BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

IN RE: PETITION FOR INCREASE IN RATES BY GULF POWER COMPANY. _____/

DOCKET NO. 110138-EI

RECEIVED-FPSC
11 DEC 15 PM 3:19
COMMISSION CLERK

VOLUME 1

Pages 1 through 249

ELECTRONIC VERSIONS OF THIS TRANSCRIPT ARE A CONVENIENCE COPY ONLY AND ARE NOT THE OFFICIAL TRANSCRIPT OF THE HEARING. THE .PDF VERSION INCLUDES PREFILED TESTIMONY.

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 12, 2011
TIME:	Commenced at 9:30 a.m.
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	MARY ALLEN NEEL, RPR, FPR

DOCUMENT NUMBER-DATE
08964 DEC 15 =
FPSC-COMMISSION CLERK

APPEARANCES:

JEFFREY A. STONE, RUSSELL A. BADDERS, and STEVEN R. GRIFFIN, ESQUIRES, Beggs & Lane, Post Office Box 12950, Pensacola, Florida 32576; CHARLES A. GUYTON, ESQUIRE, Gunster, Yoakley & Stewart, P.A., 215 South Monroe Street, Suite 601, Tallahassee, Florida 32301; and RICHARD A. MELSON, ESQUIRE, 705 Piedmont Drive, Tallahassee, Florida 32312, on behalf of Gulf Power Company.

JOSEPH A. McGLOTHLIN and ERIK L. SAYLER, ESQUIRES, Associate Public Counsel, Office of Public Counsel, c/o The Florida Legislature, 111 West Madison Street, Room 812, Tallahassee, Florida 32399-1400, on behalf of the Citizens of the State of Florida.

VICKI GORDON KAUFMAN and JON MOYLE, JR., ESQUIRES, Keefe, Anchors, Gordon & Moyle, P.A., 118 North Gadsden Street, Tallahassee, Florida 32301, on behalf of Florida Industrial Power Users Group.

ROBERT SCHEFFEL WRIGHT and JOHN T. LaVIA, III, ESQUIRES, Gardner, Bist, Wiener, Wadsworth, Bowden, Bush, Dee, LaVia & Wright, P.A., 1300 Thomaswood Drive, Tallahassee, Florida 32308, on behalf of Florida Retail Federation.

KAREN WHITE and MAJOR CHRISTOPHER C. THOMPSON, ESQUIRES, USAF Utility Law Field Support Center, 139 Barnes Drive, Suite 1, Tyndall AFB, Florida 32403-5319, on behalf of Federal Executive Agencies.

CAROLINE M. KLANCKE, MARTHA F. BARRERA, and KEINO YOUNG, ESQUIRES, Florida Public Service Commission, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850.

S. CURTIS KISER, General Counsel; Mary Anne Helton, Deputy General Counsel; and SAMANTHA CIBULA, Attorney Supervisor, ESQUIRES, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, Advisors to the Florida Public Service Commission.

I N D E X

OPENING STATEMENTS

	PAGE
Opening Statement by Mr. Stone	36
Opening Statement by Mr. McGlothlin	44
Opening Statement by Ms. Kaufman	55
Opening Statement by Mr. Wright	62
Opening Statement by Major Thompson	66

WITNESSES

NAME	PAGE
MARK A. CROSSWHITE	
Direct Examination by Mr. Stone	73
Prefiled Direct Testimony Inserted	75
Cross-Examination by Mr. McGlothlin	91
Cross-Examination by Ms. Kaufman	95
Cross-Examination by Major Thompson	102
Cross-Examination by Mr. Wright	104
Redirect Examination by Mr. Stone	118
ROBERT L. MCGEE	
Prefiled Direct Testimony Inserted	123
WILLIAM G. BUCK III	
Prefiled Direct Testimony Inserted	168
R. SCOTT TEEL	
Direct Examination by Mr. Melson	183
Prefiled Direct Testimony Inserted	186
Cross-Examination by Mr. McGlothlin	215
Cross-Examination by Ms. Kaufman	240
CERTIFICATE OF REPORTER	249

INDEX TO EXHIBITS

NUMBER		ID.	ADMTD.
1	Comprehensive Exhibit List	8	8
2-6	Service hearing exhibits	8	8
7	MFR schedules	72	72
8	RLM-1		164
9	WGB-1		167
104	Gulf Interrogatory Answer to Staff, Number 259		164
122	Gulf Production to Staff	11	11
124-137	Gulf Production to Staff	11	11
138-141	Gulf Production to OPC	11	11
142	Gulf Production to FEA	11	11
143	FEA Production to Staff, Number 1 and 2	9	9
144	FIPUG Production Staff, Number 1	9	9
158-168	Rebuttal testimony and exhibits	18	
169	Proposed Stipulations	18	18
170	Service Hearing Response	118	122
171	Gulf Interrogatory Answer to Staff, Number 30	167	167
172	Gulf Interrogatory Answer to Staff, Number 171	183	183
173	FPL PSC Earnings Surveillance Reports	236	

P R O C E E D I N G S

CHAIRMAN GRAHAM: Good morning, everyone. Let the record show it is Monday, December the 12th, around 9:30 a.m., and this is a hearing for Docket No. 110138.

A couple of administrative things just so everybody knows where we are. We've got a long week ahead of us. We will be stopping probably around one o'clock for lunch, so you guys all know. There's a room here next door, if you could go there to bring a bag lunch and eat. There's a room upstairs which is an old meeting room that's got plenty of tables and chairs. You can eat there as well. And I believe there's a cafeteria across the courtyard. We'll probably be taking about 45 minutes or so for lunch.

We have to take about a five- or ten-minute break every two hours for the court reporter. Her little fingers can go for about two hours at a time, and then we've got to give that a break.

And we plan on going until 7:00 every night this week. Hopefully we're done by Friday. If not, we're scheduled to be back here at eight o'clock Saturday morning, and if not done by Saturday, we'll be here Sunday around one.

Hopefully that works for everybody's schedule.

That all being said, let's get started, if I can get the Staff to read the notices.

MS. KLANCKE: By notice, this time and place has been set for hearing in Docket No. 110138-EI.

CHAIRMAN GRAHAM: Appearances. Who do we have here?

MR. STONE: Mr. Chairman, my name is Jeffrey A. Stone, and I have with me my partners at Beggs & Lane, Russell A. Badders and Steven R. Griffin. Joining us representing Gulf Power Company are Charles A. Guyton of Gunster, Yoakley & Stewart and Richard D. Melson of his own law firm, and we represent Gulf Power Company.

CHAIRMAN GRAHAM: Okay.

MR. WRIGHT: Good morning, Commissioners. Robert Scheffel Wright representing the Florida Retail Federation. Thank you.

MR. McGLOTHLIN: Good morning. Joe McGlothlin and Erik Sayler with the Office of Public Counsel.

MS. KAUFMAN: Good morning, Commissioners. Vicki Gordon Kaufman and Jon Moyle on behalf of the Florida Industrial Power Users Group.

MAJOR THOMPSON: Major Chris Thompson from the FEA.

MR. BADDERS: Caroline Klancke, Martha Barrera, and Keino Young from Commission legal staff.

CHAIRMAN GRAHAM: All right.

MS. HELTON: Do I get to make an appearance?

CHAIRMAN GRAHAM: Sure.

MS. HELTON: Mary Anne Helton, advisor to the Commission. I would also like to make an appearance for our general counsel, Curt Kiser, and Samantha Cibula.

CHAIRMAN GRAHAM: Thank you. Staff, preliminary matters.

MS. KLANCKE: There are several preliminary matters, the first of which is, there have been several witnesses excused from the hearing, and I can read them if you would like.

CHAIRMAN GRAHAM: Please.

MS. KLANCKE: Witnesses McGee, Buck, Twery, Crumlish, Pollock, Stowe, Dobiac, and Hicks have all been excused from the hearing. The prefiled testimony and exhibits of these witnesses can be identified and moved into the record as they would have appeared on the order of witnesses contained in the prehearing order.

In addition, there were two orders issued

denying the intervenors' motions to strike which were issued on December 7th and December 8th respectively.

In addition, I would like to mark the Comprehensive Exhibit List as Number 1 on the list and have it moved into the record.

CHAIRMAN GRAHAM: We will move the Comprehensive Exhibit List into the record.

(Exhibit Number 1 was marked for identification and admitted into the record.)

MS. KLANCKE: In addition, Staff would now like to recommend that the service hearing exhibits, which are listed on the Comprehensive Exhibit List as 2 through 6 be marked and moved into the record.

CHAIRMAN GRAHAM: If there's no objections, we'll move items 2, 3, 4, 5 and 6 into the record.

(Exhibit Numbers 2 through 6 were marked for identification and admitted into the record.)

MS. KLANCKE: At this time, I would like to have Martha Barrera recognized.

MS. BARRERA: Good morning, Commissioners. At this time I would like to turn your attention to the documents identified in the Comprehensive Exhibit List on page 24 as Staff's Exhibit Number

143 and 144. Staff's Exhibit 143 are documents produced by FEA in response to Staff's Request for Production, Number 1 and 2. Staff's Exhibit Number 144 are documents produced by FIPUG in response to Staff's First Request for Production, Number 1.

The parties have stipulated to the introduction of Exhibits 143 and 144 into the record. And, Mr. Chair, at this time, I request that Staff's Exhibits 143 and 144 be moved into the record.

CHAIRMAN GRAHAM: We will move 143 and 144 into the record.

(Exhibit Numbers 143 and 144 were marked for identification and admitted into the record.)

MS. BARRERA: Additionally, I would like to turn your attention to pages 21 to 24 of the Comprehensive Exhibit List, which contains Staff's Exhibits 122 and 124 through 142. As you can see from the descriptions in the Comprehensive Exhibit List, Exhibits 122 and 124 through 137 are documents produced by Gulf in response to Staff's Request for Production of Documents numbered 1, 3 to 7, 9, 11 to 14, and 16 through 19. Staff's Exhibits 138 to 141 are documents produced by Gulf in its responses to OPC's first, second, fourth,

and sixth Requests for Production. Staff's Exhibit Number 142 are documents produced by Gulf in response to FEA's First Request For Production.

All parties were provided with a copy of the documents. They're found in the hearing DvD in the files that cover Exhibits 122 through 142. The questions, answers, and short documents are contained in the PDF files and span Bates numbers 1252 through 1572. Voluminous documents and the Excel spreadsheets are submitted in electronic format and are contained in the folder marked with the appropriate exhibit number.

In this case, Gulf has stipulated that these documents are Gulf's corporate documents prepared and compiled by Gulf, that these documents are relied upon by Gulf in the conduct of its business, that they are kept in the course of Gulf's regularly conducted business activities, and that it is Gulf's regular practice to make and compile these documents during the course of its business activities. The documents produced as a result of these requests serve to explain and supplement the information contained in the MFRs and the testimony, prefiled testimony of Gulf's witnesses as well as intervenors' witnesses.

At this point, Mr. Chair, I would like to move these documents into the record. I also ask that if intervenors have any objections for Gulf, that they identify the document to which they specifically object and state the objections so we can address each one individually.

MR. STONE: Gulf has no objections to the request to be entered into the record as though read.

CHAIRMAN GRAHAM: We're looking to enter Exhibit Numbers 122 through 142, with 123 that has already been withdrawn. Any objections? Seeing none, we'll enter these into the record.

Staff.

(Exhibit Numbers 122 and 124 through 142 were marked for identification and admitted into the record.)

MS. KLANCKE: There are some additional preliminary matters with respect to the proposed stipulations in this case. In particular, Staff has prepared a separate sheet for your ease of reference outlining a list of proposed stipulations for the Commission to vote on at their convenience. There are proposed stipulations on the following issues: 2, 3, 4, 5, 6, 7, 15, 19, 20, 26, 34, 35, 36, 43, 44, 45, 46, 53, 58, 65, 68, 73, 75, 78, 85,

100, 101, 102, 103, 105, 106 -- 116, rather, and 118.

In addition, I would like to point out with respect to the proposed stipulation on Issue 5, the words "C. customer growth (retail): 2012-1.2 percent" should be added to the proposed stipulation language.

MR. STONE: Gulf concurs with that addition.

MS. KLANCKE: In addition, please note that the parties have agreed that Issue Numbers 13, 19, 50, 54, 81, 82, 83, and 87 may be dropped, as the respective positions are contained in other issues. For your ease of reference and for clarity, since the time of the issuance of the Prehearing Order, Issue Number 29 has been dropped. So it will still be reflected in your Prehearing Order, but please note that it has been dropped as well.

MR. STONE: Mr. Chairman, some of the issues were dropped because they were subsumed in other issues, and some of the issues were dropped because the parties determined that they were no longer at issue in the case. I just wanted to clarify that for the record.

CHAIRMAN GRAHAM: Okay. Thank you.

MS. KLANCKE: Certainly. And if it is your

preference to vote on the proposed stipulations as reflected in the Prehearing Order and in your handout, that would be good at this time.

CHAIRMAN GRAHAM: Commissioner Edgar.

COMMISSIONER EDGAR: Mr. Chairman, I would propose that the handout we have before us titled "Proposed Stipulations" be marked as an exhibit, and then if there are no questions, I'm prepared to make a motion that we adopt the proposed stipulations as reflected in this document, Category 1 and Category 2.

CHAIRMAN GRAHAM: All right. If we're going to put an exhibit number on this, Staff, I have -- the first available exhibit number is 158; is that correct?

MS. KLANCKE: That is correct.

CHAIRMAN GRAHAM: Commissioner Edgar.

MS. KLANCKE: Short title, "Proposed Stipulations"?

COMMISSIONER EDGAR: Then, Mr. Chairman, I would propose that we approve the proposed stipulations as reflected on Exhibit 158.

CHAIRMAN GRAHAM: Short title will be "Proposed Stipulations"?

COMMISSIONER EDGAR: Yes, sir.

CHAIRMAN GRAHAM: It has been moved and seconded to approve the proposed stipulations. Any further discussion?

Seeing none, all in favor say aye.

(Simultaneous affirmative responses.)

CHAIRMAN GRAHAM: Any opposed? By your action, you've approved the list of proposed stipulations.

MS. KLANCKE: At this time, there are just a few more preliminary matters. Staff also recommends that the parties, Gulf, OPC, FIPUG, FRF, and FEA, their prefiled exhibits be marked and designated as they are reflected on the Comprehensive Exhibit List.

I believe that there is one additional preliminary matter that Gulf raised with respect to one of their positions, but I'll defer to Gulf to let them present it.

MR. STONE: Mr. Chairman, on Issue 18, we circulated to the parties late last week after the issuance of the Prehearing Order a clarification to the position that did not make it to the Prehearing Order. It doesn't actually change our position, but it avoids some misunderstanding about our position.

Basically, the language I believe has been reflected in a handout that has been given to the Commissioners, but if not, I'll read it. The position as it's stated in the Prehearing Order, the last sentence, if you would delete the words "and an," a-n-d, space, a-n, and insert the words "which includes the," and then you can strike the "of 806,000," so that the position would read, "No. The appropriate level of Plant in Service is 2,672,964,000, 2,731,576,000 system. Gulf's requested amount should be increased by 61,773,000, or 63,913,000 system, to include the Crist Unit 6 and 7 turbine upgrades, as identified in Issues 8 and 9. Additionally, the amount requested should be reduced for an ECCR adjustment error totaling 862,000, which is also 862,000 system, which includes the error in Distribution Plant in Service identified in Issue 15." And for the record, Issue 15 was among the stipulated items that you just approved.

CHAIRMAN GRAHAM: Do the Commissioners have any questions on that change? Any of the intervenors? Mr. Wright?

MR. WRIGHT: Not regarding that change. I do have an issue with respect to our witness's

exhibits at the appropriate time, Mr. Chairman.

CHAIRMAN GRAHAM: Ms. Klancke, do we have to approve that change? What's the protocol?

MS. HELTON: I think the fact that he has stated it on the record and made everyone aware is sufficient.

CHAIRMAN GRAHAM: Okay. Mr. Wright.

MR. WRIGHT: Thank you, Mr. Chairman. I noticed that apparently our witness's prefiled Exhibit SWC-4, Mr. Chriss's exhibit has not been reflected on the master exhibit list. It is listed in the Prehearing Order. I guess it just inadvertently got left off as the master exhibit list was prepared on page 9 of your exhibit list. All we care about is that it get into the record for convenience of numbering. I might suggest that we mark Mr. Chriss's Exhibit SWC-4, which is Calculation of Jurisdictional Revenues Collected through Base Rates for Gulf Power Company, as Exhibit 28A, but I'm amenable to any other means of getting it into the record.

CHAIRMAN GRAHAM: Let's wait until Mr. Chriss comes up.

MR. WRIGHT: All right.

CHAIRMAN GRAHAM: And then we'll just add it

to where we are in our exhibit list.

MR. WRIGHT: Thank you.

CHAIRMAN GRAHAM: Towards the end.

MR. WRIGHT: Certainly. Thank you.

CHAIRMAN GRAHAM: Any other preliminary matters? Yes, sir.

MR. SAYLER: Mr. Chairman, one question that I've noticed in looking at the Comprehensive Exhibit List. All the rebuttal testimony and exhibits are not premarked, and I'm wondering if that might cause confusion later on if we have nonsequential numbering on the Comprehensive Exhibit List. I just wanted to point that out and see if maybe it was an oversight or if there was a reason for doing that.

CHAIRMAN GRAHAM: I was kind of curious myself why they weren't marked.

MS. KLANCKE: Perhaps I could clarify. I was going to -- with respect to the Gulf rebuttal numbers, I believe that they should be reflected as 158, beginning with -- we need to change that. 158, 159, 160, 161, 162.

MR. STONE: Ms. Klancke, if I may interrupt, I believe 158 was assigned to the proposed stipulation list.

MS. KLANCKE: Perhaps we could change that numeral, because we do have to add numbers with respect to all of the rebuttal testimony. And we only have one exhibit so far that we've identified. I think maybe just for ease -- to ensure we get off on the right foot, at least to try, maybe we could label them 159 through 168, and then make previously 158 169.

CHAIRMAN GRAHAM: Okay. So the proposed stipulations that is we put an exhibit number on, let's just go back and go ahead and number the rebuttal testimony as 158, 159, 160, 161, 162, 163, 164, 165, 166, 167, 168, and then the proposed stipulations will be now 169.

MS. KLANCKE: Correct. I apologize.

(Exhibit Numbers 158 through 169 were marked for identification and Exhibit 169 was admitted into the record.)

CHAIRMAN GRAHAM: That's quite all right, Ms. Klancke. If that's the only mistake you make this week, you've done a fantastic job.

Any other preliminary matters?

MS. KAUFMAN: Yes, Mr. Chairman. FIPUG and the other intervenors have a preliminary matter, and it relates to Ms. Klancke's comment that the

Prehearing Order, or the order issued by the Prehearing Officer, excuse me, denied the consumer intervenors' motion to strike the storm study and portions of Ms. Erickson's testimony that related to it.

It was my understanding, given the fact that the full time had not -- to file for us to seek reconsideration, that we would be permitted to do it at the beginning of the hearing, and we would ask for that opportunity.

CHAIRMAN GRAHAM: Okay. One more time, and a little slower. I'm an engineer, and this stuff goes in and out of my ears so fast.

MS. KAUFMAN: Okay. On December 7th, the Prehearing Officer entered an order that denied the consumers -- consumer intervenors' motion to strike what I shorthand as the storm study attached to Ms. Erickson's testimony, as well as some portions of her testimony that relate to the study. That was issued, with all due respect, by the Prehearing Officer. And it is our understanding, given that we didn't have the full time to file a motion for reconsideration of that order, that we would be permitted to do it orally at the beginning of the hearing. And that's Order No. PSC-11-0556-PCO-EI

issued December 7th.

CHAIRMAN GRAHAM: So you're asking me to consider overruling my Prehearing Officer?

MS. KAUFMAN: I'm asking for the entire Commission to consider reconsideration of the Prehearing Officer's order. And I think that is a right that is provided for in the Commission's rules. It's just a matter of timing.

CHAIRMAN GRAHAM: Well, I have never overruled a prehearing officer's order. I look at it this way: If the prehearing officer is not doing it, that means I have to do it or the committee as a whole has to do it. So I don't foresee that happening. Unless somebody -- one of the Commissioners here want to hear the argument, I do not plan on revisiting a decision made by the Prehearing Officer.

MS. KAUFMAN: Chairman Graham, with all due respect, I think it is our right to proffer our arguments before the entire Commission for purposes at least of preserving the record. The right to seek reconsideration is a right that is guaranteed in the Commission's rules. And if the order had been issued earlier, we would have filed a written motion for reconsideration. So I think that we're

within our rights to seek reconsideration from the entire Commission, again with all due respect to Commissioner Edgar.

CHAIRMAN GRAHAM: Commissioner Edgar?

COMMISSIONER EDGAR: Thank you, Mr. Chairman, and thank you for your support. I do believe that Ms. Kaufman is correct in what she is saying. I will point out that the order was issued timely, but I understand what you're saying about the time coming up to the hearing.

I am very, very comfortable -- having read the motions and the responses on both of the requests to strike certain portions of testimony, I am very comfortable that the orders I issued are the correct ones. However, no disrespect taken whatsoever, and if the Commissioners want to hear their arguments to see if the testimony that I included in the record for your consideration as part of the entire record to be excluded, if you want to hear those arguments, that's fine with me. But again, I am very comfortable with the orders that I issued, having read the motions, the responses, pertinent case law, and discussing it with our legal Staff.

CHAIRMAN GRAHAM: Mary Anne.

MS. HELTON: Ms. Kaufman is correct that if she seeks reconsideration of a nonfinal order, which are the types of orders that are at issue here -- I think it's within 10 days, but don't quote me on that -- that the full Commission then would need to rule upon that motion for reconsideration.

I do think to have a complete record that it would be appropriate to hear short arguments from the parties.

CHAIRMAN GRAHAM: Okay. So we will hear -- is it all the intervenors?

MS. KAUFMAN: I don't mean to speak for all the intervenors, but I am assuming that I will argue the motion on the intervenors' behalf.

MR. SAYLER: That is correct for OPC.

CHAIRMAN GRAHAM: Okay. Ms. Kaufman, you have five minutes.

MS. KAUFMAN: Thank you, Chairman and Commissioners. I appreciate it.

As I said when we were discussing this, the intervenors are seeking reconsideration of the order denying the motion to strike the storm study and Ms. Erickson's -- portions of her testimony that rely upon it.

I want to give you a little background, and that is that Ms. Erickson -- she will take the stand. She is Gulf's comptroller. She was examined extensively at her deposition about her areas of expertise, and we have no quarrel with the fact that she is an expert in regulatory accounting. But she admitted in her deposition that she has no expertise, she has no experience in hurricane modeling, the USWIND model that was used, hurricane prediction, or the matters that are addressed in the storm study. Rather, she commissioned the report and she received the report.

Gulf has presented no witness that worked on the report or prepared the report. We've had no opportunity to cross-examine anybody in that regard, and we think that the report is inadmissible.

I'm well aware of the standard for reconsideration, and so I'm going to limit my remarks to the areas that we think, with all due respect, the Prehearing Officer overlooked or misunderstood.

First, there's no dispute -- I think it's in the order -- that the study is hearsay. However,

the order relies on Section 120.57(c), which says that hearsay can supplement or support other evidence. Well, there is no other evidence in this case regarding the USWIND model, hurricane prediction, hurricane modeling other than this study, so it's not supporting any other evidence and should be stricken just on that basis.

In addition, as I understand the order, it says that Ms. Erickson can sponsor the study because she's an accounting expert. However, again, she's not an expert in the subject matter of the study, which a very complicated and technical issue dealing with computers and computer modeling. I think the order, again, with all due respect, is wrong when it says status as an accounting expert allows her to base her opinion on this study.

And if you look at Rule 90.704 of the Evidence Code, it does provide that an expert may rely on other expert opinions, reports, treatises by other experts in the same subject area. What we've got here are an accounting expert trying to rely on information of an expert, allegedly -- we don't really know, because there's no witness to demonstrate the expertise. But even if there was, she can't rely on the expertise of somebody in a

field that she is not an expert on.

Finally, the study, as I mentioned in my motion, has a very, very broad disclaimer that basically says you can't use this study for anything. And it's almost a page long, but I just want to read one sentence from the study itself put in there by the authors of the study. And they say, "The data and methodology described herein and the analysis and services provided herein are provided as is without any warranty or guarantee of any kind. Neither Equicap," which is the outfit that prepared the study, "nor any of its officers, directors, agents, subsidiaries, or affiliates guarantees or warrants the correctness, completeness, currentness, merchantability, or fitness for a particular purpose of the analysis provided hereunder."

Even the people that put together the study that have not come forward as witnesses say you can't rely on it. Now, the fact that there is this broad disclaimer I think eliminates the study from you relying on it in any way.

In the order, the Prehearing Officer found that you have a rule that requires a storm study to be filed every five years, and, yes, you do. I

have no quarrel with that. That has nothing to do with the admissibility of a piece of evidence that even its authors say you shouldn't rely on. And to that end, we think that whether you have a rule or not about the requirement for a storm study has nothing to do with whether this document is admissible, and it has nothing to do with whether or not you may rely upon it.

So that is our motion for reconsideration, and we would request that Ms. Erickson's -- I think it's CJE-1 -- be stricken and her testimony that relies on that study be stricken. And the actual references are included in our original motion.

Thank you.

CHAIRMAN GRAHAM: Gulf.

MR. GUYTON: Commissioners, the standard for review for a motion for reconsideration has been established by the courts and followed by this Commission and stated commonly as follows: Whether the motion identifies a point of fact or law that was overlooked or that the Prehearing Officer failed to consider.

In a motion for reconsideration, it is not appropriate to reargue matters that have already been considered. In this instance, Commissioner

Edgar had a very detailed motion and a very detailed response available to her. She ruled based upon all of the law, all of the facts, and she ruled appropriately and correctly. You are simply being asked to rehear and allow the parties to reargue the merits of the case or the merits of the motions to strike.

We respectfully submit that the motion for reconsideration should be denied. I am prepared to address the individual matters that are being reargued here, but in the interest of time, I will forgo that unless the Commission would like to hear specific arguments.

CHAIRMAN GRAHAM: Thank you, sir.

Commissioners. Commissioner Brown.

COMMISSIONER BROWN: I would actually like to hear the argument that FIPUG is raising regarding the lack of such supplemental evidence with regard to the hearsay exception.

MR. GUYTON: The argument is one based on the Evidence Code. The Administrative Procedure Act sets forth provisions of law that this Commission must follow, not necessarily the Evidence Code. The APA says irrelevant, immaterial, or unduly repetitious evidence shall be excluded, but all

other evidence of a type commonly relied upon by reasonably prudent persons in the conduct of their affairs shall be admissible. That's the applicable standard, and that's the standard that should be followed in this case.

However, even if you were to follow the standard invoked by the intervenors under the Evidence Code, under Section 90.704, which is the provision of the Evidence Code that addresses what experts may rely upon, they may rely upon facts or data reasonably relied upon by experts.

Witness Erickson is an expert accounting witness. She as an accounting witness regularly relies upon reports by other experts to make judgments as to what are the appropriate accounting accrual entries.

We have four or five instances of just such reports in this case. One is the storm study. Another is the Aon Hewitt study. One is another workmen's compensation study. These are typically relied upon by an accounting expert, and that is what is at issue here, what is the appropriate annual accrual to the property damage reserve.

This is evidence that supports her judgment. The evidence, it is corroborative evidence of her

judgment as an expert, and as such, it is admissible both under the Evidence Code and under the APA.

COMMISSIONER BROWN: Thank you.

CHAIRMAN GRAHAM: Commissioner Balbis.

COMMISSIONER BALBIS: Thank you, Mr. Chairman. And I appreciate the arguments made by both sides. I don't see anything here that would warrant overturning Commissioner Edgar's denial of the motion to strike. And conceptually, I think this Commission has always desired additional information, and then we can give weight to the evidence that's presented. So I'm a proponent of additional information, and with that I move -- and hopefully this is technically correct, but move to uphold the order denying the consumers' motion to strike.

CHAIRMAN GRAHAM: It had been moved and seconded to uphold the Prehearing Officer's order to -- the Prehearing Officer's order. Any further discussion?

Seeing none, all in favor say aye.

(Simultaneous affirmative responses.)

CHAIRMAN GRAHAM: Any opposed? By your action you have upheld the Prehearing Officer.

Any other preliminary matters?

Yes, sir.

MR. SAYLER: Thank you, Mr. Chairman. Erik Sayler on behalf of the Office of Public Counsel.

There was also a second motion for reconsideration -- excuse me. A second motion to strike portions of Alexander's testimony and exhibits. After careful consideration, we've decided not to seek reconsideration, but if you will indulge us, we'll give you our explanations and reasons why we're not seeking that.

CHAIRMAN GRAHAM: You're a very wise man. Please continue.

MR. SAYLER: Thank you. We do agree with Gulf Power that a base rate proceeding is not the appropriate forum in which to examine technical issues such as Gulf's future power generational needs, including nuclear power. That is set forth in their reply or answer to us.

However, when Gulf filed their rate case and their direct testimony, by two witnesses, they reference a parcel of land which they wanted to put into rate base which has the possibility of preserving the nuclear option. That was something that caught the intervenors flatfooted, a little

bit by surprise.

So our witness examined the record of the direct evidence or testimony provided by Gulf Power, and in so doing, he responded that -- he just basically observed that Gulf did not put any studies into the record, and he even questioned whether Gulf had purchased land without performing any technical analysis ahead of time.

