BEFORE THE

FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 060154-EI

TESTIMONY AND EXHIBIT

OF

R. J. MCMILLAN

In Support of Storm-Recovery Financing

GULF POWER

A SOUTHERN COMPANY

GULF POWER COMPANY

Before the Florida Public Service Commission
Prepared Direct Testimony and Exhibit of
R. J. McMillan
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 R. J. McMillan, and my business address is One Energy Place, Pensacola, Florida 32520. I am the Corporate Planning Manager for Gulf Power Company.

Q. Please summarize your educational and professional background.

A. I graduated from Louisiana State University in 1976 with a Bachelor of Science Degree in Accounting and was employed by Gulf Power in January 1977. During my employment, I also graduated from the University of West Florida in 1983 with a Master of Science Degree in Business Administration. I have held various accounting staff and management positions, including Staff Internal Auditor, Staff Financial Analyst, Staff Accountant, Coordinator of Internal Accounting Controls, Supervisor of Financial Planning, General Accounting Manager, and in 2002, I was promoted to my current position as Corporate Planning Manager.

Q. Briefly describe your duties and responsibilities as Corporate Planning Manager.

A. My primary responsibilities include providing timely and accurate financial forecasts and decision support for the Company related to its budgeting and planning activities.

Q. Have you prepared an exhibit that contains information to which you will refer in your testimony?

A. Yes. I have one exhibit consisting of three schedules to which I will refer. This exhibit was prepared under my supervision and direction.

Counsel: We ask that Mr. McMillan's Exhibit RJMc-1, consisting of 3 schedules, be marked for identification as Exhibit No. ___.

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

A. The purpose of my testimony is to discuss Gulf's storm restoration costs to be financed through storm-recovery bonds and securitized in accordance with Section 366.8260 of the Florida Statutes. I will discuss the amount of storm damage costs related to Hurricanes Ivan, Dennis, and Katrina. I will also describe the damage caused by these hurricanes to the Company's generating plants and office facilities. Mr. Mandes will address the transmission and distribution damage in his direct testimony. My testimony will also address the estimated remaining balance of storm-recovery costs associated with Hurricane Ivan previously approved for recovery; the storm-recovery costs related to Hurricanes Dennis and

Katrina; an amount to be added to the property insurance reserve to cover future storm losses; and the resulting total amount of storm-recovery costs the Company is requesting to recover through the storm-recovery financing, excluding financing costs associated with securitization. Ms. Ritenour will discuss the proposed issuance of storm-recovery bonds and the associated financing costs in her direct testimony.

Q. Does the Company have a reserve for uninsured property losses?

A. Yes. As previously authorized by the Commission, pursuant to Rule 25-6.0143, the Company established an Accumulated Provision for Property Insurance for uninsured property losses that is funded on an after-tax basis through an annual accrual from revenues received by the Company through its base rates. For purposes of my testimony, I will refer to the Accumulated Provision for Property Insurance as the "Reserve."

Q. Describe the damage caused by Hurricane Ivan to the Company's generating plants and office facilities and provide the costs of this damage.

A. Hurricane Ivan caused extensive damage to Plant Crist, the Company's largest generating plant. Plant Crist was knocked completely off line for the first time in 25 years. The cooling tower for Unit 6 suffered major damage and had to be rebuilt. Plant Crist also suffered damage in the switchyard, and windows in the plant were blown out. The Company's office facilities also suffered significant damage as a result of Hurricane Ivan. The most significant damage to our office facilities was caused by water intrusion at the Company's corporate office and Pace Boulevard facilities. The total cost of repairs to generating plants and office facilities caused by Hurricane Ivan is approximately $16.0 million.

Q. What are the total costs, known and estimated, to Gulf in responding to and recovering from Hurricane Ivan?

A. The total storm restoration cost of Hurricane Ivan is approximately $137.7 million. This includes total transmission and distribution costs of $121.7 million, which is covered in more detail by Mr. Mandes in his direct testimony, and the total cost related to generating plants and office facilities of $16.0 million. Please see Schedule 1 of my exhibit for a summary of restoration costs related to Hurricane Ivan.

Q. Is the Company requesting an amount to be financed related to Hurricane Ivan?

A. Yes. The Company is requesting that the estimated remaining balance of Ivan storm-recovery costs of approximately $13.6 million as of August 2006 be included in the amount to be financed through storm-recovery bonds, as shown on Schedule 1 of my exhibit.

