

August 1, 2008

The Honorable Michael W. Sole, Secretary
Florida Department of Environmental Protection
Chair, Florida Governor's Action Team on Energy and Climate Change
3900 Commonwealth Blvd., MS49
Tallahassee, Florida 32399

Subject: Florida Power & Light Company (FPL) Response to the Florida Climate Action Team
Regarding Proposed Policy ESD-23 on Decoupling

Dear Secretary Sole:

The concept of revenue decoupling is being touted in a number of jurisdictions as a means of encouraging higher levels of energy efficiency by utilities. Implicit in the proposals is the assumption that utilities are not doing all they can in this area, and that decoupling is the only and best means of achieving better results. While the motive is admirable, the underlying assumptions are not supportable.

It is simply not accurate to put all states and utilities together in one category and suggest that utilities are not investing in conservation. There are numerous successful energy efficiency initiatives around the country that have been successful without decoupling as a driver. As I will discuss later, the Florida regulatory climate has been extremely successful in furthering energy efficiency goals, and FPL in particular has achieved industry leading results in this area.

The policy being currently developed by the Florida Climate Action Team on decoupling (ESD-23) suggests that 1) there is an inherent incentive for utilities to minimize investments in energy efficiency, and 2) decoupling would result in more energy efficiency in Florida. On the surface, these assumptions may seem reasonable, but they are not based in fact or supported by research and simply cannot be accepted as a basis for implementation of decoupling, at least in the case of electric utilities. Moreover, the implementation of decoupling would seriously undermine the successful Florida system of electric utility regulation that has been painstakingly crafted over the last two decades.

While the current proposal (ESD-23) is short on details and specifics, in the following I discuss in more detail some of my concerns with this proposed policy.

ESD-23 suggests that there is an inherent incentive for Florida utilities to minimize investments in energy efficiency.

FPL Response

Contrary to the supposition that there is an inherent incentive for utilities to minimize investments in conservation, Florida's experience with energy efficiency reflects a history of outstanding support for these programs and initiatives. Florida's investor-owned utilities (IOUs) have actively promoted demand side management (DSM) and conservation programs in the state since the 1980s and have been leaders among utilities nationwide. FPL launched its first DSM and conservation programs in 1979, with industry-leading results:

- FPL is the No. 1 electric utility in the nation in terms of megawatt (MW) demand reduction from energy efficiency¹
- FPL is fourth in the nation in energy efficiency in terms of percent of peak demand reduction¹
- Overall, even though FPL serves only 3 percent of U.S. electric consumers, the company has achieved 13 percent of all U.S. energy efficiency and 6 percent of all load management²
- FPL currently offers 21 energy efficiency and demand response programs for both residential and commercial/industrial customers. Customer interest in our programs has been extremely positive, resulting in:
 - ✓ More than 2.3 million energy savings audits performed
 - ✓ More than 1 million high efficiency air conditioners installed
 - ✓ Nearly 750,000 customers on load control
 - ✓ More than 700,000 energy efficiency retrofits to homes and businesses
 - ✓ Over 400,000 air conditioning duct tests conducted and leaks repaired

As a result of these achievements, FPL has been able to avoid the need for 12 power plants since 1979, representing significant savings to our customers as well as reductions in greenhouse gas emissions in Florida.

Many states, on the other hand, are doing little in this regard. Generally speaking, states with relatively low cost but high carbon-content power are doing the least. Of 89 utilities with peak demands exceeding 3,000 MW, 46 offer no energy efficiency programs whatsoever. If all of these utilities achieved the same level of performance as FPL in energy efficiency and demand response, the U.S. could eliminate the need for 107,500 MW of generation and reduce 244,600,000 tons of CO₂ emissions annually.

Some people talk about energy efficiency as the "fifth fuel," after coal, natural gas, nuclear and renewables. At FPL, we regard energy efficiency as the "first fuel," and we are continuing to work to develop new programs that make sense for all of our customers. In addition, we are making a commitment to new technologies such as "smart meters" that will empower our customers by providing them choices. This smart meter technology will help customers manage their costs, provide important information about their usage and will open the door to new energy efficiency offerings in the future.