In rebuttal to OPC witness Schultz's observations, Gulf witness Alexander filed rebuttal testimony and exhibits, which included those studies and evaluations and technical analysis, and went to great length to explain why Gulf was seeking to preserve the nuclear option, so-called. The intervenors thought that was a second bite of the apple, and that's what prompted our motion to strike, because we felt it went well beyond establishing that Gulf conducted studies ahead of time prior to spending $27 million to purchase land. We also felt it did not open the door to the material which we felt should have been supplied in the direct case.

And Gulf in its response to our intervenor motion asserted that the studies were introduced in rebuttal to rebut witness Schultz's, quote,

suggestions that -- I'll paraphrase it. Schultz's suggestions that technical studies had not been performed before the expenditures were made. This is page 8 of their response.

Gulf's response further went to say, "The issue before the Commission is not whether the studies were correct, but whether Gulf's" -- excuse me, whether Gulf performed such studies essentially prior the making the land, making the land purchases.

And the Prehearing Officer after reviewing both sides decided to deny our motion. And it appears that on page 2 of the order, the order, quoting, says, "Witness Alexander responds to and seeks to rebut testimony of intervenors' witness Schultz that Gulf expended funds prior to conducting studies and obtaining technical analysis of the prudence, cost-effectiveness and reasonableness of the expenditures."

And if that is the case and the limited purpose for which Gulf is offering the testimony of Ms. Alexander and her exhibits, is to rebut Mr. Schultz's assertion that Gulf spent money on land without doing any technical analysis, then we're fine, and that is the reason why we're not

seeking any motion for reconsideration. However, if Gulf is seeking to have her testimony and exhibits be beyond just the limited purpose of rebutting the assertion that they didn't do any studies, then we would object to that, because we think that gets down the road into something that is more akin to what should be saved for a need determination proceeding.

And so we just wanted to make sure that we understood the Prehearing Officer's ruling, and also based upon reading Gulf Power's reply brief, that that was the purpose and reason why her testimony is offered into evidence. And so long as her testimony and exhibits is used for that limited purpose, then we're not seeking a motion for reconsideration.

So thank you for your time, and I just wanted to see if that was the understanding of Gulf or perhaps the Prehearing Officer.

CHAIRMAN GRAHAM: We'll start with Gulf, and then we'll finish with our Prehearing Officer.

MR. GUYTON: Commissioners, Gulf offered this testimony to explicitly rebut several aspects of Mr. Schultz's testimony. One was the suggestion that Gulf had spent money without technical

consideration of the purchase. Another was Mr. Schultz's testimony that these costs and the incurrence of these costs were not reasonable and prudent.

As we say in our response, we've offered this testimony in response to both of those allegations. In fact, he went so far as to characterize it, or mischaracterize it as speculative overreaching. And so we did it to defend the company in terms of making sure that the Commission had a factual record before it. We set forth all of the grounds, not just the ones that Mr. Sayler has set forth to you, but all the grounds that we offered for each and every aspect of this. And Commissioner Edgar considered them, considered the facts, considered the law, and in our mind, ruled appropriately.

CHAIRMAN GRAHAM: Commissioner.

COMMISSIONER EDGAR: Mr. Chairman, thank you. I spend a great deal of time on every order that I issue, but I can tell you I spent even more time on this one and looking at, again, both the, as has been characterized, very detailed motion and response and case law, and discussed it with Staff and went through many, many redrafts before it was issued. I think that the first sentence, put there

purposely right under the heading "Decision," is clear, and it is, again, the correct decision.

Should any of you choose to look at all of that and think differently, no disrespect taken whatsoever, and as I said to Ms. Kaufman and I'll say to Mr. Sayler, no disrespect taken at all with you bringing it up.

But again, I think the first statement is clear. I did not rule in favor of the motion to strike. I do believe, from the information that I had before me and the case law to review, that the information that was put forth on rebuttal met the definition of rebuttal, and I stand by that sentence and the ultimate decision in the order.

CHAIRMAN GRAHAM: Mr. Sayler.

MR. SAYLER: Commissioner Edgar, we agree with you, and we were just wanting to make sure that our understanding of your order was as limited as it appeared to be from the order. So thank you very much.

CHAIRMAN GRAHAM: Thank you, sir. Any other preliminary matters?

MS. KLANCKE: Staff is not aware of any additional preliminary matters.

CHAIRMAN GRAHAM: Okay. So we're at opening

statements.

Okay. It says here that the intervenors are going to split 30 minutes. Good Lord.

COMMISSIONER EDGAR: You don't know where we started.

CHAIRMAN GRAHAM: And then Gulf is going to have 15. Gulf, I will give you the option, if you want to use any of your 15 minutes first and then conclude with the balance, or do you just want to use your 15 minutes at the end?

MR. STONE: Mr. Chairman, I do not intend to use my full 15 minutes.

CHAIRMAN GRAHAM: Okay. Do you want anything in opening, or do you want to wait until after the intervenors?

MR. STONE: I'll open.

CHAIRMAN GRAHAM: Okay. Please, sir.

MR. STONE: Good morning, Commissioners.

As I was preparing for this morning, I thought about this being the time of year when many of us think about the blessings of our lives. Among the blessings in my life is the privilege to practice law in my hometown, Pensacola, Florida.

After spending time away for college, law school, and the early years as a practicing lawyer,

I had the opportunity to return home in 1984 to raise my family. I joined the law firm Beggs & Lane, and in 1987 I began appearing before this Commission as an attorney on behalf of Gulf Power. It has since been my privilege to continue serving as Gulf's attorney, including the last 14 years leading our firm's effort as Gulf's general counsel. I served as counsel on Gulf's last three prior rate cases, the most recent of which was decided almost exactly 10 years prior to the scheduled decision in this case.

Over the years I've experienced firsthand the vital role that Gulf serves in our communities. As a relatively young child whose family operated a small business downtown, I have memories of watching as a new transmission line to serve a growing community was built near the hospital where I was born. I remember marveling at the extremely tall line of wooden poles installed down E Street to support the new transmission line. I remember wondering where they found so many tall and straight frees for such a purpose.

In my current role, I recently observed this same transmission line being rebuilt to increase its capacity in order to assure that the residents

and businesses of downtown Pensacola continue to receive reliable electric service. Construction involved a new concrete pole design requiring far fewer poles along the route.

As a young adult, my family's business moved from its downtown location to a new site in what was then the outskirts of town. I remember the arrangements we made to ensure that we had electric service adequate to meet the growing needs of our business. Gulf Power had clearly planned for the outward growth of our community and was then well prepared to provide service to our expanding needs.

I remember the tropical storms and hurricanes of my youth and the efforts of the electric service crews to ensure that power lost to the storm was promptly restored. I remember being fascinated by the armies of tree trimmers and line crews coming through our neighborhood with their bucket trucks and other equipment and their carefully choreographed movements.

As an adult, I gained a even greater appreciation for Gulf Power as the lifeblood of Northwest Florida. I experienced firsthand the damage from back-to-back hurricanes in the summer and fall of 1995. As severe as that damaged seemed

at the time, it pales in significance when compared to the devastation caused by Hurricane Ivan in the fall of 2004 and Hurricane Dennis in the summer of 2005. I remember the sense of helplessness as Northwest Florida awoke after Hurricane Ivan to find that power was out to more than 90 percent of the customers in the region, that Plant Crist was completely dark for the first time since its initial generating unit went into service in the 1940s.

More importantly, I remember the resolve of the men and women of Gulf Power who put their communities and customers ahead of self. As they always do, these men and women immediately set about the task of restoring power, and through the restoration of power, restoring hope and a sense of normalcy for Gulf's customers and our community in the wake of this horrible storm. The men and women of Gulf Power Company recognize the vital service that we are charged with providing to Northwest Florida. We recognize and enthusiastically accept our statutory obligation of service to the customers of Gulf Power Company.

It is this obligation of service that brings us here today. After 10 years, the revenues

produced under existing rates are no longer adequate to allow Gulf to continue providing the sufficient and reliable electric service that our customers are entitled to expect, the sufficient and reliable electric service that our employees take pride in being able to deliver, while at the same time achieving the appropriate balance between the interests of customers, employees, and investors.

While it is true that Gulf Power is a regulated monopoly provider of electric service, that does not mean that Gulf does not face competition. Gulf must complete in the open market both for employees and for investor funds needed to build, maintain, and operate the infrastructure required to serve our customers with the electricity that is so vital to everyday life. We must compete to attract new business essential to the economic well-being of the communities where we all live and work.

The system of regulation under which Gulf operates requires that we come before this Commission whenever rates are no longer adequate to fully cover the cost of providing electricity to our customers. The men and women of Gulf have

worked hard to delay this day as long as possible. We delayed this case to avoid compounding the problems our customers faced during the worst of what many now refer to as the Great Recession.

As we emerge from the worst of these difficult times, Gulf must be fully prepared to meet the needs of our communities for electric service in a timely and sufficient manner. If we do not have the resources necessary to effectively meet these needs in such a manner, the economic recovery that is so vital to our communities could be disrupted, if not snuffed out before it really begins.

After these opening statements of counsel, you will begin to receive testimony and evidence. You will first hear from the witnesses of Gulf Power Company. You will hear from Mr. Crosswhite and many of his fellow officers and employees of the company. They will explain how the customer is at the center of everything we do at Gulf Power. These men and women will discuss how they go about the process of serving our customers, including the planning to meet their needs and executing on those plans. You will hear firsthand from men and women who have many years of actual experience operating this electric utility.

You will also hear expert testimony regarding investor expectations as well as expert testimony about the appropriate method for allocating the cost of service and the resulting design of efficient rates intended to match revenue creation with cost causation.

Next you will hear from the opposition. Judging from their prehearing statements and prefiled testimony, I expect there will grandiose allegations about a lack of justification for investment or expenses included in the company's 2012 test year. There will likely be emotional rhetoric about the nature of this case and its impact on customers. But one thing you will not hear from the intervenor witnesses is anything resembling actual experience operating an electric utility.

After hearing from the witnesses put on by the intervenors, you will have an opportunity to hear additional testimony from Gulf's witnesses in response to the opposition. Gulf's team of witnesses, people who actually face the day-to-day challenge of balancing the interests of investors, employees, and customers alike, will show how a rate increase calculated as proposed by the

intervenors is contrary to the statutory requirements for fair and reasonable rates necessary for Gulf to continue to provide reliable service to our customers.

In this regard, it is important to note that the consequences of the decision you will be asked to reach in this case will be experienced by the actual customers, employees, and investors of Gulf Power, not the witnesses from outside the state of Florida brought before you by the intervenors.

I started out my opening statement by referencing the blessings of life. We are truly blessed to be here at this time and in this place, blessed with the opportunity to present this case to you for your reasoned decision. We will continue to do our best to be efficient in all that we do, efficient both in the continued provision of electric service to our customers and efficient in the conduct of this rate case, a case which is so critical to Gulf's ability to continue to meet the requirements of our customers in a reasonable and reliable manner that balances the needs and expectations of all, both now and in the future.

I want to thank you for your consideration.

CHAIRMAN GRAHAM: Intervenors.

Mr. McGlothlin.

MR. McGLOTHLIN: Good morning. Joe McGlothlin with OPC.

As Commissioner Edgar directed, the intervenors huddled on the subject of allocating time, and it was determined that I'll go first. I'm pleased to report that no arm wrestling was necessary to reach that result. But on the other hand, if I use any more than 15 minutes, there may be some serious jostling going on at this end of the table, so please help me remember to stop after 15 minutes.

Among other things, I intend to preview in a very brief way some of the evidence that will be presented to you in the course of receiving testimony. And to that end, I have three or four slides, some of which I've blown up to easel size, and with your indulgence, we would like to take a moment to move the easel in place.

CHAIRMAN GRAHAM: Please.

MR. McGLOTHLIN: And we also have 8 1/2-by-11s to pass out in case they're not clearly legible from your distance, and we have copies of those for the parties as well. And everything I'm going to pass out and put on the easel is taken straight

from -- without any changes, straight from the testimony and exhibits of our Dr. Woolridge, the cost of capital witness.

MR. SAYLER: If we need to move it closer, let us know.

CHAIRMAN GRAHAM: Okay.

MR. McGLOTHLIN: Commissioners, in this case you will hear testimony with respect to the revenue requirements increase that Gulf Power has requested and also testimony from intervenor witnesses who will testify that Gulf Power is overstating its revenue requirements, revenue needs. OPC will sponsor the testimony of four witnesses whose numerous adjustments to Gulf's filing would have the effect of reducing the proposed revenue increase by approximately $85 million. That takes into account both the $93 million original request and the impact of by stipulation moving certain capital costs from one of the cost recovery clauses into base rates.

Dr. Randy Woolridge, who is a professor of finance at Penn State University, will testify for OPC on cost of capital, and he will say that based upon the current conditions of capital markets, the appropriate return on equity for Gulf Power is

9.25 percent. This is in contrast to Gulf's request that you authorize 11.7 percent return on equity. The difference between OPC's 9.25 percent value and Gulf's requested 11.7 percent ROE accounts for about $24 million of annual revenue requirements, so it's a significant issue.

OPC witness Kim Dismukes, who specializes in the analysis of affiliated transactions, looked into the dealings between and among Southern Company's large family of subsidiaries, of which Gulf Power is one. She will testify that based upon allocation factors that are biased in nature and other considerations, such as the need to ensure that Gulf Power is compensated for the benefits it confers on others, a downward adjustment to Gulf's request of approximately $4 million is needed to prevent Gulf's customers from subsidizing Gulf's sister companies.

Bill Schultz of Larkin & Associates will address, among other things, Gulf's proposal to increase its storm reserve accrual from 3.5 million $6.8 million annually. He will support a reduction of the annual accrual to $600,000 annually. That adjustment would reduce the size of Gulf's request by roughly $6 million annually.

Donna Ramas of the same firm, Larkin & Associates, will testify that among other numerous adjustments, the Commission should disallow about $12.5 million of bonus compensation proposed by Gulf because the criteria an employee would have to satisfy in order to receive a bonus are too heavily driven by the corporate profitability goals rather than customer service goals. And again, that adjustment, if accepted by the Commission, would reduce Gulf's request by $12.5 million annually.

These are only some of the subjects that our witnesses will address. The total number are too numerous to treat in this shared opening.

I'm going to focus on the return on equity subject and also the subject of the North Escambia property that Gulf refers to as preserving its nuclear option.

The first slide I want to put up is something that you've seen before, and I'll start with this because one should start at the beginning. It's the formula for the discounted dash flow analysis that is used by both ROE witnesses in this case. And the premise of the discounted cash flow is that the price of the stock, P, is a function of dividends and growth in dividends over time, which

constitute future cash flows.

And as you see in the bottom conversion of that formula, the corollary to that is that if you know the dividend and you know the price of the stock and you can estimate accurately the growth rate of dividends, then the discount factor needed to bring that back to the price can be solved for as the required return on equity, as the investors' required return.

Gulf is not publicly traded. Gulf's stock is not publicly traded, so Dr. Woolridge and Gulf's Dr. Vander Weide -- I hope I'm pronouncing that name correctly -- used a proxy group of utilities in their analyses to quantify the growth rate in the formula.

Dr. Woolridge reviewed a variety of sources, and that should lead you to the second slide. And I don't intend to get into any of the details, but you'll notice across the captions that Dr. Woolridge looked at not only projected earnings per share, but also dividends and growth in book value in order to inform his analysis with different sources. He also reviewed historical as well as projected information.

In contrast, Dr. Vander Weide focused solely

and exclusively on Wall Street analysts' long-term projections of future earnings per share. As Dr. Woolridge will explain in detail when he takes the stand, this led Gulf's witness to overstate the growth component, because Wall Street analysts, even years after reforms were in place in an effort to deal with conflicts of interest, remain overly optimistic in their long-term projections. This isn't just Dr. Woolridge's conclusion. Other observers, including McKinsey & Company, a respected and credible company, have made the same observation.

With respect to the dividend component of the DCF analysis, Dr. Woolridge increased the value of the dividend by one-half the growth rate that he established to reflect the possibility that at some point during the first year, the company might increase the dividend. This happens to be the FERC's methodology.

By contrast, Dr. Vander Weide used a quarterly dividend model, and in the implementation of that, Dr. Vander Weide assumed that each quarterly dividend payment would be increased by the growth rate, and that growth rate would be used effectively to compound the amount of the dividend

during the year. This again overstates the inputs to the DCF model, because it assumes that the investor is going to require a return on that quarterly dividend, when in fact the dividend is paid and is used by the investor for whatever the investor's purpose is outside the DCF methodology.

So when you consider that when the dividend is paid, the investor has the opportunity to invest it, and take into account that Dr. Vander Weide also compounds it inside the analysis, there's a double counting there that has the effect of overstating the dividend component of the DCF.

The next slide I want to show you is the DCF equity cost rates that Dr. Woolridge arrived at. He used a yield of 4.45 percent, increased that by one-half the growth component of 4.75 percent, and arrived at 9.3 percent ROE.

The next slide shows that the results of his second methodology, the capital asset pricing mechanism, in which he concluded the equity cost rate was 7.6 percent, and he gave greater weight to the DCF analysis to conclude that the appropriate return on equity for Gulf Power Company is 9.25 percent.

In light of the time component, I'm going to

return now to one final point of Dr. Vander Weide's analysis, and that is the last slide captioned "Summary of Dr. Vander Weide's Results." You'll see that listed in this graph, which again is taken from our witness's exhibit, Dr. Vander Weide used several approaches. And of those, he took the average of the first three methods, including the DCF and the risk premium, to arrive at an average ROE of 10.8 percent.

I want to draw your attention to the next entry, which is the capital structure adjustment. Dr. Vander Weide doesn't conclude with the results of his analyses. He takes it a further step, and he contends that because the analyses are applied to a market structure based upon book value and not market value, an adjustment is necessary to reflect greater leverage. In this case, he wants to increase the results of his analyses by 90 basis points. So it is only after adding 90 basis points to the 10.8 that you arrive at Gulf's request of 11.7 percent.

The difficulty with the adjustment is simply this: Investors are aware that this Commission engages in traditional base rate ratemaking which is based upon book value. They have that

information available. They see financial statements that are based on book value. They see SEC reports that are based on book value. All that information is available and in the public domain, and yet taking that into account, they arrive at the price that is reached at by the market.

Further, there is no change in Gulf's leverage before or after this adjustment. The risk is what the risk is, and investors are fully aware of that, so there's no basis for this leverage adjustment.

Turning to the North Escambia site, it consists of 4,000 acres of property that Gulf is in the process of acquiring. Gulf asks the Commission to allow Gulf to place the property and the cost of evaluations in rate base in this case. The request has two dimensions. First, Gulf says the site will preserve Gulf's nuclear option. Gulf also says that putting the site in rate base now will avoid an accumulation of carrying charges that Gulf is authorized to accrue under the rule governing nuclear cost recovery.

You've heard of the expression of someone putting the cart before the horse. Well, in this case, the cart is about a city block in front of the horse, because the idea of a nuclear plant is

still in a very nascent form. As you know, the rule to which Gulf refers allows utilities to collect certain costs in advance after they have received a determination of need for a nuclear unit. There is no determination of need. There's no request for a determination of need. The regulation states clearly that a site has not been selected until the utility files a petition for determination of need and says the utility may file a petition seeking recovery of site selection costs only after the Commission has entered an affirmative determination of need.

CHAIRMAN GRAHAM: Mr. McGlothlin, you're about at 13 minutes.

MR. McGLOTHLIN: Thank you.

Even if the Commission rules that Gulf can accrue a carrying charge on the site selection costs, because the rule says such site selection costs cannot be recovered until the utility has the affirmative determination of need in hand, the Commission cannot allow Gulf to collect those site selection costs through rates. And if Gulf chooses to record such carrying charges on their books, but never asks for or receives a determination of need, again, those deferred charges accumulating on the

books will never be reflected in customers' rates.

The assertion that Gulf is trying to save customers money by avoiding the accumulation of deferred charges is bogus. Gulf is not trying to invoke this rule. Instead, Gulf is trying to vault over the very regulation it cites.

The Commission should refuse Gulf's request because to grant it would require Gulf's customers to bear the full cost of a site that, if it ever does become the site of a nuclear unit, clearly will happen because Gulf has found a way to share that project with joint owners or other types of participants. It would be unfair to require Gulf to pay for all the carrying costs when others will benefit from the site if and when that happens.

Gulf also says the North Escambia plant should be -- site should be placed into rate base because it can be used for conventional generation technologies as well, but Gulf doesn't need it for that purpose. It has owned the Caryville site for decades. The Caryville site was certified for a maximum of 3,000 megawatts of fossil-fueled capacity. It has been about 30 years since I was a staff -- a PSC staff lawyer. One of the first things I remember coming across our desk was the

request of Gulf for authority for ratemaking treatment of the cancellation costs associated with its first proposed coal plant on that site. That was back when I had more hair than I have now. But it makes a point that they had that site available for that use for, again, decades, and to this point have never used it for that purpose, and it isn't clear when they ever will.

Now, with respect to the ratemaking treatment of the Caryville site, we've taken no position. But we do make the point that with the Caryville site already in its possession, in its portfolio, the North Escambia site, if targeted for conventional technology, is superfluous. It would be be excess baggage, and expensive excess baggage for which customers should not be required to pay.

Thank you for your attention.

CHAIRMAN GRAHAM: Thank you. Ms. Kaufman.

MS. KAUFMAN: Thank you, Commissioners.

I'm appearing this morning, as you know, on behalf of the Florida Industrial Power Users Group, and this is a collection of companies, industrial companies who take service in Gulf's area. I just wanted you to know that some of the members in that area include International Paper and Cerex Advanced

Fabrics.

These customers take large quantities of power, and they're vitally interested in this case, as it will impact their ability to continue their operations in Gulf's territory, to retain employees there, to hire new employees, as well as their ability to compete not only in Gulf's service territory, but on a state, national, and even an international level.

We are in an interesting position in this case in that we agree with Gulf Power on some issues, particularly those that relate to rate design, and we disagree with them on others, some of the revenue issues that Mr. McGlothlin discussed. So I'm going to talk about our areas of agreement first, because that's often more pleasant.

Gulf has some of the highest industrial rates in the Southeast. Some industrial companies have left Gulf's service territory. I don't mean they've left it, but they have engaged in self-generation in order to exit from Gulf's system. Part of that has to do with the rate design that Gulf has in place.

Gulf has come to you in this case, and they have suggested a different rate design. And I

guess I should mention as a preliminary matter that rate design issues don't have anything to do with how much money you will ultimately award or not award Gulf Power, but they relate to how any amount you award will be spread among the customer classes.

FIPUG supports the rate design proposals that Gulf has made, and you will hear Mr. O'Sheasy testify about those. And Mr. Pollock also has provided you some additional information about the propriety of what's known as the minimum distribution system to apportion costs among ratepayers. This is the methodology that is used in many states, several of them in Gulf's territory, and it is a methodology this Commission has approved as well in the matter of the CHELCO rate increase.

Now, these issues, which are 106 and 107, I believe, your Staff has taken no position on these issues. Interestingly enough, Gulf, FIPUG, and the other parties either support Gulf's position or have no position on the issue at all, so you would expect this would be an issue that would be stipulated, just as many others that you voted on this morning would be stipulated. However, even

though Staff has taken no position on the issue in the Prehearing Order, it is clear to us that they do oppose the parties on this issue. And we would urge you to carefully consider the arguments that you're going to hear.

The rate design using the MDS is not a methodology that shifts costs between classes. It is a methodology that appropriately apportions any revenue increase to the cost causer of the increase. And I'll just give you a very brief example. If you have a 100-home subdivision and you have one large customer, each of which is taking the same amount of power, you can imagine that the distribution lines, the meters, the service drops, you're going to need a lot more customer-specific information and facilities for those 100 homes than you will for the one customer, both of whom are taking the same amount of power from Gulf. That's what this system addresses. It matches the cost causers with the spread of any revenue increase.

In addition, this methodology we think will make Gulf's industrial customers more competitive, and it will help them to attract new business to Gulf's area as well as encourage them to expand in

their area. It fairly apportions rates among the entities that are causing the cost increase.

So we think that this is a methodology whose time has come in Gulf's service territory, and it is one that you should approve in this case. We were hopeful that it would be approved by stipulation, and we're still hopeful that perhaps that will occur in the case. But regardless of how the issue is played out, you should adopt the methodology that Gulf has presented to you on these cost of service issues because it is the fairest methodology for apportioning costs and taking, you know, a step toward lowering industrial rates in Gulf's service territory.

I'm just going to spend a moment now on two of the revenue issues. Gulf has asked you for approximately a $101 million rate increase, and we think that increase is excessive. I think you heard Mr. Stone tell you about the impact that certain events have particularly had on Gulf's service territory and their customers. We don't disagree. However, we do think that you need to look closely at the amounts that are being requested, and just as consumers in Gulf's territory and elsewhere have had to trim the fat,

we think you should make Gulf do that as well.

As to the return on equity that Mr. McGlothlin discussed, Gulf is asking for a 11.7 return on equity. That was a pretty shocking number to FIPUG, and we hope to you as well. We certainly suggest to you that you should be looking at somewhere below 10 percent for Gulf's return on equity as suggested by OPC's witnesses and FEA's witnesses. When you have consumers that are earning less than 1 percent on their investment, to the extent they have any investments at all, to suggest that Gulf should be permitted to earn close to 12 percent we think should be rejected out of hand.

The last revenue issue I want to touch on briefly is one you've heard a little bit about already, and that's the storm accrual issue. Gulf wants to double the storm accrual annual charge to customers. And I look at this issue as sort of a "pay me now or pay me later" issue. Gulf wants customers to pay now, in advance of any storm restoration costs. We suggest to you that ratepayers would rather keep that money in their pocket.

The Commission has a process, and it has been

used twice by Gulf and by the other utilities to come before you and expeditiously request a surcharge if necessary to fund storm restoration. That has worked, and it ties the costs to the time that the costs are incurred rather than allowing Gulf to collect those costs in advance, and we think that you should continue with that process.

Finally, related to the storm issue, Gulf has some storm hardening activities they want to include in rate base. I believe it's about $3 million. However, they have failed to consider that amount in asking for this increased surcharge. I understand their position on that to be, "Well, we've done these storm hardening activities, but we haven't had a storm, and so we're not really sure what impact those activities will have."

I would say to you they can't have it both ways. If they're doing storm hardening and they want the customers to pay for it, they should take that into account in the accrual. If they don't know if those activities are going to be beneficial or not, then ratepayers shouldn't have to be paying for them. I think you'll hear more about that as we go on that.

That concludes my opening. Thank you.

CHAIRMAN GRAHAM: You guys have about six minutes left.

MR. WRIGHT: Thank you, Mr. Chairman. Good morning, Commissioners, and thank you for the opportunity to address you today.

I'm Schef Wright, and like Mr. Stone, I too am blessed. I'm blessed to live in this beautiful part of this wonderful earth. I'm blessed to have lived right here in Tallahassee for 31 years now and worked in energy that whole time doing meaningful and challenging work. I'm blessed that my sons are here with me.

I'm also blessed to have the opportunity of representing the Florida Retail Federation, a statewide organization of about 9,500 members, from the largest grocery and department stores to literally thousands of mom-and-pop businesses. For all of our members, reliable electric service at a reasonable cost is critical to our ability to provide our services to our customers.

We believe, and the testimony will show, that it is the duty of every regulated utility in Florida to provide safe, adequate, and reliable service at the lowest possible cost. And it is against this standard that you as the Public

Service Commission must measure Gulf's requests for increased base rates of approximately $101 million per year.

The evidence will show that Gulf does not need anywhere close to this amount in order to continue providing safe and reliable service. The evidence will show that Gulf's requests are overreaching, overreaching in that the company is asking for way more than it needs in a number of areas, from ROE to an unnecessary increase in its storm accrual, to asking customers to pay returns on assets that are not used and useful, to inflated employee and compensation costs, and others. I'll touch briefly on a few of these.

Gulf has asked for an after-tax ROE of 11.7 percent. This translates to a before-tax ROE of more than 19 percent. In today's economy, with long-term interest rates at persistently low levels, this is overreaching. Gulf faces minimal risks. The Commission has recognized this principle, that low risks warrant lower equity returns, and the proof in the pudding comes right out of your last two major rate cases.

FP&L got a 10.0 percent ROE in 2010. Progress Energy Florida got a 10.5 percent ROE in 2010.

Since that time, both utilities have continued providing safe, adequate, and reliable service. Both have been able to go to the markets and raise substantial -- billions of dollars of equity and interest capital. Their parent companies have been able to increase or maintain their dividends, and their stock prices have increased.

Gulf's request to nearly double its storm accrual is almost as egregiously overreaching. Gulf has more money today in its storm reserve than it had when Ivan struck its service area in 2005. Following that storm, Gulf restored service, came to the Commission and got relief, incidentally, relief through a stipulated settlement with the consumer parties to recover reasonable and prudent costs. The same thing happened again in 2006.

Gulf has also asked to have customers pay for returns on construction work in progress on assets that will not be used and useful in the test year and a nuclear site that will not be used and useful in the test year, and which Gulf's own Ten-Year Site Plan shows will not be used for anything until sometime possibly in the 2020s, the next decade, if ever.

Finally, Commissioners, we ask you to consider

the significant adverse impacts of the proposed rate increase on individual customers and businesses in Northwest Florida.

Mr. Stone said you won't hear from us from the perspective of having experience running a utility. That's true probably for all of the witnesses. I'm not 100 percent sure. But at the same time, Gulf's witnesses don't have experience running mom-and-pop businesses. They don't have experience running large commercial operations. They don't have experience running competitive industrial enterprises, and they don't have the kind of experience as residential customers who have addressed you. In the service hearings in Pensacola and Panama City, you heard from dozens of individuals as to how hard yet another increase will impact them.

