

**Dorothy Menasco**

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**From:** ROBERTS.BRENDA [ROBERTS.BRENDA@leg.state.fl.us]  
**Sent:** Friday, March 13, 2009 9:20 AM  
**To:** Filings@psc.state.fl.us  
**Cc:** Dianne Triplett; James M. Walls; John Burnett; John McWhirter; Keino Young; Lisa Bennett; Paul Lewis; R. Alexander Glenn  
**Subject:** E-filing (Dkt. No. 070703-EI)  
**Attachments:** 070703.prehearing statement.sversion.doc

Electronic Filing

a. Person responsible for this electronic filing:

Joseph A. McGlothlin, Associate Public Counsel  
Office of Public Counsel  
c/o The Florida Legislature  
111 West Madison Street, Room 812  
Tallahassee, FL 32399-1400  
(850) 488-9330  
mcglothlin.joseph@leg.state.fl.us

b. Docket No. 070703-EI

In re: Review of coal costs for Progress Energy Florida's Crystal River Unites 4 and 5 for 2006 ad 2007

c. Document being filed on behalf of Office of Public Counsel

d. There are a total of 9 pages.

e. The document attached for electronic filing is the Prehearing Statement of the Office of Public Counsel.

(See attached file: 070703.prehearing statement.sversion.doc)

Thank you for your attention and cooperation to this request.

Brenda S. Roberts  
Office of Public Counsel  
Telephone: (850) 488-9330  
Fax: (850) 488-4491

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FPSC-COMMISSION CLERK

**BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

Review of coal costs for Progress Energy  
Florida's Crystal River Units 4 and 5  
for 2006 and 2007

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Docket No. 070703-EI

Filed: March 13, 2009

**PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL**

The Citizens of the State of Florida, through the Office of Public Counsel, pursuant to the Order Establishing Procedure, Order No. PSC-08-0710-PCO-EI, issued October 29, 2008, hereby submit this Prehearing Statement.

**APPEARANCES:**

JOSEPH A. MCGLOTHLIN, Associate Public Counsel  
Office of Public Counsel  
c/o The Florida Legislature  
111 West Madison Street, Room 812  
Tallahassee, Florida 32399-1400  
On behalf of the Citizens of the State of Florida.

1. **WITNESSES:**

Citizens will sponsor the testimony of David J. Putman.

2. **EXHIBITS:**

DJP-1	RESUME
DJP-2	FERC 423 DATA SHEETS
DJP-3	TONS RECEIVED BY WATER 2006 AND 2007
DJP-4	2004 RFP DOCUMENT
DJP-5	PEF REPORT TO MANAGEMENT: 2005-2006 PURCHASE ACTIVITY

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DJP-6	2004 RFP EVALUATION SHEET
Revised DJP-7	CALCULATION OF EXCESS FUEL COSTS
DJP-8	2006 RFP EVALUATION SHEET
DJP-9	EXCERPT OF WEINTRAUB TESTIMONY IN DOCKET NO. 060658-EI
DJP-10	INDONESIAN SUB-BITUMINOUS MINE DATA
DJP-11	EXCESS COSTS OF EMISSION ALLOWANCES 2006-2007
DJP-12	ALLOWANCE PRICE FORECAST
DJP-13	CALCULATION OF TOTAL OVERCHARGES 2006-2007
DJP-14	EXCERPT, PEF APPLICATION FOR TEST BURN
DJP-15	EXCERPT, PEF APPLICATION TO FDEP RE: 50% SUB-BITUMINOUS BLEND
DJP-16	EXCERPT, FDEP TECHNICAL EVALUATION

### 3. STATEMENT OF BASIC POSITION

In Order No. PSC-07-0816-FOF-EI, the Commission determined that Progress Energy Florida (PEF) was imprudent when it failed to obtain a permit authorizing it to burn the sub-bituminous coal that Crystal River Units 4 and 5 were designed to burn prior to 2003. It found that PEF can burn a blend containing at least 20% sub-bituminous coal without reducing the units' output. Based on a comparison of the cost of more economical sub-bituminous coal that producers offered during PEF's procurements (as those bids were evaluated by PEF) with the highest costing 20% of coal that was actually delivered to Crystal River Units 4 and 5 during 2003, 2004, and 2005, the Commission ordered PEF to refund \$13.8 million to its customers.

