BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Fuel and Purchased Power Cost Recovery Clause with Generating Performance Incentive Factor. ______________________________/	Docket No. 040001-EI Filed: December 1, 2004

FLORIDA INDUSTRIAL POWER USERS GROUP'S POST- HEARING BRIEF

As directed at the conclusion of the evidentiary hearing in this case, the Florida Industrial Power Users Group ("FIPUG") files its Post-Hearing Brief on Issue 14C. For the reasons set forth below, the Commission should deny Florida Power & Light Company's ("FPL") request that the Commission transfer to ratepayers all risks associated with the costs of its UPS power purchase contracts with Southern Company.

ISSUE 14C: Should the Commission approve the three UPS agreements between FPL and Southern Company for cost recovery purposes?

FIPUG's POSITION: *No. FPL has not demonstrated that it has adequately explored and analyzed all alternatives to meet the needs of its ratepayers and that the agreements meet the capacity needs of its retail customers at the lowest possible cost.*

INTRODUCTION

In this proceeding, FPL has asked the Commission to approve, for cost recovery, three new Unit Power Sales (UPS) contracts with Southern Company (Southern) totaling 955 MW of capacity. While FPL made the request in the proceeding on cost recovery factors for calendar year 2005, delivery under the proposed UPS contracts is not scheduled to begin until June of 2010.

FPL's witness characterized Commission approval as a "condition" of the UPS contracts. (TR-504). The effectiveness of the three UPS contracts is not contingent upon Commission approval. Rather, under the terms of the agreements, FPL has the right to terminate the contracts

if the Commission does not approve them for cost recovery within six months from the date the parties signed the agreements. FPL must act affirmatively to do so. (TR-506).

Essentially, FPL seeks to shift the risk associated with its UPS contracts from FPL to ratepayers, including FIPUG members. It was therefore incumbent on FPL to demonstrate to the Commission that it took the steps necessary to ensure that the UPS contracts are the best deal available for ratepayers. As FIPUG will show, FPL has simply failed to meet its burden. FIPUG would have preferred for the Commission to direct FPL to canvass the wholesale market meaningfully and conduct a thorough analysis of available alternatives, including the UPS contracts. In the absence of a thorough market survey, and in view of the inadequate analysis that FPL proffered as a substitute, the Commission must conclude that FPL has not justified a decision to shift the risk of cost recovery from FPL's shareholders to FPL's customers.

I. THERE IS NO NEED TO RUSH THE UPS CONTRACTS THROUGH THE APPROVAL PROCESS.

FPL claims that the Commission has only six months to approve the UPS contracts because Southern was unwilling to keep its capacity off the market any longer. However, FPL witness Hartman acknowledged that under the terms of the UPS contracts, FPL and Southern contemplate the possibility that FPL could terminate the contracts as late as December of 2005. This means that Southern is aware it may be placing the capacity underlying the UPS contracts on the wholesale market at that time. (TR-570). The claim that Southern's tough negotiators imposed a six-month deadline on the Commission therefore rings hollow. The Commission should refuse to be pressured, by means of an artificial deadline, into accepting FPL's deficient justification.

FPL also says it must have assurance of cost recovery or it cannot move forward with the contract. (TR-658-659). The Commission should ask itself why FPL has not included a

"regulatory out" clause that FPL insists on including in purchase power contracts with non-utility merchants.

Finally, this Commission should be concerned that FPL included in its case in chief only the most conclusory information about the FPL/Southern deal. During the already truncated fuel adjustment case, parties and Staff spent the little available time trying to discover the most basic information about the transaction -- assumptions, methodology, calculations -- as none of this information was provided in the FPL petition or direct testimony. This Commission should require a utility seeking approval of a transaction of this magnitude to provide, with its petition, detailed information concerning the proposal and the economics associated with it – especially when the utility is asking the Commission and parties to evaluate its request within a compressed time frame.

