BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for increase in rates by Florida Power & Light Company. DOCKET NO. 120015-EI

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TELEPHONIC DEPOSITION OF: WILLIAM E. AVERA

TAKEN AT THE INSTANCE OF: Florida Public Service Commission

DATE: Wednesday, August 8, 2012

TIME: Commencing at 10:00 a.m.
Concluding at 4:25 p.m.

PLACE: Room 382D, Gunter Building
2540 Shumard Oak Boulevard
Tallahassee, Florida

REPORTED BY: LAURA MOUNTAIN, RPR
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Clarence Prestwood
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ALSO PRESENT TELEPHONICALLY:
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I N D E X

The telephonic deposition of WILLIAM E. AVERA was taken on oral examination, pursuant to notice, for purposes of discovery, for use in evidence, and for such other uses and purposes as may be permitted by the Florida Rules of Civil Procedure and other applicable law. The reading and signing of the deposition by the witness is not waived.

* * *

MR. YOUNG: Let's get started. Let's take attendance, starting with the folks in the room, then we'll move to the folks on the phone, starting with the deponent, FPL, FPL's witness. Keino Young, Commission Staff. To my right I have --

MR. SPRINGER: Michael Springer, Commission Staff.

MR. CICCHETTI: Mark Cicchetti, Commission Staff.

MR. PRESTWOOD: Clarence Prestwood, Commission Staff.

MR. GUYTON: In Juno Beach we have Charlie Guyton, appearing on behalf of Florida Power and Light Company, and the deponent, William Avera.

MR. YOUNG: OPC?

MR. McGLOTHLIN: My name is Joe McGlothlin. I'm here for the Office of Public Counsel.

MR. REHWINKEL: This is Charles Rehwinkel listening in with the Office of Public Counsel.

MS. CHRISTENSEN: Patty Christensen, also listening in with the Office of Public Counsel. Can I ask one quick question?

MR. YOUNG: Yes, ma'am.

MS. CHRISTENSEN: For the next deposition, which is scheduled at 11:00, are you going to -- is that going forward at 11:00, or is that going to go forward after this one ends? I just want to make sure I'm clear.

MR. YOUNG: I think that's going forward at 11:00. I think we have multiple court reporters, and we're going to use a different room.

MS. CHRISTENSEN: All right, that's fine, I just need to make sure that I'm off by 11:00. Thank you.

MR. GUYTON: Now that I'm off to an auspicious start, I may even venture to pronounce my witness's name correctly this time. Bill Avera.

MR. YOUNG: Avera, yeah. Let's go with the South Florida Hospital.

MR. SUNDBACK: Good morning, Mark Sundback.

MR. RAPPOLT: This is William Rappolt.

MR. YOUNG: Village of Pinecrest?

MR. ARMSTRONG: Brian Armstrong for the Village of Pinecrest.

MR. YOUNG: Mr. Hendricks?

MR. HENDRICKS: Yes, I'm here, Keino.

MR. YOUNG: Okay. Is there anyone else on the line who did not introduce themselves?

MR. SMITH: Bob Smith.

MR. YOUNG: Okay. All right, one second, please. All right, with that, Mr. Guyton, can you swear Mr. Avera in? Avera, excuse me.

MR. GUYTON: We have a notary here.

MS. BUSSEY: Good morning, my name is Jackie Bussey and I'm a notary duly appointed and commissioned here in the state of Florida.

Thereupon,

WILLIAM E. AVERA

was called as a witness, having been first duly sworn by Jacqueline Bussey, was examined and testified as follows:

MR. GUYTON: We will have Ms. Bussey execute that and we'll FAX that to you in short order.

MR. YOUNG: Can we get the notary's name?

MS. BUSSEY: Jacqueline Bussey, B-u-s-s-e-y.

MR. YOUNG: And my FAX number is 850-413-6227.

MR. GUYTON: 6227?

MR. YOUNG: Yes. For the purposes of the deposition I would ask that to the extent that your telecommunication devices can be placed on silent or vibrate so we won't get feedback on this end.

MR. MOYLE: Keino, just for the record, Jon Moyle on behalf of FIPUG has joined. Sorry I'm a couple minutes late.

MR. YOUNG: My Moyle, do you have questions for -- I'm just trying to go around and ask everyone on the phone did they have questions, just to see, in terms of time frames, what we're looking at.

MR. MOYLE: I do have questions.

MR. YOUNG: Do you know approximately how long do you anticipate?

MR. MOYLE: It may depend somewhat on the brevity of the witness' answers. If he gives me yes or no, it should be short. If not, it will take a little longer. Maybe 30 minutes to an hour.

MR. YOUNG: Okay. And I didn't hear from Mr. Hendricks, I'm sorry. Mr. Hendricks, do you have questions for the witness?

MR. HENDRICKS: I may have, depending on what transpires before my turn comes.

MR. YOUNG: Okay, not a problem.

DIRECT EXAMINATION

BY MR. YOUNG:

Q With that, Mr. Avera -- Dr. Avera, good morning.

A Good morning.

Q Am I pronouncing your name correctly, sir?

A Yes, you are. Thank you.

Q Dr. Avera, I would like to just put some things on the record. During the course of this deposition I will be asking you a series of questions based on your testimony and your exhibits. During the course of this deposition what I'd like to do is see if I can go for an hour, hour and ten minutes, take a break, okay, take a five, ten minutes break, and then continue.

A Yes.

Q However, during the course of the deposition if you feel like you need a break, please, do not hesitate to do so.

A I will do so.

Q I'd like to note that all objections except as to form are reserved. I think, Mr. Guyton, you might want to -- if you want to jump in.

MR. GUYTON: No, that's fine.

BY MR. YOUNG:

Q And with that, Dr. Avera, can you please state your full name for the record.

A William E. Avera, A-v-e-r-a.

Q What is your occupation and business address, sir?

A I am the President of FINCAP, F-I-N-C-A-P, Incorporated at 3907 Red River, Austin, Texas, 78751 .

Q And when you say you're the President of FINCAP, you mean Financial Concepts and Applications, Incorporated, correct?

A That is correct. We are an economic financial and policy consulting firm to government agencies, utilities, businesses and law firms.

Q Okay. And what is your current responsibility in this position? And I think you said President?

A Yes.

Q What's your current responsibilities as President of FINCAP?

A To oversee the activities of the firm, to assure quality control, and I also take individual assignments to provide testimony and consultation.

Q On whose behalf are you appearing in this proceeding, sir?

A Florida Power and Light.

Q And what's the purpose of your testimony in this proceeding?

A My testimony is to address the issues of return on equity as well as the reasonableness of FPL's requested capital structure. And, of course, with the ROE, that's both the market analysis of the reasonable range plus that the ROE adder is appropriate regulatory policy and should be considered by the Commission.

Q All right. And you filed prefiled direct and rebuttal testimony in this case, in this proceeding, correct?

A Yes, sir.

Q At this time do you have any additions, deletions or corrections to your prefiled direct or rebuttal testimony and exhibits?

A No, I do not know of any.

Q When you say you do not know of any, that means at this point in time you do not have any corrections, correct?

A Correct. Sometimes I am unpleasantly surprised when people find things that I missed but I've read both testimonies carefully and didn't find anything that I thought was out of sorts.

Q All right, Dr. Avera, if we can focus on your direct testimony for a second, focusing on the return on equity.

A Yes, sir.

Q Dr. Avera, would you agree that the required return on equity is the minimum return required to attract capital to an investment?

A Yes. In regulatory terms it's got to meet other requirements, as well.

Q Would you also agree that the cost of capital as determined by the Commission in this proceeding should only reflect the costs of providing regulated electric service in Florida?

A Yes, but I think that includes adjustments to the ROE to reflect the superior management and low rates of FPL.

Q Would you agree that capital markets are generally efficient?

A Yes.

Q And would you agree that in general investors' perception of investment risk are reflected in market prices for investments?

A Yes, based on publicly available information.

Q And, sir, would you agree that, in general, investors' perception of risk, of investment risk, are reflected in analysts' growth rate projections?

A No.

MR. MOYLE: Object to the form.

THE WITNESS: Analysts' growth rate projections --

MR. YOUNG: Hold on, hold on, Dr. Avera, we have an objection. I think Mr. Moyle placed an objection to the form?

MR. MOYLE: That's correct.

BY MR. YOUNG:

Q Okay, go ahead, Dr. Avera.

A Analysts' growth expectations are based on what analysts think earnings and usually with them price growth will be. That does not reflect analysts' expectations of risk. The risk is reflected in investors' required return.

Q Okay. One second. So, Dr. Avera, to the extent that a cost of capital witness such as yourself relied on market-based costs of equity models to estimate the return, the required return on equity for FPL, would you agree, sir, that investors' perception of risk, investors' perception of investment risk will be reflected in the results of these models, of those models?

A Yes, they will. As I note in my direct, the models all are based on estimates so there are errors in observation. That's why you use a group of comparable firms to try to use sampling to reduce the effect of those errors. They're in there but we can't always extract the truth from the data.

Q One second. All right. So let me ask you to -- can you do me a favor? Let me ask you, can you please discuss your understanding of the relationship between investors' required return relative to perceived level of risk of an equity investment.

A Well, generally, investors require higher returns to compensate them for bearing higher risk. So it is accepted theory and practice that the higher the risk, the higher the required return. So if you have a very low risk security, like a bond, you would expect the required return for equity to be higher than the required return from a bond.

By the same token, a relatively low risk option like a Treasury security that's backed by full faith and credit, the ability to tax and print money, has a much lower return than an equity return which depends on economic events.

Q Okay. You are familiar with Value Line, correct?

A I am.

Q Okay. The Value Line projected returns are not specific to the expected returns for a regulated electric operation of the companies in your utility proxy group but for all operations including non-regulated operations, is that correct?

A That is correct. I believe what you're asking is do the expected returns reflect the entire holding company or just the regulated part, and the answer is they reflect the entire holding company.

Q So for the purpose of this proceeding, the Commission is not setting an ROE commensurate with the risk-slash-return requirements for a non-regulated operation of the companies in your utility proxy group, is that correct?

A That is correct. It is setting a return for the jurisdictional regulated operations of FPL.

Q So, in general, do investors consider regulated utilities to be less risky than non-regulated companies?

A In a very broad sense, they do, yes. But that doesn't mean that every unregulated business is more risky than every utility business. I believe there are significantly stable and mature non-utility businesses, such as those in my non-utility group, that actually have less risk than regulated utilities.

Q Okay. So, in general, do investors consider regulated utilities, just generally speaking, do investors consider regulated utilities to be less risky than non-regulated companies?

A Yes, as a general principle, but there are certainly material exceptions.

THE COURT REPORTER: This is the court reporter. Did I hear someone speaking an objection?

MR. MOYLE: Yes, Jon Moyle objected to the form.

BY MR. YOUNG:

Q So let me ask you this, is the variability of earnings a measure of business risk?

A It is one measure. It is not a total measure. There are many other considerations that go into business risk other than the variability. And I would also note that variability can be measured different ways: Month-to-month, year-to-year and decade-to-decade.

So in some theories, like the capital asset pricing model, variability is identified as a measure of risk, but I think in the real world risk is a more holistic measure.

Q So in general do utility earnings vary more or less than the earnings of non-regulated companies?

A In general, less. But again, as we talked about risk, there are material exceptions. There are non-regulated companies that have very stable earning streams and there are utilities that have very unstable earning streams. So in specific terms you have to look at the earning stream of the particular enterprise.

Q Okay. Have you done a study on the variability of earnings of the utility proxy group you relied upon versus the variability of earnings of a non-utility proxy group that you relied on?

A I have not done an individual study. However, one of the screening mechanisms that I used was the Value Line safety measure and an input to the safety measure is the earnings variability. So it is reflected in the criteria that I used for my group, for both groups, the utility and the non-utility group.

Q All right. Sir, can I have you turn to page 68 of your direct testimony, and specifically looking at lines 11 through 18.

A Yes, sir, I'm there.

Q Can you take a second to read that.

A Yes, sir.

Q All right, and you state there -- you state that the traditional comparable earnings tests identifies a group of companies that are believed to be comparable to the risk to the utilities. The actual earnings of those companies on the books -- on the book value of the investment are then compared to allow -- then compared to the allowed return on utilities -- of the utility. While the traditional comparable earnings test is implemented using historical data taken from accounting records, it is also common to use projections of returns on book investments such as those published by recognized investment advisory publications, e.g., Value Line. Did I read that correctly?

A Yes.

Q Sir, do you know what the average expected return on the book value equity for the period 2015 to 2017 as published by Value Line -- as published in Value Line is for your comparison groups of unregulated firms?

A It may be reflected in my BR plus SV exhibit. I can look it up.

Q All right. So subject to check, would 28.46 percent sound correct?

A Yes, that looks approximately correct. I'm looking at Exhibit WEA-8, page one of two, where it has Column C, Adjusted R. And you can see the numbers there. And looking at them, 28 percent is probably an average.

Q Do you believe, sir, that the firms that are expected -- that expect such a high return on the book value equity are comparable to Florida Power and Light?

A Yes, I believe they are in risk. The problem with the return to book value in that the accounting conventions for utilities are different than the accounting conventions for non-utilities. For non-utilities it's advantageous to write off investments as quickly as possible to achieve the tax advantages, for example, where utility generally follow the FERC accounting rules and the depreciation conventions are established by regulatory authorities.

So that's one of the reasons that the comparable earnings test kind of fell into disrepute when you were comparing utilities with non-utilities, is because of the difference in accounting conventions. And I do not apply my expected earnings method to the non-utilities. I only do the DCF to the non-utilities for that very reason.

Q So are you saying, sir, that the 28.46 percent is the result of accounting conventions?

A Largely I believe it is because, of course, that is a return on book value and to the extent that the book value is more rapidly depreciated for non-utility firms.

You could take the first one, for example, Abbott Labs. One of the biggest investments that a pharmaceutical company makes is in research to develop new drugs and devices. And that is typically expensed, when, in reality, it is the basis of their earnings. And if a utility made those kind of investments, they would be part of the rate base.

Q So, sir, just trying to bottom line it, the bottom line is that your non-regulated companies have a higher expected return than your regulated companies, correct?

A No, they have a higher earnings on book value. I think their expected returns are generally comparable. The betas are comparable, the Value Line safety measures are comparable, the bond ratings are comparable, the Value Line financial strength ratings are comparable.

So I think in terms of risk and therefore expected return to investors, they are comparable. In terms of accounting returns, they are not. That's why I didn't use the accounting returns to compare them.

Q Do the non-regulated firms have a significantly higher market-to-book ratio?

A Yes, they do, for the very reason we have been talking about. The book value is typically depreciated more rapidly so there's a greater disparity between the market value and book value than you find in the utility sector.

Q So, Dr. Avera, why didn't you do an expected earnings analysis for your non-regulated proxy group if they are comparable to FPL?

A Because the earnings are not -- the book earnings are not comparable due to the accounting differences that we've been discussing.

Q Okay. One second, please. Does a lower debt -- Dr. Avera, does a lower debt ratio or a higher common equity ratio translate into decreased financial risk for investors?

A All else being equal, it does.

Q Can you please refer to your Exhibit WEA-16, which is attached to your testimony.

A Yes, sir.

Q Can you please tell me what those schedules show.

A These -- this is the debt-to-equity ratios, including preferred stock, for the utility proxy group, both as it existed in 2010 and as Value Line projects it for the next three to five years.

Q Can you please turn to page ten of your direct testimony. And I direct your attention to lines 18 through lines 6 on the next page, page 11. Can you please take a second to read that to yourself.

A Yes, sir, I've read it.

Q Okay. The risk associated with the location and fuel mix, is this a factor -- is this risk factor systemic to the proxy or your industry group or unique to FPL?

A You're speaking of the storms and -- please repeat the question. I kind of missed it.

Q The risk associated with location and fuel mix, is this risk -- is this risk factor systemic to the industry, your proxy group, or unique to FPL?

A I believe it's unique to FPL in terms of the interaction. There are a number of companies that have natural gas generation, as FPL does, but being located in the Florida peninsula, isolated from the major web of pipelines in the continental region, for example, the upper Gulf region, makes it more difficult for FPL to access additional natural gas when there is a crisis or limitations on transport.

So it's the interaction that's unique to FPL that it is both located in a peninsula with limited access to the infrastructure of the continental United States and it's more than 60 percent dependent upon natural gas generation.

Q The risk associated with exposure to devastating storms, is this --

A Well, I think you have the same situation. Storms occur all over the country, but I think FPL is unique in, first, having a service area where one storm can affect the entire service area. Up in Texas we have tornados, which are terrible, but they are very limited in their geographic scope, where a hurricane is very broad in its geographic scope.

Also, the geography of FPL's service area interacts with the storm exposure and means that to get replacement power, to get additional resources to restore power, it has to come down the peninsula of Florida.

Houston, for example, has a great deal of hurricane exposure, but Houston is interconnected electrically with rail, with pipelines, with highways, so when there's a devastating storm in the Gulf Coast of Texas, generally resources that can be mustered very quickly from north, south, west, to restore power. Whereas, with FPL, the only avenue for recovery is from the north.

Q What about the risk associated with owning nuclear generation, is this risk factor systemic to the industry proxy group or unique to FPL?

A A number of the proxy group utilities have nuclear exposure. Some companies in the country have more exposure than FPL, but FPL has large exposure to nuclear, and again, its geographic location increases the challenge.

One of the problems -- while there are many advantages to nuclear, one of the characteristics of nuclear is, when there is an outage -- and often the outage is not because of the nuclear plant but because of some other reason -- the differential between nuclear costs and conventional fossil costs is so great that there's a large economic impact. And FPL is in the position of not having access to the north, south, east and west import of electricity because of its location at the end of the Florida peninsula.

So the thrust of my testimony is that while the risk factors are similar, they are particularly exposed for FPL because of the interaction of its location, its exposure to storm, its generation mix, and geography.

Q What about the dependency on natural gas, is that a risk factor systemic to industry proxy group or unique to FPL?

A Well, the answer would be very similar. FPL is exposed, it has a large commitment to natural gas, which is a good thing environmentally. Right now it's a good thing economically. But it is a very volatile fuel in terms of its price and sometimes there are deliverability problems with natural gas. And that means FPL has to maintain its financial strength in order to deal with volatile markets, in order to be able to hedge and negotiate from strength with suppliers, and the ability to react to transportation problems from a position of financial strength.

Q All right, let's see if we can get through these relatively quickly. The risk associated with economic fluctuation, is that a risk factor systemic to industry proxy group or FPL?

A Again, everybody -- all utilities are somewhat exposed, but FPL has what I call the double whammy, that not only does its economy react to the national economy because so much of its economic activity is tied to tourism, and tourism is particularly responsive to economic conditions. When the economy weakens, Florida Power and Light's customers suffer from the decline of tourism as well as the general decline in national economic activity.

Q What about the risks associated with large capital investments to support customer growth, is that a risk factor systemic to the industry-slash-proxy group or unique to FPL?

A It is similar. All companies have some investment requirements, but I think FPL has a particular large capital budget relative to its peers. I believe Mr. Dewhurst testified that the company expects to invest $9 billion in the next few years, so it has a very large capital budget.

And, again, because of its geographic isolation, exposure to storms, nuclear and natural gas and economic vulnerability, the company has to be in a position to make those investments in good times and bad.

Q All right. What about the risk associated with the need to finance significant capital investments, is that a risk factor systemic to industry proxy group or unique to FPL?

A Its systemic to the proxy group, but I think it is more important exposure for FPL and I think that's why FPL, for the reasons in the last question I articulated, because of the interaction of these factors, these five factors identified in the sections we're reading, FPL needs financial strength to support its capital investment that may be more significant than other companies in the proxy group.

Q All right. What about the risk referred to as ongoing regulatory risks, is that a risk factor systemic to the industry proxy group or unique to FPL?

A It's systemic to the proxy group. All of these are regulated utilities, and Moody's and Standard and Poor tell us that they consider regulation as being a major factor in their assessment of risk. The same with Value Line and other investment organizations. It's clear that regulatory risk is important.

I think FPL is in a unique position here, as well. The Florida Public Service Commission has a long history, as I describe in my testimony, of being supportive and innovative. When we started the Texas Commission in the seventies, we looked to Florida for guidance about how to do it right.

But in recent years, the last case, the order in early 2010 was upsetting to the regulatory community -- I mean, excuse me, to the investment community. They were shocked, as Value Line said, by the outcome of that case. The bond ratings were reduced, and Moody's, in a report that's actually quoted by Mr. Gorman, says the world is looking carefully at the outcome of this case to determine if Florida Public Service Commission, with the new

Commissioners, and the new start, will go back to the earlier tradition or will continue to be worrisome to investors.

Q All right. With regard to each of the risk factors that you have identified at the bottom of page 10 and the top of page 11 of your prefiled direct testimony, do you make any comparisons to how these risk factors affect FPL to how these same risk factors impact each of the IOUs listed in your Exhibit WEA-15?

A I don't do a specific comparison. I did select the proxy groups based on recognized objective risk criteria. And I am familiar with these companies. Most of them we have done cases in their state or Federal jurisdictions.

So I'm aware of these utilities and I am persuaded in my professional opinion that the risk factors that I've outlined for FPL put it in a unique position of requiring financial strength compared to these other companies.

Q In the event of a disruption of service at one of FPL's nuclear plants, would you expect FPL to petition this Commission for recovery of replacement costs or to look to its shareholders to recover those costs?

A I would expect FPL to petition the Commission. And when it does, I would expect the Commission to take a very careful look at the facts and circumstances associated with that outage to determine the extent of which those costs would be recovered. I, myself, have been involved in such a case recently.

But the important thing, from a financial strength perspective, starting in the nanosecond of the outage, FPL has to provide replacement power to keep the lights on in south Florida. So it has to start spending substantial sums of money to replace the very low energy cost nuclear power with the cost of power that almost by definition costs some multiples of what nuclear power costs. So there's an instant financial requirement of FPL that has to be met, even before it has a chance to go through a Commission proceeding.

Q In the event of a disruption at one of NextEra's non-regulated nuclear plants, who would be responsible for the cost of replacement power?

A Well, I think that depends on the contractual terms under which NextEra makes power available to the purchasing utilities. And I'm not really familiar with the details of those contracts. In my experience with purchased power agreements, very often the utility has to immediately provide the replacement power. But there is some requirement of the provider to make up some or part of the difference in the cost.

Q All right. Can you please turn to the bottom of page six, line 23.

A Yes.

Q Lines 22 and 23, excuse me, through page seven,

lines 1 and 2 of your prefiled direct testimony.
A Yes, sir, I'm familiar with those.
Q All right. In that you said that: In the past, FPL's financial strength, fostered by the support of this Commission -- I think you're talking about the Florida Public Service Commission -- has served customers well as the company has been able to raise capital on a reasonable and timely basis to meet past challenges such as devastating storms. Did I read that correctly?
A Yes, sir.
Q And my interpretation of "this Commission" is the Florida Public Service Commission, correct?
A It is. It's the only state commission regulating the retail rates of FPL.
Q Do you believe that FPL has been able to raise capital on a reasonable and timely basis after the Commission's decision in the last rate case of an ROE of 10 percent?
A No. I outline in my direct somewhat, and much more in my rebuttal, the effect of the last Commission order, in terms of the downgrades, in terms of Value Line's shock at the outcome. And I think the fact that the parties and the company worked to develop an alternative plan, which they agreed to in December of 2010, was a very important milestone in preventing the further degradation of FPL's financial

strength.

Q So do you believe that FPL has been able to raise capital on a reasonable and timely basis after the Commission ratified the stipulation agreement with an ROE of 10 percent?

A I believe so, although the bond ratings have not been restored to the previous level. But at least they've taken FPL off of the watch list and declared their bond ratings stable.

Q I just want to clarify. You said you believe so. So your answer to that question is yes, that FPL --

A It is yes. I think Mr. Dewhurst has in his direct and rebuttal more documentation of the financing activity, but as an outside expert, my impression is yes.

Q Can you please turn to page nine of your prefiled direct testimony, looking at lines 5 through 8. And I'm going to ask you to read that sentence that starts with the ten percent ROE was.

A Okay, you want me to read it aloud?

Q Yes, sir.

A The 10 percent ROE was unsettling to investors because it was such a low ROE for an electric utility in Florida and the decision was viewed as a departure from the FPSC's tradition of supportive regulation protected from political influence.

Q Sir, are you aware that FPL can earn 100 basis points above or below the 10 percent ROE decided in the last rate case?

A Yes, I understand that, and I understand under the December, 2010 settlement FPL has the ability to adjust its accounting in such a way that it in all probability will and can earn 11 percent, and, in fact, it has earned 11 percent.

Q Okay. That takes me to my next question. Would you agree that FPL was over-earning in May and June of 2010, above its 10 percent -- 100 basis point ROE threshold of 11 percent?

A I have some problem with the term over-earning. I understand it was earning more than 11 percent, or I think -- I'm not really -- the month-to-month variations you probably ought to talk to Mr. Dewhurst about.

My general understanding is that the company has been able to earn the 11 percent and has endeavored, in adjusting its accounting, to hit the 11 percent, but because of lags and so forth, it can't be done exactly.

Q So just to be clear, the company, FPL, was over-earning -- earning more than 11 percent ROE, correct?

A I really can't testify from my own personal knowledge that that is the case. I understand they haven't hit exactly 11 percent in each month but the net effect is that the earnings for the years have been 11 percent.

Q Looking at page nine, lines 11 through 14, can you read that statement for me, sir, starting with when the parties.

A When the parties reached a settlement that allowed FPL to earn an ROE of 11 percent, investors reacted with relief that the previous decision may have been a temporary deviation from the FPSC's tradition of regulatory support.

A Would you agree that FPL's midpoint ROE was 10 percent in both instances, regarding the rate case and the stipulated agreement?

A Yes, that's my understanding.

Q So the ROE did not change, correct?

