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GULF POWER
A SOUTHERN COMPANY

August 7, 2006

Ms. Blanca S. Bayo, Director
Division of the Commission Clerk and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee FL 32399-0870

Dear Ms. Bayo:

Re: Fuel and Purchased Power Cost Recovery Clause
with Generating Performance Incentive Factor

Enclosed for official filing in Docket No. 060001-EI are an original and fifteen copies of the following:

1. Prepared direct testimony of H. R. Ball. 07117-06

2. Prepared direct testimony and exhibit of Rhonda J. Martin. 07118-06

Sincerely,

Susan D. Ritenour (lw)

bh

Enclosures

cc w/encl: Beggs & Lane
Jeffrey A. Stone, Esq.

HR Ball

DOCUMENT NUMBER-DATE
07117 AUG-8 g
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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

IN RE: **Fuel and Purchased Power Cost Recovery Clause with Generating Performance Incentive Factor**)

Docket No.: **060001-EI**

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true copy of the foregoing was furnished by U. S. mail this 7TH day of August, 2006, on the following:

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BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

Docket No. 060001-EI

Prepared Direct Testimony of H. R. Ball

Date of Filing: August 8, 2006

GULF POWER

A SOUTHERN COMPANY

DOCUMENT NUMBER-DATE
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GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
H. R. Ball
Docket No. 060001-EI
Date of Filing: August 8, 2006

Q. Please state your name and business address.

A. My name is H. R. Ball. My business address is One Energy Place, Pensacola, Florida 32520-0335. I am the Fuel Manager for Gulf Power Company.

Q. Please briefly describe your educational background and business experience.

A. I graduated from the University of Southern Mississippi in Hattiesburg, Mississippi in 1978 with a Bachelor of Science Degree in Chemistry and graduated from the University of Southern Mississippi in Long Beach, Mississippi in 1988 with a Masters of Business Administration. My employment with the Southern Company began in 1978 at Mississippi Power's (MPC) Plant Daniel as a Plant Chemist. In 1982, I transferred to MPC's Fuel Department as a Fuel Business Analyst. I was promoted in 1987 to Supervisor of Chemistry and Regulatory Compliance at Plant Daniel. I was promoted to Supervisor of Coal Logistics with Southern Company Fuel Services in Birmingham, Alabama in 1998. My responsibilities included administering coal supply and transportation agreements and managing the coal inventory program for the Southern

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Electric System. I transferred to my current position as Fuel Manager for Gulf Power Company in 2003.

Q. What are your duties as Fuel Manager for Gulf Power Company?

A. I manage the Company's fuel procurement, inventory, transportation, budgeting, contract administration, and quality assurance programs to ensure that the generating plants operated by Gulf Power are supplied with an adequate quantity of fuel in a timely manner and at the lowest practical cost. I also have responsibility for the administration of Gulf's Intercompany Interchange Contract (IIC).

Q. What is the purpose of your testimony in this docket?

A. The purpose of my testimony is to compare Gulf Power Company's original projected fuel and net power transaction expense and purchased power capacity costs with current estimated/actual costs for the period January, 2006 through December, 2006 and to summarize any noteworthy developments at Gulf in these areas. The current estimated/actual costs consist of actual expenses for the period January, 2006 through June, 2006 and newly projected fuel and net power transaction costs for July, 2006 through December, 2006. Projected capacity costs for July through December remain as originally filed. It is also my intent to be available to answer questions that may arise among the parties to this docket concerning Gulf Power Company's fuel and net power transaction expenses and purchased power capacity costs.

Q. During the period January, 2006 through December, 2006 how will Gulf Power Company's recoverable total fuel and net power transactions cost compare with the original cost projection?

A. Gulf's currently projected recoverable total fuel and net power transactions cost for the period is $363,343,100 which is $16,090,874 or 4.63% above the original projected amount of $347,252,226. The resulting average fuel cost is projected to be 2.9298 cents per KWH or 5.17% above the original projected amount of 2.7859 cents per KWH. The higher total fuel expense and average per unit fuel cost is attributed to higher than projected coal prices for the period which are reflected in the fuel cost of generation. Gulf also is projecting that a greater portion of its energy needs will come from higher cost purchased power and less from lower cost system net generation. This current projection of fuel and net purchased power transaction cost is captured in the exhibit to Witness Martin's testimony, Schedule E-1 B-1, Line 20.

Q. During the period January, 2006 through December, 2006 how will Gulf Power Company's recoverable fuel cost of system net generation compare with the original projection of fuel cost?

A. Gulf's currently projected recoverable fuel cost of system net generation for the period is $487,758,630 which is 35,305,084 or 6.75% below the original projected amount of $523,063,714. Total net system generation is expected to be 16,465,574 MWH compared to the original projected generation of 17,810,860 MWH or 7.55% below projections. The resulting average fuel cost is expected to be 2.9623 cents per KWH or 0.87% above

the original projected amount of 2.9368 cents per KWH. This current projection of fuel cost of system net generation is captured in the exhibit to Witness Martin's testimony, Schedule E-1 B-1, Line 1.

