BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 060154-EI

TESTIMONY AND EXHIBIT

OF

R. R. LABRATO

In Support of Storm-Recovery Financing

GULF POWER

A SOUTHERN COMPANY

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony of
Ronnie R. Labrato
Docket No. 060154-EI
In Support of Storm-Recovery Financing
Date of Filing: February 22, 2006

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

A. My name is Ronnie R. Labrato. My business address is One Energy Place, Pensacola, FL 32520. I am Vice President and Chief Financial Officer of Gulf Power Company.

Q. Please outline your educational background and business experience.

A. I graduated from the University of West Florida in 1974 with a Bachelor of Arts degree in Accounting. Following graduation from college, I was employed by the Florida Public Service Commission (FPSC) as Auditor and Accounting Analyst. In 1977, I accepted a position as Senior Accountant and Consultant with Deloitte, Haskins, and Sells in Dallas, Texas. In 1979, I was employed by Gulf Power Company as Senior Financial Analyst. Since 1979, I have held various positions at Gulf Power, including Manager of Financial Planning, Manager of General Accounting, and Comptroller. I currently serve as Vice President and Chief Financial Officer of Gulf Power. Also, I am a licensed Certified Public Accountant and a member of the American Institute of Certified Public Accountants and the Florida Institute of Certified Public Accountants.

Q. What are your duties and responsibilities as Vice President and Chief Financial Officer?
A. I am responsible for ensuring the overall financial integrity of the Company and for maintaining the financial and accounting records of the Company in compliance with the appropriate rules and regulations. My areas of responsibility include Accounting (including Internal Controls), Corporate Planning, Secretary and Treasury, Regulatory Matters, and Supply Chain Management.

Q. What is the purpose of your testimony?
A. The purpose of my testimony is to support the Company's petition for a financing order approving the proposed issuance of 8-year storm-recovery bonds to cover prudently-incurred costs associated with Hurricanes Ivan, Dennis and Katrina, as well as to provide an additional amount to replenish the property insurance reserve. I will provide an overview of Gulf's proposed securitization transaction and discuss the benefits of securitization. I will also discuss Gulf's alternative request in the event that the primary request for securitization is not approved.

Q. Mr. Labrato, please explain Gulf Power's primary request in this docket.
A. Gulf's primary request in this proceeding is that the Commission issue a financing order pursuant to Section 366.8260, Florida Statutes, relating to storm infrastructure recovery (the "Statute") to allow for the issuance of storm-recovery bonds and the application of the associated storm-recovery charge to customer bills in order to finance and recover three

principal elements consistent with the definition of storm-recovery bonds contained in the Statute. These three elements are: (1) the remaining balance of the stipulated recovery amount of Gulf's storm-recovery costs associated with Hurricane Ivan; (2) Gulf's storm-recovery costs associated with Hurricanes Dennis and Katrina; and (3) the addition of approximately $70 million to Gulf's property insurance reserve. The purpose of this last element, consistent with the Statute, is to replenish the reserve to a level that would be reasonable in light of the Company's storm recovery experience over the past two hurricane seasons in anticipation of future storms. As part of this primary request, Gulf is proposing that the storm damage surcharge approved in Docket No. 050093-EI to recover costs associated with Hurricane Ivan (the "Ivan Surcharge") be terminated upon implementation of the storm-recovery charge requested in this proceeding which, as noted in my three elements, includes the remaining balance of the stipulated recovery amount associated with Hurricane Ivan.

Q. Briefly describe the impact to Gulf from Hurricane Ivan in 2004.

A. On September 16, 2004, Hurricane Ivan, a Category 3 storm, struck Gulf's service area causing widespread and extensive damage to Gulf's plant and property including its transmission lines, distribution feeders, substations, and Crist generating plant. As a result of Hurricane Ivan, Gulf incurred approximately $137.7 million in storm-restoration costs. This catastrophic event depleted Gulf's property insurance reserve, leaving it with a substantial deficit in excess of $95 million. Gulf witnesses

Mr. Mandes and Mr. McMillan provide further details of the storm's impact on Gulf's facilities in their testimonies.