Clearly, Florida's electric utilities have not held back in their efforts to promote energy efficiency. Even if a company was inclined to try to minimize conservation efforts, it simply would not be possible under current regulatory and legislative requirements. Florida has an open and transparent regulatory approach that has proven to be highly effective. Florida statutes require the Florida Public Service Commission (FPSC) to ensure that utilities adopt energy efficiency and DSM goals and programs. In meeting its statutory responsibility to promote energy efficiency and DSM in Florida, the FPSC is required to evaluate the full potential of all available DSM and supply-side conservation and efficiency measures. FPL in turn proactively seeks to implement all known cost-effective energy efficiency and DSM programs and must demonstrate this to the FPSC. These energy efficiency / DSM goals are established every five years and approved by the FPSC, which has broad latitude to ensure that all Florida IOUs set and meet aggressive goals for conservation. As a result, while it may be appropriate to address the financial impact of energy efficiency and DSM programs on utilities and their customers, decoupling is not the answer.

EDS-23 suggests that decoupling by itself would result in more energy efficiency in Florida.

FPL Response

The concept of decoupling originated in the gas industry as a means of sustaining revenue levels in the face of falling sales. Since then it has been touted as a means of promoting conservation in the electric industry; however, there is no research or documented evidence that any reduction in electrical demand has been achieved due to decoupling. Such claims are suppositions at best. Claims have been made regarding the impact of decoupling in California on energy usage; however, one could argue that the high prices in California and a mild climate, along with increases in natural gas usage, have played the most significant role in controlling per capita electric usage.

In a 2007 presentation by a California utility executive, it was stated that “[d]ecoupling by itself doesn’t provide incentives that encourage utilities to support energy-efficiency; but it does remove financial disincentives for utilities so they can implement energy-efficiency initiatives.” The September 2007 National Association of Regulatory Utility Commissioners (NARUC) Report on Decoupling stated that “[w]hile it can remove disincentives for utilities to promote efficiency, decoupling is not designed to create an incentive for energy efficiency.” As discussed earlier, Florida has achieved tremendous results without the need for decoupling. Thus, there is no driving need to implement decoupling in our state.

The NARUC Report also correctly points out that “[w]hether decoupling will in itself result in increased efficiency is still the subject of debate.” The report goes on to identify other potential adverse consequences of decoupling, such as the transfer of weather and economic risk to customers and the administrative complexity of attempting to correct for these risks.

In fact, a significant problem with decoupling is that it deals not only with energy conservation revenues, but also with fluctuations in revenues due to weather and other factors. We believe that subjecting customers to revenue shortfalls due to weather and other factors is inappropriate and could place an undo burden on those same customers. Furthermore, because decoupling

keeps a utility revenue neutral despite demand and weather fluctuations (and possibly other factors influencing utility revenues such as economic conditions), utilities will have a greatly reduced incentive for keeping costs as low as possible.

Also, decoupling does nothing to help address some significant obstacles that exist to achieving additional energy efficiency. These obstacles include consumers' desire to minimize upfront costs and provide for short paybacks, affordability issues for low income end-users, overall consumer awareness, and disconnects in incentives between owners and renters.

Finally, decoupling reverts back to a regulatory model that employs an ongoing system of frequent, highly administrative rate reviews focused on return on equity, which would detract from the ultimate objective of maximizing energy efficiency results. This an extremely inefficient system that adds cost to the prices ultimately paid by customers without the guarantee of any added benefits.

The existing Florida regulatory system has worked very well and can accommodate revisions to energy efficiency and conservation programs

As I stated previously, FPL and Florida's other electric IOUs have achieved tremendous results under the existing system of regulation, and we are not resting on our past accomplishments. At FPL, energy efficiency and demand response will meet fully 21 percent of FPL's future growth in capacity need through the year 2017. These results translate directly into significant savings to our customers, most directly in terms of rates that are lower than what they otherwise might have been without Florida's current regulatory approach. In addition, participating customers save on an individual level to the extent they participate in and take advantage of the many offerings available to them (such as the 2.3 million customers who have had energy audits conducted, or the 1 million customers who have installed high efficiency air conditioners).

