 4), FPL identified \$2,528,196 of advertising and public relation costs included in the 2005 storm recovery costs. (EXH 4) The response shows that \$506,507 was included for print ads, \$2,021,689 for radio ads and no public relation costs were included. Witness DeRonne stated that Staff Audit Report, Audit Control No. 05-292-4-1, under Audit Finding No. 7, provided information that the print ads consisted of newspaper ads addressing expected electric turn on dates and "Thank You" ads. (EXH 89) Witness DeRonne states that the radio ads appeared to be for safety tips or image enhancing. Therefore, witness DeRonne removed the \$2,528,196 of advertising costs from the 2005 storm restoration costs. (TR 972-73)

Lastly, witness DeRonne removed an additional \$144,068 that was included as a "Public Relations Invoice" in Staff's Audit Report, under Finding No. 7, as Public Relations costs charged to the storm recovery costs. (TR 973; EXH 89)

Staff witness Welch testified that advertising expenses in the amount of \$2,630,218, appears to be image enhancing. Witness Welch explained that some of these expenses were for radio safety ads, some for newspaper ads informing the public of expected restoration times, and some for newspaper ads thanking the public, employees, and contractors, etc. Witness Welch stated that a detailed list was compiled and included in Audit Finding No. 7. (TR 1089)

In rebuttal, witness Davis testified that public outreach advertising, including communications designed to keep customers informed of the status of FPL's restoration efforts and to inform customers of the extraordinary dangers that exist during storm restorations should be encouraged and not discouraged. Witness Davis further explains that these communications meet a critical customer need for restoration and safety-related information after a natural disaster and therefore, public safety and public outreach advertising costs should be allowed. Further, witness Davis states that thank you advertising designed to recognize foreign crews who assist in restoration efforts should be allowed in order to encourage their continued support. Finally, witness Davis states that these expenses are highly volatile and extraordinary and would ordinarily not be included in the cost of service for purposes of setting base rates. (TR 1611-12)

Witness Davis does agree that FPL has included in its 2005 storm costs, \$404,627 in image enhancing expenses on an employee campaign radio and web advertisement and these expenses were reversed from the storm reserve during March 2006. FPL also removed \$17,949 related to conservation advertising in March 2006. (TR 1612; EXH 121)

In rebuttal, FPL witness Williams does not agree with witness DeRonne's adjustments that removed all utility advertising, media relations, or public relations costs because these costs would not have been incurred had it not been for the storms and the necessity of keeping customers informed of storm restoration status and extraordinary dangers that exist during storm restoration. (TR 1407)

Witness Williams testified that the one key lesson learned was that our customers want and expect FPL to communicate more often with them during these events. In addition this information facilitates restoration efforts. In addition, witness Williams states that the thank you

advertising, designed to recognize foreign crew that assisted in restoring service, helps to encourage their continued support. Therefore, these costs are appropriately charged to the storm restoration effort. (TR 1407)

ANALYSIS

In Commission proceedings, advertising expenses are generally examined on a case-by-case basis. If the utility's advertising expenses are found to be informational, educational or safety-related in nature and beneficial to its ratepayers, the Commission generally allows recovery. If, on the other hand, advertising expenses are found to be institutional, image-building, or provide no benefit for the regulated ratepayer, the Commission generally disallows recovery. See Order No. PSC-05-0748-FOF-EI, issued July 14, 2005, In re: Petition for approval of storm cost recovery of extraordinary expenditures, related to Hurricanes Charley, Frances, Jeanne, and Ivan, by Progress Entergy Florida, Inc.; Order No. PSC-02-0787-FOF-EI, Docket No. 010949-EI, issued June 10, 2002, In re: Request for rate increase by Gulf Power Company.

Staff believes that the advertising expenditures for the thank you ads are image enhancing, specifically the ads in the Wall Street Journal. The thank you ads do not benefit the ratepayers and do not give safety information needed during the hurricane or information needed during the storm restoration. Staff also believes that the public relations expenses are image enhancing and that conservation expenses should not be recovered through the storm reserve. The total of the thank you ad expenses in Audit Finding No. 7 is \$577,272 and the public relations expenses in Audit Finding No. 7 is \$144,068. (EXH 89)

On the other hand, staff believes that the advertising expenses for giving additional information related to the safety of the ratepayers and the time schedule for the restoration of service is beneficial to the ratepayers during this stressful and potentially dangerous time period. Therefore, staff believes because of the nature and volatility of these expenses they should be included in the storm reserve.

Staff agrees with the FPL proposed adjustment of \$422,576, which removes \$404,627 of image enhancing expenses for an employee campaign radio and web advertisement and \$17,949 related to conservation advertising. (TR 1612) Staff believes that the proposed adjustment should not be removed through the true-up process because staff has the information to make the adjustment at this time.

CONCLUSION

Staff recommends the Commission disallow \$1,143,916 in image enhancing and conservation expenses that FPL charged to the 2005 storm reserve. This amount represents \$577,272 in thank you ad expenses, \$144,068 for public relations expenses, and \$422,576 in employee campaign radio, web cam, and conservation advertisements.

Issue 15: Has uncollectible expense been appropriately charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. The uncollectible account expense of \$3,582,000 should be removed from the storm reserve. (Kaproth)

Position of the Parties

FPL: Yes. Storms result in increases in uncollectible expense that FPL estimates based on incremental usage during the collection policy suspension period and incremental usage during the period where collection workers reduce the collection work backlog caused by the storms. No adjustment should be made.

OPC: No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. It would be difficult, if not impossible, to relate uncollectible accounts directly to the effects of a storm. Even if it could be done, these expenses are not directly related to the restoration of service. They are in the nature of risk, for which the Company is compensated through the rate of return on equity.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that FPL's claimed 2005 storm costs should be reduced by \$3,582,000 to remove uncollectible expense included in FPL's storm cost recovery request.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

In his prefiled direct testimony, FPL witness Davis' KMD-4 included a footnote that "estimated 2005 Storm-Recovery Costs, per Ms. Williams' Testimony includes uncollectible write-off expense." However, neither FPL witness Williams' or witness Davis' prefiled testimony quantified the amount of uncollectible expense that was included in the 2005 Storm Costs. But, the amount, \$3,582,318, was provided in Attachment 1 of FPL's response to Staff's Interrogatory No. 92. (EXH 125)

OPC witness Larkin testified that it would be difficult, if not impossible, to relate uncollectible accounts directly to the effects of a storm. He testified that even if it could be done, these expenses are not directly related to the restoration of service. He also testified uncollectible expenses are in the nature of risk, which the Company is compensated for through the rate of return on equity and is a type of business risk so it should not be compensated for

through the storm recovery costs. Consequently, OPC witness DeRonne's DD-1, which summarized OPC's proposed 2005 Storm Cost adjustments, included \$3,582,000 as a reduction to FPL's estimated 2005 Storm Costs. (EXH 85)

In his rebuttal testimony, FPL witness Davis stated that he does not agree with witness Larkin's statement that uncollectible accounts expense should not be included in the 2005 storm costs, as they are difficult to directly relate to the effects of a storm. Witness Davis testified that since FPL mobilizes a large portion of its workforce to restore service to customers as quickly and safely as possible, a majority of the resources that would be utilized to mitigate uncollectible bills are reassigned to storm restoration. He testified that base rates assume that these mitigation efforts are in place and are working. Therefore, delinquent customers receive additional days to pay and if they do not ultimately pay, the amount of uncollectible write-off expense becomes higher as a direct result of hurricane activity. Witness Davis testified further that, but for the restoration effort resulting from the storms, these additional costs would not have been incurred.

In addition, in his rebuttal testimony, witness Davis pointed to Page 16 of the 2004 Storm Order as confirmation that the Commission acknowledged the cause and effect relationship. In the 2004 Storm Order, the Commission found that there was a direct relationship between hurricane activity and the amount of uncollectible, or bad debt, expense incurred. (TR 1613-14)

Staff witness Welch, during cross-examination by FPL, also testified that it was her understanding that the Commission allowed uncollectible accounts expense in the 2004 Storm Order to acknowledge that bill collectors weren't able to go out and do the work they normally do, so FPL was not able to collect as much revenue as they normally do. She stated that it was her understanding that uncollectible accounts expense was allowed because the Commission believed FPL had to write off more than normal revenues. However, witness Welch also stated that that was her understanding only and because she was not actively involved in the hearing, she really couldn't say why the Commission decided to do it. (TR 1098)

Staff witness Jenkins testified that FPL's shareholders should share in the adverse effects of the 2005 hurricanes. (TR 1252, 1256)

ANALYSIS

FPL provided its computational support for the net write-off of \$3,582,318. (EXH 125) Also, staff acknowledges that the Commission determined in the 2004 Storm Order that there is a relationship between the increase in uncollectible expense and hurricane activity and believes that this relationship does exist. However, because the amount of the estimated uncollectible account expense for the 2004 storms was \$5.6 million and the actual uncollectible account expense that materialized was only \$1.4 million, staff has reservations about the ability to reasonably project the incremental amount that is attributable to storm activity. Although staff does not agree with witness Larkin that it is impossible to relate uncollectible accounts directly to the effects of a storm, staff does believe that the amount of uncollectible expense, is difficult, if not impossible, to accurately project. The inability to reasonably estimate the amount of uncollectible expense directly attributable to storm activity was proven to be true, as shown if the estimated \$5.6 million is compared to the actual \$1.4 million that materialized for the 2004 storm activity.

Further, staff believes that OPC witness Larkin makes a good point in his conclusion that uncollectible expenses are risks, and the Company is compensated for risk through the rate of return on equity and therefore should not be compensated through storm recovery costs. Also, as addressed in Issues 17 and 35, staff also agrees with staff witness Jenkins who testified that FPL's shareholders should share in the adverse effects of the 2005 hurricanes. (TR 1252, 1256) Finally, as OPC witness Larkin testified, these costs are not directly related to the restoration of service. (TR 915) Although this is a departure from the Commission's treatment in the 2004 Storm Order, staff believes the departure is justified due to the reasons detailed.

CONCLUSION

Based on the foregoing analysis, staff recommends that uncollectible expense of \$3,582,000 should be removed from the storm reserve.

Issue 16: Has FPL properly charged the normal cost of replacement to rate base and the normal cost of removal to the cost of removal reserve for the 2005 storms? If not, what adjustments should be made?

Recommendation: No. The 2005 storm-related costs should be reduced by \$8,745,000 to reflect the increased estimate for capital expenditures. (Slemkewicz, Kaproth, Haff)

Position of the Parties

FPL: Yes. FPL removed capital costs at “normal cost” and recorded them to rate base. What is left after adjusting for insurance recoveries represents the operations and maintenance expenses the Company has incurred to restore service to its customers. No adjustments should be made.

OPC: No. The capital portion total 2005 storm cost has increased from the original estimated amount of \$63,855,000 to \$72,600,000. This additional \$8,745,000 offset to the 2005 storm recovery costs should be made to reflect the higher portion of storm costs anticipated to be capital related, which would not be recovered from the storm reserve.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that an additional \$2,964,000 adjustment to 2005 storm recovery costs charged to the storm reserve is necessary to reflect the higher proportion of storm costs that are presently expected to be capital-related.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that FPL properly charged the normal cost of replacement to rate base and the normal cost of removal to the cost of removal reserve for the 2005 storms. After adjusting for insurance recoveries, the remainder represents the operations and maintenance expenses the Company incurred to restore service to its customers. (TR 437) Therefore, no adjustment is necessary.

OPC witness DeRonne testified that FPL increased its original estimate of capital expenditures by \$2,964,000. The witness recommended that 2005 storm costs be reduced by that amount. (TR 974)

ANALYSIS

FPL witness Davis testified that FPL properly charged the normal cost of replacement to rate base and the normal cost of removal to the cost of removal reserve for the 2005 storms. After adjusting for insurance recoveries, the remainder represents the operations and maintenance expenses the Company incurred to restore service to its customers. (TR 437) Witness Davis described the capital cost estimating process:

Each Business Unit is responsible for preparing an estimate of capital work as a result of storm damage to its assets. FPL estimates storm damages related to its Transmission and Distribution assets at normal cost utilizing the Company's estimating systems. Storm damages to all other assets are estimated individually by each Business Unit. These estimates are then reviewed by FPL's Accounting Department (Accounting) to ensure these costs are capital costs, not operating or maintenance costs. Accounting also ensures the correct amount of additions, retirements, removal, and salvage will be recorded on the Company's books. Based on the estimates developed, the capital costs are adjusted out of storm-recovery costs and are charged to rate base.

(TR 448-449)

Witness Davis also testified that the estimated amount of normal capital costs to be removed from the 2005 storm costs increased from \$63,855,000 to \$72.6 million. (TR 1604-1605)

OPC witness DeRonne testified that FPL increased its original estimate of capital expenditures by \$2,964,000. (TR 974) Subsequently, FPL increased the amount for estimated capital expenditures to \$72,600,000, an increase of \$8,745,000 from the original estimated amount of \$63,855,000. (TR 1605) Witness DeRonne testified that the increased estimate for capital expenditures should be removed from the 2005 storm costs. (TR 974)

CONCLUSION

As explained by FPL witness Davis, FPL has a sophisticated system for estimating the amount of storm repair costs that should be removed from the storm reserve and be included in rate base. Witness Davis testified that FPL's most recent estimate of capital expenditures that should be removed from the 2005 storm costs was \$72,600,000. Instead of using this latest estimate to reduce the amount of 2005 storm costs to be recovered through securitization, FPL would prefer to wait and true it up at some later date. The higher costs, however, would be the costs reflected in the securitization revenues to be recovered from the customers.

Staff agrees with OPC that the latest known estimate for the amount of capital expenditures should be used now to lower the amount of the 2005 storm costs. Staff recommends that the 2005 storm-related costs should be reduced by \$8,745,000 to reflect the increased estimate for capital expenditures.

Issue 17: If the Commission applies in this docket the methodology applied in Order No. PSC-05-0937-FOF-EI, should the Commission take into account:

- a. Amounts not recovered through base rates due to the disruption of service due to the 2005 storm season or the absence of customers after the storms;
- b. Overtime incurred by Company personnel in work areas not directly affected by the storm due to loss of some personnel to storm assignments (backfill work);
- c. Costs associated with work that must be postponed due to the urgency of storm restoration and accomplished after the restoration was completed (catch-up work);
- d. Uncollectible accounts receivable write-offs directly related to the storms;
- e. Incremental contractor, outside professional services and temporary labor costs due to work postponed due to the urgency of storm restoration and accomplished after the restoration was completed;
- f. Costs that would have otherwise been charged to clauses;
- g. Costs that would have otherwise been charged to capital;
- h. Vacation Buy-Backs; and
- i. Nuclear Payroll Expected to be Recovered Through Insurance.

Recommendation:

No for Issues 17a, 17b, 17c, 17d, 17e, and 17h. These factors do not represent reasonable and prudent costs that were or planned to be charged to the storm damage reserve. They do not directly relate to storm restoration. Consistent with the staff recommendation for Issue 35, these amounts should be borne by FPL's shareholders.

Issue 17d is addressed in Issue 15. Issues 17f, 17g, and 17i are addressed in Issue 8. (Devlin, Stallcup)

Position of the Parties

- FPL:**
- a. As previously stated, if one were to utilize an incremental cost approach, under which adjustments are based on the theory that certain storm restoration costs have already been recovered through base rates, then base revenues not achieved due to service interruptions from hurricanes must be considered, as they were in the 2004 Storm Cost Recovery Order. FPL's base revenues not achieved due to the 2005 hurricanes were \$51,354,000.
 - b. Incremental backfill costs of \$0.8 million are incremental costs that would not have otherwise been incurred in the absence of the 2005 storms, and they are not being recovered in base rates. These costs are also not being charged to the storm reserve by FPL. Under the 2004 Storm Cost Recovery Order Approach, an

adjustment for the backfill work is appropriate since, otherwise, there would be no cost recovery for these incremental storm related costs.

c. FPL incurred catch-up costs of \$7.8 million due to storm restoration activities. These costs represent additional overtime hours or contractor work incurred until the catch-up work is completed. These incremental costs were directly caused by 2005 storms, are not recovered in base rates, and are not charged to the storm reserve by FPL. Like backfill, under the 2004 Storm Cost Recovery Method, an adjustment is necessary, otherwise there would be no cost recovery of these incremental storm costs.

d. FPL's bill collectors help restore service to customers. Base rates assume bill collection is taking place. Because of storms, delinquent customers receive additional days of service causing uncollectible expenses to increase. But for the restoration effort, these additional costs would not have been incurred. Uncollectible accounts expense directly related to the 2005 storms of \$3.6 million should be allowed to be recovered consistent with the reasoning of the 2004 Storm Cost Recovery Order.

e. See response provided for part c.

f. Regular payroll charged to the storm reserve that would have ordinarily been charged to clauses of \$2.7 million should be allowed to be recovered through the storm reserve since they are not being recovered through a cost recovery clause or through base rates. Simply stated, they are not being recovered twice from customers and, therefore, should not be disallowed under the incremental cost methodology.

g. Regular payroll charged to the storm reserve that would have ordinarily been charged to capital of \$8.0 million should be allowed to be recovered through the storm reserve since they are not being recovered through base rates. These costs should not be disallowed if the 2004 Storm Cost Recovery Method is adopted.

h. FPL purchased \$1.2 million of vacation from employees who were unable to use earned vacation due to their work supporting storm restoration. Many employees worked through November to make repairs to FPL's storm-damaged infrastructure. Normal workloads will not enable employees to take missed vacation days in the future. Customers benefited from these employees performing storm restoration duties instead of taking vacation, and compensation for vacation time should be permitted if the 2004 Storm Cost Recovery Order methodology is adopted.

i. Under the 2004 Storm Cost Recovery Method, nuclear payroll expected to be recovered through insurance of \$2.5 million should not be included in the regular payroll adjustment. This is because these amounts are already removed through the adjustment for amounts expected to be recovered through insurance.

OPC:

- a. No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. Lost revenues are not a cost of restoring service. In any event, FPL's revenues exceeded budgeted amounts during the 2005 hurricane season, even including the impact from outages caused by hurricanes, so there are no "lost revenues" in this case.
- b. No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. Backfill work is part of daily utility operations and maintenance of the Company's system and are included as part of base rates. These costs are not extraordinary nor related to storm recovery, and as such should not be used as an offset in the incremental approach to storm reserve accounting or recovery.
- c. No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. Catch-up is part of daily utility operations and maintenance of the Company's system and are included as part of base rates. These costs are not extraordinary, nor related to storm recovery and as such should not be used as an offset in the incremental approach to storm reserve accounting or recovery.
- d. No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals and recovered from ratepayers. It would be difficult, if not impossible, to relate uncollectible accounts directly to the effects of a storm. Even if it could be done, these expenses are not directly related to the restoration of service. They are in the nature of risk, which the Company is compensated for through the rate of return on equity.
- e. No. Only those costs that are directly related to restoring facilities should be included in the storm restoration cost accruals. These costs are similar to those described as catch-up work, which is part of daily utility operations and maintenance of the Company's system and included as part of base rates. These costs are not extraordinary, nor related to storm recovery and as such should not be used as an offset in the incremental approach to storm reserve accounting or recovery.
- f. The Citizens agree that these costs should be offset against the regular salaries removed from the 2005 storm recovery costs.
- g. The Citizens agree that these costs should be offset against the regular salaries removed from the 2005 storm recovery costs.
- h. Vacation Buy-Backs are generated by the Company's vacation policy and not as a direct result of storm restoration activities. It reflects a discretionary action by FPL and shouldn't be charged to customers.

i. In FPL's Incremental Cost Approach adjustment it includes a \$2,490,800 offset to the regular employee salaries for nuclear payroll costs that it already removed from the 2005 estimated storm recovery costs in the adjustment to remove the estimated insurance proceeds. If this adjustment is reflected, FPL would recover the associated amount twice, once from insurers and again from ratepayers. Therefore, this offset is inappropriate.

FIPUG:

a. No. During the storm period, FPL sold more electricity to retail customers than it anticipated it would sell according to documents filed in Docket No. 050001-EI. The estimated sales provided enough money to meet ordinary O&M expenses. In calculating retail revenues, the revenues from all retail customers is the controlling factor, not the revenues received from a relatively small number of customers whom FPL was unable to serve during the period of storm restoration. FIPUG also agrees with OPC.

b. – i. Agree with OPC.

FRF:

a. No. Only those costs that are directly related to restoring facilities should be included in allowable storm restoration costs and recovered from ratepayers. The PSC should reject FPL's effort to shift additional business risk – substantively, the risk of lost revenues - onto its customers.

b. No. Only those costs that are directly related to restoring storm-damaged facilities should be included in allowable storm restoration costs and recovered from FPL's customers.

c. No. Only those costs that are directly related to restoring storm-damaged facilities should be included in allowable storm restoration costs and recovered from FPL's customers.

d. No. Only those costs that are directly related to restoring storm-damaged facilities should be included in allowable storm restoration costs and recovered from FPL's customers. FPL's claimed storm costs should be reduced by \$3,582,000.

e. No. Only those costs that are directly related to restoring storm-damaged facilities should be included in allowable storm restoration costs and recovered from FPL's customers.

f. Agree with OPC.

g. Agree with OPC.

h. Agree with OPC that "vacation buy-backs" are a result of FPL's vacation policy and not a direct result of storm restoration activities. Such amounts should not be charged to the storm reserve, nor should they be allowed to offset any adjustments made as a result of the incremental cost approach.

- i. Agree with OPC that this offset proposed by FPL is inappropriate.

AARP: The same as the Office of Public Counsel.

FEA: a. – i. Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: Issue 17 and its subparts a thru i represent FPL's alternate position in the event the Commission rejects its primary "Actual Cost" method and adopts the "modified incremental" cost recovery method as applied in the 2004 Storm Order. Issue 17h was proffered by OPC.

Lost Revenue

Issue 17a relates to amounts not recovered in base rates due to disruption of service and loss of customers in the wake of hurricane activity. This issue relates to lost revenue. In the 2004 case, the Commission authorized recovery of amounts (normal costs) to the extent there was lost revenue. The premise is that certain normal costs were not recovered in base rates in times when base rates were not generating adequate revenue to cover these costs.

In the 2004 storm case, FPL requested recovery for lost revenue. In this case, FPL requests that any adjustments relating to the use of the "incremental" method be offset up to the amount of lost revenue or \$51.4 million. FPL states that this is consistent with the Commission ruling in the 2004 Storm Order. FPL also points out that recognition of "lost revenue" is permitted under the newly adopted securitization law, Section 366.8260(1)(n), Florida Statutes.

OPC takes the position that "lost revenue" is not a cost of restoring service and states that all revenue is subject to variation due to weather. This phenomenon is part of business risk and is inherent in the determination of a fair and reasonable rate of return. In fact, FPL experienced a positive revenue effect on account of warm weather in 2005.

FPL witness Green testified that the amount of energy sales not realized due to the 2005 storm season was 1.6 Million mWh. (TR 726) According to witness Green, this quantity was estimated by obtaining the number of customers without electrical service on a daily basis and multiplying that number by the usage those customers would be expected to consume on those specific days. (TR 724) No party presented testimony that this methodology of estimating the amount of mWh sales not realized was in error.

OPC witness Larkin testified that although FPL may not have realized a certain amount of energy sales during the days following the storms of 2005, the company had in fact sold more electricity during the July through October time period than it had budgeted. (TR 909) These calculations were based upon the actual verses budgeted mWh sales reported in the last fuel docket. (EXH 84) No party challenged the accuracy of the monthly actual and budgeted mWh sales data contained in this exhibit.

In his rebuttal testimony, FPL witness Green contends that OPC witness Larkin made two errors in reaching his conclusion that actual energy sales exceeded budgeted sales during the months of the hurricanes. (TR 731) First, witness Green points out that witness Larkin erroneously assumes that any variance between actual and budget is solely explained by the effects of hurricanes in any given month. Second, witness Green points out that the billed sales for the July through October time frame used by witness Larkin would include unbilled sales from June 2005 and would not include some sales from October 2005. Witness Green attributes this error to the lag between the time electricity is consumed and when it is billed. (TR 732)

FPL witness Green goes on to testify that the appropriate time frame to consider in measuring the impact on sales due to the 2005 hurricane season is July through December 2005. (TR 733) He further notes that the billed sales for July need to be adjusted downward to account for the unbilled sales coming from June. FPL witness Green concludes by calculating that instead of actual sales exceeding budgeted sales for this time period as OPC witness Larkin contends, FPL's actual sales for the period were below forecast by approximately 1 million kWh.

Staff believes that the methodology used by FPL witness Green is appropriate for estimating the amount of energy sales not realized during the days following the hurricanes of 2005. However, staff also acknowledges OPC witness Larkin's concern that FPL had already recovered sufficient revenue from customers during the remainder of the 2005 hurricane season to cover its budgeted O&M expenses.

Staff also agrees with OPC's view that lost revenue is part of "weather" related business risk for any utility. Business risk is captured in the determination of a fair and reasonable rate of return. Consumers should not bear all of the adverse effects of business risk of FPL while FPL is able to earn a rate of return that takes into account business risk. This is a form of double recovery. For these reasons, staff recommends that FPL absorb the effects of lost revenue.

Backfill Costs

Issue 17b relates to an estimated \$.8 million of backfill costs. According to FPL, this amount represents unbudgeted costs associated with compensated overtime, temporary labor, and/or contractors, which were incurred to satisfy job accountabilities of other employees while they were assigned to storm duty. (TR 1602) FPL alleges that these are incremental costs that would not have otherwise been incurred in the absence of the 2005 storms, and, therefore, are not being recovered in base rates.

OPC witness Larkin states that FPL's adjustment for backfill costs is a back door method of requesting lost revenue. (TR 906) OPC believes that these costs do not directly relate to storm restoration.

Staff concedes that incremental costs such as backfill costs may result as FPL employees are reassigned during storm restoration. However, staff agrees with OPC that such costs are not directly related to storm restoration and only direct costs should be recoverable in this proceeding. Backfill costs represent an indirect adverse effect of the storms. Based on factors mentioned in Staff witness Jenkins' testimony, staff believes that FPL's shareholders should share in the adverse effects of the 2005 hurricanes and absorb backfill costs.

Catch-up work

Issue 17c relates to an estimated \$7.8 million of catch-up work. According to FPL, these costs represent additional overtime hours or contractor work incurred until the catch-up work is completed. FPL uses the same points to justify this cost as it used in its justification of backfill costs. OPC points out that these costs do not directly relate to storm restoration.

For the same reasons staff recommended disallowance of backfill costs, staff recommends disallowance of costs associated with catch-up work.

Incremental Contractor Work

Issue 17e relates to estimated costs of incremental outside contractor services and is part of the catch-up amounts addressed in Issue 17c. For the same reasons staff recommended disallowance of backfill costs, staff recommends disallowance of costs associated with incremental contractor work.

Vacation Buy-Backs

In its incremental approach, FPL offset regular payroll costs with vacation buy-back costs of \$1,209,000, which represents the purchase of unused vacation from employees that could not take vacation due to the length of storm restoration efforts and subsequent catch-up work. FPL witness Davis points out that many employees worked through November to make repairs to FPL's damaged infrastructure. As such, certain employees were unable to take all the vacation they were entitled to and normal workloads will not allow these employees to take those days in the future. Witness Davis states that these payments were a direct result of the 2005 storms and should be allowed as an offset to the \$26.1 million regular payroll adjustment, if the Commission determines this adjustment is necessary. (TR 1603; EXH 121)

OPC witness Larkin testified that vacation buy-backs are generated by the Company's vacation policy and not as a direct result of storm restoration activities. He also stated that FPL's policy which was applied for the year 2005 only, is that employees will be paid for any remaining unused vacation in excess of 120 hours. Witness Larkin testified that FPL could have changed its carryover policy and allowed employees to carryover any and all vacation which could not be taken in 2005. Instead the Company chose to limit the carryover hours to 120 and reimburse employees for any vacation which could not be taken in 2005. Witness Larkin stated that this 2005 vacation policy is a management decision. These costs are not directly related to the restoration of service, but are directly related to FPL's vacation policy. In addition, part of this cost may be the result of buy-backs from employees who have purchased additional vacation hours and were unable to take those hours as vacation in 2005 because of restoration activities. Regardless of whether the vacation buy-back is a result of unused vacation or vacation which the Company is purchasing from employees who had previously purchased those vacation hours, it is not a legitimate cost to be recovered from ratepayers. (TR 913-14, 920)

Docket No. 060038-EI

Date: May 8, 2006

Staff agrees that the change in vacation carryover policy was a management decision and that it should not affect the amount charged to the 2005 storm recovery costs. Therefore, staff recommends that FPL's proposed \$1,209,000 offsetting adjustment not be accepted.

Issue 18: Have landscaping costs been appropriately charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. Landscaping costs of \$3,816,864 should be removed from the storm costs. (Marsh)

Position of the Parties

FPL: Yes. Only landscaping restoration costs necessary to comply with local land use and zoning requirements have been charged to the Reserve. Failure to comply with code requirements would result in local jurisdictions initiating code enforcement actions.

OPC: No. Landscaping is not covered by insurance and should be covered as part of base rates. Accordingly, landscaping charges of \$1,503,250 should be removed from 2005 storm costs to be recovered through the storm reserve.

FIPUG: Adopts the position of OPC.

FRF: No.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis stated that landscaping costs were necessary to return landscaping to its pre-storm condition to comply with local code requirements. (TR 1623; EXH 126, p. 4) He testified that FPL was in compliance with all requirements before the storms, and if it were not for the storms, these costs would not have been incurred. (TR 1623-1624; EXH 126, p. 4) He said that the costs would be included under either FPL's proposed methodology or under the incremental cost approach. (TR 1624) He stated that code enforcement actions would result if FPL failed to restore the landscaping. (TR 1624; EXH 4, p. 397)

FPL witness Jaindl testified that landscaping at substations is necessary due to local development orders or code requirements. (TR 1333) She stated that any landscaping shown on the approved plans must be planted and maintained by FPL to avoid code enforcement actions. (TR 1333) She advised that such actions take the form of Notices of Violation and/or monetary fines. (TR 1333)

OPC argued in its brief that landscaping costs should be recovered through base rates, not through the storm reserve. (OPC BR at 36) OPC based its position on statements of staff witness Welch. As discussed further below, witness Welch testified that insurance does not cover

landscaping, and expressed concern as to whether it should be charged to the reserve. (EXH 157, p. 49)

Staff witness Welch testified that FPL included \$1,413,250 for substation landscaping and \$90,000 for Service Center landscaping totaling \$1,503,250 for Hurricane Wilma. (TR 1087; EXH 89, p. 7) She stated that other landscaping costs may have been incurred but were not examined by the auditors. (TR 1087)

Witness Welch stated that she did not find evidence to contradict FPL's assertion that it needed to replace landscaping due to the 2005 storms. (EXH 157, p. 48) The witness said that landscaping required by local authorities is a cost of providing service, but although she expressed concern, she did not make a specific recommendation. (EXH 157, pp. 49-50)

Witness Welch stated that insurance does not cover landscaping, regardless of whether it is required by zoning. (EXH 157, p. 49) She explained that:

My understanding of the reason the storm reserve was set up to begin with was to replace insurance. And if most people's insurance isn't covering it, then I'm just not sure it should be recovered.

(EXH 157, p. 49)

ANALYSIS

Although landscaping is a cost of service, OPC argued that it is more appropriate to recover the costs through base rates than to charge it to the storm reserve. Staff witness Welch testified that the reserve is essentially a replacement for insurance. The basic premise espoused by witness Welch and by OPC is that items that would not have been recoverable through insurance should be recovered through means other than the reserve. (OPC BR at 36) Under OPC's recommended approach, FPL would not be denied recovery; the means of such recovery simply would not be the storm charge.

Staff believes that much of the landscaping cost was associated with general cleanup, such as tree trimming, limb removal, sweeping of parking lots, and removal of damaged trees. (EXH 4, pp. 191-226) This type of work is a part of routine maintenance of landscaping. While the amount of work may have been increased by the storms, FPL presented no evidence that the costs incurred exceeded the normal budget for landscape maintenance. Accordingly, staff believes such costs should not be treated as storm costs.

As explained by staff witness Welch, landscaping costs were incurred in addition to those sampled by the staff auditors. (TR 1087) Staff notes that the total amount for all landscaping costs included in the storm costs, based on FPL estimates, is \$3,816,864. (EXH 4, p. 191) The amount recommended for removal by OPC represents only a portion of the landscape costs.

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CONCLUSION

Staff recommends that landscaping costs of \$3,816,864 should be removed from the storm costs.

Issue 19: Have lawsuit settlement charges been appropriately charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. The 2005 storm costs should be reduced by \$2,849,571 for lawsuit settlement charges. (Marsh)

Position of the Parties

FPL: Yes. Litigation and settlement costs that are directly related to 2005 storm restoration have been charged to the Storm Reserve. But for the 2005 storms, these costs would have not been incurred. [sic] Further, FPL is legally obligated to indemnify and hold harmless foreign crews against claims which are brought as a result of their providing assistance to FPL.

OPC: No. FPL originally included \$2,849,571 for estimated property damage and personal injury costs for 2005 storm costs. These are not costs directly related to the storm recovery efforts or for the restoration of electric service to customers and should not be included in the costs to be recovered. Additionally, these types of costs are already considered in the determination of base rates and should not be recovered via the recovery of storm restoration costs.

FIPUG: Adopts the position of OPC.

FRF: No. Lawsuit settlement charges are not directly related to storm recovery efforts or for restoring service to customers, and such costs, which are already considered in determining FPL's base rates, should not be included in allowable costs in this docket. This is another inappropriate effort by FPL to shift as much risk as possible onto its customers. FPL' [sic] claim for \$2,849,571 in such costs as 2005 storm costs should be disallowed.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that “[a]ny property damage and personal injury costs that are directly related to storm restoration should be recoverable.” (TR 1614) He stated that “but for the restoration effort associated with the 2005 storms, these costs would not have been incurred.” (TR 1614) He said that the effect of removing lawsuit costs from the storm recovery would be to treat them as if they were recoverable in base rates. (TR 1614) He explained that the Commission eliminates non-recurring costs when setting base rates, so these extraordinary costs would not be recovered through that mechanism. (TR 1614) Witness Davis stated that FPL has removed \$2.2 million of property damage and personal injury costs from the storm recovery

amount. (TR 1615; EXH 121) He testified that the remaining \$0.6 million is a direct result of the storm restoration. (TR 1615)

Witness Davis testified that \$2.2 million in legal costs for 2005 were removed after FPL's attorneys determined that some items did not meet the "but for" criteria; that is, "but for the storm restoration these costs would not have been incurred." (TR 1637) He stated that the amounts were removed because FPL concluded that the condition which led to the legal expense could have existed outside of a hurricane. (TR 1638-1639) He explained that the condition did not change; rather, FPL made a different decision regarding the appropriate treatment of the costs. (TR 1638) The witness said that he was not aware of certain facts, but upon learning of them, agreed with the FPL attorneys that certain legal expenses should be removed. (TR 1639)

In its response to the staff audit, FPL stated that it must indemnify foreign utilities for the uninsured portions of any lawsuits that result as a result of storm restoration activities as part of its mutual aid agreements. (EXH 126, p. 5) FPL stated that such costs should be charged to the reserve "to encourage, not discourage, mutual aid." (EXH 126, p. 5)

FPL witness Gower testified that nonrecurring expenses would either be excluded from operating expenses or included on a levelized basis in setting rates. (TR 1526) He provided as an example the settlement of litigation. (TR 1526-1527) The witness said that such expenses are "necessary, reasonable and prudent costs of providing utility service." (TR 1528) He stated that the appropriate methods to recover nonrecurring items include amortization over a period of years, or the application of separate billing factors. (TR 1528)

OPC witness DeRonne stated that FPL has included \$2,849,571 for estimated property damage and personal injury costs in the 2005 storm recovery amount. (TR 973) She testified that these costs are not directly related to restoration of service after the storms. (TR 973) She stated that such costs are already considered in setting base rates. (TR 973)

Staff witness Welch testified regarding a confidential audit finding regarding lawsuits. (TR 1088; EXH 158) In her discussion of lawsuits generally, she stated that extraordinary items are typically not included in the setting of base rates. (EXH 157, p. 47)

ANALYSIS

Staff's examination of the record yielded no evidence that there were any incidents in 2005 that would result in FPL making payment for litigation or settlement costs. Staff notes that FPL witness Davis' testimony regarding the examination of these costs and discussion with FPL legal staff refers specifically to a staff audit finding for 2004. (CONFIDENTIAL EXH 158) No such item was identified for 2005, yet the amount and circumstances discussed by witness Davis are the same. Further, staff agrees with OPC witness DeRonne that these costs are not directly related to restoration of service after the storms. (TR 973) Therefore, all 2005 litigation and settlement costs should be removed.

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CONCLUSION

Staff recommends that the 2005 storm costs should be reduced by \$2,849,571 for lawsuit settlement charges.

Issue 20: Have contingency portions of estimated storm costs been appropriately charged to the storm reserve for 2005? If not, what adjustments should be made?

Recommendation: No. Storm costs should be adjusted by \$26,253,351 to remove remaining contingencies. (Marsh)

Position of the Parties

FPL: Yes. FPL included contingencies in the 2005 storm cost estimate consistent with its standard project management practices. Contingencies formally recognize uncertainty concerning factors such as scope of work, material costs, contractor availability and pricing, or the length of time for completion. Any unused contingency will be reflected in the final true-up process proposed by FPL. The only remaining contingency for 2005 storm costs is \$7,478,495. No adjustments should be made.

OPC: No. The remaining contingencies should be removed from the storm cost estimates. FPL is treating upward adjustments to estimated "contingencies" as a way of maintaining its request at the level of its original petition, instead of lowering that request as actual figures come in below original estimates. The estimates in FPL's petition were a starting point subject to adjustments based on actual figures, not an entitlement.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that \$26,253,351 of contingencies remaining at the end of February 2006 should be removed from FPL's 2005 storm cost estimates.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis stated that "[e]stimates are an inherent part of the accounting process and must be based on reliable information, not mere speculation regarding future events." (TR 1628) He testified that FPL's estimates are based on reliable information. (TR 1628) He said that the use of contingencies in estimates are a standard practice used to accommodate unidentified but likely additional costs. (TR 1628-1629) The witness explained that contingencies will change or be eliminated as costs become known. (TR 1616, 1629)

Witness Davis stated that the original amount of the contingencies included in FPL's filing was \$44.5 million. (TR 1616) He testified that this was reduced to \$26.3 million by February 28, 2006, and the portion associated with Hurricanes Dennis and Rita were reduced to

\$7.5 million by March 2006. (TR 1616) He said that any unused contingencies will be reflected in the final true-up process. (TR 1616)

FPL witness Williams also stated that, as of March 31, 2006, the remaining estimated amounts included \$7.5 million of contingency. (TR 1406; EXH 106) Of this amount, she testified that \$6.9 million is associated with Hurricane Wilma distribution follow-up restoration work being performed by contractors. (TR 1406)

OPC witness DeRonne stated that a contingency amount of \$26,253,351 remained in FPL's costs as of February 28, 2006. (TR 965) She said that this amount should be removed from storm costs, because any over-estimated amounts will cause ratepayers to pay higher amounts than necessary over the recovery period. (TR 966) She testified that:

[t]he general premise that if the costs are overestimated they will be trued-up and serve to increase the available reserve funds for future storms is not a reasonable premise and is not the attitude the Commission should adopt in evaluating the proposed 2005 storm recovery costs in this case.

(TR 966)

The witness testified that some 27 percent of the proposed storm recovery costs is still based on estimates. (TR 966) She stated that removal of the contingencies would not have an appreciable impact on the amount of estimated costs proposed for recovery. (TR 966)

OPC argued that over-estimated amounts would cause ratepayers to be locked into paying more than is necessary for the next twelve years under FPL's proposal. (OPC BR at 39) OPC argued that the amount of variability in FPL's estimates for contingencies lead OPC to believe the amounts are used as a plug figure. (OPC BR at 39)

Staff witness Welch stated that FPL included contingencies in many of the accruals for storm costs. (TR 1088) She testified that FPL moves contingencies that are unused to other categories. (EXH 157, p. 58) She stated that the Commission should be aware of this practice and make certain in the future that the contingencies were used in the manner that FPL represents. (EXH 57, p. 58)

ANALYSIS

While staff agrees that the record shows a marked reduction in contingencies, staff's adjustments in this recommendation are made to the original filing amount. According to FPL witness Davis, the original contingencies totaled \$44.5 million. (TR 1616) By March 2006, the amount had been reduced to some \$7.5 million. (TR 1616)

Staff believes it is clear from the record that not all contingencies will be used. The amount of contingencies is small in relation to the overall amount requested by FPL. Staff agrees with OPC that the removal of contingencies will not have an appreciable impact on the remaining estimated costs. Staff does not believe it is appropriate to expect ratepayers to pay for

costs that may never be realized for the next twelve years. Therefore, staff believes the remaining contingencies should be removed.

Staff agrees with OPC that \$26.25 million is the amount to be removed. Although FPL indicates that a large portion of the contingencies either have already been realized or have been eliminated as reflected in amounts proposed for reduction elsewhere by FPL, staff does not see in the revised exhibits where such adjustments have been made. Further, the starting point for staff's adjustments is FPL's original filing. Removal of this amount rather than the full \$44.5 million of original contingencies gives recognition to the possibility that some amount of contingencies was actually realized. The record is silent on how much was realized and how much was eliminated by FPL.

CONCLUSION

Staff recommends that storm costs be adjusted by \$26,253,351 to remove remaining contingencies, the total amount requested by FPL in its petition.

Issue 21: Should FPL be required to true-up approved 2005 storm related costs? If so, how should this be accomplished?

