BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of:

DOCKET NO. 160007-EI

ENVIRONMENTAL COST RECOVERY CLAUSE.
_________________________________/

Volume 2

Pages 233 through 316

PROCEEDINGS: HEARING

COMMISSIONERS PARTICIPATING: CHAIRMAN JULIE I. BROWN
COMMISSIONER LISA POLAK EDGAR
COMMISSIONER ART GRAHAM
COMMISSIONER RONALD A. BRISÉ
COMMISSIONER JIMMY PATRONIS

DATE: Wednesday, November 2, 2016

TIME: Commenced at 9:50 a.m.
Concluded at 9:54 a.m.

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: LINDA BOLES, CRR, RPR
Official FPSC Reporter
(850) 413-6734

APPEARANCES: (As heretofore noted.)

I N D E X

WITNESSES

EXHIBITS

NUMBER:		ID.	ADMTD.
1	Comprehensive Exhibit List	312	312
2 through 29	(as identified on Comprehensive Exhibit List)	312	313

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of:
J. Terry Deason
Docket No. 160007-EI
Date of Filing: September 1, 2016

Q. Please state your name and business address.

A. My name is Terry Deason. My business address is 301 S. Bronough Street, Suite 200, Tallahassee, FL 32301.

Q. By whom are you employed and what position do you hold?

A. I am a Special Consultant for the Radey Law Firm, specializing in the fields of energy, telecommunications, water and wastewater, and public utilities generally.

Q. Please describe your educational background and professional experience.

A. I have 39 years of experience in the field of public utility regulation spanning a wide range of responsibilities and roles. I served as a consumer advocate in the Florida Office of Public Counsel (“OPC”) on two separate occasions, for a total of seven years. In that role, I testified as an expert witness in numerous rate proceedings before the Florida Public Service Commission (“Commission” or “PSC”). My tenure of service at OPC was interrupted by six years as Chief Advisor to Florida Public Service Commissioner Gerald L. Gunter. I left OPC as its Chief Regulatory Analyst when I was first appointed to the Commission in 1991. I served as Commissioner on the Commission for 16 years, serving as its chairman on two separate occasions. Since retiring from the Commission at the end of 2006, I have been providing consulting services and expert testimony on behalf of various clients, including public service commission advocacy staff and regulated utility companies. I have also testified before various legislative committees on regulatory policy matters. I hold a Bachelor of Science Degree in Accounting, summa cum laude, and a Master of Accounting, both from Florida State University.

Q. For whom are you appearing as a witness?

A. I am appearing as a witness for Gulf Power Company ("Gulf" or the "Company").

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present the history of Gulf's ownership interest in Plant Scherer Unit 3 (Scherer 3) and provide perspective for its appropriate regulatory treatment in the Environmental Cost Recovery Clause ("ECRC") and in base rates. I also address policy considerations for Gulf's request to recover the costs of closing its CCR pond at Plant Scholz through the ECRC mechanism.

Q. Are you sponsoring any exhibits?

A. Yes. I am sponsoring two exhibits and co-sponsoring one other exhibit. Exhibit JTD-1 is my curriculum vitae. Exhibit JTD-2 is a reference compendium containing 15 documents related to Gulf's acquisition of Scherer 3, including relevant letters, transcripts, and Commission orders.

My testimony will cite to specific pages of this document as RC-xx. I am co-sponsoring with Gulf Witness Burleson a chronology of events concerning Gulf's ownership interest in Scherer 3. This exhibit is attached to Mr. Burleson's testimony.

Q. How is your testimony organized?

A. My testimony is organized into seven parts. First, I describe the Commission's approach to long-term system planning. Second, I provide the history of Gulf's ownership interest in Plant Scherer for the benefit of its retail customers and identify key decisions made by the Commission in the course of that history. Third, I discuss regulatory principles that are applicable to Gulf's ownership interest in Scherer 3. Fourth, I explain how Gulf's ownership interest in Scherer 3 should be treated for regulatory purposes in retail rates. Fifth, I address the eligibility of Scherer 3 environmental compliance costs to be recovered through the ECRC. Sixth, I provide my conclusion for Plant Scherer. And seventh, I address the CCR costs at Plant Scholz.

I. System Planning

Q. What factors does the Commission take into account in evaluating a utility's long-term resource planning and generation commitments?

A. The Commission's approach has three fundamental components that work together. First, the Commission expects utilities to determine customers' needs based on long-term forecasts, which take into account all reasonably determined factors that affect the timing, duration, and magnitude of demands for power. Second, the Commission expects utilities to propose and pursue the correct mix of generation resources and conservation programs that reliably and cost-effectively meet customers' needs with an adequate reserve margin to insure the continuation of service during most (but not all) contingencies. And third, the Commission expects utilities to utilize a long-term planning horizon that not only considers the front-end capital costs and the ongoing operating costs of various generation alternatives, but also considers reliability, diversity of supply, and environmental sustainability. The ultimate goal of Florida's system planning process is to achieve the best balance of resources which maximizes customer benefits over the long term.

Q. Why is it important that system planning take a long-term view?

A. A long-term view is necessary to best meet customer needs in the most cost-effective and reliable manner. This is especially true when many of the most cost-effective resource alternatives have useful lives typically in excess of 40 years.

Q. Are there risks inherent in planning for such long-term horizons?

A. Yes. Forecasts of demands, capital costs, and operating costs often change with the passage of time. However, it is still true that customer benefits can best be maximized and costs minimized when planning takes the longer-term view. To facilitate utilities taking the longer-term view, regulation should provide a high degree of certainty that costs will be recovered over the life of an investment, despite the fact that demands and operating costs will change over that life. This has been the practice in Florida. In addition, to help minimize costs and best balance resources with changing customer needs, the Commission has encouraged both short-term and long-term off-system sales.

Q. Does the Commission have a policy regarding Florida electric utilities making long-term off-system sales?

A. Yes, the Commission has a policy of encouraging long-term off-system sales when certain conditions are met. The first condition is that, at the time the contract is executed, the capacity sold is not required to meet expected retail capacity needs. Second, the costs have to be fairly allocated such that retail customers are not asked to subsidize wholesale customers. And third, the generation remains ultimately available to meet retail customer needs after the contract ends. In essence, the Commission views long-term off-system sales as a bridging tool to balance capacity with need and to cost-effectively plan for retail needs while minimizing the cost burden on retail customers.

II. History of Gulf's Ownership Interest in Plant Scherer

Q. When was the Commission first informed of Gulf's intention to acquire an ownership interest in Plant Scherer?

A. In 1978, Gulf notified the Commission that it wished to cancel its remaining proposed Caryville unit, and instead purchase a portion of Plant Scherer. Gulf stated that cancelling the remaining Caryville unit and pursuing the Scherer acquisition would be a much cheaper alternative, with tremendous savings to flow to customers as a result.

Q. Did the Commission agree with Gulf's position?

A. Yes. As part of Gulf's rate case in Docket No. 800001-EU, the Commission gave tentative approval to Gulf's proposal to cancel the proposed Caryville plant and to amortize the associated cancellation charges. The Commission decided to place the unamortized portion of Caryville cancellation charges in rate base and to amortize it over five years, but required Gulf to hold the revenues collected subject to refund.

Q. Why were the associated revenues collected subject to refund?

A. The Commission wanted to insure that the Scherer acquisition actually took place. The Commission determined that the purchase of an interest in Scherer "would be beneficial to Gulf's ratepayers" but correctly noted that the Scherer acquisition had not yet been consummated. Therefore, the Commission placed the associated revenues subject to refund "in the event the transaction relied upon is not consummated…" In other words, the Commission clearly agreed that customers were better served by the Scherer acquisition than proceeding with Caryville and, therefore, used the subject to refund condition as a strong incentive for Gulf to complete the Scherer purchase.

Q. Have you seen any other evidence of the Commission's desire that Gulf purchase an interest in Scherer?

A. Yes. On February 16, 1981, at an informal workshop before all five of the then sitting Commissioners, Gulf made a presentation concerning the merits of purchasing an interest in Scherer. This workshop also had the Office of Public Counsel and Commission Staff in attendance.

Mr. E. L. Addison, the then President and CEO of Gulf, led Gulf's presentation to the Commission. Mr. Addison gave a brief history of the cancellation of the Caryville units and how this was the best decision for Gulf's customers. He also referenced the Commission's recent decision to allow the amortization of the Caryville cancellation costs in retail rates subject to refund pending consummation of the Scherer acquisition. Mr. Addison then bluntly notified the Commission that Gulf's load projections had continued to decrease to the point that the Caryville capacity (if constructed) would not be needed until 1993. This led to a dilemma for Gulf which Mr. Addison thusly described:

> "So the situation we now face is that Scherer is scheduled to be available to us six and four years ahead of what our need really is for our retail customers. However, we have the opportunity to sell at least a portion of that capacity to other utilities to displace oil-fired generation until that capacity is needed by our customers. At that time, they will greatly benefit as demonstrated by the cost comparisons.
>
> "Now our dilemma is this. If we wanted to be short-

sighted and bury our head in the sand, we could live a lot easier life for the next five or six years, and our stockholders would fair better if we did not participate in the Scherer Units. However, we're not in a short-term business. We are definitely in a long-term business, and our customers ultimately will greatly benefit from our participation in Scherer.

"In addition to the benefits to them, there is the benefit to this state of reducing oil consumption by selling that capacity into the State of Florida, or at least a portion of it. Now we are ready within a matter of a few days to sign the contract with Georgia Power Company for the purchase of that capacity. There is no doubt that if we move down the road and it's been demonstrated by our decision on Caryville, it's very easy after you pass a point in time to be second guessed about your business decision. Now we simply cannot take the business risk of having that kind of second guessing as we move down the road with the Scherer Units. We cannot embark on this program without assurance from this Commission that they are supportive of our actions. In spite of the fact that some of this capacity will not initially be used by our retail customers, they are the ultimate beneficiary."

This passage is taken from pages 9 and 10 of the transcript of the workshop, which appear as pages RC-193 and RC-194 of Exhibit JTD-2.

Q. Did Gulf's presentation also address the limited time frame to acquire an interest in Plant Scherer and the use of off-system sales to market the capacity acquired from Plant Scherer?

A. Yes. Mr. Arlan Scarbrough, Gulf's Vice President over financial matters, addressed this:

> "Now the other thing that Mr. Addison referred to is this period of time right here. We do not need this capacity until 1993. Scherer is only available, if you buy it, it's either available for '87-89 or it's not available at all. You either buy into it because it's going to be constructed by Georgia Power Company for '87 and '89 in-service, Unit 3 in '87 and Unit 4 in '89, no alternative. So during this period of time, we have commitments, pretty definite commitments for a significant portion of the output of Scherer already. We are confident, we are confident, although we do not have definite commitments, we are confident that we can market all of that output during that period of time.
>
> * * * * *
>
> "Now in order – and this sort of repeats what Mr. Addison said, but I reckon it's worth repeating because it's our whole purpose for being here. As he said, we're right on the verge of getting ready to sign this contract. These people have, in effect, told us, you know, 'Make up your mind, either do it or forget it, one or the other.' And, so we're right at that point where we're either going to make a decision to do it or

not to do it. But before we can embark on this type of financial endeavor, we must have the assurance of this Commission and the support of this Commission in our so doing."

These passages are taken from pages 17 and 21 of the workshop transcript, which appear at pages RC-201 and RC-205 of Exhibit JTD-2.

