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BEFORE THE  
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of:

DOCKET NO. 140001-EI

FUEL AND PURCHASED POWER COST  
RECOVERY CLAUSE WITH GENERATING  
PERFORMANCE INCENTIVE FACTOR.

FILED DEC 03, 2014  
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FPSC - COMMISSION CLERK

VOLUME 5

Pages 536 through 662

PROCEEDINGS: HEARING

COMMISSIONERS  
PARTICIPATING:

CHAIRMAN ART GRAHAM  
COMMISSIONER LISA POLAK EDGAR  
COMMISSIONER RONALD A. BRISÉ  
COMMISSIONER EDUARDO E. BALBIS  
COMMISSIONER JULIE I. BROWN

DATE: Monday, December 1, 2014

TIME: Commenced at 9:12 p.m.  
Concluded at 10:47 p.m.

PLACE: Betty Easley Conference Center  
Room 148  
4075 Esplanade Way  
Tallahassee, Florida

REPORTED BY: DEBRA R. KRICK  
Court Reporter and  
Notary Public in and for the  
State of Florida at Large

PREMIER REPORTING  
114 W. 5TH AVENUE  
TALLAHASSEE, FLORIDA

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I N D E X

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

2 CHAIRMAN GRAHAM: All right. My clock back  
3 there says we are two minutes past time,  
4 Mr. Butler, Mr. Moyle.

5 MR. BUTLER: The good news is it was  
6 productive. We concluded that the portion that Mr.  
7 Moyle wants to ask about out of the SF-4, we don't  
8 need to maintain confidentiality for it, so it's  
9 fine for him to discuss it on the record with  
10 Dr. Taylor.

11 CHAIRMAN GRAHAM: All right. Thanks.

12 MR. MOYLE: I am sorry to be duplicative. It  
13 is in the redacted depo, but thanks for letting us  
14 sort through it.

15 CHAIRMAN GRAHAM: That's all right.

16 Whereupon,

17 DR. TIM TAYLOR

18 was recalled as a witness, having been previously duly  
19 sworn to speak the truth, the whole truth, and nothing  
20 but the truth, was examined and testified as follows:

21 CONTINUED CROSS EXAMINATION

22 BY MR. MOYLE:

23 Q I think the pending question, Mr. Taylor was  
24 asking you to publish by reading the portion of, I think  
25 it's page 65 before you, starting after the handwritten

1 **star that I put in and going until the next page, where**  
2 **you find the handwritten star.**

3 A Okay.

4 "In addition, there are no warranties or  
5 representations expressed or implied as to the accuracy  
6 or completeness of any of data, information or material  
7 heretofore or hereafter furnished in connection with the  
8 assets as to the quality or quantity of possible  
9 hydrocarbon reserves, if any, attributable to the  
10 interest herein assigned, or the ability of the assets  
11 to produce hydrocarbon. And any and all data,  
12 information and material, furnished by assignor is  
13 provided as a convenience only, and any reliance on or  
14 use of the same is at assignees sole risk and expense.  
15 Assignor makes no warranties or representations,  
16 expressed or implied, with respect to the environmental  
17 condition of the assets, and any and all representation  
18 and warranties are hereby expressly denied."

19 Q Okay. So with respect to the first part that  
20 you read, about the data, where they are basically  
21 saying, we are not making any reps or warranties with  
22 respect to that, is that how you understand that  
23 language?

24 A This is standard industry boilerplate  
25 contractual language, and I have seen it many, many

1 times before. It doesn't mean that the data that they  
2 provided us is not accurate.

3 Q But this relationship is governed by  
4 contracts, correct?

5 A Yes.

6 Q Okay. And with respect to your analysis, you  
7 were not aware of this language before we talked about  
8 it this evening. Does it diminish, in any way, shape or  
9 form, your opinion with respect to the quality of these  
10 reserves?

11 A None whatsoever.

12 Q And that's because you just don't give those  
13 words much meaning, it's --

14 A No.

15 Q -- part of the business, they always put that  
16 in?

17 A As I said, it's standard industry contractual  
18 boilerplate language.

19 Q Have you ever seen a lawsuit where people were  
20 fighting over whether representations were made about  
21 whether there was gas somewhere and a provision like  
22 that was used as a defense?

23 A I haven't been involved in a lawsuit like  
24 that, but I am assuming that's why this kind of language  
25 is in here, for protection against such.

1           **Q     And then also they are not making any**  
2           **representations about in the environmental conditions in**  
3           **any of the assets, correct?**

4           A     We did our own environmental assessment.

5           **Q     Did you do your own assessment of the quality**  
6           **of the reserves in the subject property --**

7           A     Absolutely.

8           **Q     -- without relying on any information that was**  
9           **provided by PetroQuest?**

10          A     Absolutely.

11          **Q     And you did that?**

12          A     I did that, yes.

13          **Q     Where did you get your information?**

14          A     From public sources.

15          **Q     Which are what?**

16          A     Well, this -- the producers in the state of  
17          Oklahoma have to report their production on a monthly  
18          basis to the Oklahoma Corporation Commission. That data  
19          is then purchased by third parties, who put it in a  
20          format and sell it back to the industry. And that's the  
21          data that we used to confirm the production levels in  
22          each of the individual 19 wells.

23          **Q     When you say we, who is we?**

24          A     My staff and I.

25          **Q     Okay. The guidelines, on a go-forward basis,**

1 they contemplate, if you know, the possibility that when  
2 you are drilling wells in the future, that you may  
3 encounter oil as well as natural gas, right?

4 A I have no knowledge of the guidelines  
5 whatsoever. I haven't read them and I haven't been  
6 involved in them.

7 Q Okay. In your business, is it easy to say,  
8 hey, we are going to sink a well and all we are going to  
9 get is, you know, natural gas?

10 A If you are giving me a situation where 19  
11 wells have been drilled in 19 sections, and I have  
12 substantial production data from each of those wells, I  
13 can pretty much tell you what the next well is going to  
14 produce.

15 Q The -- what are NGLs?

16 A Natural Gas Liquids.

17 Q Those are different from oil, right?

18 A They are different from oil, yes.

19 Q And that's something else that comes up out of  
20 these wells, right?

21 A In some -- some gas wells contain NGLs and  
22 some do not. The Woodford Project is a dry gas project  
23 that has no NGLs.

24 Q So if PetroQuest, in their annual report,  
25 talked about the Woodford Project, and that it was being

1 attractive -- it was very attractive because it had wet  
2 liquids, would that just be wrong?

3 A No, it's not wrong at all, because the  
4 Woodford Shale covers a quite large area. And as you go  
5 further in the west, as I have described in my direct  
6 testimony, that the BTU value, and therefore, the  
7 wetness of the natural gas gets higher.

8 Q Okay. When there is a standstill decision  
9 made with respect to a well, what does that mean?

10 A Say again, please.

11 Q A standstill decision.

12 A I am not familiar with that term. I am sorry.

13 Q I thought you testified previously that  
14 sometimes when a well -- the production costs are above  
15 market costs, in your industry, they say, hey, hold on,  
16 you know, we are spending more money than we can sell  
17 this for, let's stand still, or words to that effect?

18 A No, I wasn't familiar with that term. I call  
19 it the economic limit.

20 Q And is that what I described?

21 A When the operating costs exceed the revenue  
22 generated from the sale of the commodity, that is the  
23 economic limit.

24 Q And would that take place in this situation,  
25 as you understand it, with respect to the Woodford

1 **Project if the --**

2 A The -- I am sorry.

3 **Q That's all right -- if the market price is --**  
4 **were less than the production prices?**

5 A It will eventually happen in every well that  
6 is currently producing on this planet.

7 **Q And you make an economic decision not to**  
8 **continue pumping if the production costs are higher than**  
9 **the market costs, right?**

10 A All production from -- nearly all production  
11 from oil and gas wells declines over time, and at some  
12 point in time, the operating costs will exceed the  
13 revenue. That has not happened in the Woodford Project  
14 in the 19 wells that have been -- that are currently  
15 producing.

16 **Q It also happens on a temporary basis, correct?**  
17 **Somebody, if they are out of the money, they could say,**  
18 **hold on, we are out of the money, let's wait and pick**  
19 **this back up when the market recovers?**

20 A Well, it would be sort of foolish in my mind  
21 to stop a revenue stream that is positive because you  
22 are out of money.

23 **Q Even if the revenue stream is not covering**  
24 **your production costs?**

25 A Well, then that's reached the economic limit.

1 That's a different scenario.

2 **Q Well, what are reclamation costs?**

3 A Reclamation costs refer to restoring the  
4 surface to its, as nearly as possible, its original  
5 condition before drilling operation commenced.

6 **Q What do you have to do to do that?**

7 A It depends on the area. So if you are in a  
8 forested area, and you had to cut down trees to prepare  
9 a drilling pad, at the end of the life of the well on  
10 that pad, you would have to replant some trees.

11 **Q What about when you put a hole in the ground,  
12 you would have to fill that hole back up?**

13 A Well, when we abandon that well, there is very  
14 specific rules in each state as what is required to  
15 properly abandon the well. And so, yes, you plug that  
16 hole, but it's more than just dumping cement in that  
17 hole.

18 **Q Were those costs considered in your economic  
19 evaluation?**

20 A You know, that's a good question. Sometimes  
21 it is and sometimes it's not. The assumption that we  
22 made is that the salvage value of the surface equipment  
23 would cover the abandonment cost of the well, and that's  
24 a generally accepted thing in the -- assumption in the  
25 industry.

1           **Q     That the salvage value of equipment used would**  
2 **cover your reclamation costs?**

3           A     Would cover the abandonment cost of the well,  
4 which include the reclamation costs.

5           **Q     Do you know what a 111(d) project is?**

6           A     I do not.

7           **Q     You heard Mr. Forrest reference it in terms of**  
8 **a risk earlier. Do you recall that or no?**

9           A     No.

10           MR. MOYLE: Okay. That's all I have. Thank  
11 you.

12           CHAIRMAN GRAHAM: Staff.

13           MS. BARRERA: No questions.

14           CHAIRMAN GRAHAM: Commissioners.

15           Redirect.

16           MR. BUTLER: Thank you, Mr. Chairman. Just a  
17 couple.

18                               REDIRECT EXAMINATION

19           BY MR. BUTLER:

20           **Q     Dr. Taylor, you were asked by Mr. Moyle about**  
21 **the chemical composition of the hydraulic fracturing**  
22 **fluids, do you remember that?**

23           A     I do.

24           **Q     As I recall, you didn't know precisely what**  
25 **the composition is, but do you have a -- do you have**

1 knowledge of what percentage of the hydraulic fracturing  
2 fluid typically is water?

3 A Well, it's certainly in excess of 90 percent.

4 Q Do you know generally the sorts of components  
5 that would comprise the other minority percentage?

6 A Well, Mr. Moyle asked me what some of those  
7 chemicals were, and I still could not name what some of  
8 those chemicals are. I can tell you what some of them  
9 do. They are generally emulsifiers and friction  
10 reducers and surfactants and things like that.

11 Q Okay. Thank you.

12 You were asked about item five on page 26 of  
13 30 in the Forrest Garb report. And this is -- that's  
14 exhibit TT-10, right?

15 A Yes.

16 Q Okay. And would you turn to page 26 of 30?

17 A Yes.

18 Q And if I recall correctly, the questions were  
19 directed -- this has a series of 11 numbered items on  
20 it, is it that correct?

21 A Yes.

22 Q And you were asked about number five. I don't  
23 want you to describe what it says there, because we have  
24 already taken the confidentiality -- maintaining the  
25 confidentiality of it. But the practice that's

1 **described in item five, how would you characterize it in**  
2 **terms of frequency or typicality of its use in the**  
3 **industry?**

4           A       Generally, it says that Forrest Garb &  
5 Associates accepted some of the parameters that were  
6 used in their analysis, accepted as presented, not  
7 researched on their part.

8           Q       **And how would you characterize it as to**  
9 **weather it's typical or atypical industry practice to**  
10 **accept information on that basis?**

11           A       Now, this is very typical in the industry. I  
12 mean, it doesn't behoove a company go out and -- a  
13 consulting firm to go out and try to run tests in a  
14 field. They are not allowed to do that, so -- the  
15 operating company is not going to allow them to do that.  
16 And as far as the data that they are presented, that  
17 generally comes from the operating company, or one of  
18 the partners in the operating company -- or partners in  
19 the project who have access to that data.

20           Q       **Mr. Moyle asked you also a series of questions**  
21 **about potential risks identified in the PetroQuest**  
22 **annual report. Do you recall that?**

23           A       Yes.

24           Q       **Would you please compare the potential risks**  
25 **described there to what you see as the realistic risks**

1 **associated with the Woodford Project?**

2 A Say again, please. I am sorry, I missed your  
3 question.

4 Q I asked you please to compare the potential  
5 risks that are identified in the PetroQuest annual  
6 report Mr. Moyle asked you about to your assessment of  
7 what the realistic expectation of risk for the Woodford  
8 Project are?

9 A Certainly. We looked at a number of different  
10 things when we did our analysis, and as we normally do.  
11 One is geologic risk. And so we fortunately had seismic  
12 data available to us that had been shot by PetroQuest.  
13 And so we examined that to verify there was no large  
14 faulting in the region that would interrupt or drain  
15 wells unnecessarily that were drilled near those faults.

16 We looked at the production data, of course,  
17 that came from the individual 19 wells. Those 19 wells  
18 drilled in those 19 sections gave me a huge amount of  
19 data that let me know that I was able, from that data,  
20 to forecast what I think is a reasonable expectation of  
21 future production from the undrilled wells and I think  
22 that risk is very low.

23 MR. BUTLER: Thank you, Dr. Taylor. That's  
24 all the redirect that I have.

25 CHAIRMAN GRAHAM: All right. Exhibits.

1 MR. BUTLER: Let's see, we would move the  
2 admission of Exhibit 21 through 30.

3 CHAIRMAN GRAHAM: Any objection to Exhibits 21  
4 through 30?

5 MR. MOYLE: We object to the Forrest Garb  
6 report coming in. It's hearsay. In his opening  
7 statement, he said his results were confirmed by  
8 Forrest Garb, indicating that it's being used to  
9 solidify his analysis. We think that's  
10 inappropriate. We think it's essentially  
11 shoehorning in an expert's report impermissibly and  
12 should be not allowed to come in.

13 MR. BUTLER: Mr. Chairman.

14 CHAIRMAN GRAHAM: Yes, sir.

15 MR. BUTLER: I mean, Dr. Taylor is, without  
16 any doubt, an expert in the field of economic  
17 evaluation for oil and gas properties. As such an  
18 expert, I think he made it clear that he will often  
19 look at different sources of information, including  
20 information by third parties, in completing an  
21 evaluation. That's what he did with the Forrest  
22 Garb report, and I think it falls squarely within  
23 the sort of reliable source of information normally  
24 used by experts in his field and is admissible as  
25 such.

1 CHAIRMAN GRAHAM: I will allow the report.

2 MR. BUTLER: Okay.

3 CHAIRMAN GRAHAM: Any other objections to 21  
4 through 30?

5 Okay, we will enter those into the report -- I  
6 mean, into the hearing.

7 (Whereupon, Exhibit Nos. 21 - 30 were received  
8 into evidence.)

9 CHAIRMAN GRAHAM: Somebody offered Exhibit 66.

10 MR. MOYLE: That is a FIPUG exhibit. We would  
11 move it in.

12 CHAIRMAN GRAHAM: Okay. Any objection?

13 All right. We will enter that into the  
14 record.

15 (Whereupon, Exhibit No. 61 was received into  
16 evidence.)

17 CHAIRMAN GRAHAM: Okay. Would you like to  
18 excuse your witness temporarily?

19 MR. BUTLER: I would. That would be grand.  
20 May Mr. -- may Dr. Taylor be excused temporarily?

21 CHAIRMAN GRAHAM: Thank you.

22 MR. BUTLER: Thank you.

23 (Witness excused.)

24 CHAIRMAN GRAHAM: OPC, your first witness.

25 MR. REHWINKEL: Public Counsel calls Donna

1 Ramas to the stand. Ms. Ramas have you been  
2 previously sworn?

3 THE WITNESS: Yes, I have.

4 Whereupon,

5 DONNA RAMAS

6 was called as a witness, having been previously duly  
7 sworn to speak the truth, the whole truth, and nothing  
8 but the truth, was examined and testified as follows: up

9 DIRECT EXAMINATION

10 BY MR. REHWINKEL:

11 Q Can you state your name for the record,  
12 please?

13 A Donna Ramas.

14 Q And on whose behalf are you appearing here  
15 today?

16 A The Florida Office of the Public Counsel.

17 Q Ms. Ramas, did you cause to be prepared  
18 prefiled direct testimony in this matter consisting of  
19 31 pages?

20 A Yes, I did.

21 Q Do you have any changes or corrections to make  
22 to that testimony?

23 A One minor correction. If you turn to page 15,  
24 line six, the word electric should be deleted. It  
25 doesn't make any material changes. It was just an edit

1 I didn't pick up.

2 Q Okay. With that change to your testimony, if  
3 I asked you the questions contained in your prefiled  
4 direct testimony today, would your answers be the same?

5 A Yes, they would.

6 MR. REHWINKEL: Mr. Chairman, I ask that  
7 Ms. Ramas' prefiled direct testimony be moved into  
8 the record and admitted as though read.

9 CHAIRMAN GRAHAM: We will enter Ms. Ramas'  
10 prefiled direct testimony into the record as though  
11 read.

12 (Whereupon, prefiled testimony was inserted.)

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1 **DIRECT TESTIMONY**

2 **OF**

3 **DONNA RAMAS**

4 On Behalf of the Office of Public Counsel

5 Before the

6 Florida Public Service Commission

7 Docket No. 140001-EI

8

9 INTRODUCTION

10 **Q. WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?**

11 A. My name is Donna Ramas. I am a Certified Public Accountant licensed in the State of  
12 Michigan and Principal at Ramas Regulatory Consulting, LLC, with offices at 4654  
13 Driftwood Drive, Commerce Township, Michigan 48382.

14

15 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC**  
16 **SERVICE COMMISSION?**

17 A. Yes, I have testified before the Florida Public Service Commission (“PSC” or  
18 “Commission”) on several prior occasions. I have also testified before many other state  
19 regulatory commissions.

20

21 **Q. HAVE YOU PREPARED AN EXHIBIT DESCRIBING YOUR**  
22 **QUALIFICATIONS AND EXPERIENCE?**

23 A. Yes. I have attached Exhibit DMR-1, which is a summary of my regulatory experience  
24 and qualifications.

1 **Q. ON WHOSE BEHALF ARE YOU APPEARING?**

2 A. I am appearing on behalf of the Citizens of the State of Florida for the Office of Public  
3 Counsel (“OPC”).  
4

5 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

6 A. In my testimony, I identify and comment on flaws and deficiencies in the support offered  
7 by Florida Power & Light Company (“FPL” or “Company”) for its request to flow its  
8 planned investments in natural gas exploration, drilling and production ventures, as well  
9 as production costs and a return on its capital investment, through the fuel cost recovery  
10 clause. This testimony responds, in large part, to the accounting and regulatory recovery  
11 proposals presented in the Direct Testimony of FPL witness Kim Ousdahl. While my  
12 testimony focuses on the proposed joint venture with PetroQuest to produce gas in the  
13 Woodford Shale region (hereafter referred to as the “Woodford Project”) addressed in  
14 FPL’s June 25, 2014 Petition (“Petition”), it is equally applicable to other potential such  
15 future joint venture investments by FPL.  
16

17 **Q. ARE ANY ADDITIONAL WITNESSES APPEARING ON BEHALF OF THE**  
18 **OFFICE OF PUBLIC COUNSEL IN THIS CASE?**

19 A. Yes. Mr. Daniel J. Lawton also presents testimony on behalf of OPC in this case.  
20

21 SUMMARY OF TESTIMONY

22 **Q. WOULD YOU PLEASE SUMMARIZE THE ISSUES AND**  
23 **RECOMMENDATIONS CONTAINED IN YOUR TESTIMONY?**

24 A. Yes. The ultimate issue before the Commission in this case is whether FPL should be  
25 permitted to recover costs associated with potential investments in natural gas

1 exploration, drilling and production ventures, inclusive of a return or profit on the  
2 associated capital investments, from its captive Florida electric ratepayers through the  
3 fuel cost recovery clause. This includes the Woodford Project and potential future  
4 ventures into the competitive natural gas exploration and production arena. In this  
5 testimony, I present several reasons why FPL's proposed transactions are ineligible for  
6 inclusion in the fuel cost recovery clause and why the Commission should deny FPL's  
7 Petition. Specifically, I make the following points within this testimony:

- 8
- 9 1. FPL witness Ousdahl attempts to invoke PSC Order No. 14546 in support of  
10 FPL's proposal to recover gas exploration, drilling and production  
11 investments and associated operating costs through the fuel cost recovery  
12 clause. The cited order provides no support for FPL's Petition. In Order No.  
13 14546, the Commission indicated its willingness to consider the recovery of  
14 certain costs that are "normally recovered through base rates" through the fuel  
15 cost recovery clause under certain conditions. However, capital investments  
16 in gas exploration, drilling and production joint ventures are so foreign to an  
17 electric utility's regulated monopoly business that such items are incompatible  
18 with the system of accounts that the Commission prescribes for electric  
19 utilities. It follows that such costs are not normally included in the base rates  
20 that are developed from the costs captured by the system of accounts  
21 prescribed for electric utilities. As such, these costs do not qualify for  
22 recovery through the fuel cost recovery clause under the order upon which  
23 FPL relies.