In accordance with 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 dated March 4, 2005, restoration costs associated with Hurricane Ivan of $51.4 million, excluding interest and revenue taxes, are being recovered from the retail jurisdiction. The retail amount is being recovered through a customer surcharge over a 24-month period that began April 1, 2005. Based upon the Company's January 31, 2006, true-up filing for the Hurricane Ivan deficit, the total jurisdictional deficit before interest and revenue taxes is now estimated to be $50.8 million. Assuming the storm-recovery charge is implemented in September 2006, as Ms. Ritenour discusses in her direct testimony, the projected remaining balance of Ivan costs previously approved for recovery is $13.6 million as of August 2006. The calculation of this amount is shown in Schedule 1 of my exhibit. The projected remaining balance includes actual and estimated interest on the jurisdictional recoverable Ivan deficit of approximately $2.0 million for the period April 2005 through August 2006. The amount of revenues billed to customers through December 2005 was $21.2 million, and the projected billings for the period January through August 2006 are $18.0 million. Therefore, the Company is requesting to finance through storm-recovery bonds approximately $13.6 million for the projected remaining balance related to the Hurricane Ivan storm-recovery costs as of August 2006.

Q. Describe the damage caused by Hurricane Dennis to the Company's generating plants and office facilities and provide the costs of this damage.

A. Plant Crist suffered major damage again due to Hurricane Dennis. The most significant damage occurred to the Plant Crist Unit 7 cooling tower. Numerous other areas of the plant also incurred damage. Hurricane Dennis also caused water damage at some of the Company's office facilities. The facilities with the most significant damage were the

Company's two largest office facilities in Pensacola and the office building in Panama City Beach. The total damage to the Company's generating plants and office buildings related to Hurricane Dennis is approximately $2.3 million.

Q. What are the total costs, known and estimated, to Gulf in responding to and recovering from Hurricane Dennis, and what are the major components of those costs?

A. The total storm restoration cost of Hurricane Dennis is approximately $59.4 million. This includes total transmission and distribution costs of $57.1 million, which is covered in more detail by Mr. Mandes in his direct testimony, and the total cost related to generating plants and office facilities of $2.3 million. Please see Schedule 2 of my exhibit for the major components of the restoration costs related to Hurricane Dennis.

Q. Describe the damage caused by Hurricane Katrina to the Company's generating plants and office facilities and provide the costs of this damage.

A. Hurricane Katrina caused only minor damage at Plant Daniel in Mississippi, which is jointly-owned by Gulf and Mississippi Power Company. Gulf's corporate office in Pensacola also incurred minor damage. The total damage to generating plants and office buildings related to Hurricane Katrina is approximately $267,000.

Q. What are the total costs, known and estimated, to Gulf in responding to and recovering from Hurricane Katrina, and what are the major components of those costs?

A. The total storm restoration cost of Hurricane Katrina is approximately $4.3 million. This includes total transmission and distribution costs of $4.0 million, which is covered in more detail by Mr. Mandes in his direct testimony, and the total cost related to generating plants and office facilities of $267,000. Please see Schedule 2 of my exhibit for the major components of the restoration costs related to Hurricane Katrina.

Q. Does the Company expect to receive any insurance reimbursement for any of the costs associated with Hurricanes Dennis and Katrina?

A. Yes. The Company's property insurance policy covers property damage to all property excluding transmission and distribution facilities. Economic insurance coverage for transmission and distribution facilities has been unavailable since Hurricane Andrew in 1992. The Company's property insurance policy is a Southern Company policy and the deductible is applied to each event. When more than one company incurs damage from the same storm, each company's share of the deductible is based on its insured loss as a percent of the total insured system loss.

Gulf's current estimate for damage to covered property is $2.3 million for Hurricane Dennis. The Company expects to receive an insurance reimbursement of $669,000. The damage to covered property during Hurricane Katrina is estimated to be $267,000. The Company expects to receive an insurance reimbursement for damage to covered property related to Hurricane Katrina of $261,000. Schedule 2, line 12 of my exhibit reflects the estimates of insurance reimbursements for each storm.

Q. What was the total amount of recoverable costs charged to the Reserve for Hurricanes Dennis and Katrina?

A. The total amount of recoverable costs charged to the Reserve was $53.4 million for Hurricanes Dennis and Katrina. This amount excludes estimated insurance reimbursements, normal capital costs including cost of removal, and operation and maintenance expenses normally recovered through base rates as shown on Schedule 2 of my exhibit.

These exclusions were made voluntarily by the Company consistent with the treatment 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. Please describe the adjustments made to exclude the capital costs and cost of removal from the amount charged to the Reserve.