Q. What was the Commission's reaction?

A. The Commission's reaction was one of support for Gulf's efforts. The Commission acknowledged that the cancellation of Caryville and the pursuit of Scherer was in the best interest of Gulf's customers and that placing the Caryville cancellation charges subject to refund was an encouragement for Gulf to follow through on the Scherer acquisition. The Commission also acknowledged that load projections had declined but also stressed the need for long-range planning. In response to Mr. Addison and Mr. Scarbrough, Commissioner Cresse stated:

"Of course, since that time the cost of fuel has gone up tremendously and all those kinds of things have happened. And, so, we were using some hindsight. But I think we did get their attention, and I don't think that the Commission is, I hope has never accused -- I hope we're never guilty of discriminating against a company that uses a little long-range planning and long-range thought processes in providing the most economical service to their customers.

"On the other hand, I'd rather think that we would be unhappier with a company that was not willing to do something innovative and different than the customary 'wait-until-the-last-minute' to build, construct, do those things that we're only obligated to do without taking a longer view.

"I think you're taking a longer view, and I don't believe that the Commission will discriminate against your company because you're taking a longer view."

This passage is taken from page 47 of the workshop transcript found on page RC-231 of Exhibit JTD-2.

Q. Was there discussion of the Commission's actions to encourage the Scherer acquisition?

A. Yes. Both Commissioner Gunter and Commissioner Cresse acknowledged that the Commission's earlier decision to place the Caryville cancellation charges subject to refund was an encouragement to consummate the Scherer acquisition. Commissioner Gunter stated: "If you want to look at the other side of that order where we ordered that money held until you did it, that maybe is a backwards way of looking at encouragement." Mr. Addison added: "We looked at it as encouragement." Then Commissioner Cresse concluded by stating:

"I think it was. I don't think anybody needs to kid themselves; that the Commission at that time felt that it was to the ratepayers in Florida's advantage for you to get that cheaper generating capacity out of Georgia than it was to build in Florida under the terms and conditions that you have to build in Florida. It's just that simple." [Transcript, page 48; RC-232]

Q. What was Gulf's next action following the February 16, 1981 informal workshop?

A. Based on the assurances received from the Commission, Gulf immediately proceeded to acquire an interest in Plant Scherer. Mr. Addison, in a memo dated February 18, 1981, directed Gulf to move with dispatch to complete the negotiations with Georgia relative to the purchase of the Scherer capacity. The contract to purchase between Gulf and Georgia Power was signed on February 19, 1981, and led to a March 3, 1981, filing to obtain the necessary Securities and Exchange Commission ("SEC") authorization to close the sale. On February 19, 1981 and February 27, 1981, the first two Unit Power Sales ("UPS") agreements were signed, committing portions of the Scherer units to interim long-term off-system sales through 1993.

Q. Was this issue addressed in Gulf's next rate case?

A. Yes. In Gulf's next rate case, Docket No. 810136-EU, the Commission reaffirmed its earlier decisions concerning the Caryville cancellation and the Scherer acquisition. In its Order No. 10557, the Commission referenced its earlier decision stating:

"In the Company's last rate case, Order No. 9628, we determined that Gulf's decision to cancel its Caryville facility was prudently based upon an economic advantage to Gulf's customers associated with purchasing the Scherer capacity in lieu of constructing the Caryville facility." [Order, p. 13; RC-247]

The Commission went on to say:

"In our opinion, this matter was fully aired and resolved during the last case, and nothing of an evidentiary nature has been offered to persuade us to depart from our earlier findings." [Order, p. 14; RC-248]

Q. Did the Commission reference the estimated cost savings associated with the Scherer acquisition?

A. Yes. In this same Order, the Commission stated:

"Based on Gulf's current budget, the cost of this Scherer capacity is estimated to be $827/kw. The comparable cost of capacity installed at Caryville in 1987 is estimated to be $2052/kw. Hence, Gulf's 404 MW net ownership share in Plant Scherer is expected to result in an estimated $495 million savings to Gulf's ratepayers." [Order, p. 38; RC-272]

Q. Did the Commission address the Caryville cancellation and the Scherer acquisition in Gulf's next rate case?

A. Yes, in Docket No. 820150-EU, Order No. 11498, the Commission reconfirmed its decisions in Gulf's two previous rate cases. The Commission also addressed a major policy issue on the question of Unit Power Sales.

Q. What is meant by Unit Power Sales?

A. Unit Power Sales or UPS is a form of power purchase agreement between two (or more) utilities providing a sale of firm generating capacity from the generating plant's owner to the purchasing utility. UPS contracts are for a stated period of time (usually for multiple years, but less than the anticipated life of the generating unit). The purchasing utility has first call on the unit's output and can rely on the unit's capacity to meet its capacity needs. When not called upon by the purchasing utility, the unit's energy output is available to the selling utility to be dispatched to meet retail energy needs or make economy sales. Because the UPS contract is a wholesale transaction, it is regulated by the Federal Energy Regulatory Commission ("FERC") and the costs of the generating unit are allocated to the wholesale jurisdiction by specific adjustments and/or jurisdictional separation factors.

Q. What did the Commission say about UPS contracts in its Order No. 11498?

A. The Commission's discussion on a UPS contract in Order No. 11498 was for Plant Daniel, not Plant Scherer. Nevertheless, the principles also apply to Plant Scherer. In rejecting a position taken by the OPC, the Commission stated:

> "However, we have examined the UPS contract and the associated cost and allocation from all angles and we come to the opposite conclusion. If the proper amounts of investment, operating expenses and revenues are allocated to UPS customers, retail ratepayers will not only <u>not</u> subsidize UPS customers, but on the contrary, they will benefit

handsomely from the sales, in the sense that they will not have to support the capacity sold in a UPS transaction for the life of the contract but the capacity will be available to serve them when they need it in the future, at a relatively reduced price when compared with the cost of future construction."
[Order, p. 20; RC-313 (emphasis added)]

Q. Did Gulf's acquisition of Scherer 3 require regulatory approval?
A. Yes. At the time of Gulf's acquisition of a portion of Plant Scherer, the SEC had jurisdiction to approve such transactions pursuant to the Public Utilities Holding Company Act of 1935.

Q. Did Gulf seek and receive approval from the SEC?
A. Yes. The application-declaration was filed on March 3, 1981, and originally sought approval to acquire 25 percent of Scherer Units 3 and 4. Due to a continuing decline in load growth, the application was later amended to include only the 25 percent of Scherer 3. On March 1, 1984, Gulf executed the Purchase and Ownership Participation Agreement and the Operating Agreement between Georgia Power Company and Gulf for a 25 percent interest in Scherer 3. The closing on Scherer 3 occurred on October 18, 1984 following SEC approval on October 10, 1984.

Q. Was there intervention at the SEC in opposition to the transaction?
A. Yes. Ratewatch, an unincorporated organization of Georgia citizens organized to promote just and reasonable utility rates, contended that the

price being paid by Gulf was too low. Ratewatch also sought to have the proposed transaction rejected in an effort to have Gulf participate in the higher-cost Scherer Unit 4 or alternatively take an ownership interest in Georgia Power's two nuclear Vogtle units. The Georgia Consumers' Utility Counsel (CUC) also appeared in opposition. The CUC sought to have Gulf pay above book value for Scherer 3 so that Georgia Power would earn a profit that could be passed through to Georgia customers.

Q. What did the SEC decide?

A. The SEC approved the transaction without an adjustment in Gulf's proposed price. In its Memorandum Opinion and Order, the SEC stated:

> "Ratewatch considers a sale to Gulf of a 25% interest in Unit 4 of greater advantage to ratepayers of Georgia. It is fair to assume for like reasons that Florida consumers served by Gulf would prefer Gulf's choice of Unit 3. We have no such regional preference, and, above all, the Act does not give us a dispensation to favor Georgia over Gulf, as Ratewatch would have us do." [RC-362-363]

Q. How did Gulf report its investment in Scherer 3 for surveillance purposes?

A. Consistent with Commission policy, Gulf allocated the portion of Scherer 3 covered by UPS contracts to the wholesale jurisdiction. The uncovered portions were included in retail and included in its surveillance reports to the Commission.

Q. When was the first time Gulf requested that a portion of Scherer 3 be included for purposes of setting retail rates?

A. As part of its rate case in Docket No. 891345-EI, Gulf requested that 63 MW of the 212 MW be included in rates. This included 19 MW that had never been sold off system up to that point and an additional 44 MW that became uncovered as the result of a default by Gulf States Utilities on a UPS contract with Gulf.

Q. What did the Commission decide?

A. The Commission decided that the 63 MW was not needed to serve retail customers and adjusted the 63 MW out of Gulf's request. In making this determination, the Commission relied on the fact that the bulk of the 63 MW (44 MW) was being made available to retail only because of the Gulf States Utilities default. In its Order No. 23573, the Commission noted that UPS sales would increase such that by 1995, none of Scherer 3 would be available to serve territorial customers until 2010. The Order also addressed the appropriate allocation of the risks and benefits of entering into UPS contracts:

> "It is clear that Gulf would not have requested 63 MW of Scherer to be in rate base had Gulf States Utilities not defaulted on their contracts. When Gulf made the decision to purchase 25 percent of Scherer 3 it was aware of the potential that their contract with Gulf States Utilities might not be honored. Since the profits from the unit power sales go to Gulf's stockholder, they should bear the risk of default, and

not Gulf's ratepayers. Therefore, we remove all of Plant Scherer from rate base. All profits and losses derived from unit power sales of Scherer, and any costs or benefits accruing from any settlement with Gulf States Utilities are to go to the stockholders of Gulf Power Company. Gulf's ratepayers, who will not see the profits from Gulf's unit power sales contracts, should not be required to pay when such a contract falls through." [Order, p. 13; RC-13]

Q. Was this always the Commission's decision?
A. No. As part of its review of Gulf's tax savings refund in Docket No. 890324-EI, the Commission had made a distinction between the 44 MW that was made available due to a UPS contract default and the 19 MW that had never been subject to a contract. Since the 19 MW had never been subject to a contract and had been available to serve native load customers the entire time, the Commission allowed the investment associated with the uncovered 19 MW to be included in Gulf's rate base. [Order No. 23536, p. 3]

Q. Was Gulf's portion of Scherer 3 at issue in any of Gulf's rate cases subsequent to its rate case in Docket No. 891345-EI?
A. No. Subsequent to the decision in Docket No. 891345-EI, Gulf has sought changes in its retail base rates in only three dockets: Docket Nos. 010949-EI, 110138-EI, and 130140-EI. In the test year for each of these three dockets, Gulf's investment in Scherer 3 was fully dedicated to long-term off-system sales under UPS agreements. In fact, other than the small portion of

the Scherer 3 capacity from 1987 through 1995, 100 percent of Gulf's investment in Plant Scherer has been committed to long-term off-system sales under UPS agreements until the end of 2015. Thus, for the first time since 1995, a portion of Gulf's investment is now serving the native load customers for whom it was planned, acquired and built by Gulf.

Q. What was the latest vintage of UPS contracts for Gulf's portion of Scherer 3?

A. In 2004, Gulf entered into three UPS contracts effective beginning in 2010 for its portion of Scherer 3. The largest of these contracts (110 MW) was with Florida Power & Light Company ("FPL") and expired at the end of 2015. A second contract with Progress Energy Florida ("PEF" now Duke) for 50 MW expired on May 31, 2016. The third contract for 50 MW is with Flint Energy, a Georgia Electric Membership Cooperative, and will expire on December 31, 2019.