Florida's constructive regulatory framework has created a set of win-win scenarios for our customers and shareholders. Up until the early 1990s, Florida's regulatory system was marked by frequent rate cases and a lack of incentives for utilities to control costs. This trend was reversed through a series of revenue sharing agreements based on sharing thresholds and caps, and has benefited customers and shareholders alike. Under the revenue sharing agreements that have been in effect since 1999, FPL customers have saved \$5.6 billion through reduced rates and revenue refunds - an average of \$560 million per year since 1999. This regulatory approach has also provided financial stability for FPL's investors who play a critical role in the funding of the Company's capital investment requirements. Most importantly, such a system also provides a strong incentive to the utility to manage costs effectively, further benefiting our customers. As a result of this constructive framework, FPL's 2007 operating and maintenance (O&M) cost per customer of \$323 is 44 percent below the 2006 national average of \$576, while service levels are in the top 25 percent. **Implementing decoupling at this time would have significant unintended consequences and would disrupt and threaten the successful Florida system of electric regulation.**

Finally, it should be noted that the Commission recently opened a docket to establish new conservation goals for the utilities. FPL formed a working group with the other utilities in Florida and selected environmental groups to work together on the first step of the DSM goal setting process - determining the technical potential for DSM. In addition to determining how much DSM can be done from a technical standpoint, the technical potential study finalizes which DSM measures should be evaluated, what their demand and energy impacts are, and what is the cost to implement them. These are the foundations for the subsequent steps in determining first how much DSM is truly achievable for each utility and second the appropriate financial incentives for utilities to achieve these results. Over the next several months, this docket will provide the opportunity for the Commission to ensure that all appropriate measures will be addressed going forward. In the past this process has provided an extremely thorough and complete review, and it is safe to say that this newly opened docket, in conjunction with recently passed energy legislation, will meet the test of identifying the full potential of future energy efficiency opportunities, all without the need for decoupling.

Summary and Conclusions

The current statutory framework in Florida, the active implementation and oversight by the FPSC, and the aggressive energy efficiency and DSM goals of Florida's utilities confirm that there is no compelling need for decoupling in Florida at this time. As I discussed above, there is no evidence that decoupling actually achieves the results being claimed or projected by its proponents. It is also clear that decoupling by itself does not provide any additional incentive to increase energy efficiency. Given the history of results in Florida, decoupling is not necessary to "remove disincentives."

The current regulatory approach has been demonstrated to work very well, and decoupling will not provide sufficient incentives for additional energy efficiency. In fact, as explained previously, we believe it could have serious unintended consequences that will undermine a highly successful regulatory process in Florida. We also clearly recognize that ever increasing fossil fuel prices and concerns about global warming may require additional energy efficiency and demand programs that don't meet today's financial tests. There are financial incentives and other approaches that we believe will work well. A number of mechanisms are currently in some stage of development or implementation in a number of states. Florida should study those and determine what is the best approach without negating the benefits of a regulatory system that has worked well for customers and shareholders.

It is difficult to imagine how FPL could have improved on its already outstanding and industry-leading results in conservation had decoupling been in place. Given those results and the uncertainty surrounding decoupling, it is simply not prudent to subject the residents of Florida - - and the customers of FPL and other Florida-based electric utilities -- to an experiment that will certainly create customer confusion, will create additional administrative costs and bureaucracy, will seriously undermine a successful regulatory process, and most likely will unnecessarily adversely impact the price they pay for electricity.

Florida should continue its highly effective and comprehensive regulatory approval process for identifying energy efficiency and DSM goals and programs that can be accomplished without

decoupling. In the long run, this will reinforce Florida's already strong commitment to such programs.

Sincerely,

Armando J. Olivera
President and Chief Executive Officer
Florida Power & Light Company

¹Based on US Department of Energy, Energy Information Agency Data for 2006, which is the most current information available

²Based on US Department of Energy, Energy Information Agency Data for 2006, which is the most current information available, and US Census data for population

Cc:

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