352

 1 BEFORE THE

 FLORIDA PUBLIC SERVICE COMMISSION

 2

 3 In the Matter of:

 4 REVIEW OF 2007 ELECTRIC DOCKET NO. 070300-EI

 INFRASTRUCTURE STORM HARDENING

 5 PLAN FILED PURSUANT TO RULE

 25-6.0342, F.A.C., SUBMITTED BY

 6 FLORIDA PUBLIC UTILITIES COMPANY.

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 PETITION FOR RATE INCREASE BY DOCKET NO. 070304-EI

 8 FLORIDA PUBLIC UTILITIES COMPANY.

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 10 VOLUME 3

 11 Pages 352 through 567

 12 ELECTRONIC VERSIONS OF THIS TRANSCRIPT ARE

 A CONVENIENCE COPY ONLY AND ARE NOT

 13 THE OFFICIAL TRANSCRIPT OF THE HEARING.

 THE .PDF VERSION INCLUDES PREFILED TESTIMONY.

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 PROCEEDINGS: HEARING

 16

 BEFORE: CHAIRMAN MATTHEW M. CARTER, II

 17 COMMISSIONER LISA POLAK EDGAR

 COMMISSIONER KATRINA J. McMURRIAN

 18 COMMISSIONER NANCY ARGENZIANO

 COMMISSIONER NATHAN A. SKOP

 19

 DATE: Wednesday, February 27, 2008

 20

 TIME: Commenced at 9:30 a.m.

 21 Recessed at 4:35 p.m.

 22 PLACE: Betty Easley Conference Center

 Room 148

 23 4075 Esplanade Way

 Tallahassee, Florida

 24

 REPORTED BY: MARY ALLEN NEEL, RPR, FPR

 25

 APPEARANCES: (As heretofore noted.)

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 1 P R O C E E D I N G S

 2 (Transcript follows in sequence from

 3 Volume 2.)

 4 CHAIRMAN CARTER: Okay. We are back on the

 5 record with our hearing, and last time Mr. Horton was in

 6 the process of cross-examination. Mr. Horton, you're

 7 recognized.

 8 MR. HORTON: Thank you.

 9 Thereupon,

 10 HUGH LARKIN, JR.

 11 called as witness on behalf of the Citizens of the State

 12 of Florida, continued his sworn testimony as follows:

 13 CROSS-EXAMINATION

 14 BY MR. HORTON:

 15 Q. Are you ready, Mr. Larkin?

 16 A. I am.

 17 Q. All right, sir. We were talking about rate

 18 case expense and the preparation of rate cases, and in

 19 your testimony, and precisely on page 31, lines 8 and 9,

 20 you make the statement, "Preparation and filing of rate

 21 cases are normal costs incurred by utilities in the

 22 normal course of business." And my question to you is,

 23 do you know how often companies file a rate case?

 24 A. Generally every four or five years.

 25 Q. Have you ever put together a rate case?

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 1 A. We have -- not from the company standpoint,

 2 but we do it all the time from a regulatory -- from a

 3 consumer standpoint, yes.

 4 Q. From the review side, but you've never put one

 5 together from scratch that has to be filed, the petition

 6 and all that? You've never done it from the company

 7 side?

 8 A. No.

 9 Q. Okay. Do you have a feel or an idea how much

 10 work is required to put together a rate case?

 11 A. Well, I mean, you're putting it together from

 12 records you're familiar with, so I can't say that it

 13 would be -- there are lots of hours involved, but I

 14 don't think it's a task that is unsurmountable.

 15 Q. But while that work is going on, regular work

 16 needs to go on as well, does it not?

 17 A. Yes, but the regular work is generally done by

 18 clerks and staff people.

 19 Q. You don't think there's regular work that

 20 needs to be going on by staff accountants and other

 21 personnel that are involved with the rate case?

 22 A. Yes, but they're supervising, and they can

 23 handle that.

 24 Q. Okay. Do you have an idea how much discovery

 25 has been filed in this case?

 357

 1 A. The number of questions asked?

 2 Q. Generally.

 3 A. A couple of hundred questions, but most of

 4 them could have been replied to by providing the

 5 documents that the company used. Normally we don't ask

 6 information that the company shouldn't have done

 7 themselves or put together themselves in preparing the

 8 case, so I don't think that there's a lot of extra work

 9 involved in answering discovery.

 10 Q. Well, if you ask an interrogatory question,

 11 Mr. Larkin, doesn't that require that the person

 12 responsible sit down, draft up and review and respond to

 13 the interrogatory?

 14 A. Yes.

 15 Q. That's not something that's just readily

 16 available that they can pick up and provide, is it?

 17 A. I would think so. I mean, when you ask me

 18 questions, I look at it, and I can dictate the answer

 19 within four or five minutes. And I've got the

 20 information. If they say, "Where did you get this," or

 21 "How did you do this," or "What's your view of that,"

 22 boy, if I can't do -- you asked me like 25 questions. I

 23 don't think it took me an hour to answer them, hour and

 24 a half maybe.

 25 Q. Do you think it's -- you have employees that

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 1 work for you in your business?

 2 A. Yes.

 3 Q. And do you offer them any type of recognition

 4 for extraordinary efforts when they're doing their job?

 5 A. No. They get a base salary, and at the end of

 6 the year, if we made money, then I divide it up between

 7 the people.

 8 Q. So you provide bonuses?

 9 A. Pardon?

 10 Q. You provide bonuses to your employees?

 11 A. Well, most of the compensation comes through

 12 bonuses. They get just enough to pay their bills

 13 through the year, and then at the end of the year,

 14 whatever money is there I divide up between the people

 15 that are working.

 16 Q. Are you aware that Florida Public Utilities

 17 does not provide bonuses to its employees no matter how

 18 much work they do?

 19 A. Well, I'm not familiar. I think you probably

 20 should ask Patricia Merchant about the compensation

 21 plan, because I'm not that familiar with it.

 22 Q. You are aware that Florida Public Utilities

 23 does not have a very large staff, do they?

 24 A. Well, I --

 25 Q. Electric staff.

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 1 A. -- assume they've got a staff that's

 2 commensurate with the size of the company.

 3 Q. You would expect that the company would put

 4 together a rate case like this in the most efficient

 5 way, and that may involve the use of outside consultants

 6 as well as employees; correct?

 7 A. I would assume so.

 8 Q. And if that meant utilizing outside employees

 9 -- or excuse me, outside consultants to perform some of

 10 the work that the staff normally would have performed so

 11 that they could work on the rate case, would that be an

 12 appropriate expense to recover?

 13 A. If it's designated and they can show that it's

 14 directly related to the rate case, it is appropriate to

 15 recover it.

 16 Q. Let me -- if -- strike that. Let me turn to

 17 another subject, inspection and testing of the

 18 substations.

 19 A. Yes.

 20 Q. You would agree that it would be prudent for

 21 the company to inspect and test its substation

 22 equipment, would you not?

 23 A. That they do do that work?

 24 Q. That they should do that.

 25 A. Yes.

 360

 1 Q. And the inspection and testing could prevent

 2 costly repairs later if it's performed regularly, would

 3 it not, could it not?

 4 A. It should.

 5 Q. And the testing and inspection would also

 6 contribute to the hardening efforts that this Commission

 7 is interested in with respect to the storms, would it

 8 not?

 9 A. It may or may not.

 10 Q. Okay. Now, I believe you were provided some

 11 documents that were used in the development of the

 12 company's substation maintenance.

 13 A. I was provided two pages, or a one-page

 14 document that listed numbers, and then a reference or a

 15 document that is generic maintenance document.

 16 Q. But you were provided a response to that. You

 17 were provided that -- you say it's a generic maintenance

 18 document, but it includes recommendations on maintenance

 19 and testing of the substation equipment, does it not?

 20 A. It includes generic recommendations.

 21 Q. Are you aware that the company does indeed

 22 have a company-specific schedule?

 23 A. Well, if they do, they didn't provide it. I

 24 mean, what they provided was a sheet of paper which

 25 listed categories such as transformers, 77,000, circuit

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 1 breakers, 8,000, circuit switches, 9,000. There was no

 2 comparison between what they currently are spending,

 3 what they think they have to spend, and what the benefit

 4 of increasing the spending was. It was just, "Here's a

 5 list of numbers, and this is how we got to here."

 6 That's not -- that doesn't justify increasing

 7 these maintenance expenses by 154 percent. All it is is

 8 a request with no substantiation. There was no

 9 step-by-step, detailed plan with costs associated with

 10 it compared to what done in prior years and a

 11 justification line by line of why that increase is

 12 necessary. It's a generic, "Give us this amount of

 13 money," and that's why we're objecting to it, why I'm

 14 objecting to it.

 15 Q. Let's move to another subject, Mr. Larkin,

 16 uncollectibles. On page 43 of your testimony, I believe

 17 you address the uncollectible accounts.

 18 A. Yes.

 19 Q. And I believe you say the bad debt expense

 20 should be $71,179; correct? That's on page 44, line 17.

 21 A. Yes.

 22 Q. Now, in your testimony there, you include a

 23 portion of a response to Interrogatory Number 115, and

 24 that's on page 43. Do you see that?

 25 A. Yes.

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 1 Q. Do you recall if there was some more

 2 information in that interrogatory?

 3 A. There was -- there might have been.

 4 Q. You don't remember if you considered any of

 5 that explanation?

 6 A. Well, I certainly did consider it. I read the

 7 whole thing and considered it. But the direct question

 8 was, how come you made a calculation and said here's the

 9 bad debt expense, and it should be 144,563, but then

 10 when you go to the work paper or the company's expense,

 11 it's 216,664? Their calculation didn't agree with what

 12 they put in the expense.

 13 And this answer -- when we asked why is that

 14 so, we get this answer back that is -- I want to be

 15 charitable, but it doesn't make any sense at all. It's

 16 a gobbledygook answer that doesn't make any sense on the

 17 way bad debt is accounted for. But that was just to

 18 show that the company's number was wrong to start out

 19 with, the wrong number is in there to start out with.

 20 Then I did a calculation comparing their

 21 actual bad debt write-offs net of recoveries. Now, the

 22 company didn't use the recoveries. They just used what

 23 they wrote off and arrived at a percentage. I used the

 24 recoveries or the write-offs net of recoveries and

 25 compared that to the annual revenue and arrived at a

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 1 percentage, which I'm trying to find. And it's that

 2 percentage that I applied to the company's projected

 3 revenues to arrive at the $71,000.

 4 And the $71,000 -- the exhibit is C-4. The

 5 $71,000 is comparable to what the company's net

 6 write-offs were from 2000 to 2006. I used 71,000. In

 7 2006, the net write-offs were 58,000. In 2005, they

 8 were 58,000. In 2004, they were 48,000. In 2003, they

 9 were 46,000. In 2002, they were 37,000. How do you go

 10 from net write-offs in 2006 of $58,000 to $212,000?

 11 There's no reasonality in the numbers. There's no

 12 comparability, no sense to it.

 13 Q. Don't you think the recent fuel increases

 14 might have impacted that?

 15 A. Well, the fuel would have been considered when

 16 I take the average recovery and apply it to the

 17 projected revenue, because the projected revenue

 18 includes the increase in fuel. I applied 11.52 percent

 19 to $62 million, which is the number that the company --

 20 61,760,000, that's the number that the company projected

 21 to be the 2008 revenues before the rate increase. So I

 22 went from actual 58,000 in 2006 to 71,000 in 2008, and I

 23 think that's a reasonable projection or progression of

 24 what has happened with the numbers.