Q. Did the Commission approve any of these UPS contracts?

A. Yes, from the buyers' perspective. The Commission reviewed the FPL and PEF contracts for their prudence and whether their associated costs should be recovered in each company's retail rates. The Flint contract is not subject to the Commission's jurisdiction.

Q. What did the Commission decide on the prudence of the FPL contract and the recovery of associated costs in FPL's retail rates?

A. These issues were addressed in the Commission's 2005 fuel and purchased power cost recovery proceedings in Docket No. 050001-EI. The

Commission determined that the contract was prudent and that the associated cost should be recovered. In reaching this determination, the Commission specifically referenced Florida's increasing reliance on natural gas-fired units and the fact that no new coal-fired generating units had been constructed either in Florida or on the Southern Company system for quite some time. Even though the overall contracts also included some gas-fired capacity from Southern Company's Harris and Franklin Units, the Commission decided that maintaining coal-fired capacity was needed and strategically beneficial. In its Order No. PSC-05-0084-FOF-EI, the Commission stated:

> "According to FPL, the purpose of the new UPS agreements is to retain as many of the benefits of the existing contracts as possible. While FPL may not have been able to retain all of the benefits of the existing UPS agreements, the new UPS agreements do provide some fuel diversity, enhanced reliability, and opportunities for economy energy purchases. Specifically, the new UPS agreements provide for: (1) the purchase of 165 MW of coal-fired and 790 MW of gas-fired capacity and energy, with the right of first refusal to purchase additional coal-fired energy if made available; (2) a short-term commitment which allows FPL to further explore ownership of new solid fuel generation; (3) enhanced reliability through geographic and fuel supply differences; and, (4) the retention of firm transmission rights within the Southern system." [Order, p. 3]

Q. What did the Commission decide on the prudence of the PEF contract and the recovery of associated costs in PEF's retail rates?

A. PEF filed a separate petition that was considered in Docket No. 041393-EI. Similar to the FPL contracts, the PEF contracts also included some gas-fired capacity. The Commission weighed the overall benefits and approved the contracts for cost recovery. The Commission identified and addressed four non-price benefits of maintaining some coal-fired capacity in the mix: Transmission Access and Economy Energy; Fuel Diversity; Planning Flexibility; and Reliability. In its Order No. PSC-05-0699-FOF-EI, the Commission stated:

> "In conclusion, we find that the non-price benefits discussed above are reasonable and provide important potential benefits for PEF and its ratepayers. The fuel diversity and planning flexibility afforded by the agreements are of particular importance due to the volatility and forecasting uncertainty of natural gas prices. The coal-fired capacity from Southern's Scherer unit will reduce PEF's ratepayers' exposure to fuel price volatility, while the timing of the contracts will give Progress the flexibility to defer natural gas-fired capacity and potentially move up the in-service date of a coal-fired unit." [Order, p. 8]

Q. Has Gulf's 25 percent interest in Scherer 3 been part of Gulf's annual planning process?

A. Yes. In recognition that Gulf's interest in Scherer 3 is a generation resource that would return for the benefit of retail customers, it has consistently been included in Gulf's Ten Year Site Plans. And in Gulf's 2007 Ten Year Site Plan there is discussion of Gulf's plans to comply with new environmental requirements to enable Plant Scherer to continue to be an operational resource for Gulf's customers. These new environmental requirements are discussed in Gulf Witness Markey's testimony and Schedule 1 of his exhibit. As a result, Gulf was required to add a scrubber system, a baghouse for additional mercury control, and a Selective Catalytic Reduction system to Scherer 3 in the 2009 to 2011 time frame in order to continue to operate the unit.

Q. Have these environmental compliance measures been installed at Plant Scherer?

A. Yes, these measures were installed on all four units at Plant Scherer.

Q. Did the Commission have an opportunity to review these environmental compliance measures?

A. Yes. The Commission's review was in the context of a request by FPL to include the environmental compliance costs for Scherer Unit 4 (a sister unit to Scherer 3) for recovery through the Environmental Cost Recovery Clause. In Docket No. 070007-EI, the Commission recognized that the measures to bring Scherer into compliance were needed and the most cost-effective alternative. The Commission approved the cost recovery of these environmental costs and required subsequent updates from FPL.

Q. How has Gulf accounted for its ownership interest in Plant Scherer?

A. Since its commercial operation date, Gulf's ownership interest in Plant Scherer has been recorded in Utility Plant in Service and other appropriate accounts in accordance with the FERC Uniform System of Accounts. Gulf's investment in Plant Scherer has been included in all of Gulf's depreciation studies submitted to the Commission since its initial acquisition. Accordingly, the depreciation rates applicable to Gulf's interest in Plant Scherer have been consistently reviewed and approved by the Commission.

Q. What is the remaining life of Plant Scherer as reflected in Commission-approved depreciation studies?

A. Plant Scherer's remaining life is approximately 35 years or until 2052.

III. Regulatory Policy Considerations

Q. What are the regulatory policy considerations relevant to the Commission's consideration of Gulf's interest in Plant Scherer?

A. They are the same considerations as those that are applied to any investment made by a regulated utility to provide service to its customers. Among these are:

- A regulated utility has the obligation to provide reliable and cost-effective service to its customers and to deploy capital to meet this obligation. Inherent in this obligation is a responsibility to manage costs and mitigate risks where reasonably possible.
- All investments are subject to a determination of prudence, based on the reasonably anticipated costs, risks, and benefits of said investment that are known or reasonably known at the time that the investment is made. Concomitant with this principle is that future changed circumstances that can be known and applied only in hindsight are not a valid basis to reverse a previous determination of prudence.
- All prudently incurred investments that are used and useful in providing service are to be afforded rate recovery treatment, both in the form of a reasonable return on the investment and a reasonable return of the investment, generally over the useful life of said investment.
- The reasonable rate of return is a necessary cost to provide service and should be set at a level to adequately compensate investors for the risk of their investment and to be fair to customers on whose behalf the capital is deployed. Inherent in this principle is the expectation that customer and investor interests are balanced in a fair and symmetrical manner.
- While the reasonable return on investment is not guaranteed, there is an expectation that rates will be set to afford a utility a reasonable opportunity to actually earn its authorized rate of return. Without that

reasonable opportunity, the allowed return would have to be substantially higher, and over time this would result in higher electric rates for customers.

- The reasonable rate of return is set and monitored to fall within an established band, so that the return is neither excessive nor deficient.

These considerations are part of the regulatory compact that has been the foundation of fair and effective utility regulation in this country for decades.

Q. What is the regulatory compact?

A. The regulatory compact is an implied contract that exists between a regulated public utility, its regulators, and its customers. It lays the foundation for regulation and balances the interests (and risks) of all stakeholders. It has been employed to characterize the set of mutual rights, obligations, and benefits that exist between the utility and its customers.

Q. Does the regulatory compact apply to Gulf's investment in Plant Scherer?

A. Yes. Consistent with the regulatory compact and its obligations under it, Gulf presented the Scherer acquisition as a more cost-effective alternative to constructing coal-fired generating units at Caryville. The Commission agreed that Scherer was a better alternative than Caryville and allowed the cancellation costs of Caryville to be amortized and reflected in rates. Absent extraordinary circumstances, once the Scherer plant was fully constructed and Gulf's acquisition of a portion of Scherer 3 was consummated, it would have become part of Gulf's rate base and all generation from its Scherer interest would have been for the exclusive benefit of its retail customers. In effect, this was the bargain that had been struck under the regulatory compact. However, there were extraordinary circumstances that affected the timing of when the bargain would be recognized in Gulf's retail rate base.

Q. What were these extraordinary circumstances?

A. At the time Gulf was required to commit to the purchase of an interest in Scherer, it had become clear that the capacity would not be immediately needed to serve Gulf's retail customers when the unit was scheduled to become operational. This was the subject of the February 1981 workshop at which the Commission encouraged Gulf to proceed with the purchase and to enter into wholesale contracts as a temporary bridge to cover the unit's revenue requirements. This is an example of the significant and often-times unavoidable risk of planning for generation to meet customer demands 10 to 20 years into the future.

Q. Who should bear this risk?

A. A strict interpretation of the regulatory compact would place this risk exclusively on the party for whose benefit the risk was taken, i.e., the customers. However, under the regulatory compact there also is a requirement to mitigate risks where reasonably possible (as long as the utility is not foreclosed the opportunity to earn a fair return on its investment). In recognition of this, the Commission decided to encourage Gulf to market its Scherer capacity on the wholesale market. And mindful of its obligations under the regulatory compact, Gulf did so. This resulted in the Scherer capacity not immediately becoming part of Gulf's retail rate base and Gulf taking the risk that it could market the capacity to enable it to earn a fair return.

Q. Was this the Commission's intent?

A. Based on my own recollection and my review of the record, I believe this was the Commission's intent. The Commission had the discretion to include the Scherer capacity in retail rate base and then recognize revenues from off-system sales to help cover Scherer's revenue requirements. However, in an effort to balance risks and still give a reasonable opportunity to Gulf to earn a fair return, the Commission chose to have the Scherer capacity temporarily become part of FERC jurisdiction via UPS contracts. It is clear that the Commission chose to have the Scherer-related costs and revenues separately accounted for so that they would not affect retail base rates. In other words, any amounts earned from the UPS contracts that could be considered to be deficient or excessive would not result in increased retail rates to cover the perceived wholesale deficiency or decreased retail rates to take advantage of any perceived excessive wholesale earnings. This is evidenced by the Commission's decision in Gulf's 1989 rate case to have retail rates remain unaffected even in the event of a default in one of the UPS contracts. This resulted in even greater risks being undertaken by Gulf and further pressure being placed on its ability to earn a fair return. Nevertheless, the Commission decided that it remained a fair allocation of risks.

IV. Appropriate Regulatory Treatment for Gulf's Interest in Plant Scherer

Q. What is the appropriate regulatory treatment for Gulf's interest in Plant Scherer?

A. The history of Gulf's investment in Plant Scherer clearly shows that the investment was made as the most cost-effective alternative to meet the needs of its retail customers and that the Commission agreed with this determination. Given this history, it is clear that Gulf's investment in Plant Scherer should ultimately be recovered from retail customers for whose benefit the investment was initially made. What is at question is by what means and during what time frame should cost recovery take place.

Q. Is it now appropriate for Gulf to seek retail cost recovery for Scherer 3?

A. Yes. Under Gulf's proposal for cost recovery, Gulf's investment in Plant Scherer would be recognized for the benefit of retail customers at its current net book value. The amount of the investment attributable to retrofits necessary to comply with requirements of applicable environmental regulations should be recovered through the ECRC. All remaining investment would become part of Gulf's retail rate base and should be reflected in earning surveillance reports. The timing would coincide with the expiration of the latest vintage of UPS contracts in an attempt to minimize, to the extent possible, the duration of Gulf's investment in Scherer being uncovered. This would be consistent with the regulatory compact in that costs and benefits would be matched and Gulf would be given a reasonable opportunity to earn a fair return on its investment.

Q. What if the Commission decides that Gulf’s investment in Plant Scherer should not be included as a retail asset at this time?

A. Given the significant long-term strategic benefits of maintaining highly efficient and environmentally compliant coal-fired generation, I believe this would be an unlikely outcome. However, such a determination would not relieve the obligation that any unrecovered costs should ultimately be recovered from retail customers for whose benefit the investment was initially made.