1           2. FPL proposes to venture into the extremely competitive gas drilling and  
2           production industry and obtain 100% recovery of any investments it makes in  
3           such potential ventures, including a return on the investments, until fully  
4           recovered from customers, regardless of whether the outcome of the joint  
5           venture's drilling and extraction efforts is competitive in the market for  
6           natural gas. The return on investment includes an equity return, which is a  
7           measurement of earnings (i.e., profit) applied for shareholders' benefit for the  
8           use of the investment funds they provide. This proposal would push 100% of  
9           the risk associated with FPL entering into this competitive market onto FPL's  
10          ratepayers while guaranteeing an equity return for shareholders. The fuel  
11          clause is intended to be a mechanism by which the reasonable costs of fuel  
12          procured from providers are passed on to FPL's customers. FPL wants to  
13          subvert that mechanism into a means of entering a different, competitive  
14          industry, thereby resulting in a risk-free expansion of the capital base upon  
15          which a return on equity is applied.

16  
17          3. An essential function performed by the Commission is the auditing of costs  
18          that regulated electric utilities seek to pass on to customers through either base  
19          rates or through the various annual clauses, including the fuel cost recovery  
20          clause. Yet, the Commission has no jurisdiction over, and therefore could not  
21          audit, the entity that would incur the costs that FPL would submit for  
22          reimbursement through the fuel cost recovery clause. The joint venture  
23          drilling and production costs that FPL intends to recover through the fuel  
24          clause would be incurred by its joint venture partner, which is PetroQuest for  
25          the Woodford Project, but it could be any number of yet undisclosed partners

1 for future joint ventures under FPL's request. The Commission has no  
2 jurisdiction over PetroQuest or any other potential future operating entities in  
3 the joint ventures. The Commission and its audit staff would not have the  
4 authority to audit the costs incurred by these non-regulated entities that fall  
5 outside of its jurisdiction. While FPL states that it would have the ability to  
6 audit PetroQuest's books under the contractual agreement, this is essentially  
7 asking the Commission to delegate its fundamental regulatory auditing  
8 functions to the very utility that is seeking authority to recover the costs.

- 9
- 10 4. The ability to effectively perform this vital auditing function would be further  
11 hampered by the highly specialized and unique form of energy accounting  
12 FPL would apply to the proposed gas exploration, drilling and production  
13 activities. FPL would not be using the FERC electric or gas chart of accounts  
14 in accounting for the activities. The highly specialized and unique form of  
15 energy accounting differs so greatly from the Federal Energy Regulatory  
16 Commission Uniform System of Accounts ("FERC USOA" or USOA"),  
17 which is prescribed by the Commission for electric utilities subject to its  
18 regulation, that FPL has indicated it would need to outsource the associated  
19 accounting, recordkeeping and related functions to an outside third party  
20 having the requisite experience in such specialized requirements. According  
21 to FPL, it would be required to apply the "successful efforts" method of  
22 accounting because its unregulated affiliate, USG, applies this method of  
23 accounting to its oil and gas production activities. The application of a highly  
24 specialized accounting method that differs from the FERC USOA that the  
25 Commission's auditors are familiar with and specialize in would add

1 regulatory risk to consumers by complicating the ability to provide effective  
2 auditing oversight.

3  
4 5. In analogous circumstances, the Commission adopted a market price test to be  
5 applied to transactions between Florida Power Corporation (now Duke  
6 Energy, Inc.) and Tampa Electric Company and their coal mining affiliates.  
7 In fact, the Commission has established, as a general policy, that where a  
8 market for the product is reasonably available, market-based pricing of  
9 affiliates' fuel services shall be used for purposes of fuel cost recovery. Under  
10 its general policy, the Commission should make it abundantly clear to FPL  
11 that if FPL purchases gas from a subsidiary participating in a joint venture  
12 with PetroQuest, the amount to be recovered from customers through the fuel  
13 clause will be limited to the market price of gas.

14  
15 6. While I strongly disagree with FPL's position that the capital investments of  
16 its yet-unnamed subsidiary in a joint venture with PetroQuest (and other  
17 potential future joint ventures with other unaffiliated operating entities) are  
18 recoverable through the fuel cost recovery clause; if the Commission decides  
19 to consider FPL's request, it should protect ratepayers from bearing undue risk  
20 by limiting any recovery of the resulting investments and associated costs  
21 through the fuel cost recovery clause to actual fuel savings demonstrated by  
22 FPL.

1 APPROPRIATENESS OF CLAUSE RECOVERY

2 **Q. PLEASE COMMENT ON MS. OUSDAHL'S ASSERTION THAT THE**  
3 **PROPOSED VENTURES INTO THE NATURAL GAS EXPLORATION,**  
4 **DRILLING AND PRODUCTION BUSINESS ARE APPROPRIATE FOR**  
5 **RECOVERY THROUGH THE FUEL COST RECOVERY CLAUSE.**

6 A. Ms. Ousdahl's assertion is incorrect. At page 22 of her testimony, Ms. Ousdahl asserts  
7 that Item 10 of PSC Order No. 14546 "...provides that Fuel Clause recovery is  
8 appropriate for projects that are intended to lower the delivered price of fuel when those  
9 costs were 'not recognized or anticipated in the cost levels used to determine current base  
10 rates.'" She claims, at page 23 of her testimony, that "The Woodford Project clearly and  
11 directly meets the test for Fuel Clause recovery set forth in Order No. 14546." She also  
12 asserts that this project "...is intended to lower the delivered price of natural gas that FPL  
13 burns in its generating units" and that "...there was neither recognition nor anticipation of  
14 gas reserve project costs in the 2013 test year that formed the basis for FPL's current base  
15 rates."

16

17 **Q. WHAT EXACTLY DOES ORDER NO. 14546 INDICATE IN THE ITEM**  
18 **REFERENCED BY MS. OUSDAHL?**

19 A. Order No. 14546, issued on July 8, 1985 in Docket No. 850001-EI-B, states that: ". . .  
20 the following charges are properly considered in the computation of the average  
21 inventory price of fuel used in the development of fuel expense in the utilities' fuel cost  
22 recovery clauses:..." It then goes on to list 10 separate items. Item 10, which is  
23 specifically invoked by Ms. Ousdahl in her testimony, states as follows:

24 Fossil fuel-related costs normally recovered through base rates but which  
25 were not recognized or anticipated in the cost levels used to determine  
26 current base rates and which, if expended, will result in fuel savings to

1 customers. Recovery of such costs should be made on a case by case basis  
2 after Commission approval.  
3  
4

5 **Q. IN YOUR OPINION, DO THE PROPOSED VENTURES INTO NATURAL GAS**  
6 **EXPLORATION, DRILLING AND PRODUCTION REQUESTED BY FPL FOR**  
7 **RECOVERY IN THE FUEL COST RECOVERY CLAUSE FALL UNDER ITEM**  
8 **10 OF ORDER NO. 14546?**

9 A. No, they do not. Item 10 clearly indicates that it applies to fuel related costs "...normally  
10 recovered through base rates..." Investments in gas exploration, drilling and production  
11 clearly do not fall under items that would be "normally recovered through base rates" for  
12 regulated electric utilities. In fact, as addressed later in this testimony, the USOA for  
13 electric utilities that FPL is required to follow under Commission Rule 25-6.014 is not  
14 even applicable to the highly specialized accounting utilized in the oil and gas production  
15 industry. The oil and gas production industry is a highly competitive industry, not a  
16 monopoly function of an electric utility regulated by the Commission.

17  
18 Additionally, Item 10 of Order No. 14546 also contains the requirement that the items  
19 "...will result in fuel cost savings to customers." (emphasis added) As addressed in the  
20 Direct Testimony of OPC witness Lawton, the unrealistic assumptions and other  
21 deficiencies in FPL's effort to identify potential savings from the joint venture render it  
22 unreliable and insufficient to meet the standard of Item 10.

23  
24 **Q. AT PAGE 22 OF HER TESTIMONY, MS. OUSDAHL REFERS TO SEVERAL**  
25 **OTHER CASES IN WHICH THE COMMISSION PERMITTED FPL TO**  
26 **RECOVER COSTS FOR CAPITAL PROJECTS THROUGH THE FUEL COST**  
27 **RECOVERY CLAUSE. ARE ANY OF THE SITUATIONS IDENTIFIED BY MS.**

1           **OUSDAHL SIMILAR TO THE PROJECTS PROPOSED BY FPL IN ITS**  
2           **PETITION?**

3    A.    No. The cases identified by Ms. Ousdahl pertain to: 1) the inclusion of a gas pipeline  
4           lateral to an FPL-owned generation facility until the lateral could be incorporated into  
5           base rates (Order No. PSC-93-1331-FOF-EI); 2) the acquisition in lieu of the leasing of  
6           rail cars used to deliver coal to an FPL generation facility (Order No. PSC-95-1089-FOF-  
7           EI); and 3) the costs associated with modifications to existing generation plants and fuel  
8           storage facilities to allow for the use of less expensive fuel oil at the facilities (Order No.  
9           PSC-97-0359-FOF-EI). None of the examples provided by Ms. Ousdahl are analogous to  
10          the investments in gas exploration, drilling and development ventures proposed by FPL  
11          in this case. Instead, all of them are examples of utility system improvements made to  
12          facilitate the regulated utility's economical *purchases* of fuel from providers.

13  
14    **Q.    ARE THERE ADDITIONAL KEY DISTINCTIONS BETWEEN THE ASSETS**  
15          **ADDRESSED IN THE CASES IDENTIFIED BY MS. OUSDAHL AND THE**  
16          **PROJECTS PROPOSED BY FPL IN THIS CASE?**

17    A.    Yes, there are. The examples identified by Ms. Ousdahl address assets that would be  
18          placed into utility plant accounts under the FERC USOA. FPL and its subsidiary are not  
19          proposing to record the investments in gas exploration, drilling and development ventures  
20          in Plant in Service accounts that fall under the FERC USOA. Rather, the initial  
21          investment would be recorded in accounts titled "Unproved Property Acquisition Costs"  
22          and "Proved Property Acquisition Costs."<sup>1</sup> A sample balance sheet provided by FPL as  
23          Exhibit KO-5, page 2 of 2, shows that the investments would be included in "Gas  
24          Reserves Investment." Similarly, the sample Fuel and Purchase Power Recovery Clause

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<sup>1</sup> Exhibit KO-3, which is attached to the Direct Testimony of FPL witness Ousdahl.

1 schedule provided by FPL in Exhibit KO-6 identifies the projects as investments, not as  
2 plant in service items. The investments in the projects proposed by FPL or its subsidiary  
3 are not for Plant in Service items that would qualify for rate base; rather, they would be  
4 for investments in a highly competitive industry.

5

6 COMMISSION LIMITATIONS ON THE APPROPRIATE AMOUNT FOR RECOVERY

7 **Q. HAS THE COMMISSION PREVIOUSLY ADDRESSED THE RECOVERY OF**  
8 **COSTS TO BE RECOVERED THROUGH THE FUEL CLAUSE ASSOCIATED**  
9 **WITH THE EXTRACTION AND PRODUCTION OF FOSSIL FUELS FROM**  
10 **RELATED ENTITIES?**

11 A. Yes, it has. The Commission has addressed the recovery of the cost of coal purchased  
12 from affiliated entities through the fuel clause on previous occasions. PSC Order No.  
13 20604 in Docket No. 860001-EI-G, issued January 13, 1989, addressed an investigation  
14 into affiliated cost-plus fuel supply relationships. The Commission's summary at the  
15 very beginning of the order states: "We have determined as a matter of policy that  
16 utilities seeking the recovery of the cost of coal purchased from an affiliate through their  
17 fuel and purchased power cost recovery clauses shall have their recovery limited by a  
18 'market price' standard, rather than under the 'cost-plus' standard now in effect." In the  
19 Background section of the order, the Commission states: "After considering the post-  
20 hearing briefs of the parties and our Staff's recommendations, we, at our September 6,  
21 1988 Agenda Conference, determined that affiliated coal should be priced at market price  
22 for recovery through the utilities' fuel cost recovery clauses and that affiliated coal  
23 transportation and handling services should also be priced at 'market' where it was  
24 reasonably possible to construct a market price for the good or service being considered."

1 Q. HOW DID THE COMMISSION ADDRESS THE APPROPRIATE PRICING OF  
2 FOSSIL FUELS IN THAT ORDER?

3 A. In the Conclusion section of Order No. 20604, the Commission addressed several key  
4 regulatory policy issues that are highly relevant to the case at hand. In addressing cost-  
5 plus pricing and the application of cost-of-service analysis required in such pricing, the  
6 Commission stated:

7 Implicit in cost-plus pricing is the requirement that one is capable of  
8 conducting a cost-of-service analysis of a business to determine that its  
9 expenses are both necessary and reasonable. This is a methodology that is  
10 demanded for monopoly utility services, and which usually proves to be  
11 complex, expensive and time consuming. It is a methodology which requires  
12 a high degree of familiarity with the capital requirements and expenses  
13 necessitated by the operations of the business being reviewed. Cost-of-  
14 service analysis of affiliate operations places additional demands upon the  
15 regulatory agency in terms of time, expense and acquiring additional  
16 expertise. All come at some additional cost that must eventually be borne by  
17 the ratepayer, either in his role as a customer or as a taxpayer. Furthermore,  
18 there seems to be no end to the types of affiliated businesses that we are  
19 expected to become sufficiently familiar with so that we might judge the  
20 reasonableness of their costs on a cost-of-service basis. For example, in this  
21 docket and the companion TECO docket we are confronted with the  
22 following types of affiliated businesses whose costs are included in the  
23 purchase price of the coal: (1) land companies owning coal reserves; (2)  
24 financial services companies; (3) equipment leasing companies; (4) coal  
25 mining companies; (5) river barge and tug companies; (6) transloading and  
26 bulk storage facilities; (7) ocean barge and tug services; (8) marine  
27 management and services companies; (9) rail car repair companies; (10)  
28 diversified holding companies; and (11) others.

29  
30 Cost-of-service regulation for public utilities is necessitated by their  
31 monopoly status and the attendant lack of significant competition, if any, for  
32 their end product. Cost-of-service regulation exists as the proxy for  
33 competition to insure that utilities provide efficient, sufficient and adequate  
34 service and at a cost that includes only reasonable and necessary expenses.  
35 Cost-of-service regulation of some type is essential when there is no  
36 competitive market for the product or service being purchased; it is  
37 superfluous when such a competitive market exists.

38 (footnotes excluded.)  
39

40 The very same concerns highlighted by the Commission in Order No. 20604 are  
41 applicable to the transaction proposed in FPL's Petition. The transaction involves FPL

1 establishing a subsidiary which would participate in natural gas exploration, drilling and  
2 production through joint ventures. Similar to the coal operations addressed in the 1989  
3 order, the natural gas operations would require a “high degree of familiarity with the  
4 capital requirements and expenses necessitated by the operation of the business being  
5 reviewed” and would place “additional demands upon the regulatory agency in terms of  
6 time, expense and acquiring additional expertise.” Also applicable to FPL’s Petition is  
7 the fact that the natural gas exploration, drilling and production industry, like the  
8 ownership of coal reserves and coal mining, is not a monopoly service because a  
9 competitive market exists.

10  
11 **Q. DID THE COMMISSION FURTHER ADDRESS THE APPROPRIATE PRICING**  
12 **OF FUELS ACQUIRED FROM AFFILIATED ENTITIES IN ORDER NO. 20604?**

13 A. Yes, it did. In the Conclusion section of Order No. 20604, the Commission also stated:  
14 “Considering the many advantages offered by a market pricing system, we, as a policy  
15 matter, shall require its adoption for all affiliated fuel transactions for which comparable  
16 market prices may be found or constructed.” The Commission also stated: “In  
17 concluding, we note the following: (1) from the record in this case, we are convinced  
18 that market prices can be established for the affiliated coal; ... (3) cost-of-service  
19 methodologies should be avoided, if possible...” In the ordering paragraphs, the  
20 Commission also ordered that “...as a matter of general policy, market-based pricing for  
21 affiliate fuel and fuel transportation services shall be used for the purposes of fuel cost  
22 recovery where a market for the product or service is reasonably available.”

23  
24 Clearly, these same principles would apply to the transactions proposed by FPL in its  
25 Petition.

1 **Q. FPL IS PROPOSING TO ESTABLISH A WHOLLY-OWNED SUBSIDIARY TO**  
2 **ENTER THE JOINT VENTURE WITH PETROQUEST. IS THIS DISTINCTION**  
3 **RELEVANT IN EVALUATING WHETHER OR NOT THE COMMISSION'S**  
4 **POLICIES ARTICULATED IN ORDER NO. 20604 APPLY?**

5 A. Absolutely not. While an affiliate is not always a subsidiary, a subsidiary is always, by  
6 definition, an affiliate. The Master Glossary of the Accounting Standards Codification  
7 defines affiliate as "A party that directly or indirectly through one or more intermediaries,  
8 controls, is controlled by, or is under common control with an entity." The decision to  
9 have the joint venture agreement transferred from USG to a subsidiary of FPL (which is  
10 an affiliate under the control of FPL), instead of staying with USG or being transferred to  
11 a separate affiliate not directly controlled by FPL, is a corporate decision that should not  
12 impact whether or not the Commission's general policy of using market-based pricing for  
13 affiliate fuel services applies. Similarly, if FPL decides to go forward with potential  
14 future gas exploration, drilling and production ventures directly through a subsidiary, the  
15 subsidiary would still be an affiliate and the Commission's general policy of using  
16 market-based pricing for affiliate fuel services would still apply. Additionally, if FPL  
17 were not to establish a wholly-owned subsidiary and were to instead include the joint  
18 venture within its own operations, its joint venture activities would not require cost-of-  
19 service pricing because a competitive market exists for natural gas. As indicated by the  
20 Commission in Order No. 20604, "Cost-of-service regulation of some type is essential  
21 when there is no competitive market for the product or service being purchased; it is  
22 superfluous when such a competitive market exists." Thus, even if the operations were to  
23 be established within FPL, cost-of-service regulation should not apply to natural gas  
24 exploration, drilling and production operations, as a robust, competitive market exists for  
25 the pricing of natural gas.

1 **Q. WHAT DO YOU RECOMMEND THAT THE COMMISSION REQUIRE AS**  
2 **PART OF ITS ORDER IN THIS CASE?**

3 A. Consistent with the Commission's prior findings related to the acquisition from affiliated  
4 entities of fossil fuels for which a competitive market exists, the Commission should  
5 make it abundantly clear in this case that if FPL purchases gas from the proposed joint  
6 venture between PetroQuest and FPL's yet-unnamed subsidiary (or even if it directly  
7 enters into the joint venture with PetroQuest), and from other potential future joint  
8 ventures, the amount to be recovered from customers through the fuel cost recovery  
9 clause will be limited to, and will not exceed, the market price of gas. The market price  
10 of natural gas is readily available to the Commission and its staff.