A. As shown on Schedule 2 of my exhibit, the Company excluded $7.1 million of estimated capital costs and $628,000 for estimated cost of removal from the total costs charged to the Reserve. These capital costs represent the portion of capital expenditures and cost of removal related to recovery from Hurricanes Dennis and Katrina equal to the normal amount that would be charged to capital accounts under normal operating conditions. The restoration costs charged to the Reserve include that portion of the otherwise capitalized charges that exceeds the normal amount that would be charged to capital accounts under normal operating conditions.

Q. Please describe the adjustments to exclude an estimate of the operation and maintenance expenses normally recovered through base rates from the total amount of recoverable costs charged to the Reserve for Hurricanes Dennis and Katrina.

A. As shown on Schedule 2 of my exhibit, the Company has voluntarily made an adjustment to deduct $1.6 million from the recoverable costs charged to the Reserve for Hurricanes Dennis and Katrina. This amount was identified by the Company as the portion of the storm restoration costs which could be considered normal operating expenses that would typically be recovered through base rates. A breakdown of the estimated normal operating costs is included on Schedule 3 of my exhibit. These costs include the portion of straight-time labor and company-owned vehicle costs for Gulf employees associated with storm restoration activity that would normally be expensed; the budgeted level for tree trimming contract labor for the number of restoration days associated with Dennis and Katrina; and normal or budgeted overtime labor charges and materials and supplies for the days of restoration.

Q. Please explain the interest amount included on Schedule 2, line 22 of your exhibit.

A. I have added $905,000 in interest to the Dennis and Katrina storm-recovery costs in accordance with Section 366.8260 (1) (n) of the Florida

Statutes. The estimated interest cost was calculated on the after-tax balance of the Reserve deficiency projected for the period January 2006 through August 2006. The interest rate applied to the Reserve deficiency was based on the interest rate of the bank note issued to temporarily finance the storm restoration costs.

Q. Is the Company also requesting an amount to be financed through storm-recovery bonds to add to the Reserve?

A. Yes. The Company is requesting that $70.0 million be approved for recovery through storm-recovery bonds to provide for a reasonable Reserve. As set forth in Section 366.8260 of the Florida Statutes, "An electric utility may petition the commission for a financing order. For each petition, the electric utility shall set forth the level of the storm-recovery reserve that the utility proposes to establish or replenish and has determined would be appropriate to recover through storm-recovery bonds. . ."

A target balance for the Company's Reserve of $25.1 to $36 million was previously established in FPSC Order No. PSC-96-1334-FOF-EI in Docket No. 951433-EI. This target balance was determined from an estimated range of possible damage costs to transmission and distribution facilities based upon the strongest hurricane on record at that time that affected Gulf's service area. The balance in the Company's Reserve prior to Hurricane Ivan was $27.8 million. The current approved target balance is substantially insufficient to cover the cost of Hurricane Ivan or the cost of Hurricane Dennis.

Q. How did you determine the $70 million addition to the Reserve was appropriate?

A. Excluding storm-recovery costs related to Hurricanes Dennis and Katrina, the Company's Reserve balance at December 2005 was $10 million. An addition of $70 million to the Reserve would provide a balance of $80 million. I believe a Reserve level of $80 million would be appropriate considering the Company's actual experience and costs related to the two recent Category 3 storms directly impacting the area served by Gulf and forecasts of a much more active hurricane period and higher than average landfall probabilities. The Company asked ABS Consulting to perform a solvency analysis to verify the adequacy of an $80 million Reserve level, which is discussed below.

Q. Did Gulf have an independent study prepared to determine the risk of uninsured transmission and distribution losses from storms?

A. Yes. The study was prepared by ABS Consulting and is being sponsored by Mr. Harris. Mr. Harris performed two analyses, which he will address in his direct testimony. He performed a loss analysis to develop an estimate of expected annual uninsured losses related to Gulf's transmission and distribution facilities, and he performed a solvency analysis to evaluate the expected balance in the Reserve and the likelihood of insolvency over an 8-year period.

Q. What does the analysis conclude regarding the expected annual long-term cost for service restoration and repair of storm damage to Gulf's transmission and distribution assets?

A. Mr. Harris' analysis concludes that the expected average annual cost for transmission and distribution storm losses is approximately $6.4 million. The storm losses include costs associated with service restoration and system repair of damage resulting from hurricanes over a long period of time.

Q. Does Mr. Harris' expected average annual cost for uninsured storm losses include an estimate for damage to insured property?

