BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Review of Florida Power Corporation's Earnings, Including Effects of Proposed Acquisition of Florida Power Corporation by Carolina Power & Light

DOCKET NO. 000824-EI

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DIRECT TESTIMONY
OF
H. WILLIAM HABERMEYER, JR.

ON BEHALF OF
FLORIDA POWER CORPORATION

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I. <u>Introduction and Background</u>

Q. Please state your name and business address.

A. My name is H. William Habermeyer, Jr. My business address is Florida Power Corporation ("Florida Power" or the "Company"), 100 Central Avenue, St. Petersburg, Florida 33701.

Q. What are your responsibilities at Florida Power?

A. I serve as the Company's President and Chief Executive Officer. In this role, I have overall responsibility for the operations of Florida Power.

Q. Please describe your educational and employment background.

A. Please see HWH-1.

II. <u>Purpose and Summary of Testimony</u>

Q. What is the purpose of your testimony?

A. I would like to discuss our recent merger, our plans and objectives for the coming years, and a broad view of our financial picture and rate proposal in this proceeding.

Q. Please summarize your testimony.

A. We are very excited about the positive benefits our recent merger provides for our customers. The merger brings together two great Southeastern utilities and enables Florida Power to gain the benefit of the centralization of various management and operational functions, the consolidation and elimination of redundant programs, the significant reduction of costs, the identification and implementation of best practices, and the enhancement of reliability and customer service. As a result of the synergies resulting from the merger, Florida Power will meet the increasing demands of its customer base, compete for capital in an increasingly competitive market, and improve upon its long tradition of strong reliability and customer service.

As we enter 2002, we are committed to realizing all of the merger synergies we project, and we will be making increased investments in reliability in Energy Delivery and Energy Supply, and in the area of customer service, introducing up-to-date technology to provide our customers with enhanced Web-based functionality and increased responsiveness overall. We have identified a number of opportunities to enhance the reliability of the Company's transmission and distribution system, and we are initiating a program to modernize and strengthen our system. At the same time, we are increasing the amount and quality of our generation reserves, introducing more power plants into our mix of reserves in order to provide our growing customer population with greater access to generation within the State of Florida.

The Company has enjoyed a long tradition of providing reliable electric service at reasonable prices, and we are now well positioned to continue, and improve upon, that tradition in the coming years. We are pleased to report that our total projected operation and maintenance ("O&M") expenses for 2002 are well below the Florida Public Service Commission ("Commission") benchmark amount. This is due in large part to significant merger synergies. Of course, merger-related savings must be "netted" against the costs associated with the acquisition premium that was incurred to bring these savings about. Once this is done, the merger may be seen as a true "win-win" for the Company and its customers.

Remarkably, even as we strengthen reliability and customer service, we are lowering prices to customers in parallel. First, we anticipate providing to our customers a $5 million rate credit each year for 15 years, totaling $75 million. This is directly attributable to the merger savings. Further, beginning in 2004, customers will receive $37 million more in reductions due to full amortization of the Tiger Bay cogeneration facility. Even more reductions are possible through efficiency incentives proposed in our rate filing. (Also, we have proposed cutting $65 million in annual fuel costs and related charges outside these proceedings, to take effect January 1, 2002.)

III. Merger

Q. Please provide an overview of the recent merger.

A. Our recent merger has provided Florida Power with exciting opportunities to strengthen its business, control or reduce costs, and enhance reliability and service to its customers. The merger was accomplished on November 30, 2000, when Progress Energy, Inc. ("Progress Energy") acquired Florida Power's parent Company, Florida Progress Corporation ("Florida Progress"), merging the operations of Florida Power with those of Progress Energy's electric utility, Carolina Power & Light Company ("CP&L"). The merger brought together two strong Southeastern electric utilities to achieve a number of important economic and strategic benefits.

In the period leading up to the merger, and since the time of the merger, Florida Power and CP&L have conducted an extensive review of best practices to develop the strongest and most efficient business and operational methods going forward. In addition, Progress Energy created a new service company, Progress Energy Service Company, LLC ("Progress Energy"), to consolidate and manage administrative and general operations previously conducted separately at the respective utilities. Other shared functions (e.g., nuclear operations) are also now managed centrally to exploit economies of scale and other efficiencies. Finally, the utilities are able to take advantage of the greater financial resources and diversity of the combined companies and the Progress Energy organization created by the merger. As a result, Florida Power is a stronger, better managed, and more efficient utility in many respects.