11

12 TRANSACTION ACCOUNTING

13 **Q. BEFORE ADDRESSING SPECIFIC ACCOUNTING ISSUES AND CONCERNS**  
14 **INHERENT IN FPL'S REQUEST, WOULD YOU PLEASE BRIEFLY**  
15 **SUMMARIZE YOUR UNDERSTANDING OF THE COMMISSION'S MISSION**  
16 **AND OVERSIGHT FUNCTIONS PERFORMED WITH REGARD TO THE**  
17 **COSTS THAT UTILITIES SEEK TO RECOVER THROUGH THE FUEL COST**  
18 **RECOVERY CLAUSE?**

19 A. Yes, I will. The stated mission of the Florida Public Service Commission is "To facilitate  
20 the efficient provision of safe and reliable utility services at fair prices."<sup>2</sup> The  
21 Commission has identified a number of goals it pursues in following its mission. One of  
22 the established goals for economic regulation is to: "Provide a regulatory process that  
23 results in fair and reasonable rates while offering rate base regulated utilities and

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<sup>2</sup> <http://www.psc.state.fl.us/about/mission.aspx> (last viewed on September 22, 2014)

1 opportunity to earn a fair return on their investments.”<sup>3</sup> One of the identified goals for  
2 regulatory oversight is to “Provide appropriate regulatory oversight to protect  
3 consumers.”<sup>4</sup>

4  
5 To accomplish its mission, the Commission performs an essential function in auditing  
6 and monitoring the costs electric that utilities seek to include for recovery. The auditors  
7 in the Bureau of Auditing of the Commission’s Office of Auditing and Performance  
8 Analysis conduct examinations of utility records and independently verify the supporting  
9 documentation for filings made by regulated companies. This includes financial audits of  
10 utilities’ requests for increases in rates through the annual clauses, such as the fuel cost  
11 recovery clause, “...to ensure ratepayers only pay for prudently incurred expenses.”<sup>5</sup>  
12 This audit function is a vital element in achieving the Commission’s mission and  
13 ensuring that costs recovered from customers are fair and reasonable, were prudently  
14 incurred, and are cost based. In fulfilling its obligations, it is important for the Bureau of  
15 Auditing to be able to review and confirm the costs that utilities seek to include in the  
16 fuel cost recovery clause and to have confidence that such costs are accurate and fairly  
17 stated.

18  
19 The Commission’s Division of Accounting and Finance fulfills another essential function  
20 in allowing the Commission to pursue several of the goals it has established to achieve its  
21 important mission. The Division of Accounting and Finance reviews the revenue  
22 requirements of rate base regulated utilities, such as FPL, and monitors earnings of the  
23 utilities. Its duties include reviewing the petitions submitted in the fuel cost recovery

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<sup>3</sup> *Ibid.*

<sup>4</sup> *Ibid.*

<sup>5</sup> Florida Public Service Commission, Statement of Agency Organization & Operations, March 2014, page 6.

1 docket and making recommendations to the Commission on the same.<sup>6</sup> In order to make  
2 recommendations on fuel cost recovery petitions, it is essential that the Division of  
3 Accounting and Finance is knowledgeable of the costs that electric utilities are seeking to  
4 recover through the clause.

5  
6 **Q. PLEASE IDENTIFY THE ACCOUNTING REQUIREMENTS THAT THE**  
7 **COMMISSION PRESCRIBES FOR INVESTOR-OWNED ELECTRIC**  
8 **UTILITIES THAT ARE SUBJECT TO ITS JURISDICTION.**

9 A. PSC Rule 25-6.014 – Records and Reports in General states as follows:

10 (1) Each investor-owned electric utility shall maintain its accounts and  
11 records in conformity with the Uniform System of Accounts (USOA) for  
12 Public Utilities and Licensees as found in the Code of Federal Regulations,  
13 Title 18, Subchapter C, Part 101, for Major Utilities as revised April 1, 2002,  
14 which is hereby incorporated by reference into this rule, and as modified  
15 below. All inquiries relating to interpretation of the USOA shall be  
16 submitted to the Commission's Division of Accounting and Finance in  
17 writing.

18  
19 As mentioned earlier in my testimony, these accounting rules are often referred to as the  
20 "FERC USOA" or "USOA."

21  
22 **Q. WHAT ROLE DOES THE USOA PLAY IN THE COMMISSION'S**  
23 **REGULATION OF INVESTOR OWNED UTILITIES SUCH AS FPL?**

24 A. The USOA is an invaluable tool that is essential to the effective regulation of public  
25 utilities subject to the Commission's jurisdiction. It contains clear and precise accounting  
26 instructions for how transactions are to be recorded and what costs are to be recorded in  
27 which specific accounts. It also gives clear instructions regarding accounting for capital  
28 investments that are used in providing regulated services. It allows for consistency in  
29 reporting and in accounting for items between utilities utilizing the USOA. It also

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<sup>6</sup> *Id.* at 7.

1 enhances the Commission staff's ability to more efficiently and effectively audit utility  
2 operations and the costs that utilities are seeking to recover from customers in rates, be it  
3 through base rates, the fuel cost recovery clause, or other applicable clauses.

4  
5 **Q. IS FPL PROPOSING TO APPLY THE USOA FOR ELECTRIC UTILITIES OR**  
6 **NATURAL GAS COMPANIES FOR ITS PROPOSED VENTURE INTO THE**  
7 **EXPLORATION, DRILLING AND PRODUCTION OF NATURAL GAS?**

8 A. No, it is not. If the Commission approves FPL's request in this case, FPL's affiliate,  
9 USG Properties Woodford I, LLC ("USG") would transfer the Woodford Project to a yet-  
10 unnamed and wholly-owned subsidiary of FPL. FPL does not propose that the unnamed  
11 subsidiary apply the FERC USOA for electric utilities or natural gas companies.  
12 According to the Direct Testimony of FPL witness Ousdahl, at page 16, the "[a]ccounting  
13 for oil and gas production is a highly specialized and unique form of energy accounting"  
14 and that "[n]either the FERC Electric nor Natural Gas chart(s) of accounts is consistent  
15 with the standard accounting utilized in the oil and gas production industry." Thus, FPL  
16 apparently views the venture it is proposing in this case as inconsistent with regulated  
17 monopoly operations for which the FERC USOA would apply. Ms. Ousdahl further  
18 indicates, at page 16 of her testimony, that FPL would be subject to Accounting Standard  
19 Codification ("ASC") 932 – Accounting for Oil and Gas Exploration for the Woodford  
20 Project (as well as for future proposed gas exploration and production ventures) and  
21 would use the successful efforts accounting method contained in ASC 932 to record  
22 activities related to the proposed gas exploration and production investments.

23  
24 **Q. DOES THE COMPANY CONTEND THAT IT MUST FOLLOW THE**  
25 **SUCCESSFUL EFFORTS METHOD OF ACCOUNTING FOR THE PROPOSED**

1           **GAS PRODUCTION ACTIVITIES, NOTWITHSTANDING THE**  
2           **COMMISSION’S PRESCRIPTION OF THE USOA?**

3    A.    Yes, it does. FPL’s response to Staff Interrogatory No. 61 states, in part, as follows:

4                   . . . SEC Staff Accounting Bulletin Topic 12.C (“SAB Topic 12.C”) states  
5                   that a consolidated entity must apply a consistent accounting method for  
6                   all subsidiaries. FPL’s parent, NextEra Energy, Inc. has elected the  
7                   successful efforts method of accounting through its subsidiary, USG.  
8                   Therefore, FPL is also required to follow the successful efforts method of  
9                   accounting.

10                   Thus, according to FPL, since an unregulated subsidiary that participates in the  
11                   competitive gas exploration and production industry utilizes the successful efforts method  
12                   of accounting for its oil and gas production activities, FPL must also utilize this method  
13                   of accounting for its potential oil and gas production activities. If FPL proceeds with its  
14                   proposed joint venture, apparently the Commission would be required to accept a method  
15                   of accounting selected by USG, FPL’s unregulated affiliate. I believe that fact supports  
16                   OPC’s position, developed in a Motion to Dismiss that is pending at the time I am  
17                   preparing this testimony, that the activities fall outside the Commission’s regulatory  
18                   purview.  
19

20  
21    **Q.    ARE THE GUIDELINES CONTAINED IN ASC 932 AND THE SUCCESSFUL**  
22    **EFFORTS ACCOUNTING METHOD SIMILAR TO THE FERC USOA FOR**  
23    **ELECTRIC UTILITIES THAT INVESTOR-OWNED ELECTRIC UTILITIES**  
24    **REGULATED BY THE PSC ARE REQUIRED TO USE IN MAINTAINING**  
25    **THEIR ACCOUNTS AND RECORDS UNDER PSC RULE 25-6.014?**

26    A.    No, they are not. In fact, the accounting requirements that FPL proposes to apply to the  
27    Woodford Project and to potential future gas exploration and production ventures are so  
28    foreign to the accounting prescribed in the FERC USOA that FPL intends to outsource  
29    the accounting, recordkeeping, reporting and ratemaking functions associated with

1 investments in such ventures.<sup>7</sup> FPL states that the accounting for the costs of gas  
2 exploration and production projects is “...very specialized, utilizing a unique chart of  
3 accounts and specialized financial systems” and that it “...intends to use one of the  
4 several well-established third party providers of accounting and recordkeeping services in  
5 order to maintain oversight and control over the accounting for the Woodford Project and  
6 any other gas reserve projects consistent with FPL’s role as a non-operator.”<sup>8</sup> FPL also  
7 states that the potential third party providers “...have the proper systems and experience  
8 to deliver the full scope of back-office services necessary to effectively participate as a  
9 non-operator in oil and gas production.”<sup>9</sup> Thus, the specialized accounting, reporting and  
10 recordkeeping functions associated with the proposed investments in gas reserves differ  
11 so greatly from the accounting system that FPL uses for its regulated utility operations  
12 that it does not have the proper systems and experience that are needed to “effectively  
13 participate” in gas production without retaining outside expertise.

14  
15 **Q. WHO WOULD INCUR THE COSTS TO WHICH FPL EXPECTS TO APPLY**  
16 **THE SPECIALIZED SYSTEM OF ACCOUNTING?**

17 **A.** For the Woodford Project, PetroQuest would be the operator. Thus, FPL’s unnamed  
18 subsidiary would be reliant upon PetroQuest (and potentially other as yet-unnamed  
19 entities for future ventures) as the operator for both the operation of the venture and for  
20 the resulting financial effects. In other words, PetroQuest (and potentially other entities  
21 for future gas exploration and production ventures) would initially incur, record, and  
22 account for the costs incurred in the operation of the exploration, drilling and production

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<sup>7</sup> Direct Testimony of FPL witness Ousdahl, pages 6, 20, and 21.

<sup>8</sup> *Id.* at 6 and 20.

<sup>9</sup> *Id.* at 20.

1 operations. PetroQuest would then invoice the FPL subsidiary monthly for costs  
2 incurred.

3  
4 **Q. WOULD THE COMMISSION BE ABLE TO AUDIT PETROQUEST OR**  
5 **SIMILAR JOINT VENTURE OPERATORS?**

6 A. No, it would not. PetroQuest is not regulated by the Commission and does not fall under  
7 the Commission's jurisdiction. While the Commission has access to FPL and FPL's  
8 affiliate records under PSC Rule 25-6.0151 – Audit Access to Records, it has no  
9 jurisdiction over PetroQuest or other potential future gas venture operators. Thus, the  
10 PSC auditors would not have the ability to audit and confirm the costs incurred by  
11 PetroQuest (and other potential future gas venture operators) in constructing,  
12 maintaining, and operating the natural gas drilling and production facilities. The fact that  
13 the Commission would have no authority to audit the entity incurring the joint venture  
14 costs that would travel through the fuel cost recovery clause is relevant to OPC's position  
15 that these investment ventures fall outside the Commission's regulatory purview.

16  
17 **Q. WHAT DOES FPL SAY ABOUT CONFIRMING THE ACCURACY OF THE**  
18 **OPERATOR'S RECORDS AND THE REASONABLENESS OF INVOICED**  
19 **COSTS?**

20 A. FPL attempts to use provisions in the contract with PetroQuest as a surrogate for the  
21 inability of the Commission to audit the entity incurring the costs. Ms. Ousdahl states at  
22 page 20 of her testimony that under the PetroQuest Agreement, FPL, through its  
23 unnamed subsidiary, would have the right to audit the invoices from PetroQuest. She  
24 also states that "FPL's external auditors will conduct substantive controls testing around  
25 these transactions to the extent necessary as a part of its overall external audit."

1           However, while FPL's subsidiary may have the right under the agreement to audit the  
2           invoices received from the operator, the fact remains that the Commission — the agency  
3           being asked to require FPL's customers to pay those costs — would not. Presumably  
4           FPL, or its subsidiary, would need to utilize outside expert assistance if FPL does elect to  
5           audit the invoices since they do not have the internal expertise in the specialized methods  
6           of accounting utilized for such operations. The Commission would have no ability to  
7           directly and independently confirm the accuracy and reasonableness of the gas  
8           production and drilling costs incurred by the operator. Essentially, FPL is asking the  
9           Commission to defer to FPL's subsidiary and accept being one important step removed  
10          from monitoring, confirming, and auditing the charges from the gas project operators.  
11          The fact that FPL is basically asking the Commission to delegate the role of auditing  
12          FPL's recovery request to FPL is germane to OPC's position that the transactions fall  
13          outside the limits of the Commission's regulatory domain.

14  
15   **Q.    FPL IS REQUESTING THAT ITS INVESTMENTS IN GAS RESERVES AND**  
16   **THE COSTS ASSOCIATED WITH EXTRACTING NATURAL GAS BE**  
17   **INCORPORATED IN ITS FUEL COST RECOVERY CLAUSE. WOULD THE**  
18   **SPECIALIZED ACCOUNTING AND RECORDKEEPING REQUIREMENTS**  
19   **FURTHER IMPEDE THE PSC AUDITORS' ABILITY TO PERFORM THEIR**  
20   **DUTIES?**

21   **A.**    In my opinion, yes. The accounting and recordkeeping system that FPL says the joint  
22          venture must employ would hinder the PSC auditors' ability to do their jobs effectively.  
23          FPL has acknowledged that the accounting is very specialized, utilizes a unique chart of  
24          accounts that differs from the FERC USOA, and requires specialized financial systems.  
25          It is my opinion that the use of a unique chart of accounts differing from the FERC

1           USOA, the use of specialized accounting requirements that are foreign to the FERC  
2           USOA, and the use of specialized financial systems would greatly impact the ability of  
3           the PSC auditors and of parties (such as OPC) to independently determine the accuracy  
4           and the reasonableness of the charges FPL would seek to include and recover from its  
5           captive electric customers. FPL itself has indicated that the accounting, reporting,  
6           recordkeeping and ratemaking functions are so specialized that it would need to retain  
7           outside services to accomplish these tasks.

8  
9       **Q. IS AN ACCOUNTANT EXPERIENCED IN ADDRESSING REGULATORY**  
10       **ACCOUNTING ISSUES NECESSARILY QUALIFIED IN WHAT FPL HAS**  
11       **DESCRIBED AS THE “VERY SPECIALIZED” ACCOUNTING AND THE**  
12       **“UNIQUE CHART OF ACCOUNTS AND SPECIALIZED FINANCIAL**  
13       **SYSTEMS” THAT FPL INDICATES IS ASSOCIATED WITH THE**  
14       **ACCOUNTING, REPORTING AND RATEMAKING FUNCTIONS**  
15       **ASSOCIATED WITH INVESTMENTS IN GAS RESERVES?**

16       **A.** No. For instance, while I have researched and addressed regulatory accounting issues  
17       throughout my regulatory career spanning approximately 23 years, I do not have any  
18       experience or expertise in what FPL describes as the “very specialized” accounting,  
19       “unique chart of accounts and specialized financial systems” associated with investments  
20       in gas reserves. Likewise, Ms. Ousdahl, who holds the position of Vice President,  
21       Controller and Chief Accounting Officer of a large, sophisticated electric utility,  
22       acknowledges in her testimony that FPL must secure such expertise from outside the  
23       company. Investing in natural gas reserves, drilling and production is neither a normal  
24       nor a necessary function of an investor-owned electric utility in providing electric service  
25       to customers; thus, this is the first case in which I have seen a request such as that

1 proposed by FPL. While the Commission has some very qualified and experienced  
2 auditors and analysts on its staff, I suspect that the PSC audit and technical staff also lack  
3 the specialized expertise in the unique and “very specialized” accounting requirements  
4 associated with the competitive gas exploration, drilling and production industry.

5  
6 **Q. OPC WITNESS DANIEL LAWTON ADDRESSES SEVERAL RISKS**  
7 **ASSOCIATED WITH FPL’S PROPOSED VENTURE. DOES THE**  
8 **ACCOUNTING ASSOCIATED WITH THE PROPOSED VENTURES ADD**  
9 **ADDITIONAL RISK NOT ADDRESSED IN MR. LAWTON’S TESTIMONY?**

10 **A.** Yes. It is my opinion that the unique and specialized accounting requirements associated  
11 with FPL’s proposed venture into natural gas production that is foreign to the Florida  
12 regulators and outside of the recordkeeping requirements of the Commission would add  
13 an additional layer of regulatory risk that would be passed on to the captive electric  
14 ratepayers. The PSC audit staff would be largely dependent on FPL (or possibly third  
15 party accountants engaged by FPL) in adequately monitoring, auditing and reporting on  
16 the gas drilling and production operations and in disclosing any accounting or cost  
17 recovery issues that may be the result of the unique and specialized accounting  
18 provisions. By way of example, the Commission would never agree to place FPL in  
19 charge of the Commission’s auditing of the costs of oil that FPL submits for recovery in  
20 the fuel cost recovery clause proceeding, or the Commission’s auditing of plant additions  
21 and operating expenses that FPL claims during a base rate case. For the same reasons,  
22 the Commission should not agree in this case to effectively delegate to FPL’s subsidiary  
23 its role of auditing the cost recovery issues relating to FPL’s proposed ventures into the  
24 gas exploration, drilling and production industry.

1 CAPITAL INVESTMENT COST RECOVERY

2 **Q. UNDER FPL'S PROPOSED ACCOUNTING METHOD, HOW WOULD THE**  
3 **CAPITAL INVESTMENTS ASSOCIATED WITH THE GAS VENTURES BE**  
4 **DEPRECIATED?**

5 A. At page 18 of her testimony, FPL witness Ousdahl describes the form of depreciation that  
6 would be used for the gas venture capital investments under the proposed successful  
7 efforts method of accounting:

8 . . . In the case of gas and oil production accounting, depreciation is  
9 recorded in the form of "depletion," which is measured on a unit-of-  
10 production basis rather than on a remaining life or whole life basis.  
11 Depletion for a gas reserve investment plays the same role as depreciation  
12 would for an electric plant asset providing for recognition of the use of the  
13 asset in the financial statements and in rates. As permitted under ASC  
14 932, for depletion purposes FPL plans to aggregate its investments at a  
15 reservoir or field level because they share common geological structural  
16 features. This will help simplify the depletion accounting.

17  
18 Ms. Ousdahl also explains that the reserve estimates used in calculating the depletion  
19 rates must be updated annually, and that FPL would be relying on reserve estimate  
20 reports provided by third party reserve engineers.<sup>10</sup> Thus, each year the depletion rate  
21 applied to the gas produced from the wells would be revised and the resulting depletion  
22 expense would also vary each year. FPL intends to include the annual depletion expense,  
23 as well as the return on the net undepleted gas reserve investment balance, for recovery in  
24 the fuel cost recovery clause. The amount of depreciation expense (or depletion expense)  
25 would fluctuate on an annual basis and would be dependent upon the amount of natural  
26 gas extracted during the year as well as the amount of estimated reserves.

---

<sup>10</sup> *Id.* at 19.

1 **Q. IS THE ANNUAL REVISION TO THE DEPLETION RATES CONSISTENT**  
2 **WITH THE DEPRECIATION REQUIREMENTS UNDER THE COMMISSION'S**  
3 **RULES?**

4 A. No, it is not. As indicated above, FPL indicates that under gas and oil production  
5 accounting, depreciation is recorded in the form of “depletion” and “[d]epletion for a gas  
6 reserve investment plays the same role as depreciation would for an electric plant asset  
7 providing for recognition of the use of the asset in the financial statements and in rates.”<sup>11</sup>  
8 Under the PSC Rules for investor-owned electric utilities, Rule 25-6.0436 – Depreciation  
9 – contains specific instructions with regards to the depreciation rates to be applied to  
10 utility plant investments. Rule 25-6.0436(2)(a) states: “No utility shall change any  
11 existing depreciation rate or initiate any new depreciation rate without prior Commission  
12 approval.” Under its Petition, FPL (or its subsidiary) would be revising the depletion  
13 rates that would be used in determining the depletion expense to include in the fuel clause  
14 each year.

15  
16 **Q. ARE THERE ANY EVENTS THAT COULD CAUSE THE DEPLETION RATES**  
17 **AND/OR THE DEPLETION EXPENSE TO FLUCTUATE SIGNIFICANTLY?**

18 A. Yes. The annual depletion expense that FPL proposes to include in the fuel clause each  
19 year is dependent upon the amount of gas extracted in a given year and the estimated  
20 amount of extractable reserves. The depletion rate would need to be evaluated and  
21 recalculated each year. If, for some reason, the estimated amount of extractable reserves  
22 changes significantly, it could have a correspondingly material impact on the resulting  
23 depletion rate that is applied.