Q. What were the primary impacts on Gulf Power from Hurricanes Dennis and Katrina in 2005?

A. As also discussed by Mr. Mandes and Mr. McMillan, Hurricanes Dennis and Katrina inflicted substantial damage to Gulf's service area. Hurricane Dennis made landfall on July 10, 2005 just east of Pensacola as a Category 3 storm causing approximately $59.4 million in storm-related damages to Gulf's facilities. Hurricane Katrina made landfall on August 29, 2005 just east of New Orleans as a Category 4 storm. Due to the extensive size and intensity of Hurricane Katrina, Gulf incurred approximately $4.3 million in storm-related damages to the Company's facilities.

Gulf's total storm restoration costs related to Hurricanes Dennis and Katrina are approximately $63.7 million. Hurricane Ivan depleted Gulf's property insurance reserve, leaving it totally inadequate to cover these costs or the costs of future storms.

Q. Please describe Gulf's property insurance reserve.

A. Pursuant to Rule 25-6.0143, Florida Administrative Code, Gulf Power maintains an Accumulated Provision for Property Insurance (the "Reserve") to provide for property losses, including hurricane damage, not covered by insurance. Charges associated with property losses are charged to the Reserve, with an annual accrual to the Reserve levelizing the impact of such property losses over time. Ideally, the balance in the Reserve would be sufficient to cover damage to utility property during any given year. However, the extremely active storm seasons of 2004 and 2005 have resulted in a substantial deficit in Gulf's Reserve. In light of recent predictions for the active Atlantic hurricane activity to continue for another 15 to 20 years, Gulf believes it would be prudent to replenish the Reserve by an appropriate amount to provide for future storm-related costs.

Q. Please describe Gulf's current storm cost recovery surcharge related to Hurricane Ivan.

A. On February 2, 2005, the Office of Public Counsel (OPC), the Florida Industrial Power Users Group (FIPUG), and Gulf Power filed a Joint Petition for Approval of the Stipulation and Settlement related to the recovery of costs associated with Hurricane Ivan. The Commission approved the Stipulation in Order No. PSC-05-0250-PAA-EI. The Stipulation provided for Gulf to implement a surcharge to recover costs related to the restoration activities resulting from the damage caused by Hurricane Ivan over a 24-month period. The initial monthly surcharge of $2.71 (per 1,000 kWh residential bill) for the first 12-month period began in April 2005. Based on true-up calculations as filed with the Commission under the terms of the Stipulation, the monthly surcharge will be reduced to $2.57 (per 1,000 kWh residential bill) for the final 12-month period beginning in April 2006.

Q. What is the amount of storm-recovery costs and reserve replenishment that Gulf is proposing to finance through the issuance of storm-recovery bonds?

A Gulf proposes to issue $87.2 million of storm-recovery bonds. As provided for in the Statute, the proceeds of the storm-recovery bonds will be used to finance the remaining balance of the stipulated costs approved for Hurricane Ivan recovery (approximately $13.6 million); storm-recovery costs related to Hurricanes Dennis and Katrina ($54.2 million), and the addition of approximately $70 million to replenish Gulf's property insurance reserve. The total of these storm-recovery costs and the requested replenishment amount is $137.8 million. The storm-recovery bonds will be issued for the after-tax amount of this total, or $84.6 million, plus financing costs. As detailed in the testimonies of Mr. Kim and Ms. Ritenour, we estimate the upfront financing costs associated with issuance of the storm-recovery bonds to be $2.6 million, for a total storm-recovery bond amount of $87.2 million.

Q. In determining the amount of storm-recovery costs to be financed, has Gulf made any adjustments to exclude the operation and maintenance expenses normally recovered through base rates from the total amount of costs incurred for storm-recovery activities associated with Hurricanes Dennis and Katrina?

A. Yes. As detailed in the testimony of Mr. McMillan, Gulf has voluntarily excluded certain types of costs from the calculation of storm-recovery costs that we are requesting be financed through storm-recovery bonds.