A The allowed midpoint did not change. I think the ability of FPL to earn did increase and that's been borne out by the investor citing the 11 percent, the fact that they've actually earned 11 percent, and, again, the Moody's quote in Mr. Gorman's testimony talks about the ten percent as being a disappointment.

Q Okay, let me go back to some questions I asked you. Do you recall me asking you that -- do you believe that FPL has been able to raise capital on a timely basis after the Commission's decision in the last rate case with an ROE of 10 percent; you remember that question, correct?

A Yes.

Q And you remember my follow-up question as do you believe FPL has been able to raise capital on a reasonable and timely basis after the Commission ratified the stipulated agreement with an ROE of 10 percent, correct?

A Yes.

Q And I asked you did the ROE change in both instances, and you said no, correct?

A That is correct.

Q Okay.

A But there's more to an ROE decision than the midpoint, and I think what investors care about is what is actually earnable. And what was actually earnable under the stipulation was 11 percent, and that's what gave them comfort.

Q Okay, I understand your interpretation. Can you please turn to page five, lines 1 through 3.

A Yes, sir.

Q Can you please read that sentence that starts: I also present the regulatory precedent.

A You want me to read it aloud?

Q Yes, sir.

A I also present the regulatory precedent supporting the 25 basis point adder to recognize FPL's excellent management, superior service, and its achievement of low rates for its customers.

Q Would you agree, sir, that the low rates are partly a result of lower natural gas prices?

A Yes, the decision to focus on natural gas has been a good one --
Q All right. And would you agree --
A -- for customers.
Q And would you agree, sir, that the lower rates are partly a result of the Commission's decision in the last rate case?
A You mean the ten percent one in early 2010?
Q Yes, with the ratified stipulation.
A Well, the rate case set those rates, but the total effect on customers is the cost of fuel. And, of course, the rates customers are paying now are based on the stipulation of December, 2010.
Q Okay. Hold on one second. Do you know, sir, what the impact would be on a typical 1,000 kilowatt kWh FPL residential bill that included the previous rate case approximately $1.2 billion amount requested by FPL in both the projected and subsequent test years, and all base plant additions?
A No, I couldn't hazard that. I remember the Staff report in the last rate case said that the total cost of capital for FPL, if the full request were granted, would be less than for TECO as ordered by the Commission with the 11.25 ROE.
Q All right, sir, moving forward to fuel mix.

A Yes, sir.

Q What is the optimal fuel mix for FPL that would minimize the risk associated with fuel, fuel mix?

A I don't know. That is not my area of expertise. Fuel mix is a very complicated issue and it changes minute to minute as the future outlook for fuel costs, for transportation, for environment regulation, changes. So fuel cost strategy is a very complicated problem.

I know it's important in terms of the outcome for investors, but I'm not the one to talk about what it is right now, in terms of optimality.

Q Okay. Can you please turn to page 22 of your pretrial direct testimony.

A Yes, sir.

Q Can you please read aloud your testimony beginning on lines 3 through 9.

A Lines 3 through 9, on 22, beginning with the question?

Q Yes.

A Do the Commission's adjustment mechanisms protect FPL from expose to fluctuations in power supply costs? To a limited extent, yes. The investment community views FPL's ability to periodically adjust rates to accommodate fluctuations in fuel and purchase power as an important source of support for FPL's financial integrity. Should I continue or --

Q No, sir. Thank you. So would you agree, sir -- would you agree that the FPL -- that the Commission's fuel cost recovery clause is supportive to FPL's credit quality?

A Yes, it is supportive.

Q And are you familiar with the Commission's fuel clause?

A Generally, yes.

Q Would you agree, sir, that the fuel clause is administered on a projected basis?

A Yes. And that, I believe, is probably the predominant way most regulatory bodies do it these days.

Q So, in your opinion, is this superior to fuel clauses administered on an historical basis?

A It is, and I think that's why most utilities now have fuel clauses that are prospective.

Q Are you aware that the Commission's fuel clause allows for mid-course corrections for timely recovery of unplanned spikes in fuel costs?

A Yes. And again, that is a feature that's common in the industry these days.

Q And are you aware, sir, that over the years FPL has availed itself to timely recovery of fuel costs through mid-course corrections?

A Yes, although there have been times when, for example, natural gas prices went up very rapidly, when the total amount of exposure was very large before the wheels turned to allow FPL to start recovering the higher costs.

Q What changes to the Commission's fuel cost recovery clause would you recommend to make the clause more supportive of FPL's financial integrity?

A I really couldn't suggest any. I think the fuel clause is a state -- what I would term a state of the art fuel clause consistent with regulatory practice around the country. So I'm not here to suggest any specific changes.

Q For the purpose of your testimony in this proceeding, did you make a comparison of the fuel mix of FPL to the fuel mix of the IOUs listed in your Exhibit WEA-15?

A No, not specifically, because I relied on the objective risk managers of Value Line and the bond ratings to get down to what the total investment risk of the securities was. Again, as I stated earlier, I'm generally familiar with a lot of these companies because of my work in the industry, but I didn't specifically compare fuel mix.

Q Okay. Can you please turn to page 17, looking specifically at lines 2 and 3. Can you please read, starting on line 2, aloud for me, sir.

A During 2011 approximately 51 percent of the electric sales were attributable to residential customers, with 42 percent from commercial and seven percent from industrial and other users.

Q Did you derive this information, sir, from the FERC Form 1, page 300?

A I thought this was from the 10-K, but it's probably the same as in the Form 1.

Q Did you compare the amount of mix of customers at FPL with other electric utilities in your proxy group?

A Not specifically. I relied on the objective risk measures. Again, I'm generally familiar, because of my work in the industry, with the various fuel mix of the other companies -- not fuel mix, I said fuel mix -- customer mix.

Q So which revenue stream is more at risk, revenue derived from residential customers or revenue derived from industrial customers?

A Well, there's a lot of debate about that and actually I've done some research on it and testified about it. And what we have found in that research was that there is no statistical relationship between the customer mix and cost of capital except to the extent that being extreme does seem to have some effect on risk.

And FPL is relatively extreme in that it has low industrial and high residential. The industry average is generally about 35 percent residential and about 30 percent industrial.

Q So which group of customers is more at risk for leaving the FPL system permanently, residential customers or industrial customers?

A Well, again, that's not all that compromises risk. The risk of a customer is very multidimensional. Industrial facilities can cut down or reduce their use, but by the same token they are generally good for their bills, they pay their bills. Bad debt experience is less of a factor than it is with residential, plus, industrial contracts give the utility some stability. Industrial rates generally have a demand component to their bills which allows the utility to more closely track its costs.

So, again, I think the statistical results are that the customers do not materially differ in the risks they add to the utility in total. The nature of the risks are different. Industrials have more economic risk. Residentials have more credit risk.

Q Okay. Is regulatory risk unique to FPL or is it systemic to the other IOUs represented by the companies in your utility proxy group?

A Regulatory risk is systemic. It's an important factor to investors in evaluating the risk of utilities. I think the special thing about FPL is that its regulatory risk, first, is undiversified. Moody's has said that it prefers to have diversified regulatory risk.

So a company like AEP that has 11 different state jurisdictions, or Southern Company, that has four state jurisdictions, is accorded less risk than FPL that has one single state jurisdiction. And that state jurisdiction is in a state of flux in the view of investors.

Q Since regulatory risk is systemic to the industry, as you stated, would you agree any risk associated with regulatory risk is already incorporated in the returns indicated by your various market models?

A To the extent the market models have accurately captured the required return, they are. My market models are applied to the comparable companies, so therefore, by definition, they don't account for the specific risk of FPL, because FPL doesn't have stock traded in the markets. So we have to do some judgment in terms of assessing the risk of FPL.

Q Okay. Would you agree with me, sir, that through the implementation of the fuel cost, the fuel cost recovery clause, the nuclear cost recovery clause, and the various means of storm recovery cost, the Florida Commission has provided FPL with a supportive regulatory environment? You would agree with that, right, sir?

A Yes, I think those mechanisms are supportive. I think they individually give comfort to investors. But I don't think they're unique to FPL. I think across the country most of the comparable companies enjoy the benefits of very similar mechanisms.

Q We talked about embedded risks. Exactly how is risk mitigation already reflected in your recommended ROE range?

A Because I did market analysis of the comparable utilities, and the comparable utilities have similar mechanisms. So to the extent that those mechanisms are relevant to investors and affect their requirements, those are reflected in the market estimates that I have presented.

Q All right. Are you aware of how many companies in your utility proxy group own nuclear generation or are proposing to build nuclear generation?

A I have not done a specific study. We can go through the list and talk about them. You know, clearly Dominion, PGE, Scana, Sempra, Southern, Xcel.

MR. YOUNG: Okay, with that, Dr. Avera, we'll take a five-minute break and then we'll come back on the record.

(Brief recess)

BY MR. YOUNG:

Q Dr. Avera, I would like to move to the dividend discount -- I mean, discounted cash flow model.

A Yes, sir.

Q Looking at the discounted cash model, DCF model in this proceeding, how is your application of the DCF model in this proceeding different from your application of the DCF model in the other proceedings?

A Do you mean other proceedings where we're filing testimony now? I don't think -- is that what you mean?

Q In the past proceedings, the past proceedings.

MR. GUYTON: In the past proceedings, Keino?

MR. YOUNG: The past FPL rate case.

MR. GUYTON: Okay.

THE WITNESS: I think it is probably similar. I didn't go back to double check it. You know, I refine my methods as I go through time and get critical feedback from commissions and staffs, but I think it is generally similar. I can't think of any specific difference.

BY MR. YOUNG:

Q Okay. When did you start using non-regulated proxy groups in your DCF models?

A Probably two, two-and-a-half years ago, as I recall. And when you asked about DCF model, I was thinking about the inputs for the model. One change is probably using the non-utility group. And I don't think I did that in the last FPL case, but I've done it in all of my cases since probably 2010.

Q Why has your application of the DCF model changed over time?

A Well, the application has not changed, I just added another proxy group. And the reason was that it occurred to me that if the goal is to get the most accurate estimate of what investors require, limiting to one industry defeats that purpose, because there may be a distortion in that particular industry. And in particular, in 2010, the Value Line suddenly became very bearish on the natural gas distribution industry and their earning growth rates became very, very low.

And so it occurred to me that we shouldn't let -- since Value Line's forecasts are so important in the application of the DCF, we shouldn't let their opinion on a particular industry distort our estimate of what investors require, since investors clearly invest across many industries.

In fact, the CAPM is founded upon the notion that investors are fully diversified. So it occurred to me that we should look at industrials, but we should look at industrials that are in the same risk class as utilities. So that's when I developed the approach of looking to non-utilities that have risk measures in the same range as utilities.

Q Did you use current market stock prices in your DCF model analysis?

A Yes.

Q Did you use forward-looking growth rates in your DCF analysis?

A Yes, I do.

Q Since you relied on the current market stock prices and forward-looking growth rates in your analysis, would you agree that the investor's expectation regarding risks faced by the electric utility industry are reflected in your application of the DCF model?

A Not exactly, because we're still estimating an unobservable parameter, which is investor's required return. And we don't know what investors expect in the way of growth. A very reasonable approximation is published analysts' forecasts by Value Line, Hybris, Zacks, Reuters.

But we don't know with certainty that that's what investors had in their heads when they paid the current market price for utility stocks. So there is an error -- you know, a zone of uncertainty around our estimates.

Q Would you agree that the latest information is more appropriate to determine forecasted amounts such as interest rates and financial models, et cetera?

A No, not necessarily. I think any observation needs to be synoptic, which is a word that means the observations have to be at the same time. So you have to match your observation of interest rates, of dividend yields and growth rates, and other risk measures at a particular point in time. So if you're going to update part of the analysis, you need to update all of the analysis.

Q Would you revise your ROE recommendation if the most current information supports a lower or a higher ROE?

A Yes, I would, but I don't think that's the case here. In my rebuttal I replicated the analyses of the opposition witnesses using the July data that they used. And when corrected, their analyses confirmed that the 11.25 percent was in the range of reasonableness, just as I had estimated using November and December data in my direct.

Q So do you plan to update the results of your DCF model or any other model during this hearing?

A At present, I don't, unless there is some dramatic change in capital markets over the next two weeks. I believe that my reworking of the opposition witnesses' DCF, CAPM, and risk premium and expected earnings is sufficient to demonstrate that under current capital market conditions my recommendation remains robust.

Q Just one second, sir. Dr. Avera?

A Yes, sir.

Q Let me ask you a question. Did you provide the discovery response to Staff's First Set of POD Number 14, which is --

A I believe I responded to every question that I knew about.

Q Okay, which is Bates stamped page -- which is Bates stamped page 000183. It's FPL RC-12, which is part of the Moody's Investors Service Rating Action.

A I think I'll see if I can find that.

MR. GUYTON: Keino, we're going to have to try to pull it.

MR. YOUNG: Okay, no problem, take your time.

MR. GUYTON: What's the Bates number, 000183?

MR. YOUNG: Yes, FPL RC-12.

MR. GUYTON: RC-12?

MR. YOUNG: Yes.

MR. GUYTON: We think we have it now.

THE WITNESS: Okay, I'm ready to respond.

BY MR. YOUNG:

Q Let me ask you to look at the third -- the third bullet that says historically strong financial metrics and cash flow. Do you see that?

A Let's see, we're on 182?

Q 183.

A 183? So the third bullet on that page. Got it.

Q Can you read that aloud, sir?

A Historically strong financial metrics and cash flow coverage metrics that may decline somewhat following the recent rate case decision, although Moody's expects any decline to be modest as a high percentage of FP&L's revenues are recovered through riders and other cost recovery provisions that remain strong. In addition, FP&L's recently awarded 10 percent ROE is consistent with those granted to some utilities in other parts of the country and its 59.1 percent equity ratio remains one of the highest in the U.S., mitigating the negative effect of the relatively low base rate increase.

Q So do you agree that with this assessment of the 10 percent ROE it's consistent with those granted to some utilities in other parts of the country?

A Yes, it is. There are other utilities that have similarly low ROEs; not in Florida at this time. And I also note that it points out the capital structure mitigated the effect, and I understand the opposition witnesses in this case are supporting a lower equity capital structure.

MR. YOUNG: All right, I need to -- can I take a two-minute break, please?

MR. GUYTON: Sure.

(Brief recess)

MR. YOUNG: Hello?

THE WITNESS: Hello, this is Bill Avera. I'm here.

BY MR. YOUNG:

Q Dr. Avera, I think we are now on -- to the previous questions, do you agree with the other parts of the assessments from the Moody's investor -- the Moody's Investor

Service action -- service rating action?

A Well, you know, whether I agree or not, when Moody's speaks, the market listens. And Moody's said, right above the part you had me read, how the decision was a departure from the FPSC's history of supportive regulation. So I think that's a very significant part of this.

Plus, not to be forgotten, the purpose of this analysis is to announce a downgrade of the bonds. So Moody's, considering all of the factors in the case and the financial structure, the equity ratio, the adjustment mechanisms, all of that, led them to downgrade FPL to closer to the other utilities in the country, which weakened its financial strength.

Q Okay. Do you have the -- are you familiar with the FPL's response to the POD -- Staff's First Set of POD Number 5, which is FPL Bates stamp number 000151? It's part of FPL RC-12. It's also part of the Moody's Credit Opinion.

A This same opinion or another one?

Q It's another one.

A Okay, I have it in front of me now. This is the 11, April, 2011?

Q Yes.

A Okay, which page of that opinion?

Q Page 151. Bates stamp 000151.

A Okay, I'm there.

Q All right. Looking at the paragraph that starts although cash flow coverage metrics -- do you see that? It's like the third full paragraph from the bottom.

A Okay, although cash flow coverage metrics could decline?

Q Yes.

A Yes.

Q Could you read that for me, please?

A Although cash flow coverage metrics could decline as a result of the base rate freeze, the use of its depreciation reserve and additional debt issued to finance high capital expenditures, Moody's expects any decline in these metrics to be modest. Coverage metrics could continue to be supported by a higher percentage of FPL's revenues that are recovered through cost recovery clauses, the slow improvement in economic conditions in its service territory, and the still adequate 10 percent return on equity that includes a range of plus or minus 1 percent. As a result, Moody's conditions in its service territory and a still adequate ten percent -- I may be reading it -- here we go.

As a result, Moody's anticipates that FPL's credit metrics will continue to remain well in excess of the financial ratio parameters required for its current A2 rating.

Q And I think you said when Moody's speaks, the market listens, correct?

A That is correct. And also part of this report is their assessment of the December, 2010 settlement, which allowed the company, through its depreciation reserve, to earn in excess of 10 percent.

Q All right. So would you agree that with this assessment -- and I quote -- still adequate 10 percent return on equity -- would you agree with that?

A Well, I think it says that, but it's in the context of the rest of the settlement, which allows FPL to effectively earn 11 percent. And I would also note it's sufficient for Moody's to maintain its stable A2 rating, not to return to the previous rating.

Q Okay. Would you agree with the statement the high percentage of FPL revenues are recovered through cost recovery clauses, relative to other electric utilities in the industry?

A Let me make sure. Let me go back. That's part of that paragraph we read on 151?

Q Yes. Yes.

MR. MOYLE: Just so the record is clear, what is the document the witness is reading from?

MR. YOUNG: The witness is reading from FPL's Response to Staff's First Set of Production of Documents Number 5, Bates stamped page Staff -- this is Staff

000151 FPL RC-12.

THE WITNESS: I do not see in that sentence relative to other utilities.

BY MR. YOUNG:

Q No, I --

A What I see is the high percentage of FPL's revenues that are recovered through cost recovery clauses.

Q And I'm asking you, do you agree with that quote relative to the other electric utilities in the industry.

A No, no. I think all utilities recover more than half of their revenues through recovery clauses.

Q Let me rephrase it. Do you agree with the statement that the high percentage of FPL's revenues that are recovered through the cost recovery clause -- that's it right there, close quote -- and then I asked you relative to the other electric utilities in your proxy group.

A And my response is FPL is not unique in my experience -- and again, I have experience with almost all of these utilities. They earn a large percentage of their revenues through recovery clauses.

Q All right.

A So that is not different. I think what Moody's is saying here is that the effect of the rate case did not affect all of the revenues of the company.

Q Okay. And this is the last POD response I'm going to ask you to look for, and that's FPL's response to Staff's First POD Number 18. And that's Bates stamped page Staff 000269 FPL RC-12.

MR. GUYTON: It may take us a minute to get this.

MR. YOUNG: No problem.

MR. MOYLE: The title of the document?

MR. YOUNG: The Moody's Investor Service Global Infrastructure Finance. This is from October 28, 2010. Uncertain Times Ahead -- and it's titled Uncertain Times Ahead; Strengthening Balance Sheets Now Would Protect Credit.

MR. GUYTON: Thank you. We're trying to find it.

MR. YOUNG: Not a problem.

MR. GUYTON: Keino, while we're looking at that, would it be helpful to the record to have both the documents you've asked Dr. Avera about attached as deposition exhibits so that we have the full context?

MR. YOUNG: Not a problem. So we can mark it as Deposition -- while he looks for that, we can mark POD -- FPL's Response to Staff's First Set of POD Number 14, Bates stamped page 000183 FPL RC-12 as Exhibit Number 1.

(Whereupon, Deposition Exhibit No. 1 was marked for identification.)

MR. GUYTON: All right. And before you identify the others, so that we don't slow us down, can you give me the Bates number of the third document that we're looking for? We're having a hard time finding it.

MR. YOUNG: 000269.

MR. GUYTON: All right. I'm sorry for the interruption.

MR. YOUNG: No problem. My apologies in terms of not giving you a heads-up on these.

The second exhibit is FPL's Response to Staff's First Set of POD Number 5 Bates stamped page Staff 000151 FPL RC-12.

(Whereupon, Deposition Exhibit No. 2 was marked for identification.)

MR. GUYTON: And both of those will be two-page documents, correct?

MR. YOUNG: Yes. Well -- hold on one second. Mr. Guyton?

MR. GUYTON: Yes, sir.

MR. YOUNG: If you want the full report, it's my understanding for the first one, the POD Number 14, it is one, two, three, four pages. And for the second exhibit, POD Number 5, it's one, two, three, four, five pages.

MR. GUYTON: I think that would be helpful for context, if Staff doesn't mind.

MR. YOUNG: Not a problem.

MR. GUYTON: We have no objection to those deposition exhibits. We're having a hard time finding the third one you've asked us about. We don't know if our Bates numbers are off or what. We're still looking for it. Can we take a couple of minutes break and try to find it?

MR. YOUNG: Not a problem.

(Brief recess)

MR. YOUNG: Charlie, you want that one marked, too, right, as Exhibit Number 3?

MR. GUYTON: If you're going to ask the witness about specific excerpts, I think having the whole document in would be helpful for context.

MR. YOUNG: So let's mark that as Exhibit Number 3, which is FPL's Response to Staff's First Set of Production of Documents Number 18, Bates stamped page Staff 000269 FPL RC-12.

MR. GUYTON: Keino, will you check and see if that's a response to 18 or 19? I think that's where we got thrown off. We think it's the response to 19.

MR. YOUNG: Okay, so strike that. Instead it's 18, it will be 19, subject to check.

(Whereupon, Deposition Exhibit No. 3 was marked for identification.)

BY MR. YOUNG:

Q Sir, can you take a second to read the second full paragraph on the page?

A Which page is this? I'm looking at the first page of the document?

Q No, I'm looking at page six of the document.

A Okay, let me get there.

Q And it's Bates stamped page number 000269.

A Okay, and it's the third paragraph?

Q The second paragraph.

A We increasingly believe?

Q Yes. Take a second to read that to yourself.

A I've read it.

Q Sir, can you read that aloud, starting with we increasingly believe?

A We increasingly believe the ROE that regulators approve for utilities will slowly decline over the next few years, perhaps to a point where the sector's average authorized ROE consistently falls below the 10 percent threshold. This falling ROE is due, in part, to our expectation that today's low interest rate environment will continue to reduce a company's all-in cost of capital. But we still don't think ROE is as important to a utility's cash flow, although we acknowledge that equity returns will influence management and Board behavior.

Absent adequate returns utilities might begin to pare back their regulated investments, theoretically in pursuit of better returns elsewhere. Regulators could also implement more formulaic rate structures, giving utilities better visibility into future ROE. We believe that most utilities would prefer the certainty of lower earned returns than the uncertainty of potentially higher allowed returns.

Q Do you agree with this assessment concerning ROE?

A No.

Q Consistently falling below 10 percent?

A No, actually, ROE, average allowed ROE, ticked up in the last quarter from -- as I remember, the number is about 10.2 to about 10.4. So I don't think -- I disagree on two counts.

Now, there are many things in this paragraph I agree with. For example, low ROEs will reduce the willingness of investors to invest in utilities. But I don't believe that interest rates will remain low. I hope they don't, for the sake of my grandkids.

I think the economy will recover and we will have higher interest rates. And I think that we will not see -- although this is my personal forecast -- the allowed returns for electrics fall below 10 percent. They aren't there yet and actually they're headed the other way.

Q All right. So you said that ROE -- that the ROE has ticked up above 10 percent, correct?

A No, it's never gone below 10 percent. The ROE for the second quarter, I think, was higher than the average ROE for the first quarter.

Q What is your source, sir, of that assessment?

A Regulatory Research Associates.

MR. YOUNG: Charlie, I'm going to ask for a late filed exhibit in terms of Regulatory Research Associates most current ROE.

MR. GUYTON: Okay. And that's -- you want to over period of time or do you want the current?

MR. YOUNG: The current.

MR. GUYTON: Okay.

MR. YOUNG: And that's going to be Exhibit Number 4. That will be a late filed exhibit. And Charlie, do you want to give it a title?

MR. GUYTON: Current Average Authorized Return on Equity?

THE WITNESS: Yeah, I think the report, itself, is called Second Quarter Update.

MR. YOUNG: One second.

MR. MOYLE: So I'd like to obviously get a copy of that, as well, if it's going to be a late filed exhibit.

MR. GUYTON: Certainly.

MR. MOYLE: And I guess the only point of clarification is the snapshots of the second quarter, and even though we're in the third quarter, is there an ability to --

THE WITNESS: We have to wait until the third quarter is over. So I think they issue this a few weeks after the end of the quarter. So this would be regulatory decisions through the end of June.

MR. MOYLE: Okay. So there's not a service or you don't try to find regulatory decisions that may have occurred in the month of July to get the most up-to-date, quote, unquote, current information? This would be, in effect, second quarter?

THE WITNESS: Right. This is a resource that I believe is quoted by other witnesses in this case. It's a recognized source of allowed returns. Mr. Gorman and Mr. Baudino both refer to it.

MR. YOUNG: Okay, so let's get the title. It will be the current -- the most current regulatory focus.

MR. MOYLE: Second quarter, 2012, right?

THE WITNESS: Right.

MR. YOUNG: Yeah, okay, Second Quarter 1012 regulatory Focus. That will be the title, okay? From Regulatory Research Associates.

THE WITNESS: Yes.

(Whereupon, Late Filed Deposition Exhibit No. 4 was identified.)

MR. GUYTON: Would you have me send that to the court reporter or would you have me send that to you and to all the parties? How do we want to distribute that?

MR. YOUNG: I think it would probably be best to me and to all the parties because -- I can forward it to the court reporter, but I think the transcript might be out before then.

MR. GUYTON: All right, we'll undertake to do that electronically.

MR. YOUNG: All right, just to clarify, we want the most current one. I think -- I don't want to just -- because if one comes out before you send it, I would like to have it.

THE WITNESS: I believe this particular report only comes out at the end of the quarter, so there will not be another one until September, or actually October.

MR. YOUNG: Okay, that's fine. All right, one second.

(Brief pause)

BY MR. YOUNG:

Q All right, back on the record. Dr. Avera?

A Yes.

Q In the 2009 FPL rate case you recommended 11.25 -- 11.25 percent on your ROE, and in the current case you're recommending -- I mean, excuse me, you recommended 12.5 in 2009, percent on your ROE.

A Yes, that's my recollection.