 25 Q. Now, Mr. Larkin, I think we're going to agree

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 1 to disagree on some of what you said, but let me move to

 2 another topic, and that would be tree replacement. Do

 3 you recall the tree replacement program?

 4 A. Yes, yes.

 5 Q. And isn't that proposal to -- wouldn't that be

 6 a least-cost approach to some of the vegetation issues,

 7 clearing and maintaining the line right-of-way?

 8 A. Well, I suppose you could look at it that way,

 9 but I don't think it's the overall ratepayers'

 10 responsibility to go into individual customers' property

 11 and remove trees and replace those trees at the expense

 12 of all the ratepayers.

 13 Now, when you plant a tree, common sense and

 14 most cities will tell you you have to keep the tree so

 15 many feet away from the right-of-way. And if they've

 16 done that, then they've complied with the law. And if

 17 the tree continues to grow, then it's either their

 18 responsibility to take it down, or the company has a

 19 tree trimming program that will cut those back out of

 20 the right-of-way. But I just don't see providing 30,000

 21 every year to go around and do landscaping for people.

 22 Q. Well, how do the owners know that they should

 23 not be planting in the right-of-way? You phrase it, I

 24 think, that they can't plant in right-of-ways. How do

 25 they know that?

 365

 1 A. Well, it seems to me that most city

 2 ordinances -- at least where I live, there are

 3 ordinances about where you can plant trees and how far

 4 away they have to be from the property line.

 5 Q. How does a property owner know about that?

 6 A. Well, he knows that by asking the city.

 7 Q. Do you think that's something that might be

 8 communicated by the company to the customers?

 9 A. You could do that, yes.

 10 Q. That would be something included in the

 11 information that the company says that they need to

 12 communicate to their customers?

 13 A. They could do that, yes.

 14 Q. And something they're seeking additional cost

 15 for? That could be covered by that, could it not, the

 16 cost in this proceeding?

 17 A. Yes. I've left money in for communicating

 18 with the company -- customers, rather.

 19 Q. Okay. Just a final clarification question.

 20 You recently provided some discovery responses to the

 21 company. Do you have a copy of that with you?

 22 A. I do.

 23 Q. Would you look at number 41, please, sir.

 24 A. Yes.

 25 Q. All right. I think that asks if you knew the

 366

 1 ratio of employees, and you said the ratio of employees

 2 to customers --

 3 A. To customers was --

 4 Q. Customers to employees was 85, or 84.59?

 5 A. Right.

 6 Q. That's the ratio of electric customers to

 7 electric employees?

 8 A. I believe so.

 9 Q. You referenced Interrogatory 43.7; correct?

 10 A. Yes.

 11 Q. Would you agree that that shows total company

 12 employees?

 13 A. Well, I wasn't aware of that. Then that

 14 calculation would be wrong.

 15 Q. Okay. This is one you did real quickly and

 16 submitted a response to?

 17 A. This is, yes, one that I got the information,

 18 part of the information myself, and part of the

 19 information I got over the phone.

 20 MR. HORTON: Okay. Thank you. I have no

 21 further questions.

 22 CHAIRMAN CARTER: Commissioners? Commissioner

 23 Argenziano, you're recognized.

 24 COMMISSIONER ARGENZIANO: Yes. Just a quick

 25 question. And I probably need you to go over it one

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 1 more time, because I'm not sure I got it right. But you

 2 had claimed that in the rate case there were costs that

 3 were not substantiated. Could you tell me again what

 4 those costs were?

 5 THE WITNESS: Which costs?

 6 COMMISSIONER ARGENZIANO: I remember -- I just

 7 grabbed it out as you were saying it, and you said that

 8 they had not substantiated.

 9 THE WITNESS: Well, one of the costs is --

 10 COMMISSIONER ARGENZIANO: Maintenance?

 11 THE WITNESS: One type of cost is the

 12 maintenance of the distribution and transmission

 13 transformers. I mean, they have a page of numbers, but

 14 as I explained to Mr. Horton, that's not a

 15 justification. You can't just type a number on a page

 16 and say, "Here's what we want." You have to have a

 17 specific program that the ratepayers represented, us,

 18 can look at and see that there's actually a benefit to

 19 the ratepayer by paying this extra money. And if there

 20 isn't and there's no justification, we're obligated to

 21 take that -- or to suggest to the Commission that that's

 22 not substantiated and it ought to be taken out.

 23 The storm damage is another example. They

 24 just said, "Well, we want a storm damage reserve that's

 25 5 percent of the transmission and distribution

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 1 investment." Well, that's about -- I think it's like

 2 3-1/2 million, or maybe 3.8 million. They've never had

 3 damages of $3.8 million. I mean, the most they ever had

 4 was in 2004, and I believe it was $800,000. And the

 5 year before 2004, the reserve was well over 2 million.

 6 The reserve is now $1.8 million. We just don't think

 7 there's a necessity to increase or have ratepayers pay

 8 additional storm damage costs when the company is not

 9 likely to incur those types of expenses in the normal

 10 scenario of storms.

 11 And one thing I should point out. This is

 12 what is called an unfunded storm reserve. That means

 13 that when you -- when the company collects this money

 14 from the ratepayers for storm costs, they don't put it

 15 away in their pocket, or they don't put it in a bank

 16 that's earning interest. They're using that in the

 17 company. It's unfunded. That means what it represents

 18 is a promise to the ratepayer that when there is a

 19 storm, we won't come to you for this level of storm that

 20 we've already collected from you; we'll go out and

 21 borrow the money or we'll get the money somewhere else.

 22 But there's no money there. There is no money there.

 23 They're using that money in day-to-day operations, which

 24 is okay.

 25 But when the numbers don't substantiate, the

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 1 numbers don't say to me -- the worst-case scenario in 19

 2 years had been $810,000. Then I say what we're doing

 3 now is just fine, let's just continue with what we're

 4 doing.

 5 COMMISSIONER ARGENZIANO: Thank you.

 6 THE WITNESS: And the bad debt expense is

 7 another thing. They took the bad debts -- what you do

 8 is, you estimate, you look at your receivables and you

 9 say, "Well, of the sales I had this year, maybe

 10 one-tenth of 1 percent is not going to be paid," and you

 11 set that up. And then you debit the reserve and you

 12 credit the expense, and this is what the ratepayer pays,

 13 this expense. But then after the customer leaves the

 14 system or fails to pay, you take that receivable and you

 15 give it to a collection agency, and they're getting, you

 16 know, maybe a third of that money back, but they didn't

 17 count that in making their calculation, and that's what

 18 I tried to take into consideration.

 19 I guess I could go on and on, but there are

 20 other things like those that I think are necessary and

 21 should be adjusted.

 22 COMMISSIONER ARGENZIANO: Thank you.

 23 Mr. Chair.

 24 CHAIRMAN CARTER: You're recognized.

 25 COMMISSIONER ARGENZIANO: Maybe the company

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 1 could respond that as well as our staff.

 2 CHAIRMAN CARTER: Sure. No problem.

 3 Mr. Horton.

 4 MR. HORTON: If it's --

 5 CHAIRMAN CARTER: Do you have one of your

 6 witnesses there --

 7 MR. HORTON: What I was going to say is, if

 8 it's appropriate, I would rather have one of the

 9 witnesses respond to that.

 10 CHAIRMAN CARTER: Not a problem.

 11 COMMISSIONER ARGENZIANO: And staff also.

 12 CHAIRMAN CARTER: While you're getting a

 13 witness, let's turn to staff. Do we have technical

 14 staff? Thank you.

 15 MS. BROWN: Commissioner Argenziano, we are

 16 going to file a written recommendation on these matters

 17 to you at the conclusion of the hearing for your

 18 determination and post-hearing recommendation agenda.

 19 So since we have no staff witnesses for the hearing, I'm

 20 a little hesitant to have them testify at the hearing,

 21 but I don't want -- if you really want some answer from

 22 us now, he's right here.

 23 COMMISSIONER ARGENZIANO: Mr. Chair, I don't

 24 want to do anything that jeopardizes things at the

 25 hearing stage. And coming from the legislative process,

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 1 I'm having quite an adjustment learning what you can

 2 blurt out and what you can't. But in trying to make a

 3 determination, I don't want to hear about

 4 unsubstantiated costs. I would like some type of

 5 defense for that, or if we are dealing with

 6 unsubstantiated costs, how we deal with that, have we

 7 done that before, and if that's even correct. I don't

 8 know.

 9 That's part of what I need ultimately at some

 10 point, because at the beginning of the storm hardening

 11 for this particular smaller company, I was concerned

 12 that we were maybe asking them to do too much for the

 13 previous year showing that they hadn't had that much of

 14 a problem, and I didn't want the ratepayer to have to

 15 suffer because we're asking them to do too much. And

 16 now it seems like maybe I'm hearing that maybe some of

 17 the numbers are based on -- I'm not sure what, and

 18 that's what I need some way.

 19 CHAIRMAN CARTER: Okay. Why don't we do this,

 20 Commissioner. We'll defer hearing from staff until

 21 later, and Mr. Horton can get one of his professional

 22 witnesses to speak to that.

 23 COMMISSIONER ARGENZIANO: Great.

 24 MR. HORTON: We'll be happy to, with the

 25 initial observation that this is the first time that

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 1 this has ever occurred in a hearing, but we're happy to

 2 provide that response. And I'm going to ask Ms. Martin

 3 to respond to a portion of it, and Mr. Cutshaw is also

 4 available, so --

 5 MS. CHRISTENSEN: Commissioner --

 6 CHAIRMAN CARTER: One moment.

 7 Ms. Christensen.

 8 COMMISSIONER ARGENZIANO: Well, Mr. Chair, may

 9 I just say something?

 10 CHAIRMAN CARTER: Yes, ma'am.

 11 COMMISSIONER ARGENZIANO: Is the first time it

 12 has ever happened because I'm here? Am I doing

 13 something wrong?

 14 MR. HORTON: No, Commissioner. I probably --

 15 we're happy to give you all the information. We want to

 16 give you all the information and responses appropriate,

 17 recognizing that this is a legal proceeding. So I kind

 18 of figured --

 19 COMMISSIONER ARGENZIANO: If you'll just bear

 20 in mind I'm not an attorney, so that -- you know, that's

 21 where I need help.

 22 CHAIRMAN CARTER: Okay. Ms. Christensen.

 23 MS. CHRISTENSEN: Might I suggest, since this

 24 is coming up in my witness's prefiled testimony,

 25 Mr. Cutshaw and Ms. Martin will also be up to address

 373

 1 the rebuttal testimony, and when they're up here for the

 2 rebuttal testimony, Commissioner, that question I

 3 think -- you know, they'll be sworn in and under oath at

 4 that time, and that probably would be the cleanest and

 5 most standard way to address your question with the way

 6 we've done these proceedings in the past. And then any

 7 follow-up questions you have for those and anything else

 8 that comes up during Mr. Larkin's testimony,

 9 Ms. Merchant's testimony, or Mr. Woolridge's testimony

 10 can be addressed when their witnesses come up for

 11 rebuttal.

 12 CHAIRMAN CARTER: Commissioner Argenziano.

 13 COMMISSIONER ARGENZIANO: That would be fine,

 14 since I've never been known to be too standard. But not

 15 knowing the process really here in a legal proceeding is

 16 where I want to be careful, so that's --

 17 CHAIRMAN CARTER: I understand, Commissioner,

 18 because the language that you heard was kind of new to

 19 all of us. So what we'll do is, obviously, we'll ask

 20 the parties as we come back on rebuttal, when we get to

 21 that point, Ms. Christensen, maybe you could have

 22 Mr. Horton --

 23 MR. HORTON: We'll be prepared to respond.

 24 CHAIRMAN CARTER: -- deal with that, because

 25 even though we are formalized and all that, I do believe

 374

 1 in allowing the Commissioners to ask whatever questions

 2 that are interesting to you, and I think I can find some

 3 basis and justification for that. But I think based

 4 upon where we are now, we can just defer and deal with

 5 it in the rebuttal portion of the case, although I would

 6 like to caution or just kind of give a gentle reminder

 7 to the attorneys on either side to just kind of -- when

 8 we get to that point, because there's going to be a lot

 9 of other stuff happening, that we would like to talk

 10 about that. All right?