Mr. Stone also said that -- he implied that they think they need an increase to help attract new business. I'll tell you what: Gulf's rates are already among the highest in the Southeast for commercial and industrial customers, and adding to them will not help attract new business.

We do agree with Public Counsel's witnesses that Gulf needs a modest increase, $16.2 million a

year. We respectfully ask that you approve that amount, but no more. Gulf simply doesn't need any more than that to continue providing safe, adequate, and reliable service.

Thank you very much.

CHAIRMAN GRAHAM: Thank you, sir.

MAJOR THOMPSON: How much time do I have?

CHAIRMAN GRAHAM: Whatever you need.

MAJOR THOMPSON: I'll be brief. I just wanted to let you know that I represent the Federal Executive Agencies, and I intervene in different states around the country.

The FEA has a unique standing in these proceedings in that we are stewards of the tax dollar. We represent six of the largest Gulf Power Companies in the region, not only Tyndall, Eglin, and Hurlburt Air Force Bases; we represent the Navy bases, Pensacola, Whiting Field, and Panama City. We have a national defense mission which is unique to the FEA.

So every base commander has more mission than they have money to accomplish the mission. Each year Congress allocates a finite budget for each base. The same pot of money that pays for the utilities also pays for the mission requirements.

When utility costs go up, something has to give. Every dollar spent on increased utility costs is a dollar less to be spent on the flying mission, deployment mission, or Navy SEAL mission, et cetera.

Every dollar counts in this economic climate. If you've been watching the news, you know that there's a possible $1 trillion cut in the DOD budget in the near future. This could be a negative effect on all that depend on the military.

Gulf Power has requested a large increase in demand and energy charges. This will result in paying millions of dollars more for electric services for the combined military bases in Gulf Power's region. The FEA's goal in this is to make the utility operate prudently, while at the same time able to provide safe and adequate services.

Specifically in this case, FEA will present two witnesses for this hearing, Mr. Mike Gorman and Mr. Greg Meyer. And Mr. Stowe, who was stipulated earlier, you won't hear from him.

But Mr. Gorman is a nationally recognized expert in rate of return issues. He has given expert opinion in regard to rate of return in excess of over a thousand times and in 30 states

and internationally in Canadian provinces. He will present evidence to support a 9.75 return of equity. I encourage you to ask Mr. Gorman specific questions in regards to this issue.

Mr. Meyer has had 29 years of regulatory experience at the Missouri Public Service Commission before joining his current firm.

FEA had a few unique issues different from our intervenors. We agree with them on many of the same things, but we had a few unique issues, but worked with Gulf Power to stipulate on all but one. The sale for resale issue in Issue 42 is still open. Our expert, Mr. Meyer, will tell you why we believe Gulf Power is underestimating the profits from sale for resale transactions in the future test year.

At the end of the day, every additional tax dollar spent by DOD on utilities is a dollar less spent on the flying jets and sailing aircraft carriers taking care of troops or protecting our nation.

If the increase requested by Gulf Power is adopted as proposed, it would equate to millions of additional dollars that are no longer available for operational mission requirements. In the face of a

trillion dollars worth of DOD cuts, FEA encourages the Commission to carefully review each aspect of the Gulf Power operation.

That's all. Thank you.

CHAIRMAN GRAHAM: Thank you.

All right. A couple of things. I'm going to swear all the witnesses in at one time. I need for you when you call your specific witnesses up and you're introducing them, make sure that you ask them on the record that they're sworn so we have that on the record.

I would like to hear -- we need to make sure that we stay away from duplicative questions. I mean, if one person has asked the question, we don't need for the next three people to ask that same question.

I know how you attorneys like to object to things all the time, which is fine. That's part of hearing process, and I get that. You'll find that I err more towards getting more and more things on the record than getting less things on the record, and I think it's the job of the Commission to weigh those things, be they hearsay or fact, when we make our decision.

There is no friendly cross unless you have a

position that's contrary to the person that's offering the witness, and we'll allow that.

If there's no other questions about witnesses, I will swear them all in. The ones that are here, if I can get you to stand and raise your right hand.

(Witnesses collectively sworn.)

CHAIRMAN GRAHAM: That all being said, I think it's about time to take a break. It's about 11 o'clock. Let's take a 10-minute break, and I'll see you back here at 10 after.

(Recess from 11:00 a.m. to 11:10 a.m.)

CHAIRMAN GRAHAM: All right. It looks like, Gulf, you have the first witness.

MR. STONE: Mr. Chairman, if I may have a moment's indulgence, I have a couple more preliminary matters I would like to take care of.

CHAIRMAN GRAHAM: Okay.

MR. STONE: First, yesterday we received word from staff counsel that the Commissioners would very likely be using a computer to access the comprehensive or composite exhibit list that they would be using, and they had suggested that it might be appropriate for our witness to have access to the CD on which those documents are produced so

that they would be looking at the documents in the same fashion that the Commissioners might be looking at it. We're prepared to do that.

However, that was a new development for us, and what we would request is that if a witness will be called upon to look at such exhibits on the CD, might it be possible for us to have a technical assistant with that witness that can help them with the computer? Since that's a relatively new development that we weren't anticipating, we haven't gone to the trouble to teach our witnesses how to access the documents on the computer, and we don't want to show which ones of our witnesses are technologically savvy and which ones aren't.

CHAIRMAN GRAHAM: Well, I can tell you that I am not technologically savvy, and I like to have a hard copy in front of me as well. So I don't know where that all came from. I mean, you guys are more than welcome to have somebody up there, but usually I'm shuffling so many papers around here, I can't do both the computer screen and the papers in front of me, so I always like to have a hard copy in front of me.

MR. STONE: The second preliminary matter is actually just that the next exhibit on the exhibit

list are the Minimum Filing Requirements that Gulf filed with its petition, and it's identified in the Comprehensive Exhibit List for entry into the record as Exhibit Number 70 -- I'm sorry, 7. And at the time, I would ask that we move the MFR schedules that were filed by the company into the record.

CHAIRMAN GRAHAM: Do we have any comments or objections about moving Exhibit Number 7 into the record.

Seeing none, we'll do it.

(Exhibit Number 7 was marked for identification and admitted into the record.)

MR. STONE: And with that, our first witness on the order of witnesses is Mr. Crosswhite.

CHAIRMAN GRAHAM: Thank you. One of the things that I didn't say earlier but I'll say now, if you have several exhibits you want to pass out, it works a lot easier for us if we can get you to pass them all out at one time when the witness comes up rather than, you know, one at a time, because that tends to prolong this process. So if you know the witnesses are coming along and you know that you have several exhibits, if I can get you to start packaging those, stapling those, or

banding those, or however you want to do that.

Please, sir.

Thereupon,

MARK A. CROSSWHITE

was called as a witness on behalf of Gulf Power Company and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. STONE:

Q. Mr. Crosswhite, you were present when the oath was administered to all the witnesses; is that correct?

A. Yes.

Q. And you took the oath?

A. Yes.

Q. Would you please state your name, your business address, and your position with Gulf Power Company.

A. My name is Mark Crosswhite. My business address is Gulf Power Company, One Energy Place, Pensacola, Florida, 32520. And I'm the president and chief executive officer of Gulf Power Company.

Q. Are you the same Mark A. Crosswhite that caused to be filed 14 pages of prefiled direct testimony in this proceeding?

A. Yes.

Q. If I were -- do you have any changes or corrections to your prefiled direct testimony?

A. No.

Q. If I were to ask you the questions and answers in those 14 pages -- I'm sorry. If I were to ask you the questions, would the answers be the same?

A. I would give the same answers, yes.

MR. STONE: We would ask that Mr. Crosswhite's testimony be inserted into the record as though read.

CHAIRMAN GRAHAM: We will insert Mr. Crosswhite's testimony into the record.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
Mark A. Crosswhite
Docket No. 110138-EI
In Support of Rate Relief
Date of Filing: July 8, 2011

Q. Please state your name, business address, and occupation.

A. My name is Mark Crosswhite. My business address is One Energy Place, Pensacola, Florida, 32520. I am President and Chief Executive Officer of Gulf Power Company (Gulf or the Company).

Q. Please summarize your educational and professional background.

A. I graduated with a Bachelor of Arts from the University of Alabama at Huntsville in 1984. In 1987, I graduated from the University of Alabama School of Law with a Juris Doctorate degree. That same year, I began working in Birmingham, Alabama with the law firm of Balch & Bingham. I remained at the law firm until 2004 when I was named Senior Vice President and General Counsel of Southern Company Generation, the business unit that oversees the generating fleet of Gulf Power and the other operating companies that make up the Southern electric system. In 2006, I moved to Alabama Power Company as Senior Vice President and Counsel, where I oversaw compliance and legal matters. In 2008, I became the Executive Vice President for External Affairs at Alabama Power, with responsibility for economic development, public relations, environmental affairs and governmental affairs. In November 2010, I was

elected President and Chief Executive Officer of Gulf Power, effective January 1, 2011.

Q. What is the purpose of your testimony?

A. The primary purpose of my testimony is to emphasize Gulf's need to receive an adequate increase in the level of its base rates in a timely manner. I will provide an overview of Gulf's filing in this case, including the major factors causing the need for such rate relief and the impact these factors have on Gulf's ability to achieve a reasonable rate of return on the investment used to serve our customers. I will also review our efforts to control costs and discuss programs we have put into place that have resulted in efficient and reliable electric service to our customers as evidenced by high customer satisfaction ratings.

Q. Would you please provide a brief overview of the case that will be presented by Gulf's witnesses?

A. Our case will be presented by a number of witnesses testifying in detail on behalf of the Company. These witnesses include Company officers and employees, as well as consultants from outside the Company with expertise on certain specific subject matters. Collectively, these witnesses will demonstrate that Gulf's costs of providing retail service have far outpaced Gulf's revenues, that Gulf's actual and projected earned rate of return is well below any reasonable level necessary to attract capital and serve customers, and that the rates that Gulf has proposed to achieve necessary rates of return are just and reasonable. Simply stated, they

show that a base rate increase is necessary if Gulf is to maintain customer satisfaction and the quality of service Gulf's customers desire.

Mr. Teel, Gulf's Chief Financial Officer, will address the overall need for rate relief, actions taken to avoid a base rate increase over the previous ten years, Gulf's capital structure and related cost of capital, and other financial matters pertinent to our request for rate relief.

Mr. McGee will address Gulf's forecast methodologies and results for customers, energy sales, peak demands and base rate revenues. Mr. McGee will also address the load research performed by and used by Gulf in this proceeding.

Mr. Buck will provide an overview of Gulf's planning and budgeting process, which results in the production of Gulf's financial forecast.

Mr. Burroughs, Gulf's Senior Production Officer, will address the operation and performance of Gulf's generation fleet. Mr. Burroughs will also review generation capital additions and fuel inventory levels necessary for Gulf's continued provision of reliable generation.

Mr. Grove will discuss Gulf's generation resources used in the production of electricity for our customers. He will also address Gulf's resource planning process, production investment, and our 2012 production O&M budget.

Mr. Jacob, Gulf's Vice President over Customer Operations, will provide an overview of that department and discuss Gulf's commitment to customer service and satisfaction. Customer Operations includes the following business functions: Transmission, Distribution, Customer Service, and Customer Operations Support.

Mr. Caldwell will discuss Gulf's transmission system, including Gulf's transmission system performance. Mr. Caldwell will also discuss our current transmission investment and cover Gulf's projected transmission capital expenditures and O&M expenses for the 2012 test year.

Mr. Moore will address Gulf's electric distribution system, including Gulf's distribution performance, and describe Gulf's service area. Mr. Moore will also address Gulf's current distribution system investment, as well as related capital and O&M budgets for the 2012 test year.

Ms. Neyman will discuss Gulf's Customer Service & Information, Customer Accounts and Sales expenses contained in the 2012 test year. Ms. Neyman will also describe the Company's commitment to customer service, conservation and energy efficiency, and the associated benefits for our customers. Lastly, Ms. Neyman will discuss the Company's economic development activities and expenses.

Ms. Erickson, Gulf's Comptroller, will explain Gulf's 2012 O&M budget associated with the Administrative and General (A&G) function. She will

outline the need to increase Gulf's property damage reserve and support the depreciation and tax expenses included in the test year. Ms. Erickson will also explain Gulf's projected test year expense for uncollectible accounts.

Mr. Twery and Ms. Crumlish, consultants to Gulf from Aon Hewitt, a global market leader in human resource consulting, will discuss the reasonableness of the Company's benefits program amid the rising costs of retirement and medical benefits.

Dr. Vander Weide, Research Professor of Finance and Economics at Duke University and President of Financial Strategy Associates, will discuss Gulf's cost of common equity.

Mr. O'Sheasy, a vice president of Christensen Associates, will address the cost of service study.

Mr. Thompson will address rate design and other tariff issues. He will set forth all proposed changes in rate design and discuss the development of the proposed rates in light of the results from the cost of service study.

Mr. McMillan will discuss the development of the test year jurisdictional adjusted rate base, net operating income, capital structure, and the resulting retail base rate revenue deficiency.

Q. How long has it been since Gulf last filed for an increase to base rates?

A. Gulf's last base rate case was Docket No. 010949-EI filed in September 2001. That last case was based on a fully projected test period comprised of the twelve months ending May 31, 2003 and resulted in an increase to Gulf's base rates that was placed into effect with meter readings beginning June 7, 2002.

Q. Are you saying that Gulf has not had price increases since 2002?

A. No. This requested increase to our base rates is not the first time our prices will have increased since our last rate case. There have been annual adjustments to our prices through the cost recovery clauses each year to cover such items as fuel to run our generating plants, conservation programs to help our customers manage their energy use, and the costs of compliance with an ever increasing array of environmental regulations.

The price increases that our customers have experienced due to the operation of the cost recovery clauses are restricted to those specific items of cost which are the subject of the annual fuel, conservation and environmental proceedings and do not address increasing costs in the areas of our business that are covered through our base rates. While the focus of this case is solely on that portion of our business that is not addressed through the cost recovery clauses, I assure you that we work diligently to control costs in all areas of our business.

Q. What are the major factors that cause the current need for rate relief?

A. Since our last request for base rate relief, the costs of continuing to provide reliable electric service to our customers have increased at a rate that outpaces the growth in our revenues. Gulf is requesting rate relief in order to continue to fulfill the public service requirements set forth in the statutes and to fulfill the needs and expectations of our customers in a reliable, safe and efficient manner.

During the years between 2002 and 2011, numerous factors have increased the cost of providing electric service. Among these are the addition of more than 850 miles of new distribution and transmission lines; replacing and repairing the Company's existing electrical infrastructure; increased spending to harden the electrical infrastructure to mitigate potential storm damage and facilitate restoration following storms; and the cumulative effect of inflation on the materials, goods and services we must purchase in order to provide service to our customers. Gulf's base rate revenues have not kept pace with these increases in our operating and capital costs. As shown on Mr. Teel's Exhibit RST-1, Schedule 2, this mismatch between the growth of capital and O&M relative to revenues has become particularly pronounced since 2007.

Q. What actions has Gulf taken since its last base rate case to control costs and avoid requesting rate relief?

A. As detailed by Gulf's other witnesses, the Company has taken a number of steps since its last base rate case to control the costs that are

addressed through base rates. One such example involves our generation resource decisions. Rather than build and operate new generating plants in the near term for which we would be entitled to earn a return, we have made arrangements to purchase power from existing generating assets owned by other companies. In each instance the cost of the contract was less than what Gulf's customers would have paid if Gulf had built a unit. The most recently signed contract was determined by the Commission to save Gulf customers more than half a billion dollars on a net present value basis through 2023. This decision saved money for Gulf's customers, improved Gulf's fuel diversity and helped defer a base rate proceeding.

Q. Please describe some of the major programs that Gulf has implemented since its last base rate case to improve its operations and customer service.

A. Gulf is focused on making it easy for customers to do business with us by identifying meaningful and relevant options that fit our customers' lifestyles. Through our website, GulfPower.com, we offer innovative solutions to help serve our customers more effectively. Customers can conduct an energy audit of their own home, pay bills or complete other account services such as connects and disconnects through our website. In 2005, the Company enhanced the voice response unit used by customers when calling Gulf's Customer Service Center. This improvement gives customers the option of using their voice to make

selections from the menus, thereby simplifying the experience for customers.

As part of our effort to bring efficiencies to Gulf's transmission and distribution system, we have partnered with the Department of Energy through the Smart Grid Investment Grant program. Participation in this program enabled Gulf to enhance our grid through the installation of intelligent electronic devices on our transmission and distribution infrastructure. The transmission devices will improve the monitoring, protection and control of the transmission system through remote monitoring devices and electronic relays for our transmission substations. Our distribution enhancements will include automated line devices which will provide automatic fault isolation and service restoration. These smart grid features increase reliability, assist with power restoration and fault location, and provide new avenues to interact with our customers through detailed usage and pricing information.

The implementation of Advanced Metering Infrastructure (AMI) is another way we are creating efficiencies for our customers. AMI meters will allow Gulf to read and remotely check meters without visiting customer premises, help identify power quality issues, and eliminate the need for estimated meter readings.

Our generation group has continued to look for ways to more effectively manage costs while continuing to maintain system reliability. As a direct

result of our effective maintenance practices we are also projecting longer lives for our fleet of generating units, which reduces depreciation rates and consequently the level of annual depreciation expense that must be supported by our base rates.

These are samples of the programs discussed by Gulf's other witnesses undertaken to improve operations and customer service.

Q. Please describe Gulf's focus on providing value to its customers.

A. Maintaining and improving the value of our service to our customers is among the highest priorities of every employee at Gulf, where we believe in putting the customer at the center of everything we do. We are in constant contact with our customers through our customer service, energy efficiency, engineering and other field representatives and through all our employees who are active members in our communities. Personal visits, letters, e-mails and telephone calls are all methods that customers use to let us know how we are doing. In addition, we have developed a survey process to give us critical feedback on how our customers rank us in comparison to the rankings of peer utilities by their customers.

Q. How does Gulf rank in customer value as compared to its peer utilities?

A. When measured against a peer group of utilities, Gulf was in the top quartile of overall performance for 2010 and has been every year since 2000. Our goal is to be among the best utilities in regards to customer service, and we are proud of our performance when compared to the top

utilities across the country. This outstanding performance is a testament to the continued efforts of Gulf's employees to exceed our customers' expectations each and every day. Ms. Neyman will explain in detail how we develop this information for use in comparing Gulf to our utility peers.

Q. How has this concern for your customers been reflected in this rate case?

A. First and foremost, our concern for our customers is reflected in the timing of this case. We worked hard to delay this case for as long as possible to keep from seeking a base rate increase during what we refer to as the Great Recession, the period between 2007 and 2010. This meant prioritizing our spending in order to do what was absolutely necessary to provide efficient and reliable service in the near term and still operate within the revenues produced by our existing rates. As part of this effort, we also slowed the hiring of new employees who are needed for the long term health and operation of our system.

While such steps are possible for short periods of time on a well maintained and operated system, we cannot sustain such restrictions on capital investment or O&M expenses over long periods of time without a detrimental effect on the system and the reliability of our service to customers. As our local economy emerges from the Great Recession, we must be ready to provide the levels of service required by our customers to meet and sustain economic growth. In order to be ready, we have been making additional necessary capital investments and performing necessary O&M activities that have caused our achieved rate of return

during each of the months since June 2010 to fall below the minimum of our authorized rate of return as determined by the Commission. Such low achieved rates of return are simply not fair to Gulf's investors and are not in the best interests of Gulf's customers.

Our concern for our customers is also reflected in the processes we use to set our capital and O&M budgets. We plan our systems to serve the long term needs of our customers as efficiently and reliably as possible. We work diligently to identify and implement in a timely manner new systems and programs that bring value to our customers. We work hard to ensure that we get the most benefit for our customers in our capital and O&M spending. We are mindful that reliable and efficient electric service is very important to our customers, and therefore we continue to work hard to spend our resources wisely.

Q. How does Gulf's requested increase compare to Gulf's total revenues before consideration of the increase?

A. Gulf is requesting a base rate increase of $93.5 million, which is less than 7.5 percent of the projected total retail revenues for 2012 using existing base rates. As a proportion of the revenue from base rates, the increase is slightly less than 21 percent. In comparison, through 2012 the Consumer Price Index (CPI) will have grown by more than 25 percent since our last change in base rates. Gulf's other witnesses in this case provide details regarding how and why many of our costs of doing business have increased at a rate that is larger than the rate of inflation as

measured by the overall change in the CPI. And yet, we have been able to control our overall base rate revenue requirements such that our rate request is lower than the cumulative overall change in the CPI. Gulf has managed to delay its request for a base rate increase for nearly ten years, and is only now seeking an overall increase for prospective application.

Q. What is Gulf's projected rate of return for the test year without rate relief?

A. As shown on Mr. Teel's Exhibit RST-1, Schedule 3, the Company's rate of return has been below the minimum of our authorized rate of return since mid-2010. Without rate relief, Gulf's return on common equity associated with base rates for the 12 months ending December 31, 2012 is projected to be 2.83 percent. This is clearly not adequate when compared to the 11.7 percent cost of common equity that Dr. Vander Weide has determined to be reasonable and appropriate for Gulf. Without timely rate relief, Gulf will continue to endure a weakening financial condition which will adversely affect our ability to provide reliable electric service to customers.

Q. Please summarize your testimony.

A. Gulf's mission is to safely provide affordable, reliable and environmentally responsible electric service to our customers, while working to improve the communities we serve. We are very proud of our commitment to this mission. Our successes are a result of the dedicated employees who serve our customers across Northwest Florida. Through the efforts of these employees, we have been successful in avoiding, over the last ten

years, the necessity to request an adjustment to our base rates. We have done so while keeping operating budgets lean in the face of increasing costs to build, operate and maintain our system.

We understand that price increases can place an economic burden on our customers. However, an inability of Gulf to meet customers' reasonable service requirements as we emerge from this recession would place an even greater burden on our customers and our local economy. We are not able to continue to defer our request for this increase in base revenues.

This price adjustment will provide Gulf the reasonable opportunity to earn a fair return, enable us to maintain access to capital markets at a reasonable cost and, most importantly, help to ensure that we are able to continue providing safe, affordable and reliable service at the levels our customers have come to expect. Keeping Gulf financially healthy by granting us the requested increase in retail revenues is in the best interests of our customers.

Q. Does this conclude your testimony?

A. Yes.

BY MR. STONE:

Q. Mr. Crosswhite, do you have a summary of your testimony?

A. I do.

Q. Please proceed.

A. Good morning, Commissioners. My name is Mark Crosswhite, and like I just said, I'm the president of Gulf Power Company. Thank you for the opportunity to speak today on behalf of Gulf Power and its customers who serve our -- excuse me, and its employees who serve our customers in Northwest Florida.

Gulf Power has provided electric service to Northwest Florida since 1926, and we understand that we can only be successful if the communities we serve are successful. We understand that electricity prices have a direct impact on our customers. We also understand that customers have seen electricity prices increase due to escalating fuel costs and environmental requirements. We also understand that the region has been in an economic downturn.

So let me be clear. Gulf Power has worked very hard to delay this request for as long as possible. In fact, Gulf Power has not asked for a base rate increase since 2001, 10 years. We would not be asking for this increase now if it were not necessary to serve

our customers.

Over the next few days, you will hear from witnesses for Gulf Power. We will discuss our efforts to reduce costs and improve efficiency, we will discuss the investments that we have made in the electric system, and we will discuss the effects of inflation on the cost of materials, goods, and services that we must purchase in order to serve our customers.

In simple terms, it costs us much more to do business today than it did when our base rates were last set. The cost of making and delivering electricity has increased. Our base rates have not. So while we are reluctant to come here and ask for an increase, we must do so. We must cover our rising expenses and continue to make investment in the electric system so that we can fulfill our obligation to provide adequate and reliable service to the public.

Today I speak on behalf of all the employees of Gulf Power by saying that we remain committed to delivering reliable electric service, outstanding customer service, and being a good community citizen.

Thank you.

MR. STONE: We tender Mr. Crosswhite for cross-examination.

CHAIRMAN GRAHAM: Okay. Intervenors, I guess

I'll let guys police which order you've got them.

Mr. McGlothlin.

CROSS-EXAMINATION

BY MR. McGLOTHLIN:

Q. Sir, I'm Joe McGlothlin with the Office of Public Counsel. I have only several questions for you.

A. Yes, sir.

Q. If you'll look at page 8 of your prefiled testimony.

A. Yes, sir.

Q. And in the context of efforts the company has taken reduce costs for customers, you cite the experience of generation resource decisions, do you not?

A. Yes, sir.

Q. And the one example you gave there has to do with entering into a purchased power contract in lieu of constructing a unit that would have been more expensive had that self-build option gone forward; correct?

A. That is correct.

Q. Mr. Crosswhite, you would agree with me, would you not, that Gulf Power Company has an obligation to pursue service at the least cost for customers?

A. Yes, sir.

Q. And in fact, with respect to decisions regarding self-build options versus purchased power

options, isn't it true that the Commission has a regulation that requires Gulf, in the instance of certain types of proposed power plants, to issue an RFP and actively solicit alternatives to a self-build proposal?

A. I really am not aware of the specific regulation, but I may be able to answer your question anyhow. Without regard to the regulation, we're going to try to serve our customers in the least expensive way we can.

MR. McGLOTHLIN: I do have one document to distribute for this witness. We don't need a number because this has already been identified as Exhibit Number 115 in the composite exhibit that Staff distributed.

BY MR. McGLOTHLIN:

Q. Before I refer you to the document, please turn to page 13 of your prefiled testimony. Beginning at line 3, you say that Gulf has managed to delay its request for a base rate increase for nearly 10 years; correct?

A. Yes, sir.

Q. The document that I've provided to you, Exhibit 115, is Gulf's response to Citizens's Fourth Set of Interrogatories, and it deals with the property

damage accrual. Take a moment and become familiar with that, if you will.

And I distribute this in response to your statement that you've delayed a base rate increase for 10 years, and I think my question to you with respect to this document will put Gulf's experience over time in fuller context with respect to its operations under existing rates.

Sir, are you familiar with the fact that in 1996, Gulf Power requested and the Commission approved discretionary authority for Gulf to increase accruals to the storm damage reserve when it had earnings that would otherwise exceed the ceiling of its authorized range of return?

A. No, sir. I'm really not familiar with that, no, sir.

MR. McGLOTHLIN: Well, let me ask the Commission to take official notice of Order No. PSC-96-0023 issued on January 8th of 1996 in Docket No. 951433.

BY MR. McGLOTHLIN:

Q. As you see, Mr. Crosswhite, the response to the interrogatory contains a summary of the accruals that Gulf Power made to its storm damage account on a yearly basis throughout the 10-year period covered by

the document. And if you'll turn to the first page, which is for the year 2001.

A. Yes, sir.

Q. And under the column "Discretionary Accrual," do you agree that this reflects that Gulf Power made an additional accrual for the storm damage in 2001 in the amount of a million dollars?

A. That is what it appears to show, yes, sir.

Q. Turn to the page showing the year 2003, which is page 4 of 12 of the document. Does this show that Gulf made a discretionary accrual to the storm damage fund in the amount of $7,100,000?

A. Yes.

Q. The next page for 2004, does this indicate that Gulf Power Company had earnings sufficient to make an discretionary accrual of $15 million in that year?

A. Yes.

Q. In 2005, the next page, does this reflect that under existing rates, Gulf Power Company had revenues and earnings sufficient to make a discretionary accrual in the amount of $6 million?

A. Yes.

Q. For the year 2006, does this page indicate that in that year, Gulf Power Company under current rates had earnings sufficient to make a $3 million

discretionary accrual to the storm damage?

A. Yes.

Q. Also on page 13, at lines 10 through 13, you state that without rate relief, Gulf's return on common equity associated with the base rates for the 12 months ending December 31, 2012, is projected to be 2.83 percent. Is that 2.83 percent based upon the assumption that Gulf's level of expenses would be that level identified in the test year in this case?

A. I'll probably need to defer that question to Mr. McMillan to get exactly what was in that number that provided that 2.83 percent.

MR. McGLOTHLIN: I have no further questions.

CHAIRMAN GRAHAM: Thank you, sir.

Ms. Kaufman.

MS. KAUFMAN: Thank you, Mr. Chairman.

CROSS-EXAMINATION

BY MS. KAUFMAN:

Q. Good morning, Mr. Crosswhite.

A. Yes, ma'am.

Q. Nice to meet you earlier.

A. Yes, ma'am.

Q. Just to follow up on one thing that Mr. McGlothlin just asked you about on page 13, the 2.83 percent --

A. Yes, ma'am.

Q. -- that you deferred to Mr. McMillan, am I right that even though you've included that number in your testimony, you can't really give us the derivation of it?

A. I'm not able to provide the details of what he just asked. I'm not exactly sure what went into the test year calculation.

I might ought to get you to repeat his question for me. I might understand it if I heard it again.

Q. I wasn't trying to repeat Mr. McGlothlin's question. I was just asking you the number that appears on line 12, where you state that if you don't have rate relief, your return on common equity is going to be 2.83 percent. And I understood you to respond that you couldn't really get into detail on that number. And my question was, you've included this number in your testimony without being able to give us the detail for it; is that right?

A. I cannot give you the detail, but I believe Mr. Teel, who is our CFO, and Mr. McMillan, who is our budget witness, can provide that information to you. And, yes, I relied on them.