II. FPL FAILED TO COMPARE THE UPS CONTRACTS WITH ALTERNATIVES BEFORE SEEKING APPROVAL FOR COST RECOVERY.

In his summary, FPL witness Hartman said, "From a cost-effective perspective these contracts compare well to available cost references." (TR-504). To assert the contracts are "cost-effective" is to claim they have been compared against alternatives. However, FPL did not seek alternatives, much less conduct meaningful comparisons. FPL's attempt to persuade the Commission it did so is rife with shortcomings.

A. FPL has not demonstrated that the UPS contracts would be more advantageous than a self-build option.

During his summary, FPL witness Hartman said, "While we might be able to build a self-build gas unit that could provide energy at $69 to $93 million lower cost on a net present value, we believe there are a number of benefits from these contracts that while difficult to quantify are nonetheless real and whose value outweighs this difference." (TR-504). The Commission should

consider four points regarding FPL's treatment of its self-build option when appraising this statement.

First, elsewhere in his testimony Mr. Hartman maintains that FPL never attempted to determine whether its self-build option was better than the UPS contracts. (TR-908). Instead, FPL decided that its objective in examining its self-build option in this instance was merely to see if the costs of the UPS contracts were "reasonable." (The witness provided no parameters regarding how much more expensive than the self-build option the UPS contracts could be before becoming "unreasonable.")[1]

Said differently, FPL says it reviewed the self-build option, preliminarily identified savings of $69 to $93 million, and promptly abandoned the endeavor. FPL's rationale is counter-intuitive and compels the conclusion that, having seized upon the UPS contracts, FPL avoided information that would get in the way of its decision.

Second, several of the advantages that FPL attributes to the UPS contracts relative to the self-build option could be met by other wholesale arrangements. For instance, FPL touts the advantage of a five-year contract that will defer a decision on a self-build option. The advantage of a short-term contract over the self-build option is not unique to the UPS arrangements. (TR-531). Similarly, wholesale arrangements other than the UPS contracts could provide the "geographical diversity" that FPL finds appealing in the UPS contracts. (TR-531).

Third, FPL acknowledged that the self-build option appeared to be more cost-effective than the UPS contracts, but referred to "other benefits." To the extent Mr. Hartman is referring to the benefits of coal-fired capacity[2], it comprises only 17.28% of the 955 MW, (TR-511), and

[1] FPL never quantified the benefits of the UPS contracts that led it to conclude the UPS contracts are preferable to the UPS contracts, even though they are quantifiable with assumptions. (TR-592).

[2] FPL did not give meaningful consideration to the greater amount of coal-fired generation available from other projects, such as the 1600 MW LS Power project described by Mr. Vogt. (TR-865, 874).

the cost advantages of that capacity are fully reflected in the cost comparison that indicates the self-build option would be cheaper. (TR-530). To the extent FPL purports to rely on non-price considerations, FPL has not identified the "other benefits" with sufficient clarity and specificity to justify requiring ratepayers to assume the risk of cost recovery -- particularly since non-UPS options, unexplored by FPL, would also have both price and non-price related considerations.

Fourth, had FPL performed a complete analysis, and had the full analysis continued to confirm a material cost advantage over the UPS contracts, FPL indisputably would have been required by rule to issue an RFP and evaluate responses (likely including proposals from Southern!) prior to reaching a decision on the best available alternative. FPL witness Hartman testified that FPL considered issuing an RFP at the time it was negotiating with Southern, even though FPL's position is that the "Bid Rule" did not require it to do so. This acknowledgment indicates FPL's awareness that an RFP can be relevant to FPL's obligations to its customers any time it serves customers' interests, not just when it is required by the "determination of need" rule. Mr. Hartman defended the decision not to issue an RFP by contending it would not have been in customers' interests. However, there was ample time to conduct an RFP. A solicitation would either have confirmed FPL's choice or indicated a better one. In either case, how could it not have been in customers' interests? Moreover, the competition would have placed downward pressure on Southern's price. (FPL acknowledged that Southern has submitted bids to FPL RFPs in the past). (TR-915). FPL made the wrong decision when it jettisoned the possibility of a contemporaneous RFP. Its decision contributes to its inability now to meet its burden of proof.