Q. What are the reasons for the difference between Gulf's original projection of the fuel cost of system net generation and the current projection?

A. The lower total fuel expense is due to lower than projected generation for the period. The higher average per unit fuel cost is attributed to higher than projected delivered coal prices for the period.

Q How did the total projected fuel cost of system net generation compare to the actual cost for the first six months of 2006?

A. The total fuel cost of system net generation was $231,486,616 which is $7,408,830 or 3.10% lower than the projection of $238,895,446. On a fuel cost per KWH basis, the actual cost was 2.9506 cents per KWH, which is 2.93% higher than the projection of 2.8666 cents per KWH. This higher cost of system generation on a cent per KWH basis is due to fuel cost in $/MMBTU being 1.73% higher than projected and heat rate (BTU/KWH) of the generating units operating being 1.47% higher than projected. This information is found on Schedule A-1, Period to Date and Schedule A-3 of the June, 2006 Monthly Fuel Filing.

Q. How did the total projected cost of coal burned compare to the actual cost for the first six months of 2006?

A. The total cost of coal burned (including boiler lighter) was $175,197,137

which is $22,269,196 or 14.56% greater than our projection of $152,927,941. On a fuel cost per KWH basis, the actual cost was 2.498 cents per KWH which is 18.33% greater than the projected cost of 2.111 cents per KWH. The higher than projected cost of coal burned and cost of coal fired generation is due to coal prices being 17.65% higher than projected on a $/MMBTU basis. This information is found on Schedule A-3 of the June, 2006 Monthly Fuel Filing.

Q. How did the total projected cost of natural gas burned compare to the actual cost during the first six months of 2006?

A. The total cost of natural gas burned for generation was $56,227,702 which is $29,739,803 or 34.59% lower than our projection of $85,967,505. On a cost per unit basis, the actual cost was 6.77 cents per KWH which is 14.30% lower than the projected cost of 7.90 cents per KWH. The total cost of natural gas burned for generation is lower than projected due to lower than projected net generation from gas fired units and lower gas prices. The cost per KWH for gas fired generation is lower than projected due to lower natural gas prices. Natural gas prices were 15.38% lower than projected on a $/MMBTU basis. This information is found on Schedule A-3 of the June, 2006 Monthly Fuel Filing.

Q. For the period in question, what volume of natural gas was actually hedged using a fixed price contract or instrument?

A. Gulf Power hedged 3,600,000 MMBTU of natural gas for the period January, 2006 through June, 2006 using fixed price financial swaps.

Q. What types of hedging instruments were used by Gulf Power Company and what type and volume of fuel was hedged by each type of instrument?

A. Natural gas was hedged using financial swaps that fixed the price of gas to a certain price. These swaps settled against either a NYMEX Last Day price or Gas Daily price. The entire amount (3,600,000 MMBTU) of gas hedged was hedged using these financial instruments.

Q. What was the actual total cost (e.g., fees, commission, option premiums, futures gains and losses, swap settlements) associated with each type of hedging instrument?

A. No fees, commission, or option premiums were paid. Gulf's gas hedging program has resulted in a net financial loss of $7,521,292 for the period January through June, 2006 (hedging settlement excluding support costs).

Q. Are Gulf Power's actual and projected operation and maintenance expenses for its financial hedging programs to mitigate fuel and purchased power price volatility reasonable for cost recovery purposes?

A. Yes, the O&M costs associated with managing the fuel hedging programs are a small percentage of the total benefit received from these programs. As an example, the actual recoverable O&M cost of managing the gas hedging program for the last twelve month period (July, 2005 through June, 2006) was $80,552 while the total financial gain credited to fuel expense from the gas hedging program for this period was $13,905,732.

Q. During the period January, 2006 through December, 2006 how will Gulf Power Company's recoverable fuel cost of power sold compare with the original cost projection?

A. Gulf's currently projected recoverable fuel cost of power sold for the period is ($166,396,834) or 17.39% below the original projected amount of $(201,426,000). Total megawatt hours of power sales is expected to be 5,110,002 MWH compared to the original projection of 5,878,653 MWH or 13.08% below projections. The resulting average fuel cost of power sold is expected to be 3.2563 cents per KWH or 4.96% below the original projected amount of 3.4264 cents per KWH. This current projection of fuel cost of power sold is captured in the exhibit to Witness Martin's testimony, Schedule E-1 B-1, Line 18.

Q. What are the reasons for the difference between Gulf's original projection of the fuel cost of power sold and the current projection?

A. The lower total credit to fuel expense from power sales is attributed to lower replacement fuel costs than originally projected. Lower market prices for natural gas during the period reduced the fuel reimbursement rate ($/MWH) for power sales. Also, there is a decrease in the number of MWH being sold due to the less favorable economic position of Gulf's generating resources in Southern Company's power pool dispatch.