Q. What would be the practical consequence of such a situation?

A. A situation, in which the Commission decides that a long-lived asset is no longer needed for retail customers and does not otherwise provide for cost recovery, would rightfully be viewed as authorization to take steps to minimize cost exposure and economic losses by getting the asset off its books. The best way to do this would be to sell the asset in question.

Q. What would be the regulatory consequences of Gulf selling its interest in Plant Scherer?

A. If a sale were consummated, the regulatory treatment would be similar regardless of whether the sale resulted in a net gain or a net loss. Consistent with Commission policy, a sale of a utility asset at a gain would usually require that the gain be amortized above-the-line for the benefit of customers over a designated number of years, usually five years. However, the length of the amortization is at the discretion of the Commission and could hinge on how significantly the yearly amortizations affect earnings. Likewise, a sale of a utility asset at a loss (or the cancellation of a utility asset during construction) would require that the loss be amortized as an above-the-line cost over an appropriate number of years. The unamortized balances in the accounts (gain or loss) would also have impacts on the calculation of the utility's working capital allowance, which is a component of overall rate base.

Q. Are amortizations above-the-line the only means to recognize the consequences of a sale of utility assets?

A. No. There are other means such as adjusting accumulated depreciation reserve accounts or creating or reducing certain regulatory assets. However, amortizations have routinely been used as a matter of policy. In a recent water utility rate case, Docket No. 110200-WU, Order No. PSC-12-0435-PAA-WU, the Commission succinctly stated its policy:

> "Over the past five years, WMSI has sold assets that have resulted in gains and losses. It is our long-standing practice to amortize capital gains from the sale of specific assets over a period of five years to the benefit of the ratepayers.
>
> Based on this practice, the net capital gains (net of capital losses) on the sale of specific assets shall be recognized and amortized over five years." [Order, p. 28]

A good discussion of this is also contained in Order No. PSC-02-1727-PAA-GU in Docket No. 021014-GU. The particular situation described there was a gain on sale, but the regulatory principles also apply to a loss on sale or the cancellation of a utility asset under construction. The important point is that the sale or cancellation of a utility asset has consequences that should be recognized for regulatory purposes. Doing so would be consistent with the regulatory compact and balance the interests of customers and shareholders.

Q. Can you give an example of costs being amortized above-the line to effectuate cost recovery?

A. Yes. The very situation that led to the acquisition of Gulf's interest in Plant Scherer and the cancellation of the proposed Caryville Units is a perfect example. As I described earlier, the cancellation of the Caryville Units and the acquisition of a part of Plant Scherer was determined to be the best alternative for retail customers. Even though the unit was never constructed, the preliminary construction costs were recognized to be legitimate costs incurred for the benefit of retail customers, were included in retail rate base and were rightfully allowed to be recovered through above-the-line amortizations over five years.

Q. Can you give a more recent example?

A. Yes. A more recent example is the Commission's decision in 2009 to allow FPL to recover the cost of its cancelled Glades Power Park (GPP) Units 1 and 2. At the time of the Need Determination for these plants, the

Commission determined that FPL had failed to demonstrate that the proposed plants were the most cost-effective alternative available and declined to grant a determination of need for them. Consequently, FPL petitioned the Commission to allow recovery of the costs that had already been invested in the proposed GPP plants. Specifically, FPL requested the use of deferral accounting and the creation of a regulatory asset for its incurred preconstruction costs associated with the GPP plants. FPL further requested that the regulatory asset be deferred and amortized over a five-year period beginning when new base rates would be implemented.

Q. What was the basis for the Commission's decision?

A. The Commission allowed the costs of the GPP units to be placed in a regulatory asset and amortized above-the-line over a five-year period commencing at the time of FPL's next rate case. In doing so, the Commission reconfirmed the use of deferred accounting and the creation of regulatory assets to effectuate recovery of reasonable and prudent costs that otherwise would have to be immediately expensed. In its Order No. PSC-09-0013-PAA-EI, the Commission went on to define a regulatory asset and its appropriate use:

> "A regulatory asset involves a cost incurred by a regulated utility that would normally be expensed currently but for an action by the regulator or legislature to defer the cost as an asset to the balance sheet. This allows the utility to amortize the regulatory asset over a period greater than

one year instead of treating it as an expense in a single year." [Order, p. 2]

Q. How is the Commission's decision for the GPP costs relevant to the Commission's consideration of Gulf's investment in Plant Scherer?

A. It is directly on point. In both situations, the issue is whether previously incurred costs of electrical generating plants should be included in retail rates on a going-forward basis. For GPP, the Commission decided that the project should not be continued and that previously incurred costs should not become part of FPL's rate base on a going-forward basis (except for working capital effects). As such, the Commission allowed recovery of the previously incurred costs by means of deferred accounting and amortization of the associated regulatory asset. The issue is relevant for Gulf's investment in Plant Scherer only if the Commission decides that Plant Scherer should not be included in Gulf's retail rates as an operating asset. In that event, the remaining unrecovered costs of Gulf's investment in Plant Scherer should be afforded deferred accounting and recovery by amortization of the associated regulatory asset in Gulf's next rate case. This would be consistent with the regulatory compact and previous decisions of the Commission.

V. ECRC Eligibility

Q. Gulf is seeking recovery of a portion of its investment in Scherer 3 in the ECRC. Is this appropriate?

A. Yes. The portion of Gulf's investment in Scherer 3 made to comply with environmental requirements should be eligible for recovery through the ECRC, just like other such investments made in other Gulf power plants. As a matter of policy, the fact that Gulf's investment in Scherer 3 has been temporarily assigned to the wholesale jurisdiction should not now disqualify it for eligibility as part of the ECRC. Of course, Gulf has the burden to factually demonstrate that the costs meet the requirements for recovery through the ECRC. I defer to the testimony of Gulf Witnesses Burleson, Markey, and Boyett for that factual proof.

Q. What are the applicable requirements for recovery of costs through the ECRC?

A. The requirements are set forth in Section 366.8255, Florida Statutes and the Commission's Order No. PSC-94-0044-FOF-EI. This order was the first time that the Commission implemented this statutory section and in it the Commission established three criteria for costs to be recovered through the ECRC:

1. such costs were prudently incurred after April 13, 1993;
2. the activity is legally required to comply with a governmentally imposed environmental regulation enacted, became effective, or whose effect was triggered after the company's last test year upon

which rates are based; and,

3. such costs are not recovered through some other cost recovery mechanism or through base rates.

Q. Do the Scherer environmental costs meet the first criterion?

A. Yes. As explained in greater detail by Mr. Burleson and Mr. Markey, all of the Scherer environmental investments were incurred well after 1993 and went in service between 2009 and 2011.

Q. Do the Scherer environmental costs meet the second and third criteria?

A. Yes. As explained in greater detail by Mr. Burleson and Mr. Markey, the Scherer environmental investments were made to comply with the Georgia Multi-Pollutant Rule, which was adopted in 2007 to reduce emissions of mercury, SO_2, and NOx state-wide. Since Gulf's entire investment in Scherer 3 was then part of the wholesale jurisdiction, there has not been a retail rate case in which these costs could have been considered for recovery through a retail base rate proceeding or some other rate recovery mechanism.

Q. Has the Commission previously addressed the question of whether past investments may be recovered through the ECRC?

A. Yes. When first implementing Section 366.8255, the Commission addressed the situation of investments made for environmental compliance that were made before April 13, 1993, the date that the statute was enacted. The Commission determined that the ongoing carrying costs of past investments would be eligible for recovery through the ECRC. In its Order No. PSC-94-0044-FOF-EI, the Commission stated:

> "We considered the date the carrying cost is incurred by the utility rather than when the actual capital investment was made when determining whether an environmental cost is incurred after April 13, 1993. It is possible for an investment to have occurred prior to April 13, 1993 and still have carrying costs which can be recovered through the environmental cost recovery factor." [Order, p. 2]

Q. Is this relevant to the eligibility for ECRC recovery of Scherer 3 environmental capital costs?

A. This determination makes it clear that the ongoing carrying costs of the past environmental investments in Scherer 3 after the expiration of the UPS agreements are eligible for recovery.

Q. Does the Commission recognize that a delay in seeking cost recovery through the ECRC may be justified, if doing so has the possibility of a more cost-effective method of compliance?

A. Yes.

Q. Is this relevant to Scherer 3 environmental costs?

A. Yes. Consistent with the Commission's policy of using off-system or wholesale sales as bridging tools to provide more cost-effective service to customers, Gulf entered into wholesale contracts for Scherer 3 capacity.

This resulted in wholesale customers paying for the operating costs and the carrying costs (including depreciation) of the Scherer 3 environmental investments for a number of years. This reduced costs for retail customers. Thus, the delay in seeking recovery of Scherer 3 environmental costs while Scherer 3 was subject to the wholesale contracts is consistent with this policy objective.

Q. What would be the consequences of a decision to declare that the Scherer 3 environmental costs are now ineligible for ECRC recovery?

A. It would be inconsistent with earlier policy pronouncements of the Commission and inconsistent with the statute creating the ECRC mechanism.

VI. Scherer 3 Conclusion

Q. What is your conclusion?

A. Based on my own recollections and my review of the record, it is clear that Gulf's investment in Plant Scherer was made as the most cost-effective alternative to meet the needs of its native load customers and that the Commission agreed with this determination. Given this history, it is clear that Gulf's investment in Plant Scherer should ultimately be recovered from native load customers for whose benefit the investment was initially made. Thus cost recovery of Scherer 3 should now be allowed in rates. This should be done by including the eligible environmental costs of Scherer 3 in the

ECRC and the non-environmental costs of Scherer 3 in base rates. Doing so would be consistent with the regulatory compact and the expectations that existed at the time Gulf initially made its investment in Plant Scherer and when the subsequent environmental investments were made.

I also conclude that Gulf's investment in Plant Scherer has reached a critical crossroads. In its efforts to best plan for its retail customers and due to unforeseen changes in demands, Gulf's investment in Plant Scherer has remained out of retail rates far longer than anticipated. It is clear to me that Gulf needs affirmation that Plant Scherer is appropriately included as a retail asset under the regulatory compact and Florida regulatory policies.

This affirmation should be provided by including Gulf's investment in Plant Scherer in Gulf's retail rates, including both the applicable portion in the ECRC and base rates. Doing so would be consistent with the regulatory compact. It would also be consistent with the policy of providing a high degree of certainty for cost recovery for long-lived assets to facilitate long-term planning for the benefit of customers. Concluding otherwise could send a chilling message concerning long-term planning and the willingness of utilities to find ways to lessen cost impacts on customers.

A decision to not allow recovery of Scherer 3 in the ECRC and ultimately base rates as an operating asset would not relieve the regulatory obligation to provide cost recovery by some means, such as the use of deferred accounting and the amortization of the associated regulatory asset. Ultimate cost recovery is needed and hopefully can be effectuated by means short of a sale of Gulf's interest in Plant Scherer that would foreclose the strategic benefits of maintaining cost-effective and environmentally compliant coal-fired generation in Gulf's generation mix.

VII. CCR Costs at Plant Scholz

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

A. The purpose of my testimony is to address, from a Commission policy perspective, the eligibility of the CCR costs at Plant Scholz for recovery through the ECRC. I defer to the testimony of Mr. Boyett and Mr. Markey for the factual support of cost recovery through the ECRC.