Q. Did they provide that number to you?

A. Yes.

Q. Now, you mentioned -- I think in your opening, Mr. McGlothlin asked you some questions related to the fact that Gulf hasn't had a rate case since 2002; is that correct?

A. I think it was filed in 2001, and the decision was in 2002, yes, ma'am.

Q. I was around then, I have to say.

But you also recognize in your testimony that Gulf has had annual increases every year in the fuel adjustment and capacity cost recovery and environmental cost recovery, the clauses that we deal with every year toward the end of the year; correct?

A. With one modification to your question. I think you said annual increases. I don't know if there have been annual increases, but there have been annual adjustments for those clauses.

Q. Would you accept, subject to check, that those have been increases?

A. I guess I -- I would prefer to see it, because I don't know if I'll be back and forth on the stand, so if I could see the --

Q. Okay. That's fair enough. And I think those orders will also speak for themselves.

A. Okay.

Q. Now, on page 7, you talk -- page 7 at line 9, you begin talking about the factors that have prompted the rate case filing that we're talking about here today; correct?

A. Yes, ma'am.

Q. And one of the factors that you talk about begins on line 13, which is increased spending to harden the electrical infrastructure to mitigate potential storm damage and facilitate restoration following storms; correct?

A. Correct.

Q. And would you agree that generally we kind of shorthand that as storm hardening activities?

A. Yes, ma'am.

Q. And these activities are intended to mitigate storm damage and quicken any restoration of service; is that right?

A. I think that's a fair characterization, yes, ma'am.

Q. Do you know how much Gulf is requesting in its rate increase that falls in the category of storm hardening?

A. I do not know the specific number, no, ma'am.

Q. Which witness would know that?

A. Mr. Teel, again, and Mr. McMillan would know.

Q. I read your introductory remarks in your testimony. And you've been the president of Gulf just since the beginning of 2011; is that right?

A. Yes, ma'am, since January 1st.

Q. Okay. Where were you based before that? Were you in Florida, or were you outside of Florida?

A. No, ma'am. I was in Birmingham, Alabama.

Q. But it would be fair to say you are aware, are you not, of the impact that, for example, the BP oil spill and the economic downturn had on Gulf's customers?

A. I've certainly learned of it since I've been in Florida, yes, ma'am.

Q. Would you also agree that many businesses in the Gulf service territory were lost, downsized, people were laid off as a result of those two events?

A. I would, yes, ma'am.

Q. Now, on page 10 of your testimony, beginning at line 9, you talk about your focus or Gulf's focus on providing value to its customers and how maintaining and improving value of service is among the highest priorities of everyone at Gulf; correct?

A. That is correct.

Q. Would you include in the value of service context the ability to provide competitive rates to your customers?

A. It is certainly something that I'm concerned about, yes, ma'am.

Q. And would you agree that Gulf's industrial rates are among perhaps the highest in the Southeast region, if not the highest, among the highest?

A. I really haven't seen a study on the level. I will concede they're higher than I want them to be.

MS. KAUFMAN: Okay. I have an exhibit that I would like to pass out if that would be all right. Mr. Chairman, this exhibit does not need a number. It is already -- or I guess it will be entered into the record as part of Mr. Pollock's exhibits.

BY MS. KAUFMAN:

Q. If you wouldn't mind taking a moment to look at this while Mr. Wright is distributing the document. And as I just said to Chairman Graham, this is a stipulated exhibit that was attached to FIPUG's witness, Mr. Pollock's testimony. So would you agree with me now looking at this stipulated exhibit that, at least for the four periods that are represented in the exhibit, that Gulf has had higher or the highest or pretty high industrial rates compared to other electric utilities?

A. I would say that is what the survey shows, yes, ma'am.

Q. And I think you just said that the industrial

rates were of concern to you, and perhaps I can interpret that to mean that you're working on that issue, and we appreciate that.

Let me ask you if in the context of making industrial rates competitive you have -- Gulf has proposed a cost of service study at least directed toward partially addressing that issue.

A. Yes, ma'am. And let me answer it slightly broader maybe than what you just said. We are concerned about industrial customers and industrial rates, and there are several elements in our rate package that are designed to make industrial rates more competitive. We've modified several of our industrial rates to give them more applicability to customers, so maybe reduce the size level requirement so a smaller customer might be able to take advantage of the rate.

We've expanded the applicability of a rate rider called the Commercial/Industrial Service Rider that gives us the ability to work with business customers and to offer them some pricing options that might not be standard rates. The Commission has approved this rate. It's on file with the Commission. Our filing package will expand the applicability of that rate and make it easier for us to offer that to businesses.

Another thing that we did do I think was something I heard in some of the opening testimony -- or opening statements by the lawyers. We have proposed a rate design mechanism called a minimum distribution system. That system or that ratemaking approach can be described best by Mr. O'Sheasy, who is our witness. But the thrust of it is to try to align cost causation, as best we can, with rates. And that is in our testimony, and it's Mr. O'Sheasy who is the real expert on that.

Q. Thank you, Mr. Crosswhite. And do you think that the Commission's approval of that minimum distribution system methodology will help to make the industrial rates more competitive?

A. I think it would do that, yes, ma'am.

MS. KAUFMAN: That's all I have. Thank you, Commissioners.

MS. HELTON: Mr. Chairman, just to make sure that the record is clear, the exhibit that Ms. Kaufman passed out has been identified as Exhibit Number 30 on the Comprehensive Exhibit List.

MS. KAUFMAN: Thank you.

CROSS-EXAMINATION

BY MAJOR THOMPSON:

Q. Yes, sir. I just have a couple of questions

for you, sir.

A. Yes, Major.

Q. What do you do to monitor or review the operations of Gulf Power?

A. Could you repeat that, please? I couldn't hear you.

Q. Do you review something to know what's going on with Gulf Power?

A. Do I personally?

Q. Yes.

A. I'm afraid I'm not understanding -- I work at Gulf Power, so I'm there every day, so I see the people. Sure, I get financial reports periodically at a high level. I get operating reports periodically. I get a report every morning that tells me whether there's bad weather coming. I get reports every morning that tell me if there's a major outage somewhere and the status of that, so --

Q. Perfect. That's exactly what I was looking for.

A. Yes, sir.

Q. Did Gulf Power provide safe and adequate services in 2010?

A. Yes, sir, I believe we did.

Q. Did Gulf Power provide safe and adequate

services to date this year?

A. I believe we have, yes, sir.

MAJOR THOMPSON: Those are all my questions. Thank you, sir.

THE WITNESS: Thank you.

CHAIRMAN GRAHAM: Mr. Wright.

MR. WRIGHT: Thank you, Mr. Chairman.

CROSS-EXAMINATION

BY MR. WRIGHT:

Q. Good morning, Mr. Crosswhite.

A. Good morning.

Q. I just have a few questions for you today.

In your summary, you mentioned that your base rate charges have not increased since your last rate case. Do you know what has happened to your base rate revenues since your last rate case?

A. I do not know how much they've grown over time. I think Mr. Teel has a chart that shows some of that, but I don't have a specific number.

Q. Thank you. So I could ask Mr. Teel about that?

A. He would be better able to answer it than I would be.

Q. Great. Thank you.

Are you familiar with the history of Gulf's

rate cases over the last 30 years?

A. No, sir, I can't say that I am.

MR. WRIGHT: Mr. Chairman, in our brief I will be asking that the Commission take official recognition of a number your orders, and I'll articulate them for you here: 10557, 10963, 11498, 14030, 19 --

MR. STONE: Mr. Chairman, I'm sorry. Mr. Wright can read a lot faster than I can write. Could he slow down just a little bit so we can keep track of the numbers?

CHAIRMAN GRAHAM: Just slow down just a hair. He said he's going to put it in his brief at the end, so you'll see it again. But go ahead and just slow down just a little.

MR. WRIGHT: I'm happy to speak more slowly, Mr. Chairman. I was trying to respect our desire to get this over with.

CHAIRMAN GRAHAM: Go ahead.

MR. WRIGHT: Thank you. I'll be asking that the Commission take official recognition of your orders in Gulf's rates cases, beginning with its 1981 rate case, which was Docket 810136-EU. I'm just going to read the order numbers, and then I'll move on. 10557, 10963, 11498, 14030, 19185, 20969,

23536, 22681, 23573, 93-0771, 99-2131, and 02-0787.

Thank you, Mr. Chairman.

BY MR. WRIGHT:

Q. Mr. Crosswhite, I'm not going to belabor this by asking you about the revenues requested and granted by the Commission in every one of those cases, but will you accept that it is true that in the company's rate cases over the last 30 years that the company has never gotten the increase that it asked for?

A. I can't accept that. I don't want to prolong it, but I just don't know that to be the case.

Q. Okay. I'm sure you would agree that Gulf has continuously provided safe and reliable service during these last 30 years; correct?

A. Yes, sir.

Q. And I hope that you would agree that if the Commission were to grant Gulf a rate increase in this case of less than the $101,000,000 that you're asking for, the company would continue to provide safe and reliable service?

A. The commitment I will make is this: Regardless of whatever the Commission does, we will do our utmost to provide safe and adequate service to our customers. We will work very hard to do that.

By the same token, I want to be real clear

that we asked for what we thought we needed. We didn't pad it. Thank you.

CHAIRMAN GRAHAM: I didn't even see his eyes move.

BY MR. WRIGHT:

Q. It's your testimony that you need a before-tax rate of return on equity of over 19 percent to produce an after-tax return on equity of 11.7 percent?

A. Well, it's my testimony that we need a return of 11.7 percent. And I want to be real clear. I'm not a financial expert. I'm not a return on equity expert by any means. We relied on Dr. Vander Weide to develop that number for us and engaged him to do that, and that's the number that he provided to us as the required return.

Q. So you don't have -- do you have an independent opinion about that?

A. I don't think I have a basis to make an independent opinion. We hired him because he was the expert, and we asked him to provide information to us.

Q. Gulf is part of the Southern Company; correct?

A. Yes, sir. We're part of the Southern Electric System.

Q. And the equity capital that eventually flows to Gulf comes through the issuance of common stock by

Southern Company; is that correct?

A. The equity capital?

Q. Yes, sir.

A. To the extent we're not self -- to the extent we're not generating our own equity, yes, sir.

Q. Are you testifying that Southern Company would not be able to raise equity capital if you got an ROE of less than 11.7 percent in this case?

A. I don't know -- I don't know the impact of that.

Q. A couple more questions along the lines of those that Ms. Kaufman asked you relating to commercial rates. Would you agree, subject to check -- and I will tell you this is in one of the exhibits sponsored by our witness, Mr. Chriss -- that the company's average commercial revenue for 2010 fourth quarter was approximately 10.9 cents per kilowatt-hour?

A. Does he have an exhibit we could look at?

Q. Yes.

A. Okay.

Q. Do you want to see it?

A. Yes, if you don't mind.

Q. I don't.

A. Back in my dark, distant past when I was an attorney, the "subject to check" words always scared me

to death.

Okay.

Q. I'll just ask you one question.

A. Yes, sir.

Q. Is that 10.9 cents a kilowatt-hour higher than you want it to be?

A. Yes, sir.

MR. WRIGHT: That's all I have. Thank you Mr. Chairman.

CHAIRMAN GRAHAM: Staff?

MS. BARRERA: We have no questions for this witness.

CHAIRMAN GRAHAM: Okay. Commissioners. Commissioner Brisé.

COMMISSIONER BRISÉ: Thank you, Mr. Chairman.

Thank you, Mr. Crosswhite, for your testimony this morning. I have two questions. One, were you present at the customer hearings?

THE WITNESS: Yes, sir, I was present at the customer hearings.

COMMISSIONER BRISÉ: And being the chief executive officer of Gulf Power here in Florida, what is your response or how do you address the many issues that were brought up by customers and the concerns that they had with respect to this

rate case?

THE WITNESS: Yes, sir. Well, we've talked several times in my testimony, and I think you'll hear other Gulf Power witnesses say similar things. But we try to keep the customer at the center of everything we do. We focus on the customer. We believe that the key to success is good customer service and customer satisfaction. And you'll hear a lot about that, I believe, when Mr. Jacob takes the stand, and Ms. Neyman.

So I was pleased by some of the things I heard at the hearings that we had. And I was there, and I know you all were there. We had about 40 people speak in Panama City and about 40 people speak in Pensacola. Of those that spoke, I heard very few actually raise concerns going to service quality. There was a lot of concern expressed about the financial condition of the state, personal finances, and I'm empathetic to that.

I am pleased that they didn't say our quality of service is bad. I heard nothing but good -- well, mostly good things, overwhelmingly good things about the quality of service. We are very concerned about the price, and we're very concerned about the customers' ability to pay.

At the hearing, we tried to reach out -- if y'all recall, we had a number of customer service representatives there, and a number of our customers who were there came and spoke to those customer service representatives and tried to get some help for their issues.

We have sent a letter to the Commission outlining the steps that we took, the customers we met with at the time and what we did to help them with their concerns. A lot of times it was things like making sure that they had energy audits, you know, how can we make sure you're getting the most for what you're paying for. We looked at in some cases maybe some low-income assistance to do some things. We did a number of things like that with those customers, and that's all detailed in the report.

Following the report, we also sent a follow-up letter to everybody we were actually able to speak with to confirm that they would provide what they needed. And we also sent a letter to everybody who attended, who spoke at the hearing. Everybody where we had their address, we sent them a letter asking them to contact us if there's anything we could do to help them with the issues they raised.

So we did reach out and try to solve those customers' concerns, and in some cases we were able to do so, and in some cases we've not heard back from the customers.

COMMISSIONER BRISÉ: Maybe one or two follow-ups. So then what do you say to the argument -- and I understand that Gulf hasn't been here for a rate case in the last 10 years, but what do you say to the argument that considering the economic situation and all of those things, that Gulf is providing adequate, reliable service right now? Why is it necessary for Gulf to come and ask for a rate increase now, considering what was expressed by the customers at the rate hearings?

THE WITNESS: Yes, sir. Well, we are providing adequate service right now. I am concerned about our ability to continue providing reliable service without this rate case. Without this relief, I questions about how long we'll be able to do that.

When we talk about our finances and how we've performed, I think it's important for us to note that we have earned below the Commission's authorized range of return for these base revenues or these base rates since the middle of 2010. So

since the middle of 2010, we have been earning below the return level that this Commission has said was appropriate for us. So we've been at that level for 18 months now, and it will probably be several more months before we have an order in this case. So we're looking at almost two years, I would say, of us earning below the allowed return.

With that, I'm not sure how long we will be able to continue providing the kind of service that we want to provide to our customers.

COMMISSIONER BRISÉ: Thank you. That's all the questions I have for now.

CHAIRMAN GRAHAM: Commissioner Balbis.

COMMISSIONER BALBIS: Thank you, Mr. Chairman, and thank you, Mr. Crosswhite, for testifying today.

THE WITNESS: Yes, sir.

COMMISSIONER BALBIS: As you indicated, we were all at those customer meetings, and I did hear the same remarks that you mentioned, a lot of positive remarks about quality of service, a lot of positive remarks about your employees being a member of the community, et cetera, which I thought was a good thing.

And on top of that, there was a lot of

discussion by the customers that testified about the hardships they're facing financially, and it's another -- it was a good reminder, a sobering reminder of the state of the economy, especially in Gulf's service territory. And so myself and the other Commissioners did hear that, and we are going to look closely at your application and look at what is appropriate.

I have a few questions for -- maybe not for you. I definitely have one for you, but for other Gulf witnesses. I'm going to save my questions about the additional personnel you're asking for, the plant held for future use, the property held for future use.

My question for you is concerning storm accrual. To your knowledge, in '04 and '05 when Gulf Power may have used a surcharge in order to recover the cost to repair, was there a cash flow situation or any other difficulties that Gulf Power encountered in using a surcharge versus an accrual?

THE WITNESS: I think that would be one I would ask you to also defer to Mr. Teel. He's the CFO, and he would have a much better handle on the cash flow situation in 2004 and '5, Commissioner.

COMMISSIONER BALBIS: Okay. And have you had

the opportunity to thank whoever elected you as president that they did it right when you were about to start a rate case?

THE WITNESS: I am very thankful to be here, actually. Regardless of the circumstances, you know, Northwest Florida is paradise on earth, and those of us who get to live here just absolutely love it. So they know I'm very grateful for being here.

COMMISSIONER BALBIS: Thank you. I have nothing further.

CHAIRMAN GRAHAM: Commissioner Edgar.

COMMISSIONER EDGAR: Thank you.

Good morning.

THE WITNESS: Good morning.

COMMISSIONER EDGAR: As you have pointed out, at the customer service hearings that we held and that we all attended, we did hear a number of positive comments about service and service quality. There were a few complaints, and I understand that you have worked to respond to those. But one of the themes that we seemed to hear was, you know, this is just bad timing. And I believe you when you say that you empathize with that sentiment, as do we all.

A question that was posed to us by a customer that I'm now going to pose to you is, with that in mind, what has Gulf done to reduce costs?

THE WITNESS: What have we done to reduce costs? Well, one thing we did -- and I'm repeating myself a bit, but we did earn less than our return, and we're still doing that, allowed return, for 18 months to two years. I mention that because I want to let you all know I think we're sharing the pain of the economy. We understand people are having a hard time, and so we're trying to -- we've tried to push this case off as long as we could, and we bore part of that pain. So that's one thing.

Other things we've done, we've discussed purchasing power when it's less expensive than us building something. That one instance that we referenced in my testimony, the Central Alabama purchased power agreement, saved over half a billion dollars for our customers. Now, we're always going to try to do the least expensive option to supply our customers, but that's one concrete example I would say was a major, major issue.

Other things that we have done would be the installation of the AMI meters. You'll hear

discussion of that, I believe, automated metering infrastructure. And that is an automated meter that allows us to take meter readers off the road and allows that information to be transmitted back without having to have people manually there.

We've taken steps to extend the depreciation lives of generating units, which stretches out their lives and produces lower costs.

We've worked on maintenance cycles to extend those where we could. We've been more efficient in the way we do outages. I mean, there's any number of things, and I would love for you to ask that question for each of the substantive areas of the company, generation and distribution and transmission, because they've done a lot, and they will be able to catalog it much better than I can.

COMMISSIONER EDGAR: Thank you.

THE WITNESS: Yes, ma'am.

CHAIRMAN GRAHAM: Redirect?

MR. STONE: If I may, may I have permission to hand a calculator and a document to the witness? And Mr. Guyton will distribute the document to the Commissioners and the parties if we have permission.

CHAIRMAN GRAHAM: I think he's got a

calculator up there, but if you have one.

MR. STONE: The document I'm handing out, I would like to identity as an exhibit, if we may. This is the letter that Mr. Crosswhite referred to during his cross-examination.

CHAIRMAN GRAHAM: We will label this as Exhibit --

MS. KLANCKE: I believe we're at 171.

CHAIRMAN GRAHAM: 170.

MS. KLANCKE: 170.

(Exhibit Number 170 was marked for identification.)

REDIRECT EXAMINATION

BY MR. STONE:

Q. Mr. Crosswhite, have you been handed a letter dated October 7, 2001, to Ms. Ann Cole, Commission Clerk, with the reference "Follow-up to Service Hearings, Docket No. 110138-EI"?

A. Yes, sir.

Q. Is this the letter to which you were referring during your cross-examination?

A. It is.

MR. STONE: This has been identified as Exhibit 170, and we would move it into evidence.

CHAIRMAN GRAHAM: A short title is letter to

Ann Cole dated October 7, 2011.

MR. STONE: The short title could be "Service Hearing Response" if you would like.

CHAIRMAN GRAHAM: One more time.

MR. STONE: "Service Hearing Response."

I have just a couple more redirect questions, Mr. Chairman.

CHAIRMAN GRAHAM: Okay.

BY MR. STONE:

Q. Mr. Crosswhite, do you still have with you the exhibit that was handed out, Exhibit Number 115?

A. Yes.

Q. First, let me be clear. You had no part in the production of this response; is that correct?

A. That is correct.

Q. Now, if you'll bear with me, do you have a calculator with you?

A. I have one now.

Q. When you were asked on cross-examination, you were asked about the discretionary accruals that were made as referenced on the page for the year 2001, the year for 2003, the year for 2004, the year for 2005, the year for 2006. Do you recall being asked that?

A. I do.

Q. You have your calculator with you. Could you

total those annual discretionary accruals?

A. 1 million in 2001, 7.1 million in '3, 15 million in '4, 6 million in '5, 3 million in '6, nothing in '7, nothing in '8, nothing in '9, and nothing '10.

Q. And when you totaled those, did you get approximately $31.1 million?

A. I had 32, but I'm history major with a calculator, so that's dangerous.

Q. Your lawyer math is probably better than my lawyer math.

You mentioned that there was no discretionary accrual in the years after 2006.

A. That's correct.

Q. In the years 2007, 2008, and 2009, do you see the column that's labeled "Storm Surcharge Credits"?

A. Yes.

Q. Could you take the totals for each of those years and add those up?

A. So starting in '7?

Q. Yes, please.

A. 18,480,906. Can we leave off the change?

Q. Certainly.

A. Plus 26,142,734. That's for '8. For '9, 10,746,277. And that's where it stops, I believe.

Q. And the total of those three years?

A. 55,369,917, so $55,369,917.

Q. And is it your understanding that that $55.3 million is money that was collected from Gulf's customers through a surcharge approved by this Commission?

A. Yes.

Q. And that $32.1 million is money that was by discretion added to the storm reserve by the company on a voluntary basis based on the authorization of this Commission?

A. According to the exhibit, there's an asterisk that said for each discretionary accrual per PSC order, and I'll leave off the reference number, Gulf has discretionary authority to increase the annual accrual above 3 1/2 million.

Q. Mr. Crosswhite, absent the $32 million that was added to the reserve, would the customers have been asked to fund that $32 million by prolonging the surcharge that resulted in $55.3 million?

A. Yes.

MR. STONE: Thank you. I have no further questions.

CHAIRMAN GRAHAM: Any exhibits to enter for this witness?

MR. STONE: We would move Exhibit 170, the service hearing follow-up.

CHAIRMAN GRAHAM: We'll move Exhibit 170.

(Exhibit Number 170 was admitted into the record.)

CHAIRMAN GRAHAM: Anything else?

MS. KLANCKE: Staff has no additional exhibits with respect to this witness.

CHAIRMAN GRAHAM: Okay. Mr. Crosswhite, thank you very much.

THE WITNESS: Thank you, sir.

CHAIRMAN GRAHAM: Mr. Stone, your next witness?

MR. STONE: The next witness in the order as set forth in the Prehearing Order is Mr. Bob McGee, Robert L. McGee. His testimony has been stipulated, and so we would ask that his testimony be inserted into the record as though read.

CHAIRMAN GRAHAM: We will enter Mr. McGee's testimony into the record.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
Robert L. McGee
Docket No. 110138-EI
In Support of Rate Relief
Date of Filing: July 8, 2011

Q. Please state your name and business address.

A. My name is Bob McGee. My business address is One Energy Place, Pensacola Florida, 32520.

Q By whom are you employed?

A. I am employed by Gulf Power Company (Gulf or the Company). I serve as Gulf's Manager of Market Research and Planning.

Q. What are your responsibilities as Gulf's Manager of Market Research and Planning?

A. As Manager of Market Research and Planning, I am responsible for forecasting, load research, Energy Conservation Cost Recovery (ECCR) filings, economic evaluations, pricing, customer research, market research, technology research and customer-sited renewables.

Q. Please state your prior work experience and responsibilities.

A. I began my career in 1984 as a research engineer with Harry Diamond Laboratories, now part of the Army Research Lab, investigating missile fuzing techniques and digital signal processors. Subsequently, I served eight years in the United States Navy as an F-14 Naval Flight Officer,

ultimately serving in combat during Desert Storm in 1991. I joined Gulf in 1994 as a Market Analyst working on the forecast, load research, Real Time Pricing (RTP) and customized metering projects. I have served as a field sales representative to large industrial customers, assistant to a previous Power Generation Vice President, Supervisor of the Instrument & Control team at Plant Crist, and Operations Supervisor at Plant Crist. I have been in my current role since 2001.

Q. What is your educational background?

A. I received a Bachelor of Science degree in Electrical Engineering from the University of Maryland at College Park in 1984. In 1993, I received a Master's degree in Business Administration from the University of West Florida.

Q. What are the purposes of your testimony?

A. My testimony presents Gulf's forecast methodologies and forecast results for customers, energy sales, peak demands and base rate revenues. The forecast is provided to Corporate Planning for use in the budgeting and planning process as discussed by Gulf Witness Buck. My testimony also addresses the load research performed by Gulf and used in this proceeding.

Q. Are you sponsoring any exhibits?

A. Yes, I am sponsoring Exhibit RLM-1, Schedules 1 through 4. Exhibit RLM-1 was prepared under my direction and control, and the information

contained therein is true and correct to the best of my knowledge and belief.

Q. Are you sponsoring any of the Minimum Filing Requirements (MFRs) filed by Gulf?

A. Yes. The MFRs I sponsor or co-sponsor are listed in Schedule 1 of my exhibit. The information contained in the MFRs I sponsor or co-sponsor is true and correct to the best of my knowledge and belief.

Q. How are you familiar with Gulf's forecast process?

A. For most of my career at Gulf, I have been involved in developing Gulf's forecasts. As a forecaster at Gulf in the mid-1990s, I assisted the lead forecaster in developing all aspects of the forecast. I was particularly involved in the forecast of customers, outdoor lighting energy and wholesale energy. For the past ten years, I have been the manager of the department responsible for the forecast. In this role, I direct and review the forecast each year as it is developed from beginning to end, provide guidance to the forecast team at important decision points, direct forecast-related analyses and process improvements, brief executive management on forecast development progress, and oversee workflow and staffing.

I. OVERVIEW

Q. Please describe the economic conditions and outlook for Gulf's service area.

A. Gulf's retail service area covers eight counties in Northwest Florida: Bay, Escambia, Holmes, Jackson, Okaloosa, Santa Rosa, Walton, and Washington. Our service area encompasses three Metropolitan Statistical Areas (MSAs): Pensacola-Ferry Pass-Brent, Crestview-Fort Walton Beach-Destin, and Panama City-Lynn Haven-Panama City Beach.

Like the rest of the country and state, Gulf's service area experienced the effects of the most recent nation-wide recession. Often referred to as the "Great Recession," this was the worst national economic and financial crisis since the Great Depression of the 1930s. According to the National Bureau of Economic Research, the official source for declaring when recessions begin and end, this most recent recession began in December 2007 and ended in June 2009. However, the effects of the Great Recession were felt in Gulf's service area well before the nation-wide downturn and have lingered beyond the official end date of the national recession. A number of economic indicators for Gulf's service area, namely income, employment, housing starts and population, were in decline at the end of 2006 or beginning of 2007 and either continued to decline or leveled off at a low point through 2008, 2009 and 2010. As it is used in my testimony hereafter, the term "Great Recession" will refer to the four year period 2007 through 2010. One result of the recent

economic downturn in Gulf's service area was a decline in average kilowatt hour (kWh) use per residential customer. This historical fact was observed by Gulf, factored into the forecast, and projected to turn around as the economy was projected to recover.

The Deepwater Horizon oil spill in the Gulf of Mexico (April 20, 2010 through July 15, 2010) had some impact on Gulf's local economy, mostly affecting tourism and recreation from May through August 2010. Gulf assumed in its forecast that the Deepwater Horizon oil spill would not affect energy sales in future years.

Gulf projects that the economy in our service area will begin recovery in 2011, and continue until the economic indicators discussed earlier either return to or exceed pre-recession levels by the end of 2012. Overall, Gulf's forecast relies on relatively optimistic economic projections in the near term.

Q. Please provide an overview of Gulf's forecast methodology.

A. Each year, Gulf produces a new forecast. Gulf starts with a projection of the number of new non-lighting customers it expects to add in each customer class – residential, commercial and industrial. Next, Gulf estimates how much energy these customers will use under normal weather conditions. For customers on demand rates, Gulf then estimates monthly billing demands. Finally, the customer (base) charge, energy charge, and demand charge from the appropriate rate schedules are

applied to the number of customers, monthly energy and monthly billing demands to estimate future base rate revenues. Outdoor lighting customers, energy and revenue are projected by rate and class. Gulf also forecasts total company peak demand using total energy projections and historical relationships between energy and demand. This same methodology has been used by Gulf to develop the forecast since I joined the Company seventeen years ago. Refinements in the methodology have been made over those years as will be described in my testimony below, but the fundamental methods have remained unchanged and continue to produce reliable forecasts.

Q Has the previously described forecast methodology for customers, energy, peak demand and revenue been used by Gulf in its regular course of business?

A. Yes. Gulf produces a forecast annually using this same methodology. The annual forecast is routinely utilized for business planning and operations. This forecast of customers, energy and revenue is used by the Company for financial planning, budgeting, distribution planning and transmission planning. The forecast of peak demand and energy is utilized by the Company for generation planning, fuel procurement planning and transmission planning.

Q. Has the previously described forecast methodology for customers, energy, peak demand and revenue been used by Gulf in other proceedings or

filings where the Florida Public Service Commission (FPSC or the Commission) has accepted, approved or relied upon Gulf's forecast?

A. Yes. This forecast methodology has been used by the Company over the years for various purposes including: Ten Year Site Plan filings; need determination proceedings; Renewable Standard Offer Contract filings; annual cost recovery filings for Gulf's fuel, purchased power, environmental and conservation cost recovery clauses; and previous rate proceedings.