Quality of Service. As a result of identifying and adapting the best practices of both utilities, Florida Power will be adopting the latest technology, improving equipment and systems, and enhancing the quality of its service in numerous respects. As described more fully in the Direct Testimony of Mark Myers (submitted September 14, 2001), Robert Sipes (submitted November 15, 2001), Sarah Rogers (submitted November 15, 2001), and Martha Barnwell (submitted November 15, 2001), the Company will be making substantial improvements in energy delivery by increasing investment in energy delivery facilities and systems, implementing improved outage response procedures and technology, acquiring a new fleet of energy delivery vehicles, installing a new radio dispatch system, implementing a regional transmission maintenance system, and adding operating centers.. At the same time, we will be improving customer service by employing automated metering technology (initially on a pilot basis), adding new payment locations, implementing new software and increased Web-based functionality, and combining forces with CP&L to provide more effective customer-service assistance, better training, and increased leverage with vendors for collections, outage reporting, payment management, and other services.

Reduced Operating Costs. As a result of the merger, we are able to consolidate and eliminate what are now duplicative functions and programs and substantially cut associated costs, including labor costs. In fact most of these savings will result from our ability to reduce payroll and related benefits. Although the Company had substantially curtailed its workforce throughout the

1990s to cut and control costs, the merger has enabled the Company to cut approximately 675 positions, more than 13 percent of Florida Power's workforce. Overall, we expect to realize $58.7 million in merger synergies in 2002.

Financial Strength. Further, Progress Energy now enjoys equity market capitalization of approximately $9.3 billion, more than twice that of Florida Progress as a stand-alone company. This enhances our parent company's ability to attract capital by increasing the liquidity of its common stock. The combined company is also able to finance the operations of Florida Power efficiently, combining borrowing facilities and achieving other financing advantages. Also significant is the fact that the combined companies will enjoy greater operational diversification and geographic diversification, mitigating business risks (and hence overall costs of capital). And the Company will be able improve its competitiveness with the same result.

Managerial, Financial, Technical, and Operational Resources. As a result of the added size and strength of the merged companies, Florida Power is now in a better position to recruit and retain the most capable managers and other key employees. We are also better able to provide cost-effective leadership programs, training, and enhanced opportunities for professional development. Among other things, we will benefit from the combined financial expertise of managers, professionals, and consultants associates with both utilities. With respect to technology, CP&L has been recognized as one of the top technology innovators in the country, and Florida Power will benefit from this expertise. We can draw upon the best practices of both companies in the technology area to solve problems, improve operations, and enhance customer service in Florida. The merger has also made possible the creation of common work practices, operational coordination, and the sharing of operational resources between the utilities.

IV. <u>Plans for the Future</u>

Q. Please describe your objectives as a Company going forward.

A. As we emerge from this transitional year and embark upon 2002, the first full year that Florida Power will be integrated into the Progress Energy system, we have adopted the priorities of realizing the significant merger synergies that I have described in general terms above and increasing the Company's commitment to Energy Delivery, Energy Supply, and customer service. It is our goal and expectation to become a world-class utility in the areas of reliability and customer service.

In the area of Energy Delivery, we will continue the Company's efforts to innovate utilizing cost-effective technology to enhance the reliability of distribution and transmission and to improve customer service. As discussed by Robert Sipes, Sarah Rogers, and Martha Barnwell in their Direct Testimony, we are committed to modernizing our systems and equipment and enhancing our capabilities (particularly the Web-based functionality of our customer service resources) to meet and exceed the evolving expectations of our increasingly technology-driven customer base. To this end, we will be increasing capital and O&M spending in transmission, distribution, and customer service and improving our performance in all of these areas.

Integral to achieving these goals is our plan to invest more than $100 million in our electric grid system over the next three years. Our goal is to improve reliability performance by 20 percent in three years. Our power quality and reliability initiative includes:

- **Upgrading performance of existing facilities.** For example, we will be installing a new series of regulators and capacitors to boost voltage for customers distant from substations.
- **Deploying automation solutions.** For example, we will be implementing GPS mapping to shorten response times in addressing system problems.
- **Increased preventive maintenance.** For example, we will be replacing up to 500 poles a year damaged by woodpeckers or rot, and we will be stepping up our efforts to clear rights-of-way to reduce outages from tree limbs.

Likewise, we are committed to increasing generation adequacy. We gave assurance to the Commission that we would observe a minimum 20 percent reserve margin planning criterion no later than the summer of 2004. We will accomplish this goal in December 2003, ahead of schedule. We will continue our leadership in cost-effective load management programs. At the same time, we are taking steps to carry more of our reserves in the form of hard generating assets, further reducing the exposure of our customers to interruptions in service due to extreme weather events and other circumstances leading to forced outages. The Company placed its 529 megawatt ("MW") combined-cycle Hines 1 Unit into service in 1999. We constructed, and we are now operating, three new 94 MW gas-fired peaking units at its Intercession City facility. These units entered service in December 2000. We will be adding the state-of-the-art, gas-fired combined cycle 567 MW Hines 2 Unit to our Hines Energy Complex in November 2003. And we will soon commence efforts to add another like-sized power block to our system.