Q And then in the current case you're recommending 11.25 percent.

A That's right, plus the 25 basis points.

Q Plus the 25 basis points. Can you state the reason for the lowering of your recommended ROE?

A Yes, that's what the numbers reflected when I did the analyses. I didn't do it relative to what I did in 2009, I did the analyses based on the data available in the end of 2011.

Q Okay. One second. Dr. Avera, can you please turn to page 29, lines 10 through 13 of your prefiled direct testimony.

A Lines 10 through 13, yes.

Q Actually, let me correct that. Can you go to line -- I'd like for you to read aloud starting on line 8 through line 13.

A How do interest rates on long-term bonds compare with those projected for the next few years? Answer: Exhibit WA-2 compares current interest rates on 30-year Treasury bonds, triple-A rated corporate bonds, and double-A rated utility bonds with near-term projections from Value Line, IHS Global Insight, and Blue Chip Financial Forecasts, Blue Chip, S&P and the EIA.

Q Have you reviewed the updated forecasts from these sources lately?

A I have. I've not committed them to memory but I'm generally familiar with them.

Q Are there any changes in terms of the current rates, current interest rates?

A All of them expect rates to increase. I think they probably moved the increase further out in time than it was. In terms of 2012, we're now halfway through, and I think interest rates have not started up yet.

Q So are there any modifications to these sources since you --

A My understanding is that they still project rates going up but have moved the dates out. So each year the rates would be lower now than displayed on WEA-2, page one of one.

MR. YOUNG: Charlie, I hate to do this, but I have to ask for a late filed exhibit of WEA-2, a late filed exhibit with the updated WEA-2.

THE WITNESS: Let me make an observation. Some of these may not yet be updated from the ones that I used, but to the extent -- do you want the sources or do you want me to recast this exhibit?

MR. YOUNG: Recast.

THE WITNESS: Okay. Well, I will do so. We will move the dates up and I just -- I can't guarantee that there will be new observations for each source, because they are periodic, just like we were talking about RRA.

MR. YOUNG: That's okay. And that will be Exhibit Number 5. It will be Updated WEA-2. I'm sorry, that will be Late Filed Exhibit Number 6.

MR. GUYTON: No, I have it as 5.

MR. YOUNG: You have it as 5? All right, my numbers are off.

(Whereupon, Late Filed Deposition Exhibit No. 5 was identified.)

BY MR. YOUNG:

Q Dr. Avera, looking at flotation costs.

A Yes.

Q Page 72, lines 3 through 5, and it states: Issuance costs are a legitimate consideration in setting the return on equity for a utility, and I recommend incorporating a minimal, 15 basis point adjustment in determining a reasonable ROE range for FPL. Did I read that correctly, sir?

A Yes, you did.

Q Have you calculated the specific flotation costs that FPL has incurred to determine this flotation cost 15 percent -- 15 basis point adjustment?

A Yes, I reviewed the 2002 -- the May, 2002 issue that FPL made of a public equity offering, and the flotation costs there were in excess of 3.11 percent. I also looked at the equity units that have been issued since then. And the flotation costs, again, even without expenses, just the discounts, were over 3.1 percent.

So I think that would suggest that the 15 percent is still within the range specifically for FPL. I noticed that Mr. Baudino suggested that maybe there were economies of scale. The largest utility equity offering in the history of the world was in 2010 by AEP, and the flotation costs of that were 3.56 percent. So I think there is no reason to believe that these are not representative numbers.

Q Does your 9.6 percent to 12.3 percent cost of equity range include an adjustment for flotation costs?

A My 9.25 to 10.25, yes, it does.

Q Looking at investor impact, can you please turn to page 73, lines 21 through 23.

A Yes.

Q Can you read aloud -- out loud the sentence that starts with without an adequate ROE?

A Without an adequate ROE FPL will not be able to compete for investors' money at the very time it is needed most to protect customers.

Q Would you agree, sir, that FPL's stock performance would be an indicator of investors' interest in an investment relative to a broader market indices such as the S&P 500?

A You mean NextEra's stock performance?

Q Yes.

A It is one indicator. There are many things, as I talk about in my direct and rebuttal, that drive stock movements besides what FPL risk and prospects are, but it is perhaps one indicator.

Q And would you agree that subject to check that NextEra Energy, Inc.'s stock has outperformed S&P 500 even after receiving a 10 percent ROE in the last rate case and in the stipulation?

A Well, as I remember it, I think I have this in my rebuttal. The stock dropped 10 percent after the first order in early 2010, and it subsequently recovered at the settlement in December, 2010.

Now, I have not looked at the net-net effect between the first order and now. I do know that utilities have generally been strong during that period, but so has the market.

Q Okay. Looking at returning to regulatory normalcy, page 75, lines 9 through 12, starting with more recently. You see that?

A Let's see, excuse me, 75, 9 through 12. Yes.

Q Can you read that aloud, starting with more recently, and stop at eliminate -- or, excuse me, climate.

A More recently, however, the rating agencies have expressed optimism that this period of regulatory and political strife has been replaced by a return to a more orderly and constructive climate. For example, the noted -- the regulatory clarity provided by the FPSC's approval of the December 10, 2010 settlement agreement governing FPL's base rates. Continue?

Q No, sir, that's good enough. In your opinion, do you believe the current Commission has a positive track record with regard to supportive regulations?

A I believe it does thus far, but as I said, and again, I think this is in Mr. Gorman's testimony, quoting from Moody's, they are watching this case with great interest to see if the track record will be extended with the outcome of this case.

Q Is the recent Commission decision to grant a 10.25 ROE to Gulf Power Company a supportive regulatory decision, in your opinion?

A Well, I only have general knowledge of Gulf and Gulf's case. I do know that FPL faces many challenges that Gulf does not. Gulf is part of a diversified holding company that has many regulatory jurisdictions, that has very strong finances. Gulf's geographic location and fuel mix are very different than FPL's.

So I'm not in a position to correlate the 10.25 and what an equivalent return to FPL would be. My analysis suggests that FPL ought to get an 11.5 return.

Q Is it true that the standard, constant growth DCF model shown on page 41, line 7 of your prefiled direct testimony is a deviation from the equation that delineates the relevant expected cash flows into perpetuity?

A Yes, it is derived from a theory advanced by John Burr Williams in 1938 that the inherent value of common stock is the present value of future dividends.

Q Okay. Can you please provide the -- I can never say that word -- derivation of your DCF model that shows the expected growth rate of earnings in the appropriate growth rate to use in your current DCF analysis?

A Well, let me show you, this model, I think I cite the 1974 paper by Myron Gordon, which is an annual model. And the growth rate there is the growth rate of everything. Under the DCF theory, earnings, dividend, book value and market price all grow at the same rate.

In the real world, investors are interested in the cash flows that occur to them, not the cash flows that continue into infinity, because, as Cain said, in the long run, we're all dead.

And as Mr. Baudino, who I guess is in the same category of Cain, said that most investors don't hold stock for five years. So investors are really concerned about their cash flows, which is the dividends they receive while they own the stock and then the price at which they sell the stock, their capital gain.

Q Can you provide a derivation showing the earnings is the appropriate growth rate?

A No, I can't, because the model, the theory in Gordon's 1974 paper is based on an infinite horizon where earnings growth and dividend growth and book value growth and price growth are all at the same rate. I can provide that derivation, if you would like, but it doesn't discriminate between earnings growth and dividend growth and book value and price growth.

In my testimony I have quotes to document that what investors care about when they're forecasting their capital gains is projected earnings growth.

Q Okay. Now let's move on to your rebuttal testimony, page seven, lines 2 through 4.

A Did you want that -- I think I have provided the Gordon paper in my work papers. Is that good enough or do you want --

Q Yeah, I think we're fine. Page seven, lines 2 through 4, starting with the allowed.

A Yes.

Q Can you read that, ending on credible?

A The allowed ROEs for the companies that opposing witnesses consider to be comparable in risk also demonstrate that their recommendations are too low to be credible.

Q What do you mean by too low to be credible?

A Well, if you look at my exhibits where I take the allowed returns of the other experts -- let's see, let's start with Exhibit 20, page one of three, Dr. Woolridge's group, the average allowed return is 10.4. The only return that is below or close to his suggestion of between 9 and 8.5 is UIL Holdings that both Mr. -- or Dr. Woolridge and I were in in 2009, and that has many special characteristics.

In fact, RA didn't even include it in their average return because of the unique characteristics. Because you take out UIL, there's nine percent, 8.5 would clearly be an outlier.

As we turn over to page two and look at Mr. Gorman's proxy group, the average is 10.62. The lowest number on the page is 9.93 for Consolidated Edison, that is a distribution only utility.

And then, finally, on page three of three, we have Mr. Baudino's proxy group which averages 10.43. And again, the lowest ROE appearing there is Con Ed, which is a distribution only utility.

And so I think it's pretty clear that if the Commission were to order an 8.5 or a 9, it would pave new ground for an ordinarily fully reintegrated utility.

By the way, UIL is for a distribution only utility. Their transmission is allowed to earn substantially more, and so is their generation.

Q So when you calculate the number that is too low, is it below your reasonable range of 9.6 percent?

A It's below that, and it's below what anybody has gotten in anybody's comparable group, except the special case of UIL. And Dr. Woolridge and I can tell you all about that case.

Q Did you calculate the credit metrics to determine if an -- one second, please.

Let me ask you, did you calculate the credit metrics to determine if an opposing witness' ROE recommendation would affect FPL's credit rating?

A Yes, I did, kind of a back of the envelope. I got Mr. Gorman's work papers and I put in his numbers without any disallowances, but just changed the capital structure to 50 percent, and it would not support a single-A rating by the S&P matrix.

Q Can you provide that as a late filed exhibit? Do you have it?

A Yes, it's not in smooth form, but I will present it if that's what you'd like.

Q Yes, and that will be Exhibit Number 6, which is late filed, and this is Dr. Avera's calculation of opposing witness's ROE effect on FPL's credit rating.

MR. GUYTON: I think it would just be Mr. Gorman's.

THE WITNESS: While I'm at it, I can put in the 8.5 ROE that's recommended, too.

MR. YOUNG: Yes.

THE WITNESS: Which would be even more of a disaster.

MR. YOUNG: Yes.

(Whereupon, Late Filed Deposition Exhibit No. 6 was identified.)

BY MR. YOUNG:

Q Dr. Avera, can you please turn to page 11 of your rebuttal testimony, lines 2 through 4.

A Page 11, 2 through 4, yes.

Q That starts FPL is no longer.

A FPL is no longer among the most highly rated utilities due to the downgrade that followed the outcome of the last rate case, but the company's financial strength is above average.

Q How many utilities, sir, in the United States, have a higher credit rating than FPL, electric utilities, have a higher credit rating than FPL?

A I would have to look. There is a report, strongest to weakest. But there are a number of double-A utilities and there are a number of single-A-plus utilities.

Q Subject to check, looking at the S&P utility credit rating distribution in the second quarter of 2012, subject to check, would you agree that only three utilities have a higher rating, an A or higher rating than FPL, which is single A, A-minus?

A I would have to see that before I would accept it subject to check. There are not a whole lot, but there are some. You know, one was -- several have been eliminated through mergers, like LGE and Kentucky Utilities, and then also the outfit up in Boston that was taken over by Northeast Utilities.

So the decline in the number is not the result of downgrades as much as it is the result of what once were freestanding companies now being absorbed by other companies.

Q Okay. Looking at page 28 of your rebuttal testimony, lines 1 through 4, can you read lines 1 through 4 out loud, stopping with respectively?

A Yes. With respect to the group of electric utilities that Mr. Gorman and Mr. Baudino concluded were most comparable to FPL's jurisdictional utility operations, as shown on pages two and three of Exhibit WEA-20, these firms are presently authorized average rates of return on equity of 10.6 and 10.4, respectively.

Q Do you believe that FPL can justify a premium of

90 to 110 basis points over the opposing witness proxy group's authorized average rate of return on equity?

A Yes, because I think FPL faces unique challenges and risks. I think it's important for the FPSC to maintain its track record of allowing higher returns than other commissions. I think the customers benefit from that.

So I think FPL should earn -- also I think FPL should properly get the adder to recognize its performance and low rates. So I think, looking at what these companies are actually allowed, I think, is supportive of the 11.5 recommendation we're making.

MR. YOUNG: All right, thank you, Dr. Avera, I have no further questions. I appreciate your time here today.

THE WITNESS: Thank you.

MR. YOUNG: Jon Moyle?

MR. MOYLE: I have questions. Why don't we just go the record.

MR. YOUNG: All right, we can go off the record.

(Off the record/brief recess)

BY MR. MOYLE:

Q For the record, Jon Moyle on behalf of FIPUG. And I wanted to ask some questions of the witness. Some of them are follow-up questions and I have some other lines of inquiry. But during the Staff questions I think you had mentioned a report that you termed the strongest to the weakest report. Do you recall that?

A Yes.

Q What is that report?

A Well, it's actually cited in Mr. Gorman's MPG-18. It is a report that S&P issues that ranks utility operating companies, and all utilities, not just electric, from the strongest to the weakest. It has about 227 companies.

Q And do you know where FPL falls in that report?

A It's near the top, but it is not at the top; stronger than most companies because most companies are in the triple-B range, whereas Florida Power and Light is still, notwithstanding the downgrade, in the A-minus range.

Q Okay. You also indicated that you had -- you were going to have a Late Filed Exhibit 6, that represented a back of the envelope analysis you did if you assumed a 50 percent FPL equity ratio, is that right?

A Right, and then I also said I would use the 9 and 8.5 percent ROEs that have been mentioned by some of the opposing witnesses.

Q And what ROE did you do on the back of the envelope analysis that you discussed?

A The 9.25 -- I'm really working off of MPG-18, Mr. Gorman's 18, where he purports to show where FPL would fall in the S&P matrix under his recommendation.

Q Did you -- when you came to the conclusion that they would not be within the credit matrix -- that's a credit matrix that's put out by who?

A Standard and Poor.

Q And did you do an analysis as to the degree by which they did not fall within that credit matrix?

A Well, the credit matrix has ranges, and Mr. Gorman -- there are some typos and mistakes on the exhibit which I have corrected, but he calculates the numbers under his recommendation and puts them against the ranges that S&P has for their degree of financial leverage. And then you go to the 2009 S&P report to see how that lines up with the bond rating given the business profile risk of the utility.

And what I did is I took Mr. Gorman's work sheet, which he supplied in discovery, and made some changes to reflect a different capital structure and I can also make changes to reflect different ROEs. I did not take into account the disallowances of rate base and expenses that had been proposed by the various parties.

Q So the two changes you made were equity structure and ROE?

A Yes.

Q And what equity structure did you run, a 50 percent? 50-50?

A Yes.

Q And you ran an ROE of 9.25?

A Or nine.

Q I'm sorry?

A I did 9.25, which was built into the table, and then I did a sensitivity using nine. But I think the 50 and the 9.25 that Mr. Gorman proposes the -- are weak -- reduction in ROE. They are clearly below those necessary to maintain the current bond rating. And if you were to consider any of the disallowances, it would even be further away from --

MR. McGLOTHLIN: Jon, this is Joe. I don't like to interrupt your flow, but I would like to note for the record that both with respect to the Staff's requested late filed exhibit and any questions that relate to it, those strike me as in the nature of supplementing this witness's rebuttal.

And I know that we've reserved objections as to form until the time of hearing, but I just want to note for the record that we regard this as outside the scope of his rebuttal and intend to object to any use of the late filed exhibit and any portion of the transcript relating to it.

BY MR. MOYLE:

Q Okay, I think that's noted. I was going to ask the witness, because you said you're also going to run one at 8.5, is that right?

A Yes.

Q And what equity debt ratio will you run on that?

A Well, it's a little unclear. That's Dr. Woolridge's position, and I think we would do it both at the actual debt ratio and at the 50 percent that he recommended.

Q Okay. If you're going to do that, could you also do a run that has a 55 percent equity ratio and a 9.5 percent return?

A 9.5?

Q Right.

A Yes, if everybody is on board with that, I'll do it.

Q I think for the purposes of providing an informative document, whether it gets admitted or not, I think that would be helpful.

A So it will be done.

Q Thank you.

MR. GUYTON: Jon, do you want that as a separate exhibit, or just part of Late Filed 6?

MR. MOYLE: Part of Late Filed 6.

MR. GUYTON: We can do that.

BY MR. MOYLE:

Q You were asked some questions about the FPL's stock price in January of 2010 when the last rate case decision was entered. Do you know what FPL's stock price was at the point in time the PSC entered its order in the last FPL rate case?

A As I sit here today, I don't remember. I remember it broke sharply down, and I believe Mr. Dewhurst has in his testimony that there was a 10 percent drop in a short period of time.

Q As we sit here today, do you know whether it has recovered from that ten percent drop?

A I don't know exactly. I know that its price -- NextEra, the successor, and other utilities have generally been strong since 2010.

Q Okay.

A In fact --

Q And are you assuming that FPL has generally been strong, or you just don't have information as to how FPL has tracked since 2010?

A Well, FPL doesn't have a stock price. NextEra has gone up. I haven't compared it to other utilities or the exact percentage.

Q Okay, but the only way you can -- or one way to track FPL's value is to see what the holding companies that contain FPL, the regulated utility, is trading for, correct?

A Well, as I discussed earlier, it is some indication but there are a lot of other factors that affect NextEra's stock price besides the value of FPL.

Q Do you think FPL is a significant factor?

A It very much is a significant factor, but it is not the only thing -- the value of FPL is not the only thing driving the stock price in the market. Investors' expectation of the future, and so forth, are important, as well.

Q Wouldn't you agree with me, sir, that the two primary components that drive the NextEra stock price, irrespective of external third-party factors, is the performance of Florida Power and Light, the regulated entity, and the performance of NextEra, the unregulated entity, that are both subsidiaries of the publicly traded NextEra Energy?

A I would say those components are important but I believe the relevant performance is the future performance, not the past performance. Investors who buy NextEra today don't get history, they only get the future.

Q I understand. But in terms of the two components that would predict the future, can you agree with me that the operations of FP&L and the unregulated entity NextEra are the two primary components of the holding company?

A Yes, they are the primary components, but earlier you had said that there are other factors driving the stock price, and I certainly agree with that, besides the prospective performance of the underlying enterprises.

Q Sure. How the Euro is doing may affect the stock price, correct?

A That's correct, and how Greece is doing, and all sorts of other things, for better or worse.

Q Right. But typically you would agree that with some variability those external factors often are matters about which FPL has no control, correct?

A That's certainly correct.

Q And that they flow across a variety of stocks and sometimes they flow across the market as a whole, correct?

A Yes, to a greater or lesser extent.

Q Okay. So to the extent that we're looking at comparisons, that's why you've come up with your proxy group; you want to try to get companies that have a lot of similarities with FPL, correct?

A Well, not just similarities, that are comparable in risk. They don't have to be similar in business, they have to, by the guidance given to us by the Supreme Court, be comparable in risk.

Q Back on the stock price, would you -- if I told you FPL's stock price was up from the 2010 rate case decision by more than 15 percent, would that surprise you?

A No.

Q And would you accept that subject to check?
A Well, I can't know that. Like I said earlier, I haven't tracked it specifically since that date, but I can certainly look at it if you would like.
Q Let me ask you if you have any information about how -- what FPL has done with respect to its dividend payments since the last rate case. Do you have any information about how FPL's dividends have done?
A I believe I saw a press release that FPL has increased its dividend every year since 1944, which is an important year to me, so I noted that.
Q Okay. So since the rate case it's your understanding that FPL has continuously increased its dividend?
A Yes, on the cycle that it has established over the decades.
Q And an increased dividend is, you would agree, the sign of a healthy company, the ability to increase dividends?
A It is --
Q A healthy company from a financial standpoint.
A It doesn't tell you whether the company is earning an adequate return or not. There are many other things --
Q I understand.
A -- that go into it.
Q My question is not about the adequate return.

I was asking you if that's a sign of a financially healthy company, the ability to increase dividends.

A Right. And my testimony, sir, is that FPL is a financially healthy company and it's in the customers' interest that it remain so.

Q Is it also your testimony that FPL remained financially healthy after the last rate case decision?

A No, I think the last rate case decision had a deleterious effect on FPL. It caused the bond ratings to deteriorate. It caused concern in the investment community, both as to FPL's prospects and the regulatory environment in Florida.

Q Did it cause FPL to suspend any dividend payments?

A It didn't cause NextEra to suspend any dividend payments.

Q Did it cause NextEra not to increase any dividend payments?

A I don't think so. I would have to refresh my recollection to see exactly when the dividend increase announcement was, whether it was before or after the December, 2010 settlement.

Q What are flotation costs?

A They're the costs that are required to issue common stock to the public to raise more equity funds to invest in utility plant and equipment.

Q And FPL, the regulated utility, does not issue equity, correct, to the public?

A No, it gets its equity from the parent, who was FPL Group, now NextEra, who issues public stock.

Q And is your testimony focusing on the flotation costs associated with FPL's equity, FPL, the regulated utility?

A Yes, its equity is only there by virtue of equity having been issued to the public in past years, for example, in 2002, and the equity units that have continued through 2010.

Q Does FPL have plans, as you know, to issue additional equity?

A Well, I believe there have been some discovery -- it is not appropriate for a public company to disclose its issue plans without disclosing it to the market under reg FD. So it is generally not the case that a utility will -- or a holding company will disclose its plans until they are actually ready to go to the SEC with documentation.

Q So I take it from that that you have no information about any plans for FPL, the regulated entity, to issue additional equity?

A You mean to issue additional equity to get equity from its parent, NextEra?

Q Or otherwise.

A Well, I think the only way it can get equity is from its parent, NextEra.

Q Okay. If that's the only way it can get equity, are you aware of any plans of either FPL, or NextEra, its parent, to obtain additional equity for FPL?

MR. GUYTON: Excuse me, Jon.

MR. MOYLE: Yes?

MR. GUYTON: I apologize for interrupting, but I'm a little bit concerned with what the witness has already told you in terms of financial disclosure and what FPL can and can't disclose publicly.

MR. MOYLE: I appreciate that, Charlie. You know, we're bound by confidentiality agreements in this case and in other context we're provided information that is material, and we can't trade on the information. So if there is such information, I'm not going to ask him what it is, I just want to know if he has any or not. And my inkling is he doesn't have any, but I think he can answer the question as to whether he has any information.

THE WITNESS: I don't have any. I have seen a discovery request that was responded to by others in the company and was deemed to be confidential about the issue of future equity issues.

BY MR. MOYLE:

Q Okay. But as we sit here today you have no firsthand information or even any hearsay information that NextEra is going to issue equity for the purposes of providing equity to FPL, correct?

A That is correct. My testimony is based on that the equity that is already there supporting the current investment had a flotation cost attendant with its arrival.

Q So if that was a past cost that had been incurred, do you know when that cost was incurred? Was it in 2002 when FPL last did an equity issue, if I understood your testimony?

A Well, there were, whatever, $9 million incurred in 2002. But it has been incurred through time, and it has never been recovered. So the best you can do from a regulatory standpoint is have a return on unrecovered flotation costs, much as the company gets a return on other past expenditures like plant and equipment or regulatory assets.

Q And is that what you're seeking with the flotation costs, a return on past expenditures?

A That is correct. It has never been, and in the regulatory framework, will never be recovered, but they represent an amount of funds that investors have put into the company.

Q And what is the time frame for which these costs are being sought, do you know? You said 2002. I mean, have you gone back and identified, you know, the times in which those costs were incurred for which they're now being sought?

MR. GUYTON: Object to the form of the question. We've got at least two there, Jon.

THE WITNESS: The approach to flotation costs that I have proposed is one that was developed by Professor Gene Brigham of the University of Florida, which is based on the percentage of flotation costs typically incurred applied to the dividend yield of the utility.

BY MR. MOYLE:

Q And I'm just trying to understand when these costs were incurred.

A They were incurred through time and the flotation costs have consistently been at least 3 percent or more, as documented in my testimony. A study of a long period of time found 3.6 percent. So they have been at that rate. In fact, if we go back long in the history, the cost of issuing stock was actually higher.

Q Are any of them incurred in 2012?

A No, I believe the last units of issue were 2010.

Q And you're aware that in this case the test year is 2012?

A Yes, I'm aware of that, but in the rate base there are expenditures that were made in the distant past. I mean, I don't think a collection of expenditures that have never been recovered and will never be recovered but are properly incurred is not limited to test year, in my experience.

Q And when FPL, itself, the regulated company, receives equity, that equity all comes through NextEra, is that right?

A At present it does. Previously there was another holding company name, but the same entity. And then in the far distant past FPL was a free-standing company.

Q And how does NextEra infuse equity into FPL, the regulated entity? Do you know the mechanics of that?

A I really don't. Mr. Dewhurst would know. That's his bailiwick.

Q Okay. But you would expect in that they're corporate affiliates that it would not be a process comparable to the issuance of common stock to the public in terms of NextEra either wiring money or doing a transfer of funds into FPL, correct?

A Correct. You're not issuing shares to the public so you don't have the same registration, accounting, legal, SEC fees or printing or the discount that's necessary to get the underwriters to undertake the issue.

Q Okay. And likewise you wouldn't have the cost associated with issuance of the public as compared to NextEra funding equity of FPL, correct?

A That is correct, but NextEra wouldn't have money but for its ability to issue it -- issue securities to the public.

Q And the securities that are issued to the public, they also -- some of that money is used to fund the operations of the unregulated entity, correct?

A Yes.

Q You had talked about the downgrade of bonds following the last FPL rate case, Moody's downgrade, correct?

A Yes, and S&P, as well.

Q Okay. And have you done any analysis or have any study or evidence you can point to that reflects any tangible cost to ratepayers that resulted from the downgrade by Moody's and Standard and Poor?

A No, because I don't think it's necessary. I think, as was discussed very early this morning, risk and return are associated together. And as a company has a higher risk, as indicated by a lower bond rating, it has to pay more for funds. It costs more to borrow, it costs more to attract equity investors and also it loses some of its negotiating power with vendors.