Q. On what basis is Gulf seeking the recovery of CCR costs at Plant Scholz?

A. As more fully discussed in the testimony of Mr. Markey, Gulf is seeking recovery of CCR costs associated with the closure of the CCR pond at Plant Scholz. These costs were allowed to be recovered in last year's ECRC proceeding pending the submittal of a final closure plan. Issues raised by OPC concerning the eligibility of these costs were also deferred until the current ECRC proceeding. The final closure plan was approved by the Florida Department of Environmental Protection (FDEP) on August 26, 2016, and a copy of the approval letter is found in Mr. Markey's Exhibit RMM-2.

Q. On what basis did OPC raise concerns about the eligibility of the Scholz CCR costs?

A. The prehearing order in last year's proceeding, Order No. PSC-15-0511-PHO-EI, set forth OPC's position that the Scholz CCR costs do not meet the requirements of Section 366.8255, Florida Statutes for recovery through the ECRC. Apparently OPC believed at the time that the Scholz CCR costs are not a requirement of an environmental law or regulation, due to Gulf having entered into a settlement to resolve a lawsuit involving the Scholz CCR pond prior to Gulf submitting the plan for its closure to the FDEP for approval.

Q. Are the Scholz CCR costs eligible for recovery under the ECRC?

A. Yes, I believe the costs are eligible because they are being incurred to comply with a governmentally imposed environmental regulation, as more fully addressed by Mr. Markey. The fact that the closure plan contains terms that are consistent with a settlement agreement to resolve a lawsuit does not make the associated costs ineligible for recovery. As Mr. Markey discussed, the FDEP has ultimate approval authority over the closure plan and was not bound by Gulf's settlement with the third party. Even if FDEP was bound by the settlement with the third party, the costs would be eligible for recovery if it meets the other criteria in Section 366.8255, Florida Statutes.

Q. Has the Commission previously allowed recovery through the ECRC of costs incurred pursuant to a settlement?

A. Yes. In Docket No. 000685-EI, the Commission allowed ECRC recovery of costs for Tampa Electric Company (TECO) associated with two settlements reached with the United States Environmental Protection Agency (EPA) and the FDEP. The first settlement was in the form of a Consent Final Judgment (CFJ) with the FDEP, which was followed by a Consent Decree with the EPA that incorporated all of the requirements contained in the CFJ plus additional requirements. As a result, on June 2, 2000, TECO petitioned for cost recovery of the Big Bend Units 1, 2, and 3 Flue Gas Desulfurization System Optimization and Utilization Program (FGD Plan) through the ECRC. Developing this plan was required by the CFJ and the Consent Decree. The Commission determined that the associated costs were eligible for recovery and allowed their recovery through the ECRC.

Q. In addition to declaring such costs to be eligible for recovery, did the Commission also make a policy pronouncement concerning the recovery of such costs?

A. Yes, the Commission determined that allowing recovery of such costs would encourage negotiations that could ultimately lessen costs for customers. In its Order No. PSC-00-1906-PAA-EI, the Commission stated:

> "From a policy perspective, we believe that to deny recovery of the incurred costs creates a disincentive for utilities to be vigorous negotiators. If we were to deny recovery of the costs incurred under TECO's circumstances, we would be sending a message to utilities to acquiesce in negotiations just so the issues can be resolved in time to file a petition before incurring costs. Under such a scenario,

utilities might incur greater costs than necessary, to the ultimate detriment of the ratepayers." [Order, p. 9]

Q. Was this same Consent Decree the subject of further proceedings at the Commission?

A. Yes. In Docket No. 050958-EI, TECO sought ECRC approval of additional projects designed to comply with the Consent Decree. OPC opposed these projects for recovery arguing that they were not required and were discretionary. The Commission allowed recovery and rejected OPC's position. In its Order No. PSC-07-0499-FOF-EI, the Commission described the Consent Decree thusly: "Clearly, the Consent Decree has been established as an eligible environmental compliance requirement for TECO pursuant to the statute and Commission policy." [Order, p. 8] The Commission went on to describe the policy aspect of its decision:

> "Under economic regulation, TECO is required to take prudent and reasonable actions to minimize the environmental compliance cost impact to its customers before funding a project, whether the project is funded through base rates or the ECRC. The cost-benefit analysis of the FGD Reliability Program that TECO conducted demonstrates the program's desirability as a compliance option. It cannot be construed as an indication that the program is discretionary and driven by its own desirability." [Order, p. 9]

Q. Has the Commission added any additional clarity when determining whether a project is eligible for recovery through the ECRC?

A. Yes, the Commission did so in a case involving modular cooling towers at Progress Energy Florida's Crystal River plants, Docket No. 060162-EI. While acknowledging OPC's concerns, the Commission allowed recovery of the modular cooling towers through the ECRC and asserted the need for flexibility in the application of the ECRC statute, as long as the basic criteria of the statute were met. In its Order No. PSC-07-0722-FOF-EI, the Commission stated:

> "Further we are not persuaded that a decision to approve the eligibility of the modular cooling towers project would lead to the scenario OPC's witness Hewson describes, as long as we continue to require a direct nexus between the project, its compliance costs, and the relevant environmental requirement." [Order, p. 8]

Q. Are these decisions relevant to the issue of Gulf's Scholz CCR costs?

A. Yes, they demonstrate that costs incurred pursuant to a settlement are permissible as long as the other statutory criteria are met. They further emphasize the need for negotiations in making efforts to reduce costs for customers. In determining if there is a requirement for a project, there needs to be a nexus between the project and the relevant environmental requirement. As more fully described in the testimony of Mr. Markey, there is a direct nexus with the Scholz CCR costs and applicable environmental regulations.

Q. Does this conclude your testimony?
A. Yes, it does.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
Jeffrey A. Burleson
Docket No. 160007-EI
Date of Filing: September 1, 2016

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

A. My name is Jeff Burleson. My business address is 600 North 18th Street, Birmingham, AL 35203, and I am the Commercial Services and Planning Vice President for Southern Company Services (SCS).

Q. Please summarize your background and professional experience.

A. I have more than 35 years of experience in the electric utility industry. I began my career with Alabama Power Company in 1980 as a cooperative education student. I graduated from the University of Alabama at Birmingham in 1984 with a Bachelor of Science degree in Electrical Engineering, with a specialization in power systems analysis. From 1984 to 1991, I held various staff and managerial positions in the Technical Services and Power Quality departments at Alabama Power Company. During this period, I attended Auburn University and earned a Master of Science degree in Electrical Engineering in 1987, again, with a specialization in power systems analysis.

In 1991, I transferred to SCS in the position of Manager of End Use Technology Research, where my responsibilities included technology assessment, various types of load and economic modeling in support of integrated resource planning, and development of certain models used in integrated resource planning. In 1996, I was named Assistant to the Vice President of Marketing and New Business Development at SCS. In 1997, I was named General Manager of Marketing Services, where my responsibilities included oversight of the SCS analytical services associated with peak demand and long term energy forecasts, load research, cost of service studies, and competitive intelligence.

In 1999, I transferred to Georgia Power as Manager of Market Planning, where my responsibilities included the load, energy and revenue forecasts, economic evaluation of demand-side management programs and assessment of demand response from certain rate designs. In 2005, I was appointed Director of Resource Policy and Planning for Georgia Power where my responsibilities included integrated resource planning, resource procurement, generation development and administration and oversight of power purchase agreements (PPAs).

In 2011, I was appointed Vice President of System Planning for SCS. In this role my responsibilities included oversight of the analytical and planning services provided to the retail operating companies for integrated resource planning, reliability planning, resource procurement, generation strategy, generation development, and various economic viability analyses.

In 2016, in addition to my System Planning responsibilities I assumed responsibility for Financial and Contract Services, Southern Wholesale

Energy, and Budgeting and Reporting for SCS Operations. As a result, my title changed to Vice President of Commercial Services and Planning for SCS.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide an overview of Gulf Power Company's (Gulf) resource planning and procurement activities over the past few decades, why Gulf made capital investments in additional environmental controls for Plant Scherer Unit 3 (Scherer 3), and how those investments were determined to benefit Gulf's customers.

Q. What are the major environmental capital investments that you plan to discuss?

A. Gulf Power installed a baghouse at Scherer 3 in 2009 for mercury reduction, a selective catalytic reduction system (SCR) in 2010 for nitrogen oxide (NO_x) reduction, and a flue gas desulfurization system (FGD or scrubber) in 2011 for sulfur dioxide (SO_2) reduction.

Q. Are you sponsoring any exhibits?

A. Yes. Exhibit JAB-1 is a joint exhibit sponsored by myself and Gulf Witness Deason. Exhibit JAB-1 is a chronology of key planning and regulatory events regarding Gulf's purchase and ownership interest in Scherer 3.

I. Gulf's Resource Planning

Q. What is the purpose of Gulf's resource planning activities?

A. The objective of Gulf's resource planning activities is to assure the Company's ability to provide reliable and cost-effective electric service to its customers, while accounting for the inherent uncertainty of the future.

Q. Please provide an overview of Gulf's participation in the Southern Company electric system pooling of generation, the associated coordinated planning process, and its relationship to planning for Scherer 3.

A. The operating companies of the Southern Company electric system have entered into an agreement known as the Intercompany Interchange Contract (IIC), thereby agreeing to operate as a single integrated electric system or power pool. Under terms of the IIC, the generating resources of all member companies are economically dispatched at actual variable cost to serve the total system load requirements. The IIC and its pooled operation of generating resources on the Southern Company electric system provides for the operating companies to participate in coordinated planning of future generation capacity. The coordination of planning across the retail operating companies assures that the overall electric system remains optimized in terms of reliability and cost and thus assures that each operating company's customers receive benefits as a result of the more reliable and cost effective electric system.

Q. What are the benefits to Gulf's customers from the pooling arrangement and its associated coordinated planning process?

A. The benefits received by Gulf's customers include, but are not limited to, the following:

1. Economies of scale through coordination of electric operations.
2. Each operating company retains its lowest variable cost resources to serve its own customers. Each operating company's excess energy is then made available at actual variable cost to the other operating companies to serve their customers if the cost of the Pool energy is less than the cost of energy from their own resources.
3. Reduced requirements for operating reserves.
4. Marketing of Pool energy and capacity in the shorter-term wholesale markets, with resulting gross margins shared with all the operating companies.
5. Peak-hour load diversity, resulting in a lower target planning reserve margin requirement for Gulf.
6. Temporary sharing of surplus/deficit reserve capacity as a result of coordinated planning.
7. Ability to cost-effectively install large, efficient generation units.

These multiple benefits that accrue to Gulf and the other system operating companies result from the coordinated planning and operation of the power pool.

In addition to the above listed benefits, the ability of the operating companies to rely on SCS for the administration of the pooled economic dispatch of the system and for certain technical aspects of each operating company's decision support and planning responsibilities avoids duplication of personnel in the various operating companies. Access to the shared resources provided by SCS is valuable since each operating company would otherwise have to employ additional professional and technical personnel with specialized expertise who might not be fully utilized on a continuous basis.