These voluntary exclusions have been made in a manner and philosophy that is consistent with the treatment of these types of costs in the negotiated Stipulation and Settlement with the Office of Public Counsel and the Florida Industrial Power Users Group that was approved by the FPSC in Order No. PSC-05-0250-PAA-EI.

Q. How did you arrive at the amount of approximately $70 million to be added to the Reserve from the proposed issuance of storm-recovery bonds?

A. Gulf believes the requested amount strikes a reasonable balance considering several factors: the uncertainty of future storm-related costs that will be incurred based on expert forecasts that we are in a more active storm period; the need to mitigate the impact on our customers' rates; and the ability to address any Reserve deficiency in future proceedings. Ideally, the Reserve would be set at a level that would at least be adequate over the proposed 8-year life of the bonds, thus minimizing the transaction costs of financing and also levelizing the rate impact on our customers over this period of time. The storm-recovery costs incurred by Gulf over the last two years, coupled with forecasts that we are in a more active hurricane period, would indicate that the Reserve over the 8-year recovery period should be much larger than the amount we are requesting. The requested level would cover only one storm equal to the average of the two major storms that directly hit our service area in 2004 and 2005. However, Gulf has also taken into account the impact that a larger amount would have on our customers' bills, and concluded that $70 million is the appropriate amount for recovery at this time. Mr. McMillan discusses the basis for determining the $70 million amount in his testimony.

Q. What are the benefits of securitization?

A. Securitization allows the Company to recover storm costs over a longer period of time without adversely impacting the Company's credit quality, and therefore minimizes the increase to our customers' rates. Using securitization, storm-recovery costs can be financed entirely with debt over a longer period of time than would be possible using other debt instruments. Based on the rating agency treatment of securitized debt as essentially "off balance sheet", a utility can incur higher debt levels without any adverse impact on its credit rating. Avoiding an adverse impact on the utility's credit rating allows the utility access to reasonably priced debt and other forms of capital for financing its normal operations and capital needs. The only viable alternative to securitization for financing storm-recovery costs over a longer period of time would be to use a mix of debt and equity to maintain credit quality, which would be more expensive for our customers. Ms. Ritenour's and Mr. Kim's testimonies further describe the benefits of securitization.

Q. What is the rate impact to Gulf's customers if the Commission approves Gulf's primary request?

A. Based on current market conditions, the proposed issuance of 8-year storm-recovery bonds would require an estimated storm-recovery charge of approximately $1.93 per month (per 1,000 kWh residential bill) for an 8-

year period. As noted earlier, this storm-recovery charge will replace the existing Ivan Surcharge upon issuance of the storm-recovery bonds. The calculation of the revenue requirements associated with the storm-recovery charge, as well as the associated periodic true-up mechanism, is discussed in the direct testimonies of Mr. Kim and Ms. Ritenour.

Q. What is the expected effective date of the new storm-recovery charge?

A. Gulf is requesting that the new storm-recovery charge be made effective on the first billing cycle of the month following issuance of the storm-recovery bonds. For the purposes of the calculations required in this filing, Gulf has projected that the resulting storm-recovery charge will be effective with Cycle 1 billings for September 2006. This reflects the time frames provided for in the Statute for the issuance of a financing order, along with additional time provided for the issuance of the storm-recovery bonds and establishment of the final associated storm-recovery charge.

Q. What if the Commission issues the financing order, but the implementation of the financing is delayed?

A. Gulf needs to eliminate the deficit and provide for a reasonable balance in the Reserve as quickly as possible in order to be prepared for future hurricane seasons. In the event that the issuance of the storm-recovery bonds is delayed for any reason, Gulf requests that the Commission approve an interim surcharge to be applied to customer bills effective with Cycle 1 billings for October 2006 in an amount calculated to recover the storm-recovery costs associated with Dennis and Katrina over a 24-month period. The monthly impact from this interim surcharge is estimated to be $2.78 (per 1,000 kWh residential bill). This additional interim surcharge would be applied in conjunction with the existing Ivan Surcharge and both would be discontinued upon issuance of the storm-recovery bonds and the amount of the storm-recovery bonds issued would be adjusted for the collections made through this interim surcharge.