Q Okay. The same question with respect to as a result of the downgrade following the last FPL rate case by Moody's and Standard and Poor. Do you have any analysis, studies, or evidence of any cost realized by shareholders?

A Well, I think there's certainly an opportunity cost, as Mr. Baudino uses the term, experienced by shareholders, because before they -- let's say, as the dawn broke in 2010, they had stock in a -- and bonds in an entity that was rated higher than it was at the end of April, 2010.

Q Okay. And I guess the question -- I understand opportunity costs, but as we sit here today you're not aware of any tangible studies or analysis that following the downgrade that quantified any cost to shareholders, correct?

A No, I am not. But that is not to say there weren't opportunity costs and there weren't other costs associated with financial weakness that ultimately harmed the customers.

Q So I understand your testimony to be advocating for a higher ROE in part to help reduce borrowing costs of the utility; is that part of the reason why you're advocating for an ROE that's higher than some of the other experts?

A Mr. Moyle, I've not advocating. I've done an analysis and those are the results of my analysis. And I believe that customers will benefit because they will save money.

In my direct testimony I have a quote from the Staff report in the last case as to the benefits of FPL having financial strength in terms of the weighted average cost of capital that customers ultimately pay compared to Tampa Electric.

Q So I want to ask you some detailed questions about this. And you say in your rebuttal testimony -- I have it on page ten, line 11 -- about FPL's low cost of debt and the ability to negotiate from a position of financial strength have saved customers money. Is that what you're referring to, or words to that effect?

A Yes, sir, that is one of the examples of benefits.

Q How much money have the customers been able to save?

A I have not tried to quantify that, sir.

Q Why not?

A Well, I think it's a little bit hard to quantify because you would have to estimate what would have happened under the scenario of a weaker FPL. So we don't have direct evidence of that by virtue of all the transactions and all the bond issues that have been made were made by FPL as it stood as a financially strong utility.

We do know the weaker you are, the more you pay. We do know that the embedded cost of debt to the other Florida electrics is higher than it is to FPL. There was some evidence in Mr. Dewhurst's testimony about the rates that FPL was able to get even in the midst of the financial crisis in 2008.

So all of that suggests that there are real intangible benefits, but it would be difficult to add them all up in the face of comparing the real world to a but-for world.

Q So couldn't you do a calculation to ascertain potential costs or savings to ratepayers on a go-forward basis if you had certain inputs?

A Well, if I knew the future, I could do it, Mr. Moyle, but I don't know.

Q Okay. Do you know what the FPL capex spend is projected to be?

MR. GUYTON: May he finish his answer, please?

BY MR. MOYLE:

Q I'm sorry, were you still --

A Yes, sir, I was. We don't know how much more FPL would have to pay if it had a lower bond rating.

Q Are you there?

A We don't know the future of -- I mean, the best we can do is guess. I don't know what that noise is. But the other feature is kind of what I call the value of an insurance policy. You know, if you have fire insurance and you didn't have a fire, you can't say the fire insurance was wasted money, you can only be happy you didn't have a fire.

One of the benefits to customers of financial strength is that if we had another 2008 next month or next year, FPL would be able to access the markets and lesser rated companies couldn't.

And we hope that that doesn't happen, but the insurance is worth something, and FPL's customers have had that insurance all this time. They called on it in 2008, and we don't know when they'll call on it again.

Q Has there been any time since 2008 that has represented a particular turbulent time in the debt markets?

A Not to the extent of 2008. There were some times earlier this year when the European crisis seemed to be spinning out of control that there were extreme movements in lower-rated debt, but not approaching what occurred in September, October and November of 2008.

Q So if I understood your last answer, you're suggesting that part of the reason to have a financially strong company is that it's tantamount to an insurance policy in the event that markets are tight, is that right?

A Right, or the event such as a natural disaster. I understand in Hurricane Andrew FPL spent $350 million in a matter of weeks to restore service. Only a financially strong company could pull that off.

Q Do you know how much FPL currently has in a storm reserve account, or has earmarked for a storm reserve account?

A I know there is a storm reserve and a storm recovery mechanism, but I don't know the amount as I sit here today.

Q Okay. If it were 350 million, give or take, would that suggest that maybe that high ROE was less needed?

A No, because that -- that's a reserve, it's not cash. So FPL has to have the ability and credibility to raise cash and get people to bring services and goods to South Florida on the hope that they will get paid. And only a financially strong entity can command that kind of credibility.

Q Do you know what FPL's current unrestricted cash reserves are?

A No, sir, as I sit here today, I don't know. Mr. Dewhurst, I think, is the person who could respond to that.

Q To the extent that they had a billion dollars in unrestricted cash reserves, those funds could conceivably be used to help with hurricane repair, wouldn't you agree?

A Yes, they would be available if they weren't being used for something else.

Q Okay. So I've kind of gotten away from what I wanted to talk with you about, which was the notion of looking at the cost of debt as it relates to certain bond ratings. But there's a difference in how much -- you had said, risk-reward, the weaker you are, the more you pay. FPL is currently rated as what kind of company? Single-A?

A Single A. Standard and Poor's corporate rating is

A-minus, which is the bottom of the single-A rung.

Q Okay, what's the next lower rating? And let's just stick with Single-A to avoid conclusion.

A Triple-B-plus.

Q Do you know the difference in basis points in terms of debt issued to a single-A company as compared to a triple-B company?

A Well, we don't have indexes that are that precise. The spread between an A-rated and a B-rated -- and that would include all the As and all the Bs, from plus, flat, and minus, is -- let's see -- I have it right in front of me. In July, 2012, the spread was 90-something basis points, the difference between 393 and 485 --

Q All right. For the purposes of --

A -- basis points.

Q -- the discussion, let's just call it 100 basis points; can we agree to that?

A Yes.

Q Okay. And do you know the revenue requirements between, say, a 10 percent ROE and an 11 percent ROE, how much additional revenue requirements that that 100 basis points represents?

A At one point I knew. I wouldn't want to hazard a guess as I sit here today. So if you have the number --

Q I've been told it's 150 to 160.

A That order of magnitude is in the right ballpark with my recollection.

Q All right. So we assume that it's 150 million with respect to the return on equity for 100 basis points. Wouldn't you agree that in order for you to do an analysis as to whether it's better for ratepayers to pay a higher -- 100 basis points in additional ROE or 100 basis points in debt, that you would need to know the amount to be financed, that you would need to know the capex spend?

A Well, that would only be a sliver of the picture. You would have to know -- I mean, we know what the spread is today. The spread today is a lot more than it was when I did my testimony. The market has become a lot more sensitive to risk. So if we say that trend is it going to continue, that the spread between single-A and triple-B is going to increase, we would have to know what that increase would be.

And we would also have to know what the other benefits would be that would be lost if FPL negotiated with its vendors, entered into natural gas hedging arrangements, and so forth, from a triple-B platform as opposed to a single-A platform.

Q Okay. Do you have any information before you about FPL's capex spent, projected capex spent?

A The numbers that I have seen are in Mr. Dewhurst's testimony. I think I mentioned this morning $9 billion over the next several years.

Q Okay. And with respect to 100 basis points on a billion dollars, what number is that?

MR. GUYTON: Could I hear the question again?

BY MR. MOYLE:

Q I asked him how much 100 basis points -- which he's testified the difference between the Bs and the As is 90 basis points, we've agreed it's 100 basis points, one percentage point. I'm asking him to give me the number that that represents on $1 billion.

A Well, that particular part would be 10 million.

Q Ten million?

A But that is only one of the ramifications that FPL would suffer and its customers would pay for from having a lower bond rating.

Q And I just want to walk through this analysis with you as it relates to this. So it's 10 million for every one billion, correct?

A Under the assumptions that we know what the spread is going to be. We don't know what the spread is going to be.

Q Other than what the spread is currently, which you testified to, right?

A That's correct. But we know that the spread increased since I did my direct until now and there's no reason not to believe it might not increase from now into the future.

Q Okay. So if you assume as your testimony that it would be a $10 million finance cost on every billion dollars, and the capex spend for FPL is nine billion, if my math is correct, that would represent additional debt cost of 90 million, right?

A Right, but recall that that 90 million would recur every year until the debt is retired. So if it's 30-year debt, that's 90 million times 30.

Q And from a ratepayer perspective, wouldn't you agree that if a ratepayer was presented with a financial equation that said would you rather pay an extra $90 million per year to represent debt service on a $9 billion capital expend or would you rather pay an extra $150 million per year, which represents an additional percent on ROE, that the better economic decision is to opt to pay the 90 million as compared to the 150, because it saves you 60 million?

A If those were the only two numbers the customers knew, they would be making is a shortsighted decision because they properly should consider that the savings might be significantly more if, in fact, the disparity increased. Plus there may come a time when triple-B utilities cannot issue bonds and single-A utilities can.

As FPL goes through time and hedges and responds to storms and does other things on the customer's behalf, it will do so more cost effectively as an A utility than a triple-B utility.

Q And you would agree that even to the extent that the spread between single-A and triple-B were to increase, you said it's 90 basis points, but even if it went up to, you know, 120 to 130 basis points, that there would still be head room in that the ratepayers would be better off by paying the higher debt cost than by paying the higher return on equity, correct, in my hypothetical?

MR. GUYTON: I want to object to the form of the question because I don't think the witness said the spread between A and triple-B was 90 basis points, he said between all As and all Bs, which I interpret to mean something else.

BY MR. MOYLE:

Q Okay, why don't you -- if you can answer my question, which is essentially to acknowledge that your previous testimony that I'll ask you to clarify the spread between all As and all Bs is 90 basis points, that there's still head room between 90 basis points and 160 million on the return on equity side of the ledger, is that right?

A No, I wouldn't say that's head room, I would say that's the arithmetic difference. But that would not consider many of the relevant and important distinctions between an A and triple-B that would be important to customers in making their vote if in your hypothetical they had the ability to make such a vote.

Q And to the point -- I don't want to, you know, be sloppy and not understand your testimony, but would I be correct that the spread between a single-A and a triple-B would be less than 90 basis points?

A Well, see, like during October of 2008 the spread was 380 basis points. The --

Q Right, and that's the point in time that the markets were frozen. We've talked about that. But I'm just trying to understand, because you had said the average between A and B was 90 basis points. Is that right?

MR. GUYTON: Jon, would you please quit interrupting the witness and allow him to finish his answer? It's becoming particularly difficult because your microphone picks up your voice and cuts us out here, and you're cutting off the witness' answer fairly consistently.

MR. MOYLE: Well, I'm sorry. You know, it makes it harder when we're on the phone. We can't see each other. Do you have any -- if you need to add something, please add something. I'm sorry if I -- I'm trying to move this along and stick to my hour, but if you feel the need to add, please add.

THE WITNESS: Mr. Moyle, I think it is important to recognize that at times of financial crisis the spread balloons. Plus, in our experience, a number of our clients in 2008 were not able to even access the market. Triple-B clients, huge reputable utility companies like AEP and PG&E simply could not open the door, and FPL could.

BY MR. MOYLE:

Q How long was that door closed?

A It was closed for six to eight weeks, completely closed. But even once it opened the disparity of actual cost was very significant. And what happened is companies -- and another one is UIL, United Illuminating -- what they did is issue five-year paper or ten-year paper because the cost of 30-year was just prohibitive.

Q Okay. So back to the question, could you please clarify your previous testimony where you said that the spread between A paper and B paper was 90 basis points.

A Yes. That's the average as reported by Moody's for the July period, and it includes securities more than 20 years in maturity and it includes As of all notches, as well as Bs of all notches.

Q Okay. So would it be your testimony, or maybe you don't know, but that given that single-A and triple-B are right next to each other on the notches, that the spread in the marketplace between those two types of paper would be -- would likely be less than 90 basis points?

A They could be, but another factor is a company loses its credit rating, it generally puts a cloud on that company, and so investors are leery because it may be that it's on a downward slide.

Our experience -- and I've seen studies of this, but I can't recall the exact authors -- that there is a tendency for bond down-ratings to cascade. So that if you are down-rated, let's say, from A-minus to triple-B-plus, there's a concern that the next thing that may happen is you're going to be triple-B or triple-B-minus.

Q And I don't really want to get into a lot of speculation about different things can happen. I appreciate that. I'm just trying to get information with respect to your expertise as it relates to the delta in financing costs for a company that's single-A rated as compared to a company that's triple-B rated.

And my question was, do you have information as to whether that delta is likely to be more the same or smaller than the delta that you've testified to, which is all of the As versus all of the Bs.

A There is no empirical information that slices things that finely, so I couldn't speak to that with evidence-based experience.

Q Okay. So you just don't know?

A I can't base it on numbers that are publicly available.

Q Do you have a view of it, whether it's based on numbers or not?

A Well, I think it would depend on the facts and circumstances of the particular issuer. Because I do believe, as I testified earlier, that a downgrade is a significant event in the life of a company and it changes the way investors look at it.

Q Has FPL shared with you their plans to go into the debt markets, or do you know of FPL's plans to go into the debt markets?

A They have not shared and I have not asked what their plans were. I can't imagine they won't go into debt markets because of the level of capital spending, but I have no knowledge of the specific plan.

Q Now, do you have any information or were you aware of anything, that during the last rate case that FPL had gone out into the debt market and had, in effect, presold certain debt?

A I'm trying to remember Mr. Pimentel's testimony in that regard. I think one of the issues there was that FPL had a major line of credit that was about to expire and they were trying to position themselves so that they wouldn't run out the clock on that line of credit.

So I remember Mr. Pimentel talking about that problem and the contingency planning the company has made, but that's about as far as my memory goes.

Q Are you aware of any similar plans as the facts present themselves in this case?

A I'm not aware of them, but Mr. Dewhurst is the Chief Financial Officer and would be in a position to speak to it.

Q Okay. You were asked some questions about the clauses that Florida has, and I was curious as to whether you had any specific information about any other states and the clauses that the other states have, as compared to the state of Florida.

A Well, as I mentioned, I have worked with many of these companies. I've worked with companies all over the country, and I'm aware of the clauses they have. In the context of discovery and other cases, we have specifically looked at the 10-Ks of various companies. And, in fact, I think I did this in the last rate case for FPL to see what kind of adjustments they have.

And then there is also a report that RRA issued in March that summarized the adjustment mechanisms around the country.

Q And do you have a copy of that report in front of you?

A I could get it in front of me. I don't think it has been provided in discovery.

MR. MOYLE: Charlie, any objection if he gets that?

MR. GUYTON: Only if -- I'm getting concerned about time, since he hasn't relied upon it.

MR. MOYLE: What?

THE WITNESS: This report came out after I did my direct, and I didn't depend on it for anything in my rebuttal.

BY MR. MOYLE:

Q Do you have a copy that you can put your hands on today?

A I have a copy in my computer, if I can find it.

Q The question I wanted to ask you was if you are aware of any state that has more cost recovery clauses than the state of Florida. If you can answer that, you know, fine. If you have to look at the report --

A California. We've done a number of cases in California, we have one coming up, and I would say California has more -- it has full revenue decoupling, it has the same fuel and purchase power, it has environmental, it has renewable, it has everything Florida has and more.

Q Okay. Any other states besides California?

A I would say Virginia.

Q Any others?

A Those are the two that are foremost in my mind.

Q And you would agree that states that have clauses by which a lot of revenue flows through represent less risk, all other things being equal to an investor, is that right?

A Yes, they do benefit. Let me add North and South Carolina, too, upon reflection.

MR. MOYLE: Okay, could I ask that that report, that RAI (sic.) report be provided as a late filed exhibit?

MR. GUYTON: Jon, I'm going to object to it because the witness hasn't relied on it for purposes of his testimony, either his direct or his rebuttal.

MR. MOYLE: Is that a true statement?

MR. GUYTON: He just testified to that effect.

MR. MOYLE: Well, I asked him about what other states and he put them out there. I didn't know if he relied on the report or whether he had the information from another source.

THE WITNESS: My response was based on my work in those states.

BY MR. MOYLE:

Q Okay. Have you reviewed this RAI report?

A I reviewed it very quickly. It was brought to my attention by one of our clients, and he sent it to me, but I haven't studied it.

Q But you reviewed it?

A Cursory, yes.

MR. MOYLE: Charlie, given the fact that he's reviewed it, I'd like to get a copy of it.

MR. GUYTON: I'll take it to my client, but the objection remains.

MR. MOYLE: All right. Well --

MR. GUYTON: Have you requested it in any discovery other than the deposition?

MR. MOYLE: I'm not sure, Charlie. Typically in depositions people are asked to bring work papers. He has it in his computer. He's an expert. He's the one that brought it up.

MR. GUYTON: And he told you that he didn't rely on it in his testimony. If it were something he had relied upon, I'd suggest that he needed to provide it but --

BY MR. MOYLE:

Q Okay, so just so the record is clear, you didn't rely on this RAI report in any way, shape or form to either, you know, confirm your sense -- I mean, it seems to me, logically, if you've done work in certain states and you can say these states are -- well, never mind. Let's move on.

Let me refer you to your Exhibit WEA-15, page one of one.

A All right, I'm there.

Q Okay, you have Gulf Power Company as a proxy company, is that right?

A Yes.

Q And why did you include them?

A Because they are a subsidiary of Southern Company and Southern Company is one of the comparable utilities.

Q Okay, and I guess it's true that Gulf's long-term debt is 51 percent?

A Yes, that's what they reported in their 10-K.

Q And you would agree that companies that have higher debt, all other things being equal, represent more risk to investors, correct?

A That's correct, assuming the business risk and the rest of the balance sheet, it would denote more financial risk and, therefore, all else being equal, more investment risk.

Q Okay. And then FPL's long-term debt is what percentage?

A Well, 59.6. Let's see, it's not on this exhibit.

Q That's their equity or their debt?

A Oh, excuse me, that's their equity. The debt would be 40 percent.

Q Okay. So just based on the capital structures of Gulf and Florida Power and Light you would agree that Gulf represents more risk to the investment community than Florida Power and Light, all things -- all other things being equal, correct?

A Well, if you just look at the debt, but all things aren't equal.

Q I understand.

A As I answered earlier in response to the Staff, there are many elements of risk that FPL has that Gulf does not share.

Q And for the purposes of the question I'm just asking you to focus on debt and equity.

A But you asked me to assume all else being equal, and I can't do that. That's contrary to fact.

Q You can't assume that for purposes of having a conversation on debt equity and return on equity?

A I can agree in the abstract, as I did, that all else being equal, more debt would indicate more risk. But if you particularize it to Gulf Power versus FPL, I can't accept that Gulf is equal to FPL in business risk.

Q Okay. Well, if you assume, just for the purposes of the analysis related to capital structure, that FPL poses less risk than Gulf, wouldn't the logic flow that FPL should receive a lower return on equity than Gulf? Again, just focusing on the capital structure components.

A Well, I can't focus just on the capital structure.

And also there's the issue of the ROE adder, which I think is appropriate regulatory recognition. And I think that should be considered in the ROE.

Now, if you're asking me abstractly should higher risk companies get higher ROEs, yes. But I can't agree with you when we get to specifics about Gulf and its 10.25 when I think it's appropriate for FPL to get 10.5.

Q Have you done any analysis as to the business risks of Gulf vis-a-vis the business risks of Florida Power and Light?

A No, I have not. I have done FERC cases for the Southern Company, but for the purposes of this case I didn't do such an analysis.

Q Okay. So just so the record is clear, I guess with respect to -- and I'm asking you to make an assumption, and I understand, you know, you're hesitant to make the assumption. But for purposes of the question, given that Florida Power and Light has more equity, less debt than Gulf, all other things being equal, according to economic theory, investors would require a lower return on equity as it relates to Florida Power and Light than Gulf Power, correct?

MR. GUYTON: Jon, objection, asked and answered, and it assumes a fact that has not been established and this witness has consistently said is incorrect.

MR. MOYLE: Well, I think I've asked it. I'm not sure I got an answer; that's why I was trying to get the answer.

MR. GUYTON: I think you've gotten three answers, you just don't like any of them.

BY MR. MOYLE:

Q Can you answer that question yes or no?

A No, I can't, because I can't agree with the presumption that FPL has the same business risk as Gulf. And I want to also say that I am not saying that the allowed return that Gulf had was the right allowed return. It is what was found.

Q But as we sit here today, you don't know the business risk of Gulf, correct? I mean, you haven't done any analysis, you haven't studied it, so you just don't know one way or the other?

A I think my answer, Mr. Moyle, was I haven't done a specific side-by-side comparison of FPL and Gulf. I am generally aware of Gulf. I looked at the Southern Company's bond ratings, its Value Line, safety and beta and financial strength and Southern Company is comparable to a NextEra.

But as I described -- and this was discussed extensively -- FPL has unique risk factors that are different because of its location, fuel mix, exposure to storm, lack of geographical and regulatory diversification vis-a-vis Gulf.

Q You made a comment earlier in your testimony about risk and a utility that has regulations in a number of states as compared to a utility that's only regulated by one state. And I thought you suggested that it represented less risk if a utility was regulated by a number of jurisdictions. Is that right?

A Yes, that -- well, it doesn't matter what Bill Avera thinks, that is what the rating agencies have said, that regulatory diversification is a good thing and reduces risk.

Q And you would suggest that's a result of diversification?

A That is correct, that if a company gets a bad outcome in one state, it can hope for a better result in other states. Whereas, FPL, all of its regulatory eggs are in the FPSC basket except that little bit that's at FERC.

Q Do you think that same analysis can apply with respect to geographic exposure to hurricanes? And I will give you two examples. You're familiar with FPL because you've testified about their service area.

Tampa Electric Company is located essentially in the Tampa Bay area. So they do not have as much exposure, but in effect all of their eggs are in one basket.

My question would be, do you think the same type of analysis with respect to diversity of geographic risk carries through as compared to the analysis you just provided about diversity of regulatory risk?

A Well, I think geographic risk does have some effect on your exposure to storm. I think I may have talked about that with the Staff. With respect to Gulf, it is part of a holding company that serves Mississippi, Alabama, and Georgia, as well as Florida. And it's seldom the case where you have a devastating hurricane strike Pensacola and also strike Birmingham, Jackson, or Atlanta.

Q But you would agree if a hurricane struck Lake City -- do you know where Lake City is in Florida?

A Yes, sir.

Q If it struck Lake City, which FPL has service territory in Lake City, and didn't strike any of south Florida or any other place, because of FPL's diverse geographic characteristics, that that would serve to mitigate that risk, right?

A Yes, if you had a hurricane with such a small footprint. That sounds more like a tornado than a hurricane.

Q I guess I could ask the same question with respect to hitting Manatee County, which FPL also serves.

A Yes. Are you asking that question?

Q Yes, sir.

A And the answer would be the same. It is possible to have a limited geographic hurricane strike for FPL. Unfortunately, the big ones have been pretty much the whole service area.

Q Sure. I want to ask you some questions about your rebuttal testimony.

A Yes, sir.

Q On page five, line 18, you make a statement about FPL's financial strength and opposing witnesses offering speculation and conjectures as to how investors and bond rating entities might react. What was the purpose of that statement?

A Well, it was to say that the opposing witnesses -- and there are many that talk about the equity ratio and bond ratings -- suggest that there could be a significant change in the bond, or in the allowed return, that had the opportunity, more importantly, the opportunity to earn from 11 percent down to 9 or 8.5, and a dramatic change in the capital structure, and that wouldn't trigger a weakness or a change in bond rating.

And they generally are either silent on that or, like Mr. O'Donnell and Mr. Lawton, purport to look at some of the ratios and say they would be okay because the rating agencies will look at that ratio and be very satisfied and let FPL slide. And that is totally inconsistent with the recent history of FPL.

When the rate order came out in 2010, there was an instant -- more or less instantaneous investor response. And when the stipulation was reached in December of 2010, again, there was almost instantaneous investor response. But the rating agencies did not raise the rating. It's stable, as it is now, earning 11 percent with a 59.6 percent capital structure. That's a fact.

And I think to suggest that you could dramatically change the world and the rating agencies would sleep is nonsense.

Q But, I mean, you've made a comment earlier about looking into the future. I mean, you would agree that nobody knows exactly what a rating agency is going to do and nobody has the ability to project into the future as to cause and result, correct?

A Right. I do not claim that ability nor do I attribute it to Mr. Lawton, Mr. O'Donnell, Mr. Baudino or Dr. Woolridge.

Q To the extent that you're making a statement or an opinion as to how bond rating agencies or investors might react, just as you suggest that they are speculating and engaging in conjecture, that would also be what you are doing as you're looking beyond the horizon, correct?

A No, it's not. We have an experiment. We have the 2010 experiment. And we can observe what rating agencies actually did, first when you had a disappointed rate order, and, second, when you had a rate order that gave them some comfort. And we can see what the rating agencies actually did. I think that history informs a judgment about what will happen.

Can I predict with 100 percent accuracy? No. But I think a judgment informed by history has more soundness and more credibility than a judgment ignoring history.

Q But you would agree that any decision by investors or bond rating agencies would take into effect multiple factors beyond a return on equity, correct?

A Yes, sir, they would look at the whole scene. But as I talked about in my rebuttal, the return on equity is a big number in terms of visibility, discreetness -- that's why RRA, as we talked about earlier, does its surveys of the ROE. On every Value Line page for a utility it has the ROE. So investors really, really care about ROE.

Q I'm going to try to kind of run through some things quickly, because I said an hour, and I'm coming up on that hour, maybe past it. So if you have a need to explain, please do, but if not, we can move it along.

On page 13, line 21 --

A Yes, sir.

Q -- you are talking about the low rates of Florida Power and Light. And Staff touched on this with you. But wouldn't be agree that a main factor in the low rates FPL customers currently pay is that FPL has considerable generating assets that are fueled by natural gas and natural gas prices are currently low?

A That is a benefit, but I would say it didn't just happen, it was a decision by FPL to build the natural gas facilities and to run them well.