B. FPL made no attempt to identify alternatives in Florida.

FPL candidly admitted that it limited its consideration to sources from outside Florida. (TR-517). Perhaps it is no surprise, then, that FPL's reference to Florida-based "alternatives"

was particularly questionable. FPL says it compared the UPS contracts to the "most relevant" proposal submitted in response to its 2003 RFP. The submission to the 2003 RFP is an artifact, not an option. The RFP data is stale, and the submission to the 2003 RFP was not designed to be responsive to a five-year, 955 MW identified need.[3] By confining the analysis to dated proposals that were not tailored to the 955 MW, five-year need, FPL ensured the comparison would favor the UPS contracts. For instance, FPL imposed on the "analysis" a significant condition (FPL must not be called upon to build peaking capacity at the Turkey Point site) that was not communicated to bidders at the time the 2003 bids were prepared. (TR-516-517).

Apparently, the "most relevant" submission FPL used was not even the most economical proposal submitted in response to the 2003 RFP. (TR-516). It was a proposal to provide 1220 MW over a period of 15 years. (TR-515). Based on the difference in the duration of the arrangements, FPL ascribed to the "most relevant" RFP submission an equity penalty more than three times greater than the equity penalty it assigned to the UPS contracts. (TR-520). The difference in equity penalties accounts for $47 million of the cost differential between the UPS contracts and the proposal from the past. (TR-519). In other words, by picking a contract longer than five years, FPL skewed the comparison by $47 million. Had the RFP submission been for an equal term, or (as decided by the Commission in the Manatee/Martin determination of need docket) (TR-522) had the consideration of an equity penalty been excluded altogether, the 15-year, 1220 MW, 2003 RFP submission from the past would be more economical than the UPS

[3] Ironically, when describing year-old submissions to a closed RFP, FPL's witness said that the proposal that he compared to the UPS contracts was "the best offer that was on the table." (TR-517). Obviously, none were on the table.

contracts in two of the three scenarios that FPL presented in its analysis, while supplying considerably more capacity for the money.[4]

More importantly, had FPL issued an RFP or otherwise solicited and negotiated proposals from the wholesale market, it could have specified a term shorter than 15 years. It could have specified a quantity of capacity smaller than 1200 MW. It could have analyzed individual offers or combinations of offers in a genuine effort to identify the best deal for ratepayers.

C. FPL did not meaningfully evaluate alternatives from outside Florida.[5]

FPL asserts its UPS contracts are superior to an "indicative bid" it received from a merchant in SERC. However, FPL acknowledges that it did not enter bilateral negotiations with any entity other than Southern. (TR-511). It "compared" the fully negotiated, final offer UPS contract with an "indicative bid" that represented the opening round from a potential alternative. FPL's comparison therefore is meaningless, and its effort to relate the UPS contracts to alternatives outside Florida is seriously deficient.

Further, FPL refused to consider alternatives involving construction because such projects are "conjecture" and FPL does not want to subject customers to this "risk." (TR-912). However, FPL has not prohibited construction proposals in response to RFPs involving less available construction time. Ironically, it appears that when FPL defends a choice already made, the greater the lead time available for construction, the lesser the consideration such a proposal will receive. FPL's proposal is as unreasonable and counter-intuitive as its decision to ignore indications that its self-build option would be cheaper than the Southern contracts.

[4] The 1220 MW proposal from the past exceeded the 955 MW target by almost 28%. When FPL alluded to "non-price considerations, it did not mention that additional megawatts, and therefore greater reliability, would be associated with the 2003 bid as compared to the UPS contracts.