II. GULF'S CUSTOMER FORECAST

Q. What are the 2012 results of Gulf's customer forecast?

A. Gulf projects that it will have a total of 438,278 retail customers by December 2012, an increase of 5,094 customers over projections for December 2011. This represents an anticipated annual growth rate of 1.2 percent for the test year. By comparison, historical growth rates of 2.1 percent, 0.1 percent, 0.1 percent and 0.6 percent were experienced in 2007, 2008, 2009 and 2010, respectively. Current projections for year-end 2011 indicate an annual growth rate of 0.6 percent.

Q. How many new retail customers will Gulf have added between the last base rate proceeding and the end of the test year?

A. By the end of the test year, Gulf will have added 49,438 retail customers to its system in the nearly ten years since our last base rate proceeding,

representing a cumulative growth of 12.8 percent, which yields a 1.26 percent compound annual growth rate (CAGR) over that period.

Q. How were Gulf's forecasts of customers and customer growth for 2011 and 2012 developed?

A. The short-term forecasts of residential, commercial and industrial non-lighting customers were based primarily on input from Gulf's field Energy Sales and Efficiency Managers with the assistance of their field employees. These field managers and their employees have frequent and consistent interaction with our customers as part of their daily job tasks. The three managers' combined direct experience with Gulf's customers and markets exceeds three quarters of a century. The projections prepared by these managers reflect recent historical trends in net customer gains as well as anticipated effects of changes in the local economy, the real estate market, planned construction projects, and factors affecting population such as military personnel movements and changes in local industrial production.

Forecasters supplied field managers with historical customer gains by rate schedule and summary economic outlooks for the appropriate MSA. After collecting initial input from field managers, forecasters reviewed the one-year-out customer projections by rate schedule, checking for consistency with historical trends, consistency with economic outlooks, and consistency across MSAs. Forecasters then supplied field managers with draft second-year-out customer projections based on number of

households which the field managers reviewed and modified as necessary. In this iterative process, forecasters challenged and field managers defended the projections until all were satisfied that the projections reflected an unbiased, most-likely estimate.

The strength of the near-term customer projection methodology, which Gulf has employed for more than 30 years, is that information is gathered at a local level and built up to the whole. Because Gulf is a relatively small company, it can manage such a localized process without needing to rely primarily on macro-economic projections to estimate residential and commercial customer growth in the near term.

Gulf projected the number of outdoor lighting customers by rate and class based on historical growth rates. Forecasters reviewed historical outdoor lighting data with Gulf's lighting team to gain insight into future trends before finalizing outdoor lighting growth rate projections.

Q. Is this the same forecast methodology for customers and customer growth that Gulf used and the Commission accepted in Gulf's last base rate proceeding?

A. Yes, with one minor exception. Gulf previously projected outdoor lighting customers by fixture type, rate and class, which resulted in over 150 separate forecasts of outdoor lighting fixtures. Several years ago, Gulf consolidated fixture types by lumen output, reducing the number of separate outdoor lighting forecasts to 56. Gulf further simplified the

process in 2010 by reducing the number of separate outdoor lighting forecasts to seven – one for each rate and class. These refinements saved time and had no significant impact on forecast accuracy.

Q. Has this forecast methodology provided reliable forecasts of customers in the past?

A. Yes. Over the four years prior to the recession, Gulf minimally over-forecast the residential customer count one year out and two years out by 0.5 percent and 0.4 percent, respectively. (Over-forecast means Gulf forecast more customers than we actually gained over that time period). During the Great Recession, Gulf slightly over-forecast the residential customer count one year out and two years out by 1.0 percent and 2.4 percent, respectively.

The commercial class is smaller and more diverse than the residential class, which makes projections more difficult. During the four years prior to the recession Gulf minimally over-forecast the commercial customer count one year out and two years out by 0.9 percent and 1.0 percent, respectively. During the Great Recession, Gulf slightly over-forecast the commercial customer count one year out and two years out by 1.8 percent and 4.7 percent, respectively.

This forecast methodology, which relies on the experience and knowledge of our field managers and their employees, has produced reliable, accurate results, even during the recent recession.

Q. How accurate have the residential and commercial customer forecasts which have been proposed for use in this proceeding been?

A. Over the twelve months of the forecast period for which we have actual data to compare to the forecast (June 2010 through May 2011), residential customers were minimally under-forecast by 0.1 percent and commercial customers were minimally over-forecast by 0.6 percent.

III. GULF'S ENERGY SALES FORECAST

Q. What are the 2012 results of Gulf's retail energy sales forecast?

A. Retail energy sales are expected to total 11,768,265 megawatt hours in the test year, representing an increase of 3.0 percent over projections for the twelve months ending in December 2011. This healthy growth is consistent with the relatively optimistic economic projections Gulf incorporated in this forecast as discussed in the Overview section of my testimony.

The retail megawatt hour (MWH) sales forecast by class consists of the following:

Residential: 5,633,215 MWH, comprising 47.9 percent;
Commercial: 4,083,041 MWH, comprising 34.7 percent;
Industrial: 2,023,502 MWH, comprising 17.2 percent; and
Street Lighting: 28,507 MWH, comprising 0.2 percent.

Q. Please provide a brief overview of the methodology Gulf used to develop its retail energy sales forecast.

A. Gulf used three multiple linear regression models to estimate residential and commercial non-lighting energy sales, one for residential and two for commercial. For forecasting purposes, the commercial class was split into two groups - small and large. Each regression model estimated energy use per customer per day on a billing cycle basis. Multiplying by the appropriate number of billing cycle days in a month and the number of customers produced total energy. The impacts of demand-side management (DSM) efforts and electric vehicle (EV) charging were then accounted for. The resulting energy projection was then adjusted for unbilled sales to yield calendar month projections. As is standard industry practice, Gulf's residential and commercial energy forecasts assumed normal weather conditions for future projections. Likewise, forecast accuracy calculations compared these normal weather forecasts of energy sales to weather-normalized actual energy sales.

The forecast of sales to small industrial customers was produced in a similar manner using historical growth rates rather than a regression model. Projections of sales to the largest industrial customers were based on field surveys. Outdoor lighting energy sales were projected by rate and class using historical growth rates. My testimony below further describes Gulf's retail energy sales forecast methodology.

Q. How was Gulf's forecast of 2012 residential energy sales developed?

A. The short term non-lighting residential energy sales forecast was developed using a multiple linear regression model.

Q. What variables were employed by Gulf in the regression model used to develop the residential energy sales forecast?

A. The dependent variable, the quantity being estimated, in the residential energy regression equation was monthly billing cycle energy per customer per billing day. The regression included a constant term and 20 years of historical data for the following variables: billing cycle residential cooling degree hours per billing day for the months April through November; billing cycle residential heating degree hours per billing day for the months November through April; indicator variables (also called binary variables) to capture seasonal variations for the months January, July and August; twelve month moving average of real residential price; real disposable income per household; and residential vacancy rate (also called housing stock vacancy rate). Also included in the model were an indicator variable for the month of September 2004 to account for the impact of Hurricane Ivan, one autoregressive term lagged one month to address first-order residual autocorrelation over time and one indicator variable for the combined months of June 2008, July 2008, and August 2008 to address residuals in those months. These variables were carefully chosen to make the model both simple and statistically robust. Variables were required to have a logical connection to residential electricity sales, substantial data history, dependable projections of future values, limited

overlap with other variables (i.e. limited multicollinearity), and good statistical significance (i.e. low p-value).

Page 1 of Schedule 2 of my exhibit is a graph comparing the residential regression model's predicted values with actual historical data. It shows how well the model's output "fits" history. Page 2 of Schedule 2 of my exhibit is a list of statistics associated with the residential regression model.

Q. Please describe the primary statistical tests Gulf used to evaluate each regression model for reasonableness?

A. Time series multiple linear regression models and their components are typically evaluated for reasonableness using the following statistics: p-value, adjusted R-squared, and the Durbin-Watson d-statistic. Standard statistical software packages routinely provide these statistics as part of their output.

A p-value is computed for each independent variable in a regression model indicating the level of statistical significance of that variable. The p-value ranges from 0 to 100 percent. A low p-value indicates a desired result, meaning that the variable is statistically significant.

An adjusted R-squared value, also called a "goodness of fit" test, is calculated for each regression model. A model is considered a "good fit" if its adjusted R-squared is high. R-squared values range from 0 to 100

percent. A regression model that fits the historical data perfectly would have an R-squared value of 100 percent.

The Durbin-Watson d-statistic is calculated for each regression model. The calculation results in a number ranging in value between zero and four. A d-statistic value near two indicates a desired result and implies no autocorrelation in the regression model residuals, i.e. residuals in one time period are not related to residuals in the previous time period.

Q. What statistical results did Gulf attain with the residential regression model?

A. As presented on page 2 of Schedule 2 of my exhibit, all variables used in the residential regression model were statistically significant (p-values were less than 5 percent) and each coefficient had the expected sign. The model's adjusted R-squared was 98.5 percent, indicating that all but 1.5 percent of the variance in the historical data was explained by the model. The model's Durbin-Watson d-statistic was 2.01, indicating no autocorrelation in the residuals. Overall, these are excellent statistical results.

Q. What data sources were employed for the economic variables used in Gulf's residential regression model?

A. Historical values and forecast projections of the economic variables "real disposable income per household," "residential vacancy rate," and "GDP price deflator" were purchased from Moody's Analytics, formerly known as

Moody's Economy.com, a well respected economic forecasting firm which has supplied data to Gulf for over 15 years. Gulf used the May 2010 vintage of Moody's economic projections, which was the most recent data available at the time the forecast was developed.

Q. How was the number of cycle billing days per month determined?

A. Gulf's customers are divided among 21 bill groups. Each bill group has a different scheduled read date, which varies from month to month and is staggered from bill group to bill group. Monthly cycle billing days were calculated as follows. For a given month, the number of billing days in a bill group was the sum of the days from the day after the prior month's scheduled read date through the current month's scheduled read date. These summed days for each of the 21 bill groups were then totaled and divided by 21 to get the month's cycle billing days.

Q. How was historical residential weather calculated?

A. Cooling and heating degree hours were calculated using the National Oceanic and Atmospheric Administration's (NOAA) Pensacola weather station's hourly temperatures. Residential cooling degree hours are the result of taking the number of degrees Fahrenheit that each hourly temperature is above a 70 degree baseline, and summing over a given time period. Residential heating degree hours are the result of taking the number of degrees Fahrenheit that each hourly temperature is below a 65 degree baseline, and summing over a given time period. These residential cooling and heating degree hour temperature baselines reflect

the observed correlation between hourly temperatures and hourly energy purchases by Gulf's residential customers.

Monthly billing cycle residential weather was calculated as follows. For each bill group, the total residential cooling (heating) degree hours were summed over the period from the day after the prior month's scheduled read date through the current month's scheduled read date. These summed residential cooling (heating) degree hours for each of the 21 bill groups were then totaled and divided by 21 to get the monthly billing cycle residential cooling (heating) degree hours.

Q. Given the strong dependence of residential energy use on weather, what weather forecast was used in the residential energy projection?

A. As is standard practice in the industry, Gulf used "normal" weather in its energy forecasts, where "normal" is defined as a long-term average of historical weather. Monthly normal weather for the residential class was developed using historical monthly cycle residential cooling (heating) degree hours per billing day averaged by month over the past 20 years. Gulf had previously used a Typical Meteorological Year (TMY) to develop residential class normal weather but switched two years ago to this 20-year average in order to simplify the process of updating Gulf's normal weather.

Q. How was the residential regression model output used to develop the residential energy forecast?

A. The residential regression model output, monthly billing cycle energy per customer per billing day, was multiplied by the projected number of non-lighting residential customers and projected cycle billing days by month. The residential class outdoor lighting energy projection was then added to produce the total residential class energy projection. The total residential class energy projection was then adjusted to reflect the anticipated impacts of Gulf's DSM plan and the introduction of electric vehicles to the market. A projection of unbilled energy was then added to the resulting billed energy projection to develop a calendar month projection of total residential class energy. Residential energy sales by rate were developed using average historical use per customer by rate.

Q. What DSM plan assumptions were included in Gulf's forecast?

A. Gulf utilized the DSM plan filed on March 30, 2010 and revised on June 14, 2010 in Docket No. 100154-EG to adjust forecast sales and annual system peak demand for projected conservation impacts. Because the DSM plan was pending approval at the time the forecast was developed, energy reductions initially planned for 2010 were assumed to occur in 2011 in the forecast. In years 2012 and following, the forecast reflects energy reductions as filed in the June 14, 2010 revised DSM plan.

Q. Please address the anticipated impacts of Gulf's DSM plan on the residential energy forecast.

A. The anticipated impacts of Gulf's DSM plan to the residential class were projected to be 67 million kWh in the test year. The forecast reflects all

expected impacts of the DSM plan – some of those impacts were embedded in the regression model output and some of those impacts were included through an exogenous adjustment to the regression model output. Gulf utilized data from ITRON (the vendor used by parties in the DSM goals docket to develop technical and achievable potential levels of DSM for Gulf and other utilities) as well as Gulf's experience in the energy efficiency market and knowledge of existing programs to determine, by program, the amount of energy savings embedded in the historical regression data. The remaining impacts, those not embedded in the historical data, formed the exogenous DSM adjustment. The exogenous DSM adjustment to residential class energy in the test year was 50 million kWh, which reduced total retail energy sales by 0.4 percent.

Q. How did Gulf project the impact of electric vehicles in its residential energy forecast?

A. Gulf assumed an electric and plug-in-hybrid electric vehicle penetration of 5 percent of new vehicle sales in the test year, resulting in an exogenous adjustment for charging electric vehicles of 8 million kWh in the test year. The penetration rate assumption was based on the July 2007 joint study performed by the Electric Power Research Institute (EPRI) and the Natural Resources Defense Council (NRDC). All charging was assumed to occur off-peak in the residential class. As customer behavior patterns emerge in the electric vehicle charging market, Gulf will refine this estimate based on load research and customer surveys. Gulf has implemented a pilot program through the recently approved DSM plan that will encourage

customers who purchase electric vehicles to charge them during off-peak hours.

Q. How was Gulf's forecast of 2012 commercial energy sales developed?

A. The short-term non-lighting commercial energy sales forecast was developed using two multiple linear regression models. One modeled "small commercial" customer energy purchases (less than 20 kilowatts (kW)), and the other modeled energy purchases of the remainder of the commercial class, the latter being referred to as "large commercial." Both models were similar in specification.

Q. What variables were employed by Gulf in the two regression models used to develop the commercial energy sales forecast?

A. In each commercial regression model the dependent variable, the quantity being estimated, was monthly billing cycle energy per customer per billing day. Each regression included a constant term and 20 years of historical data for the following variables: billing cycle commercial cooling degree hours per billing day for the months April through November; billing cycle commercial heating degree hours per billing day for the months December through March; twelve month moving average of real commercial price; and non-manufacturing employment. Also included in both models was an indicator variable for the month of September 2004 to account for the impact of Hurricane Ivan. The small commercial model included one autoregressive term lagged one month to address first-order residual autocorrelation over time. The large commercial model included indicator

variables to capture seasonal variations for the months January and May as well as one indicator variable for the combined months of July 2005, August 2005 and September 2005 to account for the impacts of Hurricanes Dennis and Katrina. These variables were carefully chosen to make the commercial models both simple and statistically robust. Variables were required to have a logical connection to commercial electricity sales, substantial data history, dependable projections of future values, limited overlap with other variables (i.e. limited multicollinearity), and good statistical significance (i.e. low p-value).

Page 1 of Schedule 3 of my exhibit is a graph comparing the small commercial regression model's predicted values with actual historical data. It shows how well the model's output "fits" history. Page 2 of Schedule 3 of my exhibit is a list of statistics associated with the small commercial regression model.

Page 1 of Schedule 4 of my exhibit is a graph comparing the large commercial regression model's predicted values with actual historical data. It shows how well the model's output "fits" history. Page 2 of Schedule 4 of my exhibit is a list of statistics associated with the large commercial regression model.

Q. Why do all three regression models use a variable to account for Hurricane Ivan, but only the large commercial model requires a variable to account for Hurricanes Dennis and Katrina?

A. Hurricanes Dennis and Katrina caused significantly fewer outages in Gulf's service area than Hurricane Ivan, so they had a smaller impact on residential and small commercial customers. Dennis and Katrina did, however, have a larger impact on tourism than Ivan primarily because they made landfall earlier in the tourist season (July and August versus September). Dennis and Katrina also caused gasoline prices to rise to a new high, which further impacted tourism in 2005. Since a majority of Gulf's tourism and recreation kWh sales are to large commercial businesses, a Dennis-Katrina indicator variable appropriately fit the large commercial regression model but was not needed in the residential or small commercial regression model.

Q. What statistical results did Gulf attain with the small commercial regression model?

A. As presented on page 2 of Schedule 3 of my exhibit, all variables used in the small commercial regression model were statistically significant (p-values were less than 5 percent) and each coefficient had the expected sign. The model's adjusted R-squared was 94.1 percent, indicating that all but 5.9 percent of the variance in the historical data was explained by the model. The model's Durbin-Watson d-statistic was 2.29, indicating no significant autocorrelation in the residuals. Overall, these are excellent statistical results.

Q. What statistical results did Gulf attain with the large commercial regression model?

A. As presented on page 2 of Schedule 4 of my exhibit, all variables used in the large commercial regression model were statistically significant (p-values were less than 5 percent) and each coefficient had the expected sign. The model's adjusted R-squared was 97.7 percent, indicating that all but 2.3 percent of the variance in the historical data was explained by the model. The model's Durbin-Watson d-statistic was 1.79, indicating no significant autocorrelation in the residuals. Overall, these are excellent statistical results.

Q. What data sources were employed for the economic variables used in Gulf's commercial regression models?

A. Historical values and forecast projections of the economic variables "non-manufacturing employment" and "GDP price deflator" were purchased from Moody's Analytics. Gulf used the May 2010 vintage of Moody's economic projections, which was the most recent data available at the time the forecast was developed.

Q. How was historical commercial weather calculated?

A. Cooling and heating degree hours were calculated using the NOAA Pensacola weather station's hourly temperatures. Commercial cooling degree hours are the result of taking the number of degrees Fahrenheit that each hourly temperature is above a 62 degree baseline, and summing over a given time period. Commercial heating degree hours are the result of taking the number of degrees Fahrenheit that each hourly temperature is below a 54 degree baseline, and summing over a given time period.

These commercial cooling and heating degree hour temperature baselines reflect the observed correlation between hourly temperatures and hourly energy purchases by Gulf's commercial customers. Observed commercial customer temperature breakpoints are lower than residential customer temperature breakpoints because commercial buildings typically contain more heat producing equipment and people than residential buildings. Thus, commercial Heating Ventilating and Air Conditioning (HVAC) equipment typically begins heating later (below a lower temperature) and begins cooling sooner (above a lower temperature) than residential HVAC equipment.

Monthly billing cycle commercial weather was calculated as follows. For each bill group, the total commercial cooling (heating) degree hours were summed over the period from the day after the prior month's scheduled read date through the current month's scheduled read date. These summed commercial cooling (heating) degree hours for each of the 21 bill groups were then totaled and divided by 21 to get the monthly billing cycle commercial cooling (heating) degree hours.

Q. How was forecast commercial weather calculated?

A. As is standard practice in the industry, Gulf used "normal" weather in its energy forecasts, where "normal" is defined as a long-term average of historical weather. Monthly normal weather for the commercial class was developed using historical monthly cycle commercial cooling (heating) degree hours per billing day averaged by month over the past 20 years.

As was the case for residential, Gulf had previously used a Typical Meteorological Year (TMY) to develop commercial class normal weather but switched two years ago to this 20 year average in order to simplify the process of updating Gulf's normal weather.

Q. How were the outputs of the two commercial regression models used to develop the commercial energy forecast?

A. The small commercial regression model output was multiplied by the projected number of non-lighting small commercial customers and projected cycle billing days by month. The large commercial regression model output was multiplied by the projected number of non-lighting large commercial customers and projected cycle billing days by month. These small commercial and large commercial results were then summed. The commercial class outdoor lighting energy projection was then added to produce the total commercial class energy projection. The total commercial class energy projection was then adjusted to reflect the anticipated impacts of Gulf's DSM plan. A projection of unbilled energy was then added to the resulting billed energy projection to develop a calendar month projection of total commercial class energy. Commercial energy sales by rate were developed using average historical use per customer by rate.

Q. Please address the anticipated impacts of Gulf's DSM plan on the commercial energy forecast.

A. The anticipated impacts of Gulf's DSM plan to the commercial class were projected to be 14 million kWh in the test year. The forecast reflects all expected impacts of the DSM plan – some of those impacts were embedded in the regression model output and some of those impacts were included through an exogenous adjustment to the regression model output. Gulf utilized data from ITRON as well as Gulf's experience in the energy efficiency market and knowledge of existing programs to determine, by program, the amount of energy savings embedded in the historical regression data. The remaining impacts, those not embedded in the historical data, formed the exogenous DSM adjustment. The exogenous DSM adjustment to commercial class energy in the test year was 6 million kWh, which reduced total retail energy sales by 0.05 percent.

Q. How was Gulf's 2012 forecast of industrial energy sales developed?

A. The short-term industrial energy sales forecast was developed using a combination of on-site surveys of major industrial customers and historical average consumption per customer per billing day.

Fifty three of Gulf's largest industrial customers, representing over 90 percent of the industrial class sales, were interviewed by Gulf's industrial segment administrators to identify expected load changes due to equipment additions and replacements or changes in operating schedules and characteristics. The short-term forecast of monthly sales to these

major industrial customers was a synthesis of this survey information and historical monthly to annual energy ratios.

The forecast of short-term sales to the remaining smaller industrial customers, which represent 1.4 percent of total retail energy sales, was developed by rate schedule and month using historical averages. The resulting estimates of energy purchases per customer per billing day were multiplied by the expected number of customers and billing days by month to expand to the rate level totals. These projections were then added to the results for the major industrial customers, the industrial class outdoor lighting energy projections and the industrial class unbilled estimates to sum to the industrial class calendar month totals.

Q. How was Gulf's 2012 forecast of street lighting energy sales developed?

A. Similar to the outdoor lighting projections for the residential, commercial and industrial classes, Gulf's forecast of street lighting energy sales was developed using an historical growth rate applied to the one rate (OS-I/II) applicable to the street lighting classification.

Q. How was the total retail energy sales forecast developed?

A. Gulf's total retail energy sales forecast was the result of summing residential, commercial, industrial and street lighting energy sales together.

Q. Is this the same forecast methodology for energy sales that Gulf used and the Commission accepted in Gulf's last base rate proceeding?

A. The overall methodology that Gulf currently uses to forecast energy sales is substantially the same as that employed in the last base rate proceeding. Gulf has made four minor changes to its forecast methodology in the past ten years that have either improved accuracy or simplified processes. First, Gulf improved the forecast of commercial energy sales by splitting the class into two components, large and small, before developing regression models for commercial energy sales. Second, Gulf added applicable economic variables to the residential and commercial regression models to better capture the effects of economic cycles on energy purchases. Third, Gulf switched to a 20-year average normal weather to improve our ability to update it. Fourth, Gulf simplified the outdoor lighting energy forecasts, reducing the number of separate projections to seven when we switched from projecting energy sales for each outdoor lighting fixture type individually to the simpler method of projecting outdoor lighting energy sales by rate and class.

Q. Did you make any adjustments to the forecast besides those already described for DSM, EV charging, and unbilled?

A. No. Because the regression equations fit the historical data well, there was no need to adjust the regression outputs.

Q. Has this forecast methodology provided reliable forecasts of retail energy sales in the past?

A. Yes. Over the four years prior to the recession, Gulf slightly under-forecast retail energy sales one year out and two years out by 3.1 percent and 3.6 percent, respectively. (Under-forecast means Gulf forecast less energy than our customers actually purchased over that time period). During the Great Recession, Gulf slightly over-forecast retail energy sales one year out and two years out by 2.5 percent and 5.7 percent, respectively. (Over-forecast means Gulf forecast more energy than our customers actually purchased over that time period).

Q. How accurate has the retail energy sales forecast which has been proposed for use in this proceeding been?

A. Over the twelve months of the forecast period for which we have actual data to compare to the forecast (June 2010 through May 2011), total retail energy sales were slightly over-forecast by 1.5 percent.

Q. How was Gulf's forecast of 2012 territorial wholesale energy sales developed?

A. The forecast of energy sales to Gulf's two wholesale customers was developed using a multiple linear regression model for each wholesale customer.

Q. What variables were employed by Gulf in the regression models used to develop the wholesale energy sales forecast?

A. Monthly energy purchases per day for each of Gulf's wholesale customers were estimated based on historical energy sales, residential weather

(heating and cooling degree hours), real disposable income per household, an indicator variable corresponding to the wholesale price level, and an autoregressive term lagged one month to address first-order residual autocorrelation over time.

Q. What statistical results did Gulf attain with the wholesale regression models?

A. All variables used in the wholesale regression models were statistically significant (p-values were less than 5 percent) and each coefficient had the expected sign. The models' adjusted R-squared values were both 95.5 percent, indicating that all but 4.5 percent of the variance in the historical data was explained by each model. The models' Durbin-Watson d-statistics were 2.06 and 2.17 respectively, indicating no significant autocorrelation in the residuals. Overall, these are excellent statistical results.

Q. How were the wholesale model outputs used to develop the total wholesale energy forecast?

A. The model outputs, monthly energy purchases per day, were multiplied by the projected number of days by month to expand to the individual customer totals, which were then summed to develop the wholesale class total.

Q. What is the importance of the wholesale energy projection in this proceeding?

A. Gulf's 2012 wholesale energy projection was used by Gulf Witness O'Sheasy in the cost of service study to develop allocators that help determine the jurisdictional split between wholesale and retail jurisdictions.

IV. GULF'S PEAK DEMAND FORECAST

Q. What is Gulf's forecasted peak demand for 2012?

A. Gulf's territorial system peak demand is projected to be 2,642 megawatts (MW) in the test year, representing an increase of 50 MW or 1.9 percent over projections for the twelve months ended December 2011. This peak is expected to occur in the summer month of July 2012.

Q. How was this forecast of peak demand developed?

A. The forecast of annual system peak demands was developed using an historical load factor analysis and territorial supply projections. The annual system peak demand projection for 2011 was based on the average of the historical annual load factors for the period 2007 through 2009 (the last full year available at the time the forecast was developed) to reflect the continuing impact of the recession. The annual system peak demand projection for 2012 reflects a gradual, linear return to pre-recessionary annual load factor levels by 2013. Gulf's annual system peak demand typically occurs in the month of July. Monthly system peak demands were developed using monthly-peak to annual-peak ratios. The resulting monthly system peak demand projections were then adjusted to

reflect the anticipated impacts of conservation programs from Gulf's DSM plan.

Q. Please address the anticipated impacts of Gulf's DSM plan on the Company's annual system peak demand forecast.

A. The anticipated impact of Gulf's DSM plan on the Company's annual system peak demand was projected to be 28 MW in the test year. The forecast reflects all expected impacts of the DSM plan – some of those impacts were embedded in historical peak demand levels and some of those impacts were included through an adjustment. As with DSM adjustments to energy, data from ITRON as well as Gulf's experience in the energy efficiency market and knowledge of existing programs were used to determine, by program, the amount of demand savings embedded in the historical data. The remaining impacts, those not embedded in the historical data, formed the DSM adjustment. The DSM adjustment to system peak demand in the test year was 19 MW, which reduced system peak demand by 0.7 percent.

V. GULF'S FORECAST OF RETAIL BASE RATE REVENUES

Q. What are the 2012 results of Gulf's retail base rate revenue forecast?

A. Retail base rate revenues are forecasted to total $451,228,000 in the test year. Using current rates, the base rate revenue forecast by class consists of the following:

Residential:	$267,534,000
Commercial:	$139,614,000
Industrial:	$ 40,993,000
Street Lighting:	$ 3,087,000

Q. Please address how the base rate revenue forecast was developed?

A. Current rate schedules were applied to monthly projections of customers, energy sales and aggregate billing demands, as applicable by rate, for each customer classification. Outdoor lighting revenue was estimated by class and rate using historical average revenue per kWh applied to the appropriate outdoor lighting energy forecast.

Q. What billing components were used to develop the revenue forecast?

A. The residential monthly billing components consisted of the customer (base) charge and the energy charge. The residential time-of-use rate (RSVP) energy charge included a low, medium and high tier. The commercial and industrial billing components consisted of the customer (base) charge, the energy charge and, where applicable, the demand charge. The non-residential energy-only time-of-use rate (GSTOU) energy charge included an on-peak, intermediate and off-peak tier by season. The commercial and industrial demand charge consisted of the max demand charge and, where applicable, the on-peak demand charge and the reactive demand charge. Primary and transmission voltage level discounts were applied to energy and demand charges as appropriate.

Q. How were forecast monthly billing determinants developed for each of these billing components?

A. Forecast year billing determinants were developed for each rate schedule and, where applicable, each voltage discount level as follows:

- Monthly number of customers was derived from the customer forecast.
- Monthly energy was derived from the energy forecast.
    - Monthly time of use (TOU) energy was based on monthly energy from the forecast allocated to tier based on monthly historical averages by tier.
- Monthly aggregate max demands for commercial and small industrial customers by rate were derived from monthly historical average max demand to energy ratios multiplied by forecast year monthly energy.
- Monthly aggregate on-peak demands for commercial and small industrial customers by rate were derived from monthly historical average on-peak demand to energy ratios multiplied by forecast year monthly energy.
- Monthly max demands, monthly on-peak demands and monthly reactive demands for the 53 largest industrial customers and the 16 largest commercial customers were derived from historical ratios applied to projected annual max demands which are collected through the large customer survey.
    - Monthly max demands for each of these customers were calculated as the product of the forecast year's annual peak demand times the ratio of an historical year's monthly max demand to annual max demand.