2005 was the most recent year for which data was available when the Commission reviewed this matter in Docket No. 060658-EI. PEF did not obtain a permit authorizing it to burn sub-bituminous coal at Crystal River 4 and 5 until May of 2007, well after it had entered contractual arrangements for coal to be delivered to the units in 2006 and 2007. The Commission should therefore apply to actual costs of 2006 and 2007 the same test it applied to the years 2003, 2004, and 2005 to determine whether the imprudences identified in Order No.

PSC-07-0816-FOF-EI continued to cause coal costs to be unreasonably high at Crystal River 4 and 5 in those years.

In his testimony, OPC witness David J. Putman demonstrates that, as a result of the same imprudences identified in Order No. PSC-07-0816-FOF-EI, when arranging for deliveries in 2006 and 2007 PEF again was not positioned to take advantage of the opportunity to purchase more economical sub-bituminous coal. In his analysis, Mr. Putman adheres strictly to the methodology of Order No. PSC-07-0816-FOF-EI. He bases his comparison on bids that PEF received and evaluated at the time PEF made the relevant procurement decisions. Applying the parameters of Order No. PSC-07-0816-FOF-EI, he shows that PEF had the opportunity to purchase more than 1 million tons of coal costing over \$40 per ton less than PEF paid for deliveries in 2006 and 2007. Further, this alternative coal contained far less sulfur than the coal that was actually delivered, meaning that the impact of PEF's imprudence on customers was compounded by the inability to take advantage of an opportunity to lower the costs of environmental compliance that are passed on to customers. Altogether, PEF's CR4 and CR5 coal costs and related costs of emissions allowances were unreasonably high in 2006 and 2007 by a total of \$61 million, excluding interest.

As the Commission prepares to conduct an evidentiary hearing in April 2009, PEF still has not performed all that prudence requires with respect to utilizing fully the flexibility of Crystal River Units 4 and 5 for which customers have been paying. In 2006 PEF applied for a permit authorizing it to burn a 50/50 mixture of sub-bituminous and bituminous coals. When it issued a permit in 2007, the Florida Department of Environmental Protection limited PEF to 20% sub-bituminous coal. The FDEP imposed this limitation because PEF performed the test burn on which it relied to support its application with only an 18% blend. At the time it issued the permit, the FDEP invited PEF to support a permit amendment by performing additional tests with blends containing higher percentages of sub-bituminous coal. Even though PEF applied for a permit authorizing 50% sub-bituminous coal, and even though a higher limit in the permit could potentially lower customers' fuel cost in the future, to this date PEF has made no effort to pursue the opportunity that the FDEP extended. The Commission should order PEF to test blends containing higher percentages of sub-bituminous coal in Crystal River 4 and 5. The tests should be overseen by an independent engineering firm, and the test results should be reported to the Commission. If the results warrant, PEF should seek an amendment to its permit.

#### 4. STATEMENT OF FACTUAL ISSUES AND POSITIONS

ISSUE 1: Did the imprudences in PEF's fuel procurement activities determined in Order PSC-07-0816-FOF-EI result in the costs of coal actually delivered to Crystal River Units 4 and 5 during 2006 and 2007 being unreasonably high?

OPC: Yes. The application of the findings and cost comparison methodology contained in Order No. PSC-07-0816-FOF-EI to the facts bearing on 2006 and

2007 establishes that the costs borne by customers were unreasonably high in the amount of \$61,279,193.

- a. How should the reasonableness of the costs of coal delivered to Crystal River Units 4 and 5 during 2006 and 2007 be measured?

OPC:

The reasonableness should be measured by the “yardstick” of Order No. PSC-07-0816-FOF-EI. The Commission issued this order in Docket No. 060658-EI, which encompassed years through 2005. In the order, the Commission determined that PEF was imprudent when it failed to have a permit to burn sub-bituminous coal in CR4 and CR5 prior to 2003. It concluded that the costs of fueling CR4 and CR5 were made unreasonably high in 2003, 2004, and 2005 as a consequence of PEF’s inability to legally burn the more economical sub-bituminous coal that was offered to PEF. PEF did not obtain such a permit until May 2007, well after it procured coal for delivery in 2006 and 2007; those years therefore are part of a continuum with the time frame of Docket No. 060658. Accordingly, the Commission should apply to 2006 and 2007 the same metrics that it used in Order No. PSC-07-0816-FOF-EI.