Recommendation: Yes. The true-up mechanism for the approved 2005 storm related costs should be based on the cut-off dates approved in Issue 26. These approved cut-off dates should be the basis for determining whether any costs should be charged to base rates rather than the storm reserve. FPL should be required to provide an annual true-up report by March 1st of each year for the preceding year ended December 31st until the repairs are completed. (Slemkewicz)

Position of the Parties

FPL: Yes. There should be a final true-up when all work has been completed and all costs are known.

OPC: Yes. FPL should be required to true-up the actual costs incurred and not continue to increase the amount of contingency costs as a plug amount to keep the storm cost equal to the original amount requested or to the estimated amount approved by the Commission. A cut-off date of December 31, 2006 should be established for charging 2005 storm restoration costs to the reserve.

FIPUG: Adopts the position of OPC.

FRF: Yes. Agree with OPC that FPL should be required to true up the actual costs incurred and continue to increase its contingency estimates. Further agree with OPC that a cut-off date of December 31, 2006 should be established for charging 2005 storm restoration costs to the reserve.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that a final true-up of 2005 storm related costs be performed when the actual costs for outstanding projects are known. (TR 1627) In its brief, OPC recommended that FPL should be required to true-up the actual costs incurred and not continue to increase the amount of contingency costs as a plug amount to keep the storm cost equal to the original amount requested or to the estimated amount approved by the Commission. A cut-off date of December 31, 2006 should be established for charging 2005 storm restoration costs to the reserve.

ANALYSIS

FPL witness Davis testified that a final-true-up be conducted for 2005 storm costs when final costs for the 2005 storm repair projects are known and can be compared and reconciled against the estimates. At a minimum, any cut-off date for 2005 storm charges to the Reserve should recognize the projects listed by witness Williams in Exhibit 107, and when the actual costs for these projects are known, any necessary adjustments to true-up these estimates should be allowed. (TR 1627)

OPC witness DeRonne recommended a December 31, 2006 cut-off date. Witness DeRonne testified that "It is not appropriate to allow an indefinite period for charging costs associated the 2005 storms to the reserve." (TR 990) Witness DeRonne also proposed some parameters that should be applied to the cut-off date. Only projects that have been identified in this docket and for which physical construction has begun on or before December 31, 2006 should be allowed to be charged to the storm reserve for 2005 storm costs. (TR 990) In its brief, OPC proposed a true-up mechanism. All costs should be true-up to the actual amounts incurred and as adjusted by the Commission. Any projects started after the OPC recommended December 31, 2006 cut-off date should be charged to base rates, not the storm reserve. Further, OPC recommends that the staff should audit the actual amounts to ensure compliance with the Commission's order. (OPC BR at 41)

CONCLUSION

Staff agrees with FPL and OPC that some type of true-up should be approved for the 2005 storm costs. The true-up mechanism for the approved 2005 storm related costs should be based on the cut-off dates approved in Issue 26. These approved cut-off dates should be the basis for determining whether any costs should be charged to base rates rather than the storm reserve. FPL should be required to provide an annual true-up report by March 1st of each year for the preceding year ended December 31st until the repairs are completed.

Issue 22: Have the costs of repairing other entities' poles been charged to the storm reserve for 2005? If so, what adjustments should be made?

Recommendation: Yes. Storm costs should be reduced in the amount of \$10,564,384 for the costs of replacing other entities' poles. Of that amount \$4,156,615 should be booked to capital, and offset when reimbursement is received. (Marsh)

Position of the Parties

FPL: Yes. An estimate for the total cost of replacing other entities' poles has been appropriately charged to the Reserve. Reimbursements will result in appropriate credits to the Reserve. FPL has estimated the total amount to be billed and the portion relating to normal capital costs, and has credited the Reserve for the difference. However, FPL recommends that the actual amount be reflected in the final true-up of 2004 and 2005 storm costs.

OPC: Yes. However, FPL has not yet billed the outside parties for the repairs or replacements. The 2005 storm costs should be reduced by a minimum of \$7,923,288 to reflect an estimate of the amounts billed to other parties. This represents a placeholder adjustment of 75% of the estimate provided by FPL witness Williams of \$10,564,384 to provide an offset for capital costs.

FIPUG: Adopts the position of OPC.

FRF: Yes. Agree with OPC that a minimum of \$7,923,288 should be removed from FPL's claimed 2005 storm costs, and that FPL should be required to true up final costs to ensure that billings to outside parties for pole repair and replacement costs incurred by FPL are based on actual costs, and that they are appropriately credited to the benefit of FPL customers.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that FPL must complete its 2005 pole survey before preparation of the billing for pole replacements can begin. (TR 1621) He stated that while the survey was not completed as of March 31, 2006, FPL estimated that the total to be reimbursed by other parties would be \$10.6 million. (TR 1621) He stated that the estimated capital amount at normal cost would be \$4.2 million, with the estimated difference of \$6.4 million credited to the storm reserve account. (TR 1621) He said that any difference between actual and estimated amounts would be reflected during the true-up of 2005 storm costs. (TR 1621)

Witness Davis disagreed with OPC witness DeRonne's adjustment of \$7,923,288 for 2005 pole replacements. He testified that the correct number is derived by subtracting the estimated normal cost of capital for the poles of \$4,156,615 from the estimated reimbursement amount of \$10,564,384, yielding a difference of \$6,407,769. (TR 1621; EXH 121, p. 1) He stated that once the actual amount of normal capital is determined, the amount will be credited to plant-in-service. (TR 1622) He said that removal means that the amount will not be included in FPL's rate base for any future proceedings. (TR 1622)

OPC witness DeRonne stated that FPL had not included an offset to its 2005 storm recovery cost estimates for amounts to be recovered from third parties for pole repairs and replacements. (TR 966) She testified that FPL's request "includes many estimates which increase the projected cost, but does not include estimated offsets to such costs, other than for insurance recoveries." (TR 966-967) She stated that FPL expects to complete the 2005 storm pole survey in May 2006, after the hearings in this case. (TR 967)

Witness DeRonne stated that the proceeds to be collected from third parties would reduce the 2005 storm recovery costs. (TR 967) She testified that "any incremental amounts billed beyond the amounts capitalized by FPL should serve to reduce the estimated 2005 storm recovery costs to be recovered from ratepayers." (TR 967) The witness said that a review should be made in FPL's next rate case to ensure that the capital amounts reimbursed by third parties do not increase rate base. (TR 967)

Witness DeRonne stated that FPL's estimate of the costs to replace third party poles is \$10,546,384 for 2005. (TR 968) She testified that a 75 percent factor should be utilized to determine the amount of adjustment to be made because she believes that "the majority of the projected storm recovery costs are expenses as opposed to capital amounts." (TR 969) Thus, she removed \$7,923,288 from the amount to be recovered for 2005. (TR 969; EXH 85, p. 1) She also recommended a future review to ensure that FPL has billed other parties the appropriate amounts. (TR 988)

Staff witness Welch testified that the 2005 pole replacement survey had been initiated, but not completed. She stated that "FPL's total unrecovered storm costs should be reduced by the amount billed to other companies less the amount capitalized for the related poles." (Welch TR 1089)

Witness Welch testified that FPL's joint use agreements with other companies require that:

Whenever, in any emergency, the Licensee replaces a pole of the Owner, the Owner shall reimburse the Licensee all reasonable costs and expenses that would otherwise not have been incurred by the Licensee if the Owner had made the replacement.

(TR 1088; EXH 89, p. 10)

Witness Welch stated that she is making a specific recommendation to the Commission on Audit Finding No. 5. (EXH 157, p. 61) She testified that "any costs in addition to the normal costs that were capitalized for the pole [sic] really should reduce storm costs, because FPL is

recovering those costs from BellSouth.” (EXH 157, p. 61) Witness Welch said that the auditors did not find a credit to the storm reserve for amounts billed to other companies over the amount capitalized for 2005. (EXH 157, p. 62) She agreed with FPL that it would not be appropriate to make an additional adjustment if FPL had already credited the reserve account. (EXH 157, p. 62)

ANALYSIS

Staff agrees with OPC and with staff witness Welch that it is inappropriate to include costs to be reimbursed by others in the amount to be paid by ratepayers. Staff believes that inclusion of third-party pole costs only serves to inflate the amount that is to be borne by ratepayers during the recovery period. Accordingly, staff believes an adjustment should be made. Witness Davis’ calculations are close to those of witness DeRonne, and appear to be more credible, because witness DeRonne simply used a flat 75 percent factor. (TR 969) Accordingly, staff believes FPL’s figure of \$6,407,769 should be accepted.

Moreover, staff believes that the amount FPL has separated as capital costs should also be removed from the storm costs. FPL witness Davis’ exhibits show a number of capital expenditures to remove from the starting figure. (EXH 121, p. 2) These adjustments were not part of the original filing. Thus, in order to capture FPL’s adjustment, it is necessary to include it in the adjustments recommended by staff. Therefore, an additional \$4,156,615 should be removed from the storm costs. (Davis TR 1621) The total of the two figures is \$10,564,384 (\$6,407,769 + \$4,156,615).

Upon removal of the amount from storm costs, staff does not believe it will be necessary to conduct a follow-up review of the amounts of other entities’ pole repairs in association with the storm proceeding. Staff agrees with OPC that any review that is needed would be more appropriate in FPL’s next rate proceeding to make certain that FPL has billed the amounts to third parties and has made the appropriate adjustments.

CONCLUSION

Staff recommends that storm costs should be reduced in the amount of \$10,564,384 for the costs of replacing other entities’ poles. Of that amount \$4,156,615 should be booked to capital, and offset when reimbursement is received.

Issue 23: WITHDRAWN

Issue 24: Has FPL charged any other costs to the storm reserve that should be expensed or capitalized? If so, what adjustment should be made?

Recommendation: Yes. The 2005 storm-related costs should be reduced by \$561,275. However, FPL should be authorized to charge the storm reserve to the extent that any of the disallowed \$316,250 in repair costs is not recovered through an existing warranty. (Slemkewicz)

Position of the Parties

FPL: No.

OPC: Yes. Additional adjustments should be made to the requested 2005 storm costs should be made for employee assistance costs and repair costs under warranty.

FIPUG: The Commission should make an adjustment to offset FPL's storm damage costs by the proceeds received from assisting other utilities with storm restoration since 2003. In the future, FPL should credit such revenues to the storm damage reserve. Agree with OPC as to any other adjustments.

FRF: Yes. Agree with OPC as to additional adjustments for employee assistance costs and repair costs under warranty.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

In its brief, FPL takes the position that no adjustments are necessary. OPC witnesses Larkin and DeRonne testified that the 2005 storm costs should be reduced by \$561,275 to remove employee assistance costs and repair costs under warranty.

ANALYSIS

OPC's two proposed reductions are \$245,025 for employee assistance costs and \$316,250 for repair costs under warranty.

Employee Assistance Costs

FPL witness Davis testified that after a storm passes, FPL provides assistance for things such as roof tarps, ice, water, etc. that allow the employee to immediately leave his or her home and report to work. If the Company does not provide this assistance, the employee is going to have to take care of these issues before reporting for storm duty which could impact their ability to report to work as quickly as they otherwise would, delaying the start of restoration. These costs would not have been incurred, but for the need to restore service due to outages caused by the 2005 storms as soon as possible. (TR 1611) Witness Davis also said that under either an incremental cost approach or FPL's proposed methodology, these costs are appropriate for recovery as they are directly related to storm restoration and are not a cost that would be budgeted or reflected in base rates. (TR 1612)

OPC witness Larkin testified that costs provided to assist FPL employees to secure their personal damaged property should be removed. These are employee benefit costs and are not directly related to restoring FPL facilities. Customers are not in a position to pass their costs on to third parties, and neither should employees of FPL be allowed to pass their personal costs related to the hurricane on to customers through FPL. (TR 914-915)

Staff agrees with OPC that these employee assistance costs are for the benefit of the employee and are not directly related to storm damage restoration activities. Staff recommends that the 2005 storm damage costs be reduced by \$245,025 to remove the employee assistance costs.

Repair Costs Under Warranty

FPL witness Davis testified:

FPL has included this amount [\$316,250] in its 2005 storm costs because the warranty claim is being contested by the manufacturer. If FPL is successful in recovering an amount under the warranty, then FPL will adjust the 2005 storm costs by this amount. Until this has been finalized, FPL believes this amount has been appropriately included in the 2005 storm costs and should not be adjusted at this time. If the Commission determines that this amount should be removed from storm cost recovery, then FPL requests that specific provision be made to allow FPL to charge the storm reserve to the extent any of the costs are not recovered through the warranty.

(TR 1609-1610)

OPC witness DeRonne testified that FPL included an estimated \$316,250 for a cooling tower fan repair at Martin Unit 8 even though a warranty claim is being pursued. Although the estimated amounts charged to the reserve will be trued-up to actual as the amounts become known, it is not appropriate to include such costs in the estimates. (TR 964)

Staff agrees with OPC that these repair costs subject to a warranty claim should not be included in the 2005 storm costs at this time. Staff recommends that the 2005 storm costs be

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reduced by \$316,250 disputed warranty claim. However, staff believes that FPL's request to charge the storm reserve to the extent any of the costs are not recovered through the warranty is reasonable and should be approved.

CONCLUSION

Based on the above discussion, staff recommends that the 2005 storm costs be reduced by \$561,275, calculated as follows:

Employee Assistance Costs	\$(245,025)
Repair Costs Under Warranty	<u>(316,250)</u>
Total Adjustment	<u>\$(561,275)</u>

Issue 25: Taking into account any adjustments identified in the preceding issues, what is the appropriate amount of 2005 storm related costs to be charged against the storm reserve, subject to a determination of prudence in this proceeding?

Recommendation: The appropriate amount of 2005 storm related costs to be charged against the storm reserve, subject to a determination of prudence, is \$725,398,982 (\$725,972,500 system). (Slemkewicz)

Position of the Parties

FPL: The appropriate amount of 2005 storm related costs to be charged against the Storm Reserve, subject to a determination of prudence in this proceeding, is \$816,016,000 (rounded) as adjusted in the final true-up. (See issue 42).

OPC: This is a fall-out issue.

FIPUG: Adopts the position of OPC.

FRF: Fall-out issue.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: This is a fall-out issue based on the resolution of other issues. Staff recommends that the appropriate amount of 2005 storm related costs to be charged against the storm reserve, subject to a determination of prudence, is \$725,398,982 (\$725,972,500 system). This amount was calculated as follows:

<u>ISSUE</u>	<u>DESCRIPTION</u>	<u>\$</u>
	2005 Total Storm Costs	906,404,000
	Capital Expenditures	(63,855,000)
	Insurance Proceeds	<u>(26,533,000)</u>
	Net 2005 Storm Costs	<u>816,016,000</u>
	STAFF ADJUSTMENTS	
7	Normal Replacements and Improvements	
	- Condenser Tube Repairs	(2,785,364)
	- Hydrolasing Costs	(221,000)
	- Proceeds from Other Power Companies	(3,468,593)
8	Non-Managerial Payroll	(17,925,918)
9	Managerial Payroll	(768,000)
11	Tree Trimming	(1,100,000)
12	Company-Owned Fleet Vehicles	(5,738,000)
13	Call Center Costs	(520,264)
14	Advertising Expenses	(1,143,916)
15	Uncollectible Expense	(3,582,000)
16	Normal Replacement and Cost of Removal	(8,745,000)
17	a – Amounts Not Recovered	0
	b – Backfill Work	0
	c – Catch-Up Work	0
	d – Uncollectible Accounts	See Issue 15
	e – Outside Hires	0
	f – Clause Payroll	See Issue 8
	g – Capital Payroll	See Issue 8
	h – Vacation Buy-Backs	0
	i – Nuclear Payroll	See Issue 8
18	Landscaping	(3,816,864)
19	Lawsuit Settlement Charge	(2,849,571)
20	Contingencies	(26,253,351)
22	Other Entities' Poles	(10,564,384)
24	Costs to be Capitalized or Expensed	
	- Employee Assistance	(245,025)
	- Warranty Repairs	<u>(316,250)</u>
---	TOTAL ADJUSTMENTS	<u>(90,043,500)</u>
25	ADJUSTED TOTAL – 2005 STORM COSTS	725,972,500
---	Jurisdictional Factor	99.921%
25	JURISDICTIONAL 2005 STORM COSTS	<u>725,398,982</u>

Issue 26: At what point in time should FPL stop charging costs related to the 2005 storm season to the storm reserve?

Recommendation: Only the projects already identified in this proceeding related to damage from the 2005 storm season on which construction has physically begun by December 31, 2006, should be allowed to be charged to the storm reserve. However, FPL has justified the reasons for the delay in starting some of the nuclear unit repairs and should be allowed to charge those costs to the storm reserve for projects on which construction has physically begun by December 31, 2008. A true-up should be performed when the projects are completed. FPL should submit a schedule of the allowable projects in progress as of December 31, 2006, by February 15, 2007. This schedule should include the amount actually spent to date, the estimated total cost, the start date and the estimated completion date. (Slemkewicz, Lee)

Position of the Parties

FPL: Consistent with its approach to 2004 storm costs, FPL has charged the full amount of its storm costs to the Reserve as of March 31, 2006, including an estimate for uncompleted work. When all work has been completed and final costs are known, a final true-up should be performed.

OPC: The Commission should order that only projects that have been identified in this docket and physical construction has begun on or before December 31, 2006 should be allowed to be charged to the storm reserve for 2005 storm costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC that only the costs for projects that have been identified in this docket and for which physical construction has begun on or before December 31, 2006 should be allowed as charges to the storm reserve for 2005 storms.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL witness Davis testified that an arbitrary cut-off date for 2005 storm charges should not be established. Witness Davis said that when all of the work has been completed and final costs are known, a final true-up should be performed. However, if a cut-off date is established, it should recognize the projects listed in Exhibit 107. (TR 1627) FPL witness Warner said that FPL should be allowed to continue to charge nuclear storm damage repairs to the reserve through 2008. That is the anticipated completion date for all storm-related repairs. (TR 391)

OPC witness DeRonne testified that December 31, 2006, should be the cut-off date for charging 2005 storm restoration costs to the reserve. (TR 990)

ANALYSIS

FPL witness Williams testified that “All projects and associated costs directly related to restoring FPL’s facilities to their pre-storm condition should be charged to the Storm Reserve, whether they are known now or not. FPL attempts to quickly identify storm follow-up projects in order to restore storm-affected facilities to their pre-storm condition as soon as possible.” (TR 1406) Nonetheless, there are unique circumstances and good business reasons to delay the timing of restoring FPL’s damaged generating unit facilities to later dates that coincide with planned overhaul schedules. (TR 1406) Witness Davis said that “There are many reasons for the extended timing including when plants come down for outages, and availability of contractors or other resources.” (TR 1627)

FPL Witness Warner testified that:

After a storm strikes, FPL’s priority is to return the low cost nuclear units back to service as safely and quickly as possible. The units can sometimes be brought back online without repairing all storm-related damage. However, the repairs are still critical to ensure the long-term reliability of plant operations and must be made at the earliest possible opportunity. Again, due to the nature of nuclear operations, it may take several years to restore the nuclear plants to pre-storm conditions.

(TR 392)

FPL witness Williams sponsored Exhibit 107 (GJW-10), which provides a listing of projects for the 2005 storm season that are yet to be completed, their total current estimated costs, and their project start and completion dates. FPL witness Davis testified that the final, actual cost of these projects should be charged to the reserve when they are ultimately completed. (TR 1627) FPL witness Warner said that because of FPL’s limited opportunities even to inspect some components of its nuclear units, it should be permitted to charge the reserve with the cost of repairs to those units that are related to the 2005 storm season until 2008. (TR 391-392)

In recommending a December 31, 2006 cut-off date, OPC witness DeRonne testified that “It is not appropriate to allow an indefinite period for charging costs associated with the 2005 storms to the reserve.” (TR 990) Witness DeRonne also proposed some parameters that should be applied to the cut-off date. Only projects that have been identified in this docket and for which physical construction has begun on or before December 31, 2006 should be allowed to be charged to the storm reserve for 2005 storm costs. (TR 990)

CONCLUSION

Staff agrees with OPC that a specific cut-off date should be established for charging the reserve for 2005 storm costs. Staff believes that a December 31, 2006, cut-off date allows FPL

sufficient time to fine-tune its estimated costs for projects that have been identified already in this docket. Staff also agrees with OPC's proposed limitation that construction must be started by December 31, 2006 for the costs to qualify for being charged to the reserve. Staff also believes that FPL should submit a schedule of the allowable projects in progress as of December 31, 2006, by February 15, 2007. These provisions would apply to all repair projects except those related to the nuclear units.

Staff believes the timing of the nuclear unit repairs warrants economic and operating considerations. Because of the high replacement power costs incurred when a nuclear unit is off-line, damage assessment and repairs to certain equipment can only be performed during refueling outages, which occur approximately every 18 months. (Warner TR 389) FPL maintains that the repairs, including repairs to the intake and discharge canals, repair of coatings in various areas of the plant, and canal dredging, are critical to ensure the long-term reliability of plant operations, but due to the nature of nuclear operations it may take several years before the units can be fully restored to pre-storm conditions. (TR 390; FPL BR at 81) Staff believes that FPL has justified the reasons for the delay in starting the nuclear unit repairs.

The costs and the true-up should be subject to staff review. In addition, FPL has to work with its nuclear property insurer, NEIL, to ensure that FPL and NEIL agreed on the scope of damage prior to commencing the repair work. These additional requirements should mitigate OPC's concern of the potential pressures for FPL to seek out additional projects to somehow tie to the 2005 storms in order to result in a certain final cost level.

Staff recommends that only the projects already identified in this proceeding related to damage from the 2005 storm season on which construction has physically begun by December 31, 2006, should be allowed to be charged to the storm reserve. However, FPL has justified the reasons for the delay in starting some of the nuclear unit repairs and should be allowed to charge those costs to the storm reserve for projects on which construction has physically begun by December 31, 2008. A true-up should be performed when the projects are completed. FPL should submit a schedule of the allowable projects in progress as of December 31, 2006, by February 15, 2007. This schedule should include the amount actually spent to date, the estimated total cost, the start date and the estimated completion date.

PRUDENCE OF 2005 STORM CHARGES

Issue 27: Did FPL adequately inspect and maintain its distribution and transmission system for deterioration and overloading of poles prior to June 1, 2005? If not, what amount, if any, should be adjusted from the costs that FPL proposes to charge to the storm reserve and recover through securitization or a surcharge?

Recommendation: No. A downward adjustment of \$5,900,000 is warranted because: (1) some 2004 repair had not been completed prior to June 1, 2005, (2) FPL does not know whether it met the requirements of the National Electrical Safety Code (NESC) at each failed pole, (3) FPL has not shown that an increased level of pole inspection and maintenance was not prudent and funded by its base rates, and (4) FPL has not shown that its level of pole inspection and maintenance did not contribute to higher hurricane restoration costs in 2005. The recommended capital offset adjustment amount is \$1,440,000. The recommended expense adjustment amount is \$4,460,000. No other fines or penalties are recommended because there is no evidence that FPL refused to comply with or willfully violated any lawful rule or order of the Commission, or any statute administered by the Commission. (Breman)

Position of the Parties

FPL: Yes. FPL's pole inspection and maintenance program was reasonable, and produced excellent results. Pole related outages during non-storm events have been negligible for over a decade, contributing only about 0.1% of all outages annually. Pole performance during the 2004 and 2005 storm seasons also shows that FPL's pole inspection and maintenance program is reasonable and has produced excellent results.

OPC: FPL's pre-storm pole inspection process was inadequate. Osmose, the only valid inspection, covers less than 1% of poles annually. Thermovision inspections exclude 845,000 lateral poles, and detect only conspicuous external damage. Hazard assessments aren't recorded in a meaningful data base. Lacking actual data, KEMA invented the term "touchpoint opportunities", and substituted convoluted, speculative "probabilities." This effort failed to mask FPL's deficiencies. The Commission should adopt OPC's estimate of poles that failed from deterioration, based on FPL's own post-storm data.

FIPUG: Adopts the position of OPC.

FRF: No. FPL's inspection activities with respect to the deterioration of wood distribution poles were inadequate. Agree with OPC as to amounts of claimed repair costs that should be disallowed. Additionally, because FPL's activities were inadequate due to FPL's intentional cost-cutting efforts, they were imprudent and FPL should be penalized pursuant to Chapter 350 for the resulting failures, which resulted in excessive outages and losses being sustained by FPL's customers.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: No. The AG adopts and agrees with the position of the OPC. Additionally, this Commission should not permit recovery of costs resulting from inadequate infrastructure maintenance, nor reward FPL for its failure to adequately plan and prepare for the storm season. FPL's position on this issue is based on negligent or arrogant indifference to known risks, incomplete or inaccurate data, and/or a willingness to allow the consumer to absorb infrastructure maintenance costs through the storm docket.

Staff Analysis: Issue 33 addresses FPL's inspection and maintenance of transmission towers. In the following analysis, all references to FPL's pole inspection and maintenance pertain to FPL's distribution pole inspection and maintenance.

PARTIES' ARGUMENTS

FPL asserts its distribution pole inspection and maintenance actions have been reasonable and prudent for both hurricane and non-hurricane conditions prior to and during 2005. (TR 1386) FPL witness Williams testified that "our 2004 efforts and costs were determined by this Commission to be prudent and reasonable. Because the '05 efforts and results are very similar for the number of customers affected, for the days to restore service, and for the total restoration costs, I would conclude that FPL's 2005 restoration efforts and costs are likewise reasonable and prudent." (Williams TR 199; EXH 14) Prior to and during 2005, FPL's pole inspection program consisted of three initiatives: – (1) a targeted pole inspection program that specifically addresses one of FPL's older pole types, (2) visual inspection of main-trunk feeder poles on a five year cycle, and (3) inspections conducted as part of daily work activities. (Williams TR 191; TR 1390-1391; Brown TR 257; EXH 15, pp. 31-32) FPL asserts its actions have been reasonable because pole outages for reasons other than hurricanes are almost nonexistent. For example, during the period 1999-2004, pole related outages accounted for approximately 130 outages per year, or just 0.1 percent of all outages experienced by FPL's customers. (Williams TR 191, 199; EXH 104) A survey of other utility standards and practices was performed by KEMA and included in Exhibit 15. FPL witness Brown states that the survey conclusions are: (1) FPL designs and constructs distribution facilities to a more stringent standard than most other companies, (2) none of the companies are required by their regulatory authority to place facilities underground in response to storm damage, and (3) most of the responding companies have a systemic pole inspection and treatment program in place with inspection cycles ranging from 10 to 15 years for older poles. (TR 260; EXH 15, pp. 81-83, 86-97) Additionally, FPL's hurricane pole replacement data from 1992 through 2005 compares favorably with that of other utilities because FPL's pole replacement rates have been consistently lower than those of other utilities. (Williams TR 1387; EXH 105)

Witness Williams believes FPL's management decisions from 1998-2004 resulted in good non-hurricane performance, which translates into good hurricane performance. (Williams TR 187-190) With respect to declines in budget levels for FPL's Pole Inspection Program (EXH 140), witness Williams stated:

[t]here's no such thing as a legacy program, so every single year when you're looking at your budget and your reliability plans, all these programs are looked at

with the fresh perspective of what kind of value can they deliver the following year. So just because you've been funded in the past does not mean that you automatically get funded in the future.

So as I look at these various funding levels from year to year, it could very well be that other programs came to the table that had a bigger benefit for the dollars to be expended. And I have to believe that, considering the excellent reliability that we've provided to our customers and really the very good pole performance that we've had throughout the time in question here.

(TR 220)

FPL witness Williams, while not agreeing that a disallowance was appropriate or supported, recalculated OPC witness Byerley's methodology using alternative assumptions that she believed to be more realistic resulting in an amount of \$1,800,000. (TR 1396-1397)

FPL's inspection and maintenance practices did not change significantly between 2004 and 2005, and no intervener testimony focuses on differences between those years. FPL finds it curious that historical inspection and maintenance practices that were deemed acceptable last year and that have not changed significantly since then, are now suddenly the subject of close scrutiny. (FPL BR at 82-83)

OPC witness Byerley believes FPL's pole inspections, prior to the 2005 storms were not adequate based on his review of FPL's 1998 pole inspections, five respondents to KEMA's survey of other utilities (EXH 15, pp. 86-97), Rule 214.A.2 of the National Electrical Safety Code, and a review of Rural Utilities Services Bulletin 1730B-121. (TR 802-809) Witness Byerley believes the KEMA Report, fails to recognize that past pole failure rates themselves were the result of a long period of insufficient pole inspection and maintenance practices. (TR 813) He was not surprised that FPL's pole performance during hurricanes has not improved over the past 14 years because FPL did no pole inspections from 1991 to 1999. (TR 813; EXH 81, p. 1) FPL suspended its pole inspection program in 1991 as a cost-cutting measure. (EXH 76, p. 4) The inspections resumed after 1999 were, in witness Byerley's opinion, inadequate. Initially, FPL performed approximately 28,000 pole inspections. (TR206)

OPC witness Byerley recommended an adjustment of \$18,319,872 for inadequacies he believed existed in FPL's inspection and maintenance of poles. (TR 811-812; EXH 152, p. 10) When questioned regarding the appropriateness of including or excluding approximately 600 poles with streetlights, he indicated that he had no recollection of seeing any FPL wooden street lighting poles that did not also have other distribution attached. (TR 860-866) He agreed that a 28% percentage was more appropriate to use in his calculations rather than a 45% percentage if one was looking at the FPL-owned poles that are creosote. (TR 870) Also, he assumed that by multiplying a normal pole replacement cost of \$1,700 per pole by a factor of four, he would approximate the higher overall costs likely to occur during the 2005 storm restoration activities. (TR 871; EXH 76, p. 17) FPL witness Williams suggested that a more reasonable estimate would be the price of \$2,000 which FPL was using for purposes of billing telephone companies for pole replacement costs incurred in 2005. (TR 1441)

FRF asserts that Hurricane Wilma was predominately a Category 1 storm. (FRF BR at 3-5, 22-28, 32) FRF references FPL's statements that its system performed as expected and designed. (TR 218) FRF concludes that FPL designs for outages to 75 percent of its total customer base in Category 1 storms. (FRF BR at 32) FRF also points to asserted cost cutting activities by FPL and concludes that FPL's long-term planning is not reasonable and prudent. (FRF BR at 5, 32; EXH 140)

FRF supports the position of OPC and the methodology for calculating the adjustment. (FRF BR at 17) FRF disagrees with witness William's estimate of \$2,000 per pole replacement because her proffered value is unsupported by any analysis in the record. (FRF BR at 17) The majority of the total 2005 storm costs for transmission and distribution of \$782 million was related to distribution costs. (TR 1420-1422) Thus, FRF believes the opinion of witness Byerley is reasonable as representative of the total costs incurred including overtime, and living expenses for visiting workers, and contractors. (FRF BR at 18)

With respect to Issues 27, 28, 30, and 31, FRF argues that penalties pursuant to Chapter 350, Florida Statutes, should be assessed. In Issues 30 and 31, FRF urges the Commission to assess a \$5,000 per day penalty from January 1, 2006 through October 23, 2006. FRF suggests the Commission could begin assessing penalties as early as 2002 when FPL began cutting its pole inspection program. (FRF BR at 5)

ANALYSIS

Standard of Performance

FPL witness Williams' apparent premise is that FPL was reasonable and prudent in its pole inspection and maintenance activities during 2005 because FPL was found to be reasonable and prudent in 2004. (TR 199) Staff disagrees with FPL because the facts in this case are substantially different. In the 2004 Storm Order, on pp. 23-24, the Commission found that:

We find that the costs that we found to be appropriately charged to the storm reserve, as set forth in the table above (in Section II.D.), are reasonable and prudent. At the customer service hearings in this docket, extensive testimony was offered in praise of FPL's storm restoration efforts. No party has challenged the reasonableness or prudence of these efforts. More importantly, no party has challenged the reasonableness or prudence of any specific cost among those that we found to be appropriately charged to the storm reserve. Thus, based on the record established, it appears that the costs that we found to be appropriately charged to the storm reserve are reasonable and prudent.

We do not, however, make a finding of reasonableness or prudence for those costs that FPL booked to its storm reserve other than listed in the table above (in Section II.D.). We believe it is unnecessary to make such a finding with respect to costs that are not being proposed for cost recovery at this time or that the Commission believes were not appropriately charged to the storm reserve and thus not appropriate for recovery through the surcharge proposed by FPL (i.e., the costs disallowed in the previous issues). Such a finding could bind this Commission in a future proceeding concerning recovery of those costs, such as a

proceeding initiated under the recently signed securitization bill or the rate case pending at the time of our decision in this docket. (emphasis added)

In this case, concerns regarding the long term consequences of FPL's past decisions have been raised both at the customer service hearings and at the technical hearing. Eleven direct statements from a total of 127 direct statements taken at the service hearings expressed concerns related to the level of FPL's pole maintenance activities, lack of responsiveness in addressing pole issues and wire down conditions, and an apparent decline in FPL's reliability performance. (Palm Beach TR 29, 37, 59, 70, 72; Ft. Lauderdale TR 62, 70, 79, 109; Miami TR 50, 81, 84) The balance of the service hearing testimony addressed matters such as corporate relations with communities, prospective infrastructure design improvements, prospective underground projects and credits, vegetation practices, potential for cost sharing, and requests for the Commission to avoid further bill increases. At the technical hearing, OPC witness Byerley and a report by KEMA (EXH 15) raised questions with respect to the level of FPL's pole inspection and maintenance programs and the level of pole performance data FPL retains. Staff concludes that in this case, there is testimony that criticizes FPL for its pole inspection and maintenance activities.

FPL must show that FPL has been prudent in each instance where FPL's 2005 charges for storm restoration activities are being challenged.

Concerns Raised

FPL's pole inspection program is sometimes referred to as the Osmose program because Osmose is the contractor. (TR 201; EXH 15, p. 25). Both FPL-owned and non-owned poles are inspected. (EXH 15, p. 31) For each pole inspected, Osmose provides a database to FPL containing: (1) pole location, by street address or other means, (2) GPS coordinates, (3) pole brand, date, month, and year, (4) pole length and class, (5) species of wood, (6) original treatment, (7) pole supplier, (8) FPL grid number if available, (9) ground line circumference, (10) condition of pole above ground line, (11) condition of attachments, (12) last year inspected, (13) last year treated, (14) decay this cycle, (15) evaluations, and (16) work performed. (TR 202; EXH 15, p. 26)

OPC witness Byerley believes that FPL's distribution pole inspection and maintenance practices have not been adequate because from 1991 through 1997, FPL did not fund such pole inspections. (TR 803; EXH 76, p. 9) In 1998, FPL conducted a study showing that 26 percent of its creosote poles were defective, yet FPL's implementation program in 1998 appeared limited. (TR 802-803; EXH 76, p. 9) The number of pole inspections declined over the years. (TR 219, 306, 307, 819; EXH 81, p. 3) KEMA, in its review of FPL's current pole inspection and maintenance program, concluded that FPL's current pole inspection program is very small in scope and focuses on specific areas. (TR 343; EXH 15, pp. 31-32) KEMA also found that FPL does not have a process in place to track what third parties do to the non-FPL owed poles when the inspections indicate remediation is needed. (EXH 15, p. 31)

Since 1998, FPL has also performed visual inspections of distribution FPL-owned and non-owned poles that comprise the main-trunk feeders. The visual inspections are performed in conjunction with another form of inspection known as the Thermovision program. (TR 200; EXH 15, p. 32) The objective of a visual pole inspection is to record any obvious outward

damage to poles. (TR 210) Witness Byerley noted that because FPL's visual pole inspection program is limited to main-trunk feeders it does not address approximately 65 percent of FPL's poles. (TR 805; EXH 15, pp. 31-32, 58). Similar to the pole inspections, FPL does not have a process in place to track what third parties do to the non-FPL owned feeder poles when the visual inspections indicate remediation is needed. (EXH 15, p. 31)

FPL field personnel perform hazard assessments of poles in the course of normal business. These assessments are estimated to address 80-90 percent of FPL's non-feeder poles over a 15-year period. (EXH 15, pp. 32, 35) Witness Byerley notes that a workman generates a report only if a condition is observed to be hazardous to the assigned task and that FPL does not maintain a database of such information for purposes of assessing pole specific performance. (TR 814) FPL did not rebut this assertion.

Collectively, FPL's distribution pole inspection and maintenance programs do not target 100 percent of the distribution poles. The pole inspection program appears focused on creosote poles because the life expectancy of creosote poles is 27 years. By 2001, creosote poles composed 48 percent of FPL's total distribution pole population of 1,300,000. Most of the creosote poles at that time were known to be over 27 years old. (EXH 76, p. 9) FPL's visual inspection activity specifically excludes 65 percent of the distribution poles. FPL's field hazard assessments, if such data were tracked, would not capture 10-20 percent of the remaining 65 percent.

Based on level of FPL's distribution pole inspections and associated maintenance, witness Byerley believes many of the poles that fell during Hurricane Wilma did so not because of high winds but because of their deteriorated condition. (TR 807) Staff agrees.

Strength of Hurricane Wilma

There is no record of wind speeds specific to each location where FPL replaced distribution poles. A wind speed assumption is necessary to perform forensic analysis. KEMA assumed that the intensity of Hurricane Wilma was initially a Category 3 and later a Category 2 hurricane. (EXH 15, p. 80; EXH 143, pp. 2, 4) However, the maximum wind speed recorded throughout Florida varied by location and not all of FPL's impacted area experienced Category 3 and Category 2 wind speeds. (EXH 143, pp. 10-14).

Wind speed assumptions are used throughout KEMA's assessment of pole failures. KEMA relied on FPL's forensic data to perform its engineering analysis. (TR 259; EXH 15, p. 50) Thus, the wind assumptions made by FPL's forensic team at each site during their respective surveys are the most significant and controlling assumptions.

Staff believes that FPL's forensic team members were sufficiently qualified to consider the variability of weather at each inspection location during their respective field surveys based on the representation of witness Williams. (TR 1458) It would not be good management practice to ignore the comments made by the forensic team members. (TR 1459) Consequently, staff recommends reliance on the opinions of FPL's forensic team with respect to the causes of pole failures because the forensic data is expected to include expert judgments as to local wind speeds and resulting damage to FPL facilities.

FPL's Industry Benchmarks

FPL witnesses Williams and Brown provided industry benchmark comparative information intended to show that FPL has taken reasonable actions and that its level of performance was at least adequate or good when compared to other utilities. (EXH 105; EXH 15, pp. 81-83, 86-97; TR 1308-1313) However, FPL's witnesses Williams and Brown did not provide any substantive assessment of the costs other utilities incur for pole inspection, the level or type of inspections, maintenance activities, and storm restoration. FPL witness Williams believes such data is necessary to perform a complete analysis. (TR 1387) Staff concludes that FPL has not shown that the industry benchmark comparative provides a complete analysis consistent with the testimony of FPL's witness. Furthermore, the industry benchmark data are in no way informative of the level of service expected by FPL's retail customers and the resultant costs.

FPL witness Williams testified that incremental utility costs, (for example: costs for more aggressive inspections and costs for pre-storm detection and replacement), need to be considered. (TR 1387) However, FPL's witnesses Williams and Brown did not provide any assessment of the costs other utilities incur for pole inspection, the level or type of inspections, maintenance activities, and storm restoration such that complete analysis could be made consistent with the testimony of FPL witness Williams. Furthermore, FPL witnesses did not show that FPL's base rates were not already set to level sufficient to address any such incremental costs.

Staff concludes that the industry benchmark comparative information does not show that FPL was reasonable and prudent to provide the level of service it did prior to and during 2005. The industry benchmarks do not show that FPL's base rates were not sufficient to address costs to implement distribution pole inspection and maintenance activities at a higher level than that set by FPL.

FPL's Performance

Beginning in 1998, FPL's pole inspection program and FPL's visual pole inspection programs can be viewed as an annual program even though FPL does not implement programs on a legacy basis. Every year since 1998, these programs have been reviewed and budgeted. (Williams TR 220) An annual renewal since 1998 means FPL found merit in the programs. The limited scope of the programs, as previously identified by KEMA and witness Byerley, means FPL repeatedly elected not to materially increase program funding subsequent to 1999 and prior to 2005.

FPL's annual review of pole inspection and maintenance activities and funding levels has resulted in approximately 125 non-hurricane related pole failures per year. (EXH 104) FPL witness Williams characterizes such events as negligible, apparently, because FPL is a large utility and the total number of outages on its system is a large number. (TR 191, 1386, 1410) In 2001, FPL did not replace poles due to budget constraints in their North Florida management area. (TR 1450; EXH 81, p. 6) Also, going into the first storm of 2005, FPL still had pending repairs to complete associated with the hurricane events of 2004. (TR 1455-1456) FPL witness Williams agreed that it is possible that some of FPL's facilities prior to the 2005 storm season were attached to poles that may not have met the requirements of the NESC or of FPL's

Distribution Engineering Reference Manual. (Williams TR 1461-1463; EXH 153, pp. 9, 12, 13) At least ten percent of FPL's distribution poles were not likely to be inspected. (EXH 15, p. 36) Additionally, KEMA notes that FPL's hurricane restoration efforts appear to cause the system to become slightly weaker because some of FPL's pole replacements were of lower strength. (EXH 15, p. 76)

FPL witness Williams believes it is not good management policy to ignore the comments made by FPL's forensic team, yet, at the same time she substantially ignores or dismisses 11 instances where the forensic team noted possible pole failures due to design overloading. Her rationale for discounting the opinions of the forensic team appears based on a view that Hurricane Katrina was a relatively low wind storm. (TR 1458-1459) It is especially disconcerting that witnesses Williams and Brown would be inclined to dismiss comments made by the well-qualified assigned experts who collected and reviewed the field data because FPL has not shown it maintains detail records regarding pole inspections and the status of remedial actions when inspections were made. (EXH 15, pp. 32-34, 51)

In 1999, when FPL began funding of a pole inspection program, that program provided FPL with the ability to develop a database of pole specific information, inspection results, and pole performance data. FPL witness Williams indicated that the same program existed in the 1980s. (TR 201-202) Yet, KEMA, in Exhibit 15, at pages 32-34 and 51, points out that FPL does not track or retain pole inspection results and pole performance data. When FPL witness Williams was asked regarding a recent Commission decision to step up FPL's recently proposed ten-year pole inspection program, she responded in part with the following:

I fully intend, now that we're going to be capturing some very specific data on our poles, both old poles as well as new poles, that if in time it does not look like those costs are prudent because they're not resulting in real, tangible benefit to the customers, then I certainly will be coming back to the Commission whenever that time is and may be asking to reduce that cycle.