- Monthly on-peak demands for each of these customers were calculated as the product of the forecast year's monthly max demand times the ratio of an historical year's monthly on-peak demand to monthly max demand.
- Monthly reactive demands for each of these customers were calculated as the product of the forecast year's monthly max demand times the ratio of an historical year's monthly reactive demand to monthly max demand.
- The historical year in these calculations was June 2009 through May 2010, the most recent 12 months of billing data available at the time the forecast was developed.

Q. Is this the same forecast methodology for retail revenue that Gulf used and the Commission accepted in Gulf's last base rate proceeding?

A. Yes, with one minor exception. Gulf previously projected each outdoor lighting fixture type individually and, therefore, could apply fixture charges by type as part of the revenue forecast. Several years ago Gulf switched to the simpler method of projecting outdoor lighting revenue by rate and class using average revenue per kWh. This refinement saved time and had no significant impact on forecast accuracy.

Q. Has this forecast methodology provided reliable forecasts of retail revenue in the past?

A. Yes. Over the four years prior to the recession, Gulf slightly under-forecast retail revenues one year out and two years out by 2.4 percent and

3.2 percent, respectively. (Under-forecast means Gulf forecast less retail revenue than we actually received over that time period). During the Great Recession, Gulf slightly over-forecast retail revenues one year out and two years out by 2.1 percent and 5.1 percent, respectively. (Over-forecast means Gulf forecast more retail revenue than we actually received over that time period).

Q. How accurate has the retail revenue forecast which has been proposed for use in this proceeding been?

A. Over the twelve months of the forecast period for which we have actual data to compare to the forecast (June 2010 through May 2011), total retail base rate revenue was slightly over-forecast by 1.0 percent.

Q. Has the particular forecast proposed in this proceeding been used by Gulf in other recent proceedings or filings before the Commission?

A. Yes. This forecast of customers, energy, and peak demand was the foundation for and was included in Gulf's 2011-2020 Ten Year Site Plan which was filed with the Commission on April 1, 2011. This forecast of energy and demand was also the basis for calculations used in Gulf's Renewable Standard Offer Contract which was filed with the Commission on April 1, 2011 and approved by the Commission on June 14, 2011 in Docket No. 110095-EQ. This forecast of customers and energy was included in Gulf's Forecasted Earnings Surveillance Report which was submitted to the Commission staff on March 14, 2011.

Q. Is the forecast prepared by and relied upon by Gulf in this proceeding appropriate for the Commission to use in setting Gulf's base rates?

A. Yes. It is based upon an established and proven methodology. It employed reliable data from well respected sources. The methodology and forecast are routinely used by Gulf in its regular course of business and were not developed just for this rate case. The methodology and the resulting forecast have been relied upon by Gulf and the Commission in a number of proceedings.

VI. GULF'S LOAD RESEARCH

Q. Please provide an overview of Gulf's Cost of Service Load Research.

A. Gulf routinely performs Cost of Service Load Research every three years in accordance with FPSC Rule 25-6.0437. This Load Research is designed to estimate the monthly coincident peak demand (CPKW) and non-coincident peak demand (NCPKW) of Gulf's customers, grouped by rate class. Gulf collects this data using sophisticated load research meters that record a customer's energy use every 15 minutes. To keep the expense of this task down, Gulf designs a statistical sampling plan that will provide an accurate estimate of the peak demands using a minimal number of these sophisticated meters. That sampling plan is filed with the Commission for review and approval in the year prior to data collection. Gulf then collects data for one calendar year. In the months following the data collection year, Gulf analyzes the collected load research data and

submits a report to the Commission for review. That report contains the monthly coincident peak demands, monthly non-coincident peak demands, annual energy, and number of customers for each rate class, as well as other details regarding sample sizes and statistical accuracies.

Q. What are the primary purposes of Gulf's Cost of Service Load Research studies routinely filed in accordance with the requirements of the Cost of Service Load Research Rule 25-6.0437?

A. As is stated in the Cost of Service Load Research Rule 25-6.0437,

> The primary purpose of this rule is to require that load research that supports cost of service studies used in ratemaking proceedings is of sufficient precision to reasonably assure that tariffs are equitable and reflect the true costs of serving each class of customer. Load research data gathered and submitted in accordance with this rule will also be used by the Commission to allocate costs to the customer classes in cost recovery clause proceedings, in evaluating proposed and operating conservation programs, for research, and for other purposes consistent with the Commission's responsibilities.

Q. What are the accuracy requirements of the Cost of Service Load Research Rule 25-6.0437?

A. The Cost of Service Load Research Rule 25-6.0437 states:

> The sampling plan shall be designed to provide estimates of the averages of the 12 monthly coincident peaks for each class within plus or minus 10 percent at the 90 percent confidence level. The sampling plan shall also be designed to provide estimates of the summer and winter peak demands for each rate class within plus or minus 10 percent at the 90 percent confidence level, except for the General Service Non-Demand rate class. The sampling plan shall be designed to provide estimates of the summer and winter peak demands for the General Service Non-Demand rate class within plus or minus 15 percent at the 90 percent confidence level.

Q. What load research results are being used in these proceedings?

A. Gulf's 2009 Cost of Service Load Research Study, filed with the Commission on June 21, 2010 pursuant to Rule 25-6.0437, is the basis of the cost of service study in this proceeding.

Q. Does Gulf's 2009 Cost of Service Load Research sample design meet the requirements of the Cost of Service Load Research Rule 25-6.0437?

A. Yes. The sample design meets or exceeds the requirements of the referenced rule.

Q. How were Gulf's Cost of Service Load Research results used in this proceeding?

A. Gulf's 2009 Cost of Service Load Research Study results were used by Mr. O'Sheasy in the cost of service study to develop NCPKW and CPKW allocators.

VII. SUMMARY

Q. Please summarize your testimony.

A. Gulf's forecast methodologies are rigorous, statistically significant and logically connected to the marketplace. Gulf's forecast methodologies are well established. They have been consistently used for many years in substantially the same form and have been reviewed and approved by the Commission in other proceedings. Gulf's methodologies appropriately incorporate adjustments for the recently approved DSM goals as well as emerging electric vehicle charging loads. Gulf's forecast methodologies consistently produce accurate results which are routinely used by many departments throughout the Company in the regular course of business. The specific forecast proposed in this proceeding, which has been relied on by the Commission in other filings, is appropriate for use in this base rate proceeding. The Cost of Service Load Research study used in this proceeding has been previously filed and reviewed by the Commission, meets the Commission's requirements in Rule 25-6.0437, and is appropriate for use by Mr. O'Sheasy in the cost of service study.

Q. Does this conclude your testimony?

A. Yes.

MR. STONE: We would ask that Exhibit 8, premarked, be admitted into the record.

CHAIRMAN GRAHAM: We will enter Exhibit 8 into the record.

(Exhibit Number 8 was admitted into the record.)

MR. STONE: Gulf's third witness has also been stipulated. We would ask that --

MR. YOUNG: Mr. Chairman, I'm sorry to interrupt. If we're still on Witness McGee, I would like to have some of the Staff's -- based on the agreement, there are several exhibits that Staff would ask to be moved into the record.

CHAIRMAN GRAHAM: Okay. What are those exhibits?

MR. YOUNG: And that's Exhibit Number 104, identified as Hearing Exhibit Number 104, Witness McGee's, and it's Gulf's response to Staff's Twentieth Set of Interrogatories, Number 259, and it's Bates-stamped number 527 through 533.

CHAIRMAN GRAHAM: What was that one, that number?

MR. YOUNG: That's Hearing Exhibit Number 104.

(Exhibit Number 104 was admitted into the record.)

CHAIRMAN GRAHAM: Okay. I got the 104. I thought you said something after that.

MR. YOUNG: And if you'll bear with me one second. Staff would ask that Gulf's response to Staff's Second Set of Interrogatories, Number 30, be identified as its own separate exhibit, given a separate hearing exhibit number, and I think we're up to 171. And I show a title of that --

CHAIRMAN GRAHAM: Wait, wait, wait, wait, wait. You said you had Exhibit Number 30 that you wanted to have a different title?

MR. YOUNG: Yes. It's a part of Exhibit Number 87, but since 87 has several other interrogatories, Staff requests that it be given its own separate hearing exhibit number for identification purposes and be moved in.

CHAIRMAN GRAHAM: The one that we passed out earlier that we said came out Number 30?

MR. YOUNG: No. This is separate.

CHAIRMAN GRAHAM: Okay. You're going to have to one more time explain to me what the heck you're talking about.

MR. YOUNG: Okay. As Number 171, Staff is asking that Exhibit Number 171 be marked as Mr. McGee, Witness McGee, and the short title will

be -- I'll get to it. I'm sorry. "Gulf's Response to Staff's Second Set of Interrogatories, number 30.

MS. KAUFMAN: Excuse me, Mr. Chairman. Could I ask a question about that?

CHAIRMAN GRAHAM: Sure.

MS. KAUFMAN: Is that something additional that's not on the list that has been distributed?

MR. YOUNG: It's on the list as being distributed, but on page number 14, as you can see, Hearing Exhibit Number 87 has several witnesses. So in order to move this process along, Staff is requesting, since the parties have not stipulated to all of 87 and Witness McGee has been stipulated, that his exhibit be broken out by itself.

MR. STONE: Mr. Chairman, as I understand what Mr. Young is suggesting, the response to Interrogatory Number 30 would be pulled out of Hearing Exhibit 87 and given its own separate exhibit number, and he's proposing that be Exhibit 171. For the record, Gulf is prepared to stipulate to the entry of all of Exhibit 87 into the record.

CHAIRMAN GRAHAM: Well, what has been stipulated has just been Number 30, so we'll do as Mr. Young has said and we'll break it out to 171,

and we'll enter that into the record.

(Exhibit Number 171 was marked for identification and admitted into the record.)

CHAIRMAN GRAHAM: Ms. Kaufman, did you get that?

MS. KAUFMAN: I did. Thank you, Mr. Chairman.

CHAIRMAN GRAHAM: I think it would have been a lot easier if Mr. Young would have told us to turn to page 14.

MR. YOUNG: Next time, duly noted.

CHAIRMAN GRAHAM: All right. Any other exhibits for McGee?

Okay. Mr. Stone, let's go to the next one.

MR. STONE: The next witness is also stipulated. His name is William G. Buck, and we would ask that his testimony be inserted into the record as though read.

CHAIRMAN GRAHAM: We will enter his testimony as though read and Exhibit Number 9 into record.

(Exhibit Number 9 was admitted into the record.)

MR. STONE: Thank you.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
William G. Buck, III
Docket No. 110138-EI
In Support of Rate Relief
Date of Filing: July 8, 2011

Q. Please state your name and business address.

A. My name is Bill Buck. My business address is One Energy Place, Pensacola, FL 32520.

Q. By whom are you employed?

A. I am employed by Gulf Power Company (Gulf or the Company) as the Supervisor of Financial Planning in the Corporate Planning Department.

Q. What are your responsibilities as Supervisor of Financial Planning?

A. I am responsible for preparing the Company Operating Budget and Forecast, administering the Capital Additions Budget, preparing various regulatory reports such as the Florida Public Service Commission (FPSC or the Commission) Surveillance Report, and preparing or assisting with various financial analyses and reports for management and outside parties.

Q. What is your educational background?

A. I graduated from Florida State University in 1998 with a Bachelor of Science in Accounting and a Bachelor of Science in Finance.

Q. Please state your prior work experience and responsibilities.

A. Immediately following graduation, I was employed by Arthur Andersen LLP in Atlanta, Georgia in the audit department. In 2001, I accepted a position as a Senior Auditor with the O'Sullivan Creel LLP accounting firm in Pensacola, Florida. In 2002, I began my career with Gulf as a Financial Analyst in the Financial Planning Department. Since 2002, I have been responsible for all department responsibilities at various times, and in April 2006 I was promoted to my current position as Supervisor of Financial Planning.

Q. Do you hold any professional licenses in the field of accounting?

A. Yes. I am a licensed Certified Public Accountant and a member of the Florida Institute of Certified Public Accountants.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide an overview of Gulf's rigorous planning and budgeting process. This process, which Gulf performs annually, uses the component budgets and financial assumptions to produce a financial forecast on which the Company relies to make decisions on how to provide adequate and reliable service to its customers. Specifically, I will describe the Capital Additions and Operations and Maintenance (O&M) budget processes, set forth the component budgets used in developing the financial forecast, and outline the assumptions used in developing Gulf's financial forecast. The financial forecast is used by Gulf's management for a variety of purposes,

and in this instance is also the basis for Gulf's projected data for the test year used in this rate case.

Q. Are you sponsoring any exhibits?

A. Yes. I am sponsoring Exhibit WGB-1, Schedules 1 through 9. Exhibit WGB-1 was prepared under my supervision and direction, and the information contained in that exhibit is true and correct to the best of my knowledge and belief.

Q. Are you sponsoring any of the MFRs filed by Gulf?

A. Yes. The MFRs that I sponsor in their entirety or that I jointly sponsor are listed on Schedule 1 of my Exhibit WGB-1. The information contained in the MFRs that I sponsor or co-sponsor is true and correct to the best of my knowledge and belief.

Q. Please provide an overview and description of Gulf's planning and budgeting process.

A. Gulf's planning and budgeting process is an ongoing process that is designed to help the Company achieve operational and financial goals and objectives, while taking into account economic and financial conditions. This process produces a budget for the current year and a budget forecast for the four subsequent years. These are utilized by management as a tool for evaluating and making decisions to ensure the Company provides efficient and reliable service to its customers. The annual 2011 Budget and Forecast, including the forecasted financial

statements for the test year, is the basis for Gulf's projected data for the 2012 test year used in this rate case. Both the 2011 and 2012 budgeted levels of O&M and Capital Additions from the 2011 Budget and Forecast are reasonable, prudent and necessary. The budgeting process for 2011 was consistently applied and produced reliable results which are suitable for establishing the revenue requirements for the 2012 test year.

Q. Please describe Schedule 2 of your exhibit.

A. Schedule 2 is a flow chart of Gulf's annual planning and budgeting process. There are eight component budgets, which are shaded on Schedule 2, that are incorporated into Gulf's financial forecast. The Customer, Energy, and Demand budgets start the process, and these budgets are used as inputs in the derivation of the Revenue, Fuel, Interchange, Capital Additions and O&M budgets. I am responsible for the financial forecast, which integrates the eight component budgets, along with various other financial assumptions and estimates, and results in projected financial statements. These projected financial statements are then used by Gulf Witness McMillan to develop the net operating income, rate base, capital structure and revenue requirements that Gulf is requesting in this filing.

Q. Who will testify on the preparation of the component budgets in Gulf's financial forecast?

A. The Customer, Energy, Demand, and Revenue Budgets are the responsibility of Gulf Witness McGee. The Capital Additions Budget is the

responsibility of Gulf Witnesses Grove, Caldwell, Moore, and McMillan. Gulf Witnesses Erickson, Twery/Crumlish, Burroughs and Neyman, along with Mr. Grove, Mr. Moore, and Mr. Caldwell will discuss the O&M Budget. The Fuel Budget is the responsibility of Mr. Burroughs, and the Interchange Budget is the responsibility of Mr. Grove.

Q. Who administers the annual planning and budgeting process, and what is the Corporate Planning department's role in the process?

A. The annual planning and budgeting process is administered by Corporate Planning under the direction of the Chief Financial Officer, Mr. Teel.

The Corporate Planning department is responsible for establishing the budget schedule, developing the Budget Message which is submitted to the Chief Financial Officer for review and approval and transmitting the Budget Message. Corporate Planning also coordinates the Capital Additions and O&M Budget processes, ensuring that all personnel involved with the processes are kept informed of the key assumptions, goals and any strategic issues facing the Company. In addition, Corporate Planning inputs information from the eight component budgets along with other financial assumptions and estimates into the financial model. Finally, Corporate Planning is responsible for the ongoing process of analyzing and maintaining the financial model logic and inputs to ensure the most accurate forecast based on current assumptions.

Q. Please describe the role of Corporate Planning in preparation of the Capital Additions and O&M component budgets.

A. Corporate Planning is responsible for establishing a process for the preparation of the Capital Additions and O&M Budgets, for administering the process under the direction of the Chief Financial Officer and for preparing the summaries, comparisons, and other information that may be requested. The Executive Management Team (the CEO and the four vice presidents) reviews and approves these Budgets. Schedule 3 of my exhibit is a flow chart outlining the Capital Additions and O&M Budget process.

Q. One of the initial steps in the budget process described on your Schedule 3 is the Budget Message. Please describe the Budget Message.

A. Each year to begin the O&M and Capital Additions Budget process, the Budget Message is provided to the Planning Units, which are organizations within the Company that have budget responsibility. The Budget Message provides annual budget guidelines for the O&M and Capital Additions Budgets, along with other assumptions to be used in the budget preparation process. Corporate Planning develops a draft Budget Message, which is submitted to the Chief Financial Officer for review and approval. Once the Budget Message is approved, Corporate Planning sends it to the Planning Units.

Q. Describe the budget process after the issuance of the Budget Message.

A. This is a multi-step, iterative process. Upon receipt of the Budget Message, each Planning Unit follows its own internal process to prepare its O&M and Capital Additions Budgets, and those internal processes are described in the testimony of other witnesses. However, there is a common element among the processes used by each individual Planning Unit – each Planning Unit examines the basic goals and objectives that must be accomplished and builds the budgets necessary to meet these responsibilities. Each Planning Unit prepares the detailed budgets that support its goals and objectives for the budget year. The Vice President for each Planning Unit reviews and, if necessary, modifies that function's budgets prior to the submission of the Planning Unit's budgets to Corporate Planning.

Corporate Planning reviews submittals for consistency with the Budget Message and compiles the data for review by the Chief Financial Officer and the other executives. Any changes resulting from the executive review and approval process are communicated to the Planning Unit by Corporate Planning. The final approved budgets for O&M and Capital Additions are summarized and communicated to the Planning Units in a letter from the Chief Financial Officer.

Q. Please describe Gulf's Capital Additions Budget.

A. The Capital Additions Budget consists of Plant Expenditures (PEs) for additional investments that are categorized as Production, Transmission,

Distribution, and General Plant. The PEs are further identified as Specific PEs and Blanket PEs. Specific PEs are generally individual projects costing $50,000 or more that require expenditures in one or more years. Blanket PEs reflect repetitive expenditures based on historical trends and projected customer growth, such as pole replacements and transformers, that are not identified as individual or separate projects at the time the budget is prepared.

Q. Who is responsible for developing PEs?

A. Planning Units are responsible for developing the PEs for their areas. The majority of the PEs are prepared under the direction of Mr. Grove, Mr. Caldwell, and Mr. Moore.

Q. Who is responsible for reviewing and approving the overall Capital Additions Budget?

A. Gulf's Executive Management Team reviews all Capital Additions Budget requests. After review and approval by the executives, the Capital Additions Budget is approved annually by the Company's Board of Directors.

Q. Does Gulf monitor the actual construction expenditures against its approved budget?

A. Yes. Corporate Planning monitors and prepares a comparison of actual to budget expenditures each month. For non-quarter end months, explanations are only required for variances that exceed $250,000. For

quarter end months, the Planning Units must submit variance explanations for each PE that has a year-to-date variance that exceeds 10 percent or $250,000, whichever is less. Variances less than $10,000 do not require an explanation. In addition to researching and explaining year-to-date variances, the appropriate Planning Unit is required to prepare an estimate of the budget status at year-end or at completion of the project. Monitoring the variances and ensuring this process is followed is the responsibility of Corporate Planning.

Q. What is the amount of Gulf's test year Capital Additions Budget?

A. Gulf's test year Total Company Capital Additions Budget is $423,622,000, and Gulf's Test Year Capital Additions Budget excluding wholesale, cost recovery clauses and non-utility is $189,103,000. These projections are shown by major functional category on Schedule 4 of my exhibit.

Q. Please describe Gulf's O&M Budget.

A. The O&M Budget consists of expenses required to safely provide efficient and reliable service to Gulf's customers, covering a period of five years. Gulf's Planning Units submit detailed budget requests through the computerized budget input system. All O&M budget amounts are required to be submitted through this process, with the exception of the fuel and interchange information, which is derived from the Fuel and Interchange component budgets. The O&M Budget is provided to the Executive Management Team for their review and approval.

Q. How is the rate of inflation used by Gulf in the preparation of its O&M Budget?

A. As stated previously, the Budget Message issued by the Chief Financial Officer includes the O&M and Capital Additions Budget guidelines for each Business Unit, in addition to other budget assumptions to be used. An inflation rate is provided as part of the Budget Message as an aid to Planning Units in the development of their budget details. However, justification of O&M expenses requires more than mere escalation by the Consumer Price Index (CPI) or any other measure of inflation. As I mentioned earlier in my testimony, each Planning Unit develops its O&M budget by examining the activities necessary to meet its goals and objectives, not by simply escalating costs associated with prior periods. The inflation rates for 2011 and 2012 included in the Budget Message were 2.1 percent and 2.8 percent, respectively. These rates of inflation were based upon forecast data for CPI obtained from Moody's Analytics, formerly known as Moody's Economy.com.

Q. How does Corporate Planning monitor O&M budget variances?

A. Corporate Planning monitors budget variance reports each month, using Gulf's accounting and reporting system. Each quarter, the Planning Units are required to submit year-to-date reports that include explanations of all variances of 10 percent or more that equal or exceed $25,000. Any variance amount that exceeds $500,000, regardless of the percentage, must also be explained. Projections for the year-end expenses are also submitted quarterly and reviewed by the Chief Financial Officer.

Q. What is the amount of Gulf's test year O&M Budget?

A. The test year System Per Books O&M Budget is $1,086,835,000, and the test year Total Adjusted O&M Budget is $288,474,000, as reflected on exhibit RJM-1, Schedule 18 of Mr. McMillan's testimony. Schedule 5 of my exhibit summarizes the test year O&M Budget by major functional category. The witnesses responsible for O&M expenses by function will address their test year O&M budgets and any O&M benchmark variances.

Q. Have there been any significant changes in Gulf's budget process since the development of the forecast that was used to support Gulf's last base rate case?

A. No. Gulf's budget process continues to successfully produce reliable budgets and forecasts. Therefore, there have not been any significant changes in Gulf's budget process since the last base rate case, and it has been consistently applied for the 2011 Budget and Forecast, which includes the 2012 test year.

Q. Turning now to the financial forecast, please explain how this forecast is developed.

A. The outputs of the component budgets that I described earlier in my testimony are input into Gulf's financial model. Additionally, various income statement and balance sheet items not captured in the component budgets are analyzed, developed and input into the financial model. The financial model, in turn, processes this data using a number of integrated calculation modules to generate the financial and accounting statements

that comprise Gulf's financial forecast. This dynamic iterative process ensures that these various items are consistent with the other budgeted items. For example, forecasted debt issuances and associated interest expense are analyzed and updated when necessary due to other budget changes.

Q. What is the financial model to which you have referred?

A. The financial model is a proprietary, computer-based model that simulates Gulf's actual financial and accounting results based on a given set of inputs. Schedule 6 is a summarized flowchart of the financial model inputs and outputs required to produce the financial forecast.

Q. Does Gulf prepare financial forecasts for purposes other than rate cases?

A. Yes. Gulf prepares and updates its financial forecast in the regular course of its business to provide management with the most accurate and up-to-date projections to manage the business and to help the Company achieve operational and financial goals.

Gulf uses the financial model to prepare the Annual Budget and Forecast, and also to continually update financial projections. These financial forecasts are also used for external purposes such as analyst earnings calls, rating agency information, forecasted earnings surveillance reports filed with the FPSC, and other financial requests.

Q. Please describe the financial statements shown on Schedules 7 and 8 of your exhibit.

A. Schedule 7 is Gulf's projected monthly Balance Sheet for the period December 2011 through December 2012, which is the basis for developing the rate base and capital structure. Schedule 8 is the projected monthly Income Statement for the twelve months ended December 31, 2012, used in developing net operating income. These financial statements from the financial model are based on current budget estimates for 2012 from the 2011 Budget and Forecast.

Q. You have summarized utility plant data on your Schedule 7. Have you prepared a report with a further breakdown of the plant balances?

A. Yes. Schedule 9 presents a further breakdown of the utility plant balances along with the monthly activity in these accounts for the test period. The projected plant data is based on the approved Capital Additions Budget, which is supported by various witnesses as noted on Schedule 4.

Q. Has Gulf Power filed a list of the assumptions used in developing Gulf's financial forecast?

A. Yes. MFR F-8 lists the assumptions used in developing Gulf's financial forecast and the supporting basis for each assumption. The assumptions used in this financial forecast, as outlined on MFR F-8, are reasonable in light of our experience and the circumstances known at the time the assumptions were developed.

Q. Please summarize your testimony.

A. Gulf utilizes a very straightforward, logical and comprehensive budget process, including the development of the component budgets that are incorporated into the financial model, which produces Gulf's financial forecast. The budgeting process is performed annually and results in a forecast that management uses as a tool in planning and decision making. The assumptions contained in the budget process are reasonable, and they have been obtained from the best sources available at the time the budget was developed. The financial forecast that results from this process provides a reasonable and sound basis for projecting the results of Gulf's operations during the 2012 test year as incorporated in the MFRs, testimony and exhibits filed in this case.

Q. Does that conclude your testimony?

A. Yes.

CHAIRMAN GRAHAM: Anything else for Buck?

MR. STONE: That's all I have for Mr. Buck.

CHAIRMAN GRAHAM: Staff?

MR. YOUNG: Yes, sir. Staff has one for Mr. Buck. And that's -- based on the stipulation, it's -- based on the agreement, excuse me, that the parties do not object to Mr. Buck's response, Gulf's Response to Staff's Fourteenth Set of Interrogatories, Item 171 be entered into the record, and Staff asks that it be given its own hearing number, and that would be Number 172.

MR. STONE: I'm sorry. I'm confused.

CHAIRMAN GRAHAM: He does a good job of confusing everybody, doesn't he? What do you want to enter as 172?

MR. YOUNG: On page 16.

CHAIRMAN GRAHAM: Thank you.

MR. STONE: It just coincidentally happened to be the same exhibit number that just previously got admitted. That's what was throwing me off.

CHAIRMAN GRAHAM: Okay. So Number 171 has been stipulated so we're going to give Number 171 its own exhibit number, and that's going to be Exhibit 172; is that correct?

MR. YOUNG: Yes, sir. I apologize, sir. I

thought everybody was with me.

CHAIRMAN GRAHAM: And so that's going to be witness -- what's the short title, Mr. Young?

COMMISSIONER EDGAR: Gulf's response to Staff's Fourteenth Set of Interrogatories, Item Number 171?

CHAIRMAN GRAHAM: We'll enter that into the record.

(Exhibit Number 172 was marked for identification and admitted into the record.)

CHAIRMAN GRAHAM: Anything else for Witness Buck?

Okay. Mr. Stone.

MR. STONE: Gulf's next witness will be Mr. Richard Scott Teel.

Thereupon,

R. SCOTT TEEL

was called as a witness on behalf of Gulf Power Company and, having been first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. STONE:

Q. Mr. Teel, have you been sworn?

A. I have.

Q. Would you state your name and business

address?

A. My name is Scott Teel. My business address is One Energy Place, Pensacola, Florida, 32520.

Q. By whom are you employed, and in what capacity?

A. I'm employed by Gulf Power Company as vice president and chief financial officer.

Q. Did you prefile direct testimony in this docket dated July 8, 2011, consisting of 26 pages?

A. I did.

Q. Do you have any changes or corrections to that testimony?

A. No, but I would point out that the numbers in my direct testimony have not been updated to reflect the impact of those stipulations that were approved by the Commission this morning, nor do they reflect the changes associated with moving the Crist, Plant Crist turbine upgrades out of the environmental clause.

Q. And with that understanding, if I were to ask you the same questions today, would your answers be the same?

A. Yes, they would.

MR. MELSON: Mr. Chairman, I would ask that Mr. Teel's direct testimony be inserted into the record as though read.

CHAIRMAN GRAHAM: We will insert Mr. Teel's direct testimony into the record.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
R. Scott Teel
Docket No. 110138-EI
In Support of Rate Relief
Date of Filing: July 8, 2011

Q. Please state your name and business address.

A. My name is Scott Teel. My business address is One Energy Place, Pensacola, FL 32520.

Q. By whom are you employed and in what capacity?

A. I am employed by Gulf Power Company (Gulf or the Company) as Vice President and Chief Financial Officer (CFO).

Q. What are your responsibilities as Vice President and CFO?

A. I am responsible for maintaining the overall financial integrity of the Company. My areas of responsibility include the Accounting, Corporate Secretary, Treasury, Regulatory Matters, Corporate Planning, and Supply Chain Management departments. I am also responsible for maintaining the overall financial and accounting records of the Company. Gulf maintains its books and records in accordance with Generally Accepted Accounting Principles in the U.S. (GAAP) and the rules and regulations prescribed for public utilities in the Uniform System of Accounts published by the Federal Energy Regulatory Commission (FERC), and adopted by the Florida Public Service Commission (FPSC or the Commission).

Our books and records are audited by Deloitte LLP, independent public accountants, and a copy of their latest audit opinion is included in the Company's 2010 Annual Report to Stockholders, which is filed as MFR F-1 in this case. Gulf's books and records are also subject to periodic review by the FERC and the FPSC.