In that regard, the Commission determined that CR4 and CR5 can burn a blend containing 20% sub-bituminous coal without a reduction in output. It concluded that the coals should be blended off-site. As a practical matter, this means the blending would occur at a transloading facility for waterborne coal. The Commission compared the costs of the 20% highest costing tons actually delivered by water in 2003, 2004, and 2005 with the evaluated costs of alternatives offered during relevant RFPs. In calculating a refund, the Commission recognized that, had PEF been able to purchase the alternative (low sulfur) sub-bituminous coal, PEF would have spent less for SO2 emissions allowances. The Commission did not reduce the amount of overcharges to be refunded by the cost of coal handling upgrades that the plant would have required, for the reason that such costs would have been considered in base rate proceedings. PEF’s contention that results for 2006-2007 should be adjusted for capital costs is misplaced. Those same handling upgrades would have been in place in 2006-2007. PEF would continue to recover the capital costs through base rates. Savings from additional purchases of sub-bituminous coal would simply serve to increase the benefit-to-cost ratio beyond what was already more than sufficient to justify the capital additions in Docket No. 060658-EI.

- b. What candidates for alternative coal purchases should the Commission consider in evaluating whether more economical coal was available for delivery to Crystal River Units 4 and 5 during 2006?

OPC:

The alternative coal that should be compared with the costs of coal actually delivered in 2006 is the lowest cost coal that was available at the time of

related procurement decisions. The lowest bids were for sub-bituminous coal from the Powder River Basin offered by Kennecott during the Request For Proposals that PEF conducted in April, 2004. The fact that the RFP was conducted in a year prior to the year of the deliveries that are the subject of the inquiry is no basis on which to exclude the bids from consideration. In fact, PEF did procure a portion of its 2006 requirements based on the results of the 2004 RFP. Also, in this docket PEF witness Heller uses a bid to PEF's 2006 RFP to compare with actual 2007 costs.

The alternative that PEF witness Heller used in his analysis of 2006 costs is wholly inappropriate for the purpose. It was not the most economical alternative offered and available to PEF; it was a tiny quantity (3,300 tons), purchased specifically for a test burn, and therefore a poor proxy for the alternative to the large volumes of coal actually purchased for ongoing operations; it was a spot, not a contract, purchase; and the small quantity of Peabody test burn coal was not even representative of the properties typical of PRB sub-bituminous coal.

- c. By what amount, if any, were the costs of coal actually delivered to Crystal River Units 4 and 5 unreasonably high in 2006?

OPC:

Comparing the evaluated costs of the 2004 Kennecott bids with the 20% highest costing tons actually delivered in 2006, the 2006 coal costs at CR4 and CR5 were unreasonably high by the amount of \$25,149,162, excluding interest. To this amount must be added \$2,915,308, to account for the fact that the alternative coal not purchased contained far less sulfur and would have resulted in lower costs of emissions allowances.

- d. What candidates for alternative coal purchases should the Commission consider in evaluating whether more economical coal was available for delivery to Crystal River Units 4 and 5 during 2007?

OPC:

Against the highest costing 20% of coal actually delivered in 2007, the Commission should compare the evaluated costs of the bids of two Indonesian producers of sub-bituminous coal. As evaluated by PEF, the bids from the Indonesian producers were far more economical than the cost of the coal actually delivered. Indonesia is one of the leading producers of coal for international markets. The coals had extremely low ash and extremely low sulfur content, both of which are valuable properties.

The coal offered by Indonesian producers was far more economical than the bid from Louis Dreyfus to supply PRB coal that PEF received in the same RFP and that PEF's witness chose to compare with actual costs to measure reasonableness. With respect to gauging whether PEF paid too much as a consequence of not having a permit to burn sub-bituminous coal in place, neither Order No. PSC-07-0816-FOF-EI nor anything the Commission has

said regarding the scope of Docket No. 070703-EI limits the source of alternative sub-bituminous coal to the Powder River Basin. PEF could not purchase the Indonesian sub-bituminous coal for precisely the same reasons it could not purchase the PRB coal in Docket no. 060658-EI. Those reasons formed a basis for a refund in Docket no. 060658-EI, and do so again in this proceeding.

- e. By what amount, if any, were the costs of coal actually delivered to Crystal River Units 4 and 5 unreasonably high in 2007?

OPC: Comparing the evaluated costs of the 2006 Indonesian bids with the 20% highest costing tons actually delivered in 2007, the 2007 coal costs at CR4 and CR5 were unreasonably high by the amount of \$25,866,364, excluding interest. In addition, the Indonesian coal contained far less sulfur than the coal actually delivered in 2007, and would have enabled PEF to save customers \$7,348,059 in the form of lower costs of emissions allowances.

ISSUE 2: If the Commission determines that the costs of coal delivered to Crystal River Units 4 and 5 during 2006 and 2007 were unreasonably high, should it require PEF to issue a refund to its customers? If so, in what amount?