Q. Please provide an overview of the coordinated planning process in which Gulf participates.

A. At the most basic level, the Company's planning process yields a load forecast that drives a schedule of supply-side and demand-side resource additions that are integrated to accomplish the objectives of providing reliable and cost-effective electric service to its customers, consistent with the Company's duties and obligations to the public as a regulated public utility. The coordinated planning process is consistently utilized by each of the Southern Company retail operating companies, with the assistance of their agent SCS. As a part of the coordinated planning process, each retail operating company develops its own load forecast and demand side plan. The load forecasts and demand side plans of the operating companies are aggregated and an optimal mix of new capacity additions is identified to meet the aggregate load of the retail operating companies. The capacity need for each future year is allocated to each operating company that is projected to have a capacity need in a given year. The allocation of the capacity need is proportional to the amount of capacity needed to move each of the operating companies that have a capacity need in a given year to the target planning reserve margin based on each operating company's own load and existing resources. Each operating company then makes its own decisions about how to best meet the capacity need and the type of resource to meet that need.

A major benefit to the operating companies of the coordinated planning process and the IIC's reserve sharing mechanism has been the ability to select the most economical generating unit size when new generation needs exist on the Southern Company electric system. As an example, Gulf has been able to completely own or purchase shares of 500 MW and 800 MW state-of-the-art generating units. This capacity has been purchased or developed at lower cost per kW and is more efficient generation than would otherwise have been available to a relatively small company such as Gulf.

The operating companies also benefit from the diversity of power needs as a result of the system providing service to such a large geographical region. The territories of the system companies have weather, time zone, and customer mix differences. These differences result in variations in load patterns because the operating companies loads do not all reach their peak at the same time. This load diversity has several benefits. It improves overall system load factor, thereby lowering cost per unit. It also lowers the necessary target planning reserve margin requirement for the system and for each operating company, thus creating cost savings for customers.

Q. Is the coordinated planning process you described only applicable to retail customers?

A. No. The objective of the coordinated planning process is to provide a reliable and cost-effective electric supply for all native load customers.

Q. Please explain what is meant by the term “native load customers.”

A. Gulf is a public utility operating in Florida under Chapter 366 of the Florida Statutes. As such, Gulf’s primary focus is on serving the needs of its retail customers in Northwest Florida. However, just as it does today, during the time frame when Gulf’s existing generation, including Scherer 3, was being planned and constructed, Gulf also provided requirements wholesale service to other retail electric providers in Northwest Florida. When providing requirements wholesale service to other retail electric providers, Gulf has a contractual obligation to plan for, and to meet, the capacity and energy growth needs of the requirements wholesale customers for the term of the wholesale sales contract. The term native load customers is used to describe the combination of Gulf’s retail customers with the requirements wholesale customers within Northwest Florida.

Q. How long has Gulf been benefiting from the decision support and coordinated planning process you describe?

A. The coordinated planning process has been in place and has provided benefits for Gulf's customers for many decades.

Q. Are the planning objectives for native load customers any different today than in previous decades?

A. No. The overall objectives of coordinated planning remain unchanged.

Q. Are the planning processes for native load customers any different today than in previous decades?

A. No. The overall planning process that has served customers well over the past decades remains unchanged, except for minor refinements to the processes and improvements to the modeling tools used in the planning process.

Q. Please provide an overview of the planning landscape during the 1970's and 1980's.

A. During the late 1960's and early 1970's, electricity demand in Gulf's territory was growing rapidly, in part due to economic growth but also due to rapid increases in the penetration of room and central electric air conditioning systems in homes.

The federal government enacted the Clean Air Act of 1970 and in that same year established the U.S. Environmental Protection Agency (EPA). In 1974, EPA issued new rules governing the "prevention of significant deterioration of air quality" (PSD). A few years later, the federal government enacted the Clean Air Act amendments of 1977. By the fall of 1977, it became apparent that all new coal generation whose construction had not already begun would have to be equipped with emissions controls such as flue gas desulfurization (FGD).

In 1973, an oil embargo was instituted against the U.S. at a time of declining domestic crude oil production, rising demand, increasing imports, and decreased OPEC production. The embargo created short-term shortages and within about six months caused world oil prices to triple to $12 per barrel. A second oil crisis began in 1979 and resulted in oil prices rising from $14 per barrel at the start of 1979 to $35 per barrel by January 1981. In addition to the oil embargo that began in 1973, a stock market crash occurred in that same year wherein the Dow Jones Industrial Average lost more than 45 percent of its value between January 1973 and December 1974.

During the period November 1973 to November 1982 three U.S. recessions occurred resulting in rising unemployment, rising inflation, rising interest rates and stagnating economic growth. These macro-economic events coupled with a saturating market for electric air conditioning led to sharp declines in load forecast growth rates across most all of the electric utility industry.

Q. Please provide an overview of Gulf's resource planning decisions during the 1970's.

A. Gulf completed the construction of Plant Crist Units 6 & 7 in 1970 and 1973, respectively. In 1973, Gulf projected a need for two additional coal units, Smith Units 3 & 4, with in service dates of 1979 and 1981, respectively. In February 1974, the site for the two planned coal units was moved from the Plant Smith site to the Caryville site, with the planned units then being referred to as Caryville Units 1 & 2 (Caryville 1&2). Caryville 1&2 were being planned as 518 MWs each with the same 1979 and 1981 in service dates as were originally targeted for Smith Units 3 & 4. By October 1974, the targeted in service dates for Caryville 1&2 were deferred to 1980 and 1981, respectively, as a result of the oil embargo and the slowing of both economic growth and growth rates of load forecasts. In October 1975, Gulf planned to purchase an ownership interest in Plant Daniel Units 1 & 2, which went in service in 1977 and 1981, respectively. At the same time, Caryville 1&2 were deferred to 1982 and 1984, respectively, as a result of the planned Plant Daniel ownership interest.

In May 1976, the Caryville site was certified by the Florida Governor and Cabinet when they approved the January 1976 Department of Administrative Hearings (DOAH) recommended order to certify the site for up to six 500 MW units and approved commencement of the development of the first two units at the site. The DOAH order acknowledged Florida Public Service Commission (FPSC) participation and all parties agreed on the need for, and authorization of, Caryville units 1&2. In 1977, Gulf purchased an ownership interest in Plant Daniel Unit 1 with the intent of also purchasing an interest in Plant Daniel Unit 2 once it was completed. The planned, combined interest in Plant Daniel Units 1 & 2 was in lieu of Plant Caryville Unit 2. This decision to purchase an interest in Plant Daniel Units 1 & 2 provided cost savings to Gulf's customers since the Plant Daniel units had started construction prior to the effective date of the 1977 Clean Air Act amendments.

In August 1978, Gulf notified the FPSC of the potential opportunity for an ownership interest in 430 MWs of Plant Scherer, which had also begun construction prior to the effective date of the 1977 Clean Air Act amendments. As part of the notification, Gulf informed the FPSC that purchasing an ownership interest in Plant Scherer would enable Caryville Unit 1 to be cancelled. In late 1978, Caryville Unit 1 was cancelled as a result of Gulf's planned ownership interest in Plant Scherer and the FPSC accounting director issued a letter to Gulf affirming Gulf's request for accounting treatment of the Caryville cancellation charges but informing Gulf that action on recovery through rates would have to be addressed in a later proceeding.

Q. Please provide an overview of Gulf's resource planning decisions during the 1980's.

A. In 1980, the FPSC issued Order No. 9628 in Docket No. 800001-EU agreeing that a Gulf ownership interest in Plant Scherer would be more economic than Caryville Unit 1 and authorized Gulf to amortize the Caryville cancellation charges and include the unamortized balance in rate base as a result of the planned purchase of an ownership interest in Plant Scherer. On February 16, 1981, Gulf participated in an informal workshop held by the Commission concerning the merits of purchasing a 25 percent ownership interest in Plant Scherer Units 3 & 4. This workshop also addressed Gulf's plan to enter into long-term off-system sales for the early years of the unit to temporarily relieve native load customers of revenue requirement responsibility for the unit. On February 19, 1981, the initial agreement between Gulf and Georgia Power Company was entered into for Gulf to purchase a 25 percent ownership interest in Plant Scherer Units 3 & 4. In 1981, Gulf purchased an ownership interest in the then completed Plant Daniel Unit 2. In December 1983, Gulf confirmed with Georgia Power Company that Gulf's potential interest in a 25 percent ownership share of Plant Scherer Unit 3 remained but that Gulf's potential interest in ownership of Plant Scherer Unit 4 no longer existed. In March 1984, the initial agreement between Gulf and Georgia Power Company was amended to reflect that Gulf was committed to a 25 percent ownership interest in only Scherer 3. In October 1984, the U.S. Securities and Exchange Commission issued an order authorizing the sale and acquisition of a 25 percent interest in Scherer 3 between Georgia Power Company and Gulf.

In 1982, UPS agreements were finalized to sell capacity and energy from Scherer 3 (inclusive of Gulf's ownership) to Florida Power and Light, Jacksonville Electric Authority and Gulf States Utilities. The UPS sale was intended to relieve retail customers from the revenue requirements in the early life of the unit. In 1986, Gulf States Utilities filed a lawsuit seeking release from its unit power sales obligations. Starting with the January 1, 1987 commercial operation date of Scherer 3, a portion of its capacity began serving retail customers and was included in Gulf's surveillance filings to the FPSC. In 1988, UPS agreements were finalized with Florida Power and Light and Jacksonville Electric Authority to sell capacity from Scherer 3 through May 2010, further relieving retail customers from the revenue requirements. In that same year, a UPS agreement was finalized with Florida Power Corporation to sell the remaining Scherer 3 capacity through May 2010.

Q. Please provide an overview of Gulf's key resource planning decisions during the 1990's.

A. In the late 1990's, Gulf secured short-term purchased power for the years 2000 and 2001 to provide needed capacity and issued an RFP in 1998 to meet 2002 capacity needs. In 1999, Gulf requested and received authorization from the FPSC to begin construction on the Plant Smith Unit 3 combined cycle natural gas generation facility with a planned commercial operation date of 2002.

Q. Please provide an overview of Gulf's resource planning decisions during the 2000's and 2010's.

A. Plant Smith Unit 3 began commercial operation in 2002. In 2004, new PPAs were executed with Florida Power and Light, Progress Energy Florida, and Flint Energies for capacity and energy from Scherer 3 beginning delivery in 2010 with the end of term ranging from December 2015 through December 2019, depending on the contract. While the FPSC did not need to approve Gulf's role in the PPAs since that is under the jurisdiction of the Federal Energy Regulatory Commission it did approve the capacity purchase commitments made by both Florida Power and Light and Progress Energy Florida.

In February 2006, Gulf issued an RFP to fill its capacity need starting in 2009. The RFP resulted in the October 2006 execution of PPAs for almost 500 MWs of capacity and energy from the Dahlberg and Coral Baconton generation facilities to serve Gulf's native load capacity needs from June 1, 2009 through May 31, 2014. In 2008 Gulf was preparing to issue an RFP for supply starting in 2014 for resources that would compete against a potential combined cycle natural gas unit to be constructed at the Plant Crist site. However, Gulf was approached by Shell Energy North America about possible interest in an attractively priced PPA for capacity and energy from the Central Alabama combined cycle natural gas facility. Gulf entered into the PPA for Central Alabama in March 2009, the FPSC subsequently approved the Central Alabama PPA for service to Gulf's retail customers from November 1, 2009 through May 24, 2023.

In addition to the Central Alabama PPA, Gulf has executed energy purchase agreements with providers of renewable energy generated by municipal solid waste, solar, and wind facilities.