(TR 1436-1437)

The above statement is clear and unambiguous. FPL has no facts to support a finding that FPL has been prudent and responsive to the level of service its customers expect. FPL does not know if FPL's distribution pole inspection and maintenance practices are prudent. FPL had the ability to implement more distribution pole inspection and maintenance activities as early as the 1980s but elected not to do so. In light of the above testimony by witness Williams, FPL has not shown that, in any way, its past distribution pole inspection and maintenance practices avoided incurring higher costs during 2005 hurricane restoration activities.

Furthermore, FPL has not provided any evidence suggesting that its base rates prior to and during 2005 were not sufficient to address any incremental costs FPL may have had to incur for increased pole inspection and maintenance activities.

Estimating the Adjustment

A downward adjustment is warranted because: (1) some 2004 repair had not yet been completed, (2) FPL does not know whether it met the requirements of the NESC at each failed

pole, (3) FPL has not shown that an increased level of pole inspection and maintenance was not prudent and funded by its base rates, and (4) FPL has not shown that its level of pole inspection and maintenance did not contribute to higher hurricane restoration costs in 2005.

A downward adjustment is calculated by OPC witness Byerley. His approach focuses on the program FPL initiated in 1998/99. (TR 811; EXH 152, p. 10) FPL's program was triggered by its expectation that creosote poles were subject to failure and expected to fail at an increasing rate. (TR 802-803)

Staff believes the methodology provided by OPC witness Byerley, with certain modifications, can be used as a regulatory tool that provides a test of the effectiveness of FPL's implemented programs. In following this approach it is understood that this effort is not intended to be a calculation of the exact impact of FPL's long term pole inspection and maintenance practices on the storm restoration costs of 2005.

Staff's modification to the methodology provided by witness Byerley is an effort to recognize non-FPL owned assets are also used to provide retail service. Staff notes that FPL has electrical facilities attached to at least 72,283 creosote poles owned by telephone companies. (EXH 81, p. 2) FPL incurs the cost to inspect poles it does not own. (EXH 15, p. 31) Further, FPL's overall quality of service is affected by the reliability of the poles it does not own.

The record supports different factors and weights than those proposed by witness Byerley. However, such efforts may be an exercise in false precision given the uncertainty of FPL's distribution pole specific data and because hurricanes are indiscriminate destroyers. Additionally, post-storm statistical inferences about damages not specifically studied by forensic review teams are not highly reliable because FPL has not maintained pole-specific performance data. Each key factor and weight used by witness Byerley that is specifically rebutted by FPL witness Williams is addressed below.

Number of Poles

Discussion regarding the number of poles with which to begin an adjustment calculation focused on whether approximately 600 streetlight poles should be included. Witness Byerley explained that he did not find evidence that wooden pole with streetlights did not also have other distribution facilities attached. (TR 860-866; EXH 152, p. 10; EXH 153, p. 10) Staff observes that KEMA reported 5,286 FPL-owned broken poles in Exhibit 15, at page 61. FPL witness Williams asserts that witness Byerley over-estimated the number of FPL distribution poles replaced by approximately 900 poles based on her estimate of 6,500. (TR 1396) She does not indicate whether her estimate includes or excludes streetlight poles. FPL is still in the process of determining which replaced poles were FPL-owned. (EXH 4, p. 236) Consequently, the precision of the number of FPL-owned poles is not known.

As previously discussed, staff believes any adjustment made in this issue should recognize that FPL has an obligation with respect to ensuring the poles it places facilities on are properly maintained regardless of ownership. Also, the adjustment should recognize FPL's practice of including the cost of replacing non-owned poles count in its estimated storm restoration costs. (TR 1419, 1441) Staff concludes that the replaced pole count of approximately

11,400 be used because FPL replaced approximately 11,400, poles in 2005 due to hurricane damage. (TR 1419; EXH 15, p. 58)

FPL Owned and Non-Owned Creosote Poles

On cross examination, witness Byerley agreed that a 28 percent weight was more appropriate to use in his adjustment calculation rather than the 45 percent weight if one was looking at the FPL poles that are creosote. (TR 820)

As previously discussed, staff does not believe FPL's obligation to serve associated with its use of non-owned creosote poles should be adjusted out as a matter of policy. Staff recommends use of a weight that represents FPL's obligations associated with using both FPL owned and non-owned creosote poles. The combined weight of both FPL owned and non-owned creosote poles is 45 percent. (EXH 152, p. 10; EXH 153, p. 10)

Pole Replacement Cost During Storm Restoration

OPC witness Byerley suggested an estimated FPL's per-pole replacement cost to be \$6,800, because he believes storm restoration costs could be approximately four times FPL's average per-pole replacement cost of \$1,700. (TR 871; EXH 76, p. 17) FPL witness Williams suggested an estimate of \$2,000 because \$2,000 is the price that FPL was using to bill telephone companies for each pole replacement that incurred in 2005. (TR 1441) In March 2006, FPL revised its method of calculating the billed amount from approximately \$6,000 to approximately \$2,000. (TR 219-220; EXH 4, p. 279) Consequently, the apparent concern with witness Byerley's testimony is his four times multiplier. Whether use of the four times multiplier results in overestimating or understating the exact impact of FPL's long term pole inspection and maintenance practices on the storm restoration costs of 2005 is not known.

Staff recommends that use of the \$2,000 per pole replacement cost is reasonable, because FPL is billing telephone companies based on an average of \$2,000 per pole replaced.

Conductor Replacement Costs

Witness Byerley calculated a factor of 0.88 for conductor replacement costs per replaced pole cost. The ratio is derived from FPL's 2004 total conductor replacement costs of \$8.3 million (Account 365) for 2004 and FPL's 2004 total pole replace costs of \$9.4 million (Account 364). (TR 812) It is important to note the factor recommended by witness Byerley is on a per dollar basis of all conductor replacements and all pole replacements for 2004. By using the 2004 pole replacement costs, he is consistent with his assumption of \$6,800 per pole replacement because that was the level of costs incurred in 2004.

FPL witness Williams believes his methodology overstates the conductor costs associated with pole replacements because she believes 90 percent of the conductor damage was due to wind, trees, and debris. (TR 1397) Thus, she suggests that a factor of 10 percent should be used. (TR 1397, 1401) Witness Williams recommends a factor that, by definition, should only be applied to the amount or cost of conductor replacements and not the cost of replacing failed poles. Nevertheless, this is apparently what was done to arrive at her estimated \$1.8 million adjustment.

Staff recommends a factor lower than the 0.88 offered by witness Byerley because staff believes FPL's pole replacement price in 2004 was approximately 3.4 times ($\$6,800/\$2000=3.4$) more than what FPL shows for 2005. Staff accepts witness Byerley's judgment regarding the relative cost relationship between replaced conductors and replaced poles because it is the only one in the record. Staff recommends use of an estimated conductor replacement cost fact of 0.26 per pole replaced ($0.88 \div 3.4 = 0.26$).

Table of Adjustments

A summary of the differences between the calculations of witnesses Byerley, Williams and staff's recommendation is provided below in Table 27-1. Staff recommends using OPC witness DeRonne's 25 percent capital offset assumption to estimate the respective rate base and expense amounts of the adjustment. (EXH 85)

TABLE 27-1
 Calculation of Distribution Pole Inspection and Maintenance Adjustment

	OPC Witness <u>Byerley</u>	FPL Witness <u>Williams</u>	<u>Staff</u>
Number of Pole Failures	6,925	6,500	11,400
Percent Creosote	28	28	45
Percent due to Deterioration	46	46	46
\$/pole Replaced	\$1,700	\$2,000	\$2,000
Escalation due to all price increases during storm restoration	4	1	1
Pole Replacement Cost	\$6,065,600	\$1,674,000	\$4,720,000
Conductor Cost per replaced Pole Cost	0.88	.10	.26
Total Adjustment (Rounded)	\$11,400,000	\$1,800,000	\$5,900,000
25 % Capital Offset Amount	\$ 2,850,000	\$ 450,000	\$1,440,000
Expense Amount	\$ 8,550,000	1,350,000	\$4,460,000

Penalties

The imposition of fines and comparable penalties pursuant to Chapter 350, or, more appropriately, Section 366.095, Florida Statutes, is limited to instances where a utility refuses to comply or willfully violates any rule, order, or statute administrated by the Commission. In this case and issue, no one has identified a rule, order or statute administrated by the Commission that FPL failed to implement or comply with. Hence, no fines are recommended.

CONCLUSION

A downward adjustment of \$5,900,000 is warranted because: (1) some 2004 repair had not yet been completed, (2) FPL does not know whether it met the requirements of the National Electrical Safety Code at each failed pole, (3) FPL has not shown that an increased level of pole inspection and maintenance was not prudent and funded by its base rates, and (4) FPL has not shown that its level of pole inspection and maintenance did not contribute to higher hurricane restoration costs in 2005. The recommended capital offset adjustment amount is \$1,440,000 and the recommended expense adjustment amount is \$4,460,000. No other fines or penalties are recommended because there is no evidence that FPL refused to comply with or willfully violate any lawful rule or order of the Commission, or any statute administered by the Commission.

Issue 28: Did FPL adequately control vegetation around its distribution and transmission system prior to June 1, 2005? If not, what amount, if any, should be adjusted from the costs that FPL proposes to charge to the storm reserve and recover through securitization or a surcharge?

Recommendation: A downward adjustment of \$3,400,000 is warranted because: (1) in 2004 and 2005, FPL was aware of avoidable tree-related customer outages, (2) in 2004 and 2005 FPL limited the implementation of a program that contributes to decreased tree-related customer outages, (3) FPL has failed to show that its reduction to the level of vegetation management, which was included in its last rate case, was prudent, and (4) FPL has failed to demonstrate that its reduced level of vegetation management did not contribute to higher hurricane restoration costs in 2005. The recommended capital offset adjustment amount is \$850,000 and the recommended expense adjustment amount is \$2,550,000. No other fines or penalties are recommended because there is no evidence that FPL refused to comply with or willfully violated any lawful rule or order of the Commission, or any statute administered by the Commission. (Breman)

Position of the Parties

FPL: Yes. The reasonableness of FPL's approach to managing vegetation is supported by excellent operating results, demonstrating improved performance over time. This performance has been achieved despite some difficult challenges. Tree density in FPL's service territory is twice the national average. Additionally, Florida's climate and twelve-month growing season result in some of the highest tree re-growth rates in the nation. FPL's vegetation management program is an important component of FPL's overall maintenance and reliability program, which has also achieved excellent results.

OPC: FPL's Vegetation Management Program is inadequate. Vegetation related outages have been increasing steadily since 1999. This concurs with the Staff Report in July 2005. The slight decrease in 2004 is due to excluding hurricane related outages. Internal studies show that FPL opted to repair damage after hurricanes rather than take preventive measures. If FPL had done preventive clearing before the hurricanes, many more consumers would have had power afterward. The Commission should adopt OPC's estimate of preventable tree-related damage.

FIPUG: Adopts the position of OPC.

FRF: No. FPL's pre-storm vegetation management activities were inadequate. Agree with OPC as to amounts of claimed repair costs that should be disallowed. Additionally, because FPL's activities were inadequate due to FPL's intentional cost-cutting efforts, they were imprudent and FPL should be penalized pursuant to Chapter 350 for the resulting failures, which resulted in excessive outages and losses being sustained by FPL's customers.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: No. The AG adopts and agrees with the position of the OPC. Additionally, this Commission should not permit recovery of costs resulting from inadequate infrastructure maintenance, nor reward FPL for its failure to adequately plan and prepare for the storm season. FPL's position on this issue is based on negligent or arrogant indifference to known risks, incomplete or inaccurate data, and/or a willingness to allow the consumer to absorb infrastructure maintenance costs through the storm docket.

Staff Analysis: Issue 33 addresses FPL's inspection and maintenance of transmission towers. In the following analysis, all references to FPL's vegetation program pertain to FPL's distribution vegetation management.

PARTIES' ARGUMENTS

FPL asserts its large size should dictate the proper evaluation of FPL's vegetation management program. (FPL BR at 92) Tree density in FPL's service territory is twice the national average and the growing season results in some of the highest tree re-growth rates in the nation. (TR 1398-1399) Vegetation-related outages decreased in 2004 and 2005. (TR 1398) FPL's overall System Average Interruption Duration Index ("SAIDI") compares favorably within the state and ranks in the top quartile nationally. (TR 1399) Focusing on increased vegetation outages in the 1999-2003 period ignores the improvements that occurred in 2004 and 2005 and FPL's SAIDI performance. (TR 815, 1398-1399)

FPL asserts that OPC witness Byerley inappropriately uses a November 2005 hurricane hardening review to conclude that FPL should have implemented a more aggressive vegetation program in years prior to 2005. (FPL BR at 94) The FPL review used by witness Byerley presents various levels of vegetation maintenance activities, estimates of implementation costs and estimates of avoided hurricane costs. (EXH 82, pp. 26-28) FPL argues that Exhibit 82 is not evidence of FPL's vegetation management decisions prior to 2005. (FPL BR at 94)

FPL asserts that OPC witness Byerley misunderstands FPL's use of the term "preventable" in categorizing vegetation-related pole damage. (TR 1400; FPL BR at 95) Witness Williams defined the term "preventable" to mean "that where there was pole damage, it was the opinion of the person that went out there, the forensics engineer, that standard trimming could have prevented the pole damage that actually occurred." (TR 217) FPL must often seek permission from the owners of trees in order to trim them, and that permission is often denied. (TR 1400) Clearly it would be unfair to penalize FPL for damage caused by vegetation that it has been denied permission to trim as implied by the calculations of witness Byerley. (TR 1400)

FPL asserts that another error by witness Byerley was using conductor breakage for Hurricane Katrina to estimate preventable vegetation pole breakages for Hurricane Wilma. (TR 815-816; EXH 82, p. 11) FPL asserts that the appropriate statistic is in the KEMA report. (EXH 15, p. 78; TR 876) Other errors FPL believes to exist in witness Byerley's calculations are addressed in Issue 27. FPL witness Williams, while not agreeing that a disallowance was appropriate or supported, recalculated OPC witness Byerley's methodology using alternative assumptions resulting in an amount of \$10,000. (TR 1396-1397)

FPL believes that any calculated adjustments pursuant to this issue should be netted against the incremental cost of the level of vegetation maintenance that witness Byerley believes should have occurred. (TR 1401-1402; FPL BR at 97)

OPC witness Byerley believes FPL is not entitled to recover costs associated with preventable tree damage because he believes FPL's decisions to fund its vegetation management is based on what is most economical for FPL. (TR 816)

Witness Byerley believes Exhibit 82, pages 26-28, further supports his conclusion that FPL budgets programs based on what is most economical to FPL, because the FPL analysis is based on costs incurred by FPL before and after storms. The FPL analysis shows it is not cost effective to FPL to improve the vegetation management program. (TR 815; EXH 82, pp. 26-28)

He concluded that FPL's vegetation management program may not be adequate based on a review of Commission staff reports and FPL's Annual Distribution Reliability Reports. (TR 804-815) The reports showed decreasing reliability through 2003 with an improvement in 2004. (TR 815) He believes that the apparent improved performance in 2004 could be in part due to adjustments to exclude 2004 hurricane outages. (TR 815)

Thus, witness Byerley believes FPL is not entitled to recover costs associated with preventable tree damage because FPL's decisions are based on what is most cost-effective to FPL. The costs are preventable. (TR 816) OPC witness Byerley recommended an adjustment of \$11,300,000 for inadequacies he believed existed in FPL's vegetation management practices and were preventable. (TR 816) OPC urges the Commission to adopt the \$11,300,000 adjustment recommended by witness Byerley. (OPC BR at 55)

With respect to Issues 27, 28, 30, and 31, FRF argues that penalties pursuant to Chapter 350 should be assessed. In Issues 30 and 31, FRF urges the Commission to assess a \$5,000 per day penalty from January 1, 2006 through October 23, 2006. (FRF BR at 5)

ANALYSIS

Standard of Performance

As presented in Issue 27, FPL carries the burden of proof in this case and must show that the Company has been prudent in each instance where FPL's 2005 charges for storm restoration activities are being challenged.

Concerns Raised

FPL's vegetation related outages steadily increased from 1999 through 2003. (TR 814, 1399) FPL's activities related to improving vegetation management since 2003 are presented in Exhibits 152 and 153, at page 16 in both documents. Exhibits 152 and 153 state that prior to 2004, FPL did not have a systematic program to trim lateral circuits. Trimming of lateral circuits began in 2004 with a 4-5 year plan to ramp up to a three year trim cycle.

Lateral poles comprise approximately 65 percent of FPL's distribution system. (TR 209; EXH 15, p. 58) Therefore, prior to 2003, FPL did not have a vegetation management program to systemically address tree growth issues on approximately 65 percent of its system. Additionally,

in 2004 and 2005, it was not FPL's plan to trim all circuits on the lateral poles within a 3-year cycle but to phase in the 3-year cycle program over 4-5 years. Furthermore, Exhibit 153, page 16, also states joint users typically do not trim trees or remove vines. Thus, FPL has not shown that its vegetation practices were complete or thorough because FPL elected to fund activities at lower levels.

During 2005, FPL developed an estimate of FPL's costs and customer outage benefits associated with the lateral circuit vegetation program. (EXH 82, pp. 37-38) Staff finds it difficult to believe FPL was not capable of performing a similar analysis in years prior to 2005. Furthermore, staff believes this analysis would be one of the various types of analysis that FPL should have performed in its project funding review.

OPC witness Byerley's testimony, taken as a whole, asserts that FPL made decisions based on the costs it incurred rather than the costs to prevent damage to facilities that FPL could have avoided. The damages would be the preventable damages that standard trimming could have prevented during non-hurricane events as well as hurricane events. Thus, FPL's charges to the storm reserve should be adjusted downward because FPL's vegetation management programs resulted in charges to the storm reserve that FPL knew were avoidable. (TR 814-816) Staff agrees.

FPL's Industry Comparative

FPL witness Williams asserts that FPL's vegetation-related outage performance improvements in 2004 and 2005 were achieved despite difficult challenges such as high tree density and high tree re-growth rates. (TR 1398) The high tree density and re-growth rates are with respect to the national average. (TR 1398) Witness Williams does not provide other utility costs pertaining to their respective performance levels. FPL has not shown that the national industry comparison in any way informs the Commission of the level of service expected by FPL's retail customers and the resultant costs.

FPL witness Williams indicated that incremental utility costs, (such as costs due to more aggressive vegetation management) need to be considered to determine the incremental costs associated with a different level of activity. (TR 1402) However, FPL witnesses failed to show that FPL's base rates were not already set to a level sufficient to address any such incremental costs.

Staff concludes that FPL's industry comparative information is inconclusive in showing that FPL was reasonable and prudent in providing the level of service it did prior to and during 2005. The industry comparatives do not show that FPL's base rates were insufficient to address costs to implement vegetation management activities at a higher level than that set by FPL.

FPL's Performance

Vegetation management is an important component of FPL's overall maintenance and reliability program. (Williams TR 137) Every year, reliability programs such as vegetation management have been reviewed and budgeted. (Williams TR 220) An annual renewal indicates FPL found merit in the program.

In 2004, FPL elected to phase in a 3-year cyclical vegetation program for 65 percent of its distribution system. The vegetation-related customer outages declined during 2004 and 2005. Some of the improved performance may be attributable to adjustments for hurricane events. Improved performance may also be attributable to the new lateral circuit vegetation program.

The post-Wilma survey of 1,741 poles by FPL's forensic team reported three pole failures that could have been avoided had FPL cleared the vegetation from the circuits. (EXH 15, pp. 58, 78; EXH 153, p. 9) As discussed in Issue 27, post-storm statistical inferences about damages not specifically studied by forensic review teams are not highly reliable because FPL has not maintained pole specific performance data. Therefore, the exact number of avoidable pole failures due to lack of vegetation management is not certain. Nevertheless, avoidable pole failures occurred and contributed to the overall 2005 hurricane restoration costs.

Estimating the Adjustment

A downward adjustment is warranted because: (1) in 2004 and 2005, FPL was aware of avoidable tree-related customer outages, (2) in 2004 and 2005 FPL limited the roll-out of a program that appear to contribute to decreased tree-related customer outages, (3) FPL has failed to show that its reduction to the level of vegetation management, which was included in its last rate case, was prudent, and (4) FPL has failed to demonstrate that its reduced level of vegetation management did not contribute to higher hurricane restoration costs in 2005.

A downward adjustment is calculated by OPC witness Byerley. His approach builds on the methodology used for pole inspection and maintenance addressed in Issue 27. Staff believes the methodology provided by OPC witness Byerley is a well reasoned regulatory tool that provides a test of the effectiveness of FPL's implemented program. In following this approach, it is understood that this effort is not intended to be a calculation of the exact impact of FPL's long-term vegetation management practices on the storm restoration costs of 2005.

Staff is concerned with adjustments witness Byerley makes for non-FPL-owned assets because they may lead one to an erroneous conclusion that all third-party contracts for services and use of facilities should be removed from all reviews of FPL's overall level of service to customers. Staff notes that FPL has electrical facilities attached to at least 72,283 creosote poles owned by telephone companies. (EXH 81, p. 2) FPL incurs the cost to inspect poles it does not own. (EXH 15, p. 31) FPL has not represented that pole ownership is a factor in the vegetation management programs. Therefore, as a matter of regulatory policy, approval of the adjustment recommend by witness Byerley should not be construed to mean that FPL's obligation to provide reliable service excludes the effects of FPL's contracts and agreements with third-parties.

As discussed in Issue 27, the record supports different factors and weights than those proposed by witness Byerley. However, such efforts may be an exercise in false precision given the uncertainty of FPL's distribution pole specific data and because hurricanes are indiscriminate destroyers. Additionally, post-storm statistical inferences about damages not specifically studied by forensic review teams are not highly reliable because FPL has not maintained pole-specific performance data.

Staff notes that the adjustments in Issue 27 and in this issue do not count the same failed poles twice because the weights used separately identify the various causes of pole failures. (EXH 152, p. 11; EXH 153, p. 11)

For purposes of completeness, the key factors and weights used by witness Byerley to estimate the number of avoidable pole failures that are specifically rebutted by FPL witness Williams is addressed below. All other factors and weights are addressed in Issue 27.

Number of Avoidable Pole Failures

Witness Byerley estimates 888 avoidable pole failures occurred due to Hurricane Wilma. (TR 816) He did not use the value of three pole failures that appears Exhibit 15, page 78, because that “the number seemed pretty unreasonable.” (TR 876) FPL’s preliminary review of Hurricane Wilma data indicated that 24 percent of the broken poles were tree related. (TR 815; EXH 83) Witness Byerley then assumed that at least half the pole failures due to trees were preventable because over 62 percent of the conductor damage was preventable. (TR 816; EXH 82, p. 11) Thus, he estimates 12 percent of the pole failures were due to FPL preventable tree damage. (TR 816) Witness Byerley applies the 12 percent rate to a pole count of 7,400.

Witness Williams believes only three avoidable pole failures occurred which she calculates to be 0.3 percent preventable pole failure rate. (TR 1401) She also believes 21 percent of the broken poles were tree related. (TR 1401) She applies both these factors to an FPL owned pole count of 6,400. Using these steps, staff finds witness Williams’ estimate of tree-preventable pole failures due to Hurricane Wilma is 4. It is notable that FPL’s forensic team made a total of 1,944 observations. (EXH 153, p. 6) However, witness Williams does not explain how the site specific observations translate to system averages. This portion of testimony is of specific concern because, as discussed in Issue 27, FPL did not have pole specific performance data. The absence of data and support for the opinion of witness Williams does not mean she is wrong. However, to agree with her testimony requires substantive factual support that is lacking in the record. Therefore, staff believes the more credible estimate of preventable pole failure rate is provided by witness Byerley.

Staff notes that if witness Byerley’s approximation of an preventable pole failure rate of 12 percent is reasonable then as many as 1,368 avoidable poles failures may have occurred. $(11,400 \times 0.12 = 1,368)$ Staff’s purpose in using a pole count of 11,400 is an effort to recognize that FPL’s obligation to provide service includes all reliability consequences associated with using third-party poles consistent with staff’s analysis in Issue 27. Staff’s recommended adjustments in Issue 27 are incorporated into Table 28-1 below.

Table of Adjustments

A summary of the differences between the calculations of witnesses Byerley, Williams and staff’s recommendation is provided in Table 28-1. Staff recommends using OPC witness DeRonne’s 25 percent capital offset assumption to estimate the respective rate base and expense amounts of the adjustment. (EXH 85)

TABLE 28-1
 Calculation of the Vegetation Adjustment

	OPC Witness <u>Byerley</u>	FPL Witness <u>Williams</u>	<u>Staff</u>
Number of Poles Failures	7,400	6,500	11,400
Percent due to Trees	24	21	24
Percent Avoidable	50	0.3	50
\$/pole Replaced	\$1,700	\$2,000	\$2,000
Escalation due to all price increases during storm restoration	4	1	1
Pole Replacement Cost	\$6,038,400	\$8,000	\$2,736,000
Conductor Cost per replaced Pole Cost	0.88	0.10	0.26
Total Adjustment (Rounded)	\$11,400,000	\$10,000	\$3,400,000
25 % Capital Offset Amount	\$ 2,850,000	\$ 2,200	\$ 850,000
Expense Amount	\$ 8,550,000	\$ 6,600	\$ 2,550,000

Penalties

The imposition of fines and comparable penalties pursuant to Chapter 350, or Section 366.095, Florida Statutes, is limited to instances where a utility refuses to comply or willfully violates any rule, order, or statute administrated by the Commission. In this case and issue, no one has identified a rule, order or statute administrated by the Commission that FPL failed to implement or comply with. Therefore, no fines are recommended.

CONCLUSION

A downward adjustment of \$3,400,000 is warranted because: (1) in 2004 and 2005, FPL was aware of avoidable tree-related customer outages, (2) in 2004 and 2005 FPL limited the roll-out of a program that contributes to decreased tree-related customer outages, (3) FPL has failed to show that its reduction to the level of vegetation management, which was included in its last rate case, was prudent, and (4) FPL has failed to demonstrate that its reduced level of vegetation management did not contribute to higher hurricane restoration costs in 2005. The recommended capital offset adjustment amount is \$850,000 and the recommended expense adjustment amount is \$2,550,000. No other fines or penalties are recommended because there is no evidence that FPL refused to comply with or willfully violate any lawful rule or order of the Commission, or any statute administered by the Commission.

Issue 29: WITHDRAWN

Issue 30: Did FPL adequately inspect and maintain its distribution and transmission system for deterioration and overloading of poles prior to October 23, 2005? If not, what amount, if any, should be adjusted from the costs that FPL proposes to charge to the storm reserve and recover through securitization or a surcharge?

Recommendation: This issue is duplicative of Issue 27. No one identified a rule, order or statute administrated by the Commission and specific to inspection and maintenance of distribution and transmission poles that FPL failed to implement or comply with for the period January 1, 2005 through October 23, 2005. Hence, no fines or penalties are recommended. (Breman)

Position of the Parties

FPL: This issue is essentially identical to Issue 27. FPL's position from Issue 27 applies here equally. There is no basis for penalizing FPL under Chapter 350, as the FRF has proposed.

OPC: Please see Citizens' position and argument on issue 27.

FIPUG: Adopts the position of OPC.

FRF: No. FPL's inspection activities with respect to the deterioration of wood distribution poles were inadequate. Agree with OPC as to amounts of claimed repair costs that should be disallowed. Additionally, FPL should be penalized pursuant to Chapter 350 for the resulting failures, which in turn resulted in excessive outages and losses being sustained by FPL's customers. The date through which such penalties should be imposed is the day before Wilma struck South Florida, October 23, 2005.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: No. The AG adopts and agrees with the position of the OPC. Additionally, this Commission should not permit recovery of costs resulting from inadequate infrastructure maintenance, nor reward FPL for its failure to adequately plan and prepare for the storm season. FPL's position on this issue is based on negligent or arrogant indifference to known risks, incomplete or inaccurate data, and/or a willingness to allow the consumer to absorb infrastructure maintenance costs through the storm docket.

Staff Analysis: This issue was raised by FRF. The only difference in scope between Issues 27 and 30 is the potential for assessment of penalties through October 23, 2005, pursuant to Chapter 350, or, more appropriately, Section 366.095, Florida Statutes. All other matters are already addressed in Issue 27.

In its brief, FRF argues that penalties pursuant to Chapter 350 should be assessed. A \$5,000 per day penalty from January 1, 2006 through October 23, 2006 is suggested. FRF also suggests the Commission could begin assessing penalties as early as 2002 when FPL began cutting its pole inspection program. (FRF BR at 5)

The imposition of fines and comparable penalties pursuant to Chapter 350, or, Section 366.095, Florida Statutes, is limited to instances where a utility refuses to comply or willfully violates any rule, order, or statute administrated by the Commission. No one identified a rule, order or statute administrated by the Commission and specific to inspection and maintenance of distribution and transmission poles that FPL failed to implement or comply with for the period January 1, 2005 through October 23, 2005. Therefore, no fines or penalties are recommended.

Issue 31: Did FPL adequately control vegetation around its distribution and transmission system prior to October 23, 2005? If not, what amount, if any, should be adjusted from the costs that FPL proposes to charge to the storm reserve and recover through securitization or a surcharge?

Recommendation: This issue is duplicative of Issue 28. No one identified a rule, order or statute administrated by the Commission and specific to vegetation around distribution and transmission facilities that FPL failed to implement or comply with for the period January 1, 2005 through October 23, 2005. Therefore, no fines or penalties are recommended. (Breman)

Position of the Parties

FPL: This issue is essentially identical to Issue 28. FPL's position from Issue 28 applies here equally. There is no basis for penalizing FPL under Chapter 350, as the FRF has proposed.

OPC: Please see Citizens' position and argument on issue 28.

FIPUG: Adopts the position of OPC.

FRF: No. FPL's pre-storm vegetation management activities were inadequate. Agree with OPC as to amounts of claimed repair costs that should be disallowed. Additionally, because FPL's activities were inadequate due to FPL's intentional cost-cutting efforts, they were imprudent and FPL should be penalized pursuant to Chapter 350 for the resulting failures. The date through which such penalties should be imposed is the day before Wilma struck South Florida, October 23, 2005.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: No. The AG adopts and agrees with the position of the OPC. Additionally, this Commission should not permit recovery of costs resulting from inadequate infrastructure maintenance, nor reward FPL for its failure to adequately plan and prepare for the storm season. FPL's position on this issue is based on negligent or arrogant indifference to known risks, incomplete or inaccurate data, and/or a willingness to allow the consumer to absorb infrastructure maintenance costs through the storm docket.

Staff Analysis: This issue was raised by FRF. The only difference in scope between Issues 28 and 31 is the potential for assessment of penalties through October 23, 2005, pursuant to Chapter 350, or Section 366.095, Florida Statutes. All other matters are addressed in Issue 28.

In its brief, FRF argues that penalties pursuant to Chapter 350 should be assessed. A \$5,000 per day penalty from January 1, 2006 through October 23, 2006 is suggested. FRF also suggests the Commission could begin assessing penalties as early as 2002 when FPL began cutting its pole inspection program. (FRF BR at 5) It appears that FRF associates vegetation management with pole inspections.

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The imposition of fines and comparable penalties pursuant to Chapter 350, or Section 366.095, Florida Statutes, is limited to instances where a utility refuses to comply or willfully violates any rule, order, or statute administrated by the Commission. No one identified a rule, order or statute administrated by the Commission and specific to inspection and maintenance of distribution and transmission poles or vegetation management that FPL failed to implement or comply with for the period January 1, 2005 through October 23, 2005. Therefore, no fines or penalties are recommended.

Issue 32: WITHDRAWN

Issue 33: What adjustment, if any, should the Commission make associated with the failure of 30 transmission towers of the 500 KV Conservation-Corbett transmission line and the failure of six structures on the Alva-Corbett 230 transmission line?

Recommendation: The resolution of this issue does not impact the ultimate decision in this case because rate base allocations are removed from the storm restoration charges. Staff recommends an adjustment of \$12,000,000 to rate base because: (1) in 1998 FPL knew that a bolt problem existed, (2) FPL's 1998 analysis called for a revised construction standard for tower bolts, and (3) FPL failed to implement the revised construction standard prior to the 2005 hurricane events. The \$12,000,000 adjustment includes an estimate of \$11,900,000 for storm restoration costs of the Conservation-Corbett 500 KV transmission line and \$100,000 for storm restorations costs for the Alva-Corbett 230 KV transmission line. (Breman)

Position of the Parties

FPL: None. FPL's actions in building, inspecting and maintaining Conservation-Corbett were reasonable based upon available information. FPL reasonably concluded that the loose and missing bolts discovered in 1998 were caused by excessive conductor vibration and that reducing the vibration eliminated the cause of the bolt loosening. From 1999 to 2003, FPL conducted several detailed inspections, which confirmed FPL's expectation that this issue had been resolved. Essentially all damage to Alva-Corbett transmission structures was the direct result of Conservation-Corbett structures collapsing.

OPC: FPL's pre-storm maintenance was inadequate. Cross-brace bolts, critical to structural integrity, were loose or missing on 31 towers in 1998. Given the risks known then, FPL shouldn't have "assumed" that measures to reduce conductor vibration would prevent future loose bolt problems. FPL should have secured the nuts on all cross-brace bolts, and documented the 1998 discovery adequately. FPL did neither, even when it discovered another bolt missing in 2002. FPL must bear full responsibility for \$10.4 million of restoration costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC that \$10,411,000 should be removed from both the total projected storm restoration costs and from the capital cost offset, and that the Commission's final order in this case should state that these costs are being disallowed and should not be included in plant in service.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: The AG adopts and agrees with the position of the OPC. Additionally, this Commission should not permit recovery of costs resulting from inadequate infrastructure maintenance, nor reward FPL for its failure to adequately plan and prepare for the storm season. FPL's position on this issue is based on negligent or arrogant indifference to known risks, incomplete or inaccurate data, and/or a willingness to allow the consumer to absorb infrastructure maintenance costs through the storm docket.

Staff Analysis: The resolution of this issue does not impact the ultimate decision in this case because rate base allocations are removed from the storm restoration charges.

PARTIES' ARGUMENTS

FPL asserts that its transmission lines are designed in accordance with the requirements of the NESC. (TR 257, 1317; EXH 15, p. 45) FPL has a maintenance program consisting of climbing inspections, visual inspections, and special assessments. (EXH 15, p. 39) FPL argues that by designing its transmission lines to NESC extreme wind requirements and performing regular maintenance on those lines, FPL believes it has ensured that the transmission system is extremely resilient in hurricane conditions. (FPL BR at 99) FPL maintains it achieved good performance in light of Hurricane Wilma's strong winds and that only 100 transmission structure failures out of a total of 64,000 in FPL's system. (FPL BR at 99; TR 1330)

KEMA, in its post-Hurricane Wilma review of the Conservation-Corbett transmission line failure, raised questions about FPL's inspection practices and reliance on manual tightening of cross-brace bolts. (EXH 15, pp. 38, 41, 43) The inspection practice called into question was FPL's reliance on a climbing inspection of 10 percent of the towers every four years. (EXH 15, p. 44) FPL witness Brown testified that after learning of additional FPL inspection activities he revised his opinion of how FPL responded to the serious situation. (TR 274)

KEMA's concern with respect to the manual tightening practice was two-fold. First, KEMA noted that manually tightening the bolts on such large structures would be difficult. Secondly, any movement in the structure would cause the bolts to loosen. (EXH 15, p. 43) FPL witness Brown of KEMA testified that manual tightening is an industry standard and appropriate for this application. (TR 266, 270) Witness Brown also testified that for at least 20 or 25 years, the industry standard has been to allow weathering steel to secure the nut once it is fastened. (TR 267) Thus, FPL appears to be implementing accepted industry practices. Nevertheless, the focus in this case has been on why FPL did not do more when it discovered that bolts were missing and loose on its transmission line.

Loose or missing bolts were detected in 1998 as a result of an outage investigation and follow-up inspections. (TR 1320; EXH 15, p. 43) During these inspections, FPL observed excessive vibration on the conductors. The root cause of the loose/missing bolts was determined to be excessive conductor vibration. (TR 1320; EXH 15, p. 42) The conductor vibration causing the bolts to loosen was due to five to fifteen miles per hour winds and not tropical force winds. (TR 1372) The loose and missing bolts discovered in 1998 were caused by conductor vibration before the weathering steel patina could secure the bolts and nuts together. (TR 1320) FPL's use

of this locking mechanism on more than 1,000 miles of 500 KV structures has proven to be effective, even under hurricane conditions. Since 1978, FPL installed 98 percent of its 3,100 weathering steel structures without lock-nuts. (TR 1339) FPL has no history of loose or missing bolts on any other structure than the Conservation-Corbett 500 KV line. (TR 1320)

In 1998, FPL added vibration dampers to reduce the conductor vibration of the Conservation-Corbett transmission line to within industry standard limits. After a follow-up conductor condition analysis, FPL installed additional vibration damping upgrades on the entire line in 1999. (TR 1322, 1363) FPL increased the frequency of inspection after the repairs. Helicopter inspections for evidence of a continuing vibration were performed in 2001 and 2003. A Thermovision inspection in 2003 also included assessing the visual condition of the structures. These inspections occurred in addition to the climbing inspection on 10 percent of the structures in 2002 and routine ground patrols. (TR 1325-1326, 1363) One missing bolt was found in 2002, during a ground patrol, as a result of all these inspections. No specific cause was identified. Witness Jaindl believes FPL reasonably concluded that the single missing bolt was an anomaly. (TR 1326)

Witness Jaindl explains that FPL was responsive to the bolt problem in 1998 because less than half of the loose and missing bolts recorded in 2005 were the same locations as the ones recorded in 1998. (TR 1323) Also, subsequent to Hurricane Wilma, FPL continues to evaluate the Conservation-Corbett transmission line but has not yet found a definitive cause for the loose and missing bolts. (TR 1326)

Prior to June 1, 2006 FPL believes it will have completed peening bolt threads and tightening all cross brace bolts and cross arm bolts to provide additional locking security beyond the natural patina. (TR 1327) Peening bolt threads is not the most desirable method of securing nuts because the nuts cannot be subsequently removed without destroying the bolt. (TR 796; FPL BR at 105) In 1998/99, one of FPL's actions was to leave the bolt alone if the nut was frozen. In hindsight, this was not adequate. (TR 1322-1323) FPL believes criticism is being made only with the benefit of 20/20 hindsight and no adjustments are supported by the record. (FPL BR at 103, 105)

Damage to a section of the Alva-Corbett transmission line occurred when the adjacent Conservation-Corbett transmission line collapsed on top of it. (EXH 15, p. 41) The Alva-Corbett transmission line was an "innocent bystander" damaged by the collapse of the Conservation-Corbett line.

FPL asserts that it responded reasonably to the loose/missing bolt issue discovered on the Conservation-Corbett transmission line in 1998. FPL argues there is no basis to find FPL imprudent or otherwise justify an adjustment to FPL's recovery of the costs associated with its repair of the Conservation-Corbett and Alva-Corbett transmission lines. (FPL BR at 106)

The interveners argue that the costs incurred to repair the Conservation-Corbett line and Alva-Corbett line should not be considered storm restoration costs and should be disallowed from recovery through base rates because: (1) in 1998 FPL knew that a bolt problem existed, (2) in 1998 FPL's analysis called for a revised construction standard for tower bolts, and (3) FPL failed to implement the revised construction standard prior to the 2005 hurricane events. They

also argue that Hurricane Wilma was not sufficiently strong to cause wind loads exceeding the design criteria of FPL's transmission towers.

Witness Williams testified that the NESC extreme wind criteria are approximately equal to hurricane Category 3 wind gusts for coastal areas in southeast, south, and southwest Florida. (TR 1414) FPL witness Brown testified that FPL designs its tower to specifically address extreme wind loading. (TR 262, 1296; EXH 15, pp. 9, 12, 37) Secured cross braces are necessary to withstand extreme wind loads. (TR 1354) FRF argues that the maximum gust wind speeds during Hurricane Wilma were within the range of a Category 1 hurricane throughout FPL's service area. (FRF BR at 20; EXH 143) The implication is that FPL's Conservation-Corbett transmission line was not compliant with the NESC extreme wind criteria because there is no record of extreme wind speeds exceeding the applicable edition of the NESC. OPC witness Byerley opined that wind load due to Hurricane Wilma was less than the applicable extreme wind load requirements for facilities built prior to 2002. (TR 790) Thus, he concludes that equipment failure due to inadequate inspection and maintenance practices resulted in the failure of the transmission line. (TR 790)

FPL's 1998 Analysis Techniques of the 500 KV fastener problem states "Revise specification for construction of overhead transmission lines. Require brace, arm and OHGW mast bolts to have peened threads after nut is tightened." (EXH 71, p. 24) FPL witness Jaindl admitted that FPL staff was aware of the 1998 revised bolt specification. (TR 1323)

There is no record that details the exact actions FPL took in 1998 and 1999 to address the bolt problem. (EXH 15, p. 43) However, FPL witness Jaindl agreed with OPC witness Byerley that FPL did not follow the revised bolt specification in 1998 and 1999. (TR 796, 1323) The testimony of OPC witness Byerley relies in part on a November 14, 2005, memorandum of C. J. Wong which presents FPL's investigation of the Conservation-Corbett 500 KV line failure. (EXH 70). FPL's report on the transmission line failure states "there is no evidence that the loosened boles were retightened during the retrofit construction." (EXH 70, p. 9)

The interveners collectively argue that FPL did not implement reasonable measures to address the loose/missing bolt problem on the failed 500 KV transmission line prior to 2005 because FPL failed to observe its own 1998 assessment and recommendation.