Q Okay. And is your analysis -- would it be symmetrical in that if FPL had made this decision, and rather than being at $2.50 or $3, now natural gas was $12, would you believe that that might warrant a further deduct in ROE?

MR. GUYTON: Object to the form of the question. I don't think the witness has assumed the premise of your question that the low rates are a function solely of gas prices. I think he's suggested to you it's a function of having efficient plants in place, which can take advantage of lower high gas prices. So I think the premise of your question is a misstatement.

THE WITNESS: Shall I answer?

MR. GUYTON: I don't know. Jon, do you want to restate, or do you want him to answer that one?

MR. MOYLE: If he understands it, to answer, I think that would move us along.

THE WITNESS: Well, I think the way regulation workd is when a Commission thinks a utility has done something imprudent or improper, what it does is disallow some of those expenses. The effect of that is to lower ROE.

But I believe that it is appropriate regulatory policy to test what the company has done, and if the company is found to have done something the Commission thinks was imprudent or unnecessary, then the remedy to protect the customers is to disallow that particular cost.

Unfortunately, if there is no cost because the company has done a good thing, there is no way to reflect that cost, the absence of that cost, exempt through the ROE. That's why I think the ROE adder -- someone earlier said it's a non-cost adder. I don't think that's true. It reflects costs that aren't there.

BY MR. MOYLE:

Q So if it's a good thing -- if it's a good thing that a company has done, in your view, it would be appropriate for an ROE adder?

A That's correct, because that's the way it works in the free enterprise system. If Apple has a great product that everybody wants, it makes lots of money. If Blackberry has a bad product that nobody wants, it loses money.

Q All right. But with respect to it's a good thing, if they did a bad thing in terms of business judgment, would you think that that would likewise warrant an ROE reduction?

A Effectively --

Q Is it a -- is it a concept, in your expert opinion, that cuts both ways, is my question.

A It does cut both ways, but it's implemented differently on the down side --

Q Because it has to be prudent or imprudent?

A Right. The specific expenditure is examined and it is disallowed. That's what happens. This is what is being recommended in this case for lots of different expenses, and that's the way the regulatory bargain works on the down side. And I'm just saying you've got to have symmetric treatment. So if there's enough cost that isn't there because of effective management, that ought to be reflected in the ROE, too. But the only way to reflect it is to increase the ROE.

Q This shouldn't take long. Page 15, you're sharing some comments about the Intervenor's position on capital, and you use the term schizophrenic and delusional. I assume that's hyperbole, isn't it? You don't really think the Intervenor's witness's view is delusional or schizophrenic, correct?

A No, no, it is hyperbole, but I think it should get attention, because they are saying let's pick a comparable group, let's adjust the ROE downward, because FPL is such a low risk utility. And then they turn around and make recommendations that would take away that low risk.

Q Okay. Moving along quickly, page 17, you talk on line 8 about your contact with rating agency personnel, and you say they jealously guarded their ability to depart from guidelines to reflect the risk of individual issuers.

A Remind me where we are on this.

Q I'm sorry, page 17 of your rebuttal, line 8.

A Okay, got it. Yes.

Q When was your last contact with rating agency personnel?

A Probably three years ago I was teaching a class for the CFA Society and rating agency personnel were present.

Q You would agree that their criteria could have changed in that three-year time frame, correct?

A Well, as a matter of fact, I don't think the criteria -- Standard and Poor last updated their criteria in 2009. But I think, as to this position, I believe I quote from the rating agency's actual document that the metrics are only a guideline.

Q Do you know, does Fitch publish its criteria?

A I don't think Fitch is as formal as -- S&P is the most transparent, then Moody's, then Fitch.

Q Okay. But your point here is there's not an equation that will necessarily guide rating decisions, that they have the ability to depart from their guidelines and make individual judgments as the facts and case warrant, correct?

A Exactly. And they say that on the face of their reports, when they talk about their judgments and criteria.

Q Okay. On page 18, line 13, you say the fact that FPL's equity ratio may be higher than industry averages. Do you know where FPL ranks with respect to its equity ratio vis-a-vis investor-owned utilities in the country?

A Well, I have, in my direct, information as to the capital structures, both -- we were talking about WEA-15, and page one, and 16, and then on 17, in terms of market value. Which, you know, several of the witnesses in their depositions have said you ought to look at holding companies and not operating companies.

If you look at holding companies, you should look at market value capital structures. And in that regard, NextEra is pretty much in the hunt.

Q So I think Staff had asked you to identify there were two other companies that had higher equity ratios than FP&L, is that right?

A No, that's not my memory. I think Staff claimed that on some document there were three utilities that had higher bond ratings, and I did not agree with that. That just didn't seem to match my recollection. But it was not for equity ratios, it was bond ratings.

Q I apologize for that, I got it confused. I guess the question would be, with respect to the equity ratios and the amount of equity in a utility company, can you tell me whether FPL is in the top 10 percent of companies that have thick equity, the top 25 percent, the top 50 percent? Can you quantify that?

A I haven't looked in terms of the whole industry. In terms -- what I said in my direct is it's higher than the average, but it's not the highest. But I haven't tried to resolve it down to their percentile ranking.

Q So with respect to being higher than the average, would average be 50 percent?

A Well, in terms of fiscal year end 2010, the average operating company was 53.8 percent common equity compared to FPL's 59.6.

MR. MOYLE: Okay, thank you for your time. I don't have any additional questions and I'll follow up with your counsel on the document that we've talked about. Appreciate it.

MR. GUYTON: We've been going a little over an hour, almost an hour-and-a-half. May we take a short comfort break?

(Brief recess)

CROSS EXAMINATION

BY MR. SUNDBACK:

Q Good afternoon. We have some questions for the witness on both his direct and rebuttal testimony. Sir, in your testimony just generally you review various sources of financial data, correct?

A Yes.

Q And you review data concerning several different enterprises, in, for instance, your proxy groups, right?

A Yes.

Q Could you list for us the trade press you review on a regular basis to stay current with the utility industry.

A Well, I generally watch CNBC and Bloomberg. I generally read the Wall Street Journal and New York Times. I sometimes look at Electric Week. I sometimes look at Public Utility Fortnightly. I also follow the Financial Analysts Journal and various academic journals like Financial Management.

Q And you believe that those are useful sources of information?

A Yes.

Q Okay. When you were creating your proxy group and preparing your evidence in this proceeding did you review the public disclosure documents of the entities that are listed in your proxy groups?

A Not initially. And I left out the biggie, which is Value Line. We based our selection of the proxy group, as explained in the testimony, beginning with the Value Line utility universe, and then eliminated those who did not fit the risk criteria or the dividend criteria or the absence of merger criteria.

Q That wasn't my question, sir. My question was, when you created your proxy group, did you review the public disclosure documents issued by those entities in the proxy group.

A And I was answering your question, Mr. Sundback. Value Line bases their reports and evaluations on the SEC filings. So in finding the proxy group, I did not look at the SEC filings. Then in terms of the capital structure information and other information, we did access the 10-Ks but that was after the companies were deemed to have been comparable.

Q But you did indeed look at public disclosure documents and 10-Ks of entities that are reflected in your proxy groups?

A That is correct, and I think that's indicated in my footnotes.

Q Okay. And, for instance, did you review public disclosure statements or 10-Ks from FPL -- I'm sorry -- from NextEra Energy?

A Yes.

Q Okay. And you also relied on corporate credit ratings with regard to those entities, as well, did you not?

A Yes.

Q Did you review the ratings analyses provided by S&P for each of those entities?

A I just looked at the published rating reports because those are the reports that investors would reference, as well. I did not access any non-public data.

Q Did you systematically review the rating agencies' material regarding FPL or NextEra from a particular date certain through the date of your rebuttal testimony?

A Well, I am generally familiar, having done a number of cases for FPL. I generally have an inventory of past bond rating reports. And when we started on this case, we got updates, and I think we continued to get updates until we finished the rebuttal testimony, and I'm unaware of anything -- any breaking news that we missed.

Q So your answer, if I understand it, is that, yes, you attempted to systematically review rating agency materials regarding Next Energy (sic.) and FPL, certainly from the outset of your participation in this case, is that fair?

A Well, I don't think that's a correct characterization. What I said was that we have an inventory of rating documents and then when we started this case we made sure our inventory was up-to-date and complete and then we got those documents that were issued. But we only referenced the publicly available rating agency reports.

Q Fair enough. And how did you determine which FPL or NextEra public disclosure documents you were going to review for purposes of preparing your testimony?

A Well, we looked at the Form 10-K and I believe we looked at some 10-Qs, as well, just for the last several years. Again, as with the rating agency reports, because of our previous work, we had an inventory of 10-Ks and the annual reports to shareholders in our office.

Q In the last FPL rate case you had testified regarding the level of institutional investment in FPL. Do you recall that?

A Yes.

Q Okay. Is it your understanding that the level of institutional investment in FPL today is approximately the same as was the case when you last testified?

A I really haven't looked to see. What I do know is that institutional ownership, generally, of utilities, is going up, because individuals are less active in equities these days.

Q Do you have an opinion as to whether institutional investors are more sophisticated or thorough than individuals who might be investors?

A I don't think I could make that generalization. Institutional investors, obviously, have professionals making investment decisions, but individuals have access to professionals, such as Value Line, and the rating agencies. So I think both institutional investors and individual investors rely on professional security analysts to formulate their views of the value of securities.

Q FPL, NextEra Energy, from time to time, also issues public statements in addition to 10-Ks and 10-Qs, do they not?

A That's right, if they are deemed to be relevant to investors, there would be an AK. And then if there are security issues, there might be an S-1s or S-2s or S-14s.

Q There are also press releases and presentations by FPL management to various groups that are publicly available, are there not?

A That is correct, but only if they're deemed to be material are they filed with the SEC. And I was speaking of the SEC filings.

Q Right. But some of these other materials are also available, for instance, on the company's Web site, isn't that correct?

A Some are. I think it depends on the material. I believe, as I understand, as a financial analyst, the obligation of the utility is if there's a material disclosure, it has to be made through an SEC filing.

Q Fair enough. Aside from the witnesses in this proceeding who testify explicitly about the level of ROE that they're recommending be established for FPL, did you review the testimony of any other witnesses?

A Well, there are some witnesses, like Mr. O'Donnell and Mr. Chriss, who didn't present full ROE presentations but they touch on financial integrity and capital structure. And Mr. -- let's see, I'm trying to remember -- there's a Supuro or Supreto (phonetic), and I think Mr. Henderson may have had some testimony that I looked at, or at least some of his discovery. And, of course, my friend Dan Lawton.

Q Okay. And aside from your testimony, what other FPL witness's testimony did you review?

A I reviewed Mr. Dewhurst's testimony, Mr. Barrett's testimony, and possibly some others, but as I sit here I can't rattle off the names.

Q All right, just to pick up sort of with some of the threads that have already been raised in your discussions today, do you recall that you had a discussion with counsel for FIPUG concerning other Florida utilities' costs of debt?

A Yes.

Q You haven't done an analysis that compares the weighted duration or maturities of debt issuances among the various Florida utilities, have you?

A No, I was relying on information in the Staff report in the last case as to the cost of debt.

Q And you haven't done an analysis of the dates and market conditions in effect when those various bond issuances took place, or among the various Florida utilities, have you? Hello?
A I'm here.
Q I'm sorry, did you answer the last question?
A Yes. I think I said I did not.
Q Thank you. I'm sorry, we didn't hear that at this end. We apologize. Okay, could you turn your attention to what's been designated as Exhibit WEA-4.
A Yes.
Q Okay. And in that exhibit you have what you deem to be a utility proxy group.
A Yes.
Q Okay. Each of the entities that's listed there is a holding company that owns a number of different subsidiaries, correct?
A That may not be true of Wisconsin Energy. I'd have to check. But the others are.
Q Okay.
A That are entities that issue common stock.
Q The entities that appear on the list on that page issue common stock?
A That is correct. They are followed by Value Line.
Q But not all of the subsidiaries of each of these

entities operates an electric utility, is that correct?

A That is correct.

Q Okay. If one compares FPL to these entities, you're comparing a single investor-owned utility to a holding company in that case, correct?

A That is correct. And that's what we must do, because holding companies are where stock is issued and you can do a DCF or a CAPM.

Q Suppose you had a publicly traded holding company comprised solely of an electric utility, and that utility had average risk, as determined by rating agencies. Do you understand the hypothetical so far?

A Yes.

Q Okay, let's say the utility earned $100 million in year one. In year two, it bought another entity, and that entity was engaged in higher risk activities, let's say it's energy trading. And let's say that that higher risk entity earned $10 million in year two.

Would the purchase of the higher risk entity raise the risk of the publicly traded holding company?

A Under your hypothetical, it could. I think one of the questions would be is there interaction between the risk of the trading company and the utility. In some cases there is synergy, which allows the risk to go down less than -- the sum of the parts has less risk than the individual entities.

Q And one of the synergies might be, for instance, the ability to use tax credits that are generated on one side of the house, if you will, through income generated on the other side of the house. Is that a potential?

A Well, that is a potential. I'm not sure if it would be a risk issue or a return issue, to have those tax opportunities.

Q All right. But that might be a benefit that's associated with the ownership of those two divergent entities?

A It might be a benefit under certain circumstances.

Q And to the extent that the trading entity in year three had earnings of $100 million, that might ultimately further increase the risk profile of the holding company, is that correct?

A Well, it depends how you're measuring risk. In the CAPM theory, risk is a function of assets, the market value of assets. So even if the unregulated company, trading company, had much higher earnings, if its assets were -- had not changed relative to the utility, then the risk of the entity, the beta of the entity wouldn't have changed. It's how you measure risk, whether it's based on earnings or assets. And at least as to current financial theory, it's based on market value of assets.

Q Okay. Now, looking back at what's been listed as

WEA-4, you have listed the various enterprises. And would we take from your prior testimony today the notion that you have a fair degree of familiarity with these enterprises?

A Many of them I've worked for. Some of them I have not.

Q With regard to, for instance, the second one, Consolidated Edison, how many operating utilities does Con Ed own?

A Two.

Q Okay. And those are both in New York state, are they not?

A Yes.

Q What are the cost trackers and recovery clauses that New York affords utilities?

A Well, Consolidated Edison is a distribution only. Orange and Rockland is, I believe, an integrated utility. Orange and Rockland does not have a fuel adjustment clause, but I believe something like 97 percent of Orange Rockland's fuel is under long-term contract.

Q So you're not able to identify, from your own knowledge, trackers or recovery clauses that would be in effect, for instance, for Orange and Rockland?

A No, I know that, on one hand, Orange and Rockland has less robust recovery clauses. On the other, it doesn't need them, because its fuel costs do not vary because of the nature of its generation mix and contractual matrix.

Q Well, that's one element of cost, isn't it? There are other elements of cost that may be subject to trackers and recovery clauses; for instance, those in Florida?

A Yes.

Q Okay. And as to those, can you see tell us what trackers or cost recovery clauses exist in New York for someone like Orange and Rockland?

A Other than the fuel, my understanding is that there are environmental and renewable trackers and there are qualifying facility trackers in New York. The specifics, I would have to review the 10-Ks to know.

Q Okay, let's look at OG&E, or OGE, also in the proxy group.

A Yes.

Q How much of OGE's revenues are derived from gas service?

A My colleague has done gas cases for OGE. A significant amount. Again, I would have to review the Value Lines to know the exact amount.

Q Does an OGE affiliate also engage in unregulated marketing activities?

A Yes.

Q And would your answer with regard to proportion of revenues derived from that activity be the same for your answer with regard to OGE's gas revenues?

A Well, typically a trading organization has very large revenues but not very large asset investment.

Q And so your answer to my question is?

A I don't know the revenues, but I can't say from that you could infer the relative contribution to OGE's risk.

Q Okay. How about DTE, also listed -- well, actually, I think we now have to go to your Exhibit WEA-19, and there you have DTE listed. That's on line 11, for instance, of page one.

A Yes.

Q Okay. You're aware DTE engages both in electric and gas marketing, as well as regulated activities, is that correct?

A Let's make sure we're on the same page, so to speak. What exhibit are we speaking of?

Q WEA-19, page one.

A Okay, so we have to go to the rebuttal, right?

Q Yeah. Actually, let's look at page --

A I mean, these are not my proxy groups. In this case, 19 are the -- is Mr. -- Dr. Woolridge's proxy group.

Q Yes, I understand.

A And DTE does do gas.

Q All right. And could you tell us what proportion of its revenues are derived from gas service?

A Well, I believe Dr. Woolridge's criteria for his proxy group was 70 percent electric, so it's something less than 30 percent. I think the gas operations are fairly significant, but no more than 30 percent, based on his criteria.

Q Okay. Let's look at your rebuttal testimony, page 25, if we could. Down at the bottom of the page, lines 21 through 23, you have a sentence asserting that regulators only establish an allowed return. Do you see that?

A Yes.

Q The returns that investors actually earned are different or may diverge from the allowed return, right?

A Yes.

Q And so they could earn more or less than the allowed return?

A That is correct. And we're speaking of investors in the marketplace, buyers and holders of common stock?

Q Well, how did you intend it in this instance? Did you mean investors in publicly traded shares or investors directly in operating utilities?

A I was speaking here of investors in publicly traded stocks because we were talking about investors' opportunity costs in the question.

Q It's also true that in a number of states utilities can earn more or less -- actual operating utilities

can earn more or less than their authorized returns, right?
A Yes.
Q We've already discussed today how that may have occurred in FPL's case, right?
A Yes. I didn't agree that it occurred, but it is possible that it may have occurred before the accounting caught up with the operating earnings.
Q And the ability to earn a return above the authorized level might impact an investor's perceptions regarding the desirability of an investment, is that correct?
A That is correct. That's why a lot of these adjustment mechanisms from an investor's perspective are a two-edged sword, because they assure that you have an opportunity to earn what you spend, at most, but you can never earn more.
Q And to the extent that you have base rate recovery, that's not the case, right?
A That is right, under the doctrine of retroactive -- prohibition of retroactive ratemaking, it is possible to earn more than the allowed return.
Q Let's look at your rebuttal, page 17, lines 4 through 6, please. Have you found that passage?
A I found page 17, lines 4 through 6. I'm here.
Q Yes, sir. You weren't implying by that passage that FPL had to maintain precisely a 59 percent

investor-supplied equity ratio in order to maintain its current credit rating, correct?

A Well, I think the credit rating goes with the equity ratio. But I think the equity ratio is first a strategic decision by the utility, and, secondly, it's a somewhat dynamic number as the utility issues securities and retains earnings. So the equity ratio moves, but it has a target and a year-end value.

Q It's not your contention that, for instance, if FPL's equity ratio for investor-supplied funds was 58 percent, that that alone would likely trigger a downgrade in rating, is it?

A No, I can't say because I think it depends on the other facts and circumstances that the rating agencies would assess. I think if you go from 58 to 50, the likelihood of downgrade increases materially.

Q Before filing your testimony did you study how much or form an opinion by how much FPL could decree its equity ratio and still maintain current credit ratings?

A No, I did not because its current equity ratio goes with its current credit ratings. And so I didn't see any need -- and it seems kind of spurious to me to assume that a company can keep slicing its equity ratio and expect no response from the rating agencies, or that investors in general will ignore the increased financial risk.

Q Given your prior answer, would we also fairly conclude that you did not study the impact of NextEra Energy, Inc. and NextEra Energy Resources' debt levels on FPL's credit ratings?

A No, I didn't study dynamically what they would do. I used NextEra's risk measures in order to select my proxy group where there were no comparable risk measures for FPL.

Q Okay. So you haven't formed an opinion as to how much NextEra Energy Resources' risk profile has affected the cost of equity, for instance, for FPL?

A No. I focused -- the analysis that I did for the cost of equity estimate is spread upon the pages of my direct and rebuttal.

Q You, in making a comparison between proxy companies and FPL, would want to do so as much as possible on an apples to apples basis, right?

A Well, that would be one criteria. I mean, you would want to try to identify objective measures that were transparent that are relevant to investors in order to identify comparable risk entities.

Q Well, for instance, you wouldn't think it optimal to compare FPL's investor-supplied capital to another entity's ratemaking capital structure, would you?

A Well, I think there's a difference between ratemaking capital structure and investor-supplied, because there are many adjustments that occur in the ratemaking process. So what I've endeavored to do is use the audited financial reports of the comparable companies to identify their capital structure.

Q Other utilities have purchased power agreements aside from FPL, correct?

A Yes.

Q Now, if we look at the members of your utility proxy group, some of those have PPAs in existence, don't they?

A Yes.

Q How many of those entities are both buyers and sellers under PPAs?

A Well, Southern Company is really more of a net seller than buyer, but it does have some buying. It has qualifying facilities. Sempra does, Vectren does, WE and Xcel do, PG&E and Scana do. ITC Holdings does not, because it only operates transmission. And Consolidated does not because it does not have -- at least on the Con Ed side -- generation, and its generation is self-sufficient, and the line has both sales and purchases.

Q When S&P analyzes the exposure under PPA, does it net the purchases and sales of an entity under PPAs?

A I think it depends on the nature of the PPA and whether they regard it as a material factor.

Q Do you think that S&P reads each of the PPAs of the utilities involved?

A No, I don't think so. I think what S&P does is ask the -- summarize its obligation and then it makes a judgment. And if there is some question, they might want to see the underlying document. But my -- I'm not sure they pore over all the PPAs, because in some cases, like the qualifying facilities, there can be hundreds.

But I also know, as I note in my testimony, or I believe it was a discovery response we made, that for many companies Standard and Poor does not even report an imputed PPA because the numbers just aren't material enough to justify any kind of adjustment. Only a few companies where there is a material impact, such as FPL, is that noted in S&P reports.

(Off the record)

BY MR. SUNDBACK:

Q Okay, in preparing your testimony, you haven't independently determined that FPL qualifies for an ROE adder, have you?

A No, the purpose of my testimony is to speak to the adder as being appropriate regulatory policy and consistent with FPSC action, and the objectives of regulation. But I rely on the testimony of other witnesses as to the specifics of FPL's entitlement.

Q Okay. If we look at your rebuttal testimony, page 93, line 20 --

A Oh, right, here we go. Sorry.

Q -- last line on the page.

A Yes.

Q You advocate increasing the ROE when a utility is performing well to serve its customers. Is that the standard that you think from a regulatory policy should be implemented in order to justify an adder?

A Well, I think there has to be superior performance. Performing well might be -- I think it is in the Commission's judgment as to whether the performance is sufficiently superior and beneficial to customers as to whether an ROE adder is -- is authorized and performing well. That's what I said, and I'll stick by it, but it's probably a little Milquetoast.

Q By Milquetoast do you mean to suggest that it might be too low a threshold?

A Yes. I would probably -- I think the adder should be in circumstances where there is a clear benefit for customers, as I think, although it's not part of my testimony, but I think there is testimony from FPL witnesses that purport to demonstrate that.

Q So it's not your testimony, then, that one must demonstrate superior management to obtain the ROE adder, is that correct?

A I don't think it's necessary to be best in class. I think it's important to be well above average in terms of the outcome that the customers receive. And I think that is a purview of the Commissioners. Sort of like balls and strikes, the umpire gets to call them.

Q All right. A lot of your testimony is dedicated to explaining your opinion that ratepayers would experience harm if FPL's ROE were reduced, right?

A Yes, if it's dramatically reduced such that the posture of financial strength that has benefited customers is undermined.

Q Okay, so if it's drastically reduced. If it was reduced from 50 basis points from your recommendation, would that constitute a dramatic reduction?

A Well, I think it depends on the rest of the rate order; what happens to capital structure and what happens in disallowances. Again, it's not my call, its investors' call and --

Q Let's focus on --

A -- if the outcome of this case is one that is shocking, as the last litigated case was, then I think customers will suffer. If it is reassuring, as the settlement was, customers will not suffer.

Q All right, but let's focus just on the ROE level.

That was really my question, sir. If the ROE level was reduced by 50 basis points, but the capital structure was maintained, and no other substantive cost disallowance was implemented, would it be your opinion that that would constitute a dramatic reduction in ROE?

A Probably not, since the company is pretty much able to earn and under the circumstances of the settlement to earn 11 percent now. Now, if, as part of the new order, customers lost confidence that the 11 percent was as solid and as earnable as it is now, I think then you would have a detriment to the financial strength and ultimately the customers.

Q All right. Well, let's look at the other side of the equation. Could you identify for us each benefit that you considered in preparing your testimony that would result, for ratepayers, if the ROE was reduced from the level requested by FPL.

A I did not.

Q Could you identify for us each benefit you considered in preparing your testimony that might arise for ratepayers if the level of debt component in FPL's capital structure for regulatory purposes might be increased in any way?

A No, my testimony focused on the benefits that the FPSC Staff and others have identified from FPL's position of strength, which is based on its ROE and its capital structure, as well as its credibility in capital markets.

Q All right. You've discussed today, as well as in your testimony, some of the risks that are posed by various fuels used for generation. Do you recall that?

A Yes.

Q Have you studied the risks that are presented for owners of coal-fired generation?

A Yes, in the context of doing cases for companies that are heavily dependent on coal.

Q Okay, could you describe for us your understanding of the amount of cost that, for instance, the Southern Company will incur over the next five years to deal with and come into compliance with rules concerning emissions standards applicable to its coal-fired plants?

A Well, first, those standards are not final and completely articulated. There is a lot of dynamism in the environmental regulations. The Environmental Protection Agency has made proposals. There have been a lot of push back on those proposals in Congress. There are cases in various courts trying to stay the effect of those proposals.

So I don't think we're in a position to know how much Southern Company or any other coal-dependent utility will end up having to invest to meet whatever the standards may end up being.

Q Would you agree that one measure of risk is the level of uncertainty associated with an outcome in the future?

A Yes, that's one measure of risk, and I think what we have in the area of coal is we've identified kind of the worst case, by most observers, and that is the EPA's proposal. And the outcome is expected to be something between that and what we have now.

Q The Xcel Companies, in addition to the Southern Company, also have substantial coal-fired generation assets, do they not?