---

<sup>11</sup> *Id.* at 18.

1 **Q. IF AN EVENT OCCURS THAT CAUSES PRODUCTION AT THE WOODFORD**  
2 **PROJECT (OR OTHER FUTURE PROJECTS) TO CEASE PRIOR TO FPL**  
3 **FULLY RECOVERING ITS CAPITAL INVESTMENT IN THE PROJECT, DOES**  
4 **FPL INTEND TO STILL RECOVER THE REMAINING CAPITAL**  
5 **INVESTMENT (AND RETURN ON THAT INVESTMENT) FROM ITS**  
6 **RATEPAYERS?**

7 **A.** Yes. It is FPL's intent that 100% of its potential investments and profits in natural gas  
8 exploration, drilling and production activities be recovered from its captive electric  
9 ratepayers, regardless of the performance of its proposed gas ventures. In response to  
10 OPC Interrogatory No. 38, subparts (b) and (d), FPL addressed the issue of potential  
11 undepleted (unrecovered) capital balances as follows:

12 b. In the unlikely event that there is a sudden unforeseen cessation of  
13 production, FPL would consider the facts and circumstances associated  
14 with the event. If the unrecovered balance is limited to one or a few wells  
15 and given the relatively small investment that would likely be remaining  
16 once production had already begun, FPL would seek to recover the  
17 undepleted investment in the fuel clause in the current period.  
18 Alternatively, an analogy could be made to the Commission treatment for  
19 unrecovered investment in retired utility plant whereby its practice has  
20 been to consider the use of capital recovery schedules to amortize  
21 remaining unrecovered balance through rates. This could be applied if  
22 necessary to the clause recovery of any retired but unrecovered gas reserve  
23 investment. The Company believes the likelihood of these scenarios to be  
24 remote.

25 . . .

26 d. As discussed in response to part b. above, FPL has many examples of  
27 retirement of assets before they are fully depreciated. Absent a finding of  
28 imprudence, the full return of the cost of the asset is recovered through  
29 rates. The Commission has discretion to determine the proper recovery  
30 period and has utilized capital recovery schedules in many cases to  
31 amortize those remaining costs into rates. The appropriate treatment for  
32 this investment would be no different.

33  
34 Thus, FPL not only wants to venture into the extremely competitive gas drilling and  
35 production industry, but it also seeks the Commission's assurance that it would obtain

1 100% recovery of any investments it makes in such potential ventures, plus profits,  
2 regardless of the performance of the drilling and extraction efforts relative to that  
3 competitive market. Under FPL's approach, 100% of the risk associated with FPL  
4 entering into gas exploration, drilling and production projects — whether from  
5 unconventional or conventional sources — would be pushed onto ratepayers. According  
6 to the responses quoted above, FPL wants to create an equivalency between its potential  
7 investments in competitive, non-monopoly gas exploration, drilling, and extraction  
8 projects and the generation, distribution, and transmission plant used to provide  
9 regulated, monopoly utility service to its captive electric customers, and thereby shield  
10 such investments from the risks of engaging in that competitive industry that is not  
11 regulated by the Commission.

12  
13 **Q. IS FPL'S ATTEMPTED EQUIVALENCY BETWEEN THE INVESTMENTS IN**  
14 **THE COMPETITIVE GAS EXPLORATION INDUSTRY AND FPL'S**  
15 **REGULATED RATE BASE VALID?**

16 **A.** No, it is not. One need look no further than the regulated and unregulated affiliates of  
17 NextEra Energy, Inc. to see that the monopoly utility and gas exploration industries, and  
18 thus the investments in respective industries, are fundamentally different.

19  
20 **Q. PLEASE EXPLAIN.**

21 **A.** If the Commission approves FPL's request without modification, the result would be that  
22 FPL's investors, who are ultimately the shareholders of NextEra Energy, Inc., would earn  
23 additional returns through the operation of FPL's fuel cost recovery clause and such  
24 returns would be guaranteed. This would result as FPL would be applying a rate of  
25 return to the associated capital costs in the fuel clause calculations. That return includes a

1 return on equity component at the Commission's authorized rate of return on equity for  
2 FPL, which is essentially the earnings or profit that is applied on behalf of investors.  
3 Under the fuel clause, the return on equity (or profit) would also be grossed-up to cover  
4 the income taxes on the resulting profit.

5  
6 Under the NextEra Energy, Inc. umbrella, there are affiliates of FPL that currently  
7 participate in the competitive natural gas exploration, drilling and production industry.  
8 USG (which consists of several different legal entities with "USG" in the name) has  
9 made investments in shale formations located in Texas, Oklahoma, Wyoming, North  
10 Dakota, and Louisiana.<sup>12</sup> Its investments are exposed to the risks of loss that exist in a  
11 competitive market. In other words, although the investments in shale plays made by  
12 USG and those contemplated by sister company FPL are similar in nature, the risk  
13 avoidance and guaranteed return sought by FPL are not applicable to investments in  
14 natural gas exploration, drilling and production made by USG. This observation supports  
15 the proposition that it is the nature (regulated [monopoly] or unregulated [competitive])  
16 of the activity, and not the name of the entity engaging in that activity, that determines  
17 whether the investment qualifies for the status of regulated utility rate base.

18  
19 Risks associated with FPL's proposed natural gas exploration, drilling and production  
20 ventures are addressed further by OPC witness Lawton in his Direct Testimony.

21  
22 **Q. IF THE COMMISSION DECIDES, NOTWITHSTANDING OPC'S TESTIMONY**  
23 **AND ARGUMENTS, TO APPROVE CLAUSE RECOVERY OF FPL'S**  
24 **PROPOSED INVESTMENTS IN SOME FORM, ARE YOU AWARE OF ANY**

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<sup>12</sup> Response to OPC Interrogatory No. 19.

1           **RECENT COMMISSION PRECEDENT THAT SHOULD PROVIDE THE BASIS**  
2           **FOR MODIFYING THE TREATMENT REQUESTED BY FPL?**

3           A.     Yes. The Commission issued Order PSC-12-0498-PAA-EI on September 27, 2012 in  
4           Docket No. 120153-EI involving Tampa Electric Company. In that order, at pages 4–5,  
5           the Commission stated as follows:

6                     Although TECO’s forecasts and assumptions appear reasonable, we note  
7                     that the price and performance variables could impact fuel savings and,  
8                     ultimately, the amount of recoverable costs of the project during the five-  
9                     year recovery period. If markets were to change substantially during the  
10                    five-year recovery period, or plant performance fell short of expectations,  
11                    the current fuel savings projections would be affected. Therefore, we find  
12                    that certain conditions shall be placed upon the recovery of costs: TECO  
13                    shall be permitted to recover the projected conversion costs through the  
14                    Fuel Clause beginning on the date the unit is placed into service, **limited**  
15                    **to the actual fuel savings**; TECO shall depreciate the Polk Unit One  
16                    conversion over the next five years using the straight line depreciation  
17                    method; and TECO shall use the actual weighed average cost of capital in  
18                    TECO’s most current May earning surveillance reports to calculate the  
19                    revenue requirement. (Emphasis added)  
20

21          **Q.     PLEASE COMPARE THE TECO PROJECT THAT THE COMMISSION**  
22          **ADDRESSED IN ORDER NO. PSC-12-0498-PAA-EI WITH FPL’S PROPOSAL**  
23          **IN THIS CASE.**

24          A.     The fuel conversion project at issue in the recent TECO docket was for the type of  
25          regulated utility system improvement project that would “normally” be recovered through  
26          base rates, whereas the highly competitive gas exploration and production ventures  
27          proposed by FPL in its Petition are not investments that would normally be recovered  
28          through base rates. Rather, the gas exploration and production ventures proposed by FPL  
29          are associated with becoming a producer, through a subsidiary, of a fossil fuel  
30          commodity that is readily available in the market and is more analogous to the acquisition  
31          of coal from affiliated entities previously addressed in this testimony.

1           Additionally, TECO proposed a five-year recovery period, whereas the Woodford Project  
2           entails a fifty-year recovery period for the associated investments. While the  
3           Commission expressed concern regarding the forecasts and the impact of price and  
4           performance variables over the five-year recovery period proposed by TECO, the forecast  
5           risk increases substantially when going from a five-year to a fifty-year forecast period.  
6           This forecast risk is addressed further in Mr. Lawton's Direct Testimony.

7  
8           In the TECO case the Commission addressed the possibility that TECO's project might  
9           not produce savings sufficient to outweigh the costs of the capital investment that TECO  
10          sought to recover through the fuel cost recovery clause. As Mr. Lawton develops, that  
11          possibility is a major issue and concern in this case.

12  
13       **Q.    IF THE COMMISSION DOES GRANT FPL'S PETITION IN SOME FORM,**  
14       **SHOULD THE RECOVERY SOUGHT BY FPL IN ITS PETITION BE SUBJECT**  
15       **TO ANY CONDITIONS?**

16       **A.**    Before responding to the question, I must first reiterate that FPL's request should be  
17       rejected outright. The Commission should make it abundantly clear that if FPL or its  
18       unnamed subsidiary goes forward with the proposed Woodford Project acquisition, or  
19       other potential future transactions of a similar nature, the recovery of the cost of natural  
20       gas obtained by FPL from such joint ventures will be limited to the market price of gas.

21  
22       If the Commission does not adopt this recommendation, it should take steps to ensure that  
23       any recoveries by FPL of its proposed investments each year are limited to the actual  
24       resulting fuel savings. In other words, the Commission should not permit any costs in  
25       excess of the demonstrated actual savings to customers to be passed to ratepayers through

1 the fuel cost recovery clause. The Commission's authorization of the proposed  
2 investments in the Woodford Project and other potential future gas ventures, and  
3 recovery of the resulting investments and associated costs and returns (profits) in the fuel  
4 cost recovery clause, should not be the equivalent of a blank check by which FPL is  
5 enabled to embark on multiple natural gas exploration, drilling and production joint  
6 ventures with the full risk going to FPL's ratepayers and no risk to FPL's investors.

7

8 **Q. DOES THIS COMPLETE YOUR PREFILED TESTIMONY?**

9 A. Yes, it does.

1 BY MR. REHWINKEL:

2 Q Ms. Ramas, did you also cause to be prepared  
3 an exhibit to your direct prefiled testimony?

4 A Yes, I did.

5 Q Do you have any changes or corrections to make  
6 to that exhibit?

7 A No, I do not.

8 MR. REHWINKEL: Mr. Chairman, I would ask that  
9 Ms. Ramas' Exhibit DR-1 be given Exhibit No. 34.

10 (Whereupon, Exhibit No. 34 was marked for  
11 identification.)

12 MR. REHWINKEL: Thank you.

13 BY MR. REHWINKEL:

14 Q Ms. Ramas, did you prepare a summary of your  
15 testimony?

16 A Yes, I did.

17 Q Would you give that testimony -- that summary  
18 at this time?

19 A Yes. Thank you.

20 Good evening, Commissioners, counsel. The  
21 ultimate issue in this case is whether or not Florida  
22 Power & Light Company should be permitted to recover,  
23 through the fuel cost recovery clause, costs associated  
24 with potential investments in natural gas exploration,  
25 drilling and production joints ventures, including a

1 return or profit on the associate capital investments  
2 from the captive Florida electric ratepayers. This  
3 would include the proposed joint venture involving  
4 PetroQuest for the Woodford Project, and potential  
5 future ventures with yet unnamed future venture  
6 partners.

7 This involves FPL through yet unnamed  
8 subsidiaries venturing into a highly competitive  
9 industry with all associated risks being passed on to  
10 FPL's Florida ratepayers, and no risk being retained by  
11 FPL and its investors. It is my opinion that FPL's  
12 proposal should be denied and that these proposed  
13 ventures are not eligible for inclusion in the fuel cost  
14 recovery clause under the method proposed by the company  
15 in this case.

16 The company attempts to invoke Commission  
17 order 14546 in support of its proposed recovery through  
18 the fuel cost recovery clause. This is wrong. In that  
19 order the Commission adopted a stipulation between  
20 various parties regarding the eligibility of costs to be  
21 considered in the fuel adjustment clauses. Specifically  
22 item 10 listed in that order is the authority FPL  
23 expressly relies on in support of its request in this  
24 case.

25 And item 10 states, quote, "fossil fuel

1 related costs normally recovered through base rates, but  
2 which were not recognized or anticipated in the cost  
3 levels used to determine current base rates in which, if  
4 expended, will result in fuel savings to customers.  
5 Recovery of such costs should be made on a case-by-case  
6 basis after Commission approval," end quote.

7 As explained in my testimony, FPL's proposal  
8 fails as least two of the three prongs of the Fuel  
9 Clause eligibility test found in item 10 of that order.

10 First, the ventures into gas exploration,  
11 drilling and production are not costs normally recovered  
12 through base rates. They are not part of an electric  
13 utility's regulated monopoly business and the incurrence  
14 of costs associated with venturing into a highly  
15 competitive industry are not costs that are necessary  
16 for providing electric service to the company's  
17 customers in Florida.

18 Second, the company is not guaranteeing that  
19 fuel cost savings to customers will result in this case.

20 In this case, FPL proposes to recover  
21 100 percent of any investment it makes in the potential  
22 gas exploration, drilling and production joint ventures,  
23 as well as a return on investments in the cost of such  
24 investments are fully recovered from its customers.  
25 This is regardless of whether any gas is found or

1 produced, and whether or not they result in costs that  
2 are lower than the market price available for natural  
3 gas.

4 FPL's proposal places 100 percent of the risks  
5 associated with entering into a competitive market on  
6 ratepayers, while guaranteeing an equity return to FPL's  
7 shareholders. Under FPL's proposal, it would  
8 essentially transfer the fuel cost recovery clause to a  
9 means entering into a competitive industry, resulting in  
10 risk free expansion of the capital base upon which a  
11 return on equity is applied.

12 In this case, FPL proposes to establish a  
13 subsidiary for entering into the Woodford Project, and  
14 intends to utilize subsidiaries in entering other future  
15 gas resolve joint ventures. I also testified the  
16 Commission has previously addressed the appropriate  
17 recovery of the costs associated with the extraction and  
18 production of fossil fuels by related entities, and has  
19 established, as a general policy, that where a market  
20 for a product is reasonably available, market based  
21 pricing of affiliate fuel services shall be used for the  
22 purposes of the fuel cost recovery.

23 In order number 20604, the Commission  
24 addressed an investigation into affiliated cost plus  
25 fuel supply relationships. In the conclusion section of

1 that order, the Commission specifically stated, quote,  
2 "cost of service regulation for public utilities is  
3 necessitated by their monopoly status and the attendant  
4 lack of significant competition, if any, for their end  
5 product. Cost of service regulation exists as a proxy  
6 for competition to ensure the utilities provide  
7 efficient, sufficient and adequate service, and at a  
8 cost that includes only reasonable costs and necessary  
9 expenses. Cost of service regulation of some type is  
10 essential when there is no competitive market for the  
11 product or services being purchased. It is superfluous  
12 when such a competitive market exists," end quote.

13 This statement made by the Commission still  
14 holds true, and is applicable to the case at hand. A  
15 highly competitive market exists for natural gas, thus,  
16 as with the case with the acquisition of coal from  
17 affiliated entities, the natural gas exploration,  
18 drilling and production industry is not a monopoly  
19 service. A competitive market does exist for this  
20 product.

21 I recommend that the Commission reject the  
22 company's request, and, instead, make it clear that if  
23 FPL goes forward with the proposed Woodford Project, or  
24 other potential future transactions, the recovery of  
25 cost of natural gas obtained from these joint ventures

1 will be limited to market price of gas.

2 Thank you.

3 MR. REHWINKEL: Public Counsel tenders Ms.  
4 Ramas for cross-examination.

5 CHAIRMAN GRAHAM: Do Retail Federation or  
6 FIPUG, do you have any non-friendly cross?

7 MR. MOYLE: No.

8 CHAIRMAN GRAHAM: Florida Power & Light.

9 CROSS EXAMINATION

10 BY MR. BUTLER:

11 Q We don't have any friendly cross either, but I  
12 do have a few questions.

13 Good evening Ms. Ramas.

14 A Good evening.

15 Q I would first like to ask you some questions  
16 about your qualifications.

17 Have you ever held a position of any nature  
18 with an electric utility?

19 A No, I have not.

20 Q Have you ever performed an evaluation of  
21 acquiring interest in oil or gas reserves?

22 A No, I have not.

23 Q Okay. Have you ever performed an evaluation  
24 of acquiring interest in oil or gas production  
25 facilities?

1 A No.

2 Q Okay. Have you ever held a position where you  
3 were responsible for overseeing natural gas hedging?

4 A No.

5 Q Natural gas storage?

6 A No.

7 Q Electric power origination?

8 A I am sorry, could you repeat that?

9 Q Electric power origination? Electric power  
10 transactions?

11 A No.

12 Q Okay. How about energy or fuel trading?

13 A No, I have not.

14 Q Okay. Have you ever been involved in  
15 negotiating a natural gas purchase agreement?

16 A No.

17 Q Okay. How about a natural gas hedging  
18 agreement?

19 A No.

20 Q How about a natural gas transportation  
21 agreement?

22 A No.

23 Q Or a natural gas storage agreement?

24 A No.

25 Q Do you have any experience in projecting

1 natural gas prices?

2 A No, I do not.

3 Q Do you have any experience in projecting  
4 availability or supply of natural gas?

5 A No.

6 Q Have you ever been responsible for financial  
7 accounting for an investor owned electric utility?

8 A No, I have not.

9 Q Okay. Have you ever audited the books and  
10 records of an investor owned utility?

11 A No.

12 Q Have you ever testified previously with  
13 respect to utility investments in gas reserve projects?

14 A No. In fact, this was the first case in which  
15 I have ever run into a electric utility requesting this  
16 type of investment.

17 Q Okay. I'm sorry, I didn't mean to limit that  
18 question to only electric utilities. Have you been  
19 involved previously in testifying with respect to  
20 utility investments in gas reserve projects, be they  
21 electric utilities or natural gas utilities?

22 A No.

23 Q Okay. Have you ever testified previously with  
24 respect to natural gas exploration or production?

25 A No.

1           Q     Are you aware of any instances in which the  
2     Florida Public Service Commission has audited the books  
3     and record of a joint venture in which an electric  
4     utility participates?

5           A     Would that be for situations in which the  
6     joint venture is not with the affiliated entity?

7           Q     That's right?

8           A     No.

9           Q     Okay. And are you aware that Florida electric  
10    utilities do participate in such joint ventures?

11          A     Yes, that's my understanding.

12          Q     Are you aware of any instances in which the  
13    Florida Public Service Commission -- I am sorry, strike  
14    that.

15                   I reviewed your Exhibit DMR-1 to your  
16    testimony, and in there, you identify instances in which  
17    you filed testimony in various states on utility related  
18    topics; is that correct?

19          A     Correct.

20          Q     Okay. And would you agree that the exhibit  
21    identifies numerous instances in which you have given  
22    such testimony?

23          A     Yes. I believe I have submitted testimony in  
24    approximately 100 cases at this point.

25          Q     Okay. Would you agree that your Exhibit DMR-1

1 identifies no instances in which you have ever testified  
2 on behalf of a utility?

3 A Correct. I have never testified on behalf of  
4 a public utility.

5 Q Okay. And am I correct that at the time you  
6 prepared your testimony, you had not inquired with the  
7 Montana Public Service Commission regarding its  
8 oversight of the Northwestern Energy gas reserves  
9 investments?

10 A No, I did not.

11 Q Okay. I want to ask you some questions,  
12 Ms. Ramas, about page four of your testimony, if you  
13 could turn there, please.

14 A Yes.

15 Q And looking at the top of page four, would it  
16 be fair to say that you criticize FPL's proposal to  
17 venture into the competitive gas drilling and production  
18 industry?

19 A Yes, I do. I don't -- as I explained in my  
20 testimony, I don't believe it's a normal function of a  
21 regulated utility.

22 Q You assert on lines 12 through 14 that FPL  
23 wants to subvert the Fuel Clause by using it to recover  
24 costs for its gas reserve project, correct?