ANALYSIS

Standard of Performance

Staff believes that a finding of prudence should be based on what FPL knew, or reasonably should have known, at the time FPL implemented its 1998/99 repairs to the Conservation-Corbett 500 KV transmission line. Additionally, any additional remedial actions that FPL took prior to the 2005 transmission line to address the bolt problem should be considered.

FPL's 1998 Response to the Loose Bolt Problem

The discovery of missing and loose bolts was made as a result of FPL's response to an outage event on the transmission line and an insulator failure in 1998. (TR 1320, 1322, 1335;

EXH 15, p. 43; EXH 71, p. 2) FPL witness Jaindl asserts that FPL concluded that the outage and bolt problem were both due to excessive conductor vibration. (TR 1320) The conductor vibration program was addressed in 1998/99. (TR 1294, 1320, 1335) Subsequent inspections showed no further evidence of conductor vibration or ongoing bolt problems. (TR 1325, 1335) Witness Jaindl explains that FPL was responsive to the bolt problem in 1998, because less than half of the loose and missing bolts recorded in 2005 were the same locations as the ones recorded in 1998. (TR 1323) The bolts are assumed to have come loose or fallen off within the first months of service because of conductor vibration. This assumption is based on the amount of time required for weathering steel patina to sufficiently develop and lock the nuts in place. (TR 1320, 1374)

FPL's witnesses Brown and Jaindl were not aware of any utility that had experienced bolts coming loose on transmission towers. (TR 1307, 1360) FPL had no history of bolts coming loose on any of its other transmission towers. (TR 1339, 1360) The implication is that FPL had no basis to be concerned with bolts coming loose on its transmission towers prior to 1998. Staff agrees.

However, the specific actions FPL took regarding loose and missing bolts are not known. (EXH 15, p. 43) Witness Byerley references FPL's Conservation-Corbett line failure analysis and noted that FPL's structural engineer reported there was no evidence that the loosened bolts were retightened during retrofit construction. (TR 794; EXH 70, p. 9)

Staff concludes that FPL's response in the bolt problem in 1998 resulted in some of the loose bolts not being retightened, other loose bolts being replaced, and replacement of the missing bolts. FPL did not peen any of the bolts in its 1998/99 response to the bolt problem.

FPL's 1998 Analytical Techniques

The only documentation of FPL's 1998 review of the bolt problem is FPL's "1998 Analytical Techniques", Exhibit 71. OPC witness Byerley believes FPL did not properly address the bolt problem because FPL did not implement the revised standard of peening the tower bolts. (TR 796, 818; EXH 71, p. 24)

Witness Jaindl believes FPL took reasonable actions to address the conductor vibration problems. (TR 1322-1323) She further believes that resolving conductor vibration problems was expected to also resolve the bolt problem because the loosening of the bolts was associated with conductor vibration. (TR 1320) One could argue that there would be no need to peen bolts if the bolt problem was, in fact, due to the conductor vibration problem. Witness Jaindl could not confirm whether FPL knew that the bolt problem was fully addressed in 1998/99 because FPL did not assume the conductor vibration was fully addressed until 2003. (TR 1325)

FPL witness Jaindl admitted that FPL did not follow the revised bolt specification in 1998 and 1999. (TR 796, 1323) She specifically references Exhibit 71, page 8, which states: "try to tighten with wrench - if nut is frozen, then leave as is." In hindsight, she now believes this criterion was not adequate. (TR 1323) If her testimony has weight with respect to FPL's efforts to tighten bolts in 1998, then her testimony should be supported with forensic evidence that FPL did take steps to re-tighten bolts. Yet the extent of FPL's efforts to tighten loose bolts is

questionable, because FPL's review of the transmission line failure reports no evidence that bolt retightening occurred. (EXH 70, p. 9)

Staff concludes that FPL did not follow its own recommendation to revise the bolt tightening standard, and that FPL has no record of retightening the 1998 loose bolts. FPL's 1998 Analytical Techniques contains no statement that revision of the construction standard should not occur if the conductor vibration problem is resolved. FPL's revised bolt fastening standard was not conditioned on failure of achieving reduced conductor vibration. Rather, staff believes that the remedy of the bolt problem was contemporaneous with the remedy of the conductor vibration problem. To do otherwise would unnecessarily compromise or risk reliable transmission tower performance.

FPL's Response To Missing and Loose Bolts After 1998

FPL increased the frequency of inspections after the 1998/99 repairs. Helicopter inspections were performed in 2001 and 2003. A Thermovision inspection in 2003 included visual checks of the structures. Additionally, a climbing inspection and ground patrol occurred in 2002. (TR 1325-1326, 1363) One missing bolt was found in 2002 as a result of all these inspections. No specific cause was identified. There was no evidence of excessive conductor vibration. Witness Jaindl believes FPL reasonably concluded that the single missing bolt was an anomaly. (TR 1326) FPL's testimony represents that specific inspection for ongoing missing bolts essentially stopped after 2003. Consequently, it is not known whether additional bolt loosening events occurred subsequent to 2003 and prior to the 2005 storms. (TR 337)

Missing or loose bolts were uncharacteristic events for FPL's other transmission lines. (TR 1320) FPL's 1998 analysis supported a revision to the bolt tightening standard that had not been implemented by 2002. Staff is concerned by the lack of FPL testimony and documentation regarding the one additional bolt, because such an event should have called into question FPL's decision not to implement a revised bolt tightening standard for the Conservation-Corbett transmission line. There is no record indicating the extent of FPL's 2002 review.

Finding of Prudence

The only record evidence that FPL may have been prudent with respect the bolt problem prior to the failures that occurred in 2005 is the testimony of FPL witness Jaindl. (TR 1316-1327) To conclude that FPL was prudent based on the testimony of witness Jaindl requires one to conclude that FPL was prudent in 1998, when it ignored FPL's 1998 Analytical Techniques that recommended a revised bolt tightening standard.

Staff is not persuaded by the testimony of witness Jaindl because FPL's 1998 Analytical Technique does not provide for options such as the actions supported by witness Jaindl. (TR 1316-1327) Also, FPL's 2005 review of the failed Conservation-Corbett transmission line found no evidence that bolt retightening occurred as suggested by witness Jaindl. (TR 1322)

Staff recommends an adjustment of \$12,000,000 to rate base because: (1) in 1998 FPL knew that a bolt problem existed, (2) FPL's 1998 analysis called for a revised construction standard for tower bolts, and (3) FPL failed to implement the revised construction standard prior to the 2005 hurricane events.

The \$12,000,000 adjustment includes an estimate of \$11,900,000 for storm restoration costs of the Conservation-Corbett 500 KV transmission line, and \$100,000 for storm restoration costs for the Alva-Corbett 230 KV transmission line. (EXH 4, p. 239)

CONCLUSION

Staff recommends an adjustment of \$12,000,000 to rate base because: (1) in 1998 FPL knew that a bolt problem existed, (2) FPL's 1998 analysis called for a revised construction standard for tower bolts, and (3) FPL failed to implement the revised construction standard prior to the 2005 hurricane events. The \$12,000,000 adjustment includes an estimate of \$11,900,000 for storm restoration costs of the Conservation-Corbett 500 KV transmission line and \$100,000 for storm restoration costs for the Alva-Corbett 230 KV transmission line.

Issue 34: Should FPL be authorized to accrue and collect interest on the amount of 2005 storm-related costs permitted to be recovered from customers? If so, how should it be calculated?

Recommendation: FPL should be allowed to charge interest at the applicable 30-day commercial paper rate on the balance of storm damage restoration costs permitted to be recovered from ratepayers. To the extent FPL has already accrued interest on a balance of storm damage restoration costs that has not been deemed to be reasonable and prudently incurred, the incremental interest should be netted against the amount approved for recovery. Based on the staff's recommendations in the prior issues, the interest should be reduced by \$1,365,500 (jurisdictional). (Springer, Lowe, Slemkewicz)

Position of the Parties

FPL: Yes. Section 366.8260(1)(n) expressly provides that “[s]torm-recovery costs shall include the costs to finance any deficiency or deficiencies in storm-recovery reserves until such time as storm-recovery bonds are issued....” The jurisdictional amount of un-recovered pre-tax 2005 storm-recovery costs proposed by FPL includes monthly interest at a commercial paper rate, consistent with the method approved by the Commission in the 2004 Storm Cost Recovery Order, Order No. PSC-05-0937-FOF-EI.

OPC: FPL should accrue and collect interest on the actual costs incurred as adjusted by the Commission. Interest should not be accrued on any estimated amounts. The accrual of interest should begin in November, 2005 and cease when the first bonds are issued at the pre-tax commercial paper rate.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC that FPL should only be allowed to accrue and collect interest on the actual amount of reasonable and prudent storm costs, net of any penalties or other adjustments, as determined by the Commission in this proceeding, and that interest accrual should begin in November 2005 and cease as of the time that the first bonds are issued (assuming securitization).

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES’ ARGUMENTS

FPL proposes to accrue and collect interest at a commercial paper rate on the amount of 2005 storm-related costs. All other parties agree with OPC that FPL should be allowed to accrue and collect interest beginning in November 2005 on only actual costs incurred and adjusted by the Commission, and cease upon the issuance of the bonds. (OPC BR at 67)

ANALYSIS

FPL estimated an \$11.5 million interest amount accrued on unrecovered 2005 storm recovery costs through July 31, 2006 as determined by Section 366.28260(1)(n), Florida Statutes. (Davis TR 448) FPL proposes the calculation of interest charges on the 2004 and 2005 storm costs by multiplying the average monthly unrecovered balance by the current estimated after-tax commercial paper rate. (Davis TR 429) This treatment is consistent with the calculation of the existing storm restoration surcharge by the 2004 Storm Cost Recovery Order. (Davis TR 429; FPL BR at 106) All parties agree that FPL should be authorized to accrue and collect interest on the amount of 2005 storm related costs. (FPL BR at 106; FRF at BR at 64; OPC BR at 67) However, OPC proposes that the interest be applied to only actual amounts less adjustments made by the Commission, and accrual of interest should begin in November 2005 and cease when the first bonds are issued at the pre-tax commercial paper rate. (FRF BR at 64; OPC BR at 67)

CONCLUSION

Staff recommends that FPL should be allowed to charge interest at the applicable 30-day commercial paper rate on the balance of storm damage restoration costs permitted to be recovered from ratepayers. However, staff recommends that any adjustments to the total by the Commission, less the incremental interest, should be netted against the amount approved for recovery.

Based on the staff's recommendation to reduce the 2005 storm costs by \$96,976,828 (\$97,053,500 system), the related interest should be reduced by \$1,365,500 (jurisdictional). This amount was calculated as follows:

Total Staff Jurisdictional Adjustments	\$96,976,828
Net 2005 Jurisdictional Storm Recovery Costs per Exhibit 20	<u>\$815,372,000</u>
Ratio	11.894%
2005 Jurisdictional Interest per Exhibit 20	<u>\$11,481,000</u>
2005 Jurisdictional Interest Adjustment	<u>\$(1,365,500)</u>
Allowable 2005 Jurisdictional Interest ($\$11,481,000 - \$1,365,500$)	<u>\$10,115,500</u>

Issue 35: Should the Commission require FPL's storm recovery costs for 2005 be shared between FPL's retail customers and FPL and, if so, to what extent?

Recommendation: Yes, FPL shareholders should share in the adverse effects of the 2005 hurricane season and they will by virtue of the various adjustments made in earlier issues to this recommendation, to the extent they have an adverse effect on FPL's return on equity. The following table depicts the adverse impacts to be borne by FPL's shareholders:

Issue Number	Description	Amount in millions
15	Uncollectibles	\$3.6
17a	Revenues not earned due to storm outages	51.4
17b	Backfill Work	.8
17c	Catch-up Work	7.8
17h	Vacation buy back	1.2
27	Pole Adjustment	5.9
28	Vegetation Management Adjustment	3.4
33	Corbett Transmission Line	12.0
	Total	\$86.1

(Devlin, Keating)

Position of the Parties

FPL: No. FPL is regulated on a cost-of-service basis. Such costs are a part of the costs to provide electric service and are not recovered in base rates. Accordingly, all such costs should be recovered in this proceeding. Requiring FPL to bear a portion of reasonable and prudently-incurred costs would be inconsistent with Florida regulatory law and policy and would require the Commission to unwind the 2005 Stipulation and 2005 Settlement Agreement.

OPC: No position.

FIPUG: FIPUG generally supports reasonable risk/reward sharing between utilities and their customers. In the as-of-yet undocketed storm damage rule review, FIPUG argued that the Commission should adopt a sharing approach. Nevertheless, FIPUG is bound by the settlement agreement in FPL's last base rate case (Docket 050045-EI), where the parties agreed that for the period of the agreement FPL

“will be permitted to recover prudently incurred costs associated with events covered by Account No. 228.1 [the storm damage account]. . . .”

FRF: Understanding this issue to address the possible sharing of costs that are determined by the Commission to be reasonable and prudent costs, the FRF's position is "No position."

AARP: Same position as FIPUG.

FEA: Agree with FIPUG.

AG: Yes. FPL has no inherent right to foist upon the backs of Florida's consumers the full cost of storm recovery. Sound regulatory policy must take into account current circumstances and adapt to a changing environment. This Commission must consider the impact on the consumer of an unprecedented series of hurricanes and embrace unprecedented solutions like sharing. Sharing is not inconsistent with nor prohibited by the Settlement Agreement. Even if it were, the Commission is not bound by the Agreement.

Staff Analysis:

PARTIES' ARGUMENTS

Staff witness Jenkins proffered sharing of storm restoration costs between shareholders and consumers. Sharing was often requested by consumers at the service hearings in this docket. Witness Jenkins noted in his testimony that sharing has been used in other situations such as the sharing of wholesale revenue, and pursuant to statute and the sharing of economic development costs. (TR 1254)

Witness Jenkins believes that sharing is appropriate in this case because of the significant financial hardship placed on consumers in recent months due to the sharp increase in fuel costs and additional storm related costs being addressed in this case. Witness Jenkins notes that rates for FPL's consumers have increased by 56 percent since 2000 and 19 percent since 2005. (TR 1253)

Witness Jenkins asserts that sharing contravenes the rate case settlement in Docket No. 050045-EI but points out that the Commission was not a signatory to that settlement. (TR 1255) Witness Jenkins notes that the settlement states that FPL will be permitted to recover prudently incurred costs but fails to explicitly state that this means "all" prudent costs. (TR 1272)

As FPL pointed out with its cross examination, a Commission decision that is inconsistent with the settlement is unprecedented. (TR 1273) The Commission has, in recent times, promoted the use of settlements. (TR 1277) FPL witness Dewhurst states that adoption of the sharing method would contravene longstanding regulatory policy, increase investors' perception of risk, and therefore cost of capital, and have a chilling effect on possible future settlements. (TR 1662) FPL also pointed out in its cross examination that the rate case settlement incorporates a form of sharing. This involves revenue sharing. (TR 1266-1269)

FPL Witness Dewhurst goes on to say that sharing is bad public policy in that it would deny FPL the opportunity to recover prudently incurred costs. (TR 1665) Witness Dewhurst opines that sharing may result in over-investing in infrastructure to the detriment of ratepayers. (TR 1669) He also testified that the Commission clearly rejected sharing in FPL's 2004 storm docket and to change now is punitive and unfair to FPL. (TR 1670) Finally, witness Dewhurst notes that the Commission has a long history of encouraging and honoring settlements. (TR 1675)

The AG does not believe that sharing contradicts the rate case settlement. The AG points out that there is no express prohibition against sharing mentioned in the settlement. It should be noted that the AG, but not Staff witness Jenkins, was part of settlement discussions and is in a better position to opine whether sharing contradicts the settlement. (TR 1258) However, this also holds true for the other parties to the docket.

On cross-examination from the AG, witness Dewhurst acknowledged that sharing would not harm ratepayers since the increased associated risk and concomitant cost of capital roughly offsets the lower amount of costs paid by consumers. (TR 1737) Witness Dewhurst conceded under the AG's cross examination that FPL would attempt to continue to provide safe and rapid restoration of power in the wake of storms irrespective of sharing (TR 1740) and therefore, it is questionable whether sharing creates a disincentive to provide quality service. Also, witness Dewhurst admitted on cross-examination that the rate settlement does not explicitly prohibit sharing and does not speak to "total" prudently incurred costs. (TR 1751) Witness Dewhurst believed specific mention of sharing in the rate case settlement was not necessary and, by virtue of other provisions in the settlement (recovery of prudently incurred costs), sharing is prohibited.

ANALYSIS

At paragraph 10, the stipulation and settlement approved in the FPL 2005 Rate Case Settlement Order addresses the recovery of storm costs. That paragraph states in full:

10. No Party to this Stipulation and Settlement shall appeal the FPSC's Final Order in Docket No. 041291-EI. Further, Parties agree to the following provisions relative to the target level and funding of Account No. 228.1 [the Reserve] and recovery of any deficits in such Account:

- a. The target level for Account No. 228.1 shall be as established by the Commission, whether on its own motion, upon petition by FPL, or in conjunction with a proceeding held in accordance with Section 366.8260, Florida Statutes. FPL will be permitted to recover prudently incurred costs associated with events covered by Account No. 228.1 and replenish Account No. 228.1 to a target level through charges to customers, that are approved by the Commission, that are independent of and incremental to base rates and without application of any form of earnings test or measure. The fact that insufficient funds have been accumulated in Account No. 228.1 to cover costs associated with events covered by that Account shall not be evidence of imprudence or the basis of a disallowance. Replenishment of Account No. 228.1 to a target level approved by the Commission and/or recovery of any costs incurred in excess of funds accumulated in Account No. 228.1 and

insurance shall be accomplished through Section 366.8260, Florida Statutes, and/or through a separate surcharge that is independent of and incremental to retail base rates, as approved by the Commission. Parties to this Stipulation and Settlement are not precluded from participating in such a proceeding, nor precluded from challenging the amount of such target level or whether recovery should be accomplished either through Section 366.8260, Florida Statutes, or through a separate surcharge.

- b. The current base rate accrual to Account No. 228.1 of \$20.3 million is suspended effective January 1, 2006.
- c. No revenues contemplated by this Section 10 shall be included in the computation of retail base rate revenues for purposes of revenue sharing under this Stipulation and Settlement.

2005 Rate Case Order, pp. 16-17.

In this case, Staff witness Jenkins has proposed that FPL not be permitted to recover up to 20 percent of its prudently incurred 2005 storm-recovery costs from customers. FPL and the AG differ with regard to whether the sharing concept proposed by witness Jenkins is consistent with the stipulation and settlement. FPL contends that the settlement reflects an agreement that 100 percent of FPL's prudently incurred storm costs would be recovered through a surcharge and/or securitization without the application of any form of earnings test or measure. Thus, FPL argues, witness Jenkins' sharing proposal is not consistent with the settlement. The AG notes that the settlement contains no reference to a prohibition on sharing storm costs and argues, therefore, that witness Jenkins' sharing proposal is not inconsistent with the settlement.

The language used in a contract or agreement is the best possible evidence of the intent and meaning of the contracting parties and is controlling regardless of the intention existing in the minds of the parties.⁶ It is necessary to read a contract's provisions harmoniously in order to give effect to all portions of the contract without negating some of its provisions.⁷ Further, no term or word of an agreement should be treated as surplusage if any meaning reasonable and consistent with other parts can be given to it.⁸ For the reasons set forth below, staff believes that FPL's position is supported by the plain language of the settlement and that the AG's construction inappropriately treats a term of the contract as surplusage.

As noted above, paragraph 10 of the settlement provides that "FPL will be permitted to recover prudently incurred costs associated with events covered by Account No. 228.1 . . . without application of any form of earnings test or measure." Paragraph 10 goes on to state that "recovery of *any* costs incurred in excess of funds accumulated in Account No. 228.1 and insurance shall be accomplished through Section 366.8260, Florida Statutes, and/or through a

⁶ See, e.g., Bill Heard Chevrolet v. Wilson, 877 So. 2d 15 (Fla. 5th DCA 2004), reh. den. July 12, 2004.

⁷ See, e.g., City of Homestead v. Johnson, 760 So. 2d 80, 84 (Fla. 2000); Paladyne Corporation v. Weindruch, 867 So. 2d 630 (Fla. 5th DCA 2004).

⁸ See, e.g., Aucilla Area Solid Waste v. Madison County, 890 So. 2d 415, 416-17 (Fla. 1st DCA 2004); Peoples Gas System v. City Gas Co., 147 So. 2d 334, 336 (Fla. 3rd DCA 1962); Siedle v. Nat'l Assoc. of Sec. Dealers, Inc., 248 F. Supp. 2d 1140 (M.D. Fla. 2002).

separate surcharge.” (Emphasis added.) These provisions place no limitation on recovery of prudently incurred storm restoration costs. Indeed, the second of these provisions provides for “recovery of *any* costs incurred in excess of funds accumulated in [the Reserve].”⁹ In ordinary usage, the word “any” can mean “all” or “any one of a number” depending on the context. In the context of this provision, the usage of the term “any costs” clearly connotes the concept of “all costs.” The alternative – that recovery of any one of a number of costs incurred shall be made through securitization and/or a surcharge – makes no sense in this context. Because the Reserve has carried a negative balance since the 2004 hurricane season, all of FPL’s 2005 storm-recovery costs were incurred in excess of funds accumulated in the reserve. Thus, construing the settlement as a whole, the plain language of the settlement given its ordinary meaning reflects an agreement that FPL will be permitted to recover all of its prudently incurred costs associated with events covered by its Reserve. The AG’s construction of the settlement would inappropriately render use of the term “any” as extraneous.

Because the settlement, given the ordinary meaning of its plain language, provides for recovery of all prudently incurred storm costs, the Commission need not attempt to interpret the settlement by ascertaining the intent of the parties.¹⁰ As noted above, the language used in a contract is the best possible evidence of the intent and meaning of the contracting parties and is controlling regardless of the intention existing in the minds of the parties. Further, by giving effect to the ordinary meaning of the plain language of the settlement, the absence of any provision prohibiting storm cost sharing becomes inconsequential. Indeed, the absence of such a provision is evidence of an intent to exclude sharing rather than include it.¹¹

Staff notes that OPC, FRF, and AARP, consumer advocates who were parties to the settlement, have taken no position with respect to witness Jenkins’ sharing proposal. FIPUG, whose position is joined by FEA, takes the position that in general it supports a risk/reward sharing between utilities and their customers but that the parties to the stipulation and settlement agreed that, for the term of the agreement, FPL would be permitted to recover prudently incurred storm costs. FIPUG states that it is bound by that agreement in this case to the extent that storm costs are prudent and do not constitute double recovery. Staff believes it is fair to imply from FIPUG’s position that FIPUG does not believe the settlement allows for any sharing of prudently incurred costs.

Regardless of whether witness Jenkins’ proposed sharing is or is not consistent with the settlement, all parties have recognized that the Commission itself is not entirely bound by the stipulation and settlement. The Commission is not a signatory to the stipulation and settlement and retains the authority to set fair and reasonable rates on a prospective basis. Pursuant to the doctrine of administrative finality, the Commission may modify its final order approving the stipulation and settlement if there is a significant change in circumstances or if modification is required in the public interest.¹²

⁹ Reading this provision together with the first, it is clear that “recovery of any costs” is limited to recovery of any prudently incurred costs.

¹⁰ See, e.g., Walgreen Co. v. Habitat Development Corp., 655 So. 2d 164 (Fla. 3rd DCA 1995), reh. denied, (June 21, 1995).

¹¹ See, e.g., Jacobs v. Petrino, 351 So. 2d 1036 (Fla. 4th DCA 1976).

¹² See Florida Power Corp. v. Garcia, 780 So.2d 34 (Fla. 2001), citing Austin Tupler Trucking, Inc. v. Hawkins, 377 So.2d 679, 681 (Fla. 1979).

Staff agrees with FPL that the Commission has encouraged settlements recognizing certain inherent benefits such as reduced litigation costs and regulatory certainty. It is true that the Commission has never altered, terminated, or otherwise changed the conditions of a settlement.

Staff believes it is good policy not to second guess the reasonableness of a settlement after its approval. All the parties found the settlement reasonable. Undoubtedly, there was much give and take on all sides. There were benefits for consumers and benefits for FPL. Therefore, the question is not whether the settlement was good or bad but whether conditions have materially changed since August 2005 to the point where action contradictory to the rate case settlement is in order.

When the Commission approved the rate case settlement in August of 2005, it specifically stated that it is not a signatory to the settlement. Staff disagrees with FPL's assertion that a Commission action contrary to the rate case settlement is punitive and detrimental to the public interest. The Commission can not abrogate its statutory responsibilities by way of a settlement. Therefore, it should not be of complete surprise if the Commission considers some alteration of a settlement if believed necessary and in the public interest. For instance, if FPL unexpectedly started gaining exorbitant profits, staff believes it would be appropriate to alter this settlement in an effort to preserve reasonable profits and therefore, reasonable rates.

The most significant event since approval of the settlement was devastation caused by Hurricane Wilma. Not only did this storm cause over \$700 million of storm costs in FPL's service territory, it was a major contributor to the drastic increase in fuel costs that resulted in the significant increase in fuel rates effective January 2006. Staff believes that because of the significant hardship consumers have faced, some level of sharing is warranted to ameliorate the effects to consumers. Unfortunately, this is difficult to do outside of an earnings review which would conflict with the rate case settlement. (TR 1255)

Staff believes by adopting the staff recommendations in Issues 15, 17, 27, 28, and 33 the Commission will effectively endorse the sharing concept without contradicting the rate case settlement. These recommendations, if adopted, will adversely impact FPL. The magnitude of making these adjustments is both significant to FPL shareholders and consumers. The total effect of these adjustments is \$86.1 million compared to 2005 storm costs of over \$700 million. This means that FPL shareholders will assume over 10 percent of the adverse effects of the 2005 storms.

It is equally important that the aggregate effect of all Commission decisions in this docket leave FPL in a financially sound basis so, in the event of another catastrophic storm or storms, it will have the financial capability to restore power in a timely fashion. Staff believes that even though FPL's profits will be negatively affected in the event the Commission adopts the staff recommendations in this case, FPL's financial status will remain viable. For instance, the use of "securitized" storm bonds, as opposed to continuance of the storm surcharge, will serve to strengthen FPL's financial position.

CONCLUSION

Staff recommends sharing of the adverse effects of the storms between ratepayers and FPL shareholders. Staff does not recommend sharing based on an arbitrary allocation factor. Rather, sharing should be based on assigning costs or other adverse effects to shareholders that are 1) not directly related to storm restoration and, 2) imprudently incurred costs.

Issue 36: Taking into account any adjustments identified in the preceding issues, what is the amount of reasonable and prudently incurred 2005 storm related costs that should be recovered from customers?

Recommendation: The amount of reasonable and prudently incurred 2005 storm related costs that should be recovered from customers is \$728,510,020 (Jurisdictional). (Slemkewicz)

Position of the Parties

FPL: The amount of reasonable and prudently incurred 2005 storm related costs that should be recovered from customers is \$816,016,000 (rounded) (provided on KMD-4) plus interest in accordance with Section 366.8260, Florida Statute (2005) in the amount of \$11,490,000 for a total of \$827,507,000, as adjusted in the final true-up. (See Issue 42).

OPC: This is a fall-out issue.

FIPUG: The appropriate amount of adjustments should be the total of OPC's proposed adjustments.

FRF: Agree with OPC that the maximum amount of allowable 2005 storm costs is approximately \$705,000,000 on a jurisdictional basis, pending other adjustments.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: This is a fall-out issue based on the resolution of other issues. Staff recommends that the amount of reasonable and prudently incurred 2005 storm related costs that should be recovered from customers is \$728,510,020 (Jurisdictional). This amount was calculated as follows:

<u>ISSUE</u>	<u>DESCRIPTION</u>	<u>\$</u>	<u>RATE BASE EFFECT (\$)</u>
25	ADJUSTED TOTAL – 2005 COSTS BEFORE JURISDICTIONALIZATION	<u>725,972,500</u>	
	ADDITIONAL STAFF ADJUSTMENTS		
27	Distribution & Transmission System Inspection & Maintenance (Pre 6/1/05)	(4,460,000)	(1,440,000)
28	Vegetation Management (Pre 6/1/05)	(2,550,000)	(850,000)
30	Distribution & Transmission System Inspection & Maintenance (Pre 10/23/05)	See Issue 27	
31	Vegetation Management (Pre 10/23/05)	See Issue 28	
33	Transmission Structure Failures	<u>0</u>	(12,000,000)
---	TOTAL ADJUSTMENTS	<u>(7,010,000)</u>	
36	ADJUSTED TOTAL – 2005 COSTS BEFORE JURISDICTIONALIZATION	718,962,500	
---	Jurisdictional Factor	<u>99.921%</u>	
36	NET ADJUSTED JURISDICTIONAL 2005 TOTAL COSTS	718,394,520	
34	2005 Jurisdictional Interest	<u>10,115,500</u>	
36	TOTAL JURISDICTIONAL 2005 STORMS INCLUDING INTEREST	<u>728,510,020</u>	

STORM DAMAGE RESERVE

Issue 37: What is the appropriate level of funding to replenish the storm damage reserve to be recovered through a mechanism approved in this proceeding?

Recommendation: FPL has not shown that a \$650 million replenishment of the storm damage reserve is appropriate. A \$200 million replenishment will (1) reduce the incidental costs associated with securitization, (2) provide more critical review of FPL's storm charges, and (3) reduce customer bills associated with FPL's request to replenish the storm damage reserve. (Breman)

Position of the Parties

FPL: FPL believes that establishing a storm damage Reserve level of approximately \$650 million is reasonable at this time.

OPC: The Commission should approve a reserve that meets the historically-stated threshold of covering the costs of most, if not all, storms. The appropriate level of funding for the storm reserve should be \$150 million. However, based on the projected increase in hurricane activity, the Commission could reasonably include a "safety margin" raising the approved reserve to \$200 million.

FIPUG: \$150 million.

FRF: Agree with OPC that the appropriate level of funding for FPL's storm reserve is \$150 million.

AARP: There is a "new day" for storm cost recovery closely akin to a recovery clause with the potential for interim rate relief prior to evidentiary hearing. Consequently, there should be \$0 for a storm reserve funded through securitization, a process involving borrowing money to invest it at a lower rate. Reserve funding, if by surcharge, should be no more than \$200 million, if a reserve is funded and at a level not to exceed the current surcharge.

FEA: Agree with OPC.

AG: \$200 million. The AG adopts the position of OPC. A lower reserve means lower bond and issuance costs, lower consumer rates and more Commission control over storm recovery costs. If storm damage exceeds reserve levels, the Commission can address that issue. A negative balance reserve has never impaired FPL's ability to restore power. Additionally, FPL must not profit by collecting taxes from the consumer based on a statutory rate then paying taxes based on a lower effective rate.

Staff Analysis:

PARTIES' ARGUMENTS

FPL proposes a replenishment amount of \$650 million to support future storm restoration activities. (TR 64-65) This amount should be large enough to address storm damage costs from most but not all storm seasons. FPL witness Dewhurst considered a number of factors including (1) an expected average annual cost for windstorm losses of approximately \$73.7 million as determined by FPL witness Harris, (2) the possibility that Florida is in the midst of a much more active hurricane period relative to average levels of activity over the much longer term, (3) the potentially diminished availability of non-T&D property insurance, (4) the impact of the recent severe and unprecedented storm seasons on customer bills in the near term, and (5) the opportunity to revisit this issue in future proceedings. (TR 65)

FPL witness Dewhurst testified that, in 1998, the Commission agreed that the storm damage reserve level should be large enough to absorb another 'Andrew type event,' and that 'a reasonable level for the reserve is \$370 million in 1997 dollars.' Further, the Commission recognized that even this level would not cover all realistically possible events but would afford a high degree of protection against any one bad year. Simply escalating the cost of Hurricane Andrew from \$370 million in 1997 dollars would be equivalent to a Reserve level of approximately \$460 million in 2006 dollars. A \$650 million increase to the Reserve recognizes that under the current rate agreement there is no ongoing accrual, that FPL's system has grown in extent by 30-40 percent since 1997, and gives some recognition to the conclusion of many meteorological experts that Florida is in a multi-decade cycle with more frequent incidence of tropical storms. (TR 1068, 1676-1677)

FPL witness Dewhurst testified that OPC and AARP witness Stewart incorrectly believes a \$200 million storm damage reserve level is reasonable. Witness Stewart's estimate of FPL's average annual loss of \$147 million per year means the Reserve would last approximately one year. (TR 1679) A lower storm damage reserve level will simply shorten the expected time before it becomes necessary to return to the Commission and seek recovery of additional restoration costs. All things being equal, this will lead to greater rate volatility. In the extreme, with no Reserve and an annual process with an annual surcharge, customers could see rates fluctuate from year to year by the equivalent of \$0 to \$8 or so per month on the typical 1,000 kWh bill. (TR 1678)

FPL contends that the passage of securitization legislation does not change the overall framework for recovery of storm restoration costs; instead, it provides the Commission with an additional tool to use. On the positive side, securitization provides the ability to replenish the storm damage reserve more rapidly than through an annual accrual or a surcharge. However, transaction costs associated with securitization bonds are higher than those associated with a surcharge. Thus, securitization is not as efficient as a surcharge coupled with an existing reserve to cover ongoing costs, and in the extreme it clearly would not be cost effective to issue bonds in small amounts on a continuing basis. If FPL is to securitize, FPL believes that it makes a great deal of sense to take advantage of this opportunity to replenish the reserve to a reasonable level. (TR 1679-1780)

A storm damage reserve replenishment of \$200 million is large enough to withstand the storm damage from most but not all storm seasons over the last 16 years because the annual average is \$147,120,000. Any storm damage reserve deficiencies resulting from excessive losses could be dealt with by a separate surcharge. Keeping the storm damage reserve replenishment as low as is reasonably possible will reduce interest and bond issuance costs and minimize the financial impact on customers' rates, while still allowing FPL and the Commission the flexibility to address recovery of FPL's prudently incurred costs from year to year. (TR 1045-1048; EXH 87)

FPL Witness Dewhurst admitted that the level of the storm damage reserve has no impact on FPL's hurricane exposure. (TR 1678) The Securitization legislation guarantees the recovery of reasonable and prudent expenses for storm damage. Therefore, no matter the amount of storm damage, FPL is statutorily guaranteed recovery of its storm expenses as long as they are deemed prudent by the Commission. (TR 1051-1054)

History indicates that the review of storm damage expenses are less stringent when the expenses are paid from an existing Reserve versus when the utility must document the expenses in an evidentiary hearing addressing an additional recovery mechanism. From 1996 to 2002 when FPL covered storm damage expenses with funds from the existing storm damage reserve, there were no hearings and consequently little chance for review of expenses by affected parties. Forcing a hearing for all but the minimal storm damage occurrences guarantees a more thorough review and the reduced likelihood that inappropriate expenditures will be charged to the storm damage reserve. (TR 1053)

FIPUG and FRF urge the Commission to set a replenishment level of \$150 million, because that is the smallest amount supported by the record. Exhibit 87, sponsored by witness Stewart, shows that the annual average cost for the past 16 years has been \$147,120,000. (FIPUG BR at 8; FRF BR at 45)

By Order No. PSC-05-1252-FOF-EI, issued December 23, 2005, in Docket No. 050001-EI, In re: Fuel and purchased power cost recovery clause with generating performance incentive factor, the Commission denied Florida Public Utilities Company's request to begin recovery of future costs associated with a 2008 change in wholesale power purchases. The request was made in part as a means to avoid future rate shock and rate volatility. (FRF BR at 38-39) FPL is similarly requesting recovery of costs it has not yet incurred and should be denied on the same basis as stated in Order No. PSC-05-1252-FOF-EI. (TR 1054; FRF BR at 38-39)

The intervenors contend that keeping the storm damage reserve replenishment as low as is reasonably possible will reduce interest, bond issuance costs, underwriting fees, legal fees, taxes, and minimize the financial impact on customers' rates. (TR 1053, 1765) The Commission should minimize the amount of money that customers must prepay to FPL to recover those costs. (FIPUG BR at 10)

ANALYSIS

Prior to the 2005 Rate Case Order, FPL's base rates provided for an annual contribution to the storm damage reserve of \$20.4 million. (TR 473) The \$20.4 million accrual was suspended due to the ability of FPL to seek recovery through a surcharge or securitization. (TR

55) The suspension of the storm damage reserve accrual was a change in fact and policy with respect to FPL's hurricane damage self-insurance program. (TR 1061, 1071) Thus, prior orders on storm damage reserve levels and accrual amounts provide little guidance as to the storm damage reserve replenishment level at issue in this case.

The interveners support a lower Reserve level while FPL supports a comparatively higher storm damage reserve replenishment level.

Lower Reserve Replenishment Level

The storm damage reserve replenishment level supported by AARP, AG, FEA and OPC is \$200 million as calculated by witness Stewart. Witness Stewart calculates \$200 million by adding approximately \$50 million to his estimate of annual storm costs of \$147.1 million based on the projected increase in hurricane activity. (TR 1053, 1059; EXH 87) Witness Stewart testified that a lower replenishment is appropriate because: (1) a lower replenishment reduces the incidental costs associated with securitization, (2) a lower replenishment provides more critical review of FPL's storm charges, (3) a lower replenishment is believed to reduce payment for costs that have not yet been incurred, and (4) because FPL can come in and get a surcharge rather quickly. (TR 046, 1051-1053, 1060, 1062, 1064, 1069, 1080) Additionally, FPL witness Dewhurst admitted that the level of the storm damage reserve has no impact on FPL's hurricane exposure. (TR 1062, 1079, 1678)

Witness Stewart opined that the Securitization legislation guarantees the recovery of reasonable and prudent expenses for storm damage. Therefore, no matter the amount of storm damage, FPL is statutorily guaranteed recovery of its storm expenses as long as they are deemed prudent by the Commission. (TR 1051-1054) The potential of a diminished availability of non-T&D property insurance doesn't lead to the conclusion that customers should support a \$650 million Reserve. The opportunity to revisit this issue in future proceedings should argue for approving a smaller, not larger, Reserve. (TR 1051)

Due to the various changes over time, it is the view of witness Stewart that the risk is completely with the consumers at this point. (TR 1073, 1074) Thus, witness Stewart concludes that a storm damage reserve replenishment should be as low as possible. (TR pp. 1072-1073)

FIPUG and FRF support a Reserve level of \$150 million apparently because it is the smallest amount supported by the record and for the reasons presented by witness Stewart. (FRF BR at 45; EXH 87)

Staff concludes that the interveners appear willing to pay a lower bill associated with a lower replenishment and risk the potential for future rate volatility because of a perceived benefit of increased review of storm charges and the lack of certainty of when the next major storm event will occur. The interveners apparently perceive the risk associated with a low Reserve level to be completely with the customers, not FPL. Whether the interveners will continue to support these views in subsequent proceedings is unknown.

Higher Reserve Replenishment Level

In proposing a replenishment level of \$650 million, FPL Witness Dewhurst testified that he considered a number of factors including (1) an expected average annual cost of approximately \$73.7 million, (2) the possibility that Florida is in the midst of a much more active hurricane period relative to average levels of activity over the much longer term, (3) the potentially diminished availability of non-T&D property insurance, (4) the impact of the recent severe and unprecedented storm seasons on customer bills in the near term, and (5) the opportunity to revisit this issue in future proceedings. (TR 65)

FPL Witness Harris developed an annual storm damage estimate of \$73.7 million based on a pure premium concept used by the insurance industry, a 103 year history of hurricane data, 100,000 simulated hurricane events, and geo-located cost estimates of the FPL facilities at risk. (TR 621-623; EXH 26, pp. 7-9) The same analysis, with minor editorial revisions and corrections, was provided in Docket No. 050045-EI, which was resolved by the FPL 2005 Rate Case Order. (TR 618) Table 37-1 is a summary of FPL witness Harris estimates of annual average storm costs.

Table 37-1
Summary of Expected Annual Storm Costs
(Source: Exhibit 26 p. 19)

Expected Annual Losses	\$ Millions	Comments
Transmission and Distribution Assets	64.4	a) Hurricanes - Category 1 through 5 b) Tropical Storms - 39-74 mph. c) Winter storms
Storm Staging Costs	3.5	FPL Pre-storm mobilization
Non T&D Assets	5.8	Losses arising from payment of deductibles on insurance policies
Totals	73.7	

The distribution assets at risk total \$9.530 billion. The transmission assets at risk total \$2.309 billion. Non-T&D assets are insured for storm losses. The deductibles under the current policies are \$25 million per event. (EXH 26, pp. 7-9)

In defense of FPL's higher replenishment level, FPL witness Dewhurst notes that witness Stewart's conclusions are not consistent with past Commission practice. (TR 1677) Yet he also admits that the level of the storm damage reserve has no impact on FPL's hurricane exposure and goes on to say:

Accordingly, a lower reserve will simply shorten the expected time before it becomes necessary to return to the Commission and seek recovery of additional restoration costs. Other things equal, this will lead to greater rate volatility. In the extreme, with no reserve and an annual process with an annual surcharge, customers could see rates fluctuate from year to year by the equivalent of \$0 to \$8 or so per month on the typical 1,000 kWh bill. In addition, a smaller reserve will, other things equal, mean more frequent regulatory proceedings, each of which carries an administrative cost and burden for all parties.