Q. Does Gulf have an alternative request in case the Commission does not approve the primary request for securitization?

A. Yes. If the Commission makes a determination that storm-recovery costs should not be securitized pursuant to the Statute, Gulf requests that the Commission authorize the implementation of a new surcharge to recover storm-recovery costs associated with Hurricanes Dennis and Katrina over a 24-month period beginning with Cycle 1 billings in August 2006. The existing Ivan Surcharge would also remain in effect through its projected ending date with the last cycle of billings in March 2007. As part of this alternative request, Gulf asks that the Commission authorize a second new surcharge beginning with the Cycle 1 billings in April 2007 (which is immediately after the completion of the Ivan Surcharge) and continuing for 36 months for the purpose of adding $70 million to the Reserve. This alternative request provides for recovery of Hurricane Dennis and Katrina costs and replenishment of the Reserve through the addition of approximately $70 million over a reasonable time frame to prepare for future storm seasons. Details of this alternative request are discussed in Ms. Ritenour's testimony.

Q. What is the rate impact to Gulf's customers if the Commission approves the alternative request?

A. The rate impact on customer bills from the alternative request is greater than the impact calculated for the primary request of securitization, but for a shorter duration. The alternative request would result in a new monthly surcharge of $2.78 (per 1,000 kWh residential bill) to cover Hurricane Dennis and Katrina costs. This surcharge, plus the existing $2.57 monthly Ivan Surcharge (per 1,000 kWh residential bill effective April 2006), would result in a total monthly storm-recovery surcharge of $5.35 (per 1,000 kWh residential bill). The total monthly surcharge would decline to $5.03 (per 1,000 kWh residential bill) at the completion of the Ivan Surcharge beginning in April 2007 and would continue at that level through July 2008. After the surcharge for storm-recovery costs related to Hurricanes Dennis and Katrina ends in July 2008, the total monthly surcharge would be $2.25 (per 1,000 kWh residential bill) through March 2010.

Q. Please summarize your testimony.

A. In summary, Gulf is requesting the Commission to approve the issuance of $87.2 million in storm-recovery bonds in accordance with Section 366.8260 of the Florida Statutes to finance the after-tax amount of (1) the $67.8 million of storm-recovery costs associated with Hurricanes Ivan, Dennis and Katrina and (2) a $70 million addition to Gulf's property insurance reserve, plus associated financing costs. The requested amount is comprised of approximately $13.6 million for the remaining balance of stipulated and previously approved storm-recovery costs related to Hurricane Ivan; $54.2 million cost deficit related to Hurricanes Dennis and Katrina; and approximately $70 million to be added to the Company's property insurance reserve to provide for a reasonable Reserve level to cover future storm restoration costs. If the Commission does not approve the issuance of storm-recovery bonds, Gulf is asking for alternative relief in the form of a 24-month surcharge beginning August 2006 for the storm-recovery costs associated with Hurricanes Dennis and Katrina and a 36-month surcharge beginning April 2007 to raise $70 million for the property insurance reserve.

Q. Does this conclude your testimony?

A. Yes.

AFFIDAVIT

STATE OF FLORIDA)
)
COUNTY OF ESCAMBIA)

Docket No. ________

Before me the undersigned authority, personally appeared Ronnie R. Labrato, who being first duly sworn, deposes, and says that he is the Vice President and Chief Financial Officer of Gulf Power Company, a Florida corporation, that the foregoing testimony is true and correct to the best of his knowledge, information, and belief. He is personally known to me.

Ronnie R. Labrato
Ronnie R. Labrato
Vice President
and Chief Financial Officer

Sworn to and subscribed before me this 20 day of February, 2006.

Judy McHenry
Notary Public, State of Florida at Large

JUDY MCHENRY
MY COMMISSION # DD 315930
EXPIRES: May 3, 2008
Bonded Thru Notary Public Underwriters