25 A Yes, I do say that.

1           **Q     Would you agree that public utilities come in**  
2 **all sizes and shapes?**

3           A     Yes, I would agree.

4           **Q     Okay.**

5           A     I don't know how you would define shapes, but  
6 all different sizes and types of utilities.

7           **Q     Sizes and types is probably a better**  
8 **characterization.**

9                   And would you agree that different utilities  
10 **have different styles of management and different**  
11 **philosophies that they use in approaching the business**  
12 **of providing service to customers?**

13          A     Yes, I would agree with that.

14          **Q     Would you agree that regardless of those**  
15 **differences, every public utility has a basic obligation**  
16 **to serve under what is generally understood as the**  
17 **regulatory compact?**

18          A     Yes. All regulated public utilities that are  
19 obligated to serve customers within a specific service  
20 area do have those obligations, yes.

21          **Q     Okay. But would you agree that different**  
22 **public utilities could approach that obligation in**  
23 **different ways?**

24          A     Yes, I would agree with that.

25          **Q     So would you agree that there is a range of**

1 management decisions that can be considered prudent,  
2 depending on the different way that different utilities  
3 would approach their obligation to serve customers?

4 A Yes.

5 Q Okay. Would you agree that management  
6 decisions can lead to different outcomes in the sense  
7 that prudent decisions can sometimes turn out to be  
8 better than expected, and other times to be less than  
9 hoped for?

10 A Yes. Absolutely.

11 Q And therefore, the price and reliability of  
12 service to customers can end up varying significantly  
13 across utilities, would you agree?

14 A Could you repeat the question? Price and --

15 Q Price and reliability of service can vary  
16 significantly across utilities?

17 A Yes. And I have seen large variances  
18 throughout the country, particularly with regards to  
19 reliability, but also with prices.

20 Q Okay. You have testified in a few cases  
21 involving FPL previously, correct?

22 A Correct.

23 Q Okay. So do you feel that you know FPL's  
24 business reasonably well?

25 A Reasonably well to the degree that I have

1 worked on several rate case proceedings and a storm cost  
2 docket review, yes.

3 Q Okay. Did you do any brushing up on FPL's  
4 recent performance in connection with your preparing to  
5 testify in this case?

6 A I guess -- could you define what you mean by  
7 recent performance? I was involved in the last rate  
8 case involving Florida Power & Light. With regards to  
9 recent performance, I believe I looked at the most  
10 recent Fuel Clause filing. Perhaps, if you have more  
11 specific questions as to what you mean by reviewing  
12 performance.

13 Q That's fine. You are familiar, I would assume  
14 fairly generally with FPL's performance as of the time  
15 of the 2012 FPL rate case, correct?

16 A Correct.

17 Q And did you do any sort of follow-up to  
18 determine how FPL has been performing in terms of price  
19 or reliability since that time?

20 A No.

21 Q Okay. You have testified in a number of other  
22 utility proceedings opposing utilities other than FPL in  
23 Florida previously, haven't you?

24 A Yes. As I indicated previously, I have  
25 testified in approximately 100 cases, so I have

1 testified in cases involving many other utilities.

2 Q Okay. Have you ever testified in a utility  
3 proceeding where the utility you were opposing had a  
4 lower nonfuel cost per kilowatt hour than FPL's?

5 A A lower nonfuel cost per kilowatt hour?

6 Q That's right.

7 A Not that I recall, but I wouldn't have  
8 necessarily have made that comparison.

9 Q Okay. What about the total cost per kilowatt  
10 hour for electricity, do you recall testifying against a  
11 utility with a lower total cost per kilowatt hour for  
12 electricity than FPL?

13 A No. Typically I wouldn't look at the  
14 resulting cost per kilowatt hour. I would look into all  
15 the different costs -- most of my experience has been  
16 with the revenue requirement for utilities, so I would  
17 have looked at the different items calculating those  
18 revenue requirements and not necessarily opine, then, if  
19 the resulting cost per kilowatt hour was comparable to  
20 other entities or not.

21 Q Okay. So would it also be true that you are  
22 not aware of whether any other utility in whose  
23 proceedings you have testified has a lower system  
24 average heat rate for fossil fuel generation than FPL?

25 A I wouldn't know that sitting here. No.

1 Q Okay. Am I correct that -- well, are you  
2 aware that FPL has made a number of decisions over the  
3 last 15 years to modernize and upgrade its generation  
4 fleet?

5 A Yes, I am.

6 Q Would you agree that FPL's modernization of  
7 its plants at Cape Canaveral, Riviera Beach and Port  
8 Everglades are examples of this sort of modernization  
9 and upgrading decisions?

10 A Yes.

11 Q With respect to those projects, do you know  
12 whether OPC supported, opposed or was neutral to FPL's  
13 proposals to undertake those projects?

14 A I don't recall.

15 Q Would you agree that at the time FPL was  
16 undertaking those modernization efforts, not everyone  
17 else in the industry was doing the same thing?

18 A That's kind of a broad statement. I am not  
19 specifically aware.

20 Q Are you aware of utilities elsewhere in the  
21 country that have done more than FPL to modernize their  
22 generation fleets over, say, the last decade?

23 A Not specifically. I am aware of other  
24 utilities that, say, have converted their facilities  
25 from coal to natural gas, or input additional cleaner

1 technologies within those plants. Whether or not the  
2 level investment is equal to or greater than the total  
3 amount FPL has invested, I am not certain.

4 **Q Okay. Would you agree that those**  
5 **modernization investments have proven to be a good idea**  
6 **in view of the EPA's 111(d) regulations that are in the**  
7 **process of being finalized?**

8 A It's my understanding that it would help to  
9 achieve compliance with those standards.

10 **Q So in preparing your testimony for this case,**  
11 **did you ask OPC, or did you undertake on your own any**  
12 **assessment of FPL's track record in making first mover**  
13 **type of decisions on modernization?**

14 A No, I didn't see them as any way relevant to  
15 whether or not the company should be permitted to  
16 venture into gas reserves, gas exploration, gas  
17 production, gas drilling, and whether or not that should  
18 become incorporated within the fuel cost recovery  
19 clause. I didn't see that as relevant to what I was  
20 looking at in this case.

21 **Q You testified, you said just a moment ago, in**  
22 **the FPL's 2012 rate case; correct?**

23 A Correct.

24 **Q Okay. And you are aware that FPL's proposed**  
25 **asset optimization program was heavily opposed by OPC in**

1 **that docket?**

2 A I don't recall them specifically opposing it,  
3 but it wouldn't surprise me. I don't believe it was  
4 anything I had addressed in my testimony in that case.

5 Q Do you know whether the asset optimization  
6 program that was proposed in that proceeding was  
7 considered unique or creative at the time?

8 A No, I am not specifically aware of that.

9 Q You don't know one way or the other?

10 A No.

11 Q Do you recall any of the Commissioners'  
12 references to that program as being creative?

13 A I don't recall that.

14 Q Okay. In preparing your testimony for this  
15 case, did you ask OPC how that asset optimization  
16 program has been working out for FPL's customers?

17 A No, I did not. In fact, I did, I believe,  
18 have some data requests about the correlation between  
19 that program and the gas that would be received from  
20 this venture and potential future gas joint ventures.  
21 But, no, I did not inquire as to what the outcome of  
22 that optimization program has been.

23 Q So you don't know, sitting here today, how  
24 much savings have been realized for customers as a  
25 result of the program?

1           A     No.

2           Q     Okay.  If opposition to the modernization  
3 projects and the asset optimization program had  
4 prevailed such that FPL had not pursued them, do you  
5 have any idea how much higher FPL's rates would be today  
6 than they are?

7           A     No, I don't.  But again, I don't find that  
8 correlation relevant to the issue at hand in this case.

9           Q     I would like you to turn to page three of your  
10 testimony, and in particular, line 16.  You have a  
11 statement starting on line 15, actually, however,  
12 capital investments in gas exploration, drilling and  
13 production joint ventures are so foreign to an electric  
14 utility's regulated monopoly business that such items  
15 are incompatible with, et cetera, do you see that?

16          A     Yes, I do.

17          Q     And is this one of the bases for your  
18 recommended rejection of FPL's gas reserves project  
19 proposal?

20          A     It's one of several reasons identified in my  
21 testimony, just demonstrate this is not part of what  
22 would typically be considered in base rates of an  
23 electric utility.  It's not a monopoly function.  So  
24 it's one of several reasons I identify within my  
25 testimony.

1           **Q     Do you know when investments in nuclear power**  
2 **were first made by electric utilities?**

3           A     Not as I sit here. I believe it was before I  
4 was testifying.

5           **Q     Would you imagine probably sometime in the**  
6 **late '60s, early 1970s?**

7           A     Yes, I would agree with that timeframe.

8           **Q     Okay. Prior to that time, would you agree**  
9 **that nuclear power assets had not been included in**  
10 **utilities' rate base?**

11          A     Generation plants had been, but perhaps not  
12 nuclear generation plants.

13          **Q     Okay. Are you aware that FPL has nuclear fuel**  
14 **for its nuclear plants included in rate base?**

15          A     That's my understanding, yes.

16          **Q     Okay. Do you think that would have been**  
17 **considered a novel treatment for fuel prior to the**  
18 **advent of nuclear power generation facilities coming**  
19 **into the utilities fleet?**

20          A     Yes. If you don't have nuclear plants, it  
21 wouldn't make any sense to have the fuel for those  
22 generation plants to get included in the rate base.

23          **Q     But are you aware of other instances where the**  
24 **fuel for a plant was included in rate base prior to**  
25 **nuclear generation?**

1           A       That would be before the timeframe in which I  
2 testified. I would assume it may have been, but I  
3 couldn't testify that it was.

4           **Q       Okay. Do you have a definition of used and**  
5 **useful that you are comfortable giving to the**  
6 **Commission?**

7           A       I would think of used and useful as being, as  
8 an example, say a generating asset is an asset that's  
9 actually in service and being used to provide service to  
10 customers. So it's still an asset that's being actually  
11 used in providing service to customers.

12          **Q       Now, the term that I had cited earlier,**  
13 **foreign to an electric utility's regulated monopoly**  
14 **power business, that's your term, is it not?**

15          A       Yeah. I don't believe I have seen it in any  
16 authoritative source, the term "foreign to".

17          **Q       Have you seen it used in any Florida Public**  
18 **Service Commission order or --**

19          A       The specific terms "foreign to"?

20          **Q       Yes.**

21          A       Not that I recall.

22          **Q       Okay.**

23          A       You could replace that with "different form",  
24 I suppose. Just "foreign to" just seemed to adequately  
25 describe it.

1           **Q     Let's go back to the used and useful**  
2           **definition that you had provided of assets that are**  
3           **being used and productively used in providing utility**  
4           **service, is that a fair paraphrase of your definition?**

5           A     That's a fair paraphrase.

6           **Q     Okay.  If FPL were to make the investment it**  
7           **has proposed in gas reserves, the gas produced from**  
8           **those reserves would be used by FPL, would it not?**

9           A     Under the company's proposal, it's my  
10          understanding that their intent is that that gas be used  
11          to supply to generate gas-fired generation plants that  
12          are used to serve customers.

13          **Q     Okay.  And would the gas not also be useful in**  
14          **the sense that it productively allows the plants to**  
15          **generate electricity?**

16          A     Under that case, yes, they could be used and  
17          useful, but that does not mean that it's appropriate to  
18          invest in a highly competitive industry that is not a  
19          necessary industry to go into to provide service to  
20          customers.

21          **Q     Are you aware of this commission having**  
22          **approved FPL's proposal to buy railcars to deliver coal**  
23          **to its share of the Scherer unit for a power plant in**  
24          **Georgia?**

25          A     Yes, I am aware that they approved that in

1 order to make it more cost-effective to deliver fuel to  
2 the plant.

3 Q Okay. And pretty much the alternative to that  
4 was, instead of owning the railcars, to lease them,  
5 correct?

6 A That's my understanding.

7 Q Okay.

8 A Or there could potentially be another scenario  
9 in which another third-party delivers the coal directly  
10 to the plant. I wasn't involved in that specific case.

11 Q Some form of delivery that didn't involve  
12 owning the cars, but would either be leasing cars or  
13 just paying someone -- some rail service to deliver the  
14 coal, correct?

15 A Correct.

16 Q And in that instance, what the Commission  
17 would be comparing is the cost of buying, and then a  
18 return on the railcars, versus whatever it would have to  
19 pay, either to lease them or to have the transportation  
20 service provide the delivery of the coal, correct?

21 A Correct.

22 Q Okay. Would you agree that the railcars being  
23 used actually to deliver coal to Scherer, and doing so  
24 at a cost to customers that was lower than the sort of a  
25 voided lease costs made them, therefore, used and useful

1 **investments?**

2 A Yes, that the Commission looked at the facts  
3 and circumstances in that case, and there was enough  
4 evidence demonstrating that there would be cost savings  
5 to customers as a result of that, so the Commission  
6 approved it.

7 Q Right. Would you agree that there could be  
8 many reasons why an investment might be found used and  
9 useful?

10 A Yeah. Yes, I would.

11 Q Let me give you some examples. That's  
12 probably pretty open-ended.

13 Would you agree that improved reliability  
14 might be one of the reasons that an investment could be  
15 found to be used and useful?

16 A Yes, if the investment is actually made and is  
17 in service, then, yes, I would agree that that could be  
18 found used and useful.

19 Q An investment made in order to achieve  
20 regulatory compliance, that could make it used and  
21 useful, correct?

22 A If it's completed and placed into service,  
23 yes, it would be used and useful.

24 Q Okay. And investments made to improve the  
25 efficiency of a facility, if the efficiency improvements

1     **are cost justified, would that be used and useful?**

2           A     It could be used and useful.  Again, if it's  
3     in service and actually providing service, or assisting  
4     in providing service, it could be used an useful, yes.

5           Q     **So would you agree, there is no finite or**  
6     **closed list of reasons that could justify an investment**  
7     **as used and useful, it really depends on the facts and**  
8     **circumstances of each individual case?**

9           A     Yes.  And I believe I agreed with you earlier,  
10    that under this scenario, you know, that investment  
11    could be used and it could be useful, but that doesn't  
12    necessarily mean that it should be incorporated in rates  
13    charged to customers.

14          Q     **Okay.  So it's your testimony that property**  
15    **that is an asset that is used and useful in providing**  
16    **utility service, that utility, nonetheless, should not**  
17    **be permitted to recover the cost of that investment?**

18          A     I guess I should correct how I responded to  
19    that.  Yes, the costs should be recovered.  And, again  
20    in this case, I haven't said that if this transaction  
21    goes forward that no cost should be recovered; rather,  
22    it's my opinion that the costs to be recovered should be  
23    based on the market of gas because there is a robust  
24    market out there for natural gas production.

25          Q     **But would you agree that if -- and assume for**

1    **this hypothetical, that FPL's projection is accurate and**  
2    **reliable, that there would be a significant level of net**  
3    **present value fuel savings to customers as a result of**  
4    **owning a gas reserve instead of buying the equivalent**  
5    **amount of gas at market prices, if that were true, would**  
6    **you consider that investment to be used and useful?**

7           A     It may be used and useful.  But, again, it's  
8    not a monopoly function that the company needs to enter  
9    no.  There is a competitive market out there for that,  
10   so it's my opinion that the company's request in this  
11   case shouldn't be approved.  But you are right, it could  
12   be used -- it could end up ultimately being used and  
13   useful in providing service to customers.

14           Q     **In going back to the railcars, there are --**  
15    **there were, and remain, alternatives to owning railcars,**  
16    **correct?  I mean, there is the option of leasing them.**  
17    **There is, as you said, the possibility of just obtaining**  
18    **rail transport services from a railroad, or whoever, to**  
19    **deliver the coal; correct?**

20           A     Yes.  I would agree with that.

21           Q     **And do you have any reason to believe that**  
22    **those aren't competitive markets for providing those**  
23    **services?**

24           A     No, I do not.  Again, it's my understanding  
25    that that case, the company was able to clearly

1 demonstrate that there would, in fact, be cost savings.

2           **Q     Okay. So, again, if that circumstance**  
3 **justified Fuel Clause recovery, what difference, other**  
4 **than your disagreement over the certainty of FPL's**  
5 **objections would there be with respect to the gas**  
6 **reserve projects?**

7           A     The gas reserve projects are risky ventures  
8 into a highly competitive industry. There is no  
9 guarantee that a cost savings would result. The  
10 projected cost savings are based on a 50-year projection  
11 of fuel costs, and assumed production costs, and  
12 assumptions regarding how much gas can be withdrawn.  
13 There is a lot more assumptions going into that, and a  
14 lot more uncertainty and risk as compared to buying some  
15 railcars that are used to deliver gas to a plant.

16                     And again, Daniel Lawton, on behalf of OPC,  
17 deals a lot more in his testimony with the risks  
18 associated with that industry and the cost projections.

19           **Q     Would you agree that decisions to spend large**  
20 **sums of money on modernizing power plants also involve,**  
21 **of necessity, projections as to what future fuel costs**  
22 **will be, and what the costs of building and operating**  
23 **the plants will be?**

24           A     Yes, I would agree with that.

25           **Q     Okay. I want to try a hypothetical with you**

1 here, Ms. Ramas, and it's relatively complicated, so --

2 A Okay.

3 Q -- a pen and paper might be useful.

4 So assume a regulated utility has a rate base  
5 \$10,000 with a 10-percent regulated rate of return,  
6 okay. The utility incurs \$1,000 of expense and has 20  
7 customers. So this would equate to a revenue  
8 requirement of \$100 per customer, consisting of \$50 to  
9 recover expenses and \$50 to provide a return on rate  
10 base.

11 A I am sorry, could you slow down? I am trying  
12 to take notes here --

13 Q Sure. I'm sorry.

14 A -- since it's a pretty detailed hypothetical?

15 Q Okay. Let me --

16 A My last note --

17 Q Did you get the \$1,000 of expense and 20  
18 customers?

19 A Yes. And the hundred dollars per customer.

20 Q Right. \$100 per customer, and then that's \$50  
21 to cover expense. In other words, the \$1,000 divided by  
22 20, right?

23 A Correct.

24 Q And then \$50 to provide a return on rate base,  
25 which would be, again, \$1,000, 10 percent times

1 10 percent -- I'm sorry -- \$10,000 times 10 percent  
2 regulated rate of return would be 1,000 divided by 20.

3 A Assuming no taxes in just a very simplistic  
4 example.

5 Q Highly simplified, yes.

6 Okay. Now, assume that the regulated utility  
7 has an opportunity to make an additional investment of  
8 \$1,000 that will provide benefits by reducing expenses  
9 by \$200. If the investment is made, the amount of  
10 return earned by the utility will increase by \$100, but  
11 the revenue requirements will decline to 95, so it would  
12 be \$55 to provide a return on rate base and \$40 to cover  
13 expenses; do you see that?

14 A Yes.

15 Q Okay. Assuming all other things are equal,  
16 should the regulated utility make that investment?

17 A It's hard to say with that hypothetical  
18 example. If we assume these are all costs that are cost  
19 to include in base rates and are necessary for providing  
20 service to customers, and that they could result in cost  
21 savings, and those cost savings are highly likely, it  
22 could be. But again, this is a very limited, high level  
23 hypothetical example.

24 Q Okay. But within the constraints of that  
25 hypothetical, if all of those facts were as

1 hypothesized, you would agree that utilities should make  
2 that investment, rather than foregoing it and leaving  
3 customers paying the higher level of total revenue  
4 requirement, wouldn't you?

5 A Based on the very limited but yet high level  
6 hypothetical, I could agree.

7 Q Okay. And if that investment were made, the  
8 utility's investors would be recovering a return on that  
9 additional \$1,000 investment, correct?

10 A Possibly, it would depend on the rate cases.  
11 Typically you set rates to allow a utility an  
12 opportunity to earn its authorized rate of return, not a  
13 guarantee that it will achieve that return. Between  
14 rate cases or between filings, you could earn higher or  
15 lower than that, but the --

16 Q One of the magic features of the hypothetical  
17 is that there is assumed to be instantaneous  
18 rate-making.

19 A Okay, then we really are hypothetical.

20 Q All right. Let me shift gears a bit with you,  
21 Ms. Ramas.

22 Page four of your testimony, the top of the  
23 page, you talk about FPL proposing to venture into the  
24 extremely competitive gas drilling and production  
25 industry; do you see that?

1           A     Page four?

2           **Q     Yes. Page four, at the top of the page there,**  
3 **lines one and two.**

4           A     Yes, I am there.

5           **Q     How do you do you define competitive as you**  
6 **are using it here?**

7           A     Competitive in that there are many  
8 participants within that industry. I believe currently  
9 FPL utilizes, I believe it was testified earlier today,  
10 approximately 40 different potential parties in  
11 acquiring natural gas, and I know there is more than 40  
12 entities that would sell natural gas in the market. So  
13 extremely competitive I would define as an industry in  
14 which there are multiple participants as opposed to a  
15 monopoly type industry.