Q. Please state your prior work experience and responsibilities.

A. Prior to moving to Gulf in 2010, I served as the Vice President and CFO for Southern Company Operations. In that role, I was responsible for the financial services of the Power Generation and Transmission organizations, which included budgeting and reporting, wholesale generation contract services, Open Access Transmission Tariff (OATT) administration and billings, and internal controls. I was also responsible for the Fleet Operations and Trading functions. Other roles that I have filled at Southern Company include Energy Trading Manager in Fleet Operations and Trading, and Assistant to Southern Company's Executive Vice President and CFO. Prior to joining Southern Company, I held various positions at Ernst & Young and Sonat.

Q. What is your educational background?

A. I graduated from the University of Alabama in 1992 with a Bachelor of Science in Commerce and Business Administration and a major in Accounting.

Q. Do you hold a professional license or certification?

A. I am currently an inactive member of the Alabama Society of Certified Public Accountants.

Q. What is the purpose of your testimony?

A. My testimony begins with an explanation of the actions Gulf has taken to avoid a base rate increase for almost a decade, particularly over the last several years during an especially difficult economic period for our customers. I then explain the Company's decision to use a projected 2012 test year for ratemaking purposes and the drivers behind the request for rate relief. I discuss the importance of the rate relief Gulf is requesting to Gulf's financial integrity and credit quality. I also discuss Gulf's capital structure and cost of capital. Finally, I explain why it is not appropriate to make a parent debt adjustment to Gulf's income tax expense in determining our revenue requirement.

Q. Are you sponsoring any exhibits?

A. Yes. I am sponsoring Exhibit RST-1, consisting of Schedules 1 to 11. Exhibit RST-1 was prepared under my supervision and direction, and the information contained in that exhibit is true and correct to the best of my knowledge and belief.

Q. Are you sponsoring any of the Minimum Filing Requirements (MFRs) filed by Gulf?

A. Yes. The MFRs that I sponsor in their entirety or that I jointly sponsor are listed on Schedule 1 of my Exhibit RST-1. The information contained in the MFRs that I sponsor or co-sponsor is true and correct to the best of my knowledge and belief.

I. GULF'S EFFORTS TO AVOID A BASE RATE INCREASE

Q. When was Gulf's last base rate increase?

A. Gulf's last base rate adjustment became effective on June 7, 2002. By the time this proceeding is complete, it will have been almost ten years between Gulf's base rate increases. The Commission's decision granting Gulf's last base rate increase was in Order No. PSC-02-0787-FOF-EI in Docket No. 010949-EI.

Q. What major events and challenges has Gulf had to address in the decade since its last rate case?

A. Over the last decade Gulf has weathered a number of events and met significant challenges while continuing to provide reliable service to a growing customer base without increasing base rates.

The day after Gulf's last rate case filing was made, the mindless destruction of the World Trade Center occurred. Our government responded by heightening security, including security associated with critical infrastructure like the power grid. In order to increase security for

critical pieces of infrastructure, Gulf has taken measures to improve physical security at substations and generation plants, including security checkpoints, cameras and other monitoring equipment. Additional measures have also been taken to improve cyber security.

The years 2004 and 2005 brought a number of major hurricanes to the continental United States and the Gulf Coast, including several in Gulf's service area. Gulf was recognized for its prompt response in restoring service and hope in the aftermath of these disasters. In both 2004 and 2005, the Edison Electric Institute awarded Gulf the Emergency Response Award for hurricane restoration in our service area and the Emergency Assistance Award for the Company's assistance to other companies who suffered hurricane damage. Gulf's efficiency and cost consciousness minimized the financial impact on its customers. These storms, however, have had lasting impacts on Gulf's distribution system as described by Gulf Witness Moore in his testimony. In addition, mandated storm hardening requirements have been enacted. These requirements are designed to benefit customers in terms of mitigating service interruptions, but they have imposed additional costs on Gulf and our customers.

In 2008, the United States experienced a near complete meltdown of its financial system, triggering a deep economic recession more severe than any since the Great Depression. This economic downturn affected Gulf on many levels. Thousands of jobs were lost in Gulf's service area, making it difficult for customers to pay their bills and increasing Gulf's bad

debt expense. The impacts to the local economy stalled sales growth and resulted in a decline in Gulf's base revenues. At the height of the financial crisis, the availability of commercial credit was severely limited; however, due to its strong financial position and credit ratings Gulf's access to the capital markets was not disrupted.

Then, to finish the decade, the entire Gulf Coast experienced an unprecedented environmental catastrophe in the form of an enormous oil spill. Prior to the oil spill, the tourism and recreation industry in Northwest Florida showed signs of recovery from the recession. The oil spill interrupted this recovery and resulted in significant reductions in tourism and associated recreational activities.

During this momentous decade, Gulf Power has successfully undertaken and performed its duty to serve the public. Despite these major challenges and associated rising costs, Gulf has maintained system reliability and customer satisfaction.

Q. How has Gulf managed to avoid requesting base rate relief for almost a decade?

A. There are a number of factors that have contributed to Gulf's ability to maintain the same base rates for nearly ten years. The combination of stable economic growth in its service area for most of this period and Gulf's effective management of its resources are primary factors. The regulatory framework in Florida has also been effective in allowing for the

recovery of certain prudent costs without a costly and lengthy base rate proceeding. Finally, Gulf has taken additional steps over the past several years to avoid a rate increase during the recession. All of these factors have allowed Gulf to provide reliable service at a reasonable cost to its customers without a base rate increase for close to ten years.

Q. What additional steps has Gulf undertaken to avoid asking for a base rate increase during the recession?

A. The Company has taken a number of actions over the last several years in an effort to avoid a base rate increase to customers. As Gulf Witness Buck discusses in his testimony, Gulf employs a rigorous annual planning and budgeting process which prioritizes resources and assures that customer needs are met in a cost-effective manner. As discussed by Gulf Witnesses Grove, Moore, and Caldwell, spending for production, distribution, and transmission has been closely managed. At the same time, concentrated efforts have been made to continue to provide reliable electric service to our customers. Gulf's excellent performance statistics are an indication that our system has been well maintained and is operating efficiently and cost-effectively.

As Mr. Grove describes in his testimony, through Gulf's effective ongoing maintenance practices, the Company has been able to extend the expected useful life of many of its generating units by as much as twenty years. This reduces annual depreciation expense and postpones the next need for additional generation resources.

In 2009, Gulf made further efforts to control costs during the economic recession by implementing restrictions on hiring and granting no merit raises to non-union employees.

The Company has done its best to reduce expenses during the difficult economic times that have faced us all the last few years. Now, Gulf finds that additional revenues are necessary to continue to provide quality service and maintain our financial integrity.

II. TEST YEAR

Q. What test year has Gulf used to calculate its proposed rate increase?

A. Gulf has chosen a 2012 projected test year. The test year projections were developed as part of Gulf's 2011 budget process. As described in more detail by Mr. Buck, Gulf's annual budget process produces a budget for the current year and a budget forecast for the four subsequent years. The 2011 "prior year" shown in the MFRs is also the result of the 2011 budget process, while the 2010 "historical year" reflects actual results for that year.

Q. Please explain why 2012 was chosen as the test period.

A. The 2012 test year is the best representation of Gulf's expected future operations. The 2012 test year properly matches Gulf's projected

revenues with the projected costs and investment required to provide service to customers during the period following the effective date of the new, permanent rates in this case. Gulf's use of a projected test year is also consistent with the Commission's long-standing practice to approve projected test years.

The most recent historic year is 2010, which is not representative of expected revenues and expenses on a going forward basis. During 2010, Gulf made significant efforts to curb capital and O&M spending levels to avoid having to request base rate relief during the recession. Also in 2010, base revenues were still in decline from peak levels in 2007. The 2012 revenue forecast is more representative of the revenues for the period the new rates will be in effect. The operating conditions experienced by the Company during the depths of the economic downturn simply are not indicative of future operating conditions.

III. GULF'S RATE REQUEST

Q. What is the amount of base rate relief that Gulf is requesting in this case?

A. Gulf is requesting an annual increase of $93,504,000 in base revenues. This is the amount necessary for Gulf to continue to provide quality service to its customers and give Gulf the opportunity to earn a fair rate of return of 11.7 percent on its common equity, as supported by the testimony of Gulf Witness Dr. Vander Weide.

Q. Why is it necessary for the Company to seek rate relief at this time?

A. As shown on Schedule 2 of my exhibit, since 2007 Gulf's rate base and O&M expenses have increased substantially while base rate revenue growth has stagnated.

During this period Gulf has made significant investment in production assets and transmission and distribution facilities. By 2012 Gulf's rate base will have increased by more than $375 million since 2007. These investments are necessary to maintain system reliability and to meet demand growth.

Similarly, despite extraordinary efforts to hold the line on spending in order to avoid a base rate increase during a recession, Gulf has experienced significant increases in O&M expenses. As Gulf's witnesses testify, many of these O&M cost increases are explained by new regulatory requirements, broader work scope associated with aging equipment, and the replacement of outdated computer applications. Meanwhile, the costs of materials and employee benefits are increasing at rates far in excess of the rate of inflation as measured by the Consumer Price Index (CPI). Gulf has undertaken significant efforts to control insurance, retirement and medical benefit costs, yet all of these necessary expenses have far outpaced the growth of CPI.

The result is a precipitous decline in the Company's earned rate of return. Gulf's currently authorized range for return on equity is from 10.75 percent

to 12.75 percent. As shown on Schedule 3 of my exhibit, Gulf's earned rate of return on equity has been below the bottom of the range since mid-2010. As of March 31, 2011, Gulf's earned rate of return on equity had fallen to 6.83 percent. It is projected to fall to 2.83 percent by year-end 2012, absent base rate relief. Base rate relief is essential for Gulf to sustain its financial integrity, preserve its ability to raise capital on reasonable terms and continue to provide the reliable service that our customers expect.

IV. CREDIT QUALITY & FINANCIAL INTEGRITY

Q. Mr. Teel, please describe the strength of Gulf's financial position since the last rate case and currently.

A. Gulf has maintained a strong financial position, as evidenced by the credit ratings of the three major credit rating agencies. Gulf has sustained long-term debt ratings in the "A" category and short-term debt ratings in the correlating categories since 2002. Schedule 4 of my exhibit is a table depicting Gulf Power's current credit ratings from each of the rating agencies for both long-term and short-term debt.

Q. What rating conventions are used by each of the credit rating agencies to distinguish companies' credit quality?

A. Each credit rating agency has its own conventions; however, each uses a variation of "A" ratings for companies of the highest credit quality. The

rating conventions and scales for long-term debt of all three agencies are shown on Schedule 5 of my exhibit.

Q. What credit ratings does Gulf target?

A. Gulf targets "A" ratings for its long-term debt, specifically A ratings by Standard and Poor's and Fitch, and A2 by Moody's. Gulf targets equivalent ratings for its short-term debt, A-1 by Standard & Poor's and F1 by Fitch. Moody's does not rate Gulf Power's short-term debt.

Q. Why is it necessary to maintain these targeted credit ratings?

A. Maintaining these targeted credit ratings for both long-term debt and short-term debt are critical for Gulf and its customers. Strong credit ratings ensure access to capital and allow Gulf to provide reliable service at the lowest financing costs possible. An electric utility's obligation to serve requires continuous access to capital markets to fund the maintenance of and investment in the assets needed to reliably generate and deliver electricity.

Q. Please explain the importance of long-term and short-term debt.

A. Long-term debt is appropriate for the financing of long-lived assets. Strong credit ratings for long-term debt are especially important during a period of significant investment. As shown on Schedule 6 of my exhibit, Gulf's capital expenditure requirements since 2008 are substantially above historic levels. In both 2012 and 2013, Gulf's projected capital spending is

in excess of $400 million, which is larger than any other year in Gulf's history.

Short-term debt, generally commercial paper, is typically used to meet shorter term funding requirements. Short-term debt is integral to financing Gulf's operations, as it is less expensive than long-term debt and does not require a commitment to interest costs over an extended period of time. Thus, short-term debt lends flexibility in financing the business. Strong credit ratings for short-term debt ensure access to the commercial paper markets. The ability to access the commercial paper markets is crucial to Gulf, as short-term funding needs can vary dramatically with volatile fuel prices and seasonal changes in customer demand. Companies with credit ratings lower than those targeted by Gulf may experience difficulty in securing short-term funding.

Q. Please provide an example of the value to electric utilities of strong credit ratings.

A. The value of strong credit ratings was clearly demonstrated during the recent financial crisis. During the height of the credit crisis, access to capital markets was restricted.

In his report, "The A Rating" published in the May/June 2009 issue of Edison Electric Institute's Electric Perspectives, Mr. Steven M. Fetter, President of Regulation UnFettered, former Chairman of the Michigan

Public Service Commission, and former head of the Global Power Group at Fitch Ratings, stated:

> . . . the current economic turmoil has resulted in some utilities within the BBB category experiencing difficulty in accessing the capital markets. Even when capital is available, it is often at significantly higher costs and upon less favorable terms and conditions.

Due to our ability to maintain the targeted "A" ratings, Gulf did not experience these difficulties in accessing capital during this tumultuous period.

Q. What factors are considered by rating agencies in determining Gulf's credit ratings?

A. The rating agencies consider both quantitative and qualitative factors in determining Gulf's credit ratings. The quantitative factors, as expressed by financial metrics, generally assess a company's ability to meet debt obligations considering its cash flows from operations, interest expense, and levels of debt. The qualitative factors consider operational and other business risks.

Of the three agencies, Moody's Investors Service provides the most definitive explanation of the factors considered to determine a utility's credit ratings. Moody's lists four key rating factors in "Regulatory Frameworks – Ratings and Credit Quality for Investor-Owned Utilities",

published June 18, 2010. These factors are: (1) regulatory framework, (2) ability to recover costs and earn returns, (3) diversification of fuel sources, generating plants, regulatory regimes, and geographic regions, and (4) financial strength and liquidity.

Q. Have Gulf's credit ratings remained on target?

A. Gulf's credit ratings by Standard & Poor's and Fitch have remained on target; however, Moody's downgraded Gulf's long-term debt rating from A2 to A3 on August 12, 2010. While Moody's does not rate Gulf's short-term debt, this long-term debt rating could impact Gulf's ability to access the commercial paper markets if one of the other rating agencies downgrades Gulf's short-term debt rating.

Q. What factors were cited by Moody's for the downgrade?

A. Moody's stated "Gulf Power's A3 senior unsecured debt rating reflects cash flow coverage metrics that are weak for its rating, higher construction expenditures for environmental compliance, and a decline in the historically supportive Florida regulatory environment." Gulf Power received an "A" rating on only one of the three primary qualitative factors and only one of the five financial metrics used by Moody's in determining their credit rating for regulated electric and gas utilities. Moody's cited additional debt leverage and further deterioration of metrics as risks to the current rating. A copy of Moody's Credit Opinion dated August 13, 2010 is attached as Schedule 7 of my exhibit.

Q. Are there any indications that either of the other two major credit rating agencies shares any of Moody's concerns about Gulf's credit quality?

A. Yes. With respect to the regulatory environment, Fitch stated in its report of October 5, 2010 on Gulf Power:

> . . . political interference in the face of the economic slowdown led to a marked regulatory environment shift in 2010. Recent decisions for unaffiliated Florida utilities have been populist, with below average allowed return on equity and base rate increases that were significantly lower than amounts requested....Fitch expects the regulatory climate in Florida to slowly return to normal after this election year and as the state's economy slowly begins to recover.

Copies of the most recent credit opinions by Fitch and Standard & Poor's are attached as Schedules 8 and 9 of my exhibit.

Q. What would be the impact on Gulf's credit quality without adequate rate relief?

A. The quantitative and qualitative factors considered by rating agencies would be adversely affected. The Company's financial metrics would deteriorate. Furthermore, allowing the returns to remain at levels below those required by investors would likely increase the agencies' concerns

about the regulatory environment in Florida. The Company's ability to maintain the targeted "A" credit ratings would be jeopardized.

Q. How would eroding credit quality affect Gulf and its customers?

A. Credit quality is a key indicator of a company's financial integrity. A weakened financial position will ultimately hinder Gulf's ability to access capital at reasonable terms. In order to sustainably provide reliable service to its customers, a utility must maintain access to capital at all times. As discussed earlier, the Company is in the midst of a significant capital investment period. This heightens the importance of maintaining its financial integrity and access to capital.

V. CAPITAL STRUCTURE AND COST OF CAPITAL

Q. What capital structure is Gulf targeting?

A. Gulf is targeting a capital structure of 45 percent common equity and 55 percent debt and preference or preferred stock.

Q. Is this the same capital structure targeted in the last rate case filing?

A. Yes.

Q. Why is Gulf's capital structure appropriate?

A. Gulf has been successful in maintaining its strong financial position and targeted credit ratings with this capital structure. Based on current

projections, and with adequate rate relief, Gulf believes it will be able to sustain its financial integrity with this structure.

Q. What cost of equity is the Company seeking in this case?

A. As Dr. Vander Weide indicates in his testimony, a fair rate of return on common equity is 11.7 percent.

Q. What is Gulf's cost of debt?

A. As shown on Schedule 12 of Mr. McMillan's Exhibit RJM-1, Gulf's embedded cost of long-term debt is 5.48 percent. For the test year, we project that our cost of short-term debt will average 2.12 percent.

Q. What is Gulf's weighted average cost of capital for ratemaking purposes?

A. As shown on Schedule 12 of Mr. McMillan's Exhibit RJM-1, Gulf's weighted average cost of capital is 7.05 percent when taking into account both investor sources of capital (common equity, preference stock, long-term-debt and short-term debt) and other sources considered for ratemaking purposes (customer deposits, deferred taxes and investment tax credits).

Q. Is the weighted average cost of capital proposed by Gulf appropriate in this case?

A. Yes. The weighted average cost of capital of 7.05 percent proposed by Gulf, including Dr. Vander Weide's recommended return of 11.7 percent

on the common equity component, is cost efficient and fair for both investors and customers.

VI. PARENT DEBT ADJUSTMENT

Q. Please provide a brief overview of Commission Rule 25-14.004 relating to the parent debt adjustment.

A. The parent debt adjustment rule was adopted by the Commission in 1983. For ease of reference, I have included a copy of that rule as Schedule 10 of my exhibit. This rule applies in rate proceedings where (1) a parent-subsidiary relationship exists, (2) the parent and subsidiary participate in filing a consolidated tax return, and (3) funds provided by parent debt have been invested in the equity of the regulated subsidiary. If all three factors are present, the rule provides a formula for reducing the subsidiary utility's income tax expense to reflect the tax effect of the parent debt that is invested in the equity of the subsidiary.

Q. In calculating Gulf's income tax expense for the test year, Mr. McMillan does not make a parent debt adjustment under Commission Rule 25-14.004. Why isn't such an adjustment required?

A. The rule does not require an adjustment in this case because only two of the three factors in the rule are met. Gulf is a subsidiary of Southern Company (Southern) and it participates in filing a consolidated income tax return; thus the first two factors are met. The third factor is not met

because no funds provided by Southern Company debt have been invested in the equity of Gulf.

Q. Doesn't subsection (3) of the rule create a presumption that Southern's equity investment in Gulf is supported by debt based on the ratio of debt in Southern's overall capital structure?

A. Yes, but the rule expressly states that the presumption is rebuttable. The presumption can be rebutted – and the rule does not require an adjustment – if the utility shows that the parent's equity investment did not come from debt issued at the parent level. In this case, the facts surrounding Southern's equity investment in Gulf are sufficient to rebut the presumption.

Q. What are the facts which rebut the presumption?

A. As shown on Schedule 11 of Exhibit RST-1, during the period from January 2003 (the middle of the test year in Gulf's last rate case) to March 2011:

- Gulf has received $459.0 million in equity investment from Southern.
- Gulf has paid $655.8 million in dividends to Southern.

Gulf's dividend payments are sufficient to support 100 percent of Southern's equity investments, as represented in Gulf's financial statements, and still result in a net payment of $196.8 million from Gulf to Southern.

Gulf has been a net returner of capital to Southern, not a net recipient. Thus, Gulf itself has effectively provided the funding for Southern's equity investment in Gulf with its own internally generated funds.

Q. If Gulf's internally generated funds have been the source of the common equity investment, why have both the common stock and paid-in capital portions of common stockholder's equity increased?

A. The increases in common stock and paid-in capital result from the accounting effect of Gulf paying dividends while also accepting equity investment from Southern.

Q. Please explain the accounting effect.

A. The effect of Gulf paying dividends to Southern and Southern subsequently returning portions of those dividends through equity investments in Gulf is that the internally generated funds are moved from retained earnings to common equity or paid-in capital on the balance sheet. Assume, for example, that Gulf pays $10 million of dividends to Southern. This payment reduces Gulf's retained earnings by $10 million. When that amount is subsequently reinvested by Southern, Gulf's paid-in capital increases by $10 million. Gulf's total common equity is the same as before the dividend, but the $10 million is now reflected as parent investment rather than retained earnings. However, this accounting treatment does not change the fact that Gulf's internally generated funds, not Southern, are the underlying source of these common equity dollars.

Because Southern is not the source of the funds, Southern's debt cannot be a source of Gulf's paid-in capital.

Q. What would be the effect under the parent debt rule if, rather than paying dividends to Southern out of internally generated funds that are then returned in the form of equity investment, Gulf had simply retained those internally generated funds?

A. There would be no additional parent investment on Gulf's financial statements for the period January 2003 through March 2011. The presumption in subsection (3) would more clearly be rebutted. Under section (4) of the parent debt rule, the retained earnings balance would be treated as internally generated funds, not parent investment, and would not be a basis for imputing any additional income tax expense. The fact that Gulf's dividend practice changes the accounting presentation should not trigger income tax imputation when Gulf has shown that its dividends more than support Southern's equity investment; thus, parent debt cannot be a source of capital for Gulf.

Q. Schedule 11 of your exhibit shows that in 2007, 2009, and 2011 (through March) Southern made equity investments in Gulf that were not supported by dividends paid in those years. Does this mean that Southern's capital contributions in those years came from some source other than Gulf's internally generated funds?

A. No. This is merely a timing difference in cash flows. Gulf pays quarterly dividends to Southern. Southern only provides funds as necessary to fund

Gulf's business. These cash exchanges may or may not offset each other in any given calendar year. Most importantly, the cash generated by Gulf has been more than sufficient to cover all of Southern's capital contributions since the last rate case and Gulf, on a cumulative basis, has been a net returner of cash to Southern at all points in time over this period.

Q. Does Gulf forecast additional dividends paid to Southern and additional equity investments in Gulf by Southern for the remainder of 2011 and 2012?

A. Yes; however, Gulf will also be a net returner of cash to Southern during this period.

Q. Isn't it true that dollars are fungible, so Gulf cannot trace the exact dollars invested in Gulf back to dollars that resulted from dividends paid by Gulf?

A. This may be true as a purely theoretical matter, but the rule cannot properly be interpreted to require such an exact tracing. If exact tracing were required, the presumption in the rule would be effectively irrebuttable. This cannot be what the Commission intended.

Q. You have focused on the period since Gulf's last rate case. How can the Commission be assured that the Southern debt outstanding at the time of the last rate case did not support its equity investment in Gulf at that time?

A. First, prior to the last rate case, Southern issued long-term debt during the growth of Southern Electric International, which was ultimately spun-out of

Southern in 2001 as Mirant Corporation. Second, Southern's commercial paper borrowings, both now and at the time of the last rate case, are used to support parent-level expenditures. They are not used as a source of funds for investments in the operating companies. Finally, the Commission did not find it necessary to make a parent debt adjustment during Gulf's last rate case.

Q. What are the financial implications to Gulf of making the parent debt adjustment?

A. The parent debt adjustment would have two primary effects on Gulf. First, imputing to Gulf the tax benefits of parent company debt would be effectively assuming the Company has more debt in its own capital structure than actually exists. The Company's capital structure already has a relatively low equity ratio and includes as much debt as is practical to maintain its financial strength. The parent debt adjustment would assume there are tax benefits of parent company debt accruing to Gulf without recognizing the associated financial risk in Gulf's capital structure. Gulf, appropriately, has not imputed parent company debt in its capital structure and it would be inconsistent to impute any tax benefits associated with such debt.

Second, by artificially reducing the federal income tax expense used to establish Gulf's required rate relief, the adjustment would decrease the effective return on equity by approximately 25 basis points below the level the Commission otherwise determines to be appropriate.

The Commission should consider these impacts of applying the parent debt rule when weighing the evidence that Gulf has presented to rebut the presumption that Southern's investment in Gulf is funded in part by parent debt.

Q. Has the Commission made a parent debt adjustment in any of Gulf's prior rate cases?

A. No. The rule was adopted in 1983. Since that time Gulf has had three rate cases before the Commission, and the Commission has never made a parent debt adjustment pursuant to Rule 25-14.004.

VII. SUMMARY

Q. Please summarize your testimony.

A. Gulf Power is committed to meeting the needs of our customers and investors and strives to maintain low rates, high quality service, and excellent customer satisfaction ratings. Despite Gulf's continued efforts to control costs and keep expenses low to avoid the need for base rate relief, there has been an increase in the cost of providing electric service since the Company's last base rate increase in 2002. These increases in costs are necessary to enable the Company to maintain reliability and meet the service expectations of our customers. Other witnesses address the details of the capital additions over the past ten years and the factors

contributing to an increase in O&M expenses. Increases in both areas are necessary in order to ensure that Gulf can continue to provide dependable and reliable service to our customers. These increased costs have grown faster than Gulf's base rate revenues, resulting in a declining net operating income.

Under present retail rates, the projected return on average common equity for the test year is 2.83 percent, which is significantly below the 11.7 percent determined by Dr. Vander Weide to be appropriate for Gulf Power. Such a low return would leave the Company in a weakened financial position. In order for Gulf to attract capital on reasonable terms and continue to meet the needs of our customers, the Company must maintain its financial integrity. Therefore, based on the revenue deficiency calculated for the test period, Gulf is requesting an annual increase of $93,504,000 in our base rate retail revenues.

Q. Does this conclude your testimony?

A. Yes.

BY MR. MELSON:

Q. And you had an exhibit to your direct testimony identified as RST-1 which has been now identified as Hearing Exhibit Number 110. Does Schedule 1 of that exhibit list the MFR schedules that you are sponsoring or cosponsoring?

A. Yes, it does.

Q. And there are a total of 11 schedules in that exhibit; is that right?

A. That is correct.

Q. Do you have any changes or corrections to your exhibit?

A. I do not.

MR. MELSON: Mr. Chairman, it has been identified as 10. Do you want us to move it now or at the conclusion of the witness's testimony?

CHAIRMAN GRAHAM: At the conclusion.

BY MR. MELSON:

Q. Mr. Teel, would you please give us a brief summary of your testimony?

A. Yes, I would.

Commissioners, Gulf Power needs rate relief now to continue to provide the level of service to our customers that they've come to expect and deserve. The purpose of my testimony is to explain the importance of

the company's financial integrity to our customers, to present our capital structure, our cost of equity, and finally, to explain the inappropriateness of making the parent debt adjustment to Gulf Power's income tax expense.

Since 2007, Gulf Power's financial strength had been challenged as our returns have declined. By mid-2010, we fell below our current authorized return range, and now we've fallen into levels far below those required by our investors, by anyone's estimation. Our returns have already fallen below 6 percent, and absent rate relief, they are projected to fall below 3 percent by the end of the proposed test year of 2012 -- I'm sorry, the test year of 2012.

As an electric utility, we have the responsibility, in fact, the obligation to serve. Producing and delivering electricity requires significant investment in -- significant and continuous investment in and ongoing maintenance of our power generation, transmission, and distribution systems. Despite a reduction in overall deman over the past several years, we simply do not have the discretion to forgo those capital investments or maintenance programs, because we must be prepared to meet our obligation, not just today, but next year, five years from now, and far

beyond.

The costs of operating our business have escalated with the price of materials and equipment. At the same time, we have already entered into a period of significant investment that is far greater than anytime in Gulf's history. For these reasons, maintaining the financial strength of the company is as important as ever. We need investors to provide the financing necessary to make these capital improvements, and in turn, we must be able to ensure those investors that we will provide them with sufficient returns.

Credit ratings are an important measure of the financial strength, and Gulf has maintained strong credit ratings over the last 10 years. However, in 2010 we did suffer a downgrade. Further downgrades could impact the company's access to capital and will almost certainly increase our debt costs. Without rate relief, Gulf's weakening financial position will jeopardize our credit ratings and ultimately our ability to attract capital on reasonable terms.

Gulf is proposing a capital structure made up of 45 percent equity and 55 percent debt or preference stock. This is consistent with the capital structure that was approved in our last rate case. As our expert witness Dr. Vander Weide will testify, we're seeking a

return on equity of 11.7 percent.

Finally, in my testimony I rebut the presumption that a parent debt adjustment to income tax expense should be made to Gulf's revenue requirements. Gulf has avoided a rate increase now for almost 10 years, and most significantly, over the last several years, as our customers have been sufferings the effects of the Great Recession. We need this increase now to sustain the financial strength that is necessary to continue to provide this service to our customers safely and reliably, today and the future.

Thank you. That concludes my summary.

MR. MELSON: We tender Mr. Teel for cross-examination.

CHAIRMAN GRAHAM: Mr. McGlothlin.

CROSS-EXAMINATION

BY MR. McGLOTHLIN:

Q. Mr. Teel, I'm Joe McGlothlin with the Office of Public Counsel. Good morning.

A. Good morning.

Q. I'll begin with what should be an easy one. We've provided you with a document which is Gulf Power's answer to Citizens' Second Set of Interrogatories, Item Number 153. Do you have that in front of you now?