A Yes, beginning with Southwestern Public Service and going up through Colorado and Minnesota.

Q And you don't have an estimate for us either of the cost that Xcel might incur in order to comply with emissions standards associated with its coal-fired generation plants, do you?

A No. The bond ratings and the Value Line risk measures for Xcel contemplate the uncertainties associated with its coal dependence, but I didn't independently make an assessment.

Q You previously stated today that FPL couldn't access capital on reasonable terms during the period between the first Florida Commission order in 2010 and the subsequent December, 2010 order on the settlement. Do you recall that?

A Yes.

Q Are you aware of how much FPL borrowed during that period?

A No. I understand from discussion with financial personnel -- and Mr. Dewhurst can certainly speak to this -- that during that period there was an effort to avoid going to the market, because of the clouds, but an enterprise as large as NextEra can't completely avoid the markets, even when there are uncertainties. But I don't, from my own personal experience, know what the financing program was between those two dates.

Q So it wasn't important to you prior to making that assertion to actually understand how much FPL was able to borrow during that period, is that correct?

A That is correct, because the assertion is based on my reading of the published public reports by the rating agencies which were very negative toward FPL and toward the regulatory prospects, and also my discussions and reading the testimony -- my discussions with and reading the testimony of Mr. Dewhurst.

MR. SUNDBACK: Those are all of our questions. Thank you, sir.

THE WITNESS: Thank you.

MR. GUYTON: May we get kind of a quick assessment of who there is remaining? Mr. Avera is only available until 5:00.

MR. McGLOTHLIN: Joe McGlothlin, with OPC, I still have 15 or 20 minutes.

MR. GUYTON: Thank you, Joe.

MR. ARMSTRONG: Brian Armstrong. I probably have less than that.

MR. HENDRICKS: Yeah, Hendricks, I probably have ten minutes.

MR. GUYTON: I'll leave it up to you gentlemen as to the order in which you want to go.

MR. ARMSTRONG: Mine will be very quick, Joe, if that's okay with you.

MR. McGLOTHLIN: It's okay.

MR. ARMSTRONG: I've been checking off as we go. And I appreciate South Florida Hospital's line of examination, because that's really what I wanted to follow, as well.

CROSS EXAMINATION

BY MR. ARMSTRONG:

Q So just a couple of lines of discussion. One is, Mr. Avera, can you tell me what the impact on investors is if a higher return on equity is authorized by the Commission?

A Well, I think investors have more opportunity to earn and they have more willingness to bear risk.

Q Is that it?

A Yes, investors are making choices between many options, and if the company has a higher allowed return and in fact is likely to earn that return, then that makes the company a more attractive investment and they are willing to put their money when the company needs it.

Q Would you admit that the obvious negative impact on customers if the Commission authorizes a higher return on equity is the higher rates that would result?

A The short run impact is higher rates than at a lower ROE than authorized, but there are other implications that I think benefit customers that we've been talking about today, and are in my direct and rebuttal.

Q Could you just in one place -- that's what I was wondering -- what are those other benefits? If the Commission were to authorize a higher return on equity, what are the benefits to customers?

A Okay, the first benefit is the company is able to save money that the customers will ultimately have to pay in their rates. It saves money when it borrows. It saves money when it contracts with the vendors. It saves money when it buys fuel. It saves money when it hedges for fuel. So there is a savings of money that occurs over time when a company is stronger financially.

The second benefit or set of benefits is the company is able to raise capital in times of distress and emergencies. These can be natural emergencies, like storms, when the company has to come up with cash to buy replacement power, to hire additional crews, to get steel and concrete on the ground.

So customers benefit because their service is restored more quickly. Customers benefit because generally the company can respond when there are fuel -- dramatic changes in fuel costs, or when a nuclear outage occurs. The company can pick up new sources of supply rapidly so the lights don't go out and the customers can continue their commerce and lives, which is very important to people, as we've observed other places where there have been extended outages.

The customers benefit when there is a financial emergency and companies are squeezed out of the credit market. But if their utility is a preferred lender, they can raise money and do what needs to be done to maintain the quality of service. And very often, in times like that, if you're able to buy when everybody else can't buy, you can get really good deals on things that you need to buy, like consumables and construction.

So I think all of those benefits inure to customers and should be recognized by the Commission as the agents for customers.

Q Is that it?

A Yes, sir.

Q Okay. Can you explain to me, if the investors and the customers receive all the benefits you've just listed, when FPL receives a higher return on equity, can you explain why FPL would be making all the accounting adjustments to reduce the return on equity that it's reporting?

A Well, I'm not an accountant, but as an economist and financial analyst, I believe what FPL is attempting to do is develop a revenue requirement presentation that is consistent with regulatory requirements and reflects what is likely to happen in the future.

Q Do you know what -- can you explain what accounting adjustments FPL is making to reduce their reported return on equities?

A No, sir. I probably made a mistake by agreeing with you at the beginning of this conversation. I am not an accountant. I am not responsible for the accounting adjustments. But generically accounting adjustments are made by utilities because it is necessary to have a representative presentation of what has happened and what is likely to happen in the future and respond to the requirements of the FERC system of accounts.

Q You would agree that accounting is an historic reflection and recording of information, though; it's not prospective, right?

A Well, accounting is not prospective. I understand in Florida the test year is partially projected, so it is necessary to use historical data, but to adjust it so it is representative of the test year.

Q Well, I guess, just let me clarify, too. You mentioned that as we began our discussion maybe you shouldn't have agreed with me about the accounting treatment to try and reduce reported return on equity, but you actually throughout the day have been asked questions that have dealt with this issue, and you're admitting that FPL has made accounting adjustments to try to reduce the reported return on equity, right?

A No, that's what I did wrong, and I'm trying to apologize for. I don't know why they're making adjustments. I know that Mr. Barrett and Ms. Ousdahl have made adjustments and those adjustments will speak for themselves. I can't agree and should not have agreed with you that their purpose is to reduce the ROE.

Q Well, won't you agree that it's important to your testimony and the reasonableness of a return on equity going forward to know whether or not the current rates that are currently offered on return on equity, that FPL has been achieving higher than that authorized return?

A Well, I think investors are interested in the returns that are actually earned. And, of course, there are measurements issues in terms of financial reporting and regulatory reporting that can become very complicated and are beyond my bailiwick.

But I think, when I speak of ROE, I am speaking of the ROE that the Commission uses to set the rates for this company and numbers like the 11 percent that the company has been able to earn and is able to earn under the stipulation.

Q Okay, let me just go to another area, and this will be relatively brief, as well. There were some questions regarding the other utilities used in your proxy group. And I guess the FPL fuel mix relative to the other industry participants is relevant criteria in your analysis of a reasonable return on equity, isn't it?

A The risk is a relevant criteria. Fuel mix is one of the components that investors consider in assessing risk. In choosing the comparable companies, I relied on objective measures of risk that investors use, things like bond ratings, Value Line safety ranks, betas. And those are holistic. They consider all the relevant aspects, including fuel mix.

Now, as I discussed earlier with the Staff, the fuel mix varies from utility to utility, but it is part of the many things that investors look at in assessing the total risk of the company, as reflected in the measures that I've used.

Q So fuel mix is one of the criteria mentioned that investors would want to know about, and customer mix was another, correct?

A That is another. I think what I said is the customer mix is not a material factor unless it is extreme, because each of the customer classes has its own risk and benefits to the utility.

Q Okay. And then the number and the amount of the pass-through cost mechanisms, those also are criteria, correct?

A Well, they are relevant. I did mention that they are a two-edged sword, because while a utility can be comfortable that it is likely to recover its cost, subject to prudency review, it cannot recover more than its cost under the normal operation of most of these adjustments.

MR. GUYTON: Mr. Armstrong, I'm trying to be real patient here, but we're really plowing over plowed ground.

BY MR. ARMSTRONG:

Q I'm coming to my point. Mr. Avera, do you represent -- are your clients any of the proxy utilities you've identified?

A Do I represent --

Q Yeah, have you testified on behalf of any of those proxy utilities that you've identified?

A Yes.

Q So you've testified in rate cases for them?

A Yes.

Q So in order to testify for them, just as with Florida Power and Light, you'd need to know their fuel mix and their customer mix and their percentage of revenues coming in through pass-through mechanisms, wouldn't you?

A Yes, I do. I can't say that I have committed them all to memory, but when I was doing cases -- we have cases ongoing for Reliant, for ITC, for PGE, for Southern Company, Xcel, Vectren. So we've done cases for those companies.

Q And tell me if I missed it, but I've scoured your testimony, direct, rebuttal, I've scoured your exhibits, I've scoured the discovery responses. I don't see anywhere where you've provided the factual information about fuel mix, customer mix, percentage of revenue recovered through pass-throughs for these other utilities in your proxy group. Have you provided that to the Commission?

A Well, I have. I think I provided the Value Lines that I reference. The Value Lines all have the customer mix, they have the fuel mix, they have the allowed return. But let me be clear. I selected these companies based on these risk measures, which take into account, as investors consider them, all of the relevant parts of risk.

But I selected these companies not because of their fuel mix, not because of their customer mix, not because of their nuclear involvement, but because these objective measures of risk were in the same area as FPL's.

Q And I believe you did testify earlier that the closer we have of an apples to apples proxy group to FPL, the more the information can be relied upon by the Commission, isn't that correct?

MR. GUYTON: Your question assumes that -- you're asking him to repeat what he testified to earlier. Asked and answered.

BY MR. ARMSTRONG:

Q Is that correct, that the closer the utilities are in your proxy group with respect to items including fuel mix, customer mix, pass-through costs as a percentage of revenue, and the other factors you've identified as far as risk factors which the shareholders would like to know about, the closer we have to an apples to apples comparison the more relevant that information is to the Commission's determination of a reasonable return on equity, correct?

A No. The Commission is not interested in apples, oranges, pineapples. It is interested in risk, because that's what the Supreme Court says. These companies must be comparable in risk. They may differ in the details of their business, their geography, but they must be comparable in risk because that's what matters to investors.

Investors don't -- I mean, in assessing risk, they study customer mix. In assessing risk, they study fuel mix, nuclear involvement, regulatory quality. But when the rubber meets the road, it's what is the risk, and, therefore, what is my required return.

Q Are you familiar with who has the burden of proof and the discussion of burden of proof when it comes to the reasonableness of the return on equity being advocated by FPL? Do you know who bears that burden?

MR. GUYTON: Objection, it calls for a legal conclusion.

BY MR. ARMSTRONG:

Q Do you know, Mr. Avera?

A As a lay person, my understanding is that the company must present a prima facie evidence of proof and then the other parties must strive to defeat that evidence.

Q Do you think it would assist the Commissioners in determining a reasonable return on equity if you had presented a chart that reflected the fuel mix, customer mix, percentage of revenue recovered in pass-through cost mechanisms in a chart for your proxy group?

A No. The relevant chart that I have presented for the Commissioners is the risk measures of these companies. And that is presented in my testimony, and that is what is relevant in assessing whether or not these companies are comparable to FPL.

Q I just need to have you answer this one thing, then. The fuel mix, the customer mix, and the pass-through mechanism of cost recovery, those are not, in your expert opinion, part and parcel of the risk faced by these other utilities in the proxy group?

A They are part and they are parcel but they are not the totality. If I just presented these, the Commission wouldn't have a complete picture. The totality of risk is reflected in the objective risk measures that investors actually use in making their choices, and that is what I presented to the Commissioners.

MR. ARMSTRONG: Okay. I just want to make sure I didn't miss anything here. Okay, I appreciate it, Mr. Avera. Thank you.

THE WITNESS: Thank you.

MR. McGLOTHLIN: Mr. Hendricks, do you want to go?

MR. HENDRICKS: Yes, I can, if that's okay with you.

MR. McGLOTHLIN: Yes, sir.

CROSS EXAMINATION

BY MR. HENDRICKS:

Q Good afternoon, Dr. Avera.

A Good afternoon, Mr. Hendricks.

Q I noticed your office is on Red River.

A Yes.

Q That's a darn good choice. I haven't lived in Austin since college, but I still have some fond memories of that area.

A Well, you're welcome to come back and visit. It's just turned better.

Q I'll do whatever I can. Let me ask you to look quickly at page 33 of your direct testimony. You describe the selection criteria for the utility proxy group there.

A Yes.

Q Including S&P ratings, two Value Line ratings, and a market capitalization. Would you enlighten me a little bit on why you relied so much on Value Line data in terms of both creating the group and then two of their measures for selection, rather than perhaps using just a couple of the bond agency ratings?

A Well, first, Value Line addresses the equity. And since we're trying to get equity risks that are comparable, it makes sense to look at equity ratings, which is what Value Line trades in. They're not a bond rating agency, they are an investment advisory service for equity.

Secondly, Value Line is, by all accounts, the most widely circulated, widely read, widely available service. It is in every library, it's in every commission, it is in every utility office, it's in every brokerage office. So Value

Line is available to investors.

Value Line has credibility. It is accepted by commissions. I've done civil litigation; it has been accepted by the courts as an authoritative resource.

It is also, as I mentioned in my rebuttal, when the general settlement of the analysts' inquiry was done, Value Line was found to be an independent source that brokerage firms must make available to their clients in addition to their own proprietary research. So for all those reasons I think Value Line is a good place to go to look at risk as investors look at it.

Q Okay. Most of the times, in talking about the bond -- bond rates, though, people do speak of the bond rating agencies.

Let me just ask you, if you look at the specific criteria that you use, and it's interesting that the group average of the companies that you selected, without including NEE in that group, is almost dead on the NEE position in both equity percent and ROE. Could this indicate an inadvertent tailoring of the selection criteria?

MR. GUYTON: I'm sorry, can you give us a reference that you're referring to, Mr. Hendricks?

MR. HENDRICKS: That's the data that's provided in the -- I've got to find the right number here. Sorry. I'll tell you what, can we come back to that?

MR. GUYTON: Sure.

MR. HENDRICKS: I will find that, but I don't want to waste too much time looking for it right now.

BY MR. HENDRICKS:

Q In your judgment, Dr. Avera, I think it would be fair to say, based on what you've said so far, that you believe that FPL and other utility investors would require a different ROE if the regulatory capital structure were changed?

A Yes, sir. I think there's a link there. If you add or subtract financial risk, then that is reflected both in what the company has to pay for bonds and the required return of equity.

Q Right. With reference to characterizing and estimating these changes, when you performed your analysis of the utility proxy group, what mechanism did you use to translate the equity ratio in the NEE capital structure, which was about 45 percent, to the about 60 percent equity ratio in the FPL recommendation?

A Well, I used the risk measures to identify companies that were comparable. And then the bond ratings of NEE and FPL are comparable and we had to use the NEE stock prices because FPL does not have stock prices. So I believe the application that I used, which is basically to take the company as it is, was the proper one.

Q All right, this time I do have the exhibit number. WEA-3, the proxy groups versus FPL.

A Thank you.

Q It looks like that some of the data here, which is the Value Line data, again, that are labeled as FPL are actually NEE data?

A Yes, I think I make that quite clear in my testimony.

Q I agree, it shows up later in the testimony, I was just thrown by it when I first saw it, because the chart seems to be inappropriately labeled.

Let me ask you to turn to page 13 of your rebuttal testimony. There you refer to the role of the Florida Public Service Commission as balancing the interests of customers and utilities where free markets don't operate effectively. And I assume you'd stand by that statement. It's not terribly unusual. I mean, my favored view refers to both achieving equity and efficiency in public utility regulation.

A I mean, I think these words actually come from the Hope and Bluefield decisions.

Q Okay. But I think the balance is the important question.

A Right.

Q It appears from looking at a lot of the analysis in this case, and particularly yours, that most of the discussion about ROE and capital structure appears to reflect what we might think of as the investor view, which is certainly appropriate for understanding investor requirements. But we need to also think about the ratepayer requirements, and they may have a slightly different view.

With that in mind, would you agree that investors are primarily concerned about the returns that they receive, but the utility rates are driven more by the revenue requirement, which also includes allowances for utility income taxes?

A Well, I don't completely agree. Let me see if I can replay it in a way that's acceptable to you. I believe investors are concerned about the risk and return, and they also know that for the utility to be viable, it has to meet the requirements of the regulators who are the agents for customers.

So the utility -- an investor knows the utility cannot long prosper if the customers are unhappy. So I think investors are not blind to what's in the best interests of the customers, as well. And I think, in assessing the revenue requirements, the Commission obviously has to take into account the reality that taxes must be paid. And if the utility is not able to recover from customers enough to pay its taxes, it cannot be profitable.

Q Right. I would certainly not dispute that. Do you see any value in considering that taxes are a fairly substantial element in translating the regulatory ROE into a revenue requirement in looking at a pretax version of the weighted average cost of capital?

A Yes, taxes are important, and, of course, the measures that rating agencies, for example, use, use before and after-tax data, because bond holders are aware that taxes actually give them a cushion, so that if the utility is in financial distress, the equity holders don't get their money and Uncle Sam doesn't get his money, either, so there's more left for the debt holders.

Q Okay. Could you take a look at your rebuttal testimony -- I'm trying to go as quickly as possible -- on pages 27 and 29.

A Yes, sir.

Q And there you talk about it being important to consider the current -- and I don't think you specifically say it, but you talk about expected future capital market conditions, and that those are important in determining ROE and capital structure.

A Yes. Future conditions are really important because, as discussed earlier, that's where the investor lives and what they get in the future.

Q Right. If you could flip over to Exhibit WEA-11, page three of four.

A That's back in the direct now?

Q Yes, it is. I'm sorry. I should have had these organized a little better.

A Yes.

Q Do you agree that this table indicates that there is a historically low average utility bond yield and a historically high risk premium based on allowed ROE at the end of this table which shows 2011?

A Yes.

Q It looks like we have about a 5.13 percent yield which is an average of about 8.91, and a 5.09 premium versus an average of 3.41. And this reflects a really substantial percentage, particularly as a percentage of the cost of the bond yields.

In estimating the evolution of these -- now, should these be taken into account in looking at capital structure?

MR. GUYTON: Object to the form of the question.

I'm sorry, Mr. Hendricks, I just didn't follow it.

BY MR. HENDRICKS:

Q Okay, this is Dr. Avera's data, so I didn't make it up, I'm just asking him if he thinks that the fact that these rates are historically low should be taken into account.

A I think there are separate issues. There's the issue of what investors require, and what you've observed is validated by the statistical measures that I present on the next page that there is indeed an inverse relationship.

When interest rates are very high, as they were in the seventies, the risk premium is narrow. When interest rates are exceedingly low, as they are now, the risk premium is wide. That's why I think you ought to take into account this relationship, as Mr. Gorman does not.

Q Okay. In estimating the evolution of these rates in the near future, would you take into account the Federal Reserve's announced intention to continue accommodating policy for the next two years or more?

MR. GUYTON: Objection, assumes facts not in evidence.

THE WITNESS: The Federal Reserve's accommodated policy primarily operates on the short end. And it is the expectation of most observers and certainly hopefully the hope of Dr. Bernanke, that the economy will find its bottom and start to go up, in which case interest rates will go up and presumably with that the risk premiums will decline.

BY MR. HENDRICKS:

Q Well, right, but I would think that if you look at the -- well, thank you, I'm not going to debate that. But while rates do remain in the neighborhood that they're in now, where they are now and where they may be for the next couple of years, do you see a value to the ratepayer for locking in more funds with long-term fixed bonds at these historically low rates?

A Well, I think it makes sense for the company to issue long-term bonds rather than short-term bonds. But I think the company also has to be mindful of its capital structure and the effect of its capital structure on the risk of the company and the availability of finance. And, in fact, if it issues too many bonds, the cost of bonds will start going up because the risk will go up. And the ratepayers, the customers, will end up paying that for the next 30 years.

Q Well, but the rates that the -- the fixed rates that you put on a bond that you sell today are not going to change next year just because other conditions change.

A That is correct. So that's why it's prudent to issue long-term bonds, but it's not prudent to issue so many bonds that your financial position deteriorates.

Q Correct. So how would you -- how do you actually balance those two advantages: The issuing of more long-term bonds give the ratepayers a chance to take advantage of low-cost capital now and not see the cost of that go up in a larger percentage, but it does also put at risk some of the future rates, particularly for equity?

A Well, I think that is a balancing challenge, and Mr. Dewhurst is the guy that has to do it. And he uses his staff and the best information available to make those choices. But one of the choices cannot be or should not be to issue so much debt that he -- let me use the expression kills the golden goose, by destroying the financial strength that has been so beneficial to customers.

Q Okay, one final question, and then I'll let you go. I know you've had a long day of dealing with us.

A Yes, sir.

Q Let me just ask you, you did -- it's not a primary subject of these hearings, but since you just brought it up in the context of your answers, particularly about Orange and Rockland Utilities, and the effect of risk on expected return. Is it your observation that the -- that fuel cost recovery clauses tend to weaken utility incentives to manage fuel price risk?

A There's been a lot of debate about that, especially in the early seventies, when fuel clauses first came into popularity. Personally, where I come down is no. I think it's in the company's interest to lower fuel cost as much as possible to keep customers and the Commission as happy as possible. And the company knows that if it incurs a fuel cost that is questionable, it is vulnerable to a disallowance.

Now, I do think having some incentives built into the fuel clause is a good thing. And when I was at the Texas Commission, we experimented with that, and I know the Florida PSC has experimented with that.

So just like I think incentives in the ROE is good policy and is consistent with free enterprise -- regulation that models free enterprise, I think that could be extended to the fuel clause.

I was asked earlier today could the fuel clause be improved, and I said, you know, I haven't focused on that. But my thought is, to the extent that incentives could be built in without undermining the risk benefits of the fuel clause, that would be a good thing.

MR. HENDRICKS: Okay, very good, I thank you so much for your patience, and wish you well in getting back to Austin.

THE WITNESS: Thank you.

CROSS EXAMINATION

BY MR. McGLOTHLIN:

Q Dr. Avera, this is Joe McGlothlin with the Office of Pubic Counsel.

A Good to talk to you again, Mr. McGlothlin.

Q You, also. I have a few questions about the document that has been identified as Late Filed Number 6. And this is the one that you described as back of the envelope and in rough form. Do you remember that characterization?

A Right, right, the reworking of MPG-18.

Q Without asking about specific values and the content of that document, can you describe the document further in terms of what it is, physically? And by that, I mean, for instance, is it handwritten or typed?

A Actually, it's in the computer. What I did is, we had Mr. Gorman's work papers, which included the spreadsheet that he used for MPG-18, and it's also used for MPG-1 and one other of his exhibits. And what it does is it tracks through, if you change the capital structure, it tracks through what it does to the metrics that S&P uses, the three metrics: Capital structure, funds from operations over EBIT, and cash flow over debt.

Q When did you prepare it?

A What?

Q When did you prepare it?

A I prepared it actually yesterday on the plane. And what I did, I also added --

Q I only asked you when you prepared it.

A Yesterday on the plane.

Q Okay. And what occasioned you to prepare that particular exercise?

A We had done a similar thing in the Lone Star case in Texas where we reworked his numbers. He had a similar exhibit and a similar analysis, and we had gone through and used that as a basis for testing some of the Intervenor and Staff proposals. And I was thinking we might be able to do the same thing in this case, so I was just looking at how his exhibit worked in this case and what happened if you changed some of the inputs.

Q When you say we, who do you mean?

A Well, I'm the one that did the computer. In the Texas case, I did the analysis and the attorney asked the questions.

Q Okay. In terms of the document or the exercise you performed on the plane yesterday, was that your initiative, or were you asked to do it?

A It was my --

MR. GUYTON: I object. We're getting into trial preparation at this point. I don't think that's an appropriate question, and one that would be protected by privilege.

THE WITNESS: It was on my --

BY MR. McGLOTHLIN:

Q In any event, Dr. Avera, it is not a work paper to either your direct testimony or your rebuttal testimony, correct?

A It is not.

Q And you did not rely on it for any purpose in preparing your direct testimony or your rebuttal testimony, did you?

A I did not.

Q And in response to another question you made this statement -- and I'm paraphrasing -- but I think you said something like I can put 8.5 percent on there, too. Do you remember saying that?

A Yes.

Q And by the 8.5, are you referring to the ROE recommendation of OPC's witness, Dr. Woolridge?

A Yes.

Q And do I understand correctly that the document or the exercise or analysis that's been identified as Late Filed 6 does not yet incorporate the 8.5 percent ROE recommended by the OPC witness?

A No, it does not.

Q I have a few questions about some of your testimony and answers today that relates to the description of the first order in the most recent FPL case as shocking and the effect of the December, 2010 settlement as reassuring. Do you remember using those words?

A Yes, in fact, I think those words were taken from Value Line. Those are not my words, Mr. McGlothlin.

Q I think you did say that the effect of the settlement was to better enable FPL to earn 11 percent. Do you remember saying that?

A Yes.

Q And you are aware, are you not, that the 11 percent was nothing new with respect to the settlement; that was part of the authorized range in the first order?

A Yes, I know that.

Q Okay. When did your engagement for the last rate case end, Dr. Avera?

A Well, there was a period of time after the order when the company asked me to do some research in the context of their negotiations about a settlement, so I did some analyses at the request of the company and I obtained scme documents from other states that had settlements and mechanisms. And that continued for several months. I don't exactly remember when it ended.

Q Okay. In response to a question from Staff that related to the achieved ROE in the months of May and June, you said that you didn't have personal knowledge but that your understanding was that FPL could adjust its accounting; do you remember that question and answer?

A That is correct. My understanding is that because of the mechanism of the depreciation reserve, there was some flexibility that FPL had.

Q To the extent you know, can you tell me what the provisions for depreciation reserve surplus were in the first order and how that changed in the settlement agreement?

A No, Mr. McGlothlin, you've gone deeper than my knowledge of those specifics. I understand it was a big issue in the rate case and I understand it's part of the mechanism in the settlement.

Q I have a few questions about your testimony on the subject of power purchase agreements and the manner in which S&P imputed some debt equivalence there.