We are committed as well to enhancing our customer service. Our goal is to achieve best-in-class customer service among our peer utilities in Florida. We will endeavor to excel in meeting our customers' needs in all areas: turning on service, handling service calls, restoring service, and responding to customer calls. We are taking steps to ensure that our customers understand better the services we provide, for example, by enhancing our customers' ability to pay for their electric service via the Internet and by creating new payment locations. And we are preparing for automated meter reading, made possible by economies of scale resulting from the merger.

IV. Expenses

Q. Please provide an overview of the Company's financial profile for 2002.

A. I am pleased to say the Company is positioned to provide reliable, safe, and reasonably priced electric service to our customers into the future as it has in the past. Florida Power has a strong history of success, as evidenced by the fact that the Company has held its base rates constant since 1993, while continuing to provide quality service to its customers. By applying best practices from the merged companies combined with a renewed focus in the areas of generation reserves, transmission and distribution reliability, and customer service, I believe that the new Florida Power can do even better and can achieve top quartile performance in all significant areas of service.

In fact, even with our ambitious goals to enhance reliability and customer service in 2002, we are projecting that total O&M expenses during the test year will fall substantially short of the 1992 Commission benchmark amount ($473 million projected, as compared with a benchmark of $621 million). As I mentioned, this is due in significant part to the savings resulting from merger synergies. Of course, not all of these savings are truly "net" of the costs that will be incurred to bring them about. As explained more fully in the Direct Testimony of Mark Myers (September 14, 2001) and Dr. Charles Cicchetti (September 14, 2001) it will be important to "net" the annual projected merger synergies (equal to $31 million annually, on an adjusted retail basis) against the retail acquisition premium of $25 million (expressed on an annual basis, spread over a 15-year recovery period) in order to get the true "net" merger synergies produced by the merger.

As Dr. Cicchetti and Mark Myers explain in their testimony, we anticipate providing to our customers a $5 million rate credit each year for 15 years, totaling $75 million. This is directly attributable to the net savings from our merger. Even more reductions are possible through the efficiency incentives described in Dr. Cicchetti's testimony. Further, beginning in 2004, customers will receive $37 million more in reductions due to full amortization of the Tiger Bay cogeneration facility. (We have also proposed cutting $65 million in annual fuel costs and related charges outside these proceedings.)

Overall, taking into account our full financial picture, I am able to state, as we enter the new millennium, that our costs are under control, the Company is financially sound, our commitment to world class reliability and customer service has never been greater, and our recent merger has positioned the Company to be able to continue to provide reliable service at a reasonable cost to our customers for many more years to come.

V. <u>Conclusion</u>

Q. Does this conclude your testimony?

A. Yes, it does.

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WITNESS: H. WILLIAM HABERMEYER, JR.

H. William Habermeyer, Jr.
President & CEO
Florida Power Corporation

Bill Habermeyer is president and chief executive officer of Florida Power Corporation, one of two major utility subsidiaries of Progress Energy, a Raleigh, N.C. –based diversified energy holding company serving 2.8 million electric and natural gas customers in the Carolinas and Florida.

He joined CP&L, Progress Energy's other major utility holding, in 1993 after a distinguished 28-year career in the U.S. Navy. He retired from the Navy in 1992 as a rear admiral after serving various assignments including Commander Submarine Group Two, New London, CT; Director of Attack Submarines for the Office of the Chief of Naval Operations; and Commandant of Midshipmen, U.S. Naval Academy.

During his tenure with Progress Energy and CP&L, Habermeyer has served as CP&L's vice president, Nuclear Services and Environmental Support from 1993 – 1995; vice president, Nuclear Engineering from 1995 – 1997; and vice president, Western Region from 1997 – 2000.

While overseeing CP&L's Western Region operations, Habermeyer was responsible for regional distribution management, customer support and community relations. He was also very active in the Asheville, N.C., community, serving as chairman of the Asheville Area Chamber of Commerce. Now based in St. Petersburg, Florida Habermeyer was named to his current position in August 2000.

Habermeyer is a graduate of the U.S. Naval Academy and has a master's in public administration from George Washington University.

Civic or Community Activities:

- Enterprise Florida - Board Member
- Pinellas County Board of Education Foundation - Board Member
- Tampa Bay Partnership – Board Member
- Florida Chamber of Commerce – Board Member
- SunTrust Bank – Board Member
- USF Foundation Board of Trustees – Board Member

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