16          **Q     Okay. So did you perform any analysis to**  
17 **conclude that the gas drilling and production market is**  
18 **extremely competitive?**

19          A     No. That's just based on my understanding of  
20 common knowledge, because there are so many players  
21 within that market, and so many shale plays and other  
22 plays throughout the country.

23          **Q     Okay. Are you aware that FPL purchases gas**  
24 **turbines, transformers, heat recovery steam generators**  
25 **or HRSGs, for use in providing electric service?**

1           A       Yes, they would need to occasionally purchase  
2 such things in order to maintain their plants and to --  
3 for the initial building of the plants.

4           **Q       Okay. Have you assessed the competitiveness**  
5 **of the market for HRSGs, gas turbines or transformers?**

6           A       Not specifically, no. I know there are  
7 several large organizations that provide that type of  
8 equipment, but, no, I haven't reviewed the  
9 competitiveness or the amount of players in that  
10 industry.

11          **Q       Do you have any sense of how the**  
12 **competitiveness of the markets for those components**  
13 **compares to the competitiveness of the gas drilling and**  
14 **production industry?**

15          A       It's my understanding there are a much more  
16 limited number of producers of those components for  
17 energy plants. Whereas, in the gas drilling and  
18 production and exploration industry, it's my  
19 understanding there are a lot more players.

20          **Q       Would you agree that most economists would**  
21 **conclude that competitive markets produce competitive**  
22 **prices?**

23          A       In general I would agree.

24          **Q       Have you done any sort of study or assessment**  
25 **of the market for drilling services?**

1           A     For drilling services?

2           Q     **Right.**

3           A     No.

4           Q     **No, okay.**

5                     **Do you consider yourself an expert in the**  
6 **field of drilling services?**

7           A     No, I do not.

8           Q     **Okay. So do you have any idea of whether**  
9 **drilling and production costs are going up or down?**

10          A     It's my understanding they are going down, but  
11 I don't have any specific thing I can cite to for that,  
12 just based on reading articles in the industry and  
13 information in this case.

14          Q     **Okay. Would you agree that the market for**  
15 **producing gas from shale is pretty active currently?**

16          A     Yes.

17          Q     **And would you agree, therefore, that the**  
18 **market for production in drilling operations, oil field**  
19 **services is pretty mature?**

20          A     That would be my understanding.

21          Q     **Okay. As a mature market, would you expect**  
22 **the prices in that to be relatively stable?**

23          A     As far as the actual drilling and production  
24 aspects of it?

25          Q     **Yes.**

1           A     Yeah, I would expect them to be somewhat  
2     stable.

3           Q     Okay.  Would you agree that the market for --  
4     **the commodity market for natural gas is rather volatile?**

5           A     Yes, I would agree.

6           Q     Would you agree that currently, with FPL  
7     **buying essentially 100 percent of its gas requirements**  
8     **in the commodity market at market prices, that customers**  
9     **bear the risk of all of that volatility in natural gas**  
10    **prices?**

11          A     It's my understanding the risk the customers  
12    bear is with the annual true up, so fluctuations during  
13    the year up and down aren't being experienced by  
14    customers throughout the year, that that's trued up  
15    annually.  So on an annual basis there can be  
16    fluctuation in that, right.

17          Q     **At the end of the day, the customers will pay**  
18    **the full experience, the full range of volatility in the**  
19    **natural gas prices, correct?  Just it may await the true**  
20    **up process before that's fully played out?**

21          A     Yeah.  The ups and downs that occur throughout  
22    the year will all be averaged into the fuel rate charge  
23    for the next year, and that rate will be based on the  
24    total costs actually incurred.  And the costs in any  
25    given period, or any given billing that the company

1 receives would have fluctuation and volatility.

2 Q And you are aware that FPL has a hedging  
3 program currently for its natural gas purchases?

4 A I understand they have one. I don't -- I am  
5 not proficient on the details of that program, but I  
6 understand they do have one in place.

7 Q Okay. Would it be your understanding that, to  
8 the extent FPL hedges a particular portion of the  
9 natural gas prices, if the market prices go up compared  
10 to the point at which they hedged, there will be savings  
11 that would be passed on to customers?

12 A Yes.

13 Q And then conversely, if the stock market goes  
14 down relative to the price at which FPL hedged, that  
15 there would be additional cost, and that additional cost  
16 would also be passed on to customers?

17 A Yes, that's my understanding.

18 Q Okay. Isn't that essentially what is expected  
19 to happen if FPL invests in the natural gas reserves  
20 that, to the extent market prices go up compared to  
21 expectations, the savings will be even larger than  
22 projected, and if the prices go down relative to  
23 projections, that the savings will be lower than  
24 expected?

25 A I don't agree that they are comparable because

1 there are so many additional variables going into  
2 venturing into gas reserve beyond just the impact of the  
3 market prices. You have the success of the wells. The  
4 production costs. The amount of wells that are drilled.  
5 The amount of wells that are successful or not  
6 successful. There are other items that can impact the  
7 price and whether or not there are resulting savings or  
8 benefits than just the market price of gas. I really  
9 don't see the two as comparable.

10 In this project, you are not locking in a set  
11 price and a set quantity for a set period of time.  
12 There are many variables associated with going into this  
13 new type of venture.

14 **Q But you have not conducted any sort of**  
15 **quantitative evaluation of that variability and the cost**  
16 **of production, have you?**

17 A No, I haven't.

18 **Q So you don't know how that variability**  
19 **compares to the variability of market prices for natural**  
20 **gas, do you?**

21 A No. You wouldn't have the month to month  
22 volatility to the degree you do with natural gas prices;  
23 but over the long-term, no, I haven't.

24 **Q Okay. Ms. Ramas, are you familiar with the**  
25 **concept of build or buy decisions, or capital**

1       **substitution?**

2           A       By build or buy decisions, do you mean  
3 decisions going into whether or not, say, a generation  
4 plant should be built versus buying electricity in the  
5 market?

6           **Q       That's right.**

7           A       I have some familiarity with that. And what  
8 was the second part of your question?

9           **Q       The second part of the question was on whether  
10 you are familiar with the concept of capital  
11 substitution, which I view is at least an alternative  
12 way of describing that same phenomenon?**

13          A       I don't know if I know it as a general term,  
14 but I understand the concept you are trying to make, as  
15 opposed to if you are going to construct something  
16 versus acquiring something in the market.

17          **Q       Would you agree that there are hundreds or  
18 probably thousands of inputs into the actual cost of  
19 service provided by an electric utility?**

20          A       Oh, absolutely. Yes.

21          **Q       Would you agree that utilities over the years  
22 have made a wide variety of decisions as to the  
23 appropriate build or buy approach to those inputs to  
24 providing service?**

25          A       Yes, would agree.

1           **Q**     Okay.  Would you agree that these factors  
2     would be relevant to the decision whether to build or  
3     buy with respect to an input the reliability that's  
4     achieved, supply, security, customer savings and price  
5     stability?

6           **A**     I agree those are all items that should be  
7     considered in deciding whether or not, say, a plant  
8     should be built versus energy purchased in the market.

9           **Q**     Okay.

10          **A**     You would look at the overall costs and risks  
11     associated with those projects.

12          **Q**     Okay.  Would you agree that in recent years,  
13     some utilities have been told by regulators or  
14     legislatures to divest themselves of generation and/or  
15     transmission?

16          **A**     Yes.  I have worked in several jurisdictions  
17     where the generation assets and transmission assets have  
18     been largely divested.

19          **Q**     Would you agree that those decisions have been  
20     made based, at least in part on the assumption or  
21     premise, that narrowing the scope of the utility  
22     investment and supply chain would produce lower overall  
23     prices for electric service?

24          **A**     Could you repeat that question?

25          **Q**     I will try.

1           **Would you agree that those decisions, the**  
2           **decisions requiring divestiture, have been made based, at**  
3           **least in part, on the assumption or premise that**  
4           **narrowing the scope of utility investment in the supply**  
5           **chain would produce lower overall prices for electric**  
6           **service?**

7           A       Yeah. It's my understanding that in requiring  
8           many utilities to divest of their generation assets, the  
9           thought was that it would introduce more competition  
10          into the industry that could result in lowering the cost  
11          of the long-term because you would have more players in  
12          the market, and it would be, therefore, competitive  
13          industry that would drive costs down. That's my  
14          understanding of the reasons why many jurisdictions have  
15          chosen to go the divestiture route.

16          **Q       Would you agree that there remains a lot of**  
17          **debate as to whether those policies have produced the**  
18          **desired results?**

19               MR. MOYLE: Mr. Chairman, this has gone on for  
20               quite some time. I am going to object on relevancy  
21               grounds. I mean, we are talking about what other  
22               jurisdictions have done with respect to divestiture.  
23               It's coming up on 10:30.

24               MR. BUTLER: It's also coming up on my last  
25               two questions.

1 MR. MOYLE: Oh, I will withdraw the objection.

2 THE WITNESS: And since it's 10:30, I believe  
3 there is a question out there, if you could repeat  
4 it?

5 BY MR. BUTLER:

6 Q Would you agree that there remains a lot of  
7 debate as to whether those policies, the divesture  
8 policies, have produced the intended results?

9 A Oh, yes, there has. And there is also the  
10 debate on whether or not a competitive industry did, in  
11 fact, result that drove costs down -- yes, there are  
12 many, many debates around the decision to divest, and  
13 whether or not certain functions should be reregulated.

14 Q So the bottom line is, in your view, that in  
15 the electric utility industry today, there really isn't  
16 an absolute and precise model as to what is or is not or  
17 should or should not be part of an electric utility  
18 investment, you would agree? In other words, how  
19 vertically integrated the utility should be?

20 A With regard to how vertically integrated,  
21 however, I would not agree that that would apply to this  
22 situation, because I am not aware of any electric  
23 utility in the country that has ever gone into an actual  
24 gas exploration and drilling production. That's taking  
25 it a step further from anything I have ever seen in the

1 country.

2 MR. BUTLER: Okay. Thank you. That's all the  
3 questions that I have.

4 THE WITNESS: Thank you.

5 CHAIRMAN GRAHAM: Staff?

6 MS. BARRERA: No questions.

7 CHAIRMAN GRAHAM: Commissioners.

8 Commissioner Balbis.

9 COMMISSIONER BALBIS: Thank you, Mr. Chairman.  
10 And it is past 10:15, so I will try not to descend  
11 it into the fireside chat portion of the  
12 questioning, but I do have a few questions for you,  
13 Ms. Ramas.

14 You indicate in your testimony and your  
15 summary and discussions, in responses to  
16 cross-examination that you feel there is a  
17 competitive market and, therefore, utilities should  
18 just pay market price.

19 THE WITNESS: Yes.

20 COMMISSIONER BALBIS: Okay. And so -- but  
21 wouldn't that keep utilities to continue being  
22 susceptible to market forces that are outside of  
23 their control?

24 THE WITNESS: With regards to gas exploration  
25 and drilling, yes, it would keep them susceptible

1 to items outside of their control --

2 COMMISSIONER BALBIS: What --

3 THE WITNESS: -- but again, I guess I am not  
4 sure I agree that a utility that has never done  
5 this before can somehow beat market and produce gas  
6 at a cost that's less than what's available in that  
7 market.

8 COMMISSIONER BALBIS: Well, and I will get to  
9 that. My question is, if they are just going to  
10 pay the market price, then they are going to  
11 continue to be susceptible to market forces,  
12 whether what we saw with the polar vortex in the  
13 northeast earlier this year that impacted prices, I  
14 mean, they would continue to be susceptible to  
15 that, you would agree?

16 THE WITNESS: To a degree. They do do some  
17 hedging now in Florida that lacks in costs -- in  
18 production and costs for short-term, but I am not  
19 aware of anything in the long-term that they can  
20 do.

21 COMMISSIONER BALBIS: Okay. But wouldn't one  
22 of the results of approving FPL's position -- or  
23 petition mitigate some of that susceptibility?

24 THE WITNESS: It may or it may not, because  
25 there is no guarantee with regards to the amount of

1 production that will come out. I mean, beyond just  
2 the Woodford Project in this case, the company is  
3 seeking approval for guidelines of potential future  
4 projects. At this point, I don't know that you can  
5 have any level of certainty with regards to what  
6 kind of production output, what portion of such  
7 wells could be successful or not successful. You  
8 are really taking on that market risk as far as the  
9 ability to continually find successful shale plays.

10 COMMISSIONER BALBIS: Right. But again, if  
11 you are focusing on insulating from market forces  
12 that are outside of their control, this --  
13 participation in the Woodford Project, and we will  
14 start with that --

15 THE WITNESS: Uh-huh.

16 COMMISSIONER BALBIS: -- that would insulate  
17 at least some of that exposure, would it not?

18 THE WITNESS: To the market price volatility,  
19 yes, it could dampen that.

20 COMMISSIONER BALBIS: Okay. And then you also  
21 recommended that, if we were to move forward, you  
22 would limit the price for the gas to the market  
23 price, so essentially having a cap, is that a  
24 good --

25 THE WITNESS: Really, our primary -- my

1 primary recommendation is that, based on prior  
2 commission orders, that the amount to be recovered  
3 through the Fuel Clause should be based on the  
4 market price of gas.

5 However, if the Commission determines that  
6 they should, in fact, receive fuel cost recovery  
7 associated with the capital portion, you know, of  
8 these costs, then I would recommend that the amount  
9 they recover be capped at the market cost of gas,  
10 so that they don't recover more than the cost  
11 that's available in the market.

12 COMMISSIONER BALBIS: Okay. So then a  
13 producer that enters into this contract would then  
14 not be able to realize the benefits -- the  
15 additional profits, if you will, there is no  
16 revenues associated with the higher price, correct?

17 THE WITNESS: Now, are you considering FPL to  
18 be the producer?

19 COMMISSIONER BALBIS: No. No. That would be  
20 the producer that's entering into this arrangement  
21 with FPL's subsidiary.

22 THE WITNESS: So say, for example PetroQuest?

23 COMMISSIONER BALBIS: Yes.

24 THE WITNESS: My understanding is that the  
25 natural gas that would be going to FPL and that the

1           company is seeking to recover through the Fuel  
2           Clause is limited to FPL's portion of the gas  
3           that's extracted from those wells. But under the  
4           agreements, and without getting into the  
5           confidential terms, PetroQuest retains its portion,  
6           or a percentage of that natural gas to market as it  
7           sees fit. That portion that stays under the  
8           ownership of PetroQuest would not then be passed on  
9           through the Fuel Clause unless it's acquired by FPL  
10          at the market price.

11                 So PetroQuest would still have an incentive to  
12          go forward if it finds the market price of gas  
13          would allow it to cover its investment for its  
14          portion of the gas that would be extracted.

15                 COMMISSIONER BALBIS: And would you assume  
16          that that would result in additional cost to the  
17          FPL subsidiary and FPL to provide that cap?

18                 THE WITNESS: I guess the cap with regards to  
19          the amount to be recovered through the Fuel Clause?

20                 COMMISSIONER BALBIS: Yes.

21                 THE WITNESS: I guess I don't understand what  
22          you mean by additional costs.

23                 COMMISSIONER BALBIS: Because there is  
24          additional risk now being applied to either the  
25          subsidiary or are PetroQuest, as an example,

1           wouldn't that result in additional costs?

2                   THE WITNESS:   Again, I am not sure how the  
3           risk is applied to PetroQuest, because the portion  
4           of the gas that's extracted that remains under the  
5           ownership of PetroQuest, they will still be  
6           marketing that, is my understanding.  100 percent  
7           of the gas isn't going to FPL only, FPL's ownership  
8           interest percentage of that gas.  So how the  
9           Commission approves this transaction, whether or  
10          not it allows the company's proposal, I don't think  
11          really has a bearing on PetroQuest's potential  
12          profit for its portion of the gas that's being  
13          withdrawn, because PetroQuest's portion, that gas  
14          would not be coming through the Fuel Clause.

15                  COMMISSIONER BALBIS:   Okay.  And then I think  
16          this might be my last question, but in FPL's  
17          projections for the market price forecast, each and  
18          every one of those is compared to the affected  
19          price for PetroQuest, it was higher than the  
20          affected, right?

21                  THE WITNESS:   Yes.

22                  COMMISSIONER BALBIS:   Are you questioning the  
23          validity of those projections?

24                  THE WITNESS:   Oh, of the cost of gas coming  
25          from PetroQuest operating it, yes.  What I

1 understand those are comparing to are the costs  
2 that would be passed on to FPL for its portion of  
3 the gas that's extracted from those joint venture  
4 operations. I am not sure that -- I might not be  
5 understanding your question.

6 COMMISSIONER BALBIS: No, that's okay. It's  
7 just that in FPL's economic evaluation, each and  
8 every year that they projected for the FPL market  
9 price forecast showed a price -- the market price  
10 to be higher than the effective cost coming from  
11 the PetroQuest contract.

12 THE WITNESS: Yeah. Uh-huh. Correct.

13 COMMISSIONER BALBIS: Each and every one. And  
14 if we do not move forward with this contract,  
15 aren't we eliminating the opportunity for customers  
16 to realize those savings?

17 THE WITNESS: Yes. But again, if the opposite  
18 ends up being true, where the market price of gas  
19 is lower than that production cost, then you are  
20 requiring ratepayers to also pay for that  
21 difference while, at the same time, guaranteeing an  
22 equity return on the investment made by FPL in the  
23 venture.

24 COMMISSIONER BALBIS: Other than your  
25 recommendation to limit to the market price, do you

1 have any other recommendations that could further  
2 protect ratepayers while still giving them the  
3 ability to realize any potential savings, either in  
4 the PetroQuest or the next stage of the process,  
5 which is the parameters, or guidelines?

6 THE WITNESS: You mean as far as incentives to  
7 go forward with the transactions perhaps? Again,  
8 my primary recommendation is that it be based on  
9 the market price of gas. And in my opinion, that  
10 should give FPL a pretty good incentive to go  
11 forward with these if they think there is a high  
12 level of confidence that their projections will pan  
13 out, because they could profit, you know, above the  
14 rate of return if that be the case.

15 Under the alternative scenario I offered,  
16 which is more similar to what was done in a TECO  
17 case, the actual production costs would be flowed  
18 through the fuel costs as proposed by FPL but  
19 capped at the market price of gas, just as a way to  
20 protect ratepayers in this scenario.

21 I really don't see under the company's  
22 proposal any protection measures in place to  
23 protect ratepayers should, say, the cost of gas  
24 decline substantially. There is nothing in there  
25 really projecting them over this project that's

1 projected to last 30 to 50 years.

2 COMMISSIONER BALBIS: Okay. Thank you.

3 THE WITNESS: You are welcome.

4 CHAIRMAN GRAHAM: Commissioner Brown.

5 COMMISSIONER BROWN: Thank you, follow-up to  
6 that.

7 You say that you don't foresee any protection  
8 measures in place should the cost of gas decline.  
9 What kind of measures would you proffer?

10 THE WITNESS: I really haven't thought of  
11 different scenarios of ways to flow this through,  
12 because it's my opinion it shouldn't go through the  
13 Fuel Clause as proposed.

14 COMMISSIONER BROWN: It is a form of hedging,  
15 per se. So if we take that argument, then what  
16 protection mechanisms would there be?

17 THE WITNESS: I think the main protection I  
18 recommend is that it be based on the market price  
19 of gas, or capped at the market price of gas. If  
20 you cap it at the market price of gas, that would  
21 provide a great protection to customers because  
22 they wouldn't be paying more than they otherwise  
23 would have paid.

24 COMMISSIONER BROWN: Okay. So you are saying  
25 cap it at the market price of gas, but -- so that's

1 ignoring all capital expenditures associated with  
2 the overall project then?

3 THE WITNESS: What you would do under that  
4 scenario is you would -- to do the calculations the  
5 way the company's proposed them, I believe in Ms.  
6 Ousdahl's exhibit, where she shows how you would  
7 calculate the revenue requirements associated with  
8 it, which would include the rate of return on the  
9 investment, but if that total cost, you know, the  
10 return, all the expenses, the production costs  
11 exceed the market price of gas, then it would be my  
12 recommendation that you cap it market price of gas.