Q. What is the basis for the summary of Gulf's historical generation decision making that you describe above?

A. Mr. Deason and I reviewed a number of historical documents and worked together on the development of Exhibit JAB-1, which is a chronological summary of the key planning and regulatory events and decisions associated with Gulf's 25 percent ownership interest in Scherer 3. Additionally, I relied on other Company information and knowledge of general Company, U.S. and world events that transpired over this historical period.

II. Gulf's Current Generation Outlook

Q. Please provide an overview of the resource planning landscape facing Gulf today.

A. As can be observed from the historical events I describe above, long term planning has always involved uncertainty. Gulf's current resource planning landscape is no different. There is uncertainty regarding the long term rate of U.S. economic growth, the long term rate of Gulf's load growth, future natural gas price volatility, the timing and amount of natural gas price increases, future potential environmental regulations that could impact both natural gas and coal production as well as utilization. Compounding the planning challenges associated with these uncertainties is the fact that commitments to dispatchable generation additions are typically required to be made many years in advance and typically get added as "lumpy" capacity additions. The long, multi-year lead times are necessary to allow for engineering, permitting and construction of the generation as well as development of associated electric transmission infrastructure that is typically needed. The “lumpiness” of generation additions is a result of the fact that the major components of dispatchable generation come in discrete sizes and that the most efficient and economic generation sizes typically don’t match well with any given year’s capacity need.

Despite the uncertainties, the long lead times and the “lumpiness” associated with generation additions, what is certain is Gulf’s obligation to serve its customers with reliable and economic electric service. From a planning perspective, this obligation combined with the previously discussed planning challenges results in commitments to generation additions that virtually never exactly match the timing or amount of capacity need. This mismatch between the amount and timing of the need for capacity and the Scherer 3 rededication to retail service is the case facing Gulf today, just as it was the case in virtually every dispatchable generation addition that has been previously made by Gulf and approved by this Commission. Because of the long lead times associated with dispatchable generation additions and the uncertainties associated with planning, these mismatches between the amount and timing of needed capacity versus future generation additions will continue to exist in the future. So, these types of mismatches existed in the past, they exist today and they will continue to exist in future generation additions.

Q. Despite the mismatch you previously described, how does the rededication of Scherer 3 to retail service relate to Gulf's future resource plans?

A. The rededication of Scherer 3 to native load service complements Gulf's resource plans by offsetting a portion of the lost fuel diversity associated with recently retired coal-fired units, serving as a hedge to the volatility of natural gas prices and avoiding the need for 210 MWs of future capacity additions that would otherwise be needed.

Q. Please describe the change in fuel diversity associated with Gulf's generation resource changes.

A. Since April 2015, Gulf has retired four coal fired generating units at Plant Scholz and Plant Smith representing almost 450 MWs of generation capacity. The rededication to retail service now of Scherer 3's 160 MWs of Powder River Basin (PRB) coal-fired capacity (with rededication of the remaining 50 MWs by 2020) restores a portion of the lost fuel diversity in Gulf's energy mix.

Diversification is a recommended approach in the financial community to address uncertainty and volatility of markets. Likewise, diversification of energy resources is a valuable approach to address uncertainty in natural gas prices and future environmental requirements. By rededicating energy from the environmentally well-controlled, low variable cost Scherer 3 unit to Gulf's resource mix, Gulf's customers will continue to be served by a diverse fuel mix.

It is also important to maintain diversification to ensure a high level of reliability. By diversifying the type of fuel used for electricity generation, the supply basins from which that fuel is procured and the transportation providers and infrastructure that move the fuel from the fuel basin to the generator, the risks of disruption of fuel delivery to the generation fleet are reduced. If a given fuel supply basin is temporarily unusable due to natural, regulatory or other reasons, having a diverse source of fuel supply basins helps minimize fuel supply disruption to the generation fleet. Likewise, if a given fuel transportation provider or a portion of fuel transportation infrastructure is temporarily unavailable due to natural, regulatory or other manmade reasons, having a wide variety of fuel transportation sources is helpful to ensure fuel is available to provide reliable electric service to customers.

Q. Please describe how Scherer 3's rededication complements Gulf's fuel hedging activities.

A. The reintegration of Scherer 3, with its low price volatility PRB coal fuel complements the recent change to Gulf's natural gas fuel hedging program, which reduced Gulf's target natural gas hedge volume. Scherer 3's rededication to retail service enables the use of its low variable cost, PRB coal, and allows its dispatchability to serve as an inherent fuel hedge. Maintaining a diverse array of dispatchable resources is a highly-effective hedge against volatile natural gas prices. A diverse array of dispatchable resources is more effective as a hedge than either financial natural gas hedges or 100 percent fixed price renewables because the utilization of the dispatchable resource can be varied in direct response to the price of natural gas. This variation in dispatchable resource utilization can displace natural gas in periods of high natural gas price and can be displaced by natural gas in periods of low gas price.

III. Scherer 3 Environmental Capital Investments

Q. What is the purpose of the environmental capital investments Gulf has made at Scherer 3?

A. The environmental capital investments Gulf made at Scherer 3 equipped the unit with the latest environmental controls to reduce emissions of sulfur dioxide, nitrogen oxides, and mercury, which are byproducts of the combustion process. A baghouse reduces mercury emissions by injecting a sorbent into the flue gas to combine with mercury which is then collected in large fabric bags. A flue gas desulfurization system, or a scrubber, removes sulfur dioxides (SO_2) from the flue gas stream of the plant by using limestone to react with the SO_2 gas, forming gypsum. A selective catalytic reduction system, or SCR, reduces the emissions of nitrogen oxides (NO_x) by using ammonia to react with the NOx in the presence of a catalyst to produce water vapor and nitrogen.

Q. Why were these investments made at Scherer 3?

A. In March 2005, the EPA published the final CAIR, a cap and trade rule that reduces power plant SO_2 and NOx emissions found to contribute to nonattainment of the 8-hour ozone and fine particulate matter standards in downwind states. Twenty-eight eastern states, including Florida, Georgia and Mississippi, were subject to the requirements of the rule. Under CAIR, each of the affected states were required to submit state implementation plans, or SIPs, which would specify the requirements for the power plants in that state. Additionally, the EPA in 2005 issued the Clean Air Mercury Rule (CAMR) to reduce mercury emissions. In response to these EPA rules, the State of Georgia also issued the Georgia Multi-Pollutant Rule (GaMPR) in 2007 requiring installation of SCRs and scrubbers, and in some cases baghouses, on certain coal-fired generating units in Georgia by specific dates, including Scherer 3. GaMPR required Scherer 3's owners (Gulf Power and Georgia Power) to install a baghouse on Scherer 3 by June 1, 2009, and a scrubber and SCR on Scherer 3 by July 1, 2011.

Q. What alternative to making these environmental capital investments did Gulf Power have under the Georgia Multi-Pollutant rule?

A. The only alternative to the installation of the environmental controls specified in the rule (baghouse, SCR, and scrubber for Scherer 3) was to cease to operate the unit after the specified deadline. Essentially, the choice was either to invest in the environmental controls or to retire the unit.

Q. Was there an economic analysis of the investments from a customer perspective?

A. Yes, in 2006, an economic analysis was performed to evaluate the two options of either making the required environmental capital investments at

Scherer 3 or retiring the unit. The case included an investment in all of the environmental controls needed to comply with GaMPR, which included the baghouse, FGD, and SCR.

Q. What were the results of that economic analysis?

A. The analysis showed that investing in the environmental controls was in the best interest of customers, as compared to the alternative of retiring the unit. In the base case, the analysis showed overwhelming benefits for all Gulf customers to make these investments and continue to operate the unit. In addition to the base case, 41 sensitivities were analyzed, which varied factors such as natural gas prices, capacity prices, capital costs, and O&M costs. The base case concluded there was $228 million in 2006 net present value benefits to Gulf's customers, with the sensitivities producing a range of $85 million to $519 million of benefit for customers on a net present value basis in 2006 dollars. So in all 42 cases, making the environmental capital investments and continuing to operate Scherer 3 was in the best interest of customers.

Q. Has Gulf received any compensation for those capital investments to date?

A. Yes. At the time the SCR and scrubber became operational (and one year after the baghouse was installed) the output from Gulf's ownership interest in Scherer 3 was committed to Florida Power & Light (FPL), Florida Power Corporation (now Duke, or DEF) and Flint Electric Membership Corporation (now Flint Energies, or Flint) under PPAs that had been executed in 2004 for terms beginning on June 1, 2010. Under the provisions of these contracts, Gulf Power was allowed to recover any increased costs that were associated with a change in law. As a result of the new GaMPR, CAMR, and CAIR requirements, change-in-law notices were sent to each of the PPA customers (FPL, DEF, and Flint), and negotiations were completed to ensure that Gulf Power received appropriate compensation for the fixed and variable costs associated with the environmental controls that were applicable to the terms of the PPAs.

Q. Please summarize your testimony.

A. As a result of the passage of the GaMPR in 2007, Gulf Power was required to either install environmental controls on Scherer 3 that included a baghouse, FGD, and SCR or to retire the capacity. An economic evaluation performed at the time showed conclusively that the decision to invest in these environmental controls and continue to operate Scherer 3 was in the best interests of Gulf's customers. Additionally, Scherer 3's rededication to retail service is consistent with its originally planned purpose and is complementary to Gulf's future resource plans.

Q. Does this conclude your testimony?

A. Yes.

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
Xia Liu
Docket No. 160007-EI
Date of Filing: September 1, 2016

Q. Please state your name and business address.

A. My name is Xia Liu. 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 Vice President and Chief Financial Officer (CFO).

Q. What are your responsibilities as Vice President and CFO?

A. I oversee all financial matters and decisions for Gulf and am responsible for maintaining the overall financial integrity of the Company. My areas of responsibility include the Accounting, Corporate Secretary, Treasury, Regulatory, Corporate Planning, Forecasting and Pricing departments. I am responsible for financial planning and for maintaining the Company's financial and accounting records. I also maintain strong relationships with the financial community including the rating agencies and serve as a member of Gulf's Management Council. Additionally, I represent Gulf Power as a member of the Southern Company Accounting, Finance and Treasury (AFT) Management Council, which is comprised of CFOs from Southern Company and all sister operating companies.

Q. Please state your prior work experience and responsibilities.

A. I have been employed with the Southern Company system since 1998. I have lived in three of the four states where the Southern electric system of which Gulf is a part serves retail customers. In my career, I have held positions working with Southern Company Services, Alabama Power and now Gulf Power.

Prior to moving to Gulf in 2015, I served as senior vice president of finance and treasurer of Southern Company. In that role, I had responsibilities overseeing the overall finance and treasury functions of Southern Company including strategic development, mergers and acquisitions, financial analysis, corporate planning and budgeting, treasury, enterprise risk management, insurance management, and pension and trust finance management. I oversaw rating agency, fixed income investor, investment banking and commercial banking relations and had regular meetings with all these financial institutions both domestically and internationally.

Prior to 2010, I served in various roles in the Southern Company system. I was the director of financial planning and assistant treasurer for Alabama Power Company, where I testified on behalf of Alabama Power before the Alabama Public Service Commission. I was the environmental and compliance manager for fuel services at Southern Company Services from 2005 to 2007, where I had responsibilities developing fuel procurement strategies including coal, natural gas, environmental commodities and emission allowances.