Q. How did the total projected fuel cost of power sold compare to the actual cost for the first six months of 2006?

A. The total fuel cost of power sold was ($81,213,834) which is $4,687,166 or 5.46% less than our projection of ($85,901,000). On a fuel cost per KWH basis, the actual cost was 3.0931 cents per KWH which is 5.11% below the projected cost of 3.2596 cents per KWH. This information is found on Schedule A-1, Period to Date of the June, 2006 Monthly Fuel Filing.

Q. During the period January, 2006 through December, 2006 how will Gulf Power Company's recoverable fuel cost of purchased power compare with the original cost projection?

A. Gulf's currently projected recoverable fuel cost of purchased power for the period is $32,355,700 or 37.33% above the original projected amount of $23,561,000. Total megawatt hours of purchased power is expected to be 970,606 MWH compared to the original projection of 464,921 MWH or 108.77% above projections. The resulting average fuel cost of purchased power is expected to be 3.3336 cents per KWH or 34.22% below the original projected amount of 5.0677 cents per KWH. This current projection of fuel cost of purchased power is captured in the exhibit to Witness Martin's testimony, Schedule E-1 B-1, Line 12.

Q. What are the reasons for the difference between Gulf's original projection of the fuel cost of purchased power and the current projection?

A. The higher total fuel cost of purchased power is attributed to Gulf purchasing a greater amount of MWH to supplement its own generation to meet load demands. However, replacement fuel costs are lower than projected as a result of lower natural gas market prices for the period.

These lower fuel prices have decreased the fuel reimbursement rate for purchased power.

Q. How did the total projected fuel cost of purchased power compare to the actual cost for the first six months of 2006?

A. The total fuel cost of purchased power was $18,564,700 which is $6,724,700 or 56.80% greater than our projection of $11,840,000. On a fuel cost per KWH basis, the actual cost was 2.7001 cents per KWH which is 37.48% lower than the projected cost of 4.3187 cents per KWH. The higher than anticipated purchased power expense is due to actual KWH purchases being 150.8% above the projected amount during the first six months of the year. This information is found on Schedule A-1, Period to Date of the June, 2006 Monthly Fuel Filing.

Q. Were there any other significant developments in Gulf's fuel procurement program during the period?

A. No.

Q. Were Gulf Power's actions through June 30, 2006 to mitigate fuel and purchased power price volatility through implementation of its financial and/or physical hedging programs prudent?

A. Yes, Gulf's physical and financial fuel hedging programs have resulted in more stable fuel prices. Over the long term, Gulf anticipates lower fuel costs than would have otherwise occurred if these programs had not been utilized.

Q. Should Gulf's fuel and net power transactions cost for the period be accepted as reasonable and prudent?

A. Yes, Gulf's coal supply program is based on a mixture of long term contracts and spot purchases at market prices. Coal suppliers are selected using procedures that assure reliable coal supply, consistent quality, and competitive delivered pricing. The terms and conditions of coal supply agreements have been administered appropriately. Natural gas is purchased using agreements that tie price to published market index schedules and is transported using a combination of firm and interruptible gas transportation agreements. Natural gas storage is utilized to assure that supply is available during times when gas supply is curtailed or unavailable. Gulf's fuel oil purchases were made from qualified vendors using an open bid process to assure competitive pricing and reliable supply. Gulf makes sales of power when available and gets reimbursed at the marginal cost of replacement fuel. This fuel reimbursement is credited back to the fuel cost recovery account so that lower cost fuel purchases made on behalf of Gulf's customers remain to the benefit of those customers. Gulf purchases power when necessary to meet customer load requirements and when the cost of purchased power is expected to be less than the cost of system generation. The fuel cost of purchased power is the lowest cost available in the market at the time of purchase to meet Gulf's load requirements.

Q. During the period January 2006 through December 2006, what is Gulf's projection of actual / estimated net purchased power capacity transactions

and how does it compare with the company's original projection of net capacity transactions?

A. As shown on Line 3 of Schedule CCE-1b in the exhibit to Witness Martin's testimony, Gulf's total current net capacity payment projection for the January 2006 through December 2006 recovery period is $29,403,149. Gulf's original projection for the period was $29,458,820 and is shown on Line 3 of Schedule CCE-1 filed in September, 2005. The difference between these projections is $55,671, or less than 1% lower than the original projection of net capacity payments and represents the difference between actual capacity payments year to date June 2006 and the original projection for this period.

Q. Mr. Ball, does this complete your testimony?

A. Yes.

AFFIDAVIT

STATE OF FLORIDA)
)
COUNTY OF ESCAMBIA)

Docket No. 060001-EI

Before me the undersigned authority, personally appeared H. R. Ball, who being first duly sworn, deposes, and says that he is the Fuel Manager at Gulf Power Company, a Florida corporation, and that the foregoing is true and correct to the best of his knowledge, information, and belief. He is personally known to me.

H. R. Ball
Fuel Manager

Sworn to and subscribed before me this 4th day of August, 2006

Notary Public, State of Florida at Large

Commission Number: DD 284322

Commission Expires: 25 Jan 08

NOTARY PUBLIC
Connie L. Happney
Exp. Date
Jan. 25, 2008
DD 284322
STATE OF FLORIDA