(TR 1678)

Thus, FPL's rebuttal testimony does not challenge the notion that the risk associated with a low replenishment level to be completely with the customers, inclusive of the five factors considered by FPL witness Dewhurst.

Staff concludes that FPL's proposed high Reserve level addresses Commission policy prior to the 2005 Rate Case Order. The approved settlement constituted a departure from the past policy which included an annual accrual to the Reserve. Staff also concludes that FPL has not shown that it requires a \$650 million Reserve to address specifically or collectively, the five factors Witness Dewhurst considered.

Selecting the Replenishment Level

FPL has not shown that a \$650 million replenishment of the storm damage reserve is needed. However, this finding does not mean that FPL's request for \$650 million to replenish the storm damage reserve is unreasonable.

Witness Stewart expressed concerns with respect to the level of review associated with large storm damage reserve balances. In his opinion, there should be more critical and frequent review of FPL's storm charges to the storm damage reserve. These concerns can be addressed by requiring FPL to make specific filings whenever storm restoration costs exceed a threshold amount such as \$200 million. Such requirements can be made part of the Commission's decision or by rule. Therefore, there is no need to reduce the replenishment amount to address an apparent request by the intervenors for more hearings regarding FPL's charges to the storm damage reserve.

However, the record clearly establishes that the level of the storm damage reserve has no impact on FPL's hurricane exposure. It is also clear that the risk associated with a high or low replenishment level, at this time, is completely with the customers. A benefit of a lower replenishment amount is a reduction in the securitization costs, and resultant customer bills associated with this case. Two large use customer groups, FIPUG and FRF, seek the lowest storm damage reserve replenishment supported by the record. The only testimony addressing a replenishment amount lower than \$650 million is that of Witness Stewart. Therefore, staff recommends a replenishment level of \$200 million, which is supported by witness Stewart.

CONCLUSION

FPL has not shown that a \$650 million replenishment of the storm damage reserve is needed. A \$200 million replenishment will (1) reduce the incidental costs associated with securitization, (2) provide more critical review of FPL's storm charges, and (3) reduce customer bills associated with FPL's request to replenish the storm damage reserve.

Issue 38: What portion, if any of the Reserve must be held in a funded Reserve and should there be any limitations on how the Reserve may be held, accessed or used?

Recommendation: The amount of the storm damage reserve that should be placed in a fund is the amount, after any applicable taxes, of the replenishment amount credited to the storm damage reserve as determined in Issue 37. The use of the fund should be restricted to purposes consistent with Rule 25-6.0143, Florida Administrative Code, for Account No. 228.1, Accumulated Provision for Property Insurance. This treatment would be the same whether the replenishment is accomplished through either securitization or a surcharge. (Slemkewicz, Springer, Breman)

Position of the Parties

FPL: FPL proposes a funded Reserve of \$650 million, and that the Reserve should be used for all of the purposes provided for in and consistent with Rule 25-6.0143, Florida Administrative Code for Account No. 228.1, Accumulated Provision for Property Insurance.

OPC: Once the reserve regains a positive balance, the reserve should continue to be held in a funded account with the interest earned accruing to the benefit of the ratepayers. By law, funds obtained through securitization must be restricted to storm recovery activities caused by named tropical storms or hurricanes.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC that once FPL's storm reserve attains a positive balance, the reserve should continue to be held in a funded account with interest accruing to the benefit of FPL's customers.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL has proposed that the reserve (Account 228.1) be funded. The monies in the fund would be available for use pursuant to the provisions of Rule 25-6.0143, Use of Accumulated Provision Accounts 228.1, 228.2, and 228.4, Florida Administrative Code. In its brief, OPC agrees that the reserve should be funded. However, OPC believes that the use of the monies in the fund obtained through securitization should be used only to finance storm-recovery costs. (OPC BR at 70)

ANALYSIS

FPL has maintained Account No. 228.1¹³, Accumulated Provision for Property Insurance, on a funded basis since 1958. FPL's proposal to continue funding this reserve is consistent with its prior practices. The monies to be placed in the fund would be the after-tax amount of the reserve replenishment amount. Based on FPL's request, the reserve replenishment amount would be \$650 million and the after-tax monies placed into the fund would be \$400 million. (TR 57) In its brief, FPL states that the monies in the fund can be used for any purposes provided for in Rule 25-6.0143, F.A.C. (FPL BR at 120)

OPC agrees that the reserve should be maintained on a funded basis. In its brief, however, OPC states that funds obtained through securitization may be used only to finance costs that have, or will be, incurred to undertake storm-recovery activities related to named tropical storms or hurricanes. OPC cites sections 366.8260(1)(j), (k), and (n), Florida Statutes, as its basis for that opinion. (OPC BR at 70)

Rule 25-6.0143(1), F.A.C., states that the purpose of Account No. 228.1 is to provide for property losses through accident, fire, flood, storms, nuclear accidents and similar type hazards that are not covered by insurance, as well as insurance deductible amounts and nuclear accident retrospective premiums. To date, it appears that the major use of Account No. 228.1 has been to provide for property losses resulting from storms. Rule 25-6.0143, F.A.C., however, does not provide any guidance, restrictions or limitations regarding the use of any monies that may be placed into a fund related to the reserve.

CONCLUSION

Staff agrees with the parties that the reserve should be maintained on a funded basis. Although the balance in Account No. 228.1 is commonly referred to as the "storm reserve," its stated purpose in Rule 25-6.0143(1), F.A.C., is to cover all uninsured property losses regardless of the cause. Account 228.1 is currently depleted and the \$20.3 million annual accrual to the reserve has been suspended pursuant to the terms of the Stipulation approved in Order No. PSC-05-0902-S-EI, issued September 14, 2005, in Docket No. 050045-EI, In re: Petition for rate increase by Florida Power & Light Company and 050188-EI, In re: 2005 comprehensive depreciation study by Florida Power & Light Company. There is no evidence in the record to support OPC's contention that any provisions of Section 366.8260, Florida Statutes, place any restrictions on the use of the reserve or the monies in the fund.

Based on the foregoing, staff recommends that the reserve be funded on an after-tax basis. Staff further recommends that the use of the fund should be restricted to purposes consistent with Rule 25-6.0143, F.A.C., for Account No. 228.1, Accumulated Provision for Property Insurance. This treatment would be the same whether the replenishment is accomplished through either securitization or a surcharge.

¹³ This account was previously identified as Account 261, Property Insurance Reserve, prior to 1985.

RECOVERY MECHANISM

Issue 39: Is the issuance of storm-recovery bonds and the imposition of the Storm Charge, as proposed by FPL, reasonably expected to result in lower overall costs or avoid or significantly mitigate rate impacts to customers as compared with alternative methods of financing or recovering storm-recovery costs and storm-recovery reserve?

Recommendation: The issuance of storm recovery bonds for the recovery of reasonable and prudently incurred storm damage restoration costs and the replenishment of the storm damage reserve as proposed by FPL is not expected to result in lower overall costs to ratepayers. However, the issuance of storm recovery bonds is expected to mitigate rate impacts to ratepayers as compared with alternative methods of recovery of these costs and replenishment of the storm damage reserve. (Springer, Draper)

Position of the Parties

FPL: Yes. This statutory standard adopted by the legislature in Section 366.8260(2)(b)2.b., Florida Statutes (2005), is met by FPL's proposal, a primary benefit of which is to immediately replenish the Reserve and to "smooth out" the significant rate impact of an extreme sub-period of storm activity, making it a useful tool for recovery of existing deficits and replenishment of the Reserve.

OPC: Yes, but only if the Commission takes an active role in the bond issuance process and does not approve FPL's proposed methodology. To ensure that the issuance of storm-recovery bonds results in the lowest overall cost to ratepayers compared with the alternative methods of financing, the "best practices" outlined in Commission staff witness Fichera's direct testimony should be adopted including active participation by the Commission, its staff, and financial advisors which ensures ratepayer protection.

FIPUG: No. Securitization will result in higher overall costs for the customer, which outweigh the value of securitization to mitigate rate impacts.

FRF: No position.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL's proposed issuance of storm-recovery bonds and the imposition of the Storm Charge is designed to mitigate rates. FIPUG believes that securitization will result in higher overall cost for the customer, which outweighs the value to mitigate rate impacts with

securitization. FRF takes no position. The remaining parties agree with OPC that securitization will result in the lowest overall cost to ratepayers compared with the alternative methods if the Commission takes an active role in the bond issuance.

ANALYSIS

FPL witness Dewhurst testified that the issuance of storm recovery bonds in this case is based on an assertion that there would be rate mitigation associated with the issuance of the bonds as compared to another alternative. (TR 113) In his summary of his direct testimony, witness Dewhurst stated:

[T]here is no clear analytical way of saying which alternative is better. The choice comes down to policy judgment. Securitization will produce a smaller monthly charge. The surcharge proposal has a shorter recovery period. Under the current circumstances, we believe the securitization approach makes sense, even though the charge will be in place for a longer period, but we can appreciate that some customers might prefer the alternative.

(TR 81)

Witness Dewhurst testified that FPL did not conduct a net present value analysis to compare the overall total cost of the ratepayers of the primary recommendation and the alternative. (TR 111-113) Witness Dewhurst did note that "if you strictly took a 'what's the fewest dollar approach,' that would say we should use the alternative." However, witness Dewhurst continued, the alternative would produce a much higher monthly charge for a shorter period of time. (TR 113)

Witness Morley testified that compared to the proposed storm charges, the alternative would result in significantly higher typical bills. (TR 766) The current 1,000 kWh residential bill is \$108.61, which includes the current 2004 storm charge. With the implementation of the proposed storm charge and termination of the current charge, the same residential bill would be \$108.53. Under FPL's alternative request, the 1,000 kWh residential bill would be \$113.93, which includes the current surcharge, surcharge for 2005 costs, and surcharge for replenishment of reserve.

OPC supports the lower but longer-term charges associated with the issuance of storm-recovery bonds as long as the Commission adopts the "best practices" outlined in Commission staff witness Fichera's direct testimony, including active participation by the Commission, its staff, and financial advisors which ensures ratepayer protection. (OPC BR at 70-71) OPC believes that with the goal of avoiding or significantly mitigating rate impacts to customers, the Commission must use every tool available to ensure that the ultimate costs are the lowest costs that can be achieved.

CONCLUSION

Staff believes that the issuance of storm recovery bonds is expected to mitigate rate impacts to ratepayers as compared with alternative methods of recovery of these costs and replenishment of the storm damage reserve. However, the issuance of storm recovery bonds as

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proposed by FPL is not expected to result in lower overall costs to ratepayers, as addressed in Issue 68.

Issue 40: WITHDRAWN

Issue 41: Should the unamortized balance of 2004 storm costs continue to be recovered through the current surcharge or should the balance be added to any amounts to be securitized?

Recommendation: The unamortized balance of the adjusted 2004 storm costs should be added to any amounts to be securitized. This treatment is dependent on the Commission's decision to approve the issuance of storm recovery bonds. (Slemkewicz, Springer)

Position of the Parties

FPL: FPL's primary recommendation is that the unamortized balance of 2004 storm costs be added to any amounts to be securitized, so as to enhance the rate impact "smoothing" benefit of issuing bonds.

OPC: If the Commission approves securitization, FPL's 2004 storm costs should be reduced by \$51,264,919 as addressed in Issue 1. Corresponding reductions should be made to interest accrued based on actual storm costs, interest rates, and the most recently available revenue collections.

FIPUG: The unamortized balance of the 2004 storm costs should continue to be recovered via a surcharge. Securitization will result in higher overall costs for the ratepayer.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL proposes to add the unamortized balance of 2004 storm costs to any amounts to be securitized as a rate mitigation. AARP, AG, and FRF agree with OPC that FPL's 2004 storm costs should be reduced by \$51,264,919 with corresponding reductions made to interest accrued based on actual storm cost, interest rates, and the most recently available revenue collections. (OPC BR at 73) FEA agrees with FIPUG that the unamortized balance of the 2004 storm costs should continue to be recovered via a surcharge, and securitization will result in higher overall costs for the ratepayer. (FIPUG BR at 13)

ANALYSIS

FPL's bond issuance would be used to fund the balance of unrecovered 2004 and 2005 storm-recovery costs, replenish the Reserve and pay upfront bond issuance costs. (Dewhurst TR 55) FPL states that the recovery of the 2004 storm deficiency would result in the termination of the Storm Restoration Surcharge. (Morley TR 762) FPL proposes that upon issuance of the storm-recovery bonds, the storm bond repayment charge and tax charge would replace the existing 2004 Storm Restoration Surcharge. (Dewhurst TR 56) OPC states that a separate surcharge for 2004 storm costs combined with securitization of the 2005 storm costs and replenishment of the Reserve would result in a higher monthly charge than if the Commission permitted all of the storm costs to be recovered through a monthly securitization charge. (OPC BR at 74) FIPUG proposes that the 2004 storm costs should continue to be recovered through a surcharge, since it believes that securitization results in higher overall costs. (FIPUG BR at 13)

CONCLUSION

To ensure that the issuance of storm recovery bonds significantly mitigates rate impacts to customers, staff recommends that the unamortized balance of the adjusted 2004 storm costs should be added to any amounts to be securitized for rate mitigation. Based on the staff's recommendation in Issue 3, the amount of adjusted 2004 storm costs to be recovered through securitization would be \$198,680,432 on a pre-tax basis. However, this treatment is dependent on the Commission's decision to approve the issuance of storm recovery bonds.

Issue 42: Based on resolution of the preceding issues, what amount, if any, should the Commission authorize FPL to recover through securitization?

Recommendation: The amount to be approved for recovery would be determined by the amounts approved in Issue 3 for 2004 storm-related costs, Issue 36 for 2005 storm-related costs, and Issue 37 for the appropriate level of the storm damage reserve. Based on staff's recommendations in those issues, the amount to be recovered through securitization is \$1,127,190,452 on a pre-tax basis, plus \$11,425,000 in up-front bond issuance costs. The total after-tax amount is \$703,801,734. (Slemkewicz, Springer, Breman)

Position of the Parties

FPL: The total amount of storm-related costs that the Company should be authorized to recover through storm-recovery financing is \$1,690.2 million, which includes the proposed \$650 million replenishment of the Reserve, 2005 jurisdictionalized unrecovered storm-recovery costs of \$826.9 million, 2004 jurisdictionalized unrecovered storm-recovery costs of \$213.3 million.

OPC: FPL's requested storm-related costs of \$1,690,160,000 should be reduced by all of the adjustments set forth in response to preceding issues. Corresponding reductions should also be made to interest and income taxes related to the adjustments recommended and to reflect that interest should only be calculated on the actual not estimated amounts.

FIPUG: The Commission should not authorize FPL to recover via securitization. However, if securitization is granted, the appropriate amount to be securitized should be based on the following: (1) the recovery of the unamortized balance of the 2004 storm costs; (2) the replenishment of the storm reserve to \$150 million, and; (3) the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments.

FRF: Based on resolution of the preceding issues, if the Commission approves securitization, FPL's requested storm-related costs of \$1,690,160,000 should be reduced by at least \$660,000,000, and further reduced to reflect any penalties or other adjustments determined to be appropriate by the Commission.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: As noted in the positions above, all of the parties except FIPUG have recommended the Commission approve FPL's primary recommendation to use securitization to recover reasonable and prudently incurred storm damage restoration costs and replenish the storm damage reserve. FIPUG argues that due to tax considerations, reduced interest expense, a reduction in the amount of storm damage restoration costs FPL is allowed to recover, and a lower storm reserve level, ratepayers are better off if the Commission approves a new storm

surcharge over a three year period compared to recovery through securitization over a period of 12 years. (FIPUG BR at 5–10) To the extent the Commission decides in other issues that the amount of reasonable and prudently incurred storm damage restoration costs and replenishment of the storm reserve are less than the respective amounts FPL has requested, the amount FPL will be allowed to recover from ratepayers will be the same whether FPL pursues securitization or a surcharge. (Dewhurst TR 110) In addition, taxes are assessed based on actual customer consumption of electricity. FIPUG has not demonstrated that total taxes paid by ratepayers will be significantly greater if a small charge is spread over 12 years compared to a significantly larger charge spread over three years. Finally, with respect to the issue of the interest rate, staff acknowledges in Issues 39 and 68 that securitization is more expensive than alternative methods of recovery. (TR 113–114) While FIPUG’s members may prefer a substantial monthly surcharge for the next three years, the groups representing all other FPL ratepayers have expressed a strong preference for a significantly smaller storm charge even if this charge extends for several years. (See positions above) For these reasons, staff recommends the Commission issue a financing order as recommended in Issues 61 and 74B permitting FPL to issue storm recovery bonds instead of imposing a new storm surcharge for the recovery of reasonable and prudently incurred storm damage restoration costs and replenish the storm damage reserve.

The amount to be securitized is a fall-out issue based on the resolution of other issues. Staff recommends that the amount to be approved for recovery would be determined by the amounts approved in Issue 3 for 2004 storm-related costs, Issue 36 for 2005 storm-related costs, and Issue 37 for the appropriate level of the storm damage reserve. Based on the staff’s recommendations in those issues, the amount is \$1,127,190,452 on a pre-tax basis. Staff has also included FPL’s \$11,425,000 estimate of up-front bond issuance costs. The total after-tax amount is \$703,801,734. This amount was calculated as follows:

<u>ISSUE</u>	<u>DESCRIPTION</u>	<u>\$</u>
36	NET ADJUSTED 2005 TOTAL JURISDICTIONAL COSTS	728,510,020
	ADDITIONAL STAFF ADJUSTMENTS	
37	Storm Reserve Replenishment	200,000,000
3, 41	Unamortized 2004 Storm Costs	<u>198,680,432</u>
---	TOTAL STORM COSTS SUBJECT TO STORM RECOVERY FINANCING	1,127,190,452
---	Less: Income Taxes @ 38.575%	<u>(434,813,718)</u>
---	AFTER-TAX COSTS SUBJECT TO RECOVERY FINANCING	692,376,734
51, 53	Up-Front Bond Issuance Costs	11,425,000
---	Rounding	<u>0</u>
42	TOTAL BOND ISSUANCE AMOUNT	<u>703,801,734</u>

Issue 43: Based on resolution of the preceding issues, what amount, if any, should the Commission authorize FPL to recover through a traditional surcharge or other form of recovery?

Recommendation: No. However, if the Commission approves recovery other than through securitization as set forth in Issue 42, the amount to be approved for recovery would be determined by the amounts approved in Issue 3 for the 2004 storm-related costs, Issue 36 for the 2005 storm-related costs and Issue 37 for the appropriate level of the storm damage reserve. Based on the staff's recommendation in those issues, the amount to be recovered is \$1,127,190,452 on a pre-tax basis. (Slemkewicz, Springer, Lowe, Kyle, Breman)

Position of the Parties

FPL: The total amount of storm-related costs proposed for recovery through a traditional surcharge or other form of recovery is approximately \$1.7 billion, which includes the 2005 storm costs, proposed replenishment of the Reserve and the remaining balance of 2004 unrecovered storm costs. If the 2004 storm surcharge is continued, the recovery amount in this proceeding should be reduced accordingly. If FPL's primary recommendation is rejected, the Commission should authorize FPL to recover approximately \$1.5 billion through a conventional surcharge.

OPC: Based on the resolution of the preceding issues in accordance with the recommended adjustments advocated by Citizens, no amount should continue to be collected through a surcharge or other form of recovery if the Commission approves the securitization methodology set forth in the "best practices" standard.

FIPUG: The Commission should grant recovery via a surcharge. The surcharge should be designed to recover the following: (1) the replenishment of the storm reserve to \$150 million and; (2) the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments.

FRF: Based on resolution of the preceding issues, if the Commission approves recovery through traditional surcharges or another form of recovery, FPL's requested storm-related costs of \$1,690,160,000 should be reduced by at least \$660,000,000 and further reduced to reflect any penalties or other adjustments determined to be appropriate by the Commission.

AARP: The same as the Office of Public Counsel.

FEA: FEA supports recovery through securitization. We agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: This is a fall-out issue based on the resolution of other issues. Staff recommends that the amount to be approved for recovery, other than by securitization, would be determined by the amounts approved in Issue 3 for the 2004 storm-related costs, Issue 36 for the 2005 storm-related costs and Issue 37 for the appropriate level of the storm damage reserve.

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Based on the staff's recommendation in those issues, the amount to be recovered is \$1,127,190,452 on a pre-tax basis. This amount was calculated as follows:

<u>ISSUE</u>	<u>DESCRIPTION</u>	<u>\$</u>
36	NET ADJUSTED 2005 TOTAL JURISDICTIONAL COSTS	728,510,020
37	Storm Reserve Replenishment	200,000,000
41	Unamortized 2004 Storm Costs	<u>198,680,432</u>
43	TOTAL STORM COSTS SUBJECT TO STORM RECOVERY SURCHARGE	<u>1,127,190,452</u>

Issue 44: Should the Commission approve FPL's alternative request to implement a surcharge to be applied to bills rendered on or after June 15, 2006, for a period of three years for the purpose of recovering its prudently incurred 2005 storm costs and attempting to replenish the Reserve? If so, how should the Commission determine the following:

- a. The amount approved for recovery; and
- b. The cost allocation to the rate classes.

Recommendation: No, the Commission should not approve FPL's alternative request to implement a surcharge and subparts a. and b. are moot. However, if a surcharge is approved, then a. and b. need to be addressed and are discussed below.

a. The amount to be approved for recovery would be determined by the amounts approved in Issue 36 for 2005 storm-related costs and in Issue 37 for the appropriate level of the storm damage reserve. Based on staff's recommendation, the amount would be \$928,510,020 on a pre-tax basis. (Slemkewicz)

b. If the Commission approves an amount for recovery, the allocation to the rate classes should be made as proposed by FPL witness Morley and as discussed in Issue 80. The surcharge should be applied to bills rendered on or after June 15, 2006, for a period of three years, unless all approved costs are recovered sooner. (Draper)

Position of the Parties

FPL: In the event that the Commission decides not to approve the requested storm-cost financing, the Commission should grant FPL's alternative request, as detailed in Dr. Rosemary Morley's testimony. If the alternative request is approved, then the allocation of costs to the rate classes should be consistent with the manner in which equivalent costs were treated in the last filed cost of service study as provided by FPL in Exhibits 57 and 58.

OPC: Based on the resolution of the preceding issues in accordance with the recommended adjustments advocated by Citizens, no amount should continue to be collected through a surcharge or other form of recovery if the Commission approves the securitization methodology set forth in the "best practices" standard.

FIPUG: The Commission should grant recovery via a surcharge. The surcharge should be designed to recover the following: (1) the replenishment of the storm reserve to \$150 million, and; (2) the recovery of FPL's 2005 storm costs minus Pock's proposed adjustments. Costs should be allocated based on the cost of service methodology last filed with and approved by the Commission in Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

FRF: No position.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' POSITION

FPL's primary request is to issue storm-cost recovery bonds. OPC, AARP, AG, and FEA agree with FPL. FIPUG recommends that the Commission grant recovery via a surcharge designed to recover the replenishment of the storm reserve to \$150 million and the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments. FRF takes no position.

STAFF ANALYSIS

If the Commission approves FPL's primary request for securitization of its 2005 storm costs and replenishment of the storm reserve (Issue 42), this issue is moot. FIPUG's recommended reduction of the storm reserve from \$650 to \$150 million is addressed in Issue 37. FPL's reasonable and prudently incurred 2005 storm costs are addressed in Issue 36, with adjustments identified in preceding issues.

However, if a surcharge is approved, then the appropriate amount and the cost allocation to the rate classes need to be addressed and are discussed below. The amount to be approved for recovery would be determined by the amounts approved in Issue 36 for 2005 storm-related costs and in Issue 37 for the appropriate level of the storm damage reserve. The allocation to the rate classes should be done as proposed by FPL witness Morley in her direct testimony and as discussed in Issue 80. FIPUG's position regarding the allocation of the costs is also addressed in Issue 80. The surcharge should be applied to bills rendered on or after June 15, 2006, for a period of three years, or until such time as all approved costs have been recovered. (FPL BR at 127) Prior to implementation of the surcharge, FPL should file tariff sheets and associated storm charges by rate class for administrative approval by staff.

CONCLUSION

If the Commission approves FPL's primary request, i.e., securitization, then this issue is moot. If the Commission approves FPL's alternative request, then the amount approved for recovery and cost allocation should be done as discussed in the staff analysis. The \$928,510,020 amount represents \$728,510,020 for the 2005 storm costs (Issue 36) plus an additional \$200 million to replenish the storm reserve (Issue 37).

Terms and Conditions of Financing Order for Securitized Amounts

Issue 45: What adjustment, if any, should be made so that the treatment of the deferred tax liability is revenue neutral from the ratepayer's perspective?

Recommendation: No adjustment is necessary for the deferred tax liability. However, the deferred tax debits related to the funded storm damage reserve should be removed for AFUDC and earnings surveillance purposes. (Lowe, Kyle)

Position of the Parties

FPL: No adjustment is necessary since FPL would calculate interest on the storm costs on an after-tax commercial paper rate basis.

OPC: All effects of the funded reserve should be eliminated for base rate, AFUDC and surveillance purposes. Accounts specifically removed should be the regulatory asset not sold to the SPE and the associated credit deferred taxes, the storm reserve fund, the storm reserve and associated debit deferred taxes. The current AFUDC rate should be investigated to ensure that the increase in credit deferred taxes for 2004-2005 storm losses has been applied to current plant construction projects.

FIPUG: For the benefit of future customers, the Commission should order FPL to adjust the monthly AFUDC rate to reflect the changes in the deferred tax balance resulting from the storm charge. The Commission can protect current customers by ordering FPL to use part of the deferred tax account to pay current taxes.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: No position.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The utility argues that no adjustment is necessary to insure that the treatment of deferred tax liability is revenue neutral from the ratepayer's perspective. Witness Davis testifies that the deferred tax liability arises from the fact that the utility has deducted or will deduct the storm damage costs on its tax return, but has not yet recovered those costs from its customers. (TR 498, 518-519) He further testifies that as revenues to recover the storm costs are received from customers, the deferred tax liability associated with those storm losses will decrease. (TR 498) In addition, he testifies that the deferred tax liability account would be properly included in the capital structure at zero cost. (TR 501)

OPC expands the issue to argue that all effects of the funded reserve should be eliminated for base rates, AFUDC, and surveillance purposes. OPC put on no evidence regarding this expansion of the issue and provided no position or testimony with respect to the revenue neutrality of the utility's treatment of deferred tax liability resulting from this case.

FIPUG also argues that the utility's AFUDC rate should be adjusted. It also expands the issue to state the Commission can protect current customers by ordering FPL to use part of the deferred tax account to pay current taxes. FIPUG put on no evidence with respect to either of these expanded positions.

Staff believes that the utility's position with respect to the issue as stated is correct. The utility witness is correct with respect to how the deferred tax liability arises and its proper accounting treatment. The utility had storm damage expenses that it wrote-off on its tax returns in 2004 and 2005. Presuming that the utility will be allowed to recover these costs from the customers in the future, this creates a deferred tax liability equal to the amount of the deductible expense times the tax rate.

In future years, assuming allowable recovery, FPL will collect revenues from its customers that have no corresponding expense. In each of those future years FPL will pay taxes on those revenues. In other words, FPL has an expense deductible in one year and recoverable over future years. It is a timing difference subject to normalization. FPL gets the benefit of the deduction now, but will have to pay the taxes over future years.

The Commission has historically included net deferred income tax liabilities in the capital structure with a zero cost of capital. Witness Davis testifies, that this is the appropriate treatment. (TR 501)

Staff believes that the utility's position is the correct one with respect to the issue as stated. With respect to the expanded issue, FPL witness Davis under cross examination, testified that the deferred tax assets would be included in the utility's rate base. (TR 493-494) He further testified when questioned by Commissioner Deason, that the Commission could order the utility to remove it from the utility's rate base. (TR 524-525) We understand that accounting requirements establish the deferred tax asset. Since FPL's storm damage reserve is funded and earns interest; the reserve, the fund and the debit deferred taxes should all be removed for AFUDC and earnings surveillance.

Issue 46: Is the recovery of income taxes a financing cost eligible for recovery under Section 366.8260, Florida Statutes?

Recommendation: Yes. The recovery of income taxes is a financing cost eligible for recovery under Section 366.8260, Florida Statutes. (Lowe, Kyle, Springer)

Position of the Parties

FPL: Yes. Section 366.8260(1)(e)(1) defines “financing costs” to include “any income taxes resulting from the collection of storm-recovery charges in any such case whether paid, payable, or accrued.

OPC: No position.

FIPUG: Yes, but the storm reserve account balance should reflect the total sum collected from customers for the reserve via the Storm Bond Repayment Charge and the Storm Bond Tax Charge.

FRF: Yes.

AARP: Same position as FIPUG.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: No party disagrees that the recovery of income taxes is a financing cost eligible for recovery under Section 366.8260(1)(e)5., Florida Statutes. The statute defines “financing costs” to include “[a]ny income taxes resulting from the collection of storm-recovery charges in any such cases whether paid, payable, or accrued . . .”

Issue 47: If recovery of the taxes assessed on the storm recovery charges are not securitized, should the tax charge be included in the irrevocable financing order?

Recommendation: Yes. The recovery of income taxes should be allowed and included in the irrevocable financing order. (Lowe, Kyle, Springer)

Position of the Parties

FPL: Yes. Recovery of taxes is provided for in Section 366.8260, Florida Statutes, and is an integral part of recovery of storm costs.

OPC: No position.

FIPUG: Yes, but the storm reserve account balance should reflect the total sum collected from customers for the reserve via the Storm Bond Repayment Charge and the Storm Bond Tax Charge. However, if storm recovery charges are not securitized, there is no need for an irrevocable financing order.

FRF: No. It would be inappropriate to include charges that are not part of the securitized amounts within the scope of an irrevocable financing order.

AARP: Same position as FIPUG.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC. (Also discussed below is the AG's proposal to eliminate the "tax effect.")

Staff Analysis: All parties, except FRF, either take no position or agree with the Company's position. FRF's position is that it is inappropriate to include charges that are not part of the securitized amounts within the scope of an irrevocable financing order. FRF does not present any arguments or references for its position. As there is no evidence contrary to the company's position, staff recommends that the company's position be accepted.

FIPUG expands the issue to include a statement about what the storm reserve account balance should reflect and a separate statement that if storm recovery charges are not securitized, there is no need for an irrevocable financing order. What the storm reserve balance should reflect is included in other issues and should not be addressed in this issue. Although there is no argument or evidence on this issue with respect to the need for an irrevocable financing order when storm recovery charges are not securitized, staff agrees with the assertion.

In addition, in their brief, the AG proposes to eliminate the "tax effect." It states that the tax effect refers to the profit derived by FPL by collecting federal taxes from the consumer based on a statutory rate but ultimately paying out to the federal government based on a much lower effective rate.

The AG presented no witnesses for this proposal. It attempted to establish a record for this adjustment through cross examination of FPL witness Davis. Witness Davis was asked about the

difference between the statutory federal tax rate used in FPL's tax calculations and the effective rate that FPL Group paid to the federal government. (TR 578-579) Witness Davis explained that the differences were caused by several items. He explained that for FPL the differences between the marginal rate and the effective rate would be for items like the amortization of the investment tax credit and any tax exempt income. (TR 579) In addition, he explained that some of the differences for FPL group would be associated with energy tax credits associated with the wind energy that is produced by a nonregulated subsidiary as part of the federal government's inducement to build those wind farms as renewable energy. (TR 580)

Witness Davis also testified that it has been the policy of the Commission to calculate income taxes on a stand-alone basis so that the customer is insulated from any tax issues on the nonregulated side. (TR 578) Staff is persuaded by Witness Davis' testimony. We would note that using the statutory tax rate has been the Commission's practice. See, e.g., Gulf Power Company, Docket No. 71342-EU, Order No. 5471, P. 22, (6/30/72).

Issue 48: Should FPL indemnify its ratepayers against an increase in the servicer fee in the event of the servicer's default due to negligence, misconduct, or termination for cause?

Recommendation: Yes. FPL in its role as servicer has control over any action that could cause an increase in the servicer fee. Therefore, the Commission should require the Company to indemnify ratepayers against an increase in the servicer fee in the event of the servicer's default due to negligence, misconduct, or termination for cause. (Maurey)

Position of the Parties

FPL: No. Under the servicing agreement, FPL commits to service the storm recovery property in material compliance with applicable law and regulations and using the same degree of care and diligence that it exercise with respect to the collection of its other charges.

OPC: Yes. FPL should indemnify ratepayers against an increase in the servicer fee to protect the ratepayers from any potential negligence, misconduct, or termination for cause by FPL as FPL is in the best position to prevent such misconduct by its own actions.

FIPUG: Yes.

FRF: Yes.

AARP: Adopt same position as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The proposed form of servicing agreement prohibits FPL from resigning as servicer unless FPL determines that it can no longer legally perform its servicing functions. (TR 136) Witness Dewhurst testified that the basic functions in the servicing arrangement are tightly bound up with the Company's day-to-day operations and that FPL would never intentionally default under the servicing agreement. (TR 136-137) When asked, witness Dewhurst could not provide any examples of why FPL would no longer be able to legally perform the servicer functions. (TR 136)

Staff witness Fichera testified that the proposed servicing agreement is essentially an agreement between affiliated parties with all the liabilities associated with the agreement falling to FPL ratepayers. (TR 1190) Because FPL shareholders do not directly bear the burden of issuance costs, including servicing fees, and because the economic burden of an increase in fees would be recognized through operation of the true-up mechanism, FPL ratepayers would be responsible for any increase in the servicing fee. (Dewhurst TR 1693; Fichera TR 1157) FPL witness Olson acknowledged that if FPL were to default as servicer, the servicing fee could increase from the proposed level of \$525,000 a year (annualized amount equal to 0.05 percent of the initial principal amount of the storm recovery bonds) to over \$6 million a year (0.6 percent of the initial principal amount) without the need for additional Commission approval. (TR 674)

Witness Fichera testified that commissions in other states have required the sponsoring utility acting as servicer to indemnify its ratepayers against an increase in the servicer fee in the event of default due to negligence, misconduct, or termination for cause. (TR 1157) FPL has suggested that the Commission could instead impose penalties on FPL for defaulting as servicer pursuant to Section 366.8260(15), Florida Statutes. (Dewhurst TR 1707) This provision allows the Commission to impose penalties pursuant to Section 366.095, Florida Statutes, or such other penalties as the Commission deems appropriate. Section 366.095, Florida Statutes, only authorizes the Commission to penalize a utility up to \$5,000 per occurrence for a violation of a statute or Commission rule or order. A fine of \$5,000 would be insufficient to compensate ratepayers for bearing up to \$5.5 million in additional annual costs due to default. (Fichera TR 1213; Dewhurst TR 1707; EXH 4, p. 267) Further, imposition of any penalty would likely require an adversarial proceeding.

In conclusion, requiring FPL to indemnify its ratepayers for any increase in the servicer fee caused by FPL's default properly puts the burden of the cost of default on the party whose actions would lead to default, rather than place the burden on the Commission to pursue through an adversarial proceeding penalties that may not sufficiently protect ratepayers. Therefore, the Commission should require the Company to indemnify ratepayers against an increase in the servicer fee in the event of the servicer's default due to negligence, misconduct, or termination for cause.

Issue 49: WITHDRAWN

Issue 50: What is the appropriate up-front and ongoing fee for the role of servicer throughout the term of the bonds?

Recommendation: The appropriate up-front servicer set-up fee is \$350,000. The appropriate ongoing servicer fee is 0.05 percent of the initial principal amount of the bonds. Based on the amount of storm recovery bonds FPL has proposed be issued, this fee would be \$525,000 per year. These fees are necessary to ensure an “arms-length” transaction for bankruptcy law considerations. (Springer, Slemkewicz)

Position of the Parties

FPL: To obtain the requisite bankruptcy opinions, FPL must be paid an amount that is deemed to cover its actual costs. FPL as the initial servicer should be paid its upfront costs incurred to make necessary system modifications to enable FPL to bill and collect the Storm Charges and an annualized amount equal to 0.05% of the initial principal amount of the storm-recovery bonds for the ongoing cost of servicing the bonds. This rate is at the lower end of a range of such fees that have been approved in other utility securitizations, and attempting to track actual costs likely would not be cost effective.

OPC: The appropriate up-front and ongoing fee for FPL’s role as the servicer throughout the term of the bond is the incremental cost to FPL for performing the servicer duties. The difference between the servicing fee necessary to create an arms-length transaction and FPL’s approved incremental costs should be used to increase the storm reserve available for recovery of future storm costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES’ ARGUMENTS

FPL’s form of servicing agreement provides up-front and ongoing fees for FPL’s role as servicer in the amount of \$350,000 and 0.05 percent (\$525,000), respectively. The intervenors concur that those amounts are appropriate to create an arms-length transaction, but assert that the difference between these amounts and the incremental cost of providing the services required by the agreement should be used to increase the storm reserve. Staff’s recommendation regarding the intervenors’ latter point is discussed in Issue 51.

ANALYSIS

The servicer calculates, bills, and collects storm recovery charges for the respective storm-recovery bonds on behalf of the Special Purpose Entity (SPE) and remits them to the bondholders' trustee. (Fichera TR 1155) Additionally, the servicer prepares, files, and processes the periodic Storm Bond Repayment Charge true-up adjustments. (Olson TR 673) These related duties are designed to ensure that collections are sufficient to timely satisfy the payment of principal and interest on the bonds as well as other ongoing costs. (Dewhurst TR 75; Fichera TR 1155) Periodically, the servicer will prepare reports detailing the results of remitting the collections to the trustee for deposit into the collection account. (Olson TR 673)

It is important for the servicer to be adequately compensated for the services it provides to create an "arms-length" relationship between FPL and the SPE. (Fichera TR 1155; Olson TR 674) This type of arrangement is a requirement of bankruptcy law to preserve the integrity of the bankruptcy-remote structure of the SPE and thus ensure the high credit quality of the bonds. (Fichera TR 1155; Olson TR 674) An upfront servicer set-up fee of \$350,000 and the ongoing servicer fee of 0.05 percent (\$525,000 annually) of the principal amount of the storm recovery bonds are the fees proposed by FPL for its role as servicer. (EXH 8) No party disagrees that FPL should be allowed to collect a servicing fee that is necessary to establish an arms-length transaction. (FPL BR at 131; FRF BR at 69; OPC BR at 85)

CONCLUSION

Staff recommends that the appropriate up-front and ongoing fees for FPL's role as servicer in the amount of \$350,000 and 0.05 percent of the principal amount of the storm recovery bonds, respectively. These fees were set to ensure an arms length transaction for bankruptcy law considerations between FPL and the SPE. The amounts FPL should be permitted to receive from ratepayers for its role as servicer are discussed in Issue 51.

Issue 51: How much should FPL be permitted to recover from ratepayers for its role as servicer in this transaction?

Recommendation: FPL should be permitted to collect the servicer set-up and on-going servicing fees that are necessary to establish an arms-length transaction for purpose of creating an independent SPE as discussed in Issue 50. FPL should be allowed to recover the \$350,000 servicer set-up fee it estimates would be necessary to adapt its existing systems to bill, collect, and process the storm charge and set up the reporting function. However, with respect to the on-going servicing fee, FPL should be allowed to keep only its incremental costs for performing the servicing function. Because FPL has not justified the \$525,000 annual fee it proposes to collect and because the activities appear to be extremely closely related to activities the Company already performs in the normal course of its operations, staff recommends the annual fee of 0.05 percent of the initial principal amount of the storm recovery bonds be used to increase the storm reserve available for recovery of future storm costs. (Maurey)

Position of the Parties

FPL: To obtain the requisite bankruptcy opinions, FPL must be paid an amount that is deemed to cover its actual costs. FPL should recover the up-front costs to bill and collect the Storm Charges and annual fees paid by the SPE under the servicing agreement. Separate tracking and identification of such costs is not likely to be cost effective; however, if FPL is required to do so, any excesses or deficiencies should be credited to or withdrawn from the Reserve.

OPC: FPL should be permitted to collect from ratepayers the servicing fee that is necessary to establish an arms-length transaction for purpose of creating an independent SPE. However, FPL should be allowed to keep only its approved incremental costs for servicing the bonds. The difference between the servicing fee necessary to create an arms-length transaction and any approved incremental costs should be used to increase the storm reserve available for recovery of future storm costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: Staff incorporates by reference the discussion under Issue 50 for a description of the servicer function and an explanation of why it is important to set the related fee at a level necessary to establish an arms-length transaction for bankruptcy law considerations. (Fichera TR 1155; Olson TR 674; EXH 4, p. 252) FPL witness Dewhurst testified that the activities of billing the customer, collecting the storm charge from the customer, accounting for the collections accurately, and making sure the funds are remitted to the SPE are “very tightly bound

up” with the Company’s day-to-day operations. (TR 115–119, 136–137) He also testified that FPL did not provide any analysis or support for the incremental cost of performing the servicer function. (TR 116–117) Finally, FPL witness Davis acknowledged that many of the activities involved in developing the storm charge and performing the servicer function are already done by FPL in the normal course of its operations. (TR 589–590; EXH 4, pp. 258, 264–266)

FPL provided support for the \$350,000 it estimates would be necessary to adapt its existing systems to bill, collect, and process the charge and set up the reporting function. (EXH 171, pp. 20-25; EXH 4, pp. 248–249) However, because FPL has not justified the \$525,000 annual fee it proposes to collect from ratepayers for performing the servicer function and because the servicer activities appear to be extremely closely related to activities the Company already performs in the normal course of its operations, staff recommends the annual fee of 0.05 percent of the initial principal amount of the storm recovery bonds be used to increase the storm reserve available for recovery of future storm costs.