Q. What is your educational background?

A. I graduated from Renmin University of China, one of the nation's top universities located in the capital city of Beijing, with bachelor's and master's degrees in finance. I also hold an MBA from Emory University's Goizueta Business School in Atlanta, Georgia. Additionally, I spent two years in the Ph.D. in Economics program at Emory University and completed preliminary Ph.D. course work.

Q. Do you hold any certifications?

A. Yes. I have been a Chartered Financial Analyst (CFA) since 2001. The CFA designation is a professional credential offered internationally by the American-based CFA Institute to investment and financial professionals. It measures the competence and integrity of financial analysts. Candidates are required to pass three levels of exams covering areas such as accounting, corporate finance, economics, ethics, money management and security analysis.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to support the incorporation into retail rates the revenue requirements associated with the portion of Gulf's investment in Plant Scherer Unit 3 (and related common facilities at Plant Scherer) that serves native load customers (collectively "Scherer 3"). This is accomplished by first allowing recovery through the Environmental Cost Recovery Clause (ECRC) of the costs associated with the environmental retrofit projects and other environmental compliance activities at Scherer 3. As discussed by Gulf

Witnesses Markey and Boyett, these costs are for projects and activities similar to those being recovered through the ECRC mechanism for Gulf's other generation plants. The ECRC revenue requirements currently represent more than 40 percent of the total revenue requirements for the portion of Scherer 3 that serves native load customers. The remaining revenue requirements that are not recoverable through the ECRC mechanism will be addressed for recovery through Gulf's base rates in other regulatory proceedings.

I explain why it is critical for the Florida Public Service Commission ("Commission") to recognize and approve the reintegration of Scherer 3 into the retail jurisdiction and to authorize recovery of Scherer 3 environmental costs through the ECRC mechanism. Gulf Witnesses Burleson and Deason describe the planning and regulatory history of Scherer 3 in more detail.

Q. Why is it appropriate to authorize ECRC recovery of costs associated with these existing environmental compliance activities?

A. First and foremost, because the legislature has established the ECRC mechanism for the recovery of environmental compliance costs separate and apart from base rates when those costs are not already being recovered through another cost recovery mechanism. All of the projects and expenses for Scherer 3 identified by Mr. Markey are activities undertaken subsequent to Scherer 3's original in-service date. As discussed by Mr. Deason, they are no different from the environmental compliance activities undertaken subsequent to Gulf's 1990 rate case that were the basis of Gulf's initial implementation of the ECRC mechanism in 1994.

Q. In your view as Chief Financial Officer of Gulf, how is an electric utility different from other businesses?

A. One of the primary differences between Gulf and many other businesses is that Gulf has the obligation to provide reliable service to our native load customers and to deploy capital well in advance to ensure we meet the long-term needs of these customers. Our business is capital intensive, our capital assets are long lived, and generating units in particular have a long planning and construction lead time. Thus, we must constantly make long-term investment decisions based on the best information available to us at the time in order to meet the current and future needs of the customers we are obligated to serve.

As a regulated utility, once a prudent investment has been made to serve our customers, we must be afforded the opportunity to earn a fair return on that investment. Under the regulatory compact that Mr. Deason describes in more detail, utilities need the assurance that they will be allowed to recover the cost of prudent investments over the life of the asset, regardless of future changes in circumstances. It is important to ensure fair regulatory treatment of utilities' past long-term investments in order to preserve the ability to make future long-term investments. Without the assurance that prudent costs will be recovered, utilities would find it difficult to continue to consistently make the long-term investments that are required by their obligation to serve.

Q. When and why did Gulf make its investment in Scherer 3?

A. As described by Mr. Burleson and Mr. Deason, Gulf acquired its interest in Scherer 3 in the mid-1980s as a cost-effective alternative to a generating unit then being planned for construction at Gulf's Caryville site for the purpose of serving Gulf's native load customers. At that time, Gulf had the opportunity to enter into interim long-term wholesale contracts in order to provide a bridge that would temporarily relieve Gulf's native load customers of the obligation to support the Scherer 3 revenue requirements. As discussed by Mr. Deason, the Commission encouraged Gulf to proceed with the purchase of an interest in Scherer 3 and to enter into the interim long-term wholesale contracts for the ultimate benefit of Gulf's retail customers.

Q. Did Gulf in fact make long-term off-system sales to temporarily relieve native load customers of the obligation to support Scherer 3?

A. Yes. Gulf entered into Unit Power Sales (UPS) contracts that initially committed most of the unit's capacity to the wholesale market through 1995. Subsequently, Gulf entered into other wholesale contracts that ultimately continued to commit the Scherer 3 capacity to the wholesale market through December 31, 2015 (110 MW), May 31, 2016 (50 MW) and December 31, 2019 (50 MW).

Q. What is the situation with Scherer 3 today?

A. For the first time since Scherer 3 began commercial operation, a substantial majority (76 percent) of Scherer 3 is not committed to long-term wholesale contracts. The first of the last vintage of three wholesale contracts, covering 52 percent of Gulf's interest in Scherer 3, expired on December 31, 2015. The second contract of that vintage, covering 24 percent of Gulf's interest in Scherer 3 expired on May 31, 2016. The final of the three contracts will expire at the end of December 2019. As these wholesale contracts expire, Gulf's Scherer 3 investment is being rededicated to serving the native load customers for whom it was originally planned, acquired and ultimately built.

Q. Please explain the impact on Gulf of the expiration of the long-term wholesale contracts.

A. The costs of the rededicated portion of Scherer 3 are not currently being recovered through any rates despite the fact that it is now serving Gulf's native load customers.

Q. What action are you asking the Commission to take with respect to Scherer 3 at this time?

A. We are asking the Commission to approve the rededication of Scherer 3 as a retail asset by allowing recovery through the ECRC for the environmental compliance activities at Scherer 3. If Scherer 3 had not been committed to long-term off-system sales, these environmental compliance activities would have been included in the ECRC mechanism when they were initially incurred. Instead, the revenue requirements for these environmental compliance activities have been recovered on an interim basis through the wholesale contracts. This docket represents the first opportunity since the wholesale contracts expired for Gulf to begin incorporating the revenue requirements associated with its investment in Scherer into the Company's retail rates. Although a change to Gulf's base rates is not possible until July 2017 pursuant to the terms of the settlement agreement approved in Gulf's last rate case docket, this does not prevent the recovery of the revenue requirements associated with the environmental compliance activities that are not presently being recovered through rates.

We are asking the Commission to 1) reconfirm Gulf's ownership of Scherer 3 as a resource intended for and serving our native load customers, and 2) approve recovery through the ECRC of 52 percent of the environmental costs of Gulf's interest in Scherer 3 for the period January 1, 2016, through May 31, 2016, and 76 percent of those costs beginning June 1, 2016, as shown in the testimony of Mr. Boyett.

These actions will make it clear that the costs associated with the portion of the investment in Scherer 3 not committed to long-term off-system sales should be recovered from the native load customers being served by that investment. The Commission contemplated this result when it encouraged Gulf to market the Scherer capacity off-system as a temporary bridge of responsibility for supporting the revenue requirements associated with this investment. The Scherer 3 investment that was prudently made to serve native load customers will now be supported by those customers, although at its depreciated net book value. This treatment is consistent with the regulatory compact discussed by Mr. Deason.

Q. Why is this treatment critical to Gulf's customers and investors?

A. As I stated earlier, Gulf must continually evaluate and make long-term investments in order to fulfill its obligation to serve. It is critical to both Gulf and our customers that the utility be assured that it can recover through rates the cost of the prudent investments it undertakes to meet that obligation. That is the essence of the regulatory compact described by Mr. Deason. If Gulf were denied the ability to recover its investment in Scherer 3 from the customers for whom it was planned, acquired and ultimately built, that decision would make it difficult for Gulf to continue to consistently take a long-term view when making future investment decisions. Such a decision could also harm the current perception of a constructive regulatory environment in Florida, which would negatively impact Gulf and other Florida utilities.

Q. Does that conclude your testimony?

A. Yes.

CHAIRMAN BROWN: Moving on to the exhibits, Ms. Lherisson.

MS. LHERISSON: Staff has compiled a stipulated Comprehensive Exhibit List, which includes the prefiled exhibits attached to the witnesses' testimony in this case on staff -- and one staff exhibit. The list has been provided to the parties, the Commissioners, and the court reporter. This list is marked as the first hearing exhibit, and the other exhibits should be marked as set forth in the chart.

CHAIRMAN BROWN: We have those marked.

(Exhibits 1 through 29 marked for identification.)

Moving on to moving the Exhibit 1 into the record, staff, is it your desire to move that in at this time?

MS. LHERISSON: Yes, Madam Chair.

CHAIRMAN BROWN: Okay. Seeing no objections to moving into the record Exhibit 1, we will go ahead and do that.

(Exhibit 1 admitted into the record.)

How about Exhibits 2 through 29?

MS. LHERISSON: Staff asks that all exhibits be included in the record as set forth in the Comprehensive Exhibit List, Exhibits 2 through 29.

CHAIRMAN BROWN: All right. Seeing no objections to Exhibits 2 through 29, we will go ahead and move into the record Exhibits 2 through 29.

(Exhibits 2 through 29 admitted into the record.)

So, staff, this is the right time to possibly make a bench decision for the Commission?

MS. LHERISSON: Yes, Madam Chair. If the Commission decides that a bench decision is appropriate, staff recommends that the proposed stipulations for all issues, which are found on pages 9 through 19 of the Prehearing Order, should be approved by the Commission. And as indicated in the Prehearing Order, all parties either support or do not oppose the proposed stipulations.

CHAIRMAN BROWN: Thank you, Ms. Lherisson.

Those are, Commissioners, Issues 1 through 12, as delineated on pages 9 through 19 of the Prehearing Order.

Commissioners, are there any questions or discussion on those issues? And if not, I will entertain a motion.

Seeing none, can I get a motion?

Brisé, Commissioner Brisé.

COMMISSIONER BRISÉ: Thank you, Madam Chair.

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Seeing none, can I get a motion?

Brisé, Commissioner Brisé.

COMMISSIONER BRISÉ: Thank you, Madam Chair. So we will at this time accept the proposed stipulations on Issues 1 through 12 in Docket 160007-EI, and with that, that is my motion.

CHAIRMAN BROWN: Thank you.

COMMISSIONER EDGAR: Second.

COMMISSIONER GRAHAM: Second.

CHAIRMAN BROWN: Thank you. We've got a motion from Commissioner Brisé seconded by Commissioner Graham and Edgar. Any further discussion? Seeing none, all those in favor, say aye.

(Vote taken.)

Okay. Thank you. Passes unanimously.

Are there any other matters to address in the 07 docket? Bless you.

MS. LHERISSON: No, Madam Chair.

CHAIRMAN BROWN: Okay. Any other discussion on this docket? Seeing none, we will go ahead and adjourn the 07 docket.

(Hearing adjourned at 9:54 a.m.)

STATE OF FLORIDA)
: CERTIFICATE OF REPORTER
COUNTY OF LEON)

I, LINDA BOLES, CRR, RPR, Official Commission Reporter, do hereby certify that the foregoing proceeding was heard at the time and place herein stated.

IT IS FURTHER CERTIFIED that I stenographically reported the said proceedings; that the same has been transcribed under my direct supervision; and that this transcript constitutes a true transcription of my notes of said proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney, or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorney or counsel connected with the action, nor am I financially interested in the action.

DATED THIS 4th day of November, 2016.

Linda Boles

LINDA BOLES, CRR, RPR
Official FPSC Hearings Reporter
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