A. I'm sorry. I do not.

Q. Okay. We'll catch up to you in a second. I thought that was in the process. It will just take a moment.

A. Thank you.

MR. MELSON: Could you give us that reference one more time? I didn't catch the number. I'm sorry.

MR. McGLOTHLIN: It's Citizens' Interrogatory 153, the second set. And we don't need a number, because this has been assigned Number 114 by stipulation.

CHAIRMAN GRAHAM: Okay.

BY MR. McGLOTHLIN:

Q. Have you had a chance to look at this document, sir?

A. Yes, I have.

Q. And in the answer there's a reference to Witness Teel. Do I assume correctly that you were involved in its preparation?

A. Yes, I am Witness Teel. This calculation was actually performed by Mr. McMillan.

Q. I see. Are you familiar with the calculation?

A. Yes, I am familiar with it.

Q. As I understand the answer to the interrogatory, first there's the caveat that Gulf Power

disagrees with the applicability of the parent debt adjustment, but then there's a calculation that quantifies the impact on return on equity if the Commission agrees with Public Counsel's assertion that it should be made; correct?

A. Yes, that is what is here.

Q. And do I understand correctly that this calculation indicates that the impact on jurisdictional ROE would be approximately 25 basis points?

A. Yes, based on this calculation. However, since then, Mr. McMillan has recognized an error in his formula and I believe in his rebuttal testimony he has revised this calculation.

Q. So this calculation came from Mr. McMillan and not Mr. Teel, in other words?

A. Mr. McMillan performed this calculation.

Q. I see. So we should take that up with Mr. McMillan?

A. Yes, sir.

Q. It wasn't as easy as I thought.

Well, I have some questions that relate to your prefiled testimony, and the first one relates to page 5. You're describing the impacts of storms on the distribution system, and you refer to the fact that mandated storm hardening requirements have been enacted,

and those, of course, require the company to incur costs in the process of implementing those hardening measures; correct?

A. That is correct. There are incremental costs.

Q. Would you agree with me that one reason to take on the measures of the storm hardening is the expectation that once hardened, the system will be more resistant to storm damage if another storm occurs?

A. Yes, I would agree that's the objective.

Q. And if that objective is achieved, would you agree with me that customers will see a benefit in the form of fewer storm repair costs than would otherwise be the case?

A. Yes, again, that would be the objective. However, we do not have the experience yet to know what the impact is of the storm hardening initiatives. And while we hope, we certainly hope that this investment will mitigate the costs of storm damage for our customers, we simply don't have the experience yet to know exactly what that impact will be.

Q. Well, if there's no advantage in the form of fewer damages and fewer costs, then this is not money well spent, is it?

A. I believe there are other benefits to some of these initiatives, and I believe Witness Moore could

probably be able to give you some more details of some of the benefit of the storm hardening initiatives.

Q. Now look at page 6, if you would. You say there are a number of factors that have contributed to Gulf's ability to maintain the same base rates for nearly 10 years. Would you agree with me that if rates are designed in a manner such that higher costs are accompanied by increased revenues, that relationship mitigates any impact on the earned rate of return?

A. Yes, I would agree that that would be ideal if your base revenues grew at the same rate. What we have seen most recently is that that has not been the case.

Q. Recent experience doesn't mean, though, that the impact of time on base rates is necessarily to erode the earned rate of return, does it?

A. I'm sorry. Would you repeat that question.

Q. Well, let me rephrase. You were here when I asked Mr. Crosswhite some questions about the discretionary accruals; correct?

A. Yes, I was.

Q. And you're familiar with the fact that those discretionary accruals are made in years in which Gulf would otherwise exceed the maximum of its approved return on equity?

A. Yes, I believe those discretionary accruals

are made when we have the financial means.

Q. Financial means measured in terms of earnings that would otherwise exceed the maximum of your authorized range?

A. Commissioners, I'm not familiar with the statute in terms of exactly what the conditions would be to make a discretionary accrual.

Q. Okay. You are aware that the maximum of Gulf Power's authorized range as set in the rate case 10 years ago is 12.75 percent; correct?

A. Yes, I am aware of that.

Q. Turn to page 15, if you will. There are references there to Florida's regulatory environment and the metrics that would be used to assess Florida's regulatory environment. You're familiar with that portion of your testimony?

A. Yes, I am.

Q. In terms of the metrics that analysts and other observers would apply to the regulatory framework and the regulatory environment, would you consider the authorized fuel cost recovery clause as one portion of that regulatory environment?

A. Yes. And let me state that a little bit differently. The assessment, the regulatory environment is not necessarily a metric in terms of there being a

score in every case associated with that. However, yes, I think that the cost recovery clauses, appropriately so, as they've been established here in Florida recognize that there are certain costs that may be imposed or are volatile that can impact the cash flows of a utility and that timely recovery of those costs is appropriate. But, yes, I believe that that is something that the credit rating agencies view as supportive.

Q. And with respect to the particular type of fuel cost recovery clause that has been authorized for utilities' use in Florida, you're aware of the fact that the utilities are authorized to project their costs for the coming year and then effectively collect their costs on a current basis at the same time they're being expended?

A. Yes, that is my understanding, that the fuel rate also is based on projected fuel costs for the next year. That is a component.

Q. Would you expect analysts and other observers to see that as a favorable aspect of the environment, of the regulatory environment?

A. Yes. As I've said, I believe that the credit rating agencies do view the cost recovery clauses in Florida as being credit supportive.

Q. And the particular clause that's authorized

for use in Florida contains a true-up feature, does it not?

A. Yes, it does.

Q. Would you expect analysts and other observers to regard the fact that there's a true-up mechanism designed to ensure that there is precision with respect to the amount of costs incurred and the amount of costs recovered to be a favorable aspect of the regulatory environment?

A. I think, yes, they would. They would view that as being favorable to recover the prudent costs associated with producing electricity, being the fuel.

Q. Gulf Power Company has incurred in the past and is expected to incur in the future significant compliance costs associated with environmental regulations, is it not?

A. In fact, yes, we have incurred significant compliance costs. Over the past 10 years, we have invested more than $900 million in environmental controls to comply with environmental regulations. And, yes, there is the specter that more investment is on the way.

Q. You're familiar with the fact that in Florida, regulated utilities are authorized to recover the costs of environmental compliance through an environmental

cost recovery clause?

A. Yes, I'm also familiar with that.

Q. And that is done on a projected basis and collected on a current basis?

A. This is also true.

Q. And does it incorporate a true-up mechanism similar to the one in the fuel clause?

A. Yes, it does incorporate a true-up.

Q. Do you think analysts observing the regulatory framework and environment in Florida would regard the ability of Gulf and other regulated utilities to collect the full costs of environmental compliance on a current basis with the true-up mechanism to be a favorable aspect of the regulatory framework?

A. Yes. Again, I think the credit rating agencies do view the cost recovery clauses as being credit supportive, and they have recognized that in their assessment of the Florida regulatory environment and that framework as being historically supportive.

Q. Would the same be true of the conservation cost recovery clause and the associated ability of the utility to project the costs of conservation programs and collect them with a true-up mechanism?

A. That is also true.

Q. What about the ability of a utility to collect

the costs it incurs through purchased power contracts through the cost recovery mechanism on a projected basis subject to a true-up mechanism? Would that be viewed by a rating analyst and other observers as a favorable aspect to utilities?

A. I think they would view that as being a favorable respect, but also from the respect of encouraging the utilities to do what is the best interest of the customers in terms procuring the necessary generation capacity. So, yes, I think that is also a very appropriate and good mechanism here in Florida.

Let me interject here and explain a little bit about what's in my testimony, if I could, Commissioners.

Q. I'm sorry, sir. You're answering my questions on cross-examination, and you answered the last one.

What about the fact that --

CHAIRMAN GRAHAM: If I can, I'll just explain. The way it's laid out is that you're allowed to answer the questions yes or no and give a brief explanation. I normally let the witness editorialize as long as they want until there's some objection by the person asking the questions. So you just need to make sure that you just answer the questions and be brief.

THE WITNESS: Yes.

CHAIRMAN GRAHAM: Mr. McGlothlin, I apologize.

BY MR. McGLOTHLIN:

Q. The questions relate to references to Florida's regulatory environment. And earlier you noted your disagreement with the term "metric" because in your view that connotes a score of some kind, and I've tried to amend my questions accordingly. But so far, would you agree with me that I've enumerated several aspects of the regulatory environment in Florida that analysts should view as favorable in that they reduce the risk of the company?

A. Yes. The cost recovery clauses do mitigate some of the risk associated with cash flows and the timely recovery of those costs that are largely beyond our control through imposition of environmental regulations or changes in commodity prices.

In terms of the regulatory environment, yes, I don't think that has changed with respect to the cost recovery clauses. The concern about the regulatory environment in Florida has been a result over the last couple of years, and frankly, some recent -- some decisions in some rate cases. And each of the credit rating agencies has expressed some concern that although historically the Florida regulatory environment,

including the framework, which includes the cost recovery clauses, has been very credit supportive. However, they have some concern now that there has been some deterioration in that. And while they are optimistic that this is going to improve, as we are, that has been the concern. The cost recovery clauses have not been at issue, and they do view those as being credit supportive.

Q. And we'll get to the concerns that you just identified in due course.

In this case, did Gulf Power apply for an interim increase in revenues?

A. Yes, in fact, we did, and it was approved.

Q. And you're aware that the ability of the company to apply for and receive an interim increase is provided by statute?

A. Yes, that is my understanding.

Q. Would you believe that rating analysts and other observers would regard the statutory mechanism that calls for the Commission to respond to a request for an interim increase within 60 days of filing to be a favorable aspect of the regulatory environment in Florida?

A. Yes, I believe they would. I think they would also recognize that that interim rate relief was

necessary. Even with that interim rate relief, we have already fallen below 6 percent on our returns today.

Q. You're aware of the fact that under the Florida Statutes, this particular proceeding is governed by a statutory clock, if you will, that sets deadlines for resolution of the request that Gulf filed?

A. Yes, that is my understanding as well.

Q. Would you regard -- do you believe analysts would regard measures such as that designed to limit regulatory lag would be viewed upon as favorable?

A. Limiting regulatory lag is favorable and I think desirous of most regulatory commissions.

Q. Did Gulf Power base its request on a projected test period in this case?

A. Yes, we did.

Q. Would you regard that as a form of forward-looking assessment of the company's requirements?

A. Yes, I would.

Q. Would you regard the use of a test period as an effort by the Commission to ensure that the rates it fixes in this case are designed to operate within the time frame in which they would be effective?

A. That's correct. My understanding is that is the purpose of the test year.

Q. As compared to regulators that use historical periods, would you regard -- do you think an analyst would regard the use of a projected test period as a favorable aspect of the regulatory environment in Florida?

A. Yes. I think that is more appropriate.

Q. Now, at page 15, you refer to a decline in the historically supportive Florida regulatory environment, and on page 16, you quote from the Fitch report that's attached to your testimony as an exhibit, do you not?

A. I'm sorry. Did I miss a question?

Q. At page 16, you quote from the Fitch report that is attached to your testimony as an exhibit, do you not?

A. Yes, I do.

Q. The quotation reads, "Political interference in the face of the economic slowdown led to a marked regulatory environment shift in 2010. Recent decisions for unaffiliated Florida utilities have been populist, with below average allowed return on equity and base rate increases that were significantly lower than amounts requested." Do you understand this passage in the Fitch report to refer to the FPL and Progress Energy cases that were decided in that time frame?

A. Yes, I believe these comments were made

following those rate cases.

Q. The author of that report refers to the issuance of a below average rate of return. Do you think the responsibility of a regulator -- and I'm being more abstract now, not this regulator and not a particular case. But generally speaking, do you think the responsibility of a public service commission that has jurisdiction over a regulated utility is to ensure that it approves average rates of return?

A. No, I do not. I think what is appropriate is to allow a return that an investor requires at that point in time.

Q. Would you agree with me that, for instance, hypothetically speaking, all other things being equal, a utility that has an equity ratio of 60 percent would be less risky than a utility with an equity ratio of 44 percent?

A. Yes. I believe financially, yes, there would be less risk associated with a higher equity ratio.

Q. And would you expect the regulators to take such differences in risk into account when arriving at the return on equity the regulator deems appropriate for the utility under review?

A. Could repeat that question, please?

Q. Yes. I believe you agreed with me a moment

ago that all other things being equal, hypothetically speaking, hypothetical utilities, if one utility has an equity ratio of 60 percent and another has 44 percent, the utility having the 60 percent equity ratio would have lower financial risk than the other utility; correct?

A. Yes, the higher the equity ratio, the lower the financial risk.

Q. And would you expect a regulator to take that difference in the risk profiles into account when determining the appropriate return on equity that each should be awarded?

A. We're getting into, I believe, the expertise of our cost of equity witness here. These questions will be better answered by Dr. Vander Weide with his expertise.

Q. You don't believe you would have the wherewithal to answer that question?

A. No. We hired Dr. Vander Weide as our cost of equity witness, and these questions are more appropriately directed to Dr. Vander Weide.

Q. Well, I'll move away from the hypothetical. Would you expect the regulator, generally speaking, to try to assess the risk profiles of the utilities over which it has jurisdiction and take the differences into

account when arriving at authorized returns on equity for each of them?

A. As the Commission considers the appropriate return on equity, they will consider, I believe, the testimony of the cost of capital experts. The basis of that should be the return on equity and cost of equity of comparable companies, comparable risks.

Q. In the same quotation, the author of that report says that recent decisions involved base rate increases that were significantly lower than amounts requested. Do you see that passage?

A. Yes, I do.

Q. Do you think the fact that a utility asks for X dollars and receives something less than that is necessarily an indication of a deteriorating regulatory environment?

A. What a rating agency, an investor would consider as a deteriorating regulatory environment is an assessment that a utility was not afforded the ability to recover its costs on a timely basis and an opportunity to earn a fair return.

Q. Would you agree with me then that the fact that the utility did not receive dollar for dollar 100 percent of its request is not necessarily an indication of a deteriorating regulatory environment?

A. I can't answer that question with respect to prior decisions. What I reference in my testimony is a quote by Fitch Rating Service indicating that the companies were not permitted to receive the amount -- a low percentage of the amount that they requested and that they testified that they needed to operate their business.

Q. Yes, that's what it says. My question to you is whether your view is that that's an indication of something that has gone amiss in a regulatory environment.

A. I don't have enough knowledge of those cases myself to have a view on the amount of cost recovery they were afforded.

Q. Let's put it this way. Hypothetical example, hypothetical utility, hypothetical regulator. Utility A files a request for an increase in revenues of $100 million annually. Based upon analyses presented in evidence, the consensus of the regulator is that the utility should receive $80 million, not 100, but 80. In that situation, should the regulator award $100 million based on the proposition that a Wall Street analyst is looking at this as something of a pass/fail situation, that they asked for this, but they got less, therefore, it's a negative comment? Or should the regulator base

its decision based on what it necessary the fact and the law support?

A. The regulators should make the decision based on the amount of rate relief that they deem to be necessary to provide service.

Q. There's a reference to the economic slowdown as one consideration that led to the situation that the analyst is commenting on. Would you agree with me that some aspects of an economic slowdown would be relevant to both a utility's request and the regulator's treatment of that request?

A. The economic slowdown has resulted in declines in our base revenues. Ultimately, a utility needs to be provided with the rates that support their ability to provide service to the customers, and that is what we've asked for.

Q. Would you agree with me that in some respects, an economic slowdown could also lead to lower costs being incurred by the utility, for instance, fewer numbers of new customers being hooked up?

A. Yes, that would be one aspect.

Q. Would you agree with me that an economic slowdown as another example could lead to a decline in the growth of peak demand, enabling the utility to postpone or defer the construction of expensive

generation?

A. Yes, that is true, and I think that has been reflected in our projections of our site plan.

Q. So then would you agree with me that an economic slowdown is not necessarily irrelevant to either the utility's request or the regulator's treatment of that request?

A. I would agree that the impacts of the economic slowdown on the utility is relevant.

Q. Now, you agreed with me that the author of this report was commenting on the FPL rate case and the Progress Energy rate case of a couple of years ago; correct?

A. These reports were published following those rate cases.

Q. Now, did you follow those cases at all?

A. I was not at Gulf Power during that time, so, no, I did not follow them closely.

Q. Well, I'll represent to you that in general terms, Florida Power & Light Company requested an increase of in excess of $1 billion over a two-year period, a primary increase and then a step increase in that case, and that the decision awarded FP&L an increase of $75 million. Do you think that is the relationship between amounts asked and awarded that the

author is commenting on here?

A. Yes, I believe that's the case.

Q. Have you followed what your peer utilities have accomplished in terms of earnings reports since the time the FPL decision was made?

A. I do periodically review the surveillance returns, yes.

Q. Are you aware that with the increase of $75 million, FPL for the period calendar year 2010 earned the maximum of its authorized range, 11 percent, in every month of that period?

A. No, I'm not that familiar with those numbers.

Q. Well, we've passed out some numbers for you to see them.

CHAIRMAN GRAHAM: Do you need an exhibit number on this one, Mr. McGlothlin?

MR. McGLOTHLIN: Yes, we do.

CHAIRMAN GRAHAM: We will give this --

MR. SAYLER: Mr. Chairman, it should have the description "FPL PSC Earnings Surveillance Reports."

CHAIRMAN GRAHAM: We'll give this 173.

MR. McGLOTHLIN: I'm sorry, sir. Would you repeat that?

CHAIRMAN GRAHAM: Exhibit Number 173.

MR. McGLOTHLIN: 173.

CHAIRMAN GRAHAM: And what did you say for the short title?

MR. McGLOTHLIN: FPL PSC Earnings Surveillance Reports, December 2010, June 2011, and July 2011.

(Exhibit Number 173 was marked for identification.)

MR. MELSON: Did you get us copies, Joe? I don't have a copy.

THE WITNESS: I don't have a copy.

MR. McGLOTHLIN: I thought we handed it out. Could we take a moment in place and see where we are in passing it out?

MR. SAYLER: I think we passed them all out.

THE WITNESS: I'm sorry. I do have this.

MR. McGLOTHLIN: Do you have it, Rick?

MR. MELSON: Yes. Thank you.

BY MR. McGLOTHLIN:

Q. Are you somewhat familiar with the format of the surveillance earnings report?

A. Somewhat, yes.

Q. I'll refer you to the entry that is captioned "Return on common equity, FPSC adjusted," and ask you to agree with me that for calendar year 2010 and for the two months in the summer of 2011, these earnings reports

reflect that FPL earned 11 percent.

A. Yes, that's the number represented here.

Q. And are you aware that that's the ceiling of their authorized range?

A. I'm sorry. Could you repeat that?

Q. Are you aware that that 11 percent is the ceiling of their authorized range?

A. I'm sorry. You said that too quickly for me.

Q. Are you aware that 11 percent represents the ceiling of FPL's currently authorized range?

A. Oh, I'm sorry. I missed the "ceiling." Yes.

Q. FPL has consistently earned returns on equity at the top of their authorized range since the rate case decision in which they were granted a $75 million increase. What do you think their financial situation would look like if instead the Commission had granted $1 billion of an increase?

A. The cash flows would be better.

Q. And would the result also have been more constructive?

A. I can't answer that.

Q. Would it have been less populist?

A. I can't give you an opinion on this.

Q. At page 16, sir, you say that allowing returns to remain at levels below those required by investors

would likely increase the agencies' concerns about the regulatory environment in Florida; correct?

A. Yes.

Q. Now, with respect to returns required by investors, your witness says that should be 11.7 percent; correct?

A. Yes, he does.

Q. And you're aware that our witness, Dr. Woolridge, asserts that 9.25 percent is adequate to serve that role; correct?

A. Yes, I am.

Q. And that makes it a contest, doesn't it?

A. They're a bit apart, yes.

Q. And that contest is going to be determined by the Commission based upon the evidence presented; correct?

A. That's correct.

Q. One more short series of questions, and this series relates to the parent debt adjustment. If you'll look at the Schedule 11 of RST-1, as I understand it, this schedule compares the amount of dividends that Gulf sent to Southern with the equity investments from Southern to Gulf over the time frame 2003 to 2011; correct?

A. Yes.

Q. And the fact that the dividends exceed the equity infusions forms the basis for your contention that there should be no parent debt adjustment?

A. Yes. What this would indicate is that Gulf has generated cash flow that is sufficient to fund its own equity over this period of time.

Q. You chose 2003 because that was in the test period of your prior rate case; correct?

A. That is correct. We chose that. We went back to the last rate case, where the parent debt adjustment to our income tax expense was not made, and the circumstances have not changed since then.

Q. Would you agree with me that depending on where you draw the line, 2004, 1996, 1984, this comparison could look very different?

A. Yes, it could. I don't know what those numbers looked like beyond the last rate case.

Q. Depending on where they draw the line, the equity infusions could be more or less than the dividends?

A. Certainly. Where you draw the line, I'm not aware that the numbers in history beyond this would indicate any different.

Q. You don't know?

A. No, I don't know that.

MR. McGLOTHLIN: No further questions.

CHAIRMAN GRAHAM: Mr. Kaufman.

CROSS-EXAMINATION

BY MS. KAUFMAN:

Q. Good afternoon, Mr. Teel. I'm Vicki Kaufman with the Florida Industrial Power Users Group.

A. Yes. Good afternoon.

Q. Good afternoon, yes.

I want to talk to you a little bit more about the ROE issue. You were here for Mr. Crosswhite, correct, his testimony?

A. Yes, I was.

Q. He kind of maybe punted a few of those issues over to you, so --

A. A couple.

Q. Yes. Let me ask you if you can tell us what Gulf's return on equity was in 2007.

A. Yes. I would refer you, Commissioners, to -- I believe Schedule 3.

Q. This is the graph, right, that you're referring me to?

A. Yes. This is the graph which indicate that in 2007, we were approximately -- it looks like 12.75.

Q. And what was your return on equity in, let's say -- I guess you're going at year-end here.

December 2010.

A. Year-end 2010, we were approximately 9 1/2.

Q. When the company earned 9 1/2 in 2010, was it able to provide safe and reliable and efficient service to its customers?

A. Yes, we continued to provide safe and reliable service to our customers. During this period of time, we implemented cost controls. Those cost controls were intended to control and cut those costs that would not have an immediate impact on our customers. A&G costs, for example, was an area that you look to first, which is where we looked to. And, yes, we continued to provide safe and adequate service because we performed that work that were required of us to continue service in the near term.

Q. So just so we understand each other, when you were earning 9 1/2 on your ROE in 2010, you were able to provide reliable and efficient service to your customers; right?

A. Yes, that is correct. We controlled costs. Now we're at the point where we can no longer control costs, and those levels of returns will not allow us to provide that level of service sustainably into the future.

Q. And we're almost to the end of 2011, just a

few weeks left. What was the return that the company earned, at least to the point that you know it in 2011?

A. The surveillance report I believe we filed today indicated that our return has fallen to 5.43 percent.

Q. And would you agree with me that through 2011 up to where we are now, that the company has provided safe and reliable and efficient services to its customers?

A. Yes, that is true. Again, I would submit to you that that is not sustainable in the long term.

Q. But at least for 2010 and most of 2011, you've been able to do it with an ROE below 10 percent; correct?

A. Yes.

Q. I want to talk to you a little bit about the hurricane issue. You address that on page 5 of your testimony, beginning at line 6. Are you there?

A. Yes.

Q. Okay. And you tell us that in 2004 and 2005, there were a number of major hurricanes in the United States, including several in Gulf's territory; correct?

A. That is correct.

Q. And you also tell us that you were -- the company was recognized for its prompt response in

restoring service in the aftermath of the hurricanes; correct?

A. Yes.

Q. Now, when you were engaged in storm restoration for 2004 and 2005, am I correct that the company came to the Commission and asked for -- we called it a storm surcharge in order to effectuate repairs and restoration?

A. Yes, I believe there was an agreement. A storm surcharge was put in place to permit Gulf Power timely recovery of the costs associated with the repairs.

Q. And would you agree with me that at least one of those petitions to the Commission was stipulated to by all the parties?

A. I don't recall the details of that agreement, no.

Q. In your view, did the Commission act promptly on those requests?

A. I wasn't here during that time. I can't answer that question.

Q. Would you expect the Commission to act promptly on storm surcharge requests in the future?

A. Yes, I would.

Q. And using the storm surcharge in those two

years, Gulf was able to restore its system; correct?

A. We were able to restore service to our customers. However, you'll see in testimony that follows that despite the fact that we were able to restore service and repair our lines, we have seen some impact to our service since then.

Q. But we're focusing on the storms that you referenced in your testimony, 2004, 2005. Gulf came to the Commission, received the requested surcharge, and promptly and efficiently restored service to your knowledge; correct?

A. To my knowledge, correct.

Q. You had some quite extended discussion with Mr. McGlothlin about the views of certain rating agencies and their opinions regarding the regulatory environment in Florida; correct?

A. Yes.

Q. And I'm not going to rehash that with you. You looked worried, but don't worry.

And you have attached to your testimony three different publications, if you will, one from Moody's, and this is your Schedule 7; one from Fitch, which is your Schedule 8; and another one from Standard & Poor's, which is your Schedule 9; correct?

A. Yes; that's correct.

Q. And these three rating agencies give various and sundry opinions about their view of the market and of Gulf; correct?

A. Yes, that is correct, with respect to the credit risk, yes.

Q. Right, with respect the credit risk.

Now, has Gulf provided us with a witness from any of these rating agencies to address the comments in these reports?

A. No, we have not. What I provided are the reports and the opinions from the credit rating agencies. And I do spend some time with these credit rating agencies, and have in the past, and do understand the factors that they consider in creating these assessments and opinions.

Q. Let's just look at one of them, Schedule 7, which is the Moody's credit opinion about Gulf Power dated August 13, 2010. Do you know who the author of this report is? I mean the person.

A. The person -- I'm not certain he is the author. Mike Haggarty is the lead analyst for Moody's.

Q. But you don't know if he's the author of this document?

A. Not specifically whether he authored it, no.

Q. Did Gulf consider producing Mr. Haggarty or

whoever the author was to discuss the report with the Commission?

A. No, we did not. It's sufficient to read these reports to determine what their assessment of Gulf Power's credit risk is.

Q. I just want to understand. The company didn't even consider asking one of these -- the authors of any these documents to appear at this hearing?

A. No, we didn't. Again, I think the credit reports are sufficient. We did not consider incurring the expense of bringing Mr. Haggarty or any of the other analysts down here to describe what's in their reports, no.

Q. Mr. McGlothlin talked to you a little bit also about the parent debt adjustment, and you discuss it beginning -- well, I want to talk to you about your comments on page 23. And just to set the scene a little bit, there is a rule -- is it not true that there is a rule that requires a parent debt adjustment unless the presumption for that is rebutted; correct? And you describe the rule in your testimony, don't you?

A. I describe the rule. And actually one of my schedules has the rule, Schedule 10, I believe.

Q. And what that rule provides is that the requirement for a parent debt adjustment is a rebuttable

presumption; correct?

A. That is correct.

Q. And what you're trying -- part of your testimony attempts to rebut the testimony; correct?

A. Yes, we do rebut the presumption. And as we discussed with Mr. McGlothlin, the net cash flows between the parent company and Gulf Power since the last rate case indicate that we have generated sufficient funds internally, so therefore, the debt on the parent company's books would not have provided any of the equity in Gulf Power.

Q. I understand your position, but it's also true -- and I think you described this on page 23 -- isn't it, that you cannot trace those dollars flowing between Southern Company and Gulf Power?

A. No, I cannot trace those dollars. And in fact, there is no way to trace those dollars affirmatively or negatively. If the requirement for the rebuttable presumption is to in fact trace those dollars, the presumption is, in effect, irrebuttable.

Q. Well, wouldn't another way to look at be that if you can't track and trace those dollars, then you have not rebutted the presumption that's set out in the rule?

A. No, I would not agree with that. We have

rebutted the presumption through the demonstration of those cash flows on the schedule we reviewed just a few moments ago.

Q. So your position is that the chart that you discussed with Mr. McGlothlin, which is Schedule 11, is sufficient, even though you've admitted that the company cannot track the dollars between Southern Company and Gulf; correct?

A. That's correct. We cannot track them affirmatively or negatively.

MS. KAUFMAN: Thank you, Mr. Chairman. That's all I have.

CHAIRMAN GRAHAM: All right. It looks like a good time to take a lunch break. We're at 10 after one. Let's reconvene here at two o'clock. We're in recess.

(Proceedings recessed at 1:10 p.m.)

(TRANSCRIPT CONTINUES IN SEQUENCE IN VOLUME 2.)

CERTIFICATE OF REPORTER

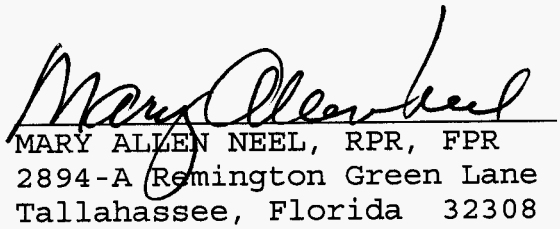
STATE OF FLORIDA:

COUNTY OF LEON:

I, MARY ALLEN NEEL, Registered Professional Reporter, do hereby 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 1 through 248 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, or relative or employee of such attorney or counsel, or financially interested in the foregoing action.

DATED THIS 14th day of December, 2011.



MARY ALLEN NEEL, RPR, FPR
2894-A Remington Green Lane
Tallahassee, Florida 32308
850.878.2221