 11 MS. CHRISTENSEN: We'll see if we can remind

 12 Commissioner Argenziano she may have some questions for

 13 the witness.

 14 CHAIRMAN CARTER: Okay. Good deal. Staff?

 15 Wait a minute. Commissioner McMurrian, you're

 16 recognized.

 17 COMMISSIONER McMURRIAN: Thank you.

 18 Mr. Larkin, in the exchange earlier with Mr. Horton

 19 about bad debt expense, he asked about the effect of the

 20 recent fuel rate increases on bad debt expense.

 21 THE WITNESS: Yes.

 22 COMMISSIONER McMURRIAN: Can you help me -- I

 23 know you answered him then, but can you help me

 24 understand your answer maybe a little bit in more detail

 25 about how you accounted for the fuel rate increase in

 375

 1 your analysis? And if there's a schedule to point me

 2 to -- I think we looked at one earlier, but I can't

 3 remember where.

 4 THE WITNESS: If you look at my Schedule C-4,

 5 and if you look at the columns, in the year 2000, the

 6 company wrote off $75,000, 75,649. They recovered

 7 either part of that, or from prior years, 38,495, for a

 8 net write-off of 37,154.

 9 Now, I took each year and I totaled those, and

 10 then I got a relationship for that five-year period of

 11 the net write-offs, which is 249,000 to 216,377. So the

 12 relationship between what they billed for base rates and

 13 fuel over the five-year period is a loss of .001152, or

 14 less than a percentage point.

 15 Now, if -- and historically, these things tend

 16 to stay in relationship. So if we apply that write-off

 17 or that loss factor to a revenue figure that included

 18 the increase in fuel, then we get the right number. And

 19 what I did was go to the company's MFRs and went to the

 20 year 2008, and I said, "What does the company say the

 21 total revenues for 2008 will be?" And they said the

 22 total revenues for 2008 would be $61,786,961, excluding

 23 this base rate increase here. And I'll explain why that

 24 should be excluded.

 25 So I took the factor that had been the

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 1 historical relationship of these losses and applied it

 2 to the new number, which included the high increase in

 3 the cost of fuel and energy, and got a higher number.

 4 And that's why I've accounted for the fuel, because I've

 5 used their projected revenue number, but used my

 6 calculation of what I think the write-offs will be.

 7 Now, the revenue conversion factor -- what

 8 that 61 million doesn't include is whatever additional

 9 revenue you will give them in this hearing. Now, that's

 10 accounted for in the conversion factor. So when we

 11 start out with a net income number, we gross that number

 12 up for taxes, bad debt write-off, franchise taxes, to

 13 get this lower number to a higher number, which then

 14 goes into the rates. And that's how they collect the

 15 increase in bad debts associated with the increase in

 16 revenue we're going to give them, you're going to give

 17 them, I'm not going to give them.

 18 COMMISSIONER McMURRIAN: One follow-up,

 19 Mr. Chairman?

 20 CHAIRMAN CARTER: Absolutely.

 21 COMMISSIONER McMURRIAN: Okay. That helps.

 22 That helps me understand how you calculated the bad debt

 23 factor. You don't think that the bad debt factor itself

 24 might go up with the more recent fuel increases that

 25 have happened in the last year or two?

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 1 THE WITNESS: Well, that's a possibility, but

 2 you only have history to look at, you know,

 3 unemployment, the economy should go bad. But, you know,

 4 if the rest of the people in Marianna and Fernandina

 5 Beach have to deal with their incomes going down, I

 6 mean, we shouldn't factor in and protect the utility by

 7 giving them a little extra because they might get some

 8 write-offs. We should be looking at the poor people

 9 that can't pay these bills. They're the ones we should

 10 be concerned about and not -- you know, the utility can

 11 come back and they can ask again if we make a mistake.

 12 COMMISSIONER McMURRIAN: Thank you,

 13 Mr. Larkin. I think we are concerned about those

 14 customers, definitely.

 15 CHAIRMAN CARTER: Commissioners, any further

 16 questions? Staff?

 17 MS. BROWN: No questions.

 18 CHAIRMAN CARTER: Ms. Christensen.

 19 MS. CHRISTENSEN: Just a few brief redirect

 20 questions.

 21 REDIRECT EXAMINATION

 22 BY MS. CHRISTENSEN:

 23 Q. On the topic of the last -- or the last topic

 24 that we were discussing, the uncollectible percentage

 25 factor, have you seen any documentation or explanation

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 1 from the company, other than their statement that new

 2 fuel rates have gone into effect, that explains why they

 3 -- that a higher percentage ratio should be applied to

 4 uncollectibles?

 5 A. Well, the one reason that their rate was

 6 higher is that they never accounted for the subsequent

 7 collections. They just took the write-offs and got the

 8 relationship between revenues and the write-offs and

 9 forgot about they're collecting some of these bad debts

 10 when they send it to a collection agency. That's why

 11 they got 2 percent and I got 1.1 percent.

 12 Q. Okay. Now, let me ask you, in your -- I think

 13 you were asked some questions regarding the low-growth

 14 tree replacement program for replacing trees that are

 15 not in the right-of-way, but are on the private

 16 homeowner's property. And I think Mr. Horton had asked

 17 you about whether or not this was information that

 18 should be provided by the company. Do you recall that

 19 discussion?

 20 A. Yes.

 21 Q. Would an economical way to provide that

 22 information to FPU's customers be to place that

 23 information in their website?

 24 A. Yes. That's another way to do it, yes.

 25 Q. Okay. Excuse me. And I believe you were

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 1 asked some questions about rate case expense and the

 2 fixed contract for Christensen Associates and the

 3 request for additional moneys above and beyond the fixed

 4 contract?

 5 A. Yes.

 6 Q. Mr. Larkin, what's your understanding of what

 7 a fixed contract is supposed to do?

 8 A. My understanding is that a fixed contract is

 9 that you agree to do an amount of work for that dollar

 10 amount, regardless of -- to do certain tasks for that

 11 amount of money, and regardless of whether the tasks

 12 take you more time or less time, then that's the maximum

 13 you can get. You can't get any more if you misjudge and

 14 agree to a bad fixed rate contract.

 15 Q. Okay. And are you aware -- and you may not

 16 be, but are you aware of whether or not Christensen

 17 Associates provided any other assistance in this rate

 18 case other than MFR preparation and preparation for cost

 19 of capital issues in this case?

 20 A. I'm not aware of any.

 21 Q. Now, in your summary you listed some of the

 22 issues that you discuss in your testimony. Did you

 23 intend to be all-inclusive in your summary of all the

 24 adjustments that you recommended in your testimony?

 25 A. No. I just tried to hit the large ones. I

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 1 didn't list every one, and I wasn't aware of every one

 2 that was stipulated, so I tried to skip the ones that

 3 were stipulated that I understood, so I didn't touch

 4 everything.

 5 Q. And finally, you were talking about the cash

 6 that the company has requested, and you had mentioned

 7 that they could transfer the cash to an investment

 8 type --

 9 A. Account, yes.

 10 Q. Account. If they were to transfer the moneys

 11 to an investment type account, would they earn a return

 12 on that money?

 13 A. Well, presumably, yes.

 14 MS. CHRISTENSEN: Okay. I have no further

 15 questions.

 16 CHAIRMAN CARTER: Okay. Thank you. Let's

 17 deal with our exhibits now.

 18 MS. CHRISTENSEN: I would ask to move

 19 Mr. Larkin's exhibits, Appendix 1, HL-1 and HL-2 into

 20 the record.

 21 CHAIRMAN CARTER: Those are marked on the

 22 comprehensive exhibit list as --

 23 MS. CHRISTENSEN: I'm sorry. Twenty-seven,

 24 28, and 29.

 25 CHAIRMAN CARTER: Twenty-seven, 28, and 29,

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 1 Commissioners, on your comprehensive exhibit list. Any

 2 objection from any of the parties? Show it done.

 3 (Exhibit Numbers 27, 28, and 29 were admitted

 4 into the record.)

 5 CHAIRMAN CARTER: Now, will Mr. Larkin also be

 6 available for rebuttal?

 7 MS. CHRISTENSEN: I believe --

 8 CHAIRMAN CARTER: Or actually, for -- go

 9 ahead.

 10 MS. CHRISTENSEN: I believe this is all the

 11 testimony that he has filed in this case.

 12 CHAIRMAN CARTER: Okay. So then he can be

 13 excused.

 14 MS. CHRISTENSEN: Yes. I was going to ask you

 15 that, Commissioner, if I can have my witness excused.

 16 CHAIRMAN CARTER: Absolutely.

 17 MS. CHRISTENSEN: Thank you.

 18 CHAIRMAN CARTER: You may call your next

 19 witness.

 20 MS. CHRISTENSEN: The next witness Office of

 21 Public Counsel would like to call is Dr. Woolridge.

 22 Thereupon,

 23 J. RANDALL WOOLRIDGE

 24 was called as a witness on behalf of the Citizens of the

 25 State of Florida and, having been first duly sworn, was

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 1 examined and testified as follows:

 2 DIRECT EXAMINATION

 3 BY MS. CHRISTENSEN:

 4 Q. Dr. Woolridge, can you please state your name

 5 and business address for the record?

 6 A. Yes. My name is the initial J. Randall

 7 Woolridge, W-o-o-l-r-i-d-g-e. My business address is

 8 120 Haymaker Circle, State College, Pennsylvania.

 9 Q. And, Dr. Woolridge, did you cause to be filed

 10 in this proceeding prefiled direct testimony?

 11 A. Yes.

 12 Q. And do you have any corrections to your

 13 testimony?

 14 A. I have one correction. Actually, there are

 15 two numbers that need correcting. If you look at page

 16 11 of my testimony on line 17, I'm putting -- I'm there

 17 simply stating debt cost amounts and capitalization

 18 amounts and ratios on line 17. The table below that has

 19 the correct numbers. I've adopted the company's cost

 20 rates for long-term debt and preferred stock. On line

 21 17, instead of 6.05, that should be 7.96, and instead of

 22 4.81, it should be 4.75.

 23 Q. With those corrections to your prefiled

 24 testimony, if I were to ask you those questions today,

 25 would your answers be the same?

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 1 A. Yes.

 2 MS. CHRISTENSEN: I would ask to have

 3 Dr. Woolridge's testimony entered into the record as

 4 though read.

 5 CHAIRMAN CARTER: The prefiled testimony will

 6 adopted into the record as though read.

 7 BY MS. CHRISTENSEN:

 8 Q. Dr. Woolridge, did you also attach exhibits to

 9 your prefiled testimony, Appendix A and Exhibits JRW-1

 10 through JRW-16?

 11 A. Yes.

 12 Q. Do you have any corrections to make to any of

 13 your exhibits?

 14 A. No.

 15 (Exhibit Numbers 30 - 46 were marked for

 16 identification.)

 17

 18

 19

 20

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 1 BY MS. CHRISTENSEN:

 2 Q. Dr. Woolridge, can you please summarize your

 3 testimony?

 4 A. Yes. Mr. Camfield previously had identified

 5 and talked about the cost of capital or rate of return

 6 and its importance in utility rate setting, so I'm not

 7 going to repeat that.