On page 84 you say that Standard and Poor imputed $940 million of debt. Can you describe for me how Standard and Poor calculated that amount?

A S&P -- let's see, this is 84 of the rebuttal? No, this is 84 of the direct?

Q The direct, yes, sir.

A As I understand the process -- and it's late in the day so I don't know that I can go through the exact math. But they make an assessment of first how firm the obligation is. And based on that they give a debt equivalency to the obligations. They take the series of annual payments that are required under the PPA and they discount that back in order to get an amount of debt equivalence.

And then they also apply an interest rate to that amount to put in an amount of interest rate and an amortization equivalent that would go with that debt. And then they use that in calculating the metrics.

So it's a process of taking the PPA obligations and converting them to an equivalent amount of debt and how that would hit the balance sheet and income statement of the company, and then they adjust the balance sheet and income statement for the amount, and then that is reflected in the calculation of the metrics.

Q In your answer you refer to an interest rate. Are you using that to describe the risk factor that S&P applies or is that a separate component of the calculation?

A There are separate components. There is a risking or an application of the firmness of the obligation that determines -- and then there is a discount rate that is used and a rate that is used to convert the debt balance to annual payments.

Q And can you tell me what the risk factor -- what value for the risk factor S&P used for the calculation of 949 million?

A As I sit here today, Mr. McGlothlin, I can't remember. It is footnoted in the S&P reports for FPL, and I could look it up, but it's laid out there, I believe. And those documents have been provided in discovery.

Q All right. As we talk I'm trying to winnow some of my questions in this area because counsel for the South Florida Hospital Association has covered some of this ground, so I don't want to duplicate those questions. So bear with me for a second.

MR. GUYTON: Take as much time as you need to winnow questions, Joe.

BY MR. McGLOTHLIN:

Q Since you have referred to some S&P documents that are available, let me just ask you a few that are related. In preparing your testimony, did you review the power purchase agreements to which FPL is a party?

A No. I reviewed the discussion of those agreements that's in the 10-K and then the bottom line calculations that S&P made, but I did not review them, the agreements, themselves. And as in many things, my opinion doesn't matter, it's S&P and the investment community that counts.

Q With respect to the regulated utilities under the Florida Commission's jurisdiction, are you familiar with which part of the process FPL's power purchase agreements are presented to the Commission for approval?

A I don't know in detail. I know that in order to recover the costs in its adjustments they have to be reviewed by the Commission, and they are subject to prudency review. But the actual process, again, I think I knew at one point, because you and I participated in the NEE cases and many other cases where those were highly relevant. But as I sit here today, I'm a little fuzzy on the actual process of approval.

Q Do you know whether the costs are recovered through base rates or through a separate recovery mechanism?

A Some of the costs are through a recovery mechanism. I'm not sure about the capacity payments as I sit here today. But the fuel costs or the energy costs are.

Q With respect to the costs that are recovered through the clause mechanism, do you know whether those are recovered on a current basis, as opposed to having a lag before recovery?

A Again, I don't have specific knowledge. The general recovery in Florida is, as in many places, is prospective. But I can't tell you exactly how it works for those PPA energy payments.

Q Do you know whether the particular clause mechanism applicable to power purchase costs have the true-up mechanism?

A I don't know specifically. My impression is that there are true-ups in the purchase power clauses. But again, from my personal knowledge, I can't say for certain.

Q With respect to your Exhibits 14 -- would you turn to that for a moment?

A Yes, sir.

Q Okay, you beat me to it.

MR. GUYTON: We're highly motivated, Joe.

BY MR. McGLOTHLIN:

Q There is an entry on 14 for the S&P debt equivalent of $949 million, correct?

A Yes.

Q And do I understand correctly that the purpose of this exhibit is to calculate an implied equity ratio on the assumption that the $949 million of debt equivalent is reflected in the investor sources?

A Yes. It is to demonstrate the effect that has on the capital structure as S&P and I think other investors would look at it.

Q But would you agree with me that this particular adjustment is not part of FP&L's formal financial statement?

A No, it is an adjustment, an imputation made by S&P and I believe other investors, also, because PPA is a fixed obligation.

Q So it follows that this particular entry would not appear either in FP&L's financial statements or in reports to the Commission or to the SEC?

A That is correct. The underlying data as to the PPA obligations is in the 10-K and is reported to the SEC. And in my past experience, both with rate cases and NEE cases, the Commission looks at this debt equivalent as a relevant consideration.

MR. McGLOTHLIN: Those are all my questions. Thank you, Dr. Avera.

THE WITNESS: Thank you.

MR. GUYTON: If you'll bear with me, I have just a few redirect.

(Off the record)

CROSS EXAMINATION

BY MR. GUYTON:

Q I hope you recall this morning. I think I do. You were asked by Staff about the variability of earnings of your utility proxy group as well as the variability of earnings in your non-utility group. Do you recall that line of questions?

A Yes.

Q What impact, if any, does weather have on the variability of earnings for a utility?

A It can have a great deal, depending on the ratemaking process, but generally the sales of an electric utility are a function of, among other things, the weather. And when it's very hot, the air conditioners run, the water pumps run, and the utility sells more energy.

Q You were asked a question about FPL's ability to raise capital after the last decision in the last rate case authorizing FPL a return on equity of 10 percent. Do you recall that?

A Yes.

Q And you were also asked about the ability to raise capital after the settlement agreement in the last rate case. Do you recall that?

A Yes.

Q In your mind why was the company able to raise capital on a reasonable basis with a return on equity of 10 percent after the settlement agreement?

A Because the investment community, as reflected in the bond agency reports and Value Line reports, saw the settlement as very constructive, that the company would be able to actually earn 11 percent, and it represented a step back from the harshness of the original rate order so that they found this to be constructive and reassuring.

Q And do you recall Staff counsel's remark in your earlier answer that that was your interpretation?

A That is correct.

Q And what was your interpretation based upon?

A My interpretation was based on the actual words that Moody's, Standard and Poor, and Value Line used in characterizing the news of the stipulation. And the words that Mr. McGlothlin was asking me about, like shock and reassured, are actually words that are in their reports.

Q You were asked by several parties about the impact of low natural gas prices on FPL's existing rates. Do you recall those inquiries?

A Yes.

Q Who made the decision to install the efficient gas-fired units on FPL's system that could take advantage of those low natural gas prices?

A I believe that management proposed those, and the Commission agreed, and the company went forward with the blessing of the Commission after the initiative of management.

Q And would the efficiency, the high efficiency of those gas units, work to the customers' advantages even if there were high natural gas prices?

A Yes, it would soften the impact because the heat rates are so low that the net cost to customers is less.

Q You were asked by Staff counsel to read your answer at page 22, lines 3 through 7. Do you recall that?

A Yes.

Q Actually, it was a question and the first part of the answer. Was there an additional part of the answer that you were not asked to read?

A Yes.

Q Would it be appropriate to read only the part you were asked to read without reading the rest?

A No, I think it's important to see the rest of the story.

Q Okay. In the interests of time, I won't ask you to read it, I just wanted to make sure we covered it.

A Yes, sir.

MR. ARMSTRONG: Hi, this is Brian Armstrong.

MR. GUYTON: I'm sorry, Brian?

BY MR. GUYTON:

Q You were also asked to read a question -- bear with me, I'm going to have to see if it was your direct or rebuttal, at page eight.

UNIDENTIFIED SPEAKER: Hello?

MR. GUYTON: I'm sorry, we got a hello. Is there somebody here that we need to talk to? Do we still have the court reporter?

THE COURT REPORTER: Yes, you have me.

MR. GUYTON: Okay. Well, good.

BY MR. GUYTON:

Q You were asked by staff counsel to read the question at page eight and the answer at lines 10 through 13. Do you recall that?

A Yes.

Q And was the portion of the answer that you were asked to read a complete answer?

A No, there was more to the answer that I think is significant.

Q And should the entire answer be read in the context of the question rather than just the first part?

A Absolutely.

MR. SUNDBACK: Counsel, we're going to object. We haven't objected yet, but the form of the question, these are all leading questions on redirect, and that's just not proper. So consider this an objection to be lodged going forward on any further questions. We object to any leading questions.

MR. YOUNG: That was Mr. Sundback, right?

MR. SUNDBACK: Correct. We're supposed to be hearing from the witness, not the lawyer.

MR. GUYTON: Bear with us one minute, please. That's all we have. Thank you for your patience. We want to read and sign.

MR. YOUNG: Not a problem.

MR. McGLOTHLIN: I have a small housekeeping matter. It won't take more than a minute. Keino, are you on?

MR. YOUNG: Yes, I am.

MR. McGLOTHLIN: In light of the questions and answers with respect to Late Filed Exhibit 6, in which Dr. Avera acknowledged that the exercise was done yesterday, well after the rebuttal deadline, and that the information with respect to the 8.50 percent that our witness recommends is not part of that analysis as yet, I would ask the Staff to revisit that request and possibly withdraw it, because it appears to me that it's an effort by FPL's witness for FPL to bolster its case after the deadline for rebuttal has come and gone.

During the deposition counsel for FP&L objected to providing the report on the grounds that it was not relied on by the witness for his direct or rebuttal testimony.

Well, the witness acknowledged the same is true with respect to Late Filed Exhibit 6. And the only reason I say that he offered it to you was because they believe it enhances their case. And it's coming in after the deadline at this point and would be prejudicial to our ability to deal with it prior to hearing.

MR. GUYTON: May I respond?

MR. YOUNG: Yes. Who is that, is that Charlie?

MR. GUYTON: This is Charlie. I don't think the witness offered it up, I think he was asked about it. And he only provided it in response to a question to which it was responsive, posed by Staff.

MR. YOUNG: All right.

MR. GUYTON: But we're entirely comfortable with providing whatever Staff feels like it needs or wants.

MR. YOUNG: Joe, I talked to my technical staff. We don't have a problem withdrawing that request.

MR. McGLOTHLIN: I appreciate it. That enhances the fairness of the process. I appreciate it.

MR. YOUNG: No problem. We are now at that point of -- I'm sure Mr. Guyton would like to read. I think he might have stated that.

MR. GUYTON: Yes, sir.

(Whereupon, the deposition was concluded at 4:25 p.m.)

STATE OF FLORIDA

COUNTY OF PALM BEACH

CERTIFICATE OF OATH

I, the undersigned authority, certify that WILLIAM AVERA personally appeared before me at 700 Universe Boulevard, Juno Beach, Florida, 33408 and was duly sworn by me to tell the truth.

WITNESS my hand and official seal in the City of Juno Beach, County of Palm Beach, State of Florida, this 8th day of August, 2012.

JACQUELINE S. BUSSEY
MY COMMISSION # DD 972569
EXPIRES: July 18, 2014
Bonded Thru Notary Public Underwriters

Jacqueline S. Bussey
Notary Public
State of Florida

My Commission Expires:

Personally known ✓ or who has produced ________.
Type of identification produced ________________

Docket # 120015-EI

CERTIFICATE OF REPORTER

STATE OF FLORIDA)
COUNTY OF LEON)

I, LAURA MOUNTAIN, Court Reporter, do hereby certify that I was authorized to and did stenographically report the foregoing deposition; and that the transcript is a true record of the testimony given by the witness.

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

Dated this 20th day of August, 2012.

Laura Mountain

LAURA MOUNTAIN, RPR
Post Office Box 13461
Tallahassee, Florida 32317

MOODY'S
INVESTORS SERVICE

Rating Action: Moody's Downgrades FPL Group to Baa1 and FP&L to A2

Global Credit Research - 09 Apr 2010

Approximately $12 Billion of Debt Securities Downgraded

New York, April 09, 2010 -- Moody's Investors Service downgraded the ratings of FPL Group, Inc. (Issuer Rating to Baa1 from A2); FPL Group Capital Inc. (senior unsecured to Baa1 from A2); and Florida Power & Light Company (FP&L, Issuer Rating to A2 from A1, senior secured to Aa3 from Aa2). Moody's downgraded FPL Group Capital's short-term rating for commercial paper to Prime-2 from Prime-1 and affirmed FP&L's Prime-1 short-term rating for commercial paper. The rating outlook of FPL Group, FPL Group Capital, and FP&L is stable. This rating action concludes the review for downgrade initiated on January 19, 2010.

"The downgrade of the ratings of the FPL Group family reflects higher risk throughout the consolidated organization resulting from increased leverage at the company's unregulated businesses, higher earnings and cash volatility, a growing energy trading and marketing business, and a deterioration in the political, regulatory, and economic environment at its core Florida regulated utility," said Michael G. Haggarty, Vice President and Senior Credit Officer.

The downgrade of FPL Group and FPL Group Capital considers the following factors:

• FPL Group has incurred substantial debt at FPL Group Capital and NextEra Energy Resources over the last several years, which together now account for 62% of the total debt of the consolidated organization (38% at FPL Group Capital and 24% at NextEra). At this level of debt, Moody's believes that wider notching between the ratings of the parent and the utility more appropriately reflects the risks associated with both the size and scope of the unregulated businesses and the amount of leverage supporting that sector.

• The significant growth in leverage at FPL Group Capital has diluted the value of FPL Group's unconditional guarantee, which now cover $7.5 billion of debt and commercial paper obligations, nearly $2 billion more than at the end of 2008, in addition to counterparty obligations. The company has relied heavily on hybrid securities to finance growth at FPL Group Capital, which may be viewed as having a higher debt component going foward.

• Although another $4 billion of debt at NextEra Energy is at the project level and not explicitly guaranteed by FPL Group, this debt is characterized as "limited recourse" on the company's financial statements due partly to implicit ties to FPL Group and/or FPL Group Capital in some of these transactions, such as guarantees of wind project production tax credits, for example.

• FPL Group has experienced higher cash flow and earnings volatility from its unregulated generating portfolio over the last year due to a combination of low power prices, a poor national wind resource negatively affecting its entire fleet of wind power assets, a longer than anticipated outage at its Seabrook nuclear unit, and a continually challenging Texas power market.

• The company has a growing energy marketing and trading business based in the Houston offices of NextEra and has for the first time articulated an intention to grow this business in its FYE 2009 SEC financial statement filings. This is a strategic shift from the predominantly asset based business strategy it had pursued in the past which in Moody's opinion represents a material elevation of the company's business risk profile.

• The company is subject to higher execution risk with regard to its wind asset development program, with increased commodity costs, more competition, and higher project financing costs. There has also been less willingness on the part of utilities to commit to long-term power purchase agreements with these projects because of uncertainty over renewable portfolio standards, the timing of potential carbon costs, economic uncertainty, and load growth prospects.

• With limited growth prospects at Florida Power & Light due to regulatory and economic constraints, Moody's believes that growth at FPL Group's unregulated businesses will continue to outpace the utility, accelerating the transformation of FPL Group into a predominantly wholesale generating business, with overall credit quality less reliant on its core, lower risk regulated utility business. The company's decision to change its corporate name to NextEra Energy is an indication of its intention to further distinguish these two businesses.

The downgrade of Florida Power & Light Company (FP&L) is attributed to:

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• A decline in the utility's political and regulatory environment as evidenced by its most recent rate case which was plagued by delays, controversy, and political interference in the regulatory process. Because of these developments, Moody's now views FP&L's regulatory framework as substantially less supportive than it has been previously and more characteristic of an average regulatory environment.

• The utility continues to experience weak sales volumes and difficult economic conditions in its service territory, particularly related to the Florida housing market. The challenging Florida economy was a contributing factor to the company's rate case decision, with the Florida Public Service Commission exhibiting sensitivity to economic conditions in the state throughout the rate proceedings.

• Historically strong financial metrics and cash flow coverage metrics that may decline somewhat following the recent rate case decision, although Moody's expects any decline to be modest as a high percentage of FP&L's revenues are recovered through riders or other cost recovery provisions that remain strong. In addition, FP&L's recently awarded 10% ROE is consistent with those granted to some utilities in other parts of the country and its 59.1% equity ratio remains one of the highest in the U.S., mitigating the negative effect of the relatively low base rate increase.

The stable outlook on the ratings of FPL Group and FPL Group Capital reflects Moody's expectation that the size and diversity of the company's unregulated generating portfolio will continue to insulate it to some degree from poor power markets and variable wind resource conditions; that the portfolio will generate adequate cash flow to maintain cash flow coverage metrics adequate for its current Baa1 rating; and that the company will maintain sufficient liquidity to offset the growth of its energy trading and marketing business at NextEra. The stable outlook on the ratings of FP&L reflects Moody's view that the utility's financial performance and cash flow coverage metrics will remain strong for its rating despite the unexpected rate case decision in January and that FP&L's political and regulatory environment will improve once the Florida economy recovers.

The last rating actions on FPL Group, Florida Power & Light Company, and FPL Group Capital were on January 19, 2010, when their ratings were placed under review for possible downgrade.

The principal methodology used in rating these issuers was Regulated Electric and Gas Utilities, which can be found at www.moodys.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating these issuers can also be found in the Rating Methodologies sub-directory on Moody's website.

Ratings downgraded include:

FPL Group, Inc.'s Issuer Rating, to Baa1 from A2;

FPL Group Capital's senior unsecured, to Baa1 from A2; junior subordinated to Baa2 from A3; short-term rating for commercial paper, to Prime-2 from Prime 1; and the trust preferred rating of FPL Group Capital Trust I, to Baa2 from A3.

Florida Power & Light Company's Issuer Rating, to A2 from A1; and senior secured, to Aa3 from Aa2.

Ratings affirmed:

Florida Power & Light Company's Prime-1 short-term rating for commercial paper.

FPL Group, Inc. is a parent holding company for regulated utility Florida Power & Light Company and unregulated subsidiaries FPL Group Capital Inc and NextEra Energy Resources, LLC (unrated) and is headquartered in Juno Beach, Florida.

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FPL's Response to Staff's 1ST Set of POD #14

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Moody's
INVESTORS SERVICE

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MOODY'S
INVESTORS SERVICE

Credit Opinion: Florida Power & Light Company

Global Credit Research - 11 Apr 2011

Juno Beach, Florida, United States

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating	A2
First Mortgage Bonds	Aa3
Senior Secured Shelf	(P)Aa3
Senior Unsecured Shelf	(P)A2
Subordinate Shelf	(P)A3
Preferred Shelf	(P)Baa1
Commercial Paper	P-1
Parent: NextEra Energy, Inc.	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured Shelf	(P)Baa1
Subordinate Shelf	(P)Baa2
Preferred Shelf	(P)Baa3

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Key Indicators

[1]Florida Power & Light Company

	2010	2009	2008	2007
(CFO Pre-W/C + Interest) / Interest Expense	6.2x	10.5x	6.6x	8.3x
(CFO Pre-W/C) / Debt	27%	46%	29%	36%
(CFO Pre-W/C - Dividends) / Debt	24%	38%	29%	18%
Debt / Book Capitalization	33%	36%	36%	38%

[1] All ratios calculated in accordance with the Global Regulated Electric Utilities Rating Methodology using Moody's standard adjustments.

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Stabilized Florida political and regulatory environment with two year rate settlement

- Strong financials, robust cash flow coverages, and low leverage

- Challenging economic conditions in service territory are showing some signs of improvement

- High capital expenditure requirements in 2011 and 2012, mostly for new generation

- Strong liquidity

EXHIBIT
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Depo. of Avera

Corporate Profile

Headquartered in Juno Beach, Florida, Florida Power and Light Company (FPL, A2 Issuer Rating, stable outlook) is a vertically integrated regulated utility with a service territory that includes most of the Florida coastal communities. It is a subsidiary of NextEra Energy, Inc. (Baa1 Issuer Rating, stable outlook), one of the largest providers of electricity-related services in North America with annual revenues of over $15 billion. NextEra Energy is also the parent and guarantor of NextEra Energy Capital Holdings, Inc. (Baa1 senior unsecured, stable outlook), the entity that finances most of its unregulated operations, primarily independent power projects through its wholly owned subsidiary, NextEra Energy Resources, LLC (unrated).

SUMMARY RATING RATIONALE

FPL's ratings reflect the stabilization of the political and regulatory environment for investor owned utilities in Florida; the company's strong financial performance, robust cash flow coverage ratios, and relatively low leverage; good cost recovery mechanisms in place; and a large, mainly residential service territory. This service territory has been under significant economic pressure over the last few years, with the company experiencing stagnant residential sales growth in some years, although there have been recent indications that economic conditions are improving. The company's capital expenditure program is large, particularly over the next two years as it adds new gas fired generation and increases capacity at its nuclear plants.

DETAILED RATING CONSIDERATIONS

- Stabilization of the utility's political and regulatory environment with new Florida commissioners in place and the execution of a two year rate settlement

The political and regulatory environment for investor-owned utilities in the state of Florida has stabilized since highly politicized rate proceedings in 2009 and early 2010 resulted in a rate outcome calling for a $75 million base rate increase for FPL, a small fraction of the $1 billion that had been requested by the company. Since these rate proceedings, however, there has been an almost complete change in the composition of the Florida Public Service Commission (FPSC) with the turnover of four of the five commissioner seats. There is also a new governor in place in the state. Because of the political and regulatory developments that unfolded during the 2009 and 2010 rate proceedings, Moody's lowered FPL's score on Factor 1 in our rating methodology grid, Regulatory Framework, to the "Baa" or average category from the "A" or above average category. For more details on this and other factors in our methodology, please see Moody's Rating Methodology for Regulated Electric and Gas *Utilities, published in August 2009.*

Despite the adverse rate case outcome, FPL continues to operate under traditional rate of return regulation with strong cost recovery provisions in place in Florida. These include fuel and capacity clauses which are adjusted annually based on expected fuel and power prices and for prior period differences between projected and actual costs. FPL may also recover pre-construction and construction work in progress for nuclear capital expenditures and since 2009 has been able to recover costs associated with the utility's three new solar generating facilities. Additionally, FPL has an environmental cost recovery clause that is adjusted annually for capital spending and operating expenses related to emissions.

In December 2010, the FPSC approved a settlement agreement between FPL and most interveners that freezes base rates through 2012. It also permits the company to reduce its depreciation reserve by up to $267 million in 2010, and again by $267 million in 2011 and 2012 (plus any amounts not used in prior years), up to a total of $776 million over the term of the settlement. FPL must use at least enough of its depreciation reserve to maintain a 9% earned regulatory ROE but may not use any that would result in an earned regulatory ROE over 11%. The rate freeze does not apply to the company's cost recovery clauses and the company's midpoint for return on equity is the same as mandated in its rate case outcome at 10%. If the company's earned ROE falls below 9% at any time before December 31, 2012, the company can seek a rate adjustment. The settlement also includes a provision that caps the size of the surcharge that can be implemented to recover storm costs at $4 per 1,000 kHz of usage on residential bills, with the remainder to be recovered in later years. However, if storm costs exceed $800 million, FPL may request a higher customer surcharge.

Although the settlement freezes base rates and utilizes its depreciation reserve in lieu of higher rates, both are negatives from a cash flow and credit standpoint, it does provide regulatory clarity through 2012 and should avoid the need for additional base rate proceedings at least until the *newly constituted* FPSC *has been in place for a period of time and* has exhibited a meaningful track record.

- Strong financials, robust cash flow coverages, and low leverage

FP&L continues to exhibit some of the strongest financial performance measures and cash flow coverage ratios in the industry. These include CFO pre-working capital interest coverage in the 7.0x to 8.0x range and CFO pre-working capital to debt in the 30% to 35% range, after adjusting for the volatility caused in some years by fuel recoveries. Its debt to capitalization of 33.4% at December 31, 2010 is among the lowest in the *industry and the company maintains a fully funded pension plan, contributing to this low leverage* (as Moody's adds pension underfunding to debt).

Although cash flow coverage metrics could decline as a result of the base rate freeze, the use of its depreciation reserve, and additional debt issued to finance high capital expenditures, Moody's expects any decline in these metrics to be modest. Coverage metrics should continue to be supported by the high percentage of FP&L's revenues that are recovered through cost recovery clauses, the slow improvement of economic conditions in its service territory, and a still adequate 10% return on equity that includes a range of plus or minus 1%. As a result, Moody's anticipates that FP&L's credit metrics will continue to remain well in excess of the financial ratio parameters required for its current A2 rating.

- Challenging economic conditions in service territory are showing some signs of improvement

After several years of high residential sales growth rates averaging of 2% annually in some years, FP&L's service territory experienced a significant economic slowdown beginning in 2007, resulting in much lower customer growth rates and lower usage per retail customer. The company's retail customer growth was only 0.3% in 2008 with the situation worsening in 2009 with a decline of retail customer sales of 0.2%, before a slight 0.5% improvement in 2010. The company expects positive customer growth to continue in 2011, although below the 1.6% average rate over the last 10 years. The challenging Florida economy was a contributing factor to the company's 2009 and 2010 rate case proceedings, with the FPSC exhibiting sensitivity to economic conditions in the state during the rate hearings and throughout the rate proceedings. Unless the Florida economy improves, Moody's believes it will likely continue to remain a potential issue in future rate proceedings.

- High capital expenditure requirements, especially in 2011 and 2012, mostly for new generation

FPL has sizeable capital expenditure program that peaks in 2011 and 2012 as the company adds new conventional generation, modernizes two existing plants, and increases capacity at its two nuclear plant sites. Total capital expenditures are projected to increase to $3.3 billion in 2011 (including $1.5 billion for new generation) and $3.6 billion in 2012 ($1.9 billion for new generation), up from $2.5 billion in 2010 ($1.1 billion for new generation). FPL is in the process of constructing West County Unit 3, a 1,220 MW natural gas-fired combined-cycle plant that is expected to be in service by mid-2011. As part of its rate settlement, incremental cost recovery through FPL's capacity clause for the plant is permitted up

FPL's Response to Staff's 1ST Set of POD # 5 to the amount of the projected fuel savings for customers during the term of the settlement. FPL expects to recover all costs associated with construction of the plant. In addition, FPL is modernizing its existing Cape Canaveral and Riviera Beach power plants, which are scheduled to be completed by 2013 and 2014, respectively. When finished, each plant is expected to provide 1,200 MW of capacity. FPL is also in the process of adding between 400 MW and 460 MW of capacity through uprates at its St. Lucie and Turkey Point nuclear plants. In addition to the spending for new and existing generation, FPL's capital expenditure estimates also includes funds for transmission and distribution investments and for nuclear fuel.