Issue 52: What is the appropriate up-front and ongoing fee for the role of administrator throughout the term of the bonds?

Recommendation: The appropriate up-front and ongoing fee for the role of administrator should be \$125,000 per year. This fee is necessary to ensure an “arms-length” transaction for bankruptcy law considerations. (Springer, Slemkewicz)

Position of the Parties

FPL: To obtain the requisite bankruptcy opinions, FPL must be paid an amount that is deemed to cover its actual costs. FPL as Administrator should be paid the actual costs incurred to set up the SPE from bond proceeds and an annual fee of \$125,000 plus expenses to perform the administrative functions necessary to maintain the SPE. This amount is comparable to the administration fees paid in similar transactions. Attempting to track actual costs likely would not be cost effective.

OPC: The appropriate up-front and ongoing fee for FPL’s role as the administrator throughout the term of the bond is the incremental costs to FPL for performing the administrator duties. The difference between the administration fee necessary to create an arms-length transaction and FPL’s incremental costs should be used to increase the storm reserve available for recovery of future storm costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES’ ARGUMENTS

FPL’s form of administration agreement provides for an ongoing fee for FPL’s role as administrator in the amount of \$125,000 plus expenses on an annual basis. The intervenors concur that this amount is appropriate to create an arms-length transaction, but assert that the difference between the requested amount and the incremental cost of performing administrator duties should be used to increase the storm reserve.

ANALYSIS

FPL, in its role as administrator, establishes the SPE and performs the administrative duties necessary to maintain the SPE. (FPL BR at 133; Olson TR 674; OPC BR at 87) FPL estimates that the up-front costs to establish the SPE will be \$15,000, but is willing to be reimbursed for the actual costs incurred subject to Commission review subsequent to the

financing. (FPL BR at 133; EXH 8) However, FPL believes that the appropriate up-front and ongoing fee for the role of administrator is \$125,000 per year. (FPL BR at 133) Similar to the Servicing Agreement, bankruptcy law considerations require that the administration agreement reflect an arms-length transaction to ensure that the SPE is a bankruptcy remote entity. (Olson TR 674; FPL BR at 133) OPC has proposed that the administrator fee should be fixed at \$125,000 with no future increase of this amount through the true-up mechanism. (OPC BR at 87) All parties agree that FPL should be allowed to collect an administration fee of \$125,000 annually to allow for an arms-length transaction between FPL and SPE. (FPL BR at 133; FRF BR at 69; OPC BR at 87)

CONCLUSION

Staff recommends that the appropriate ongoing fee for the role of administrator should be \$125,000 per year. The amount FPL should be permitted to receive from ratepayers for its role as administrator is discussed in Issue 53.

Issue 53: How much should FPL be permitted to recover from ratepayers for its role as administrator in this transaction?

Recommendation: FPL should be permitted to collect the administration fee necessary to establish an arms-length transaction for purposes of creating an independent SPE as discussed in Issue 52. However, FPL should be allowed to keep only its incremental costs for performing the administration function. Since FPL has not provided or supported any incremental costs of performing this function, the full amount of the proposed \$125,000 annual administration fee should be used to increase the storm reserve available for recovery of future storm costs. (Maurey)

Position of the Parties

FPL: To obtain the requisite bankruptcy opinions, FPL must be paid an amount that is deemed to cover its actual costs. FPL should recover up-front costs incurred to establish the SPE and the annual fees paid by the SPE under the administration agreement. Separate tracking and identification for these expenses is not likely to be cost effective. If FPL is required to separately identify and track actual costs, any excesses or deficiencies should be credited to or withdrawn from the Reserve.

OPC: FPL should be permitted to collect from ratepayers the administration fee that is necessary to establish an arms-length transaction for purpose of creating an independent SPE. However, FPL should be allowed to keep only its approved incremental costs for administering the bonds. The difference between the administration fee necessary to create an arms-length transaction and approved incremental costs should be used to increase the storm reserve available for recovery of future storm costs.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: Staff incorporates by reference the discussion under Issue 52 for a description of the administration function and an explanation of why it is important to set the related fee at a level necessary to establish an arms-length transaction for bankruptcy law considerations.

FPL proposes an annual fee of \$125,000 for performing certain activities under the administration agreement. (EXH 8) FPL has not provided or justified any incremental costs it will incur for performing this function. (EXH 171, pp. 20–25; EXH 4, pp. 256–258, 265) In its brief, OPC argues “since FPL has not supported its incremental costs by the time of the hearing where those costs would be subject to examination, the full amount of the administration fee should be used to increase the storm reserve available for recovery of future storm costs.” (OPC

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BR at 89) Staff agrees with OPC on this point and recommends the Commission order FPL to pay the \$125,000 annual administration fee into the storm damage reserve.

Issue 54: STIPULATED: How frequently should FPL in its role as servicer be required to remit funds collected from ratepayers to the SPE?

Recommendation: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue: “FPL will remit funds deemed collected from customers to the SPE on a daily basis, pursuant to the terms of an agreement between FPL and the SPE. Any earnings on funds transferred will be used to reduce future charges.” Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue: “FPL will remit funds deemed collected from customers to the SPE on a daily basis, pursuant to the terms of an agreement between FPL and the SPE. Any earnings on funds transferred will be used to reduce future charges.” Staff recommends approval of this Stipulation.

Issue 55: In the event any amounts remain in the Collection Account after all storm recovery bonds have been retired, what should be the disposition of these funds?

Recommendation: Any amounts remaining in the Collection Account, and any additional storm recovery charges that have been incurred but not yet collected and deposited to the Collection Account, after all storm recovery bonds have been retired should be credited to current consumers' bills in the same manner that the storm charges were collected. However, if it is not cost effective to credit the remaining amount, the residual amount could either be applied to the storm reserve or returned to customers through a credit to the capacity clause. (Springer)

Position of the Parties

FPL: Upon repayment in full of the Storm Bonds and all related financing costs, any remaining amounts held by the SPE (exclusive of the amounts in the capital subaccount, representing the equity contribution, and any interest earnings thereon) should be remitted to FPL and added to the Reserve if the amount is insignificant and the process of applying a credit to customer rates is not cost effective due to customer billing program changes.

OPC: The amounts should be reflected as a credit on each customer’s bill as a refund allocated among customer classes in the same manner that the storm charges were collected.

FIPUG: The funds should be added to the storm reserve or refunded to FPL’s customers.

FRF: Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL requests that any amounts remaining in the collection account after all bonds have been retired be added to the storm reserve if the amounts are insignificant and to the point that crediting consumers' bills would not be cost effective due to customer billing program changes. (FPL BR at 134–135) The AG, AARP, and FRF agree with OPC that the remaining amounts should be reflected as a credit on each customer's bill allocated in the same manner the charges were collected. (OPC BR at 90) FEA agrees with FIPUG that the funds should be added to the storm reserve or refunded to FPL's customers. (FIPUG BR at 15)

ANALYSIS

FPL proposes that upon payment in full of the storm bonds and all related financing costs, if there are any remaining amounts held by the SPE (exclusive of the amounts in the capital subaccount, representing FPL's equity contribution, and any interest earning thereon) FPL will remit a like amount to the Reserve, or in the alternative, will allow a like amount to be applied as a credit to customer rates. (Davis TR 459) FPL proposes that any amount above \$10 million should be applied as a credit to customer rates if it is cost effective to do so, but that any amount below this threshold be added to the Reserve. (FPL BR at 134) OPC has proposed that any remaining amounts should be applied as a credit to each customer bill as a refund allocated among customer classes in the same manner that the storm charges were collected. (OPC BR at 90) It has been an accepted practice in other states to return excess revenues to consumers. This is consistent with a "best practice" to establish procedures that ensure all savings flow to ratepayers. (TR 1186) Staff believes this same treatment should apply to any additional storm recovery charges that have been incurred but not yet collected and deposited to the Collection Account as of the date when all storm recovery bonds have been retired. This can be accomplished by requiring the Collection Account be kept in place until all storm recovery charges have been collected.

CONCLUSION

Staff recommends that any amounts remaining in the Collection Account after all storm recovery bonds have been retired should be applied as a credit to each current customer in the same manner that the storm charges were collected. However, if it is not cost effective to credit the remaining amount, the residual amount could either be applied to the storm reserve or returned to customers through a credit to the capacity clause. This determination will be made when the bonds are retired and the amount is known. In addition, staff recommends the Collection Account be kept in place until all storm recovery charges have been collected.

Issue 56: How should the Commission determine that the upfront bond issuance costs are appropriate?

Recommendation: It is not necessary for the Commission to determine that FPL's estimated upfront bond issuance costs are appropriate at this time. In accordance with Section 366.8260(2)(b)5., Florida Statutes, FPL is required to file for the Commission's review actual bond issuance costs within 120 days after the bond issuance. In its review, the Commission must determine if such costs resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of the issuance and the terms of the financing order. If the Commission determines at that time that the estimated issuance costs included in the determination of the initial storm charge were overstated, the Commission should require FPL to increase the storm damage reserve by the amount of the difference in accordance with the statute. (Maurey)

Position of the Parties

FPL: In accordance with Section 366.8260(2)(b)5., Florida Statutes, within 120 days after the bond issuance, FPL shall file supporting information on the actual upfront bond issuance costs. The Commission shall review such costs to determine compliance with Section 366.8260(2)(b)5., Florida Statutes; however, if FPL has selected the lowest cost qualified provider for bond issuance services as a result of competitive solicitation, FPL should be deemed to have satisfied the statutory standard.

OPC: The Commission should adopt the "best practices" standard. The Commission's financial advisor should make an independent evaluation regarding lowest cost and that evaluation should be made available to the parties. If there is a dispute as to whether the lowest costs for the front costs were obtained based on the independent evaluation or other means, the matter should be brought before the Commission for resolution in the 120 day proceeding.

FIPUG: Adopts the position of OPC.

FRF: If the Commission determines to approve securitization, then the Commission should adopt the "best practices" standards applicable to reviewing and approving issuance costs.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: All of the upfront bond issuance costs proposed by FPL are estimates. (EXH 8). There is no statutory standard or requirement that the Commission pre-approve FPL's estimated upfront bond issuance costs. In addition, there is reason to believe certain of these estimated costs are subject to revision based on future negotiations during the structuring, marketing, and

pricing of the storm recovery bonds. (Olson TR 1494; EXH 167, pp. 23–24; Noel TR 1118–1123; Fichera TR 1178–1182)

Section 366.8260(2)(b)5., Florida Statutes, states

The Commission shall review such information [the actual issuance costs] to determine if such costs incurred in the issuance of the bonds resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of the issuance and the terms of the financing order. The Commission may disallow any incremental issuance costs in excess of the lowest overall costs by requiring the utility to make a contribution to the storm reserve in an amount equal to the excess of actual issuance costs incurred, and paid for out of storm-bond proceeds, and the lowest overall issuance costs as determined by the Commission.

Pre-approval of FPL's estimated bond issuance costs is not required, and in fact could impede the Commission in carrying out its statutory responsibility with regard to these costs.

To afford the Commission an opportunity to make an informed decision with regard to the reasonableness of the upfront bond issuance costs, the Commission should participate in the proposed transaction as discussed in Issue 74B. (Klein TR 1233–1236; Noel TR 1120–1123; Fichera TR 1185–1190; Olson TR 1480–1482) A cursory review of FPL's estimated upfront bond issuance costs shows that underwriting fees is the single largest line item cost. (EXH 8) There is evidence in the record that this cost may be overstated. (TR 1494; EXH 167, pp. 23–24) As part of the Commission's review of this cost, the competitive solicitation and selection of underwriters should be overseen by the Commission to ensure that the process is truly competitive and will result in the selection of transaction participants that have experience and ability to achieve an efficient and lowest cost transaction. (TR 1123; 1179–1181)

Rather than make a determination at this time regarding the appropriateness of FPL's estimated upfront bond issuance costs, staff recommends the Commission review the actual issuance costs as required by Section 366.8260(2)(b)5., Florida Statutes. If the Commission determines at that time that the estimated issuance costs included in the determination of the initial storm charge were overstated, the Commission should require FPL to increase the storm damage reserve by the amount of the difference in accordance with the statute.

Issue 57: How should the Commission determine that the on-going costs associated with the bonds are appropriate?

Recommendation: It is not necessary for the Commission to determine that FPL's estimated on-going costs associated with the storm recovery bonds are appropriate at this time. In accordance with Section 366.8260(2)(b)5., Florida Statutes, FPL is required to file for the Commission's review supporting information on actual bond issuance costs within 120 days after the bond issuance. In its review, the Commission must review the actual issuance costs to determine if such costs resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of issuance and the terms of the financing order. If the Commission determines at that time that the estimated costs included in the determination of the initial storm charge were overstated, the Commission should require FPL to increase the storm damage reserve by the amount of the difference in accordance with the statute. (Maurey)

Position of the Parties

FPL: FPL's testimony and exhibits provide support for the conclusion that FPL's estimated ongoing financing costs will be reasonable, and that they are consistent with similar rate reduction bond transactions.

OPC: The Commission should adopt the "best practices" standard. The actual on-going costs should be flowed through the storm-recovery bonds charged to ratepayers through a true-up mechanism. But FPL should be required to increase the storm-reserve for any on-going costs that do not meet the lowest costs standard and that are higher than the estimated on-going costs in this docket. On-going fees should be limited as described in the previous issues.

FIPUG: Adopts the position of OPC.

FRF: If the Commission determines to approve securitization, then the Commission should adopt the "best practices" standards applicable to reviewing and approving ongoing costs associated with the bonds.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: It is not necessary for the Commission to determine that the estimated on-going costs associated with the storm recovery bonds are appropriate at this time. Section 366.8260(2)(b)5., Florida Statutes, states:

The Commission shall review such information [the actual issuance costs] to determine if such costs incurred in the issuance of the bonds resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of the issuance and the terms of the financing order. The Commission may disallow any incremental issuance costs in excess of the lowest overall costs by requiring

the utility to make a contribution to the storm reserve in an amount equal to the excess of actual issuance costs incurred, and paid for out of storm-bond proceeds, and the lowest overall issuance costs as determined by the Commission.

Pre-approval of FPL's estimated on-going costs associated with the storm recovery bonds is not required, and in fact could impede the Commission in carrying out its statutory responsibility with regard to these costs.

In its brief, OPC contends FPL should be required to ensure that the on-going costs meet "the lowest overall costs based on market conditions" standard identified above. OPC continues that while the actual amount of on-going costs will be flowed through the true-up mechanism, if FPL fails to demonstrate that an increase in on-going fees meets the lowest cost standard, FPL should be required to apply any unjustified increase to the storm damage reserve for recovery of future storm costs. (OPC BR at 93-94)

To afford the Commission an opportunity to make an informed decision with regard to the reasonableness of the on-going costs associated with the storm recovery bonds, the Commission should participate in the proposed transaction as discussed in Issue 74B. (Klein TR 1233-1236; Noel TR 1120-1123; Fichera TR 1185-1190; Olson TR 1480-1482) Rather than make a determination at this time regarding the appropriateness of FPL's estimated on-going costs, staff recommends the Commission review the actual costs as required by Section 366.8260(2)(b)5., Florida Statutes. If the Commission determines at that time that the estimated costs included in the determination of the initial storm charge were overstated, the Commission should require FPL to increase the storm damage reserve by the amount of the difference in accordance with the statute. To the extent any on-going costs increase in the future (beyond the 120-day look-back review period), and FPL is unable to justify the increase to its flowing through the true-up mechanism, FPL should be required to increase the storm damage reserve by the amount of the excess.

Issue 58: Is FPL's process for determining whether the upfront bond issuance costs satisfy the statutory standard of Section 366.8260(2)(b)5., Florida Statutes, reasonable and should it be approved?

Recommendation: No. The Commission should not predetermine that upfront bond issuance costs resulting from a competitive solicitation, or within a certain range of estimates, meets the statutory standard of Section 366.8260(2)(b)5., Florida Statutes. Accordingly, FPL's proposed process should not be approved. (Maurey)

Position of the Parties

FPL: Yes, for the reasons explained with respect to Issue 56 above.

OPC: No. The process outlined by FPL in its petition, proposed order, and testimony, does not allow the active participation of the Commission. FPL's process does not afford independent protection for the ratepayers to ensure that the up-front costs, on-going costs, and interest rates achieve the lowest overall cost based on real time market conditions. Therefore, FPL's proposed process is not reasonable and should not be approved.

FIPUG: Adopts the position of OPC.

FRF: No. Because the process proposed by FPL in its filings does not provide for the active participation of the Commission, FPL's process does not afford adequate, independent protection for its customers with regard to up-front costs, issuance costs, ongoing costs, and interest rates. Accordingly, FPL's proposed process should not be approved.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The proposed process for determining whether the estimated upfront bond issuance costs satisfy the statutory standard articulated in FPL's position in Issue 56 is not reasonable and should not be approved. Contrary to FPL's position, a standard of documented expenditures falling within a range of estimates is not the standard articulated in Section 366.8260(2)(b)5., Florida Statutes. Moreover, a predetermination of reasonableness by the Commission would not provide the appropriate incentive to FPL to attain the lowest upfront bond issuance costs. (Fichera TR 1199-1202, 1205-1207, 1213-1215)

The Commission should not predetermine that upfront bond issuance costs resulting from a competitive solicitation, or within a certain range of estimates, meet the "lowest cost" standard of Section 366.8260(2)(b)5., Florida Statutes. Whether a competitive solicitation results in the lowest cost depends on how the solicitation is conducted and how negotiations that result from the solicitation are conducted. (Fichera TR 1175-1180) That determination can best be made through active oversight of the proposed transaction as discussed in Issue 74B. (Klein TR 1233-

1236; Noel TR 1120–1123; Fichera TR 1185–1190; Olson TR 1480–1482) In addition, as discussed in more detail in Issue 65, FPL should be required to demonstrate in the issuance advice letter that its competitive solicitation and negotiation process resulted in a package of fees and services that will result in the lowest cost consistent with prevailing market conditions and the terms of the financing order.

In conclusion, there is no statutory standard or requirement the Commission predetermine that FPL's upfront issuance costs resulting from a competitive solicitation, or within a certain range of estimates, are reasonable. Accordingly, FPL's proposed process for seeking Commission approval of its estimated upfront bond issuance costs is unnecessary and should not be approved.

Issue 59: Is FPL's process for determining whether the on-going costs satisfy the statutory standard of Section 366.8260(2)(b)5. reasonable and should it be approved?

Recommendation: No. FPL's proposed process for determining whether the estimated on-going costs associated with the issuance of the storm recovery bonds satisfy the statutory standard is inconsistent with the express language of Section 366.8260(2)(b)5., Florida Statutes, and should not be approved. (Maurey)

Position of the Parties

FPL: While the standard set in Section 366.8260(2)(b)5 does not apply to ongoing costs, FPL's testimony and exhibits provide support for the conclusion that FPL's estimated ongoing financing costs will be reasonable, and that they are consistent with similar rate reduction bond transactions.

OPC: No. The process outlined by FPL in its petition, proposed order, and testimony, does not allow the active participation of the Commission. FPL's process does not afford independent protection for the ratepayers to ensure the up-front costs, on-going costs, and interest rates achieve the lowest overall cost based on real time market conditions. Therefore, FPL's proposed process is not reasonable and should not be approved.

FIPUG: Adopts the position of OPC.

FRF: No. Because the process proposed by FPL in its filings does not provide for the active participation of the Commission, FPL's process does not afford adequate, independent protection for its customers with regard to up-front costs, issuance costs, ongoing costs, and interest rates. Accordingly, FPL's proposed process should not be approved.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: As discussed in Issues 56, 57, and 58, Section 366.8260(2)(b)5., Florida Statutes, explains the statutory requirement regarding Commission review of "the actual costs of the storm recovery bond issuance." This Section of the statute draws no distinction between upfront costs and on-going costs associated with the issuance of the storm recovery bonds. Moreover, there is no statutory standard requiring the Commission to pre-approve the estimated on-going costs associated with the issuance of the storm recovery bonds as requested by FPL. Approximately 75% of the estimated on-going fees are comprised of the servicing fee (discussed in Issue 50) and the administration fee (discussed in Issue 52). (EXH 8; EXH 171, pp. 40-43)

A determination by the Commission whether on-going costs associated with the issuance of the storm recovery bonds are reasonable can best be made through active oversight of the proposed transaction as discussed in Issue 74B. (Klein TR 1233-1236; Noel TR 1120-1123;

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Fichera TR 1185–1190; Olson TR 1480–1482) The statutory requirement is for Commission review of actual costs, not for Commission approval of estimated costs. Since there is no statutory standard or requirement that the Commission predetermine that FPL’s estimated on-going costs associated with the storm recovery bonds are reasonable, FPL’s proposed process for seeking Commission approval of these costs is unnecessary and should not be approved.

Issue 60: If the issuance of storm recovery bonds is approved, should the bonds be sold through a negotiated or competitive sale?

Recommendation: It is premature for the Commission to make this decision at this time. Both methods for the sale of storm recovery bonds should be considered to determine the most cost effective means of issuing the bonds based on prevailing market conditions near the time of issuance. However, based on the particular characteristics of these types of bonds and the method that has been used in previous transactions, both FPL and the Commission's financial advisor believe a negotiated sale will likely be preferable. (Springer)

Position of the Parties

FPL: Normally an assessment of whether bonds should be sold through a competitive bidding process or a negotiated sale would be made near the time of issuance based on factors such as issue size, complexity of issue, and current market conditions. Given the size of this offering, the risk premium that underwriters would require in a competitive bidding process would likely be greater than the underwriting fee in a negotiated sale. Therefore, a negotiated sale likely is preferable under the circumstances.

OPC: The methodology that is employed should be that which produces the lowest overall cost based on real time market conditions.

FIPUG: Adopts the position of OPC.

FRF: The sale method that produces the lowest overall cost based on real-time market conditions should be the method that is used to determine allowable costs. If the Commission allows FPL the discretion, after the Commission issues its order in this case, to decide which sale mechanism to use, then any such decisions by FPL must be subject to further prudence review, in subsequent proceedings in which all substantially affected parties have a point of entry.

AARP: No position at this time.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL proposes that a negotiated sale is preferable based on the fee for a higher risk premium that underwriters would require for a competitive sale compared to a lower underwriting fee for a negotiated sale. However, FPL proposes that this decision be made near the time of issuance based on factors such as issue size, complexity of issue, and current market conditions. The intervenors posit that the methodology employed should be that which produces the lowest overall cost based on real time market conditions. FRF proposes that if the

Commission grants FPL the flexibility to choose the methodology, that FPL should be subject to a prudency review in which all affected parties have a point of entry.

ANALYSIS

FPL Witness Dewhurst testified that “the decision as to which method may be preferable is dependent on factors such as issue size, complexity of issue, and current market conditions, some of which are not known with certainty.” (TR 76) FPL asserts that, given the size of this offering, underwriters would likely require a higher risk premium for a competitive sale as compared to the fee for a negotiated sale, thus a negotiated sale would be preferable. (FPL BR at 138) OPC states that the parties should be given some flexibility to choose the methodology that will result in the lowest overall costs to ratepayers based on market conditions, but that this flexibility is predicated on the Commission adopting the “best practices” standard and being active in the transaction. (OPC BR at 99) In his testimony, witness Noel states that all options should be evaluated, but that this issue should probably be sold through a negotiated offering. (TR 1117-1118) This is based on witness Noel’s evaluation that investor education is needed to inform investors of the unique characteristics of Florida’s first securitization issuance, the first issuance of storm recovery bonds, the effectiveness of the state’s pledge of safety, and the applicability of the true-up mechanism. (TR 1118)

CONCLUSION

Staff believes it is premature for the Commission to decide the manner in which the storm recovery bonds should be sold. Staff recommends both methods, competitive or negotiated sale, should be considered to determine the most cost effective means of issuing the bonds based on prevailing market conditions.

Issue 61: What additional terms, conditions or representations should be made in the financing order to enhance the marketability of the bonds and achieve the lowest possible cost?

Recommendation: The financing order should include ordering paragraphs, findings of fact, and conclusions of law that will give appropriate comfort to investors about the high quality of storm recovery bonds as a potential investment. Examples include:

1. A finding that the Commission anticipates stress case analyses will show that the broad nature of the State pledge under Section 366.8260(11), Florida Statutes, and the automatic true-up mechanism under Section 366.8260(2)(b)2.e. and 4., Florida Statutes, will serve to effectively eliminate for all practical purposes and circumstances all credit risk associated with the storm recovery bonds;

2. A finding and an ordering paragraph directing that the automatic true-up mechanism is to be applied at least semi-annually, as discussed in Issue 83;

3. A finding and an ordering paragraph that the automatic true-up mechanism will be implemented within 60-days after a filing by the servicer, as discussed in Issue 82;

4. A finding and conclusion of law that the broad nature of the State pledge under Section 366.8260(11), Florida Statutes, and the automatic true-up mechanism under Section 366.8260(2)(b)2.e. and 4., Florida Statutes, constitute a guarantee of regulatory action for the benefit of investors in storm recovery bonds;

5. A conclusion of law that any interest rate swap counterparty is to be treated as a “financing party” for purposes of Section 366.8260(1)(g), Florida Statutes;

6. A conclusion of law that storm recovery property is not a receivable under Section 366.8260(5)(a)1., Florida Statutes;

7. An ordering paragraph directing that partial payments shall be allocated first to storm recovery charges, including past due storm recovery payments;

8. A conclusion of law that the Commission’s obligation under the financing order relating to storm recovery bonds, including the specific actions the Commission guarantees to take, are direct, explicit, irrevocable, and unconditional upon the issuance of storm recovery bonds, and are legally enforceable against the Commission, a United States public sector entity; and

9. A conclusion of law and an ordering paragraph that the financing order is irrevocable under Section 366.8260(2)(b)4. and (11), Florida Statutes.

In addition, the financing order should require fully accountable certifications from the lead underwriter(s), FPL, and the Commission’s financial advisor that the actual structure, marketing, and pricing of the storm recovery bonds in fact resulted in the lowest storm recovery charges consistent with then-prevailing market conditions and the terms of the financing order and other applicable law. (Maurey)

Position of the Parties

FPL: No additional terms, conditions or representations are necessary. The utility asset-backed bond market is mature and highly liquid, and trading spreads are extremely tight. Issuing a financing order in substantially the form submitted by FPL will enable an efficient, low cost transaction. If the Commission wishes particular statements regarding the quality of the securities to be included in the offering documents, such statements should be included in the financing order as findings of fact or conclusions of law.

OPC: To enhance marketability of the bonds and to achieve the lowest overall cost to ratepayers, the "best practices" outlined in witness Fichera's testimony should be adopted. In addition, the bonds should be marketed broadly with active education regarding the nature of the bond issuance.

FIPUG: Staff witnesses have recommended criteria that will result in greater marketability and lower costs, these recommendations should be adopted, except the bonds cannot pledge the full faith and credit of the state or any local government.

FRF: The financing order should prescribe the ratepayer protections described in Staff witness Fichera's testimony, especially the provisions by which the Commission would be actively involved at all times and in all stages of the structuring, marketing, and pricing of the storm-recovery bonds.

AARP: No position at this time.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The Commission is being asked to use its regulatory authority in a way that has never been previously done in Florida. (Fichera TR 1198) To achieve the maximum benefits of the storm recovery financing under Section 366.8260, Florida Statutes, and to minimize the financial burden on ratepayers, FPL should include an accurate and complete description of the credit risk of this investment in the marketing materials and offering documents. (Noel TR 1126-1127)

The storm recovery bonds that will be issued for the recovery of reasonable and prudently incurred storm damage restoration costs and the replenishment of the storm damage reserve that are the subject of this proceeding are very different from the typical bonds issued by FPL. (TR 1120) The Commission is being asked to forego future regulatory oversight in order to create a financing instrument of superior quality and a completely separate credit from the sponsoring utility. (TR 1198) Section 366.8260, Florida Statutes, requires the Commission to issue an irrevocable financing order in which the sponsoring utility is insulated from any and all costs associated with the financing. (Klein TR 1229) The Commission is also required to approve a true-up mechanism that commits the Commission to periodically adjust the storm recovery charge that supports the storm recovery bonds to whatever level is necessary to pay the bonds'

principal and interest on time. (TR 1230) In addition, the State and the Commission are required to pledge to the bondholders never to take or permit any action to be taken that would interfere with their right to payment. The irrevocable nature of the financing order, the direct broad-based storm charge applied to all FPL ratepayers, the unconditional Commission guarantee to adjust the storm charge as necessary, and the explicit pledge of the State not to interfere with the bondholders' rights to repayment result in an incredibly strong credit independent of FPL. (TR 1159)

Another difference between typical FPL bonds and storm recovery bonds is the degree of Commission oversight after the issuance. In typical utility debt financings the Commission retains the right to disallow any costs for ratemaking purposes, including adjustments for the interest rate. For the proposed issuance of storm recovery bonds, while the issuance costs are subject to review under Section 366.8260(2)(b)5., Florida Statutes, FPL argues that the interest rate on the bonds is not an issuance cost and is not subject to Commission review. (EXH 4, p. 445) Without conceding to FPL's interpretation of Section 366.8260(2)(b)5., Florida Statutes, regarding whether Commission review extends to the interest rate, the statute does state "the Commission may not make adjustments to the storm recovery charges for any such excess issuance costs."

The final difference between typical utility bonds and storm recovery bonds is how these bonds impact the Company's financial position. In more typical debt offerings, FPL has a strong incentive to negotiate hard with underwriters for the lowest possible interest rates as well as the lowest possible underwriting fees. FPL also has a strong incentive to minimize other issuance costs. Between rate cases, the benefit from a low net cost of funds is enjoyed at least in part by FPL's shareholders and the detriment from a high net cost of funds is borne at least in part by these same shareholders. These same checks and balances do not exist for the issuance of storm recovery bonds. (TR 1120) While typical utility bonds directly impact FPL's financial ratios, storm recovery bonds are not direct obligations of FPL and are non-recourse to FPL. (TR 1147–1149) Storm recovery bonds will not be recognized in the determination of FPL's debt coverage or other financial ratios. For these reasons, the same incentives and consequences for pursuing a lowest cost of funds with regard to FPL's typical utility bonds are not present with respect to the proposed storm recovery bonds. (TR 1120) Unless the superior credit quality of these bonds is accurately reflected in the marketing materials, the storm recovery bonds will not achieve the lowest cost of funds. (TR 1126–1127)

While FPL concedes that attaining low total cost, including both upfront and on-going issuance costs, is the single most important objective in judging the success of a securitization issuance, the Company does not agree that a lowest cost standard under prevailing market conditions and consistent with the terms of the financing order is a necessary or permissible standard to apply to the proposed issuance of storm recovery bonds. (Dewhurst TR 1684–1686)

FPL argues that the Commission should not impose a lowest cost of funds standard in this docket because the Legislature considered and rejected such a standard. FPL states that an early House version of the securitization law included language that explicitly provided a lowest cost of funds standard,¹⁴ but that this language was removed in a subsequent House version,¹⁵

¹⁴ Committee Substitute 1 for House Bill 303, p. 11 of 32. (EXH 133)

¹⁵ Committee Substitute 2 for House Bill 303, p. 10 of 31. (EXH 134)

was not present in the Senate's companion bill (SB 1366), and did not survive the legislative process. (FPL BR at 142-143) Citing Section 366.8260(2)(b)2.b., Florida Statutes, FPL asserts that the Legislature instead chose to impose a standard requiring the Commission to "[d]etermine that the proposed structuring, expected pricing, and financing costs of the storm-recovery bonds are reasonably expected to result in lower overall costs or would avoid or significantly mitigate rate impacts to customers" FPL claims that a lowest cost of funds standard is inconsistent with this standard, thus it cannot be adopted by the Commission.

Section 366.8260(2)(b)2.a.-j., Florida Statutes, sets forth the matters that the Commission is required to address in a financing order issued to an electric utility. Subparagraph g. of this section provides that the Commission, in its financing order, shall "[s]pecify the degree of flexibility to be afforded to the electric utility in establishing the terms and conditions of the storm-recovery bonds, including, but not limited to, repayment schedules, *interest rates*, and other financing costs." (Emphasis added.) Further, subparagraph j. of this section provides that the Commission shall include in its financing order "any other conditions that the commission considers appropriate and that are not otherwise inconsistent with this section." These provisions clearly provide the Commission with the authority to establish and apply a lowest cost of funds standard with respect to the issuance of storm-recovery bonds.

Contrary to FPL's arguments, adopting a lowest cost of funds standard as a condition to the financing order is entirely consistent with the law. First, FPL has mistakenly identified the standard for reviewing the costs of this type of transaction. FPL suggests that the standard is whether the proposed structuring, expected pricing, and financing costs of the storm-recovery bonds are reasonably expected to result in lower overall costs or would avoid or significantly mitigate rate impacts to customers. This is not the standard for reviewing the costs of the transaction; rather, it is the standard by which the Commission must determine whether to issue a financing order at all.¹⁶ Notably, in the early House Bill cited by FPL, the standard asserted by FPL appears just prior to the "lowest cost" language FPL claims was rejected by the Legislature. (EXH 133) Accepting FPL's assertion, the early House Bill would have been at odds with itself because it would have included two different standards, side-by-side, for reviewing the same thing – cost of funds.¹⁷ Clearly, as demonstrated by the early House Bill, there can be a standard for judging cost of funds that is different from, but not inconsistent with, the standard for determining whether to issue a financing order at all.

¹⁶ See Section 366.8260(2)(b)1.b., Florida Statutes, which provides that "[t]he commission shall issue a financing order authorizing financing of reasonable and prudent storm-recovery costs, the storm-recovery reserve amount determined appropriate by the commission, and financing costs if the commission finds that the issuance of storm-recovery bonds and the imposition of storm-recovery charges authorized by the order *are reasonably expected to result in lower overall costs or would avoid or significantly mitigate rate impacts to customers* as compared with alternative methods of financing or recovering storm-recovery costs and storm-recovery reserve." (Emphasis added.)

¹⁷ Further, staff believes that the standard cited by FPL cannot be applied to cost of funds. FPL would have the Commission judge the cost of funds on the basis of whether the cost achieved is reasonably expected to result in lower overall costs, which leaves the obvious question: Lower than what? Or under FPL's analysis, the Commission could judge the cost of funds on the basis of whether the cost achieved is reasonably expected to mitigate rate impacts to customers, which again leaves the question: Mitigated as compared to what? These criteria are clearly at issue in determining whether to approve a financing order versus a more traditional surcharge, but cannot be applied with any meaning in judging cost of funds.

Second, FPL fails to point out that the “lowest cost” standard in the early House Bill was not eliminated. The early House Bill provided that in a financing order issued to a utility, the Commission was required, among other things, to “[e]nsure that the marketing, structuring, pricing, and financing costs of the storm recovery bonds will result in the lowest cost of the funds and the lowest storm recovery charges that are consistent with market conditions and the terms of the financing order.” (EXH 133) In the subsequent House version of the bill, this language was removed from subparagraph (2)(b)2. of the proposed law, but a “lowest cost” standard was added in subparagraph (2)(b)5. of the proposed law which provides for a post-issuance review of “the actual costs of the storm-recovery bond issuance.”¹⁸ The law as enacted retained the new language. The law provides for the Commission to determine if “the actual costs of the storm-recovery bond issuance . . . resulted in the *lowest overall costs* that were reasonably consistent with market conditions at the time of issuance and the terms of the financing order.”¹⁹ Staff believes this language provides evidence of the Legislature’s intent that the Commission ensure the transaction be conducted at the lowest cost.

FPL asserts in a conclusory fashion that interest rates on the storm-recovery bonds are not issuance costs under the securitization law and thus are not subject to the “lowest overall costs” criteria specified in subparagraph (2)(b)5. of the law. (FPL BR at 135). Yet the securitization law does not define “issuance costs,” and staff can find nothing in the law that supports the limited definition of issuance costs asserted by FPL.²⁰

Also puzzling about FPL’s resistance to the use of a lowest cost standard with regard to the issuance of its proposed storm recovery bonds is the fact that FPL’s financial advisor in this proceeding has provided this exact form of certification on the behalf of Credit Suisse as the underwriter for other recent transactions involving the issuance of similar ratepayer-backed bonds. (EXH 167, pp. 64–67) In the most recent ratepayer-backed bond transactions in Texas and New Jersey, the sponsoring utilities, the lead-underwriter (in each case Credit Suisse), and the respective Commission financial advisors (in each case Saber Partners), each issued a certification to the effect that the respective transaction achieved the lowest ratepayer charges consistent with market conditions and the terms of the applicable financing order. (EXH 167, pp. 64–67) FPL will receive the same amount of money from the issuance of storm recovery bonds regardless of the level of the interest rates or other issuance costs, and regardless of the degree of Commission involvement in the issuance process. (TR 1214) To minimize the financial burden on FPL’s ratepayers, staff recommends use of the same lowest cost standard and degree of

¹⁸ Committee Substitute 2 for House Bill 303, p. 13 of 31.

¹⁹ Section 366.8260(2)(b)5., Florida Statutes.

²⁰ Section 366.8260(1)(e), Florida Statutes, defines “financing costs” to include, among other things, “interest . . . payable on storm-recovery bonds” (subparagraph (1)(e)1.) and “any other cost related to issuing, supporting, repaying, and servicing storm-recovery bonds, including, but not limited to, servicing fees, accounting and auditing fees, trustee fees, legal fees, consulting fees, administrative fees, placement and underwriting fees, capitalized interest, rating agency fees, stock exchange listing and compliance fees, and filing fees, including costs related to obtaining the financing order” (subparagraph (1)(e)3.). Although “issuance costs” are not defined in the statute, FPL appears to define issuance costs as those items set forth in subparagraph(1)(e)3. (FPL BR at 135-137). Staff believes that this limited definition is not consistent with the language of the statute. The use of the word “other” to modify those costs “related to issuing, supporting, repaying, and servicing storm-recovery bonds” in subparagraph (1)(e)3. necessarily implies that the costs listed in prior subparagraphs, including interest as specified in subparagraph (1)(e)1., are also costs related to issuing, supporting, repaying, and servicing storm-recovery bonds. Hence, FPL’s definition of issuance costs fails to appreciate that the statute considers “interest payable on storm-recovery bonds” to be an issuance cost.

accountability for FPL's proposed transaction that has been successfully employed in ratepayer-backed bond transactions in these other recent ratepayer-backed bond transactions. (TR 1182, 1188, 1200-1202)

This said, having the principal transaction parties certify that they achieved the lowest cost under prevailing market conditions and consistent with the terms of the financing order with regard to the issuance of ratepayer-backed bonds by itself is not sufficient to ensure that ratepayers receive the greatest benefit of this special form of financing. (TR 1164) Unless the sponsoring utility is committed to pursuing a lowest cost transaction by accurately communicating the unique and high quality characteristics of the proposed ratepayer-backed bonds, the bonds will not trade at the spreads commensurate with the value and safety of these bonds. (TR 1126-1127; 1164) Despite an explicit lowest cost standard in the New Jersey statute, the results have not always been the lowest cost relative to the value of comparable securities. From 2001 - 2004, the utilities, underwriters, and the New Jersey Commission's financial advisors were allowed to place significant qualifications on the lowest cost standard in their certifications. Rather than being strictly held to a lowest cost standard in the certification process, the utilities and their underwriters were allowed to qualify certain aspects of their certifications with terms such as "reasonable" and other means to avoid accountability for their certifications. In contrast, for the 2005 transaction for the benefit of Public Service Electric & Gas (PSE&G), the New Jersey Commission and its financial advisor eliminated these provisions by adopting the Texas Commission financing order certification model. As shown on Exhibit 100, the spread for the 2005 PSE&G transaction was considerably tighter (i.e., less expensive to ratepayers) than any previous ratepayer-backed bond transaction completed in New Jersey. (TR 1126-1127; EXH 100)

To achieve the maximum benefits of the storm recovery financing under Section 366.8260, Florida Statutes, and to minimize the financial burden on ratepayers, FPL should include an accurate and complete description of the credit risk of the storm recovery bonds in the marketing materials and offering documents. (TR 1126-1127) To this end, the financing order should include ordering paragraphs, findings of fact, and conclusions of law that will give appropriate comfort to investors about the high quality of storm recovery bonds as a potential investment as described in the recommendation statement.

The securitization law provides many important protections for bondholders to enhance the marketability of the bonds and achieve a lowest cost transaction. Pursuant to Section 366.8260(11)(b), Florida Statutes, the state provides a pledge to bondholders to ensure its support of the bonds:

The state pledges to and agrees with bondholders, the owners of storm-recovery property, and other financing parties that the state will not:

1. Alter the provisions of this section which make the storm-recovery charges imposed by a financing order irrevocable, binding, and non-bypassable charges;
2. Take or permit any action that impairs or would impair the value of storm-recovery property; or

3. Except as allowed under this section, reduce, alter, or impair storm-recovery charges that are to be imposed, collected, and remitted for the benefit of the bondholders and other financing parties until any and all principal, interest, premium, financing costs and other fees, expenses, or charges incurred, and any contracts to be performed, in connection with the related storm-recovery bonds have been paid and performed in full.

The law further provides that any entity that issues storm-recovery bonds may include this pledge in the bonds and related documentation.²¹

After storm-recovery property has been transferred to an assignee or storm-recovery bonds have been issued (whichever comes first), the Commission's financing order becomes irrevocable and the Commission is not permitted to "amend, modify, or terminate the financing order" or "reduce, impair, postpone, terminate, or otherwise adjust storm-recovery charges in the financing order." Section 366.8260(2)(b)6., Florida Statutes.