 8 A major theme of my testimony is that capital

 9 costs for companies in the United States today are

 10 really at historic lows. If you look at -- there's

 11 three components to capital costs, and primarily if you

 12 look at -- what has happened is that interest rates have

 13 declined, obviously. The equity risk premium that you

 14 add to that to get an equity cost rate has declined.

 15 And the tax rate on investment income has gone down,

 16 which means that investors' required return is lower

 17 than it has been in the past.

 18 Now, if you just focus on interest rates real

 19 quickly, you know, the long-term Treasury rates have

 20 been in the 4 to 5 percent range over the last five

 21 years. Prior to that time, this time period, we haven't

 22 seen long-term Treasury rates as low as 4 and 5 percent

 23 since the early 1960s. So to give you a time frame,

 24 that's some 40 to 45 years. In fact, you almost have to

 25 go back to '61 to '64, where we find a time period when

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 1 interest rates have been that low.

 2 The major contention in this case is obviously

 3 the cost of equity. Mr. Camfield has estimated the

 4 company's cost of equity at 11-1/2 percent. My studies

 5 indicate it's 9.15 percent.

 6 Now, in establishing a cost of equity for the

 7 company, Mr. Camfield has used two proxy groups of

 8 electric and gas companies, and I've used those

 9 companies. I've performed a risk study of the companies

 10 and compared it to FPU and find that FPU and the

 11 electric companies are rather comparable in risk,

 12 whereas FPU appears a little riskier than the gas

 13 companies.

 14 Now, the major issue, as I said, is what is

 15 the equity cost rate. There are several primary issues

 16 between Mr. Camfield and myself. Number one is,

 17 Mr. Camfield gives very little weight to his DCF

 18 results, in my opinion. Second of all, and I think a

 19 primary contention, is his exclusive use of historic

 20 stock and bond returns to establish what the risk

 21 premium is.

 22 Now, in addition to those two issues, he has

 23 included an issuance or flotation cost, and in certain

 24 approaches, he has applied a premium for the size of the

 25 company, which I haven't. I haven't included those, and

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 1 I explain that in my testimony.

 2 Now, just very briefly talking about the cost

 3 rate approaches, his DCF approach provides equity cost

 4 rates prior to issuance cost of 9.3 percent and

 5 9.2 percent for the two groups. Those are very close to

 6 my numbers, and especially if you update his figures for

 7 the more recent data, we have pretty much the same DCF

 8 equity cost rates. On his capital asset pricing model,

 9 his risk premium, and his realized market return

 10 approaches, basically these are all risk premium

 11 approaches. You take a risk-free rate and you add a

 12 risk premium. Since he filed his testimony, interest

 13 rates have come down, of course, so the cost rates will

 14 be lower today. But the big issue is, he has relied

 15 exclusively on historic stock and bond returns to come

 16 up with an equity risk premium. For example, in his

 17 capital asset pricing model approach, he uses an

 18 expected stock market return based off of historic

 19 figures of 13 percent.

 20 Now, surveys of CFOs and financial forecasters

 21 today, no one expects to have a stock return in the

 22 future of 13 percent. It's just unrealistic given

 23 today's conditions. In fact, if you look at the

 24 company's pension plan, their expected return on pension

 25 assets doesn't include a stock return of 13 percent.

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 1 It's just unrealistic. Historically, equity cost rates

 2 have been slightly higher than projected rates, and as I

 3 explain in my testimony, there's a lot of empirical

 4 reasons for that.

 5 Anyhow, based off that expected stock market

 6 return, he comes up with an equity risk premium of

 7 8.27 percent. And in my testimony on schedule -- or

 8 Exhibit JRW-10, page 6, I lay out all the studies I've

 9 been able to find on the equity risk premium in the last

 10 10 years, and none of those figures are as high as

 11 8.27 percent.

 12 And in fact, if you look at the more recent

 13 approaches, because there are different approaches to

 14 apply to find an equity risk premium, a common way is to

 15 look at surveys of CFOs. CFOs use this stuff every day.

 16 In December of 2007, the CFO survey of 500 CFOs, the

 17 average indicated an equity risk premium of 4.24

 18 percent. Again, they use this type of data all the time

 19 in making investing and financing decisions. Again,

 20 these figures are so much lower than the equity risk

 21 premiums used by Mr. Camfield just because he relies

 22 strictly on historic data.

 23 So in summary, the major theme is that

 24 historic cost rates for capital for companies are low

 25 today compared to the past, and my 9.15 percent

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 1 recommendation reflects this really low cost rate

 2 environment for companies for capital.

 3 MS. CHRISTENSEN: I tender Dr. Woolridge for

 4 cross-examination.

 5 CHAIRMAN CARTER: Just one second, Mr. Horton.

 6 Mr. Woolridge, you said that capital costs are

 7 extremely low; right?

 8 THE WITNESS: Yes.

 9 CHAIRMAN CARTER: Now, this is an issue that

 10 I've been following real closely lately too. And from

 11 reading the Wall Street Journal and listening to CNBC,

 12 what they're saying is that the rates are low, but the

 13 loans are not readily available. Does that line up with

 14 what you've been reading and studying?

 15 THE WITNESS: Well, that's obviously a factor,

 16 what has happened since the mid-summer, where there has

 17 been somewhat of a credit crisis going upon because of

 18 the defaults on the real estate. A lot of the financial

 19 products created by Wall Street has created a credit

 20 squeeze to some degree, especially in the riskier

 21 environments, and that's tied primarily to, you know,

 22 the mortgage -- you know, the run-up in housing prices,

 23 the mortgage going to the subprime market and that sort

 24 of thing. That's where most of that's tied to.

 25 CHAIRMAN CARTER: But this has nothing to do

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 1 with what you're talking about? Is that what you're

 2 saying?

 3 THE WITNESS: I think what has happened is,

 4 since maybe last year, we've seen risk premiums go up,

 5 say, since mid-summer or so last year tied to this. If

 6 you look at the yield spreads on corporate bonds,

 7 they've gone up somewhat. But they're still at

 8 relatively low levels compared to, say, the last 30 or

 9 40 or 50 years.

 10 CHAIRMAN CARTER: I was just interested in

 11 hearing what you had to say, because from what I was

 12 reading, they were saying that while the Feds have

 13 lowered the rates, but because of a number of things

 14 that have happened within the financial community within

 15 the last year or so, that the funds for loans are not

 16 necessarily readily available by either corporate or

 17 individual borrowers.

 18 THE WITNESS: Well, what has happened is, in

 19 segments of the market, in particular the riskier

 20 segments of the market, that's where it's tougher to get

 21 a loan, just because there's so much lending going on,

 22 and a lot of these financial institutions have gotten

 23 burned lending in those portions of the market. Plus

 24 when you had housing prices crashing and people just

 25 forfeiting on their loans because their loans are at

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 1 500,000 and their house is worth 400,000, that's where a

 2 lot of the lenders got in trouble.

 3 CHAIRMAN CARTER: Okay. Commissioners?

 4 Commissioner Skop.

 5 COMMISSIONER SKOP: Thank you, Chairman

 6 Carter. Just a quick question to the witness with

 7 respect to the capital asset pricing model.

 8 I guess from what I hear, you're advocating

 9 basing the -- or discarding historical market returns in

 10 favor of CFO type data or what their consensus is on an

 11 appropriate return. And why -- again, a historic

 12 approach I think is what I've always seen used for that

 13 model, but why wouldn't it be more appropriate in your

 14 eyes to use data over a shorter time period, and what

 15 type of impact would that have if, you know, we went

 16 through a different economic time where we had

 17 significant inflation and rates suddenly increased?

 18 THE WITNESS: Well, you're incorrect. I did

 19 use historic returns. If you look at my schedule, page

 20 6 of Schedule 10, there's three approaches to developing

 21 a equity risk premium. One is using historic returns.

 22 Another is using what they call ex ante models, and

 23 these are the studies that have been done over the last

 24 decade using expected return models to compute. And

 25 these have been done by the best academics out there.

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 1 And the third way is to use surveys.

 2 Obviously, I give equal weight to all these,

 3 so I use historic returns. I look at -- you know,

 4 there's just not one historic return. They compute

 5 historic returns using different measures over different

 6 time periods, that sort of thing. So at the top of

 7 Exhibit JRW-10, page 6, those are all the historic

 8 return studies I can find. Some of them go back to

 9 1802, like the one by -- well, Goyal and Welch went back

 10 to 1872. So I did use historic returns. I also used

 11 ex ante models, such as some of the models were

 12 commissioned by the office of the chief actuary of the

 13 Social Security Administration. And then I used

 14 surveys.

 15 The survey of CFOs I highlight, first of all,

 16 CFOs are well aware of what historic returns are. I

 17 mean, every CFO has taken a finance course and has seen

 18 the Ibbotson data. Yet as recently as December of this

 19 past year when they were asked what's their expected

 20 equity risk premium, the average of over 500 CFOs is 5

 21 -- what is it? 4.24 percent. I mean, these people use

 22 that sort of data every day, and they're well aware of

 23 what historic returns are. So as I say, it reflects

 24 what the current market environment is.

 25 COMMISSIONER SKOP: Mr. Chair, just a quick

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 1 follow-up with respect to the surveys, the 500 CFOs. I

 2 imagine that was through diversified industry and not

 3 specific to utilities; would that be correct?

 4 THE WITNESS: Exactly.

 5 COMMISSIONER SKOP: All right. Thank you.

 6 CHAIRMAN CARTER: Thank you, Commissioners. I

 7 appreciate that. I just wanted to get that out while it

 8 was on my brain before I forgot. And we still may have

 9 other questions, but at this point in time, Mr. Horton,

 10 you're recognized.

 11 MR. HORTON: Yes, sir. Thank you,

 12 Mr. Chairman.

 13 CROSS-EXAMINATION

 14 BY MR. HORTON:

 15 Q. Mr. Woolridge, in your summary, I think you

 16 made reference to the pension return.

 17 A. Yes.

 18 Q. And that would not all be equity, would it?

 19 That would be a mix? That return would be a mix of

 20 various things, equity, fixed income, cash?

 21 A. Yes. I didn't see the breakdown, but I'm sure

 22 if I found -- I looked through the data requests, and I

 23 did not see a breakdown for equity versus debt. It was

 24 just overall at 8-1/2 percent. And I'm 100 percent

 25 certain it doesn't include an equity return of

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 1 13 percent.

 2 Q. Okay. Turn to page 1 of 3 of JRW-3, if you

 3 would, please, sir.

 4 A. Yes.

 5 Q. And on that page, you list a number of

 6 electric and gas utilities, and those are the sample

 7 companies that you used, are they not?

 8 A. Yes.

 9 Q. All right. I think I heard what you said

 10 earlier, but I want to make sure. How did you select

 11 those companies?

 12 A. Generally, they were the companies that

 13 Mr. Camfield used.

 14 Q. Okay. You didn't do any separate risk

 15 analysis or any separate -- you just used the same ones

 16 he did?

 17 A. Pretty much so, yes.

 18 Q. Okay. I'm through with that exhibit.

 19 In discovering through your studies equity

 20 return recommendations in other proceedings, have you

 21 used the same sample that you employ in this present

 22 proceeding?

 23 A. Excuse me. I don't understand your question.

 24 Q. Have you used different sample companies in

 25 other proceedings?

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 1 A. Yes.

 2 Q. Are there any particular reasons why you would

 3 use different sample companies in other proceedings?