Liquidity Profile

FPL maintains a strong liquidity profile with a total of $3.3 billion of mostly unused bank credit facilities that expire in 2013 (except for $17 million expiring in 2012 and $250 million expiring in 2014). The company had $20 million of cash on hand as of December 31, 2010, down from $83 million at December 31, 2009. Commercial paper outstanding at December 31, 2010 totaled $101 million, down from $818 million at the end of 2009. The company also had $8 million of letters of credit outstanding. FPL's bank revolving credit facilities are also available to support the purchase of $633 million of pollution control, solid waste disposal, and industrial development bonds in the event they are tendered to the company and not remarketed.

FPL's cash flow has been strong (totaling $1.9 billion in 2010) but variable in recent years due to large regulatory deferrals in some years caused by storm damages and high fuel costs. High capital expenditures of $3.3 billion in 2011 and $3.6 billion in 2012 will continue to require some external debt financing, which the company generally does with first mortgage bonds. FPL has a very manageable $45 million of long-term debt coming due within the next twelve months. The company has no material adverse change clause in its bank credit agreements and is in compliance with the 65% debt to capitalization financial covenant contained in these agreements as of December 31, 2010, the calculation of which it does not make public.

Rating Outlook

The stable rating outlook reflects the regulatory clarity provided by its two year rate settlement and Moody's view that the political and regulatory environment for investor owned utilities in Florida will not deteriorate further and may improve once the newly constituted FPSC begins to establish a track record. It also reflects the generally strong cost recovery provisions that are in place in the state and our expectation that FPL's financial performance measures and cash flow coverage metrics will remain strong for its rating.

What Could Change the Rating - Up

An upgrade could be considered if there is an improvement in the political and regulatory environment in Florida, which may not be evident until the utility files its next rate case following the expiration of its two year rate freeze at the end of 2012. An upgrade could also be considered if there is significant improvement in economic conditions in FPL's service territory. Upward movement of FPL's ratings is constrained by the utility's limited geographic diversity, ongoing exposure to event risk caused by storms in its service territory, and its substantial near term capital expenditure program.

What Could Change the Rating - Down

A downgrade could be considered if the political and regulatory environment for investor owned utilities declines further, if there are significant cost disallowances or other changes to Florida's currently strong cost recovery provisions, or if there is a sustained decline in cash flow coverage metrics, including CFO pre-working capital interest coverage below 5.0x and CFO pre-working capital to debt below 25%, or an increase in debt to capital above the 40% range.

Rating Factors

Florida Power & Light Company

Regulated Electric and Gas Utilities Industry [1][2]	Current 12/31/2010		Moody's 12-18 month Forward View* As of April 2011	
Factor 1: Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Regulatory Framework		Baa		Baa
Factor 2: Ability To Recover Costs And Earn Returns (25%)				
a) Ability To Recover Costs And Earn Returns		A		A
Factor 3: Diversification (10%)				
a) Market Position (5%)		Baa		Baa
b) Generation and Fuel Diversity (5%)		Baa		Baa
Factor 4: Financial Strength, Liquidity And Key Financial Metrics (40%)				
a) Liquidity (10%)		A		A
b) CFO pre-WC + Interest/ Interest (3 Year Avg) (7.5%)	7.8x	Aa	7.5 - 8.5x	Aa
c) CFO pre-WC / Debt (3 Year Avg) (7.5%)	34.1%	Aa	35 - 40%	Aa
d) CFO pre-WC - Dividends / Debt (3 Year Avg) (7.5%)	30.2%	Aa	30 - 35 %	Aa
e) Debt/Capitalization (3 Year Avg) (7.5%)	35.2%	A	30 - 35%	A
Rating:				
a) Indicated Rating from Grid		A2		A2
b) Actual Rating Assigned		A2		A2

Staff 000152
FPL RC-12

* THIS REPRESENTS MOODY'S FORWARD VIEW; NOT THE VIEW
OF THE ISSUER; AND UNLESS NOTED IN THE TEXT DOES NOT INCORPORATE SIGNIFICANT ACQUISITIONS OR DIVESTITURES

[1] All ratios are calculated using Moody's Standard Adjustments. [2] As of 12/31/2010(L); Source: Moody's Financial Metrics

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SPECIAL COMMENT

U.S. Electric Utilities: Uncertain Times Ahead; Strengthening Balance Sheets Now Would Protect Credit

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» The U.S. electricity sector's credit outlook appears stable for the next 12 to 18 months, but the industry faces longer-term risks related to increasingly strict environmental mandates and elevated capital investment requirements.

» We see little evidence that electric companies are proactively strengthening their balance sheets and bolstering liquidity reserves to prepare for more challenging business conditions. We'd likely view such proactive action as a credit positive.

» We expect growth in outstanding debt to outpace utilities' cash flow, which could contribute to a decline in projected financial credit metrics that could eventually pressure company ratings.

» Concerns that consumers would resist steadily rising electric rates in a low inflation, high unemployment economy could cause regulators to limit utilities' ability to recover their costs from consumers. If utilities object, a more contentious regulatory environment might arise.

Overview

The U.S electric utility sector is quickly approaching a crossroad, where the 20th century business model of providing universal access for affordable and reliable power ("socialized power costs") is shifting to the 21st century model of consumer empowerment and cleaner power supplies. This transition requires a less carbon-intensive generation fleet and a modernized transmission and distribution grid that provides real time data to consumers. The shift has already begun, whether utilities acknowledge it or not.

To facilitate such a transition, the long-standing system that allows utilities to recover their capital investment costs, plus a reasonable rate of return, from consumers through electricity rates will need to change. Change could come through increased use of specific cost trackers or other suites of recovery adjustment mechanisms. Regardless, it appears that higher costs for end-use consumers are coming.

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But a sustained period of sluggish economic growth, characterized by high unemployment, could stress the sector's recovery prospects, financial performance and credit ratings. The quality of the sector's cash flows are already showing signs of decline, partly because of higher operating costs and investments. Utilities also appear reluctant to issue equity as a principal form of financing.

Nevertheless, we continue to incorporate a view that utilities tend to place a high priority on their existing rating categories, and therefore are more prone to take defensive actions. One of the more defensive actions to prepare for more challenging business conditions, and which resides squarely within the control of the boards of directors, is to strengthen the balance sheets (by issuing equity or selling noncore assets to reduce debt) and bolstering their liquidity sources (by issuing debt to raise cash or establishing new, incremental credit facilities).

This Special Comment addresses what we believe to be some of the bigger financial, regulatory and environmental risks facing electric companies today.

TABLE 1
Illustrative Sub-Sector Financial Profile (3-Year Average Totals: 2007 – 2009)

($ billions)	Parent	Vertically	T&D	G&T	Muni*	Merchant
Revenue	$392.1	$185.0	$82.4	$12.3	$44.5	$88.9
Taxes	$10.2	$5.4	$1.4	$ -	$ -	$2.9
CFO	$73.3	$36.6	$12.9	$1.4	$10.3	$16.4
Cap Ex	$80.0	$44.1	$11.5	$2.9	$ -	$12.0
Div	$17.3	$8.0	$4.3	$ -	$ -	$36.6
FCF	$(24.0)	$(15.5)	$(2.9)	$(1.5)	$ -	$(8.2)
Debt	$452.5	$177.9	$78.3	$22.9	$81.3	$104.6
Equity	$265.3	$155.5	$62.4	$4.8	$ -	$50.8
PP&E	$672.7	$372.7	$120.2	$22.8	$206.1	$124.4
Assets	$1,086.9	$516.0	$208.1	$31.8	$ -	$228.8

Source: Moody's

* Comprised of both municipal electric utility systems and Joint Power Authorities. Moody's estimates.

Defending the Ratings

The electricity sector faces a sustained period of elevated capital investment needs, due largely to increasingly stringent environmental mandates. Utilities will also need to adjust their business plans to meet new requirements associated with a modernized, digital grid that provides a two-way flow of information. Investment decisions relating to long-lived infrastructure assets are complicated by shifting legal frameworks and flip-flopping political agendas.

A prolonged weak economy is likely to threaten utilities' ability to recover costs in a timely manner, especially as we expect 3% to 5% annual rate increases over the next few years with little evidence of inflation. The result could be a more contentious regulatory environment - a scenario we currently don't incorporate into our ratings and rating outlooks, but one we view as a potential risk.

Despite these concerns, we believe the regulated utilities are better positioned to deal with a more uncertain future than non-regulated, merchant power generators, which typically sell electricity on the wholesale market. Merchants, which aren't regulated by local authorities, can't seek direct recovery of their costs from consumers plus a reasonable return. Their financial profile is declining more quickly due to a sustained period of low commodity prices. We've downgraded many of the pure non-regulated merchant power companies over the past year, due largely to our revised expectations for a sustained period of weak cash flow compared to outstanding debt.

We believe the hybrid companies, which own both regulated utilities and non-regulated merchant generation, may increasingly be pressured by their boards of directors to choose a focus. We actually see some political / regulatory risks, especially in cases where the regulated utilities appear to be supporting, perhaps indirectly, the non-regulated business activities. These non-regulated affiliated generators are also suffering under today's low commodity prices, while utilities benefit from reduced purchased power costs. Still, we haven't taken significant rating actions on the hybrid parents or the affiliated generators yet, as most are better positioned within their respective rating categories than the pure merchants. Moreover, we believe most of these hybrid companies may be more willing to defend their existing ratings and they tend to have a wider variety of financing alternatives to achieve that goal. But with an expected period of sustained low commodity prices, their financials might need some infusion of equity, reduction of debt or a revision to dividend policy.

We have taken several negative rating actions on the generation and transmission cooperative utilities. These G&T cooperatives, which generally control their own rate setting authority, have experienced deterioration in their financial profiles, often due to large capital expenditure requirements. Their self-determined rate increases don't appear to be fully covering their elevated costs. Ratings are not being defended, as many G&T cooperatives appear reluctant to fully raise the rates on their own distribution members due to the tough economic environment. This could be a potentially leading indicator for what might soon transpire in the investor-owned sector.

The municipally owned electric utilities continue to enjoy relatively high ratings and stable rating outlooks, even though they also face the same issues as their investor-owned utility peers. These municipal systems generally have autonomous rate-setting flexibility, and for some, costs are back-stopped by property tax authority. Nevertheless, we need to monitor their behavior to see whether rate increases are actually coming with enough regularity to maintain their own financial metric thresholds. This is especially the case given the weak economy, where many municipally owned systems are increasing their transfer payments to municipal governments' general funds in an effort to hold down property taxes. But in times of financial distress, we believe a municipal authority will intervene to support its local utility system.

Strengthening the Balance Sheet and Bolstering Liquidity

Of all the factors that contribute to the sector's rising business and operating risk profile, only the financial and liquidity profile remains squarely in control of management, and more accurately, the board of directors. But we see little evidence that boards are instructing their management teams to pursue material steps to proactively strengthen their balance sheets.

We observe that vertically integrated utilities[1] have produced remarkably stable financials over the past seven years. However, the financial health would likely weaken if we enter a period of increasingly contentious regulatory relations, perhaps due to a prolonged weak economy. Cash flows appear to be more stressed, especially if we exclude the benefits of certain stimulus implications. Debt is rising, both

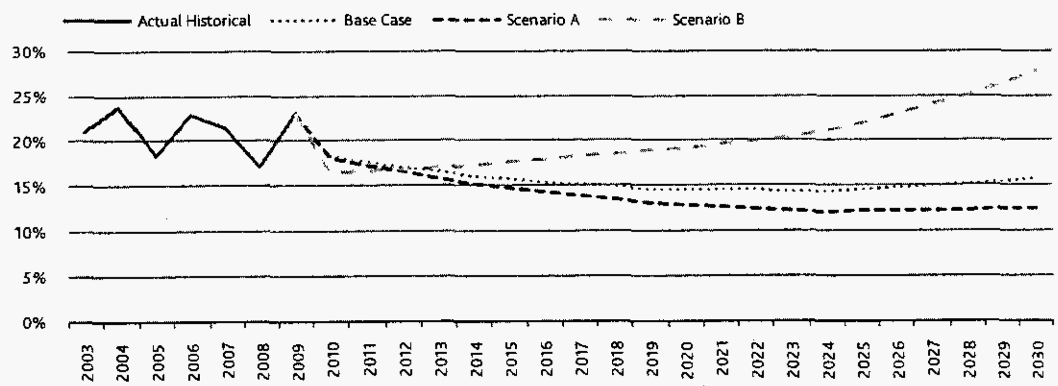
[1] Includes about 60 vertically integrated electric utilities.

due to the negative free cash flow generation, but also due to expected increases in underfunded pension obligations.

By taking a look at the pure, vertically integrated electric utility sub-sector and using some simple straight line projection assumptions regarding annual volume growth (1% - 2.5%), annual rate increases (2% - 5%), and a steady relationship of cash flow from operations (CFO) to revenue (17% - 20%), we forecast a worrisome decline in the CFO to debt metrics.[2]

Of course, these projections provide only a single perspective. Projected metrics are subject to our assumptions regarding capital expenditures, which we keep elevated under all three scenarios. The financial metrics are most positive under Scenario B, where we assume 2.5% annual volume growth and 5% annual rate increases, but the estimated all-in costs to residential consumers (as a percentage of their estimated annual disposable income) rises to an alarmingly high level of almost 10%. We don't, however, believe that scenario is likely given today's weak economy and high (real) unemployment.

CHART 1
Cash Flow to Debt



Source: Moody's

Today, we still view the vast majority of utilities as well-positioned within their respective rating categories, so a modest decline in credit metrics shouldn't immediately trigger rating downgrades. More importantly, we believe utilities will revise their corporate finance policies to defend their existing ratings. But a prolonged period of financial deterioration - a scenario we view as increasingly likely without a change to these corporate finance policies - would eventually lead to rating downgrades. This is especially the case for the hybrid parents, where consolidated financial results are being dragged down by their non-regulated merchant generation activities and where dividend payouts partly rely on their cash flows. Hybrids already have an elevated business and risk profile.

The capital markets remain open and welcoming for the vast majority of regulated utilities, a significant credit positive. The higher the credit rating, the better the access. We believe many companies could take advantage of this access, and of their existing banking relationships, to bolster their liquidity sources while they can. Tapping today's low interest rates with sizeable debt offerings, which can be used to either pre-fund maturities over the next two to three years, resolve increasingly large underfunded pension obligations, or sit on the balance sheet for general corporate purposes

[2] A summary of the assumptions for our different scenarios is included in Appendix A.

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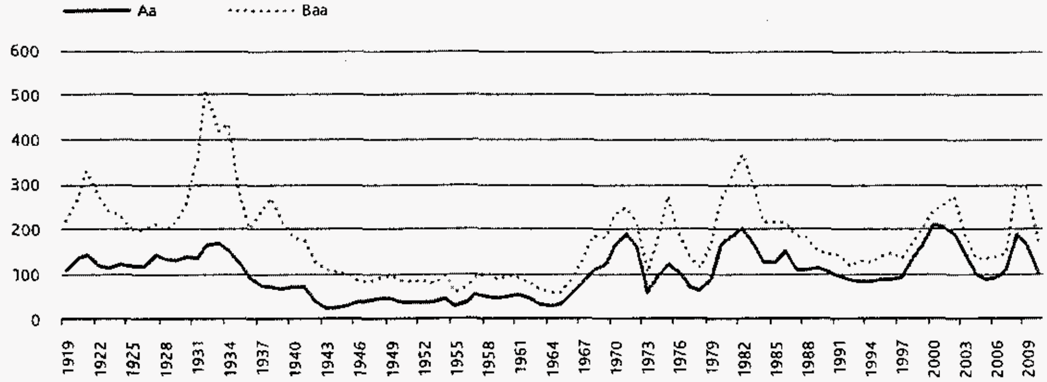
would most likely be viewed as a credit neutral event, or even a positive one. This would be especially true for those companies that are already well positioned (or strongly positioned) within their respective rating categories.

CHART 2
Utility Bond Yield Spread Over 30-Year Treasury



Source: Moody's

Increased liquidity could also help utilities offset any negative credit implications associated with a temporary deterioration in CFO-to-debt credit metrics. Should the sector suddenly find itself without a ready source of external capital (which we view as unlikely today), ratings could be impacted. Mismanaging liquidity is one of the fastest ways a company, including a seemingly sound one with a strong business model, can trigger multi-notch rating downgrade or even a default.

Managing Regulatory Relationships

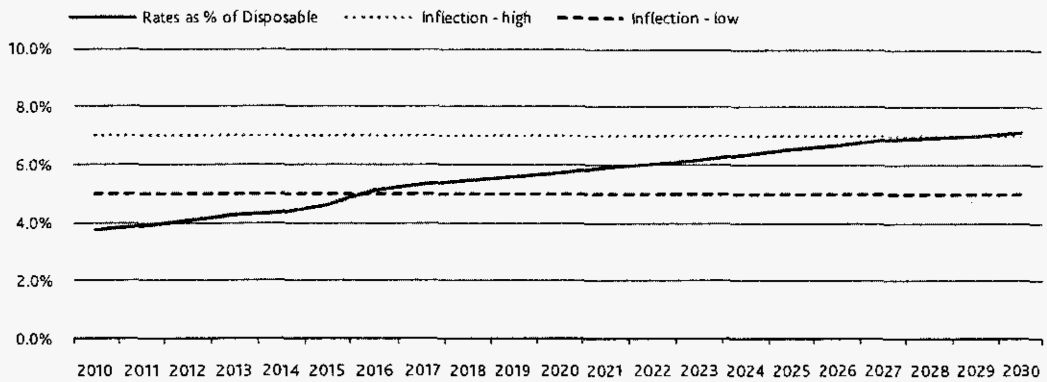
A utility's regulatory environment and suite of rate recovery mechanisms are among the most critical elements of our credit rating analysis. We believe the existence of regulation (and a utility's corresponding business model) provide relatively predictable and stable revenues and cash flows for years to come. As a result, regulated utilities can attain investment grade ratings with a much weaker financial profile than most of their capital-intensive, industrial peers.

Today, we continue to believe regulators will provide timely recovery of prudently incurred costs and investments with a reasonable return. We also believe regulators would prefer to regulate financially healthy utilities. This doesn't mean utilities are likely to receive 100% of their rate relief requests or that we'd view anything but full cost recovery as a negative. We think the vast majority of regulatory outcomes will be, at a minimum, neutral and more likely slightly positive to a utility's credit profile.

Yet we believe consumers are likely to eventually balk if their annual average electricity bills continues to rise while their incomes remain stagnant. Our opinions associated with this potential risk can be summarized in a ratio of annual residential electricity costs divided by annual disposable income. We refer to this as the inflection point, and it's about 3.5% today, but it varies by region. We are also incorporating a view that consumers would start seriously complaining to their elected officials when this inflection point breaches 5% and approaches 7%.

CHART 3

Projected annual residential electric costs as a % of projected disposable income



Once a chorus of complaints begins, we believe elected officials would quickly press the local regulators (who are, by definition, political, due to their own elections or appointments by elected officials) to limit a utility's financial recovery. This could take the form of lower authorized returns on equity (ROE) or increasingly large deferred balances, which might only postpone future rate hikes. On the heels of the recent Florida regulatory developments (which we continue to evaluate), we are also monitoring Georgia Power's large rate request in Georgia for guidance, given that state's longstanding support for the regulated utility sector. We're also watching Ohio's next round of regulatory restructuring initiatives, developments in California, and the sizeable rate request underway in the economically challenged state of New Mexico, just to name a few.

We increasingly believe the ROE that regulators approve for utilities will slowly decline over the next few years, perhaps to a point where the sector's average authorized ROE consistently falls below the 10% threshold. This falling ROE is due, in part, to our expectation that today's low interest rate environment will continue to reduce a company's all-in cost of capital[3]. But we still don't think ROE is as important as a utility's cash flow, although we acknowledge that equity returns will influence management and board behavior. Absent adequate returns, utilities might begin to pare back their regulated investments, theoretically in pursuit of better returns elsewhere. Regulators could also implement more formulaic rate structures, giving utilities better visibility into future ROE. We believe most utilities would prefer the certainty of a lower earned return than the uncertainty of a potentially higher allowed return.

Additionally, we think the popularity of specific cost and recovery trackers and the certainty they provide for utility profits causes regulators to view the utility business as having a fundamentally lower risk profile than other types of capital-intensive companies. A formulaic rate structure would also likely be perceived by regulators as contributing to a lower business and operating risk profile. We generally agree with this argument, especially when comparing the electric sector to non-regulated corporate industrial peers. In addition, a more material revision to rate structure might help utilities transition their business plans to better empower customers to control their electricity use. With increased consumer empowerment, the political pressure associated with steadily rising rates could be mitigated.

FPL's Response to Staff's 1st Set of POD #18

[3] See the section on open and welcoming capital markets noted above.

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Reducing Emissions

The prospect of increasingly stringent environmental mandates continues to represent a critical credit issue, despite the outlook for a material delay in comprehensive legislation pertaining to climate change (formerly known as global warming).

We continue to view comprehensive, federal environmental legislation as preferable to the current patchwork system of regulations emanating from numerous federal, state and local regulators. We remain concerned that the current patchwork of regional approaches would cause complications for large, multi-state utility holding companies. We also believe the Environmental Protection Agency (EPA) will continue to push for reduced emissions standards. Empowered by certain U.S. Supreme Court rulings, the rules the agency has proposed, but not yet fully implemented, are likely to raise operating costs for most large, coal-fired generation fleets. These increased costs will not be accompanied by increased electricity production volumes, so the benefits are less tangible. We believe regulators will provide recovery of these costs for the regulated utilities, but recovery by the non-regulated merchants is not assured. Nevertheless, as we mentioned above, the economy could contribute to an environment where recovery may not be as timely, especially if consumers object forcefully to their elected officials.

Additional Credit Considerations

Catalyst Needed to Spur Consolidation

The industrial logic behind consolidating homogenous, capital-intensive companies like electric utilities can spread fixed costs across a larger asset base is sound. We expect to see a continued steady pace of merger and acquisition activity. We believe the economics of a transaction and social issues remain the most important consolidation criteria. Regulators look most favorably on tie-ups that can limit annual rate increases. Non-regulated merchant power consolidation is also expected to continue, perhaps at an even quicker pace as the costs associated with increasingly stringent emission regulations become more clear.

Sustained Period of Low Energy Commodity Prices

In our opinion, a modest shift in the generation supply mix that results from older coal plants closing permanently or temporarily isn't likely to trigger a material change in demand for coal or natural gas that significantly alters the prices of those commodities. Nevertheless, we see natural gas as the fuel of choice for generators that can use multiple fuel types because natural gas emits half the carbon dioxide as coal. Natural gas plants are also faster and less expensive to build than many other types of generators. We expect natural gas prices to remain low, around $4.50 to $5.00/million cubic feet for the next few years. But natural gas prices can be volatile and cause consumers' rates to jump, as regulators typically allow utilities to pass fuel price increases onto customers.

This view, that commodity prices remain low, could easily be proved incorrect, due to the evidence of historical volatility. Low commodity prices can help delay the arrival of the inflection point; but should prices quickly rise, the impact on consumers could be more acute (given the all-in rate increases that were mitigated by lower commodity prices). As we've discussed above, regulators could limit utilities' cost recovery.

Nuclear Development Appears to Have Slowed

We view nuclear development, by itself, as neutral to regulated utilities' credit quality as long as companies take actions that mitigate their higher business and operating risk profile. We believe regulators and lawmakers will continue to support new projects and allow developers to recover their costs through a variety of mechanisms, including the costs of construction work in progress in rates. Still, utilities must bolster their balance sheets and liquidity sources to mitigate their elevated risk, given the long term nature of construction and execution risks .

Conclusion

We see a disconnect developing between our stable 12-to-18-month outlook - which assumes supportive regulatory relationships and utilities adjusting their financial policies to maintain cash flow credit metrics – and material increases to the longer-term industry risk profile. Utilities' free cash flow and credit metrics appear to be declining. Yet regulators, pressured by consumers and legislators, won't allow rates to rise indefinitely. If conditions become more challenging due to stagnant economic growth and continued high employment, companies that fortified their balance sheet and secured access to ample supplies of liquidity are likely to fare better as their weaker counterparts struggle. Companies are best-equipped to take steps to defend their credit ratings when the companies aren't under pressure.

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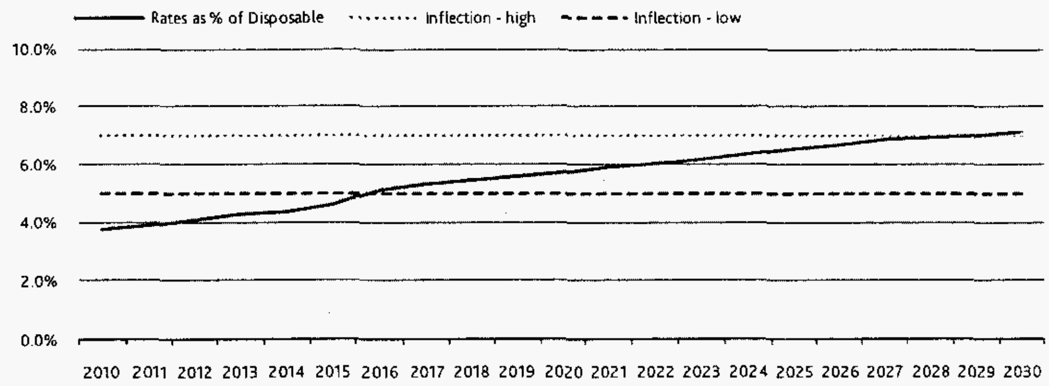
CHART 3

Projected annual residential electric costs as a % of projected disposable income



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