There are only two conditions under which the financing order may be adjusted.²² First, storm-recovery charges will be adjusted either up or down on a periodic basis pursuant to a formula-based true-up mechanism approved in the financing order.²³ These adjustments "shall ensure the recovery of revenues sufficient to provide for the payment of principal, interest, acquisition, defeasance, financing costs, or redemption premium and other fees, cost, and charges in respect of storm-recovery bonds approved under the financing order." Section 366.8260(2)(b)4. As noted in Issue 83, this true-up mechanism should be used at least every six months. Application of the true-up mechanism is subject to review only for mathematical accuracy.²⁴ Second, at the utility's request, the Commission may conduct a proceeding and issue a new financing order that provides for retiring and refunding storm-recovery bonds issued under the original financing order if the Commission determines that the new order satisfies the statutory criteria for issuance of a financing order.²⁵ In that event, the Commission may adjust the related storm-recovery charges as appropriate upon retirement of the refunded bonds and issuance of the new bonds.

In addition, the Commission is required in a financing order to provide that "storm-recovery charges authorized in the financing order shall be paid by all customers receiving transmission or distribution service from the electric utility or its successors or assignees under commission-approved rate schedules or under special contracts, even if the customer elects to purchase electricity from an alternative electric supplier following a fundamental change in regulation of public utilities in the state."²⁶ Hence, regardless of a change in corporate structure or even a change in regulatory scheme, the securitization law provides for repayment of the bonds through non-bypassable charges.

²¹ Section 366.8260(11)(c), Florida Statutes.

²² Section 366.8260(2)(b)6., Florida Statutes.

²³ Section 366.8260(2)(b)4., Florida Statutes. See Issue 82 for discussion of the true-up mechanism.

²⁴ Id.

²⁵ Section 366.8260(2)(c), Florida Statutes.

²⁶ Section 366.8260(2)(b)2.c., Florida Statutes.

To enhance the marketability of the storm-recovery bonds, the Commission should find that the investor protections established through the above provisions – the irrevocable nature of the financing order, the broad nature of the state pledge, the required ongoing application of the true-up mechanism, and the required imposition of non-bypassable charges – constitute a guarantee of regulatory action for the benefit of investors in storm recovery bonds. (Fichera TR 1153–1154)

It is clear under the securitization law that such a guarantee does not make the state or the Commission liable in any way for repayment of the bonds. As noted in Section 366.8260(9), Florida Statutes, all storm-recovery bonds must provide a statement on their face to the effect that “Neither the full faith and credit nor the taxing power of the State of Florida is pledged to the payment of principal of, or interest on, this bond.”²⁷

In addition, based on the statutory provisions discussed above, the Commission should find that its obligations under the financing order relating to the storm recovery bonds, including the specific actions the Commission guarantees to take (i.e., implementation of the true-up mechanism and adherence to the state pledge), are direct, explicit, irrevocable, and unconditional upon the issuance of storm recovery bonds, and are legally enforceable against the Commission, a United States public sector entity. This finding will enhance the marketability of the bonds and help achieve the lowest possible cost by qualifying the bonds for a 20% risk weighting. A 20% risk weighting can help expand the market for these bonds to an international level, in turn increasing competition and lowering cost. (Fichera TR 1172; EXH 94) In making this finding, the Commission would not be guaranteeing repayment; as noted above, the securitization law makes clear that neither the state nor the Commission shall be liable in any way, directly or indirectly, for repayment of the bonds other than in the state’s capacity as a purchaser of electricity delivered by FPL. Rather, the Commission would find that its obligations under the securitization law are legally enforceable against it, but to no greater extent than those obligations would be legally enforceable absent a separate finding.

Finally, the financing order should require fully accountable certifications from the lead underwriter(s), FPL, and the Commission’s financial advisor that the actual structure, marketing, and pricing of the storm recovery bonds in fact resulted in the lowest storm recovery charges consistent with then-prevailing market conditions and the terms of the financing order and other applicable law. If the Commission determines that all required certifications have been delivered and that the transaction complies with the financing order and other applicable law, the transaction would proceed without any further Commission action, as discussed in Issue 74B. Staff believes that if the transaction proceeds on these terms, any costs, including interest, addressed in the lowest cost certifications likely would not need further review in the post-issuance review under Section 366.8260(2)(b)5., Florida Statutes.

²⁷ Section 366.8260(9), Florida Statutes.

Issue 62: Should all legal opinions and other transaction documents and subsequent amendments be filed and approved by the Commission before becoming operative?

Recommendation: All transaction documents and subsequent amendments should be reviewed and approved by the Bond Team as discussed in Issue 74B before becoming operative. All legal opinions associated with the proposed storm recovery bond transaction should be submitted to the Commission automatically without requiring the Commission to specifically request the documents. (Keating, Maurey)

Position of the Parties

FPL: Documents submitted with the Petition include a Storm-Recovery Property Sale Agreement, Administration Agreement, and Storm-Recovery Property Servicing Agreement, Indentures, and Limited Liability Company Agreement. The substance of the agreements should be approved in connection the financing order, subject to changes as part of the Commission Pre-Issuance Review Process. The agreements themselves require Commission approval of amendments. Forms of legal opinions should be delivered for review as requested by the Commission, but should not be subject to Commission approval.

OPC: Yes.

FIPUG: Adopts the position of OPC.

FRF: Yes.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: While it is reasonable to approve the general concept that certain legal opinions and other transaction documents will be necessary elements of the proposed transaction, the specific terms, conditions, covenants, warranties, representations, and specific language contained in the documents will be impacted by the Commission's decisions on other issues and must be reviewed in consideration of the financing order approved by the Commission.

The transaction documents that are the subject of this issue will have a meaningful impact on the structure, marketing, and pricing of the storm recovery bonds. (Fichera TR 1189–1190) The majority of the documents submitted to date for consideration in this proceeding are simply shells or templates of the actual documents. (EXH 33–39) In some cases, there is no substantive information for the Commission to actually consider and approve. (Appendices A and B to Exhibit B of FPL's petition) In other cases, the draft financing order as an example, staff will recommend the Commission make certain additions, deletions, and modifications before the documents become operative. (See discussion in Issues 61 and 74B) For these reasons, staff recommends that all transaction documents and any subsequent amendments be reviewed by the Bond Team and be approved before any of the documents become operative. (TR 1187–1190)

With respect to legal opinions regarding the storm recovery bond transaction, staff recommends the Commission require FPL to submit these opinions automatically to staff without the need for the Commission or its staff to specifically request the documents. (FPL BR at 146) In addition, as part of the review process discussed in Issue 74B, it is recommended that FPL and the Commission (the Bond Team) employ a competitive process in selecting, among equally qualified firms, the various law firms that will ultimately be required for the documentation, marketing, and execution of the proposed financing. (EXH 132, p. 2) Finally, FPL attempts to distinguish legal opinions from other transaction documents and says such opinions do not require Commission approval. (FPL BR at 147) Staff does not agree with FPL on this point. Staff recommends that any transaction documents or legal opinions that will have an impact on the structure, marketing, and pricing of the storm recovery bonds be reviewed and approved by the Bond Team before becoming operative as discussed in Issue 74B.

Issue 63: Is FPL's proposed Staff Pre-Issuance Review Process reasonable and should it be approved?

Recommendation: No, FPL's proposed staff pre-issuance review process is not reasonable as filed and should not be approved. For the reasons outlined below, the pre-issuance review process discussed in Issue 74B should be approved. (Maurey)

Position of the Parties

FPL: Yes. FPL believes that the proposed Staff Pre-Issuance Review process will enable the Commission, through its Staff, to ensure that any issuance of bonds pursuant to the financing order is in compliance with that Order. If the Commission wishes to take a more active role in the pre-issuance process, it should adopt a procedure consistent with FPL's proposal submitted in response to new sub-issue (b) under Issue 74.

OPC: No. The process outlined by FPL in its petition, proposed order, and testimony, does not allow the active participation of the Commission. FPL's process does not afford independent protection for the ratepayers to ensure that the up-front costs, on-going costs, and interest rates achieve the lowest overall cost based on real time market conditions. Therefore, FPL's proposed process is not reasonable and should not be approved.

FIPUG: Adopts the position of OPC.

FRF: No. Because the process proposed by FPL in its filings does not provide for the active participation of the Commission, FPL's process does not afford adequate protection for its customers with regard to up-front costs, issuance costs, ongoing costs, and interest rates. Accordingly, FPL's proposed process should not be approved.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: FPL has made significant movement with respect to making the proposed storm recovery bond transaction more transparent. From its initial proposal of filing certain documents 30 days in advance and the issuance advice letter five days in advance of the launch date (Olson TR 683-684), the Company has now agreed to the formation of a "bond team" comprised of the Commission and/or staff plus their outside legal counsel and financial advisors to work with the utility, the underwriters, and their respective counsels. (Olson TR 1480-1482) However, there continue to be key differences of opinion regarding how ratepayers' interests will be represented in the actual pricing of the storm recovery bonds, the appropriate standard to apply in determining a successful transaction, and the degree of accountability for the outcome of the transaction. The first point is discussed in Issue 74B. The latter two points are discussed in Issue 61. To afford the Commission an opportunity to make an informed decision with regard to

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the reasonableness of the issuance of storm recovery bonds, the Commission should participate in the proposed transaction as discussed in Issue 74B. (Klein TR 1233–1236; Noel TR 1120–1123; Fichera TR 1185–1190; Olson TR 1480–1482)

Issue 64: Should the Financing Documents be approved in substantially the form proposed by FPL, subject to modifications as addressed in the draft form of financing order?

Recommendation: No. While it is reasonable to approve the general concept that the financing documents will be necessary elements of the proposed transaction, the specific terms, conditions, covenants, warranties, representations, and specific language contained in the documents will be impacted by the Commission's decisions in other issues and must be reviewed in consideration of the financing order approved by the Commission as discussed in Issue 74B. (Maurey)

Position of the Parties

FPL: Yes. Documents submitted with the Petition include a Storm-Recovery Property Sale Agreement, Administration Agreement, and Storm-Recovery Property Servicing Agreement, Indentures, and Limited Liability Company Agreement. The substance of the agreements should be approved in connection the financing order, subject to changes as part of the Commission Pre-Issuance Review Process. The agreements themselves require Commission approval of amendments. Forms of legal opinions should be delivered for review as requested by the Commission, but should not be subject to Commission approval.

OPC: No position.

FIPUG: FIPUG supports the testimony of Staff witness Fichera.

FRF: If the Commission approves recovery through securitization, the Financing Documents should incorporate, to the extent applicable and practicable, the "best practices" and "financing order recommendations" set forth in Staff witness Fichera's testimony.

AARP: No position.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The financing documents that are the subject of this issue are referenced in FPL's position above. While it is reasonable to approve the general concept that the financing documents will be necessary elements of the proposed transaction, the specific terms, conditions, covenants, warranties, representations, and specific language contained in the documents will be impacted by the Commission's decisions in other issues and must be reviewed in consideration of the financing order approved by the Commission. (TR 1186-1187) In addition, FPL notes in its brief that the financing documents shall be subject to additions, deletions, and modifications as may be necessary subject to negotiations regarding the structure, marketing, and pricing of the storm recovery bonds. (FPL BR at 147-148)

It would be premature for staff to spend a large block of time reviewing and making recommendations for substantive changes to the transaction documents until the Commission has issued its financing order in this docket, providing guidance on what terms will be appropriate

for these transaction documents. Thus, it would be inappropriate for the Commission's financing order to approve the transaction documents in substantially the form filed by FPL. Rather, the financing order should authorize FPL and the SPE to enter into the required transaction documents (e.g., the indenture, the storm recovery property sale agreement, the servicing agreement, the administration agreement, and the LLC agreement), but leave the terms of those transaction documents to be approved by the Commission's designated personnel and financial advisor taking into account the requirements of the financing order. For these reasons, staff recommends the Commission approve the general concept of the financing documents but reserve final approval of the actual language until such time the Commission, its staff, its outside counsel, and financial advisor has had an opportunity to review the proposed financing documents relative to the financing order issued by the Commission. Approval of these documents should occur during the review process discussed in Issue 74B.

Issue 65: Should the Issuance Advice Letter be approved in substantially the form proposed by FPL?

Recommendation: No. The draft issuance advice letter in the form proposed by FPL does not provide sufficient detail for the Commission to make an informed decision regarding the proposed storm recovery bond issuance. (Maurey)

Position of the Parties

FPL: Yes. The draft issuance advice letter will provide the most current and up-to-date information concerning the final terms and conditions that only becomes available as the launch date for a bond series becomes very near.

OPC: No position.

FIPUG: FIPUG supports the testimony of Staff witness Fichera.

FRF: No position.

AARP: No position.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: FPL has proposed filing a draft issuance advice letter at least five days prior to the expected launch date for the sale of the storm recovery bonds. (Olson TR 683) The draft issuance advice letter proposed by FPL will reflect the preliminary bond structuring information for the proposed issuance, the expected and final maturities, over-collateralization levels, any other credit enhancements, and revised estimates of the upfront bond issuance costs proposed to be financed from proceeds of the bonds and estimates of debt service and other on-going costs for the first collection period. (TR 683)

The Commission should require FPL to file the issuance advice letter (IAL) and initial true-up letter (combined into one document) in draft form at least two weeks prior to pricing based upon the best information available at that time, and in final form on the day of pricing or within one business day of pricing. (Fichera TR 1191-1194; 1216) In addition, the final IAL should contain detailed analyses and representations regarding the actual structuring, marketing, and pricing of the bonds, as well as the initial storm recovery charges. (Klein TR 1233) In addition to the information suggested by FPL for inclusion in the IAL, other factors that should be addressed include the actions taken by the Company in the marketing of the bonds; a comparison of the pricing relative to an independent benchmark versus other similar securities historically and at the time of pricing; the amount of orders received and from whom; and other factors the Commission, its staff, and its financial advisor consider in their expert judgment to be necessary. (TR 1234) Finally, the IAL should include certifications from FPL, from the underwriters, and from the Commission's financial advisor that the structuring, marketing, and pricing of the storm recovery bonds resulted in the lowest cost of funds consistent with

prevailing market conditions and the terms of the financing order. (TR 1233–1234) The portion of this filing relating to the initial true-up letter is discussed in Issue 66.

The IALs filed in numerous successful Texas securitization transactions provide the Texas Commission with this level of detail. (TR 1240–1241; EXH 101) In contrast, the draft IAL as proposed by FPL is a simple summary of the key terms of the transaction. (Appendix A to Exhibit B of FPL’s petition) To afford the Commission an opportunity to render an informed decision regarding the outcome of the proposed storm recovery bond issuance, staff recommends the Commission require FPL to file an IAL with sufficient representations and detailed analyses to demonstrate that the parties took all reasonable steps to produce the lowest cost transaction consistent with prevailing market conditions and the terms of the financing order. The proposed draft issuance advise letter filed by FPL is not sufficient.

Issue 66: Should the Initial True-up Letter be approved in substantially the form proposed by FPL?

Recommendation: No. While it is reasonable to approve the true-up mechanism proposed by FPL, if the Commission adopts staff's recommendation that the issuance advice letter be expanded to include the initial storm recovery charges, there should be no need for a separate initial true-up letter. (Maurey)

Position of the Parties

FPL: Yes. The Initial True-up letter as proposed by FPL will provide Staff, acting at the Commission's direction, information necessary to ensure that any proposed issuance complies with the financing order.

OPC: No position.

FIPUG: FIPUG supports the testimony of Staff witness Fichera.

FRF: No position.

AARP: No position.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The initial true-up letter provides the projected initial storm bond repayment charges and storm bond tax charges for each customer class resulting from the preliminary bond structuring information and the application of the formula approved in the financing order. The initial true-up letter also includes the draft tariff sheets implementing the storm recovery charges. (Olson TR 683-684)

In Issue 82, staff recommends certain additions to FPL's proposed true-up mechanism filing to provide staff with the additional information necessary to conduct a timely review of FPL's future true-up filings. While it is reasonable to approve the true-up mechanism proposed by FPL, if the Commission adopts staff's recommendation in Issue 65 that the issuance advice letter be expanded to include the initial storm recovery charges, there should be no need for a separate initial true-up letter. (Fichera TR 1186)

Issue 67: How should the Commission ensure that the structure, marketing, and pricing of the storm recovery bonds result in the lowest possible burden on FPL's ratepayers?

Recommendation: The ratepayers should be effectively represented throughout the life cycle of the proposed transaction. The Commission can ensure the structure, marketing, and pricing of the storm recovery bonds resulted in the lowest possible burden on FPL's ratepayers consistent with prevailing market conditions and the terms of the financing order by participating in the transaction as discussed in Issue 74B. (Maurey)

Position of the Parties

FPL: A financing order in the form submitted with the Petition, including the proposed findings of fact and conclusions of law, contains provisions consistent with the statute and necessary to facilitate triple-A credit ratings, providing the requisite investor confidence in the storm-recovery bond issuance, and resulting in an efficient and cost-effective financing. If the Commission wishes to take an active role in directing and overseeing the issuance process, it should employ the approach recommended by FPL in response to sub-issue 74(b).

OPC: The Commission should adopt the "best practices" standard which includes active participation by the Commission, its staff, and financial advisors in the bond issuance process.

FIPUG: Adopts the position of OPC.

FRF: If the Commission determines to approve securitization, then the Commission should adopt the "best practices" standard.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: The ratepayers should be effectively represented throughout the life cycle of the proposed transaction when information and options are being evaluated and decisions are being made that impact the ultimate cost to ratepayers. It is difficult, if not impossible, to evaluate such decisions after the fact. (Fichera TR 1198-1202; Klein TR 1232-1234) The Commission can ensure the structure, marketing, and pricing of the storm recovery bonds resulted in the lowest possible burden on FPL's ratepayers consistent with prevailing market conditions and the terms of the financing order by including findings of fact, conclusions of law, and ordering paragraphs in the financing order as discussed in Issues 61 and 74B; by participating in the transaction review process as discussed in Issue 74B; and by insisting on accountability of the principal transaction parties by requiring lowest cost certifications as discussed in Issue 65.

Issue 68: Is the “proposed structure, expected pricing and financing costs of the storm-recovery bonds reasonably expected to result in lower overall costs or avoid or significantly mitigate rate impacts to customers as compared with alternative methods of recovery?”

Recommendation: As discussed in Issue 39, the proposed structure, expected pricing, and financing costs of the storm recovery bonds cannot be expected to result in lower overall costs to ratepayers as compared with alternative methods of recovery of reasonable and prudently incurred storm damage restoration costs and replenishment of the storm damage reserve. However, issuance of storm recovery bonds is reasonably expected to mitigate rate impacts to customers as compared with alternative methods of recovery. By adopting the processes recommended in Issues 61, 65, and 74B, the Commission can maximize the rate mitigation impact of securitization. (Maurey)

Position of the Parties

FPL: Yes. This statutory standard adopted by the legislature in Section 366.8260(2)(b)2.b., Florida Statutes (2005), is met by FPL’s proposal, a primary benefit of which is to immediately replenish the Reserve and to “smooth out” the significant rate impact of an extreme sub-period of storm activity, making it a useful tool for recovery of existing deficits and replenishment of the Reserve.

OPC: Yes, but only if the Commission takes an active role in the bond issuance process and does not approve FPL’s proposed methodology. To ensure that the issuance of storm-recovery bonds results in the lowest overall costs to ratepayers compared with the alternative methods of financing, the “best practices” outlined in Commission staff witness Fichera’s direct testimony should be adopted including active participation by the Commission, its staff, and financial advisors which ensures ratepayer protection.

FIPUG: No. FIPUG supports a 3 year surcharge, which will provide considerable savings to customers on interest, taxes and financing costs.

FRF: No. Without the ratepayer protections, including the "best practices," described in Staff witness Fichera's testimony, the proposed structure, pricing, and financing costs cannot be reasonably expected to provide appropriate and available benefits to FPL's ratepayers.

AARP: Agree with OPC.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: As discussed in Issue 39, the proposed structure, expected pricing, and financing costs of the storm recovery bonds cannot be expected to result in lower overall costs to ratepayers as compared with alternative methods of recovery of reasonable and prudently incurred storm damage restoration costs and replenishment of the storm damage reserve. However, issuance of storm recovery bonds is reasonably expected to mitigate rate impacts to

customers as compared with alternative methods of recovery. (Dewhurst TR 113–114) By adopting the processes recommended in Issues 61, 65, and 74B, the Commission can maximize the rate mitigation impact of securitization. (Fichera TR 1198–1202) To provide the Commission with the access necessary to make informed decisions with regard to the structure, marketing, and pricing of the storm recovery bonds and to ensure ratepayer interests are effectively represented throughout the life cycle of the transaction, the Commission should participate in the proposed transaction as discussed in Issue 74B. (Klein TR 1233–1236; Noel TR 1120–1123; Fichera TR 1185–1190; Olson TR 1480–1482)

Issue 69: WITHDRAWN

Issue 70: WITHDRAWN

Issue 71: What flexibility should FPL be afforded in establishing the terms and conditions of the storm recovery bonds, including, but not limited to, repayment schedules, interest rates, and other financing costs, as well as the use of floating rate securities, interest rate swaps, and call provisions?

Recommendation: FPL and the Commission should work together in a collaborative process to allow for flexibility by the principal transaction parties (Bond Team) to ensure that the lowest overall costs consistent with prevailing market conditions and the terms of the financing order are achieved. (Maurey)

Position of the Parties

FPL: FPL should be afforded flexibility described in the proposed financing order including: issue bonds in one or more series and tranches; reduce the amount of issuance if necessary to maintain the initial average retail charge below the current storm surcharge; recover certain costs through the storm charge subject to true-up; utilize floating rate securities and interest rate swaps; change the amortization period up to one year to accommodate market preferences; and include call provisions.

OPC: The Commission and FPL should work together in a collaborative process as described in the “best practices” standard to allow for flexibility by the parties to ensure that the lowest overall costs are obtain for the benefit of the ratepayers.

FIPUG: Adopts the position of OPC.

FRF: Agree with OPC. Additionally, the Commission should ensure that any post-approval exercise of flexibility is demonstrated, in appropriate proceedings that afford substantially affected parties a point of entry, to provide real, measurable benefits to customers, and that FPL's customers are protected from any adverse consequences of imprudent FPL decisions pursuant to allowed flexibility.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: FPL and the Commission should work together in a collaborative process to allow for flexibility by the principal transaction parties (Bond Team) to ensure that the lowest overall costs consistent with prevailing market conditions and the terms of the financing order are achieved. (Olson TR 1480; Klein TR 1232–1233) A general framework for this collaborative process is discussed in Issue 74B.

Issue 72: STIPULATED: If the Commission approves FPL's proposed financing order, should FPL be allowed to establish a regulatory asset for the amount to replenish the Reserve?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: "Yes." All Intervenors maintained "no position" on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation. A regulatory asset should be established for the amount to replenish the Reserve if the Commission approves FPL's proposed financing order.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: "Yes." All Intervenors maintained "no position" on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation. A regulatory asset should be established for the amount to replenish the Reserve if the Commission approves FPL's proposed financing order.

Issue 73: STIPULATED: Should the Commission authorize FPL to establish a separate regulatory asset for the storm recovery property sold to the SPE and a separate regulatory asset for income taxes payable on the storm recovery costs to be financed?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: "Yes." All Intervenors maintained "no position" on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation. The Commission should authorize FPL to establish a separate regulatory asset for the storm recovery property sold to the SPE and a separate regulatory asset for income taxes payable on the storm recovery costs to be financed.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: "Yes." All Intervenors maintained "no position" on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation. The Commission should authorize FPL to establish a separate regulatory asset for the storm recovery property sold to the SPE and a separate regulatory asset for income taxes payable on the storm recovery costs to be financed.

Issue 74: Based on resolution of the preceding issues, should a financing order in substantially the form proposed by FPL be approved, including the findings of fact and conclusions of law as proposed?

Recommendation: No. The form of the financing order, including the findings of fact and conclusions of law, proposed by FPL should be revised to reflect resolution of all issues in this proceeding. (Maurey, Keating)

Position of the Parties

FPL: Yes. The proposed financing order, including the findings of fact and conclusions of law, contains provisions consistent with the statute and necessary to facilitate AAA credit ratings, providing the requisite investor confidence, and resulting in an efficient and cost-effective financing. FPL's financing order provides the Commission with flexibility to be involved in every critical step of the process; however, if the Commission decides to take a direct and active role, it should adopt measures outlined in sub-issue 74(b).

OPC: No, the financing order needs to reflect the Commission's decision in this proceeding including findings of fact and law.

FIPUG: Adopts the position of OPC.

FRF: No. Agree with OPC that, assuming that the Commission approves securitization such that a financing order is needed, the financing order needs to reflect the Commission's decisions in this proceeding, including findings of fact and conclusions of law.

AARP: The same as the Office of Public Counsel.

FEA: Agree with OPC.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: This is a fall-out issue based on decisions rendered in other issues. Please see Issues 61 and 74B for a discussion of the terms, conditions, representations, findings of fact, conclusions of law, and ordering paragraphs staff recommends the Commission include in the financing order.

Issue 74A: If the Commission votes to issue a financing order, what special procedures (if any) should be used after the Commission vote and before the issuance of the financing order to ensure that the order accurately reflects the Commission's decision and meets the anticipated requirements of the financial community?

Recommendation: The Commission staff should hold an informal meeting with the parties and their financial advisors during the week of May 22, 2006, to review and obtain input on the portions of the financing order relating to securitization. Any party who believes that the order as issued does not accurately and properly reflect the Commission's decisions has the right to request reconsideration within 5 days after issuance of the order. (Keating, Maurey)

Position of the Parties

NOTE: Only OPC stated a separate position on this sub-issue. The position stated for FPL represents staff's synopsis of its discussion of the sub-issue.

FPL: Commission staff should provide FPL with a mark-up of the proposed form of financing order (exclusive of provisions that relate strictly to the prudence issues in this case) on or before May 18. The parties should participate in an informal meeting in Tallahassee on May 22, and if necessary with the Prehearing Officer on May 23, to resolve any disputed issues and work to achieve a financing order than minimizes potential conflict. Any issues that cannot be separately resolved by the parties shall be resolved by the Prehearing Officer.

OPC: Commission should hold at least one informal meeting of the parties after the Commission vote and prior to the issuance of the financing order to ensure that the financing order meets all requirements. A draft of the order should be provided to the parties for their comments. Any disputes should be addressed by the Commission at an Agenda Conference.

FIPUG: No position.

FRF: No position.

AARP: No position.

FEA: Agree with OPC.

AG: No position.

Staff Analysis: The customary practice in Commission dockets is for staff to prepare a final order reflecting the Commission's decisions without further input from the parties. In this case, the precise wording chosen to reflect the Commission's decisions regarding the securitization portions of the order may affect FPL's ability to issue securitized bonds on the most favorable terms. Staff, therefore, recommends a collaborative process in which staff, the parties, and their financial advisors and legal counsels would hold an informal meeting during the week of May 22, 2006, to review a draft of the securitization portions of the financing order prior to its issuance.

Staff believes that the Commission's normal post-order procedures for reconsideration and/or clarification provide sufficient opportunity for any party who is concerned about the specific language of the financing order to seek review by the full Commission. By statute, the deadline for filing petitions for reconsideration in securitization proceedings is 5 days after the issuance of the financing order. (Section 366.8260(2)(b)1.b., Florida Statutes) The financing order is scheduled to be issued on Tuesday, May 30, 2006. Under Rule 28-106.103, Florida Administrative Code, when the period of time allowed for an action by any applicable statute is less than 7 days, intermediate Saturdays, Sundays and legal holidays are excluded from the computation. Thus, the deadline for petitions for reconsideration and/or clarification will be Tuesday, June 7, 2006.

Issue 74B: If the Commission votes to issue a financing order, what post-financing order regulatory oversight is appropriate and how should that oversight be implemented?

Recommendation: The ratepayers should be effectively represented throughout the proposed transaction. The Commission, its staff, its outside counsel, and its financial advisor, along with FPL, FPL's financial advisor, and its counsel should work in a collaborative process to ensure the structuring, marketing, and pricing of the storm recovery bonds result in the lowest cost consistent with prevailing market conditions and the terms of the financing order. The Commission should be represented primarily by its staff, who should be advised by the Commission's financial advisor and outside counsel. Staff should periodically brief the Commissioners and the parties on the progress of the transaction. Issues that arise during the process that cannot be resolved collaboratively should be submitted in writing to a designated Commissioner for guidance. If any party objects to the designated Commissioner's proposed resolution, the matter should be submitted to the Commission for *de novo* consideration. The final structure of the transaction, including pricing, should be subject to review by the full Commission for the limited purpose of ensuring that all requirements of law and the financing order have been met. The Commission should specifically determine that the fees and expenses of its financial advisor and outside counsel in this post-financing order collaborative process are entitled to payment from the bond proceeds. (Maurey, Keating)

Position of the Parties

NOTE: Only OPC stated a separate position on this sub-issue. The positions stated for FPL and FEA represent staff's synopsis of their discussion of the sub-issue.

FPL: FPL and the Commission should designate the members of a "bond team." The Commission should be represented on the bond team by the Prehearing Officer, who may be advised by the Commission's staff and financial advisor. The bond team should expect to meet by conference call no less than weekly. Any disputes relative to the transaction documents or the issuance, structuring, marketing, and pricing process that the Commission has reserved the authority to resolve shall be heard by the Prehearing Officer. Any party represented on the bond team should have the opportunity to have the Prehearing Officer's decision reviewed *de novo* by the full Commission.

OPC: Commission should take an active role in the issuance process. Parties should receive periodic updates on the status of the transaction through designated Commission staff. The Commission should retain final decision making authority. Any disputes should be addressed by the Commission either at an Agenda Conference with shortened recommendation filing as necessary or through the use of a designated Commissioner as a hearing officer. Parties should be provided a point of entry if there are future disputes.

FIPUG: No position.

FRF: No position.

AARP: No position.

FEA: Agree with OPC.

AG: No position.

Staff Analysis:

Procedural Options for Active Commission Participation

There are a number of potential options for Commission participation in the review and approval of the final transaction documents and in the collaborative process for structuring, marketing and pricing of the storm recovery bonds. Staff believes that the option selected should balance the need for an efficient process that does not unduly delay the issuance of the bonds with the need to ensure that ratepayer interests are adequately protected. If the Commission decides to use the “Bond Team” approach, there are three basic decisions to be made:

Decision 1: Who should participate on behalf of the Commission in day-to-day activities of the Bond Team? Options include:

- the Commission staff, financial advisor and counsel
- a designated Commissioner, staff, financial advisor and counsel
- a panel of Commissioners, staff, financial advisor and counsel
- the full Commission, staff, financial advisor and counsel

Staff recommends that day-to-day participation should be through the Commission staff, advised by the Commission’s financial advisor and counsel. Due to the anticipated frequency of meetings and/or conference calls, staff believes it is impractical for one or more Commissioners to participate in light of other demands on Commissioners’ time. In addition, notice requirements under the Sunshine Law could delay the process if a panel of Commissioners (or the full Commission) is designated to participate. If staff’s recommendation is adopted, staff can brief Commissioners on the progress of the transaction at whatever frequency individual Commissioners desire.

Decision 2: What process should be used to resolve any issues on which the Bond Team members are unable to reach agreement? Options include:

- decision by the Commission staff and/or financial advisor acting pursuant to authority delegated in the financing order, subject to *de novo* review by the full Commission
- decision by a designated Commissioner, subject to *de novo* review by the full Commission
- decision by a panel of Commissioners, subject to *de novo* review by the full Commission
- decision by the full Commission

Staff recommends that any issue that the Bond Team participants are unable to resolve should initially be presented in writing for resolution by a designated Commissioner, subject to *de novo* review by the full Commission. This approach: (i) avoids any potential concern about the scope of authority that can properly be delegated to the Commission staff and/or financial advisor; (ii) recognizes that if the Commission staff and/or advisor cannot informally resolve the issue with FPL, the issue appropriately should be resolved at a higher level; and (iii) avoids the delay that would be introduced by Sunshine Law requirements and Commissioner scheduling concerns if disputes initially had to be submitted to a panel of Commissioners or the full Commission.

All parties who took a position on this issue indicated that it would be acceptable for a single Commissioner to initially resolve such issues, provided that parties had the right to seek *de novo* review by the full Commission or some other point of entry. (FPL BR at 162; OPC BR at 113) Staff agrees that *de novo* review would be appropriate in this unique situation. The designated Commissioner's decisions could affect the substantive rights of the parties in a way that is fundamentally different from routine Prehearing Officer decisions that are reviewed under the highly deferential reconsideration standard. Staff recommends that all parties to this docket should be provided notice of any dispute taken to the designated Commissioner and provided the opportunity for comment before the designated Commissioner. All parties should also be provided notice of any decision reached by the designated Commissioner.

The parties do not appear to agree on who should have the right to seek full Commission review of a determination made by the designated Commissioner. FPL would limit the right to parties represented on the Bond Team (i.e., FPL and the Commission) whereas the Intervenors would extend the right to all parties. Because the specific features of the securitization transaction can affect the rates to be paid by consumers, and hence the substantial interests of the parties, staff recommends that any party be allowed to seek full Commission review.

Decision 3: How should the pricing of the storm recovery bonds be approved? Options include:

- advance approval by the full Commission contingent upon the final price being supported by fully accountable certifications of lowest cost from FPL, the lead underwriter(s), and the Commission's financial advisor
- advance approval by the full Commission contingent upon the final price being fixed within a specified range (e.g. 1-2 basis points) identified no more than 48 hours prior to final pricing
- pricing subject to limited review by the full Commission after the bonds are priced, but before they are issued

Staff recommends the pricing of the storm recovery bonds be subject to limited review by the full Commission after the bonds have been priced but before the bonds have been issued. FPL will file a proposed form of issuance advice letter with the Commission at least two weeks before the expected pricing date. Within one week of receiving the proposed form of issuance advice letter, the Commission's staff with input from its financial advisor will provide comments and recommendations to FPL regarding the adequacy of information proposed to be provided. Within one business day of pricing, a meeting will be noticed for three business days after

pricing to afford the Commission an opportunity to review the proposed transaction. The first day after pricing is for receipt of the actual details of the transaction including the lowest cost certifications from FPL, the underwriter(s), and the Commission's financial advisor. The second day is for the staff's and the Commission's financial advisor's review of this information. The third day would be for a staff presentation of the results of its review and the Commission's deliberations on the transaction. If the Commission determines that all required certifications have been delivered and the transaction complies with applicable law and the financing order, the transaction proceeds without any further action of the Commission. However, if the Commission were to determine that the transaction fails to comply with applicable law or the financing order, or if FPL, the bookrunning underwriter(s), or the Commission's financial advisor is unable or unwilling to deliver the required certifications in a form acceptable to the Commission, the Commission would have discretion to issue an order to stop the transaction. The Commission would have no authority to issue an order to stop the transaction for any other reason, for example, a change in market conditions after the moment of pricing.

Other Matters

FPL's brief suggests a number of specific limitations on the role of the Commission and its financial advisors. FPL states that, as a result of securities law concerns, FPL must retain ultimate editorial control over the statements made in its registration statement and in the materials for an internet-enabled road show. (FPL BR at 160) FPL also states that participation in marketing and sales calls will be limited to FPL and its underwriters for the same reason. (FPL BR at 161). Staff believes that it is premature to address these or other specific limitations. The question of editorial control, for example, will arise only if the Bond Team and FPL disagree about specific disclosure language. Rather than addressing such issues in the abstract, the mechanism recommended above for resolving any future disputes can be used to focus on the specific language in question if a disagreement about such language cannot be resolved informally.

FPL also questions for the first time in its brief whether Section 366.8260, Florida Statutes, contemplates that activities by the Commission's financial advisor and counsel after entry of the financing order and before the post-financing cost review qualify for payment from bond proceeds. (FPL BR at 145; 159 at fn. 50) Staff recommends that the Commission find and direct that such costs are properly payable from bond proceeds.

Section 366.8260(2)(b)2., Florida Statutes, provides:

In performing the responsibilities of this subparagraph [2.] and subparagraph 5., the commission may engage outside consultants or counsel. Any expenses associated with such services shall be included as part of financing costs and included in storm-recovery charges.

Subparagraph 2 identifies the contents of a financing order, and authorizes the Commission to "specify the degree of flexibility to be afforded to the electric utility in establishing the terms and conditions of the storm-recovery bonds" and "include any other conditions that the commission considers appropriate and that are not otherwise inconsistent with this section." Section 366.8260(2)(b)2.g. and j., Florida Statutes. Subparagraph 5 relates to the

Commission's after-the-fact review to determine if the actual costs of the storm-recovery bond issuance "resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of the issuance and the terms of the financing order."

Staff believes that if the financing order (1) specifically limits the flexibility afforded to FPL by requiring active participation by the Commission, its financial advisor, and outside counsel in the structuring, marketing and pricing of the bonds, and (2) imposes conditions on FPL the monitoring of which requires the Commission to rely upon the services of a financial advisor and outside counsel, then the fees and expenses of the advisor and counsel qualify for payment from bond proceeds. To avoid any question about this matter, the Commission's conclusion concerning the recovery of these expenses should be included in the financing order.

Staff Analysis of FPL's Proposed Review Process

In its brief on this issue, FPL proposes a review process for active Commission involvement consisting of seven enumerated points. These points are set forth below, each followed by staff's comments and recommendations.

1. Establish Bond Team

FPL and the Commission designate the professionals on their respective teams, representing in-house business, regulatory, finance and legal disciplines as well as outside advisors. The Commission itself shall be represented on the "Bond Team" by and through the pre-hearing officer in this matter, who may be advised by the Commission's staff and financial advisor and other members of the Bond Team. FPL will propose a transaction timeline in consultation with the Bond Team, establishing clear expectations as to all key issuance activities and the responsibility for each. The Bond Team will review the results of competitive solicitations for services for transaction participants. Throughout the process, the Bond Team should expect to meet by conference call no less than weekly for detailed and documented discussion of progress and next steps. (FPL BR at 159)

As previously discussed, staff recommends day-to-day participation in Bond Team activities through Commission staff, advised by the Commission's financial advisor and outside counsel, with a designated Commissioner to resolve any disputes. In addition, the development of the competitive solicitation and selection of underwriters and other transaction participants should be overseen by the Bond Team to ensure that the process is truly competitive and will result in the selection of transaction participants that have experience and ability to achieve an efficient and lowest cost transaction. (TR 1123, 1179-1181, 1185-1186) The underwriters work for the Bond Team but are not on the Bond Team.

2. Transaction Documents, Offering Documents and Legal Opinions

FPL recommends that Staff complete its review of transaction documents filed with FPL's petition on January 13, 2006 and make recommendations for substantive changes in the Staff Recommendation to be filed May 8, 2006 for vote by the Commission at the Special Agenda on May 15, 2006. The transaction documents submitted are in substantially final form and conform to applicable

law. Finalization of transaction documents is a key step to a successful and timely bond issuance. Subsequent changes in the transaction documents necessary to meet rating agency requirements or to conform to final structuring and pricing requirements will be reviewed with the Bond Team. FPL will be responsible for the initial draft of the registration statement and term sheet which will be provided to the Bond Team for comment and review if requested. FPL as issuer and the party with securities law liability for statements made in these documents will retain final editorial control over the document contents. All legal opinions will be submitted to Bond Team for review and comment if requested. (FPL BR at 159-160)

As discussed in Issues 62, 64, 65, and 66, the various documents that are necessary elements of this proposed transaction should be reviewed and approved consistent with the financing order issued by the Commission. It would be premature for staff to spend a large block of time reviewing and making recommendations for substantive changes to the transaction documents until the Commission has issued its financing order in this docket, providing guidance on what terms will be appropriate for these transaction documents. Thus, it would be inappropriate for the Commission's financing order to approve the transaction documents in substantially the form filed by FPL. Rather, the financing order should authorize FPL and the SPE to enter into the required transaction documents (e.g., the indenture, the storm recovery property sale agreement, the servicing agreement, the administration agreement, the LLC agreement), but leave the terms of those transaction documents to be approved by the Commission's designated personnel and financial advisor taking into account the requirements of the financing order. Staff recommends such review and approvals take place as necessary based on when certain decisions are anticipated to occur throughout the transaction timeline discussed by FPL in Paragraph 1 above. (TR 1186) Subsequent changes or amendments to these documents will be reviewed with, and approved by, the Bond Team before becoming operative. (TR 1703, 1190) Any issues that cannot be resolved by the Bond Team would be submitted to the designated Commissioner for initial decision.

Expert outside legal counsel has advised staff that FPL's assertions regarding securities law liability fail to provide a complete description of securities law liability in relevant respects. Although FPL might also have securities law exposure as a "control person", FPL will not be the issuer of the storm recovery bonds. The SPE will be the issuer and in that capacity will have the most direct exposure to securities law liability. The automatic true-up mechanism will place ratepayers at risk for any securities law liability actually incurred by the SPE. Any damage award payable by the SPE would be a revenue requirement in the true-up of storm-recovery charges to be recovered from ratepayers. Even if a claim asserted by investors is ultimately unsuccessful, attorneys' fees and other litigation expenses incurred by the SPE in defending the matter would be a revenue requirement in the true-up of storm-recovery charges to be reflected on all ratepayers' bills. Consequently, ratepayers have a direct interest that the marketing documents do not contain any statements that are false, misleading, or incomplete. In this respect, the interests of ratepayers are aligned with the interests of the SPE issuer and FPL. Further, as a practical matter, in the absence of fraud, the strength of the securitization law, including the broad nature of the state pledge and the true-up mechanism, make any liability arising from the content of the prospectus or other marketing materials remote unless there has

been a default or other event disrupting or threatening to disrupt the timing or amount of payments on the storm-recovery bonds.