 4 A. Generally if a witness likes one group -- I

 5 mean, you look at companies that have certain

 6 characteristics. The number of gas companies is rather

 7 limited, so you're pretty much -- and water companies,

 8 the sample is pretty limited. You have a larger number

 9 of electric companies to use. I've used as many as 30

 10 electric companies in a study.

 11 Q. The methods that you employ in other

 12 proceedings for your cost of capital -- excuse me, cost

 13 of equity methods, I'm sorry, are the methods that you

 14 employ in other proceedings similar to those that you've

 15 taken in this proceeding?

 16 A. Generally, yes.

 17 Q. And that includes the DCF and CAPM model;

 18 correct?

 19 A. Yes.

 20 Q. So you've advanced the DCF and CAPM models in

 21 your testimony in those other proceedings?

 22 A. Yes, as a general approach. I feel that

 23 especially the DCF model, because of the nature of the

 24 business of providing electric service, I believe it

 25 provides a good indication of a capital cost for, in

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 1 this case, FPU.

 2 MR. HORTON: Can I have just one second?

 3 CHAIRMAN CARTER: You're recognized. While

 4 you're doing that, let me -- Commissioners, with your

 5 indulgence, since you're already on this Exhibit JR2-3,

 6 on this chart, I was looking just trying to draw some

 7 kind of comparison or some kind of conclusion with the

 8 electrical versus the gas in terms of the comparison for

 9 FPUC, FPU, Florida Public Utilities.

 10 What does -- I mean, I'm trying to draw --

 11 what kind of conclusion do you draw from the two of

 12 these? Because it seems to me that you've got -- if you

 13 go down to the gas one, you're showing probably one of

 14 the lowest market-to-book ratios and one of the highest

 15 PE ratios, and then you've got a lower service

 16 territory, if you will. Do those correlate, or am I

 17 looking at apples and grapefruits?

 18 THE WITNESS: Well, I think if you compare

 19 these two groups -- and again, Mr. Camfield really

 20 provided the emphasis to use two different groups. I

 21 mean, I think one thing you see, I believe, is that the

 22 gas companies are less risky than these electric

 23 companies. And actually, the basis of that goes over to

 24 page 2 of 3 of Exhibit JRW-3, where I've looked at

 25 various risk metrics provided by Value Line, and on most

 474

 1 of those risk metrics, it appears that the gas companies

 2 are a little less risky than the electric companies, and

 3 the gas companies are a little less risky than FPU,

 4 whether you're talking about how predictable their

 5 earnings are, their stock price stability in the case of

 6 -- for example, the average for the gas companies is 98

 7 out of 100. The average for the electrics is 91 out of

 8 100. So I just look at different risk metrics to see

 9 which one appears to be less risky, and I would say from

 10 this that the gas companies are performing a little

 11 better. They have higher average return on equities,

 12 that sort of thing, and they have slightly lower risk,

 13 in this time.

 14 CHAIRMAN CARTER: And because of that factor,

 15 is there a premium on the risk for electric companies

 16 versus the risk on gas companies?

 17 THE WITNESS: No. I think where you see it

 18 is, if you look at the average market-to-book ratio, the

 19 average market-to-book ratio for the gas companies is

 20 2.06. The average for the electric companies is 1.65.

 21 So you see that because of this, they have a higher

 22 valuation. They're priced higher relative to the book

 23 value of their equity. And that's where you really see

 24 this relationship, especially for regulated companies.

 25 CHAIRMAN CARTER: So then there's no cost

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 1 associated with what you see? There's a higher risk for

 2 the electric companies versus the gas companies?

 3 THE WITNESS: I would say there's a higher

 4 risk for -- right now if you look at these two groups, I

 5 would say, yes, the risk is a little bit higher for the

 6 electrics than the gas.

 7 CHAIRMAN CARTER: And would that not be priced

 8 as such in terms of the financial markets?

 9 THE WITNESS: Well, it's priced in terms of

 10 their market-to-book ratios, yes. They sell at a

 11 premium, a higher market-to-book ratio.

 12 CHAIRMAN CARTER: Okay. Mr. Horton.

 13 BY MR. HORTON:

 14 Q. Yes. Mr. Woolridge, that same page you were

 15 referring to, page 2 of 3 of that exhibit.

 16 A. Yes.

 17 Q. Aren't the Betas for all of the companies in

 18 those two samples higher than the Beta for Florida

 19 Public Utilities?

 20 A. Yes.

 21 Q. With respect to your DCF analysis, for

 22 estimates of growth, you appear to rely on analysts'

 23 expectations for 2007 for some period in the future.

 24 Would you agree with that? Is that correct?

 25 A. That's one of the inputs; that's correct.

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 1 Q. Over what forward time frame does the

 2 analysts' projections cover?

 3 A. Three to five years.

 4 Q. If you were to sample the analysts today,

 5 would you expect the estimates would be above or below

 6 analysts' expectations of 2007?

 7 A. Well, these were collected in December of

 8 2007, and if I look at today, which is two months later

 9 -- I was just looking at some gas data, and they're a

 10 little bit lower. But I've studied these things and

 11 have studies on the accuracy of these things. They tend

 12 to be a little upwardly biased. I think it's pretty

 13 well known in the financial community that analysts'

 14 projected earning per share growth rates are high, and

 15 the further out you go, the more upwardly biased they

 16 are.

 17 CHAIRMAN CARTER: Mr. Horton, I see some smoke

 18 coming out of your ears right there, and your wheels are

 19 probably turning. Would this be an appropriate time for

 20 us to kind of take a little break and come back in?

 21 MR. HORTON: That would be fine.

 22 CHAIRMAN CARTER: Because you're on this

 23 financial area here, and I think -- it looked like you

 24 needed a couple of minutes to get your notes together.

 25 MR. HORTON: To be honest with you, he

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 1 actually answered some of our questions earlier on, and

 2 I was trying to eliminate some of those.

 3 CHAIRMAN CARTER: Well, I'll tell you what.

 4 We'll give you an opportunity to look over your notes

 5 and be sure on that. Commissioners, I'm looking at

 6 3:26. Let's come back at 3:36. I don't know how to

 7 calibrate that with the clocks on the wall. Ten

 8 minutes, just go with 10 minutes, wherever you can find

 9 it. We're on recess.

 10 (Short recess.)

 11 CHAIRMAN CARTER: We are back on the record,

 12 and the last time we left, Mr. Horton was looking at his

 13 notes to ensure that he had asked the appropriate

 14 questions on cross-examination. Mr. Horton, you're

 15 recognized, sir.

 16 MR. HORTON: Thank you, sir.

 17 BY MR. HORTON:

 18 Q. Mr. Woolridge, in your observation over recent

 19 years of regulatory agencies, would you agree that

 20 regulatory agencies have generally settled on allowed

 21 rate of return levels around 8 percent average?

 22 A. Allowed rate of return?

 23 Q. Yes, sir.

 24 A. About 8 percent?

 25 Q. Yes, sir.

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 1 A. Does that include debt? I mean, overall rates

 2 of return; correct?

 3 Q. Overall.

 4 A. I don't know. I would say 7-1/2 to 8-1/2

 5 percent. I don't know. I mean, I look probably more at

 6 the allowed equity return more than the allowed overall

 7 return.

 8 Q. Okay. With respect to interest rates, I think

 9 in your testimony -- and I'm sorry. I don't have a page

 10 cite, but let me ask the question. You have reviewed

 11 the short-term -- have you reviewed the short-term

 12 Treasury yields, intermediate-term Treasury yields, or

 13 the average yields on Baa and AAA corporate debt?

 14 A. I've looked at long-term Treasuries.

 15 Obviously, I do an analysis between Treasuries and

 16 corporate -- Treasuries and utility bonds. But

 17 primarily, most of my observations are based off of

 18 Treasury securities, and that's because that's what the

 19 market focuses on. You know, if you turn on CNBC, they

 20 show you the rate on the 10-year Treasury or the 30-year

 21 Treasury. That's what the market really focuses on, is

 22 long-term Treasury rates.

 23 Q. What does the empirical record indicate

 24 regarding yields on debt?

 25 A. What do you mean? I don't understand your

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 1 question. I mean, the yields on debt, if you look over

 2 the last -- as I explain in my testimony, we haven't

 3 seen Treasury rates this low since the 1960s. Long-term

 4 Treasury -- and it's been since -- you know, they really

 5 declined to this level in the 2002, 2003 time period,

 6 but they've stayed that low, and they've stayed that low

 7 for an extended period of time. We would have to go

 8 back to the '50s and '60s to see long-term Treasury

 9 rates that low.

 10 Q. Do you know what the current yield on Baa

 11 corporate debt is?

 12 A. The current yield on Baa -- what maturity?

 13 Q. I'm sorry?

 14 A. What maturity?

 15 Q. Longer than 20 years.

 16 A. Long-term. It's in the vicinity of 6 percent

 17 or so. I can't give you the exact number today. I

 18 would have to look it up.

 19 MR. HORTON: Thank you. I have no other

 20 questions.

 21 CHAIRMAN CARTER: Thank you. Staff.

 22 MS. BROWN: We have no questions.

 23 CHAIRMAN CARTER: Mr. Christensen, any

 24 redirect?

 25 MS. CHRISTENSEN: Thank you.

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 1 REDIRECT EXAMINATION

 2 BY MS. CHRISTENSEN:

 3 Q. Dr. Woolridge, you were explaining earlier the

 4 market-to-book ratio and how the gas companies'

 5 market-to-book ratio is higher than the electric

 6 companies'. Can you explain a little bit more what the

 7 market-to-book ratio shows?

 8 A. Well, I think I explain that in my testimony,

 9 and actually, I lay it out in an exhibit. I demonstrate

 10 the relationship, and it's fairly strong for utilities.

 11 It's very strong for financial companies as well. If

 12 you look at Exhibit JRW-5, I show the relationship

 13 between expected returns on equity and market-to-book

 14 ratios for electric utilities, for natural gas

 15 companies, and for water companies, and it's very

 16 strong. Companies that have higher expected returns on

 17 equity have higher market-to-book ratios. And as I

 18 explain in my testimony, the reason I use that

 19 relationship is because, you know, basic economics tells

 20 us that if your expected return on equity is greater

 21 than your cost of equity, your market-to-book ratio is

 22 greater than 1. And I use it and in my testimony

 23 explain why -- part of why my recommendation is very

 24 reasonable given these statistics. Obviously, returns

 25 on equity for these companies are higher than the cost

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 1 of equity, and that's why their market-to-book ratios

 2 are greater than 1.

 3 Q. And Dr. Woolridge, if you know -- I think you

 4 were asked if you knew what the average rate of return

 5 for electric companies was for 2007, and you said you

 6 had looked and were more familiar with returns on

 7 equities. Do you know what that would be for 2007?

 8 A. Well, I mean, the average returns on equity

 9 allowed have been coming down over the last three to

 10 four years, I think, as commissions have recognized that

 11 equity cost rates are lower because of the reasons I

 12 said, that capital costs are at historic lows. I mean,

 13 if you look at more recent data, I was just in a case in

 14 Connecticut, Connecticut Light & Power, and their

 15 allowed return was 9.4 percent. The fact is, I think

 16 commissions are finally realizing that capital costs are

 17 indeed low and that the cost of equity has been coming

 18 down as well.

 19 Q. And the Connecticut case you're referencing,

 20 that would be a distribution and transmission type of

 21 company?

 22 A. Yes. And the decision was like January 28th.

 23 It was a very recent decision.

 24 MS. CHRISTENSEN: Okay. Thank you. I have no

 25 further questions.

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 1 CHAIRMAN CARTER: Okay. Thank you very much.