OPC: Yes. One of the Commission's most important functions is to insulate customers from having to bear costs that have been made unreasonably high as a consequence of utility imprudence. In this instance, the Commission should order Progress Energy to refund to customers the amount of \$61,279,193 plus interest.

ISSUE 3: Based on the evidence of PEF's fuel procurement approach and activities as they relate to Crystal River 4 and 5, what additional action, if any, should the Commission take in this docket?

OPC: PEF did not "test burn" sub-bituminous coal in CR4 and CR5 until May 2006. Subsequently, when it applied to the Florida Department of Environmental Protection for the permit authorizing it to burn the coal at CR4 and CR5, it requested permission to burn as much as a 50/50 blend-which is also the design basis fuel that PEF prescribed for its units at the time they were designed and built. The FDEP permit limits PEF to 20% sub-bituminous coal because 20% approximates the only blend that PEF tested. However, the FDEP also invited PEF to perform tests of blends containing higher percentages of sub-bituminous coal to support a permit authorizing greater use of sub-bituminous coal. From the time the FDEP issued the permit in September 2007, PEF has made no effort to pursue the matter further, and it appears PEF has no intention of doing so. OPC believes PEF's failure to follow through on this matter compounds its past

imprudence. To prevent PEF from wasting a valuable asset for which its customers have been paying since the mid-1980s, the Commission should direct PEF to conduct a test burn of blends designed to ascertain the highest percentage of sub-bituminous coal that can be used in a blend while maintaining 105% overpressure and satisfying all environmental requirements. The tests should be overseen by a qualified, independent engineering firm. The report should be furnished to the Commission by a date certain. If the results of a properly conducted test support the use of a blend containing more than 20% sub-bituminous coal, PEF should apply to the FDEP to have its permit amended accordingly.

To be clear, with this recommendation OPC is not attempting to reopen or relitigate the appropriate level of refund that the Commission ordered in Order No. PSC-07-0816-FOF-EI; nor does OPC seek to advocate the use of a blend containing more than 20% sub-bituminous coal as the Commission calculates the appropriate amount of refund in this docket. Rather, OPC submits that on a forward looking basis, and in the clear absence of any PEF initiative for doing so, the Commission should require PEF to take all actions necessary to ensure that it can in the future utilize all of the flexibility for which customers are paying.

5. STIPULATED ISSUES:

None.

6. PENDING MOTIONS:

None.

7. STATEMENT OF PARTY'S PENDING REQUESTS OR CLAIMS FOR CONFIDENTIALITY:

Citizens have no pending requests for claims for confidentiality.

8. OBJECTIONS TO QUALIFICATION OF WITNESSES AS AN EXPERT:

Citizens do not expect to challenge the qualifications of any witness.

9. STATEMENT OF COMPLIANCE WITH ORDER ESTABLISHING PROCEDURE:

There are no requirements of the Order Establishing Procedure with which the Office of Public Counsel cannot comply.

Dated this 13<sup>th</sup> day of March, 2009.

Respectfully submitted,

J. R. Kelly  
Public Counsel

s/ Joseph A. McGlothlin  
Joseph A. McGlothlin  
Associate Public Counsel

Office of Public Counsel  
c/o The Florida Legislature  
111 West Madison Street  
Room 812  
Tallahassee, FL 32399-1400

Attorney for the Citizens  
of the State of Florida

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the foregoing PREHEARING

STATEMENT OF THE OFFICE OF PUBLIC COUNSEL has been furnished by

electronic mail and U.S. Mail to the following parties on this 13<sup>th</sup> day of March, 2009, to

the following:

Keino Young, Esquire  
Lisa Bennett, Esquire  
Division of Legal Services  
Florida Public Service Commission  
2540 Shumard Oak Blvd.  
Tallahassee, FL 32399-0850

Paul Lewis, Jr.  
Director, Regulatory  
Progress Energy Florida  
106 E. College Ave., Suite 800  
Tallahassee, FL 32301

R. Alexander Glenn, Esquire  
John T. Burnett, Esquire  
Progress Energy Service Co., LLC  
Post Office Box 14042  
St. Petersburg, Florida 33733-4042

James Michael Walls, Esq.  
Dianne M. Triplett, Esq.  
Carlton Fields, P.A.  
Post Office Box 3239  
Tampa, FL 33601-3239

John McWhirter  
McWhirter, Reeves Law Firm  
P.O. Box 3350  
Tampa, FL 33601-3350

s/ Joseph A. McGlothlin  
Joseph A. McGlothlin