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DATE: May 1, 2009
TO: Peter H. Lester, Public Utilities Supervisor, Division of Economic Regulation
FROM: Denise N. Vandiver, Chief of Auditing, Division of Regulatory Compliance
RE: Docket No: 090001-EI; Company Name: Gulf Power Company;
Audit Purpose: Intercompany Interchange Contract; Company Code: EI804;
Audit Control No: 09-023-1-1;

Attached is the final audit report for the utility stated above. I am sending the utility a copy of this memo and the audit report. If the utility desires to file a response to the audit report, it should send a response to the Office of the Commission Clerk. There are no confidential work papers associated with this audit.

DNV/tbm

Attachment: Audit Report

CC: Division of Regulatory Compliance (Salak, Mailhot, Harvey,
District Offices, File Folder)
Office of Commission Clerk (2)
General Counsel
Office of Public Counsel

Ms. Susan D. Ritenour
Gulf Power Company
One Energy Place
Pensacola, FL 32520-0780

J. Stone/R. Badders/S. Griffin
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FLORIDA PUBLIC SERVICE COMMISSION
DIVISION OF REGULATORY COMPLIANCE
BUREAU OF AUDITING

Tallahassee District Office

GULF POWER COMPANY

INTERCOMPANY INTERCHANGE CONTRACT AUDIT

TEST YEAR ENDED DECEMBER 31, 2008

DOCKET NO. 090001-EI
AUDIT CONTROL NO. 09-023-1-1

A handwritten signature in black ink, appearing to read "Debra M. Dobiak", written over a horizontal line.

Debra M. Dobiak, Audit Manager

A handwritten signature in black ink, appearing to read "Lynn M. Deamer", written over a horizontal line.

Lynn M. Deamer, District Audit Supervisor

DOCUMENT NUMBER-DATE

04267 MAY-5 8

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TABLE OF CONTENTS

AUDITOR'S REPORT

PAGE

I. PURPOSE..... 1

II. OBJECTIVES AND PROCEDURES 2

DOCUMENT NUMBER-DATE
04267 MAY-58
FPSC-COMMISSION CLERK

**DIVISION OF REGULATORY COMPLIANCE
AUDITOR'S REPORT**

April 24, 2009

TO: FLORIDA PUBLIC SERVICE COMMISSION

We have performed the procedures enumerated later in this report to meet the agreed upon objectives set forth by the Division of Economic Regulation in its audit service request. We have applied these procedures to the Intercompany Interchange Contract and its supplemental schedules as filed with the Federal Energy Regulatory Commission (FERC) annually, and as it is applicable to Gulf Power Company in support of its filing for Fuel Clause Audit, Docket No. 090001-EI.

This audit was performed following general standards and field work standards found in the AICPA Statements on Standards for Attestation Engagements. Our report is based on agreed upon procedures and the report is intended only for internal Commission use.

I. OBJECTIVES AND PROCEDURES

INTERCOMPANY INTERCHANGE CONTRACT (IIC)

A. Objective: To gain an understanding of the Intercompany Interchange Contract and the implementation of procedures under the Southern Company umbrella. To determine if the transactions between the companies within the IIC are consummated on terms equivalent to those that prevail in arm's length transactions. To determine that the procedures and policies followed by Gulf are in compliance with the IIC.

1. Reviewed the IIC including any addendums. Determined contract specifications to ensure compliance with the FERC Standards of Conduct and obtained the FERC issued Audit Report of Southern Company. Determined operating company responsibilities as per the contract. Reviewed Gulf's IIC Monthly Invoice Review Process with its Financial & Regulatory Reporting Desktop Procedures.
2. Reviewed the IIC supplemental schedules applicable to Gulf and filed with FERC annually. Recomputed peak period load ratios. Traced sample calculations for load, capacity and reserve determinations to Monthly Estimated Load Capacity Comparisons for the operating companies. Traced planned monthly estimated load capacity for Gulf during October 2008 to the actual October 2008 IIC invoice.
3. The audit staff was able to gain an understanding of the Intercompany Interchange Contract and the implementation of procedures under the Southern Company umbrella. The audit staff placed reliance on the audit performed by the FERC Office of Enforcement regarding the transactions between the utilities within the IIC, and whether the transactions are consummated on terms equivalent to those that prevail in arm's length transactions. The FERC audit report did note gaps in segregation of duties, but the utility did comply with the stated recommendations in order to remove the possibility of affiliate abuse. It appears that the procedures and policies followed by Gulf are in compliance with the IIC.

B. Objective: To determine that the ratepayers aren't being negatively affected by transactions under the IIC.

1. Obtained Schedules A-1, A-6, A-8, A-9, and A-12 that the utility filed in the FPSC Fuel docket for October 2008.
2. Obtained the Interchange Analysis, the pertinent IIC Invoice Reports, and the supplemental schedules for October 2008. Reconciled and/or recalculated the schedules to the invoice to the interchange analysis, and traced them to the filed "A" schedules.

3. The audit staff was able to trace and reconcile the reports and schedules without exception. The audit staff recognizes that the voluminous components and the constant changes on a minute-to-minute basis that exist in the decision-making process of choosing to purchase vs. generate energy can cause difficulty in recording the costs of supplying energy to its customers. However, based on discussions with Gulf employees as well as the testing of the computations, the audit staff believes that the ratepayers are not negatively affected by transactions under the IIC.

C. Objective: To investigate the trend in Gulf Power's sales into the Southern Company pool. To determine the effect of Gulf not leaving itself some coal spot market exposure.

1. From the Accounts Payable Analysis, scheduled coal, natural gas, and oil purchases monthly for the year 2008. Calculated average price for each commodity monthly.
2. From the Energy Information Administration website, obtained historical average spot coal prices and natural gas future prices for 2008. Compared Gulf's average prices to the market average spot prices for January, April, July, October, and December 2008. Determined if Gulf's costs were lower or higher than market for the different periods noted above.
3. Gulf's power sales into the intercompany interchange pool, as well as total power sold, have declined since 2007 but more significantly in 2008. In addition, total fuel costs have increased. Hence, the ratepayers ultimately are responsible for the increasing costs with less of the offsetting benefit of power sales for similar KWHs generated. However, Gulf paid less than market for coal purchases from April through December 2008, while it paid higher than market for natural gas purchases from July to December 2008. Gulf is locked into sales contracts for coal purchases through 2010. As of March 2009, the market rates are lower than the contract rates, and Gulf's activity should be monitored going forward to determine if conditions require spot purchases in order to reduce fuel generating costs.