 2 Let's deal with our exhibits.

 3 MS. CHRISTENSEN: I would ask to have

 4 Dr. Woolridge's exhibits, and that would be Number 30

 5 through 46, moved into the record.

 6 CHAIRMAN CARTER: Thirty through 46. Any

 7 objections? Without objection, show it done.

 8 (Exhibit Numbers 30 through 46 were admitted

 9 into the record.)

 10 CHAIRMAN CARTER: And Mr. Woolridge may be

 11 excused. Call your next witness.

 12 MS. CHRISTENSEN: Office of Public Counsel

 13 would like to call Patricia Merchant to the stand.

 14 Thereupon,

 15 PATRICIA W. MERCHANT

 16 was called as a witness on behalf of the Citizens of the

 17 State of Florida and, having been first duly sworn, was

 18 examined and testified as follows:

 19 DIRECT EXAMINATION

 20 BY MS. CHRISTENSEN:

 21 Q. Ms. Merchant, can you please state your name

 22 and business address for the record, please.

 23 A. My name is Patricia W. Merchant, and I'm

 24 employed by the Office of Public Counsel, and my address

 25 is 111 West Madison Street, Tallahassee, Florida, 32301.

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 1 Q. Ms. Merchant, did you cause to be filed

 2 prefiled testimony in this docket?

 3 A. Yes, I did.

 4 Q. And do you have any corrections to your

 5 testimony?

 6 A. No, I do not.

 7 Q. If I were to ask you the same questions today,

 8 would your answers be the same?

 9 A. Yes, they would.

 10 MS. CHRISTENSEN: I would ask that

 11 Ms. Merchant's prefiled testimony be entered into the

 12 record as though read.

 13 CHAIRMAN CARTER: The prefiled testimony will

 14 be entered into the record as though read.

 15 BY MS. CHRISTENSEN:

 16 Q. Ms. Merchant, do you have exhibits attached to

 17 your prefiled testimony labeled PM-1 through PM-3?

 18 A. Yes, I do.

 19 Q. Do you have any corrections to those exhibits?

 20 A. No.

 21 (Exhibit Numbers 47 - 49 were marked for

 22 identification.)

 23

 24

 25

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 1 BY MS. CHRISTENSEN:

 2 Q. Ms. Merchant, can I ask you to please

 3 summarize your testimony.

 4 A. Thank you. Good afternoon, Commissioners.

 5 We've stipulated many of the issues in this case that

 6 relate to my testimony, so I'm only going to summarize

 7 the ones that are left outstanding.

 8 First I would like to talk about the new

 9 positions that the company has requested as over and

 10 above increases in their MFRs and in subsequent filings

 11 in the rebuttal testimony.

 12 In the MFRs, the company has requested five

 13 new positions. These included information technology

 14 program vacancies, a combined joint use audit and pole

 15 inspections position for storm hardening. The third one

 16 that they asked for is a corporate accounting position

 17 for special audits and internal control. They also

 18 asked for a new customer relations analyst and

 19 coordinator for internal control, and they asked for a

 20 new corporate services administrator for compliance.

 21 In response to OPC discovery questions

 22 regarding incremental training costs, the company added

 23 in their rebuttal testimony yet another new position for

 24 a full-time training coordinator.

 25 There are varying reasons why I have agreed or

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 1 disagreed with the new positions, which I will address.

 2 One main thing that has existed throughout this case has

 3 been the lack of supporting detail provided by the

 4 company and confusion surrounding the numerous over and

 5 above adjustments requested. Additionally, with the

 6 exception of the information technology positions, no

 7 hiring activities have occurred to date other than

 8 announcing the vacancies. We learned just last week

 9 that the IT positions were not new and had been filled

 10 in 2007. And after review of the actual salaries that

 11 the company has for those positions, we've stipulated

 12 that issue and included those in the case.

 13 I've next recommended that the Commission

 14 allow the new position for the storm hardening

 15 activities, for monitoring pole inspections and joint

 16 use audits. However, I believe that this new position

 17 should also absorb some of the other incremental safety

 18 and training components that they've requested for the

 19 Northwest Division, and because of this, I've

 20 recommended that no additional travel allowance be given

 21 for that position because he'll be taking care of that

 22 local territory.

 23 I also believe that the existing safety

 24 coordinator in the Northeast Division can absorb the

 25 additional reporting and training needs for that

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 1 operating territory.

 2 Additionally, I recommend that the company

 3 recover the salary for the new corporate accounting

 4 position, but that position appears -- it appears

 5 justified, but it won't be filled until at least the

 6 middle of 2008, and thus, I've recommended that only 50

 7 percent of that position be included for rate setting

 8 purposes.

 9 And for the remaining two positions, for the

 10 customer relations and the clerical customer service

 11 administrator, I've recommended that these positions not

 12 be approved. The company has failed to adequately

 13 support the need for these incremental positions, and

 14 the company's responses to much of the requested

 15 discovery was not sufficient.

 16 I next take issue with the requested increase

 17 related to the salary survey which was completed in late

 18 December 2007. First, the company admitted that the

 19 electric portion of the salary survey adjustment was

 20 overstated by approximately 23,000. Second, even if the

 21 Commission considers that any adjustments are needed,

 22 the majority of the increase that the company has

 23 proposed relates to increased salary ranges, not pay

 24 rate increases. They're not immediate raises to the

 25 employees, and if granted, may be given throughout the

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 1 year, and as such, a full year of salary increase for

 2 the salary survey is unwarranted. Accordingly, I

 3 believe that the over and above adjustment for the

 4 salary survey should be removed.

 5 The company also included increases in

 6 executive salary expenses for the company's three

 7 executives in 2008, and the only justification they

 8 provided to me or to the Office of Public Counsel prior

 9 to rebuttal testimony was the supporting calculations,

 10 how they calculated the adjustment, and a statement that

 11 said that this adjustment was necessary to bring their

 12 salaries into compliance with the market. The 2006

 13 executive salary levels including incentives were

 14 escalated from 2004 to 2006 by 21.5 percent, and that's

 15 prior to the test year, and then their over and above

 16 adjustment is an additional 11 percent for 2007 and a

 17 5.5 percent for 2008.

 18 Without further support, I do not believe the

 19 company has justified why its executives should receive

 20 these levels of pay increases, especially when its

 21 rank-and-file employees received only 5.5 percent pay

 22 increases. And those were not necessarily pay

 23 increases. They've asked for the pay grade increase,

 24 not necessarily a pay increase. And accordingly, I've

 25 removed the company's over and above adjustment for

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 1 executive salaries.

 2 Lastly, I testify that the company's request

 3 to receive a full year of rate base recovery for a

 4 transformer is inappropriate because the project won't

 5 be placed in service until at least spring 2008. The

 6 proper ratemaking adjustment would be to reflect this

 7 plant on a 13-month average basis in rate base based on

 8 the date that the plant is put in service. The

 9 rationale provided for this exception by the company was

 10 that that a future rate case might be needed if full

 11 recovery is not allowed. The test year matching concept

 12 provides that the average rate base is matched with

 13 average cost of capital, revenues, expenses, and

 14 customer billing factors. If you mismatch one of the

 15 individual components, the risk increases that the

 16 resulting rates will be skewed and unreasonable.

 17 And this concludes my summary.

 18 MS. CHRISTENSEN: I tender the witness for

 19 cross-examination.

 20 CHAIRMAN CARTER: Okay. First we'll hear from

 21 the bench. Commissioner Skop, you're recognized.

 22 COMMISSIONER SKOP: Thank you, Chairman

 23 Carter. Getting back to the thing, I guess

 24 Ms. Merchant's testimony deals somewhat with percentage

 25 increases of executive compensation, so at the

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 1 appropriate time, it would still be nice see the

 2 unredacted confidential exhibit. I don't know whether

 3 staff or what have you, but I would like to see it, and

 4 I think Commissioner Argenziano also had an interest in

 5 seeing that.

 6 MS. BROWN: Mr. Chairman, we have them, and we

 7 can pass them out for you all right now if you would

 8 like.

 9 CHAIRMAN CARTER: I suppose this is as good a

 10 time as any. Let's take a moment and pass those out.

 11 Thank you.

 12 (Documents distributed.)

 13 CHAIRMAN CARTER: Commissioners, do you want

 14 to take a moment to look those over before we go

 15 further?

 16 Okay. Mr. Horton, or is it -- let's see.

 17 Mr. Konuch. Did I get it right this time?

 18 MR. KONUCH: We have no questions at this

 19 time.

 20 CHAIRMAN CARTER: No questions. Thank you.

 21 Mr. Hatch?

 22 MR. HATCH: No questions.

 23 CHAIRMAN CARTER: Mr. Horton.

 24 MR. HORTON: Yes. It's my turn again.

 25 CHAIRMAN CARTER: You're recognized.

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 1 CROSS-EXAMINATION

 2 BY MR. HORTON:

 3 Q. Ms. Merchant, good afternoon.

 4 A. Good afternoon.

 5 Q. A couple of things you didn't -- I want to

 6 talk to you about a couple of things you didn't mention

 7 in your summary, first of all, transmission inspections.

 8 A. Okay.

 9 Q. Now, the company is proposing use a contractor

 10 for inspection of its transmission poles, and you agree

 11 that this is something that needs to be done; correct?

 12 A. Yes. It's in compliance with the storm plan.

 13 Q. And the company received an estimate and used

 14 this as the basis for their request; correct?

 15 A. Yes. They had one estimate. It wasn't a

 16 contract or a bid or anything like that.

 17 Q. And your issue there is that they only had one

 18 estimate. The company's proposal is to do the

 19 inspections over a six-year cycle, and they've included

 20 one-sixth of the expense in the test year, and so far we

 21 have no objection. You don't have any objection to

 22 those proposals, do you?

 23 A. To a six-year amortization of the cost?

 24 Q. Right, the one-sixth for the year, yes.

 25 A. No.

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 1 Q. The objection is strictly that we only had one

 2 estimate?

 3 A. That's correct.

 4 Q. And I believe you also expressed concern at

 5 the fact that the estimate was for a specific period of

 6 time; correct?

 7 A. That's correct. It was based on 2006

 8 information.

 9 I also expressed on page 37 of my testimony

 10 that -- and 38 that they -- no, just 37, that they were

 11 not exactly sure what the cost was going to be, so there

 12 was still some reservation on the company's part as to

 13 what the real contract would be.

 14 Q. Well, isn't it the case here that the company

 15 did request from a vendor an estimate on the cost to do

 16 the inspections, they received that request, and based

 17 their estimate -- this wasn't for a purchase, but this

 18 was for an estimate to include the cost associated with

 19 the inspection. Isn't that where we are now? They got

 20 an estimate?

 21 A. Right. They have one estimate, and our

 22 position on this is that they should have gotten more

 23 than one just to be able to tell us that -- you know,

 24 similar to how they did for the pole costs. They got, I

 25 think, four for the pole, the concrete pole costs, but

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 1 here they got one, and that was just what we were

 2 looking at. And all I did was reduce it by 25 percent

 3 because they didn't have but just one. So we're

 4 recognizing 75 percent of the cost, and the 25 percent

 5 that we've recommended to be disallowed is basically for

 6 not having more than one estimate.

 7 Q. Would you expect vendors -- if you were a

 8 vendor, would you be willing to spend a lot of time and

 9 effort on the preparation of an estimate if you knew

 10 there wasn't a chance of a purchase or if it was just

 11 being used for preparation?

 12 MS. CHRISTENSEN: Objection. Calls for

 13 speculation.

 14 MR. HORTON: I'll rephrase it.

 15 CHAIRMAN CARTER: Okay.

 16 BY MR. HORTON:

 17 Q. Have you ever had the opportunity to request

 18 estimates from vendors?