13 COMMISSIONER BROWN: Okay. Thank you.

14 THE WITNESS: You are welcome.

15 CHAIRMAN GRAHAM: Commissioner Balbis.

16 COMMISSIONER BALBIS: Thank you. I just want  
17 to follow up a little bit more on this.

18 THE WITNESS: Okay.

19 COMMISSIONER BALBIS: And just come up with an  
20 example, and I will just use the numbers from the  
21 2015 projection from FPL and the market price  
22 forecast versus the effective cost for the  
23 PetroQuest contract. And in that case, they -- let  
24 me make sure I am using the right exhibit -- but a  
25 \$3.75 per MMBTU is the market price forecast, and

1 effective cost is 3.48. So your proposal is that  
2 if that market -- if the actual price is below the  
3 3.48, then FPL -- well, what is your proposal?  
4 Because it seems to me it's applying a lot of risk  
5 to the producer, and that risk has to have an  
6 associated increase in cost.

7 THE WITNESS: Yes. I mean, under that  
8 scenario where the market price is \$3.75 and their  
9 production cost with the return on investment  
10 included is 3.48, it would be my position that it  
11 should flow through the Fuel Clause based on that  
12 market cost of gas at 3.75, which would provide,  
13 you know, quite the benefit to FPL in that  
14 scenario.

15 COMMISSIONER BALBIS: Right. And so now we  
16 are looking at the alternative, the price -- the  
17 market price is below 3.48, so your proposal is  
18 that FPL could only recover whatever the market  
19 price is, say it's \$2.50?

20 THE WITNESS: Yes, that would be my proposal.

21 COMMISSIONER BALBIS: Okay. So all of that  
22 investment and all of that risk is borne by the  
23 producers and/or FPL?

24 THE WITNESS: Yeah. If FPL chooses to go into  
25 a competitive industry, it's my opinion, then,

1 investors should bear the risk that the results of  
2 that venture, you know, won't resulting in output  
3 that's less than the market cost of gas, rather  
4 than, under the company's proposal, you are putting  
5 100 percent of that risk on customers.

6 COMMISSIONER BALBIS: Well, there is two  
7 issues that I have. One, I don't see how that's  
8 not going to result in additional costs. And I  
9 think that's why we haven't seen these long-term  
10 contracts where a portion of the risk, or  
11 100 percent risk will be borne by the producer, and  
12 I think that's why these are not existing.

13 So in this instant, the entity, which in this  
14 case would be the ratepayers, who are going to  
15 benefit are from that drop or that increase in the  
16 market price, those are the ones that are going to  
17 get the benefit. And under your proposal, the risk  
18 is going to be borne by the entity, at least in  
19 this case, PetroQuest, which does not receive any  
20 benefit from.

21 THE WITNESS: Again, I am sorry, I guess I  
22 don't understand how PetroQuest is being harmed by  
23 this, because they are still going to be paid by  
24 FPL or its subsidiary the full cost that would flow  
25 through the JIBs. So I guess I don't understand

1           how PetroQuest would be harmed by that.

2                   I mean, they are operator, but it's my  
3           understanding under the agreement, no matter -- if  
4           FPL goes forward with it, that under the agreement,  
5           FPL would still pay PetroQuest the costs that are  
6           incurred based on those JIBs, regardless of what  
7           recovery method that the Commission approves.

8                   COMMISSIONER BALBIS: No, and I agree. But if  
9           you look at PetroQuest acting on its own as a  
10          producer, then this price goes up, they could have  
11          additional revenues, et cetera. So I think you are  
12          assigning -- your proposal assigns some risk to the  
13          parties that are not receiving the benefit of the  
14          lower gas prices. And in FPL's proposal, at least  
15          there is an opportunity for the customers to  
16          benefit from the fact that their effective cost is  
17          less than the market price, and that's just -- you  
18          know, I wanted to flesh out a little bit.

19                  THE WITNESS: Yeah, if their projections  
20          panned out, there could be a lower to customers  
21          that results.

22                  COMMISSIONER BALBIS: Okay. So other than  
23          that recommendation, you do not have any other  
24          recommendations or additional protections to the  
25          framework that could perhaps protect customers

1 without incurring additional costs?

2 THE WITNESS: I haven't offered any, no.

3 COMMISSIONER BALBIS: Okay. Thank you.

4 THE WITNESS: You are welcome.

5 CHAIRMAN GRAHAM: Redirect?

6 MR. REHWINKEL: Thank you, Mr. Chairman.

7 REDIRECT EXAMINATION

8 BY MR. REHWINKEL:

9 Q Ms. Ramas, you were asked a series of  
10 questions about FPL's efforts, by Mr. Butler, relating  
11 to what I will generally call them being a first mover;  
12 do you recall that?

13 A I don't recall -- oh, yeah. Yes, I do.

14 Q With respect to modernization of plants and  
15 things like that?

16 A Yes.

17 Q Okay. Do you think a utility should be  
18 giving -- that may have taken steps for their benefit in  
19 that way, that generates lower prices, should be given  
20 extra leeway to make speculative investments in gas  
21 reserves?

22 A No, I do not.

23 Q Are you familiar with an effort by FP&L to  
24 have a coal fire plant called the Glades Plant approved  
25 by the Commission?

1           A       Was that the plant that would have been a  
2 gasification plant?

3           Q       **It's the one that the Governor and Cabinet**  
4 **turned down, or do you --**

5           A       I don't have any specific knowledge on that.

6           Q       **All right. Have you ever seen a used and**  
7 **useful concept applied to an item that is not**  
8 **capitalized?**

9           A       To an item that's not capitalized? Typically,  
10 when you look at the term used and useful, you are  
11 dealing with capital items.

12          Q       **Is gas that has been recovered capitalized?**

13          A       No.

14          Q       **You were asked a question about -- by**  
15 **Commissioner Brown about additional protections that you**  
16 **might recommend. Do you see -- do you accept that the**  
17 **proposal by FPL is a hedge?**

18          A       Not under my understanding of what a hedge is,  
19 no.

20          Q       **Okay. Is it the Public Counsel's burden, in**  
21 **your opinion, to identify protections or items that**  
22 **might make FPL's proposal better?**

23          A       No.

24                   MR. REHWINKEL: I have no further questions.

25                   Thank you.

1 CHAIRMAN GRAHAM: Exhibits.

2 MR. REHWINKEL: The Public Counsel moves  
3 Exhibit 34.

4 CHAIRMAN GRAHAM: Any objection to entering  
5 34? And I don't think there is any other exhibits  
6 offered. Okay.

7 (Whereupon, Exhibit No. 34 was received into  
8 evidence.)

9 MR. REHWINKEL: May Ms. Ramas be excused?

10 CHAIRMAN GRAHAM: Yes.

11 (Witness excused.)

12 CHAIRMAN GRAHAM: All right. I think we are  
13 about done for today.

14 Mr. Moyle, would you like to enter Mr.  
15 Pollock's stuff so we can close that out?

16 MR. MOYLE: Sure. FIPUG would move the  
17 introduction of Mr. Pollock's direct prefiled  
18 testimony into the record, along with exhibits JP-1  
19 through JP-4.

20 CHAIRMAN GRAHAM: Which is Exhibits 40 through  
21 43.

22 Any objection to entering Mr. Pollock's  
23 prefiled direct testimony and those four exhibits  
24 into the record?

25 MR. BUTLER: None from FPL.

1                   CHAIRMAN GRAHAM: We will enter those five  
2 things into the record.

3                   (Whereupon, Exhibit Nos. 40-43 were received  
4 into evidence.)

5                   MR. MOYLE: Thank you.

6                   (Whereupon, prefiled testimony was inserted.)

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**DIRECT TESTIMONY OF JEFFRY POLLOCK**

1 **Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A Jeffrey Pollock, 12647 Olive Blvd., Suite 585, St. Louis, MO 63141.

3 **Q WHAT IS YOUR OCCUPATION AND BY WHOM ARE YOU EMPLOYED?**

4 A I am an energy advisor and President of J. Pollock, Incorporated.

5 **Q PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.**

6 A I have a Bachelor of Science Degree in Electrical Engineering and a Masters in  
7 Business Administration from Washington University. Since graduation in 1975, I  
8 have been engaged in a variety of consulting assignments, including energy  
9 procurement and regulatory matters in both the United States and several  
10 Canadian provinces. My qualifications are documented in **Appendix A**. A partial  
11 list of my appearances is provided in **Appendix B** to this testimony.

12 **Q ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

13 A I am testifying on behalf of the Florida Industrial Power Users Group (FIPUG).  
14 Numerous FIPUG members purchase electricity from Florida Power & Light  
15 Company (FPL) under various rate schedules. They require a reliable affordably-  
16 priced supply of electricity to power their operations. FIPUG members who  
17 receive electrical service from FPL have substantial interests that will be affected  
18 by FPL's proposal to incur costs associated with the proposed acquisition, and  
19 include those costs in rates that they (and other FPL customers) will pay if FPL's  
20 Petition is approved.

21 **Q WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

22 A My testimony addresses FPL's proposal seeking determinations that:

- 1                   • It is prudent to acquire an interest in the Woodford Gas Reserves  
2                   Project (Woodford or Project);
- 3                   • The revenue requirements associated with investing in and  
4                   operating Woodford are eligible for recovery through the Fuel and  
5                   Purchased Power Cost Recovery Clause (Fuel Clause); and
- 6                   • FPL's proposed Gas Reserves Guidelines should be adopted by  
7                   the Commission to determine whether FPL should invest in future  
8                   natural gas reserve acquisitions without a formal review.<sup>1</sup>

9   **Q        ARE YOU SPONSORING ANY EXHIBITS WITH YOUR TESTIMONY?**

10  A        Yes. I am sponsoring **Exhibits JP-1** through **JP-4**. These exhibits were  
11            prepared by me or under my supervision and direction.

12  **Q        ARE YOU ADDRESSING ALL ASPECTS OF FPL'S PETITION?**

13  A        No. However, the fact that I am not addressing certain aspects of FPL's Petition  
14            should not be interpreted as an endorsement of its proposals, and any  
15            suggestion to the contrary is misplaced.

16  **Summary**

17  **Q        PLEASE SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS.**

18  A        Put simply, FPL will benefit more from its investment in Woodford than its  
19            customers. Further, there is no assurance that customers will benefit at all. If  
20            the customers' benefits should materialize, those benefits will be minimal and not  
21            significantly affect customers' electricity costs. Although FPL's benefits are  
22            virtually guaranteed, the benefits to FPL's customers are uncertain and will  
23            depend on the future market value of natural gas and the operating costs  
24            incurred to produce and deliver the gas to FPL.

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<sup>1</sup> Exhibit SF-9.

1                   As a first of its kind project for a vertically integrated electric utility, the  
2 Project raises broad policy considerations, such as:

- 3                   • Whether it is appropriate for FPL to use ratepayer-supplied capital  
4                   to make a 50-year investment in a more risky business (*i.e.*  
5                   natural gas extraction) than running an electric utility;
- 6                   • Whether Fuel Clause recovery, where FPL is guaranteed to  
7                   recover its investment and a full regulatory return on Woodford (or  
8                   other similar gas reserve projects), provides appropriate  
9                   incentives for FPL to maximize the benefits to FPL's customers;
- 10                  • Whether the Commission has the proper tools to appropriately  
11                  oversee FPL's management of Woodford and other gas reserve  
12                  acquisitions; and
- 13                  • Whether there are any other unknown risks for which customers  
14                  would be solely responsible over the 50-year assumed Project life.

15                  Accordingly, with only speculative and minimal customer benefits, and without  
16                  clear answers to these important policy questions in its proposed Gas Reserves  
17                  Guidelines, the Commission should reject FPL's arguments and deny its Petition.

18                  If the Commission approves the Petition, any general and administrative  
19                  (G&A) expenses charged to FPL should be recovered in base rates.

## 20 **Projected Benefits and Costs**

21 **Q       WHY IS FPL ASKING THE COMMISSION TO APPROVE ITS PETITION?**

22 **A**       FPL states that the Project would allow it to purchase natural gas in-kind at  
23                  actual production cost rather than in the market place at market prices. FPL  
24                  asserts that customers could benefit because it projects that actual production  
25                  costs will be below future natural gas market prices.<sup>2</sup> As discussed later,  
26                  customer benefits are highly uncertain.

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<sup>2</sup> Petition at 5-6.

1 **Q WHAT FACTORS WILL DRIVE THE ECONOMICS OF THE WOODFORD**  
2 **PROJECT?**

3 **A** The economics of FPL's investment in the Project will critically depend upon:

- 4 • The market value of the gas produced at Woodford, which in turn  
5 will depend on projected natural gas prices; and,  
6 • FPL's ability to manage the production costs and the costs of  
7 gathering and transporting natural gas from Woodford to the  
8 Southeast Supply Header Pipeline (SSHP).

9 **Q HOW WOULD FPL'S CUSTOMERS POSSIBLY BENEFIT FROM FPL'S**  
10 **INVESTMENT IN THE WOODFORD PROJECT?**

11 **A** FPL's customers would benefit, but only if the all-in costs of producing, gathering,  
12 transporting and managing the gas supply from Woodford, including  
13 compensating FPL for and providing a return on its investment, is below the  
14 market value of the natural gas produced.

15 **Q HAVE YOU REVIEWED FPL'S COST-BENEFIT ANALYSIS?**

16 **A** Yes. FPL presented a cost-benefit analysis for the 50-year estimated life of  
17 Woodford. The results of FPL's cost-benefit analysis are summarized in the  
18 table below.

<b>Woodford Project Summary of Sensitivity Scenarios (\$Million NPV)<sup>3</sup></b>			
<b>Production Sensitivity</b>	<b>Pricing Sensitivity</b>		
	<b>Low Case</b>	<b>Base Case</b>	<b>High Case</b>
<b>Low</b>	(\$14.4)	\$72.6	\$159.5
<b>Base</b>	\$10.3	\$106.9	\$203.5
<b>High</b>	\$34.1	\$140.4	\$246.7

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<sup>3</sup> Direct Testimony of Sam Forrest at 38.

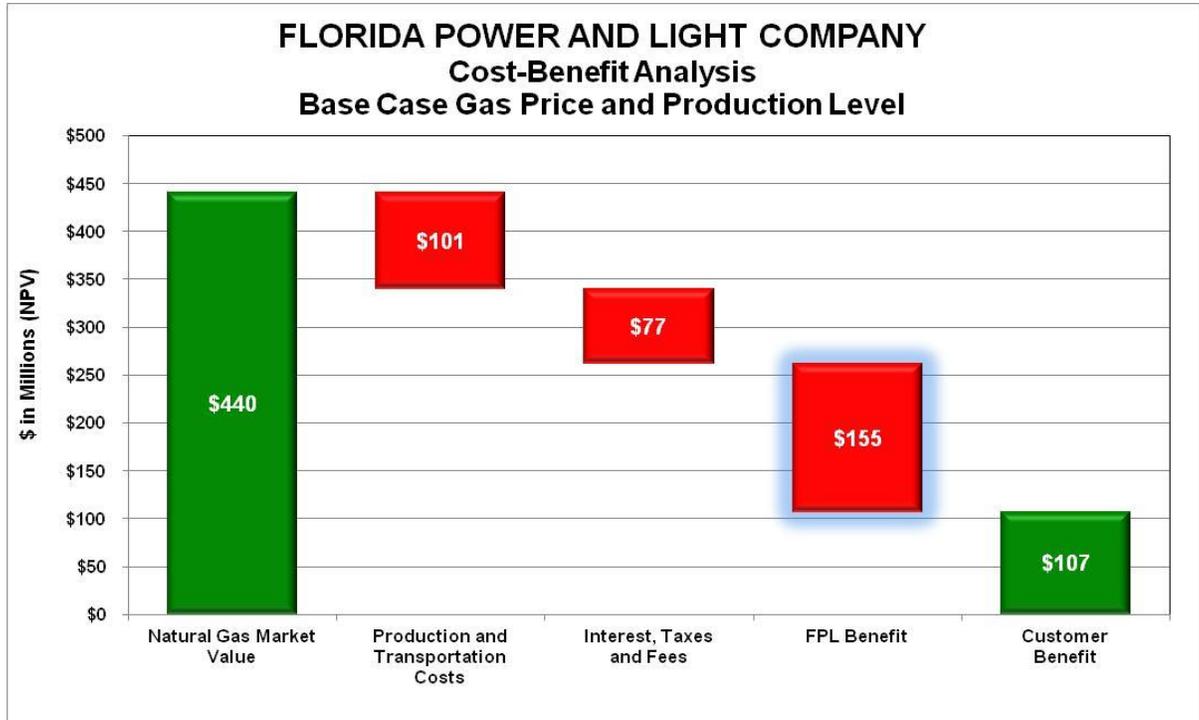
1 As can be seen, FPL conducted a base case and various sensitivity cases that  
2 reflect different production levels (*i.e.*, Production Sensitivity), as well as different  
3 natural gas pricing assumptions (*i.e.*, Pricing Sensitivity). FPL projects customer  
4 benefits ranging from -\$14.4 million (low natural gas pricing and low production  
5 levels) to \$246.7 million (high natural gas pricing and high production levels).  
6 FPL expects net benefits of \$107 million (*i.e.* base case pricing and production  
7 levels). However, FPL's sensitivity analysis indicates the customers' benefits are  
8 unclear and uncertain, while FPL's benefits are clear and certain.

9 **Q ARE THE PROJECTED FPL CUSTOMER BENEFITS SIGNIFICANT?**

10 A No, not really in the context of what FPL is seeking. As discussed later, the  
11 projected \$107 million net present value (NPV) benefits for FPL's customers  
12 would result in a savings of only 1.3¢ per 1,000 kilowatt hours (kWh).

13 **Q IF FPL IS PROJECTING ONLY MINIMAL CUSTOMER BENEFITS THEN WHY**  
14 **IS IT INTERESTED IN INVESTING IN THE WOODFORD PROJECT?**

15 A FPL will not only recover its incremental expenses (*i.e.*, production,  
16 transportation, interest, taxes and G&A), it will benefit by recovering its  
17 investment (*i.e.*, depletion) while earning a regulated return on the equity portion  
18 of its investment. The latter are clearly benefits to FPL and its shareholders. As  
19 can be seen, FPL's base case projections show that the FPL benefit would be  
20 \$155 million NPV. This is in contrast with a customer benefit of \$107 million  
21 NPV.



- 1 The corresponding results under the low and high gas price scenarios are shown  
2 in the table below.

<b>Woodford Project Cost-Benefit Analysis Base Case Production (\$Million NPV)</b>			
Component	Base Case Gas Price	Low Gas Price Case	High Gas Price Case
<b>Market Value</b>	\$440	\$344	\$537
<b>Production Cost</b>	\$23	\$23	\$23
<b>Transportation Cost</b>	\$78	\$78	\$78
<b>Interest, Taxes and G&amp;A</b>	\$77	\$77	\$77
<b>FPL Benefits</b>	\$155	\$155	\$155
<b>Customer Benefits</b>	\$107	\$10	\$204
<b>Projected Net Energy For Load (GWh)*</b>	7,998,616		
<b>Net Benefit Per 1,000 kWh</b>	1.3¢	0.1¢	2.5¢
<b>Source:</b> FPL's Response to OPC POD 12 (Confidential) and POD 34 * FPL's 2014 Ten Year Site Plan, Schedule 2.3, trended to 2065.			

1 **Q PLEASE EXPLAIN THE COMPONENTS OF THE COST-BENEFIT ANALYSIS.**

2 A Market value reflects the projected cost of purchasing natural gas in the market.  
3 Production costs are the costs incurred for exploration, drilling, and extracting  
4 natural gas. Transportation costs include “gathering” to move the gas from the  
5 producing fields to the pipeline and transportation from the pipeline to FPL.  
6 Interest, taxes and G&A expenses include FPL’s debt financing costs, taxes  
7 (including income tax on FPL’s equity return) and the fees charged to FPL to  
8 manage the Project. FPL benefits include the return of FPL’s investment as well  
9 as the return on the equity portion of this investment. Customer benefits are the  
10 difference between market value and sum of the direct operating costs (*i.e.*,  
11 production, transportation, interest, taxes and G&A) and FPL benefits.  
12 Essentially, FPL’s customers would receive the remaining market value, if any,  
13 after taking into account direct operating expenses and FPL benefits.

14 **Q WOULD THE FPL BENEFITS VARY UNDER ANY OF THE SCENARIOS THAT**  
15 **FPL MODELED IN ITS COST-BENEFIT ANALYSIS?**

16 A No. As shown in the above table, the FPL benefits would remain constant across  
17 all gas price scenarios. The same is also true across all production level  
18 scenarios. In other words, FPL’s cost recovery proposal would ensure that it  
19 recovers its investment and earns its full return on equity irrespective of whether  
20 FPL’s customers receive any benefits. As discussed later, the risk of investing in  
21 natural gas extraction are considerable. Thus, guaranteeing FPL full recovery of  
22 its investment, a fixed return on equity regardless of the outcome, while not  
23 providing similar guaranteed benefits to FPL’s customers, would not be in the  
24 public interest.