The process for writing and reviewing the prospectus and other disclosure documents requires extensive due diligence on the part of all transaction participants. There should be a balancing of competing interests based on rigorous analysis and the making of informed judgments. Thus, while the Commission itself might not be exposed to securities law liability, if the Commission were to believe that disclosure language proposed by anyone is materially false or misleading, it should decline to allow the storm-recovery bonds to be issued so as to avoid exposing ratepayers to the SPE's potential securities liability by means of the true-up. Similarly, if FPL were to believe disclosure language as proposed by anyone is materially false or misleading, FPL would have a responsibility to decline to allow the storm recovery bonds to be issued. To date, this never has been the case in other securitization transactions, and it is extremely unlikely to be the case in connection with storm recovery bonds. To the contrary, after carefully reviewing all disclosure language in the prospectuses, outside legal counsel for both the issuer and the underwriters in connection with each prior issue of publicly offered ratepayer-backed bonds has delivered a letter confirming that nothing has come to its attention that would lead it to conclude that the prospectus disclosure was materially false or misleading.

Staff recommends all legal opinions related to the proposed storm recovery bond transaction be submitted automatically to the Bond Team for review and comment without the requirement that said opinions be specifically requested from FPL. (TR 1186)

3. Rating Agency Process

FPL will be responsible for obtaining credit ratings. FPL will review progress and any issues encountered with the Bond Team at scheduled update meetings. (FPL BR at 160)

Staff recommends all rating agency presentations be submitted to the Bond Team for review and comment before the presentations are made to the rating agencies. (TR 1186) In prior ratepayer-backed bond transactions when the state commission has retained an active financial advisor, that financial advisor commonly has been an active participant in interfacing with rating agencies. (TR 1175-1176) Staff recommends the Commission's financial advisor similarly be an active participant in rating agency presentations.

4. Structuring and Marketing Process

A detailed marketing plan will be prepared by FPL and the bookrunning underwriter(s) for review and comment by the Bond Team. The bookrunning underwriter(s) will develop a proposed bond structure for marketing purposes reflecting comments of all parties. The structure will be refined over the course of the marketing period and finalized at pricing. In addition to the prospectus and term sheet to be filed with the SEC, a draft set of slides for an internet-enabled roadshow will be provided for review and comment by the Bond Team. FPL will retain ultimate editorial control over these documents as they will likely constitute a "free-writing prospectus" under new SEC rules. Similar to the registration statement, FPL as the party with securities law liability will retain final editorial control over these presentations. During the execution of the marketing plan, it is

anticipated that update calls with the Bond Team to provide market feedback will become more frequent. Alternatively, the Commission's representative and its advisor may choose to observe marketing presentations to potential investors made by the Company and its underwriters. Participation in marketing and sales calls will be limited to FPL and the underwriters as FPL has potential securities law liability for all statements made to potential investors at these meetings. (FPL BR at 160-161)

Preparation of the offering documents and the actual marketing of the storm recovery bonds are very important steps in the issuance process of ratepayer-backed bonds. Staff believes the limitations suggested by FPL over the Bond Team's involvement in the marketing function are unnecessary and will undermine the transparency of the transaction. (TR 1174-1176) The record shows examples of successful ratepayer-backed bond transactions for the benefit of other utilities that have not been subject to these unnecessary restrictions on Commission involvement in the marketing process. (TR 1175-1176) Moreover, these transactions involved the same financial advisors - Credit Suisse on behalf of the sponsoring utilities and Saber Partners on behalf of the respective Commissions - that are present in same roles in this transaction. (TR 1175-1176; EXH 167, pp. 64-67)

As discussed earlier, staff disagrees with FPL's assertions regarding securities law liability. (TR 1204-1205) Staff's comments with respect to Paragraph 2 above apply equally to Paragraph 4.

5. Pricing Process

FPL and the underwriters will consult with the Bond Team on strategy prior to release of pricing indications to the market. As feedback is received, each refinement of price guidance is discussed with the Bond Team. Bookrunning underwriters will develop a "pricing book" containing relevant data to be examined by all parties. It is anticipated that FPL and the Bond Team will assist in the refinement of this document. The Bond Team will discuss and agree on an the estimated range for final spreads that will cause the bonds to clear the market prior to "launching" the transaction with final guidance and scheduling a pricing call. FPL would expect to have the Commission's representative agree that, if we are able to price within that range, that we should execute the transaction, or if not to indicate what alternative the Commission proposes. (FPL BR at 161)

The limitations on the Commission's involvement in the pricing of the storm recovery bonds are unnecessary and will undermine the transparency of the transaction. (TR 1174-1176) The actual interest rate payable on the storm recovery bonds is not fixed until the very last moment. (TR 690) The approach suggested by FPL is fundamentally at odds with the approach used to obtain superior pricing results in the five prior Texas transactions and in the 2005 New Jersey transaction. The Commission's financial advisor needs to be an active and visible participant in the actual pricing process in real time if the Commission is to obtain maximum benefits for ratepayers.

To effectively represent ratepayer interests in this process, staff recommends the full Commission have an opportunity to review the transaction after the bonds have been priced but

before the bonds have been issued. As discussed in Issue 65, FPL will file the issuance advice letter (IAL) and initial true-up letter (combined into one document) in draft form at least two weeks prior to pricing based upon the best information available at that time. FPL will file an IAL in final form with the Commission within one business day of expected pricing at which time a meeting will be noticed for three business days after pricing to afford the Commission an opportunity to review the proposed transaction. The first day after pricing is for receipt of the actual details of the transaction including the lowest cost certifications from FPL, the underwriter(s), and the Commission's financial advisor. The second day is for the staff's and the Commission's financial advisor's review of this information. The third day would be for a staff presentation of the results of its review and the Commission's deliberations. If the Commission determines that all required certifications have been delivered and that the transaction complies with applicable law and the financing order, the transaction proceeds without any further action of the Commission. However, if the Commission were to determine that the transaction fails to comply with applicable law or the financing order, or if FPL, the bookrunning underwriter(s), or the Commission's financial advisor is unable or unwilling to deliver the required certifications in a form acceptable to the Commission, the Commission would have the discretion to issue an order to stop the transaction. (TR 1215-1218) The Commission would have no authority to issue an order to stop the transaction for any other reason, for example a change in market conditions after the moment of pricing.

6. Issuance Advice Letter

As part of the Staff Pre-Issuance Review process proposed by FPL, at least five business days prior to the proposed pricing date for the bonds, FPL will submit to Staff a draft pro-forma issuance advice letter for review by the Bond Team and other responsible parties. This pro-forma issuance advice letter will reflect pricing guidance from the marketplace. At the same time, a draft of the initial true-up letter, reflecting the pro-forma initial bond and tax charges, will be submitted. Not later than 48 hours after the pricing and sale of the bonds, FPL will file with the Commission a final issuance advice letter and a final true-up letter reflecting the final terms of the bonds and the resulting charges. All of the activities described above are contemplated within the scope of FPL's proposed financing order. It is not necessary for the financing order to specify all of the particulars of the due diligence process that the Commission ultimately adopts. Tr. 1506 (Olson). These activities all fall within the Scope of Saber Partners' current contract with the Commission. Ex. 136. (FPL BR at 161-162)

Staff recommends the Commission require the issuance advice letter to contain detailed analyses and representations as discussed above in this issue and in Issue 65. This will obviate the need for a separate initial true-up advice letter. Consistent with staff's comments under Paragraph 5 above, staff recommends the Commission reserve the right to issue a stop order at any time until 5:00 pm Eastern Time on the third business day after pricing if the Commission determines that the transaction fails to comply with applicable law or the financing order, or if FPL, the bookrunning underwriter(s), or the Commission's financial advisor is unable or unwilling to deliver the required certifications in a form acceptable to the Commission.

7. Dispute Resolution

Any disputes relative to the foregoing activities that the Commission has reserved to itself authority to resolve shall be heard before the pre-hearing officer in this matter, with the opportunity for any party represented on the bond team to have the pre-hearing officer's decision reviewed *de novo* by the full Commission. (FPL BR at 162)

Staff's comments under Paragraph 1 above apply equally to Paragraph 7. In addition, staff recommends that any issue that the Bond Team and FPL are unable to resolve should initially be submitted in writing for resolution by the designated Commissioner, subject to *de novo* review by the full Commission. All parties who took a position on this issue indicated that it would be acceptable for a single Commissioner to initially resolve such issues, provided that parties had the right to seek *de novo* review by the full Commission or some other point of entry. Because the specific features of the securitization transaction can affect the rates to be paid by consumers, and hence the substantial interests of the parties, staff recommends that any party be allowed to seek full Commission review.

Summary

The ratepayers should be effectively represented throughout the proposed transaction. The Commission, its staff, its outside counsel, and its financial advisor, along with FPL and its counsel should work in a collaborative process to ensure the structuring, marketing, and pricing of the storm recovery bonds result in the lowest cost consistent with prevailing market conditions and the terms of the financing order.

Based on the evidence presented, staff believes that it is simply not possible to determine, in a review that takes place after issuance of the bonds and under the limited terms of participation suggested by FPL, whether the interest rates achieved on the bond issuance resulted in lowest overall costs consistent with market conditions at the time of pricing. Thus, staff recommends that the Commission, as an appropriate condition of the financing order, ensure its real time involvement in the pricing of bonds at the time of pricing and adopt a lowest cost approach under which FPL, the bookrunning underwriters involved, and the Commission's financial advisor each individually certifies that lowest overall costs were achieved for the storm recovery bonds under then prevailing market conditions and the terms of the financing order.

The Commission should be represented primarily by its staff, who should be advised by the Commission's financial advisor and outside counsel. Staff should periodically brief the Commissioners and the parties on the progress of the transaction. Issues that arise during the process that cannot be resolved collaboratively should be submitted in writing to a designated Commissioner for guidance. If any party objects to the designated Commissioner's proposed resolution, the matter should be submitted to the Commission for *de novo* consideration. The final structure of the transaction, including pricing, should be subject to approval by the full Commission as outlined above. The Commission should specifically determine that the fees and expenses of its financial advisor and outside counsel in this collaborative process are entitled to payment from the bond proceeds.

Issue 75: If the Commission approves the substance of FPL's primary recommendation, should the financing order require FPL to reduce the aggregate amount of the bond issuance in the event market rates rise to such an extent that the initial average retail cents per kWh charge associated with the bond issuance would exceed the average retail cents per kWh 2004 storm surcharge currently in effect?

Recommendation: Yes. (Draper, Springer)

Position of the Parties

FPL: Yes. If the Commission approves the substance of FPL's primary recommendation and market rates rise as described above, to ensure that the rate mitigation benefits of securitization are realized, FPL should reduce the aggregate amount of the storm-recovery bond issuance to an amount whereby the initial average retail cents per kWh Storm Charge requested would not exceed the average retail cents per kWh 2004 Storm Restoration Surcharge currently in effect.

OPC: No position.

FIPUG: No position.

FRF: No position.

AARP: No position.

FEA: No position.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL's position is as stated above. None of the parties took a position on this issue.

ANALYSIS

FPL witness Dewhurst testified that the actual average retail storm charge per kWh will vary based on changes in market interest rates that may occur between now and the issuance date of the bonds. (TR 57) If market rates rise to such an extent that the average retail kWh charge associated with the bond issuance would exceed the average retail kWh charge associated with the storm restoration surcharge that is currently in effect, the aggregate amount of the storm-recovery bond issuance would be reduced to an amount whereby the initial average retail kWh storm charge would not exceed the average retail kWh surcharge currently in effect. (TR 57-58)

The current average retail surcharge factor approved in the 2004 Storm Order, effective January 1, 2006, is 0.146 cents per kWh (¢/kWh), which is determined by dividing the total

storm costs by the total retail kWh sales. (EXH 4, pp. 165-166) Witness Morley testified that under FPL's primary recommendation, i.e., issuance of storm-recovery bonds, the average retail storm charge would be 0.138 ¢/kWh. (TR 764, EXH 60, p. 3) Storm charges by individual rate classes vary, with some being below the average retail rate, others above. FPL's proposed storm charge per rate class can be seen in EXH 60, p. 3. The current residential 2004 storm surcharge is 0.165 ¢/kWh. With the implementation of the proposed storm surcharge and simultaneous termination of the current surcharge, the residential storm charge would be approximately 0.158 ¢/kWh. However, FPL stated in its brief that market rates have risen since FPL's January 2006 filing initiating this proceeding and they may further increase before bonds are actually issued. (FPL BR at 162) Witness Dewhurst stated that while FPL's proposal would reduce the amount of reserve replenishment, it strikes a reasonable balance between customer interests in the mitigation of rate impacts and the need to fund the reserve. (TR 58)

Staff notes that FPL's proposal only applies to the **initial** average retail storm charge. As discussed in Issue 82, the storm charges will be subject to true-ups. However, witness Morley stated that FPL's proposal would also tend to reduce subsequent true-up factors to the extent the total amount of the storm bond issuance is reduced. (EXH 4, p. 234)

CONCLUSION

Staff recommends approval of FPL's proposal to reduce the amount of the storm bond issuance if market conditions change to such an extent that the average retail storm charge would exceed the average retail storm surcharge currently in effect. This proposal is designed to mitigate rate impacts to ratepayers in the event market interest rates increase and should therefore be approved.

Issue 76: Should the Commission approve FPL's request that a surcharge be applied to bills rendered on or after August 15, 2006 to enable FPL to recover its prudently incurred 2005 storm costs in the event the issuance of storm-recovery bonds is delayed? If so, how should the Commission determine the following:

- a. The amount approved for recovery;
- b. The calculation of the surcharge;
- c. The cost allocation to the rate classes; and
- d. The surcharge's termination date.

Recommendation: No. FPL's primary justification for the issuance of storm recovery bonds for the recovery of reasonable and prudently incurred storm damage restoration costs is rate mitigation. Any additional surcharge on top of the 2004 storm charge would negate the benefit of rate shock mitigation to ratepayers avoided by the use of securitization. (Maurey, Draper, Slemkewicz)

Position of the Parties

FPL: If it becomes necessary to implement such a surcharge due to delay in the issuance of storm-recovery bonds, a new tariff would be proposed and submitted by FPL for administrative approval and calculated so as to recover the total amount of 2005 storm costs approved for recovery in the financing order over approximately three years.

OPC:

- a. FPL should not be permitted to initiate an interim rate to begin collecting for 2005 storm costs if the bond issuance is delayed. If the initial bond issuance is delayed beyond the period in which all actual, adjusted 2004 storm costs have been collected, the 2004 storm-surcharge rate should continue until all of the 2005 actual, trued-up, storm costs have been collected or until the first bond is issued. All subsequent bond issuances should be netted for any amounts collected.

b. See above position under section (a).

c. No position.

d. See above position under section (a).

FIPUG:

- a. The Commission should grant recovery via a surcharge. The surcharge should be designed to recover the following: (1) the replenishment of the storm reserve to \$150 million, and; (2) the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments. Costs should be allocated based on the cost of service methodology last filed with and approved by the Commission in Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

b. The Commission should grant recovery via a surcharge. The surcharge should be designed to recover the following: (1) the replenishment of the storm reserve to \$150 million, and; (2) the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments. Costs should be allocated based on the cost of service methodology last filed with and approved by the Commission in Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

c. The Commission should grant recovery via a surcharge. The surcharge should be designed to recover the following: (1) the replenishment of the storm reserve to \$150 million, and; (2) the recovery of FPL's 2005 storm costs minus OPC's proposed adjustments. Costs should be allocated based on the cost of service methodology last filed with and approved by the Commission in Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

d. Agree with STAFF.

FRF: a. FPL should not be allowed to implement an interim rate for 2005 storm costs if the bond issuance is delayed.

b. See FRF position above.

c. No position.

d. See FRF position above.

AARP: The same as the Office of Public Counsel.

FEA: a. – d. Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: In its brief, FPL argues "it is critical that a mechanism for recovery is in place before significant new storm or other costs are incurred to free up short-term liquidity to support ongoing operational requirements such as the fuel hedging program, construction program, and clause under recoveries." (FPL BR at 164) FPL witness Dewhurst acknowledged that investment and rating agency analysts report that FPL operates in a constructive regulatory environment. (TR 103–110; EXH 4, pp. 329–330, 332, 439) Witness Dewhurst also testified that the Company went through the entire 2005 hurricane season with a negative balance in its storm damage reserve. (TR 119) If the Commission issues a financing order for the recovery of reasonable and prudently incurred storm damage restoration costs and the replenishment of the storm damage reserve as proposed in FPL's primary recommendation, it is staff's contention that the Company will have a recovery mechanism in place and an interim surcharge for recovery of 2005 storm costs is unnecessary.

In addition, FPL's primary justification for the issuance of storm recovery bonds for the recovery of reasonable and prudent storm damage restoration costs is rate mitigation. (Dewhurst TR 113–114) Any additional surcharge on top of the 2004 surcharge would negate the benefit of

rate shock mitigation to ratepayers avoided by the use of securitization. (EXH 171, pp. 49–50) Moreover, if the Commission were to approve FPL's request for an additional surcharge, such action could have the unintended effect of unduly delaying the transaction by removing FPL's incentive to seek an expeditious issuance of the storm recovery bonds. (Dewhurst TR 1687) For these reasons, staff recommends the Commission deny FPL's request to approve a surcharge to bills rendered on or after August 15, 2006, to enable FPL to recover its prudently incurred 2005 storm costs in the event the issuance of storm recovery bonds is delayed. (OPC BR at 115)

However, if the Commission approves FPL's request to apply a surcharge to bills rendered on or after August 15, 2006, in the event the issuance of storm recovery bonds is delayed, the staff analysis below discusses how the Commission should determine the following:

a. The amount approved for recovery

If the Commission approves FPL's request for a surcharge to recover its 2005 storm costs, the amount would be the amount that was determined in Issue 36. Per the staff's recommendation in Issue 36, the amount would be \$728,510,020.

b. The calculation of the surcharge

Witness Dewhurst testified that the surcharge be applied to bills rendered on and after August 15, 2006, to recover the 2005 storm costs over approximately three years, or until the costs have been recovered. (TR 59) Witness Morley's calculation of the surcharge is shown in her prefiled direct testimony. (EXH 61, p. 1) Based on the Commission's vote in part a) of this issue, the 2005 storm costs for year one should be allocated to the rate classes based on the allocation percentages developed by witness Morley. (EXH 61, p. 1) Each rate class's cost responsibility should then be divided by its projected kWh sales for the period August 2006 through July 2007 to calculate a cents-per-kWh surcharge. With respect to FIPUG's position on the cost allocation, see the staff analysis in Issue 80.

c. The cost allocation to the rate classes

The amount approved for recovery by the Commission in part a) of this issue should be allocated to the rate classes based on the allocation percentages shown in FPL witness Morley's direct testimony. (EXH 61, p.1) As discussed in detail in Issue 80, FPL allocated the total 2005 storm costs based on the amount of damage in each functional area, e.g., transmission, distribution, etc. The allocation of the costs by functional area to the rate classes should be consistent with the way equivalent costs were treated in the last filed cost of service study. (TR 761) With respect to FIPUG's position on the cost allocation, see the staff analysis in Issue 80.

d. The surcharge's termination date

Witness Dewhurst testified that the surcharge should be discontinued when the storm-recovery bonds are issued and that the amount of the bonds issued would be adjusted for the impact of collections of this surcharge. (TR 59) If the Commission approves FPL's request to apply this surcharge in the event the issuance of the bonds is delayed, staff agrees with witness Dewhurst's proposal.

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Finally, if the Commission approves FPL's request to implement a surcharge to recover its 2005 costs in the event the issuance of the bonds is delayed, FPL should file for administrative approval tariffs and associated surcharges by rate class based on the amount approved for recovery.

Terms for Traditional Recovery of Non-Securitized Amounts

Issue 77: If the Commission approves a recovery mechanism other than securitization, should an adjustment be made in the calculation of interest to recognize the storm-related deferred taxes?

Recommendation: No adjustment is necessary. In Docket No. 041291-EI, concerning FPL's petition to recover 2004 storm damages through a surcharge, the Commission approved an adjustment to interest expense to recognize storm related deferred taxes. The utility has made the adjustment by applying a net-of-tax rate. (Lowe, Kyle)

Position of the Parties

FPL: No adjustment is necessary since FPL would calculate interest on the storm costs to be recovered on an after-tax commercial paper rate basis.

OPC: Yes. FPL should accrue and collect interest on the actual storm costs incurred less the adjustments ordered. Interest accrual should begin in November, 2005 and the interest rate should be the pre-tax commercial paper rate for each month.

FIPUG: Yes. Each month FPL should calculate interest on the outstanding net-of-tax balance of the storm damage account, which shall be the outstanding balance of the storm damage account less 38.575% taxes.

FRF: Yes. Agree with OPC.

AARP: The same as the Office of Public Counsel.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: In Docket No. 041291-EI (2004 storm damage case), the Commission made an adjustment to the calculation of interest to recognize the storm-related deferred taxes that were not included in the utility's rate case. Customers only benefit if the deferred taxes are included in the capital structure at a zero cost rate and rates set using that new capital structure. As the capital structure was not changing in the 2004 storm damage docket, the Commission used a net-of-tax balance for purposes of calculating the interest carrying charge.

FPL witness Davis testified that the interest charges included in the recovery of the 2004 and 2005 storm costs were calculated by multiplying the average monthly unrecovered balance by the current estimated after-tax commercial paper rate. In addition he stated that "these charges represent the interest expense associated with the debt the Company would incur or has incurred to cover the net-of-tax storm costs." (TR 429) Further, Exhibit 19 (Unrecovered 2004 Storm-Recovery Costs) , footnote (2) states that the interest carrying charges are calculated on a net-of-tax balance. Exhibit 20 (Unrecovered 2005 Storm-Recovery Costs) shows the interest calculation for 2005.

No other evidence or testimony on this issue was presented by any other party.

Staff recommends that no adjustment is necessary if the Commission approves a mechanism other than securitization for the calculation of interest to recognize the storm-related deferred taxes.

Issue 78: If the Commission approves a recovery mechanism other than securitization, what is the appropriate accounting treatment for the unamortized balance of the storm-related costs subject to future recovery?

Recommendation: If the Commission approves a recovery mechanism other than securitization, the appropriate accounting treatment for the unamortized balance of the storm-related costs subject to future recovery is to record the costs as a regulatory asset in a subaccount of Account 182.1, Extraordinary Property Losses. (Slemkewicz)

Position of the Parties

FPL: The Commission should authorize the transfer of the unamortized balance of the storm related costs subject to future recovery from the Storm Damage Reserve (Account 228.1) to a deferred Regulatory Asset (Account 182.1) The amount transferred should be amortized consistent with the amounts recovered as revenue through the authorized surcharge recovery factor.

OPC: No position at this time.

FIPUG: The storm damage account should be credited each month with the actual amount recovered from ratepayers.

FRF: No position.

AARP: Same position as FIPUG.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis: After an amount is approved for recovery and amortization through a surcharge, it meets the definition of a regulatory asset. In this instance, the appropriate accounting treatment for the unamortized balance of the storm-related costs subject to future recovery is to record the costs as a regulatory asset in a subaccount of Account 182.1, Extraordinary Property Losses. In order to assist in the tracking and review of the amounts included in this account and their subsequent amortization, a separate subaccount of Account 182.1 should be established to record these transactions. This is consistent with the treatment of the 2004 storm-related costs that were approved for recovery through a surcharge in the 2004 Storm Order.

Based on the foregoing, staff recommends that if the Commission approves a recovery mechanism other than securitization, the appropriate accounting treatment for the unamortized balance of the storm-related costs subject to future recovery is to record the costs as a regulatory asset in a subaccount of Account 182.1, Extraordinary Property Losses.

RATES

Issue 79: STIPULATED: Are the energy sales forecasts used to develop the bond amortization schedules and the recovery mechanism appropriate?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “Yes. The energy sales forecasts used to develop the bond amortization schedules and the recovery mechanism are appropriate.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “Yes. The energy sales forecasts used to develop the bond amortization schedules and the recovery mechanism are appropriate.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Issue 80: If the Commission approves recovery of any storm-related costs through securitization, how should the recovery of these costs be allocated to the rate classes?

Recommendation: The jurisdictional costs approved by the Commission for recovery through securitization (Issue 42) should be allocated to the rate classes using the allocation percentages developed in FPL witness Morley’s Direct Testimony, Exhibit No. RM-6, page 2 of 2 (EXH 59). These percentages are based on the amount of storm damage in each functional area (e.g., transmission, distribution, production, etc.) and then allocated by rate class based on the methodology used for each function in FPL’s last filed cost-of-service study. Each rate class’s cost responsibility should then be divided by its projected kWh sales for the period August 2006 through July 2007 (Issue 79) to calculate a cents-per-kWh Storm Bond Repayment Charge and Storm Bond Tax Charge. (Draper, Keating)

Position of the Parties

FPL: The allocation of the costs to the rate classes should be consistent with the manner in which equivalent costs were treated in the last filed cost-of-service study as provided by FPL in Document Nos. RM-3, RM-4 and RM-5.

OPC: No position.

FIPUG: With respect to allocating costs between customer classes, FIPUG endorses the approach that matches revenue collections to storm costs incurred — that is, customers taking service from the transmission system should not be charged for damages to the distribution system. Costs should be allocated based on the cost-of-service methodology last filed with and approved by the Commission in

Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

FRF: No position.

AARP: Same position as FPL.

FEA: Agree with FIPUG.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

This issue addresses the manner in which the total costs that are approved for securitization in Issue 42 are allocated to the rate classes.

PARTIES' ARGUMENTS

FPL states that the allocation of the costs to the rate classes should be consistent with the manner in which equivalent costs were treated in its last filed cost-of-service study as provided by FPL in the direct testimony of witness Morley, Document Nos. RM-3, RM-4, and RM-5. (EXH 56-58)

AARP takes the same position as FPL. The AG, FRF, and OPC take no position. FEA and FIPUG argue that customers taking service from the transmission system should not be charged for damages to the distribution system and that the costs should be allocated based on the cost-of-service methodology last filed with and approved by the Commission in Docket No. 830465-EI, consistent with the method used in Docket No. 041291-EI.

ANALYSIS

To determine the storm charges by rate class, FPL witness Morley proposed to first allocate the storm-recovery costs based on the actual and expected amount of damage incurred by functional area, i.e., production, transmission, distribution, general plant, and customer service. The general plant category includes costs associated with human resources, general counsel, and marketing. The customer service category includes costs associated with customer call centers and local community support. (EXH 4, p. 160) Allocating the costs incurred by functional area is consistent with the approach the Commission approved in the 2004 Storm Order. (TR 754) FPL performed this functional analysis for the 2004 storm costs, the 2005 storm costs, and future storm costs respectively.

Section 366.8260(2)(b)2.h, Florida Statutes, requires that the storm recovery charges be allocated to the rate classes in the manner in which these costs were allocated in the cost-of-service study approved in connection with the utility's last rate case. The statute further provides that if the utility's last rate case was resolved by a settlement agreement, the cost-of-service methodology filed by the utility in that case shall be used. Witness Morley testified that FPL allocated the functionalized costs consistent with the manner in which equivalent costs were

treated in the cost-of-service study filed in the 2005 FPL rate case. (TR 753, 754) To the extent that the storm charge recovers costs associated with distribution plant, FPL allocated these costs consistent with the treatment of distribution costs in the last filed cost-of-service study. Likewise, to the extent that the storm charge recovers costs associated with transmission plant, FPL allocated these costs consistent with the allocation of transmission costs in the last filed cost-of-service study. (TR 753) This allocation of costs was performed for the 2004 storm costs, the 2005 storm costs, and future storm costs.

In her direct testimony, witness Morley assigned weights to the 2004 storm costs, the 2005 storm costs, and future storm costs based on the amount financed through storm bonds. (TR 755) For example, the \$214 million in proposed unrecovered 2004 storm costs represent 13 percent of the total amount requested through securitization. (EXH 59, p.1) The resulting allocation factors by rate class are shown in the direct testimony of witness Morley, Exhibit RM-6. (EXH 59, p. 2) The allocation factors are applied to the year one storm bond repayment charge revenue requirement. The resulting costs by rate class were then divided by each rate class's forecasted August 2006 – July 2007 sales to calculate a cents per kilowatt-hour storm bond repayment charge. The same steps are performed to calculate the storm bond tax charge. (TR 757; EXH 60, pp. 1-2)

FIPUG contends that the costs should be allocated based on the cost-of-service methodology last filed with and approved by the Commission in Docket No. 830465-EI, the 1983 FPL rate case. In its brief, FIPUG stated the 2005 FPL rate case was settled and that the cost-of-service study was never approved. (FIPUG BR at 11)

Section 366.8260(2)(b)2.h., Florida Statutes, clearly requires that where a utility's last rate case was resolved by a settlement agreement, the cost-of-service methodology filed by the utility in that case shall be used for allocating storm-recovery charges. As previously noted, FPL's last rate case was resolved by settlement agreement.

Nonetheless, FIPUG asserts that application of the statutory requirement would result in a denial of due process to FIPUG because the cost-of-service study filed in FPL's last rate case was "actively disputed" and "never approved." Further, FIPUG asserts that the statutory requirement constitutes an unlawful delegation of authority from the Legislature to FPL to determine the correct cost-of-service to be used in setting storm-recovery charges.

The Commission is not at liberty to ignore the plain language of the securitization law by not using the cost-of-service study filed by FPL in its last case. The statute is clear and unambiguous with respect to which cost-of-service study to use.

Further, the Commission lacks jurisdiction to determine the facial constitutionality of the statute. FIPUG's allegation that the statutory provision at issue constitutes an unlawful delegation of authority from the Legislature to FPL is an attack on the facial validity of the statute. Thus, the Commission is in no position to make the finding suggested by FIPUG or to remedy the constitutional deficiency in the statute alleged by FIPUG.

Likewise, the Commission lacks authority to find that the statute, on its face, denies FIPUG due process by requiring that a cost-of-service study not previously approved by the

Commission must be used in this case. Staff believes it is unlikely that any court could determine that application of the statute would deny FIPUG due process. Well after the time that Section 366.8260, Florida Statutes, became law, FIPUG signed the 2005 FPL rate case settlement which explicitly provided that storm cost recovery could be accomplished through Section 366.8260. Hence, FIPUG should have known that by signing the settlement, it was depriving itself of the opportunity to challenge the cost-of-service study that would be used in any application for securitization filed during the multi-year term of the settlement.

During cross-examination by FIPUG, FPL witness Morley pointed out that in the 2005 rate case, FPL used the same cost-of-service methodology that was approved by the Commission in the 1983 rate case with one exception, the treatment of the St. Lucie Unit 2 production unit. In the 1983 rate case the Commission approved that the majority of the costs for the St. Lucie plant be allocated on an energy basis. In the 2005 FPL rate case, the settlement provided that all production units, including the St. Lucie Unit 2, be allocated on a 12 coincident peak and 1/13 average demand methodology. (TR 776) That is the only difference between the cost-of-service study filed in the 2005 rate case and the cost-of-service study approved by the Commission in the 1983 rate case. (TR 776)

FIPUG also maintains that customers taking service from the transmission system should not be charged for damages to the distribution system. (FIPUG BR at 17). During cross examination by FIPUG, FPL witness Morley explained that the only distribution costs allocated to transmission customers are meters because that portion of distribution costs is required to serve transmission customers. (TR 779) No other distribution costs are allocated to transmission voltage customers. (TR 780) In its brief, FPL further states that the allocation of meter costs to transmission voltage customers is consistent with the cost-of-service approved by the Commission in the 1983 FPL rate case and the cost-of-service filed in the 2005 FPL rate case. (FPL BR at 167). In the 2004 Storm Order, the allocation of distribution costs is not consistent with the way distribution costs were allocated in FPL's last filed cost-of-service study. (TR 780)

CONCLUSION

FPL's proposed allocation of the costs approved for securitization as described in the direct testimony of witness Morley is appropriate and should be approved.

Issue 81: If the Commission approves recovery of any storm-related costs through securitization, what is the appropriate recovery period for the Storm Recovery Charge?

Recommendation: Based on the amount proposed in FPL's petition, the appropriate recovery period is up to 12 years or until the storm recovery bonds and associated charges have been paid in full, depending on the issuance date of the bonds, maturity of the bonds, and market conditions at the time of the issuance. If the amount approved by the Commission for recovery through securitization is reduced based on Commission decisions on other issues, it may be possible to reduce the maximum maturity of the bonds (and thus the recovery period) and still have a leveled charge that is comparable or less than the current 2004 storm charge. (Draper, Springer)

Position of the Parties

FPL: The appropriate recovery period is approximately twelve years, subject to the flexibility to accommodate market preferences discussed in Issue 71.

OPC: No position.

FIPUG: Agree with FPL.

FRF: No position.

AARP: No position.

FEA: FEA supports a 12 year recovery period.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL states that the appropriate recovery period is approximately twelve years. AARP, AG, FRF, and OPC take no position. FEA and FIPUG agree with FPL.

ANALYSIS

FPL witness Dewhurst testified that the storm recovery bonds will be issued in multiple tranches (or classes) with varying maturities to attract a greater number of investors. Exact pricing, terms, tranches and other characteristics will be determined at the time of the issuance and will depend on prevailing market conditions. (TR 76) FPL witness Olson also testified on this issue stating that storm-recovery bonds will be issued in multiple tranches, with average lives that range from two to ten years approximately. The scheduled maturity of the bonds will match the intended recovery period at twelve years from the date of issuance. (TR 657) In his prefiled direct testimony, witness Olson provided a table showing a list of the tranches which he would recommend under market conditions as of November 30, 2005. (EXH 30) The table shows four tranches with scheduled maturity dates ranging from 2010 to August 2018.

During cross examination, witness Dewhurst explained that the recovery period could be changed, but FPL has proposed a series of tranches of different maturities that investors typically buy. (TR 1784) He further stated that it would be possible to shorten the period, but that it would be difficult to stretch the recovery period out much further without running into market acceptance problems. (TR 1785)

CONCLUSION

Based on the amount proposed in FPL's petition, the appropriate recovery period is up to 12 years or until the storm recovery bonds and associated charges have been paid in full, depending on the issuance date of the bonds, maturity of the bonds, and market conditions at the time of the issuance. If the amount approved by the Commission for recovery through securitization is reduced based on Commission decisions in other issues, it may be possible to reduce the maximum maturity of the bonds (and thus the recovery period) and still have a levelized charge that is comparable or less than the current 2004 storm charge.

Issue 82: Is FPL's proposed Storm Charge True-Up Mechanism appropriate and consistent with 366.8260, Florida Statutes, and should it be approved? If not, what formula-based mechanism for making expeditious periodic adjustments to storm-recovery charges should be approved?

Recommendation: Yes. FPL's proposed Storm Charge True-Up Mechanism is appropriate and consistent with Section 366.8260, Florida Statutes. According to the statute, the Commission has to approve the requested true-up or inform FPL of any mathematical errors in its calculation within 60 days. In its true-up filings with the Commission, FPL should also provide workpapers showing all inputs and calculations, including the calculation of the storm bond repayment charges and storm bond tax charges by rate class. (Draper, Slemkewicz)

Position of the Parties

FPL: Yes, FPL's proposed mechanism is appropriate, consistent with the statute, and should be approved.

OPC: No position.

FIPUG: Agree with FPL.

FRF: No position.

AARP: No position.

FEA: No position.

AG: Adopts and agrees with the position set forth by OPC.

Staff Analysis:

PARTIES' ARGUMENTS

FPL states that its proposed true-up mechanism is appropriate and consistent with the statute. AARP, AG, FRF, and OPC take no position. FEA and FIPUG agree with FPL.

ANALYSIS

FPL witness Davis testified that according to Section 366.8260(2)(b)2.e, Florida Statutes, if the Commission issues a Financing Order to FPL, the Commission will

Include a formula-based mechanism for making expeditious periodic adjustments in the storm-recovery charges that customers are required to pay under the financing order and for making any adjustments that are necessary to correct for any overcollection or undercollection of the charges or to otherwise ensure the timely payment of storm-recovery bonds and financing costs and other required amounts and charges payable in connection with the storm-recovery bonds.

Witness Davis further testified that this true-up mechanism helps to ensure that the customers pay no more or less than what is required under storm-recovery financing and helps mitigate bondholders' exposure to differences in actual and estimated sales forecasts, uncollectible accounts receivable, and cash flow variability. (TR 456)

In addition to prescribing a formula-based mechanism, Section 366.8260(2)(b)4, Florida Statutes, requires FPL to detail in its true-up filing any adjustment made for the undercollection or overcollection of revenues as follows:

Such adjustments shall ensure the recovery of revenues sufficient to provide for the payment of principal, interest, acquisition, defeasance, financing costs, or redemption premium and other fees, costs, and charges in respect of storm-recovery bonds approved under the financing order.

(TR 457)

Witness Davis in his direct testimony provided an exhibit that shows how the true-up mechanism would work. (EXH 24)

In summary, FPL's proposed true-up mechanism would address the overcollection or undercollection of the storm bond repayment charge and the storm bond tax charge for the prior period. (TR 458) That amount would be added or subtracted to the bond revenue requirement to be billed during the upcoming period. Based on forecasted sales for all retail classes for the upcoming period, FPL proposes to calculate an average retail storm bond repayment charge and an average retail storm bond tax charge.

FPL witness Morley explained how the average retail storm bond repayment charge and the average retail storm bond tax charge are broken down to specific charges per rate class. (TR 759) The average retail storm bond repayment charge will be compared to the average retail storm bond repayment charge currently in place. The same comparison will be performed for the storm bond tax charge. To the extent that the two charges differ, proportional adjustments will be made to each rate class's individual charges. (TR 759; EXH 4, p. 173) Witness Morley also testified that each rate class's storm charge should be relatively constant over time barring unexpected sales and cost variations. (TR 760)

As stated in stipulated Issue 83, FPL will file for a storm charge true-up at least every six months, in accordance with Section 366.8260(2)(b)4, Florida Statutes. Witness Davis testified that the Commission should either approve the requested true-up or inform FPL of any mathematical error in its calculation within 30 days of filing the true-up. (TR 456) Staff notes that Section 366.8260(2)(b)4, Florida Statutes states that within 60 days after receiving an electric utility's request pursuant to this paragraph, the Commission shall either approve the request or inform the electric utility of any mathematical errors in its calculation.

CONCLUSION

Staff agrees with FPL that its proposed true-up mechanism is appropriate and consistent with the statute. However, staff does not believe it is appropriate to reduce the Commission's time to review FPL's requested true-up from 60 days as allowed by Section 366.8260(2)(b)4, Florida Statutes, to 30 days as proposed by FPL. Staff will endeavor to review FPL's proposed true-up in a timely manner, but does not believe that the Commission should limit its review time from what is prescribed in the statute. In its true-up filings with the Commission, FPL should also provide workpapers showing all inputs and calculations, including the calculation of the storm bond repayment charges and storm bond tax charges by rate class to allow for a complete and thorough review.

Issue 83: STIPULATED: How frequently should the Storm Charge True-up Mechanism be conducted?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “At least every six months.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “At least every six months.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Issue 84: STIPULATED: If the Commission approves the securitization of unrecovered 2004 storm costs, on what date should the 2004 Storm Restoration Surcharge be terminated?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “The current Storm Restoration Surcharge should be terminated concurrent with the effective date of the proposed Storm Charge.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “The current Storm Restoration Surcharge should be terminated concurrent with the effective date of the proposed Storm Charge.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Issue 85: STIPULATED: If the Commission approves an amount to be securitized, on what date should the Storm Recovery Charge become effective?

Recommendation: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “The Storm Charge and its components, the Storm Bond Repayment Charge and the Storm Bond Tax Charge, should be implemented on the first meter reading day after the issuance of the storm recovery bonds.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, FPL and staff agreed to the following position on this issue: “The Storm Charge and its components, the Storm Bond Repayment Charge and the Storm Bond Tax Charge, should be implemented on the first meter reading day after the issuance of the storm recovery bonds.” All Intervenors maintained “no position” on the issue but did not object to the Stipulation between staff and FPL. Staff recommends approval of this Stipulation.

Issue 86: STIPULATED: Should the Storm Recovery Charge be recognized as a separate line item on the customers' bill?

Recommendation: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue: “Yes.” Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue: “Yes.” Staff recommends approval of this Stipulation.

Issue 87: STIPULATED: Are revenues collected through the approved mechanism for recovery (securitization or surcharge) excluded for purposes of performing any potential retail base rate revenue refund calculation under the Stipulation and Settlement approved by Commission Order PSC-05-0902-S-EI?

Recommendation: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue: “Yes.” Staff recommends approval of this Stipulation.

Staff Analysis: As reflected in the Prehearing Order, the parties Stipulated to the following position on this issue. “Yes.” Staff recommends approval of this Stipulation.

Issue 88: Should this docket be closed?

Recommendation: This docket should remain open throughout the bond issuance process and through the completion of the Commission's post-issuance review of the actual costs of the bond issuance. Prior to implementing the initial storm charges by rate class, FPL should file tariff sheets to be administratively approved by staff within 3 business days. (Brubaker, Gervasi, Keating, Draper)

Staff Analysis: This docket should remain open throughout the bond issuance process and through the completion of the Commission's post-issuance review of the actual costs of the bond issuance. After the sale of the bonds and prior to implementation of the initial storm charges by rate class, FPL should file tariff sheets to be administratively approved by staff within 3 business days. FPL proposed in its financing order (EXH B to FPL's Petition, p.3) that staff review the tariff sheets and associated storm charges within 24 hours. Staff will endeavor to review FPL's initial storm charges within 24 hours, but believes that a review time up to 3 business days is more appropriate to allow for a complete and thorough review.