 19 A. Yes, many times.

 20 Q. For what purpose?

 21 A. I just did a kitchen remodel.

 22 Q. And how many estimates did you get?

 23 A. Lots. For all different types of -- for the

 24 different types of contractors that I needed, I went and

 25 got probably two or three for each one.

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 1 Q. And they knew that you were in a position to

 2 award that estimate, go ahead and make a purchase at

 3 that time, did they not?

 4 A. I don't know what they knew, but -- I mean, I

 5 was asking for their business, or I was inquiring about

 6 their business. If they're in the business to -- if

 7 they want my business, then they would probably answer

 8 my question. And that's the experience I had, is that

 9 they were willing to give me estimates.

 10 Q. Do you think if they had not known that you

 11 were willing to give them the business that they would

 12 have been as willing to give you an estimate?

 13 A. I didn't go up front and tell them that I'm

 14 not going to choose them. And we did -- I think that's

 15 just a common thing. You're not going to give all your

 16 cards when you're asking for an estimate, but you just

 17 see what it is. You just see what the range is, you see

 18 how their quality is. You might pay more for better

 19 quality, or they might be equal quality, and one is a

 20 cheaper contract. So you've just got to look at each

 21 individual, and then when you have all these different

 22 contracts together, you can consider which one is the

 23 best option to go with.

 24 Q. All right. But you took the estimate. You

 25 recognize that this needs to be done and there is a

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 1 cost, and you took the estimate and reduced it by

 2 25 percent, and your only basis for reducing it by

 3 25 percent is that we only had one estimate; is that

 4 correct?

 5 A. Right. I reduced it by 25 percent because we

 6 would have preferred to have seen more than one estimate

 7 or contract or bid. If we had seen several of these

 8 things, it might have been that that was the more

 9 reasonable, but we didn't see any more to compare it to,

 10 so we didn't have a basis to say that was the most

 11 reasonable contract that we had, or bid or estimate.

 12 Q. But having that estimate did give us an idea

 13 of the costs that are associated with these inspections,

 14 did it not?

 15 A. It gave you one option for the cost.

 16 Q. Do you know how many -- do you have any idea

 17 how many vendors there are that could provide this

 18 inspection?

 19 A. No, I don't know how many there are. I was

 20 trying to look to see if the company had answered that

 21 in discovery, but I can't find that right now.

 22 Q. Is there any accounting principle that would

 23 require bids or proposals, multiple bids or proposals

 24 for establishing a budget estimate?

 25 A. I don't think that there's any accounting

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 1 principles, but I think it makes good business sense to

 2 be able to figure out whether or not the estimate that

 3 somebody is giving you is in the reasonable range.

 4 Q. Let's turn to the distribution inspections.

 5 And again, there's a bid for the inspection of the

 6 distribution poles, is there not?

 7 A. Yes, there was one.

 8 Q. Is that the one attached to your testimony?

 9 A. Yes. It was from Osmose. That's Exhibit

 10 PWM-3.

 11 Q. Okay. We're going to come back to that in a

 12 second. Again, do you know how many potential bidders

 13 there are?

 14 A. No, I don't. I was just relying on the

 15 company's support for this adjustment that we asked for.

 16 Q. Okay. You've got that exhibit in front you?

 17 A. Yes, I do.

 18 Q. Okay. If I understand correctly, you would

 19 agree that the external -- well, tell me what on that

 20 schedule you would recognize for the cost.

 21 A. Well, according to what the company told us in

 22 the deposition, Mr. Cutshaw, these stars -- I've added

 23 these stars to this exhibit, but this is what he told us

 24 in the deposition. The 29.88 for the external treat was

 25 one component he used. The sound and bore of $7.75 he

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 1 used. The FastGate delivery of 60 cents he used,

 2 LoadCalc for $7.26, CATV attachments, which is cable TV,

 3 60 cents, telephone attachments of 60 cents, and GPS

 4 reading, 98 cents. And that totaled $47.67 per pole.

 5 Q. I'm sorry, Ms. Merchant. I thought I asked

 6 what components did you use?

 7 A. I used all but -- of the list I just read, I

 8 took out the LoadCalc of $7.26, the CATV attachments of

 9 60 cents, and the telephone attachments of 60 cents.

 10 Q. So you included the external treat, sound and

 11 bore, FastGate?

 12 A. Yes, and GPS reading.

 13 Q. And GPS reading.

 14 A. I believe that's --

 15 Q. Why did you eliminate LoadCalc? Isn't that

 16 something that's going to have to be done with or

 17 without an attacher?

 18 A. It's my understanding that the LoadCalc was

 19 necessitated because the company, when they put the pole

 20 up, they know what the pole's capability is, and when

 21 they go through -- and they know that it's capable of

 22 holding their equipment, or it should be when they put

 23 it up, should meet the design criteria. And when they

 24 go along subsequently and inspect it, they're going see

 25 the full load on that pole, and the LoadCalc is

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 1 calculating the amount of the load of all the

 2 attachments on the pole. And so that's why we removed

 3 it as something that was directly caused by other

 4 attachers, because the company has already spent the

 5 money when they put the pole up to figure out what their

 6 load is for their own equipment.

 7 Q. Do you know if the revenues from the

 8 third-party attachers -- we do receive revenues from the

 9 third-party attachers, do we not?

 10 A. Yes, you do. And the company did not project

 11 an increase for the revenues from the third-party

 12 attachers in this rate case. And essentially what we've

 13 done is said, while we recognize that this type of cost

 14 would be incurred for an inspection, it's just that the

 15 cost is driven more by the third-party attachers, and

 16 the ratepayers shouldn't have to pay an incremental cost

 17 for an inspection that is going to recovered or should

 18 be recovered from other attachers. And that's

 19 essentially why we removed it, because there's not a

 20 revenue to go along with that. It's not that we're

 21 saying you shouldn't spend the money. It's just that

 22 the ratepayers shouldn't have to pay for that, because

 23 subsequently it should be recovered in other means.

 24 Q. Do the revenues the company receives from

 25 these third-party attachers exceed the costs associated

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 1 with the inspections?

 2 A. I don't know. I don't believe that the

 3 agreements have been changed in a while, so I don't

 4 think that they -- if they haven't been increased for

 5 this rate case, then these costs are not in there for

 6 the contracts to be changed. Any of the storm

 7 hardening, any of the new storm hardening costs are not

 8 in there. I would assume that.

 9 Q. I'm not sure I follow you, Ms. Merchant. I'm

 10 not sure -- the question was whether or not the revenues

 11 from the third-party attachers -- under the current

 12 arrangements, do the revenues from the third-party

 13 attachers exceed the costs associated with the

 14 inspections, the pole inspections?

 15 A. This pole inspection, the one that you're

 16 asking to have the increase, or the ones that were

 17 existing prior to the test year?

 18 Q. The company currently pays for pole

 19 inspections, does it not?

 20 A. They do internal -- not to the degree that

 21 they do for this program. This is a much higher program

 22 of pole inspections than what they do currently.

 23 Q. All right. Currently, then, do revenues

 24 received from third-party attachers exceed the expenses

 25 associated with the pole inspections?

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 1 A. I don't know exactly whether or not they cover

 2 the costs, cover a portion of the costs, but I could

 3 assume that -- and I know it's a very complicated

 4 formula, but I would assume that they would recover a

 5 portion of the costs associated with maintenance of

 6 transmission systems. And since this cost is not in the

 7 historical cost and the contracts have not been revised

 8 as of late, then I would assume that these new

 9 incremental costs would not be in the current contracts.

 10 And that's an assumption that I'm making, but the

 11 company has never incurred this detail of pole

 12 inspection costs.

 13 Q. All right. But if the revenues are exceeding

 14 the expenses associated with the inspections, are not

 15 the customers receiving a benefit from those

 16 arrangements?

 17 A. If the revenues from the pole -- can you say

 18 that one more time?

 19 Q. If the revenues from the third-party attachers

 20 are exceeding the expenses associated with the

 21 inspections of the poles, are the customers not

 22 receiving a benefit from that?

 23 MS. CHRISTENSEN: Objection. Assumes facts

 24 not in evidence. I think he can ask it as a

 25 hypothetical, but I'm not sure that there's record

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 1 evidence to support whether or not the current revenues

 2 from pole inspections actually exceed the cost of pole

 3 inspections.

 4 MR. HORTON: I think I prefaced the question

 5 with an "if."

 6 CHAIRMAN CARTER: Let's try it again.

 7 BY MR. HORTON:

 8 Q. If the revenues from the third-party attachers

 9 exceeded the expenses associated with the inspections,

 10 would not that benefit the customers?

 11 A. Only if that was the only basis that was used

 12 to derive the cost charged to the third-party attachers,

 13 because if there's any rate of return component or any

 14 other expense other than pole inspections -- and my

 15 understanding is that there would be more costs included

 16 that would be shifted up to the third-party attachers.

 17 You can't just look at this expense and say if the

 18 revenues exceed this expense, then the customers receive

 19 a benefit. It's what is all in the formula that's used

 20 to calculate the rates that the third-party attachers

 21 collect -- or pay, excuse me.

 22 Q. Let me ask you just a couple of questions

 23 about the new positions. The compliance accountant, I

 24 believe you agreed that that position is needed and

 25 should be approved?

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 1 A. I don't know which compliance accountant

 2 you're talking about, because the words were all shifted

 3 around.

 4 Q. That would be in the corporate accounting

 5 department, the compliance accountant, and that would

 6 be --

 7 A. Right. I was calling that the corporate

 8 accountant for special audits, inventory, cash, and

 9 other procedures. Compliance was another position, but,

 10 yes, I recommended that 50 percent of that position be

 11 allowed.

 12 Q. Right. I think that's Issue 77. And your

 13 basis for the recommendation on the 50 percent was that

 14 it wasn't going to be filled until later in the year;

 15 isn't that correct?

 16 A. That's correct.

 17 Q. All right. Going forward, though, isn't the

 18 effect of that recommendation that the salary is cut in

 19 half for that position?

 20 A. Well, we're looking at a test year. We're

 21 allowing 50 percent of the salary for this year, for

 22 2008, which is what they would incur in 2008. And

 23 that's the test year concept, is that you look at what

 24 is likely to be incurred in 2008. You look at the

 25 things that go up in 2008. You're not going to give the

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 1 pay raises that occur at the end of 2008 for the full

 2 year of 2008 because they weren't in effect until the

 3 end of 2008. It's the same type of thing. It's the

 4 same concept that you would use for using a 13-month

 5 average for plant in rate base. You want to match the

 6 rate base with the expenses with the revenues that are

 7 expected to be in place during the test year.

 8 Q. The test year is supposed to be representative

 9 of going-forward periods; correct?

 10 A. That's correct. But also, when you go outside

 11 the test year, you have a lot of other changes that can

 12 occur. Things can go down outside the test year, and

 13 you're not looking at those things that might go down.

 14 Accumulated depreciation increases. All kinds of things

 15 change. When you go outside the test year, you start

 16 skewing the result. And that's essentially what my

 17 testimony is, is that you should just recognize exactly

 18 what's in the test year.

 19 Q. I understand, Ms. Merchant. Let's stick to

 20 this position, though. If the person is hired in --

 21 pick a month, I don't care -- June at $50,000, but you

 22 have only recommended recovery or inclusion of $25,000

 23 of that expense this year, then how much of the person's

 24 $50,000 salary would the company recover in 2009?

 25 A. Well, in 2009, they would have the full

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 1 salary. But they could also have a person that retires

 2 in 2008 that had a higher salary and they replace that

 3 person at a substantially less salary, so you would have

 4 the full salary in the test year projected because they

 5 were in 2007 and 2006. So you have all kinds of things

 6 change. But once you step outside the test year, the

 7 whole picture changes. Anything can change.