[5] See TR. at 602-605 for a long list of suppliers that FPL could not even be bothered to contact.

D. FPL attempted to divert attention from the deficiencies of its case.

Put very simply, FIPUG's position is that competition should be given an opportunity to provide or confirm the best alternative before the Commission places cost responsibility for 955 MW of capacity on ratepayers. At hearing, FIPUG did not advocate that any particular source or project be chosen over the UPS contracts. FIPUG presented the testimony of representatives of Vandolah Power Company, LLC and LS Power Development, LLC. The witnesses testified that their companies had not been invited to present proposals, and that their companies are prepared and willing to compete for the opportunity to provide capacity and energy to FPL. FIPUG also co-sponsored the testimony of David Dismukes, who presented a survey of the myriad of opportunities in the wholesale market which might meet FPL's need but which FPL blithely ignored. The testimony FIPUG sponsored illustrates in vivid fashion the existence of a wholesale market, eager to compete, that FPL did not consult before committing to the UPS contracts.

The transcript of the hearing is replete with FPL's negative references to "merchant" witnesses and with FPL's claim that the interests of FIPUG's witnesses are inconsistent with those of FPL's customers. FPL's anti-merchant theme is disingenuous; FPL's attempt to discredit the testimony of FIPUG's witnesses by applying the "merchant" label itself lacks credibility. Consider that in this case FPL is sponsoring three contracts that Southern negotiated while in the capacity of a merchant. In fact, FPL's Mr. Hartman refers explicitly to Southern's Franklin and Harris "merchant units." (TR-508). FPL has a merchant affiliate named FPL Energy. FPL's witness, Mr. Hartman, worked for FPL's merchant sibling before joining FPL, where he helped merchant FPL Energy win competitions to supply power to purchasing utilities. While Mr. Hartman professed not to have cared when he was a merchant, he acknowledged that

a purchasing utility should protect its customers. (TR-917-18). It follows that, as long as the utility is doing its job, the interests of a selling merchant that wants to win the competition align (whether or not it cares) with the interests of the ratepayers such as FIPUG members. For FIPUG to advocate the benefits of competition and to sponsor testimony describing the untapped wholesale market was completely consistent with FIPUG's interests.

Having failed to consider alternatives, FPL tried unconvincingly to find reasons to continue to exclude them after the fact. Thus, FPL pointed out that Vandolah Power's parent, Northern Star Generation LLC, is a recent entrant into the wholesale generation market, but conveniently overlooked the fact that when it acquired the assets of El Paso, Northern Star also acquired a contingent of El Paso's experienced operating personnel. (TR-859). Mr. Hartman claimed the ability to assert the power from Vandolah would not be "cost-effective," (TR-892), when FPL had made no attempt to ascertain what the cost of the power would be.

As to LS Power, which has the ability to fill all of FPL's need with coal and is on the same transmission pathway as the Southern units, FPL claimed that Mr. Vogt engaged in "wishful thinking" when he testified that the LS Power Early County, Georgia project would be on line to serve FPL's needs. (TR-905). Mr. Hartman's dismissal of the project based on his limited information flies in the face of Mr. Vogt's representation, based on his direct and intimate knowledge of the circumstances, that LS Power's Georgia project is on track to be fully permitted in 2005.

CONCLUSION

Regulated utilities describe their "integrated resource planning" as a process in which a utility undertakes a thorough search for available sources of capacity and energy, screens them to identify feasible alternatives, and conducts a rigorous economic analysis to identify the most

advantageous option. In this case, FPL stood this concept on its head. FPL began by deciding upon the UPS contracts, and then assiduously avoided meaningful comparisons with alternatives. FPL's responses when challenged merely serve to underscore the manner in which FPL bypassed any consideration of competing alternatives. FPL has presented insufficient justification to transfer the risk of the UPS contracts from shareholders to ratepayers.

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CERTIFICATE OF SERVICE

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