1 **Q DO YOU HAVE ANY CONCERNS ABOUT FPL'S COST-BENEFIT ANALYSIS?**

2 A Yes. First, as can be seen in the above table, production and transportation  
3 costs account for \$101 million of the projected total cost. Transportation costs  
4 assume that FPL would transport gas through the Enable Gas Transmission,  
5 LLC (Enable) system to the SSHP. However, in estimating these costs, FPL  
6 assumed no escalation of either production or transportation costs. Further, FPL  
7 conducted no sensitivity analysis using different assumptions for either  
8 production or transportation costs.

9 **Q IS IT REASONABLE TO ASSUME THAT PRODUCTION AND**  
10 **TRANSPORTATION COSTS WILL NOT CHANGE DURING THE PROJECTED**  
11 **50-YEAR LIFE OF THE WOODFORD PROJECT?**

12 A No. For example, it is unreasonable to expect that Enable will not seek to  
13 increase transportation rates over the 50 year projected life. In fact, Enable has  
14 not had a rate case to adjust its base transportation rates since 1996. With all of  
15 the investment that Enable (and its predecessors, CenterPoint Energy Gas  
16 Transmission and NorAm) has made to expand its system, it is only a matter of  
17 time before it seeks a substantial rate increase.

18 **Q HOW WOULD THE NET BENEFITS BE AFFECTED IF PRODUCTION AND**  
19 **TRANSPORTATION COSTS WERE ESCALATED AT A HIGHER RATE THAN**  
20 **FPL ASSUMED?**

21 A This is shown in **Exhibit JP-1**. As can be seen, applying a 2% per year  
22 escalation rate to production and transportation costs increases the direct  
23 operating costs by \$16 million NPV under FPL's base case production and gas  
24 price scenarios.

1 **Q DO YOU HAVE ANY OTHER CONCERNS WITH FPL'S COST-BENEFIT**  
2 **ANALYSIS?**

3 A Yes. As previously stated, the assumed market value of the natural gas  
4 produced at Woodford is a key assumption in determining whether FPL's  
5 customers will realize any benefits. FPL's forecast of natural gas prices,  
6 however, was based on market conditions that existed on October 7, 2013.<sup>4</sup> A  
7 more current forecast is presented in **Exhibit JP-2**, column 1. This updated  
8 forecast used the most recent 30-day average closing price of Henry Hub futures  
9 contracts through the year 2026, and subsequent years were escalated based on  
10 a long-term forecast conducted by the Energy Information Administration (EIA).  
11 For comparison, FPL's projected natural gas prices are also shown (column 2).  
12 As can be seen, gas prices have moved downward since last October.

13 **Q HOW WOULD USING A MORE CURRENT NATURAL GAS PRICE**  
14 **FORECAST AFFECT THE COSTS AND BENEFITS OF THE WOODFORD**  
15 **PROJECT?**

16 A The impact is shown in **Exhibit JP-3**. Using the current natural gas price  
17 forecast shown in **Exhibit JP-2**, the customer benefit would decline to \$27 million  
18 NPV. In other words, updating just the natural gas forecast reduces the  
19 projected customer benefit by \$80 million NPV. Despite the lower projected  
20 benefits, FPL would continue to earn \$155 million in benefits from Woodford.

21 **Q IN YOUR VIEW WILL CUSTOMERS BENEFIT FROM THE PROJECT?**

22 A No. Although there may be potential benefits for FPL's customers, they are  
23 unclear and uncertain. For example, assuming a 2% per year escalation rate in

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<sup>4</sup> Response to Staff Interrogatory No. 21.

1 both production and transportation costs and making use of the more recent  
 2 natural gas price forecast, customer benefits would be only \$11 million NPV.  
 3 Should any benefits materialize, they are too small to compensate for the  
 4 significant risks that customers would bear.

5 **Q DOES FPL'S COST-BENEFIT ANALYSIS DEMONSTRATE THAT INVESTING**  
 6 **IN THE WOODFORD PROJECT IS IN THE PUBLIC INTEREST?**

7 A No. FPL is providing no guarantees that FPL customers will realize tangible  
 8 benefits from the Project. However, the one constant is that FPL will recover its  
 9 investment and earn a full regulatory return, regardless of the benefits (if any)  
 10 that FPL's customers ultimately realize. Allowing FPL to venture into natural gas  
 11 exploration and extraction also allows FPL to expand its rate base in non-  
 12 traditional ways, a tactic that may benefit FPL shareholders, but holds only  
 13 marginal and questionable benefit for FPL's customers. Thus, FPL's proposal  
 14 fails to balance the interests of FPL and its customers. For this reason, it should  
 15 be rejected.

16 **Policy Issues**

17 **Q DOES FPL'S PETITION RAISE ANY POLICY ISSUES?**

18 A Yes. The Project would be the first of its kind for a large vertically integrated  
 19 electric utility. Thus, FPL's Petition raises important policy issues and  
 20 unanswered questions. Among the broader policy issues are:

- 21 • Should the Commission approve investments that provide a virtual  
 22 guaranteed benefit to the utility as an incentive to reduce fuel  
 23 costs?
- 24 • Should a fully regulated integrated electric utility be allowed to  
 25 become more vertically integrated by investing in natural gas  
 26 producing fields?

- 1                   • Does the Commission have the proper tools to properly oversee  
2                   FPL's management of an unrelated business?
- 3                   • Should a regulated utility be allowed to invest in a more risky  
4                   business without also subjecting its shareholders to higher risks?
- 5                   • Should the Commission adopt FPL's proposed guidelines for  
6                   participating in future ventures as the PSC guidelines?

7                   Among the questions unanswered by its Petition are:

- 8                   • How should FPL's customers be compensated for any "upstream"  
9                   sales of natural gas?
- 10                  • If the cost of gas from Woodford (or other similar gas reserve  
11                  projects) were to become uneconomical, should FPL continue to  
12                  recover its investment and earn a full regulatory return?

13    **Q        IS IT IN THE PUBLIC INTEREST TO GUARANTEE FPL A BENEFIT TO**  
14    **PROVIDE AN INCENTIVE TO LOWER FUEL COSTS?**

15    A        No. FPL has an obligation to provide reliable service at the lowest reasonable  
16              cost. This obligation includes procuring and managing natural gas and other  
17              production inputs in a prudent and reasonable manner that also benefits  
18              customers.

19    **Q        DOES FUEL CLAUSE RECOVERY PROVIDE A STRONG INCENTIVE TO**  
20    **DELIVER TANGIBLE BENEFITS TO FPL'S CUSTOMERS?**

21    A        No. Allowing full cost recovery in the Fuel Clause will not ensure that FPL's  
22              customers actually receive benefits from the Project.

23    **Q        HAS FPL COMMITTED TO PROVIDE SUPPLEMENTAL INFORMATION THAT**  
24    **WILL ALLOW THE COMMISSION TO EVALUATE THE BENEFITS TO**  
25    **CUSTOMERS?**

26    A        No. FPL proposes to supplement its Fuel Clause filings to include support for the  
27              costs incurred. Although this will allow the Commission to verify the accuracy of  
28              the costs, the supplemental information would provide no guidance on how well

1 the Project is being managed or whether it is producing tangible benefits to FPL  
2 customers.

3 Further, FPL is under no obligation to periodically determine whether the  
4 Project has provided or will provide real benefits to customers despite changing  
5 circumstances. In other words, customers have no assurance whatsoever that  
6 they have actually received any benefits or that they will likely benefit in the  
7 future from either Woodford or similar future gas reserve projects.

8 **Q WHAT ARE THE POLICY IMPLICATIONS OF FPL'S ACQUISITION OF THE**  
9 **WOODFORD PROJECT?**

10 A FPL's acquisition of Woodford would expand FPL's utility operations to include  
11 natural gas exploration and extraction. Currently, FPL controls electricity  
12 generation, delivery and sales to retail customers. The Woodford acquisition  
13 would give FPL control over the production of a portion of the natural gas used  
14 for generation. However, natural gas extraction is not a similar business to FPL's  
15 other utility operations. Further, this Commission has no direct regulatory  
16 authority over, or experience overseeing natural gas exploration and extraction.  
17 Commission oversight would clearly be more difficult in this case given that  
18 Woodford is nearly 1,000 miles from FPL's service area.

19 Thus, in the absence of direct regulatory authority over a new segment of  
20 FPL's business, the Commission may need new and better tools to ensure that  
21 FPL properly manages and oversees an unrelated business venture that will  
22 clearly benefit FPL, but may not benefit FPL's customers. It also means that FPL  
23 should have to meet higher standards to justify the recovery of all costs incurred  
24 at Woodford (or similar projects), including whether Woodford is being managed  
25 and operated at a level comparable to peer natural gas extraction operations.

1 Without these additional tools, and absent requiring FPL to demonstrate the  
2 prudence and reasonableness of the management of the Project relative to  
3 prudent industry practices, and that Woodford is providing tangible benefits to  
4 FPL's customers, the proposed acquisition would not be in the public interest.

5 **Q WHY ELSE IS THIS A CONCERN?**

6 A Unlike investing in a related business to an integrated investor-owned electric  
7 utility, natural gas exploration and extraction is a risky proposition. As evidence  
8 of the much higher risk, PetroQuest, the operator of Woodford, has a bond rating  
9 below investment grade. FPL is a strong A-rated company.

10 PetroQuest's lower bond rating reflects the numerous risks associated  
11 with natural gas extraction. For example, recoverable reserves and/or future  
12 production levels may be either greater or less-than expected. The same holds  
13 true with the level of future actual production, gathering and transportation  
14 expense. There are also environmental risks associated with natural gas  
15 fracking. In particular, the chemicals used in the fracking process could  
16 contaminate the ground water. Oklahoma, where the project in question is  
17 located, has also seen an increase in seismic activity that some suggest may be  
18 attributable to natural gas fracking. This raises questions of who bears the  
19 ultimate responsibility for any remediation costs as well as any ongoing legal  
20 liability. These risks are asymmetric because 75% of the benefits (*i.e.*, gas  
21 supply) from the Project will have been realized in just one-third of Woodford's  
22 projected 50-year life.

1 **Q WHY SHOULD THE COMMISSION BE CONCERNED ABOUT THE SALE OF**  
2 **ANY UPSTREAM NATURAL GAS?**

3 A Although FPL states that all of the in-kind gas will be used to generate electricity  
4 in FPL's footprint, there is a possibility that some or all of the natural gas  
5 produced at Woodford could be sold into the market. However, if the sale price  
6 is not at or above cost, which also includes FPL's depreciation and return on  
7 equity, FPL's customers would be unnecessarily subsidizing these market sales.  
8 In other words, FPL customers would bear the risk of these losses. The  
9 Commission should not sanction a policy that forces FPL's customers to  
10 subsidize upstream market natural gas sales.

11 **Q WHY SHOULD THE COMMISSION BE CONCERNED ABOUT COST**  
12 **RECOVERY IN THE EVENT THAT THE GAS FROM FPL'S ACQUISITION(S)**  
13 **BECOMES UNECONOMICAL?**

14 A FPL's cost recovery proposal, which locks in the recovery of FPL's investment  
15 and a return on equity, would shift all of the Project risk to its customers.  
16 However, FPL's customers should only bear risk to the extent that they can also  
17 have a reasonable opportunity to realize the benefits of the investment that they  
18 are underwriting. Thus, the Commission must not absolve FPL's shareholders of  
19 any risks associated with the investment in Woodford (or similar future gas  
20 reserve projects). FPL must have "skin in the game" to ensure a proper  
21 allocation of risk and to provide incentives to deliver savings to FPL customers.

22 **Q DO FPL'S PROPOSED GUIDELINES ADDRESS THE ABOVE ISSUES?**

23 A No. The proposed guidelines do not address the sharing of risks between FPL  
24 and FPL's customers particularly if the gas supply were to become uneconomical

1 or if other as yet unknown risks are encountered. Nor do they impose an  
 2 ongoing obligation on FPL to demonstrate that FPL customers have benefitted  
 3 and will benefit from acquiring natural gas reserves.

4 **Q WHY SHOULD THE COMMISSION GIVE MORE CAREFUL CONSIDERATION**  
 5 **TO THESE POLICY ISSUES AND UNANSWERED QUESTIONS?**

6 A Although FPL touts that it is not the first electric utility to invest in a working gas  
 7 production field, there is little precedent to draw upon for guidance.

8 **Q PLEASE EXPLAIN.**

9 A Only one other electric utility, NorthWestern Energy (NorthWestern), has  
 10 received approval to invest in a working natural gas field. **Exhibit JP-4** is a press  
 11 release downloaded from NorthWestern's web site describing NorthWestern's  
 12 purchase of the Battle Creek natural gas field.

13 **Q ARE THE CIRCUMSTANCES SURROUNDING NORTHWESTERN'S**  
 14 **PURCHASE OF BATTLE CREEK COMPARABLE TO FPL'S ACQUISITION**  
 15 **OF THE WOODFORD PROJECT?**

16 A No. Although NorthWestern is an integrated utility, like FPL, the circumstances  
 17 surrounding the Battle Creek purchase are clearly different from FPL's Woodford  
 18 acquisition. For example:

- 19 • NorthWestern sells *both* electricity and natural gas. Gas sales  
 20 account for about 25% of NorthWestern's revenues. Further, 20  
 21 billion cubic feet (BCF) out of NorthWestern's 25 BCF strategic  
 22 natural gas acquisitions serve that utility's natural gas customers.<sup>5</sup>  
 23 FPL sells only electricity.

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<sup>5</sup> FPL's Response to Staff's POD No. 5 (Bates No. 14-00330).

- 1 • NorthWestern does not own any significant natural gas  
 2 generation. In 2013, natural gas comprised only 15% of  
 3 NorthWestern's generation mix. It owns no combined cycle  
 4 natural gas plants as does FPL.
- 5 • The Battle Creek gas field was located in NorthWestern's service  
 6 territory. It had been in production since 1978. In fact,  
 7 NorthWestern purchased gas from the same field for its natural  
 8 gas customers. Woodford is located in Oklahoma and must be  
 9 transported approximately 480 miles to the SSHP and then an  
 10 additional 400 to 500 miles to FPL's service area.
- 11 • NorthWestern's purchase of a natural gas producing field was  
 12 made pursuant to a state statute, and it was subject to approval  
 13 from state regulators. It is unclear whether there is statutory  
 14 authority authorizing FPL's involvement in natural gas extraction.

15 **Q DOES THE APPROVAL OF NORTHWESTERN ENERGY'S BATTLE CREEK**  
 16 **ACQUISITION PROVIDE AMPLE PRECEDENT TO APPROVE FPL'S**  
 17 **PETITION?**

18 A No. Although the Montana Commission findings can provide some guidance in  
 19 this instance, the circumstances surrounding Battle Creek are clearly different  
 20 than for Woodford. For this reason, the Commission must require FPL to adhere  
 21 to a much higher burden of proof before the Woodford (or similar future gas  
 22 reserve projects) acquisition(s) can be considered to be in the public interest.

23 **Q SHOULD THE COMMISSION ADOPT FPL'S PROPOSED GUIDELINES AS**  
 24 **COMMISSION GUIDELINES?**

25 A No. First, as previously demonstrated, natural gas extraction is a risky business  
 26 that should not be financed by ratepayers without imposing comparable risks on  
 27 FPL's shareholders. Second, FPL's proposed guidelines would allow the  
 28 regulated utility to recover its costs with little to no risk, while placing market risk,  
 29 production risk, and operation risk on ratepayers. This is an unjustified and  
 30 unwarranted allocation of risk between the utility and its customers. Third, the  
 31 proposed guidelines are silent on several key policy issues. Fourth, the

1 Commission should not summarily accept FPL's proposal. It should hold  
2 workshops to hear from other investor-owned utilities and interested parties  
3 before considering or adopting a policy allowing electric utilities to engage in  
4 similar upstream projects.

5 Finally, FPL's suggested guidelines have a loophole that could render the  
6 other provisions of the guidelines meaningless. Specifically:

7 Flexibility to respond to market opportunities is in the best interest  
8 of FPL and its customers. Therefore, it is understood that FPL  
9 may ... seek Fuel Clause recovery for a project that deviates from  
10 one or more of the guidelines upon a showing that the project  
11 nonetheless is executed to benefit FPL customers.<sup>6</sup>

12 This provision would effectively allow FPL to not follow the guidelines should it  
13 decide not to do so. In sum, FPL's proposed guidelines should not be adopted  
14 as the Commission's guidelines because of the unnecessary and unwarranted  
15 risk placed on customers. If the Commission decides to authorize Florida's  
16 investor-owned to invest in upstream businesses, it should hold workshops and  
17 promulgate rules addressing the topic.

18 **Q WHAT DO YOU RECOMMEND?**

19 **A** The Commission should not approve the Woodford acquisition without thoroughly  
20 vetting the policy issues and the unanswered questions raised by FPL's Petition.  
21 There is too much risk on FPL's customers for little or no return, while providing  
22 ample (and virtually guaranteed) benefits to FPL. For these reasons, the Petition  
23 should be denied.

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<sup>6</sup> Exhibit SF-9, page 4.

1 **General and Administrative Expenses**

2 **Q IS FPL PROPOSING TO RECOVER GENERAL AND ADMINISTRATIVE**  
 3 **EXPENSES THROUGH THE FUEL CLAUSE?**

4 A Yes. FPL's cost-benefit analysis projects \$300,000 per year in G&A associated  
 5 with the Project. These expenses would be included in the Fuel Clause.<sup>7</sup>

6 **Q IS THE RECOVERY OF GENERAL AND ADMINISTRATIVE EXPENSES**  
 7 **THROUGH THE FUEL CLAUSE APPROPRIATE?**

8 A No. G&A fees do not qualify for Fuel Clause recovery because, unlike the  
 9 commodity and transportation cost, they are relatively fixed and not volatile.  
 10 These expenses do not vary with the volume of natural gas from the Project.  
 11 Further, given that 65% of FPL's generation is from natural gas, it follows that  
 12 FPL possesses the necessary resources to procure and manage its natural gas  
 13 supply.<sup>8</sup>

14 **Q DOES THE COMMISSION HAVE A SPECIFIC POLICY OF THE TYPES OF**  
 15 **COSTS FOR WHICH FUEL CLAUSE RECOVERY IS APPROPRIATE?**

16 A Yes. The Commission's policy was adopted in Order No. 14546 issued in Docket  
 17 No. 850001-EI-B on July 8, 1985. Specifically, with respect to G&A, the  
 18 Commission stated:

19 Fuel Procurement Administrative Charges. Each of the utilities  
 20 have staffs responsible for fuel procurement, and the costs  
 21 associated with fuel procurement and administration do not bear a  
 22 significant relationship to the volume or price of fuel purchases.  
 23 These costs are relatively fixed and are not volatile; they are more  
 24 appropriately recovered through base rates.

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<sup>7</sup> Direct Testimony of Kim Ousdahl at 24 and Exhibit KO-6.

<sup>8</sup> Direct Testimony of Sam Forrest at 10.

1           Accordingly, excluding G&A costs from the Fuel Clause is also consistent with  
2           this Commission's policy.

3   **Q       DOES THIS CONCLUDE YOUR TESTIMONY?**

4   **A       Yes.**

1                   CHAIRMAN GRAHAM: We will enter those five  
2                   things into the record.

3                   (Whereupon, Exhibit Nos. 40-43 were received  
4                   into evidence.)

5                   MR. MOYLE: Thank you.

6                   (Whereupon, prefiled testimony was inserted.)

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1                   CHAIRMAN GRAHAM: Okay. We will take up Mr.  
2                   Lawton tomorrow and all the rebuttal. Everybody  
3                   travel safe. We will start tomorrow morning at  
4                   9:30 -- 9:30, and I will see you then.

5                   Thank you.

6                   (Transcript continues in sequence in Volume  
7 6.)

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CERTIFICATE OF REPORTER

STATE OF FLORIDA     )  
COUNTY OF LEON     )

I, DEBRA R. KRICK, Professional Court Reporter, certify that the foregoing proceedings were taken before me at the time and place therein designated; that my shorthand notes were thereafter translated under my supervision; and the foregoing pages, numbered 536 through 662 , are a true and correct record of the aforesaid proceedings.

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 2nd day of December, 2014.




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DEBRA R. KRICK  
NOTARY PUBLIC  
COMMISSION #EE212307  
EXPIRES JULY 13, 2016