 8 Q. Ms. Merchant, I think this is a real simple

 9 question and a real simple issue. If you only allow

 10 recovery of a half year's expense in 2008, that's all

 11 the company is going to recover in 2009. Forget

 12 retirements or anything else. If you're trying to

 13 project the expenses, isn't that what you do when you

 14 annualize, you normalize to make the test year look like

 15 future periods?

 16 A. I agree that sometimes you do annualize and

 17 normalize to make the test year look more normal. But

 18 the flip side of that is that the company could have

 19 increased revenues. It could be a very warm season that

 20 they might not anticipate that the revenues are going to

 21 go up as much. They could have some more growth than

 22 what they projected. There's all kinds of things that

 23 can change once you get beyond the test year.

 24 Q. All right. You win, Ms. Merchant.

 25 Training, let's switch to training. You

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 1 wouldn't deny and you wouldn't disagree that training of

 2 the linemen and the personnel that work on the lines is

 3 an important function of the company?

 4 A. No. I think it's important.

 5 Q. Okay. And you understand that FPUC is having

 6 to make different arrangements to have their linemen

 7 trained than they've had in the past? Do you agree with

 8 that?

 9 A. Based on the information that we received from

 10 them, they are attempting to change their training

 11 method, yes. I agree with that. They tried the Tampa

 12 Electric program, and that didn't work out, and they

 13 revised their plan after that.

 14 Q. All right. So they're going to be training

 15 themselves; correct?

 16 A. I'm not exactly sure what they're going to do,

 17 but I can tell you that they gave me information saying

 18 they would.

 19 Q. You said they gave you information. You're

 20 referring to the exhibit, the PowerPoint exhibit that

 21 compares the various options to the company?

 22 A. Right. I looked at that. I looked at their

 23 response to Interrogatory 45, and I looked at the

 24 PowerPoint, the portion that was provided with 45, and

 25 then I got the subsequent one that was the complete

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 1 version of it.

 2 Q. But that reflects that the company has

 3 considered various options for presenting this training;

 4 correct?

 5 A. That PowerPoint presentation presented all

 6 those options, but it didn't come up with a conclusion

 7 that I recall. And --

 8 Q. Go ahead.

 9 A. I was just going mention, the requested

 10 increases in expenses that the company had in the

 11 response to Interrogatory 45 were just lot of numbers

 12 that they gave and just said, "Here's the new cost."

 13 You know, I've got that on page 25 of my testimony.

 14 They just said, "We're going to have a new person, we're

 15 going to have some travel expenses, we're going to have

 16 some supplies," and all these other numbers they just

 17 gave us.

 18 And we asked for more support behind all these

 19 numbers. We just never got any more support behind all

 20 these numbers. The considerations that -- the company

 21 kept saying they're already training some of these

 22 people on the state program, which is the existing type

 23 of program, but they never came back and told us how

 24 many people and how much was included in the 2006 test

 25 year so that we could compare that to any of these

 560

 1 numbers or even break down any of these numbers. And

 2 that's just where we were. We just weren't given the

 3 level of support that we felt we could use to analyze

 4 all these new numbers.

 5 Now, of course, they need training, but they

 6 just didn't give us what we asked for to support it.

 7 MR. HORTON: I don't think I have any more

 8 questions. Thank you.

 9 CHAIRMAN CARTER: Staff?

 10 MS. BROWN: No questions.

 11 CHAIRMAN CARTER: No questions from staff.

 12 Commissioners? Commissioner Argenziano, you're

 13 recognized.

 14 COMMISSIONER ARGENZIANO: I guess -- I think

 15 you've answered most of the questions I had previously

 16 about the salary issue. Well, I guess I can't go into

 17 that because it's confidential. I have the information.

 18 I had another question, and it escapes me.

 19 forgive me. If I remember, I'll ask you. I forgot what

 20 it was. I'm sorry. I should have wrote it down.

 21 CHAIRMAN CARTER: That's all right. We have

 22 those moments.

 23 Staff, no questions?

 24 COMMISSIONER EDGAR: I'm sorry.

 25 CHAIRMAN CARTER: Oh, Commissioner Edgar,

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 1 you're recognized.

 2 COMMISSIONER EDGAR: Thank you. I do have a

 3 question about the exhibit, the confidential exhibit,

 4 and I think I can ask it in a way that does not

 5 compromise the confidentiality. Is it appropriate to

 6 pose -- let me pose it to Ms. Merchant, and if you can

 7 answer it, do, and if not, I'll try it again with

 8 somebody else.

 9 THE WITNESS: Okay.

 10 COMMISSIONER EDGAR: If would you pull out the

 11 exhibit. And let's see. The third page of the stapled

 12 items that we have, which is the first page of the

 13 chart, chart 2, right towards bottom of the columns

 14 where it says "FPUC 2007 compensation." I'm going to

 15 state no numbers. But my question is, is that all the

 16 electric portion, or is some of it electric and gas

 17 allotted?

 18 THE WITNESS: Are you looking at a page -- I

 19 don't have numbers on my exhibit, but it's a page that

 20 has different companies on the left and Florida Public

 21 on the right and a little box down at the bottom.

 22 COMMISSIONER EDGAR: Correct. And then just

 23 above the box --

 24 THE WITNESS: Right, where it's bold, where

 25 the letters are A, B, C, D?

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 1 COMMISSIONER EDGAR: Correct. And it says

 2 FPUC 2007 compensation.

 3 THE WITNESS: Yes, ma'am.

 4 COMMISSIONER EDGAR: Those numbers right below

 5 there, CEO, COO, CFO.

 6 THE WITNESS: That's correct.

 7 COMMISSIONER EDGAR: Okay. And my question

 8 is, are those numbers just the electric portion, or does

 9 that include electric and gas?

 10 THE WITNESS: That is the total company,

 11 electric, gas, LP gas, the whole company.

 12 COMMISSIONER EDGAR: Okay. That's what I

 13 wanted to know. Thank you.

 14 CHAIRMAN CARTER: Commissioners? Nothing

 15 further. Ms. Christensen, you're recognized.

 16 REDIRECT EXAMINATION

 17 BY MS. CHRISTENSEN:

 18 Q. Just a few brief questions on redirect. Again

 19 looking at that confidential document, those bottom

 20 numbers, you have -- looking at those bottom numbers,

 21 you have recommended a salary increase that would be

 22 over and above what those bottom numbers reflect in your

 23 testimony?

 24 A. I'll have to check that. I'm not sure if this

 25 is projected 2007 or actual 2007, but I can pull out a

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 1 document real quick.

 2 That must have been the actual 2007. It does

 3 say 2007 compensation, because the numbers don't match

 4 the 2006 actual numbers that I have. They're higher

 5 than that.

 6 Q. What did you recommend for the increases for

 7 the executive salaries?

 8 A. I recommended above the 2006 actual numbers,

 9 5-1/2 percent for 2007 and 5-1/2 percent for 2008, which

 10 is consistent with what they asked for for their other

 11 employees.

 12 Q. Okay. And that would be -- so you would

 13 assume that the number at the bottom of the page would

 14 at least go up 5-1/2 percent?

 15 A. Above that, yes. Now, the shaded box over

 16 here that's directly under the words "Florida Public

 17 Utilities" up at the top of the column does say -- the

 18 little fine print right under Florida Public Utilities

 19 does say that the 2007 numbers have been adjusted by

 20 inflation.

 21 Q. Okay. And that would also be recommended in

 22 the --

 23 A. And as with the 2008 numbers down there, just

 24 -- so I would assume the 2007 is adjusted to 2008.

 25 Q. Okay. Thank you for that clarification. I

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 1 had, I think, just one more question. To your

 2 knowledge, what level of training did FPUC do in 2006

 3 and before 2006?

 4 A. They did the state lineman program, which is a

 5 home study program, which is part of what they want to

 6 continue doing.

 7 There was confusion in our deposition. We

 8 couldn't ever tell how many people they were actually

 9 training in 2006 between the two different divisions. I

 10 think we got several different numbers, and even in the

 11 rebuttal testimony, that number is different. So I

 12 wasn't really sure exactly how many people were already

 13 trained under the state lineman program and projected

 14 already in the base year by inflation and customer

 15 growth to get to the 2008 before they made the over and

 16 above adjustment. So I'm not sure. There might be some

 17 double counting of some portion of that state lineman

 18 program and training materials in that number, but I

 19 don't know, because I didn't get the information.

 20 Q. But you did allow for some level of training

 21 to continue and to be escalated for 2007 and 2008?

 22 A. Correct. What was in 2006 was escalated up to

 23 2007 and escalated forward to 2008.

 24 MS. CHRISTENSEN: I have no further questions.

 25 CHAIRMAN CARTER: Okay. Let's deal with our

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 1 -- well, before we -- nobody leaves the room. Why don't

 2 we collect these up first before we deal with the

 3 exhibits. I'll feel better, and I'm sure that my fellow

 4 Commissioners will feel better too that we just collect

 5 these documents in their red folders.

 6 Okay. So we're no longer on the Hunt for Red

 7 October; right? Good.

 8 Now let's deal with our exhibits.

 9 Ms. Christensen, you're recognized.

 10 MS. CHRISTENSEN: I would ask that we move

 11 Exhibits 47, 48, and 49 into the record.

 12 CHAIRMAN CARTER: Any objections? Hearing

 13 none, show it done.

 14 (Exhibit Numbers 47, 48, and 49 were admitted

 15 into the record.)

 16 CHAIRMAN CARTER: Ms. Christensen.

 17 MS. CHRISTENSEN: That concludes the Office of

 18 Public Counsel's witnesses.

 19 CHAIRMAN CARTER: Okay. Commissioners, I beg

 20 your indulgence for a moment. I want to kind of

 21 converse with staff, or maybe allow staff an opportunity

 22 to converse with the parties to see if this is a

 23 breaking point or should we go further. Staff, let's

 24 take five, and maybe you can talk with the parties and

 25 see what our next phase should be on that, because my

 566

 1 plans are for us to stop at 5:00. I omitted to ask the

 2 Commissioners this morning about time constraints and

 3 all like that, so my plans are to stop at 5:00 today.

 4 So staff, why don't we take 10 minutes and converse with

 5 the parties. We're in recess.

 6 (Short recess.)

 7 CHAIRMAN CARTER: We're back on the record. I

 8 appreciate the expediency of staff as well as the

 9 expeditious discussion with the parties, and we are sure

 10 that probably the next phase will take about an hour and

 11 a half. I mean, I'm pretty good, but I don't think I

 12 can squeeze an hour and a half into 24 minutes. So with

 13 that, we'll recess for the day and reconvene tomorrow at

 14 9:30 a.m. We are in recess.

 15 (Proceedings recessed at 4:35 p.m.)

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 1 CERTIFICATE OF REPORTER

 2

 3 STATE OF FLORIDA:

 4 COUNTY OF LEON:

 5 I, MARY ALLEN NEEL, Registered Professional

 6 Reporter, do hereby certify that the foregoing

 7 proceedings were taken before me at the time and place

 8 therein designated; that my shorthand notes were

 9 thereafter translated under my supervision; and the

 10 foregoing pages numbered 352 through 566 are a true and

 11 correct record of the aforesaid proceedings.

 12 I FURTHER CERTIFY that I am not a relative,

 13 employee, attorney or counsel of any of the parties, nor

 14 relative or employee of such attorney or counsel, or

 15 financially interested in the foregoing action.

 16 DATED THIS 28th day of February, 2008.

 17

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