A. No. His estimates represent costs for storm damage to only uninsured transmission and distribution facilities. Since Gulf carries insurance on its generating and office facilities, the uninsured losses on our property other than transmission and distribution facilities are generally limited to the insurance deductible amount.

Q. What does the analysis conclude regarding the expected value of the Reserve?

A. Mr. Harris' reserve solvency analysis reflects that the Reserve balance will decrease over time and there is a 15% chance of insolvency in one or more years during the 8-year recovery period.

Q. Explain why the Company believes the addition of $70 million to the Reserve is reasonable.

A. The Company's request to add $70 million to the Reserve is reasonable based upon (1) the actual storm-recovery costs incurred after the two recent Category 3 storms; (2) expert forecasts of projected hurricane activity that conclude we are in a period of increased storm activity and higher probabilities of hurricane landfall; (3) the conclusions of Mr. Harris' analysis that the expected average annual cost for uninsured storm losses associated with Gulf's transmission and distribution facilities is $6.4 million; (4) as discussed by Mr. Harris, an initial Reserve balance of $80 million and the expected Reserve balance of $63 million at the end of the 8-year recovery period should be adequate to cover the damage to transmission and distribution facilities for one Category 3 hurricane for most but not all landfall areas in our service area; and (5) Mr. Harris' analyses did not include an estimate for damage to insured property. This would suggest that the addition of $70 million is conservative and the Reserve balance could be more deficient than what is shown in Mr. Harris' analysis. The Company's request will provide a reasonable balance in the Reserve to minimize the potential need for the Company to seek additional relief from customers for storm restoration costs during the 8-year period the storm-recovery bonds are outstanding.

Q. How does the Company propose to handle differences between the estimated remaining balance of Ivan costs and estimates of storm-recovery costs for Hurricanes Dennis and Katrina included in the Company's petition and revised estimates of these storm-recovery costs on the date the storm-recovery bonds are issued?

A. The Company proposes that any differences between the estimates made in the Company's petition and the revised estimates on the date the storm-recovery bonds are issued for the remaining balance of Ivan costs and storm-recovery costs for Hurricanes Dennis and Katrina be reflected in the amount added to the Reserve.

Q. Please summarize your testimony.

A. The Company is requesting to recover $137.8 million of storm-recovery costs and Reserve replenishment costs through a storm-recovery charge pursuant to Section 366.8260 of the Florida Statutes. This amount is made up of approximately $13.6 million for the remaining balance of storm-recovery costs associated with Hurricane Ivan previously approved for recovery as shown in Schedule 1; $54.2 million for Gulf's combined prudently-incurred storm-recovery costs associated with Hurricanes Dennis and Katrina as shown in Schedule 2; and the addition of $70.0 million to the Reserve to cover future storm restoration costs. Ms. Ritenour discusses in her direct testimony the additional financing costs related to securitization and the resulting storm-recovery charge and customer impacts.

Q. Does this conclude your direct testimony?

A. Yes.

AFFIDAVIT

STATE OF FLORIDA)
)
COUNTY OF ESCAMBIA)

Docket No. ________

Before me the undersigned authority, personally appeared Richard J. McMillan, who being first duly sworn, deposes, and says that he is the Corporate Planning Manager 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.

Richard J. McMillan
Corporate Planning Manager

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

Linda C. Webb
Notary Public, State of Florida at Large

NOTARY PUBLIC STATE OF FLORIDA

LINDA C. WEBB
Notary Public-State of FL
Comm. Exp: May 31, 2006
Comm. No: DD 110088

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Hurricane Ivan Restoration Cost and Deficit Recovery

1	Total Estimated Transmission and Distribution Costs			$ 121,689,000
2	Total Estimated Generating Plants and Office Facilities			16,036,000
3	Total Estimated Hurricane Ivan Costs (Line 1 + Line 2)			$ 137,725,000
4	Less: Estimated Insurance Reimbursement Net of $1.9 Million Deductible			14,136,000
5	Estimated Costs net of Insurance Reimbursement (Line 3 - Line 4)			$ 123,589,000
6	Less: Balance in Property Insurance Reserve			27,800,000
7	Total Estimated Ivan Deficit (Line 5 - Line 6)			$ 95,789,000
8	Less: Company Voluntary Exclusions from Ivan Deficit Cost Recovery Surcharge			
9	Estimated Capital Costs Under Normal Operating Conditions	$ 21,438,000		
10	Estimated Cost of Removal Under Normal Operating Conditions	3,499,000		
11	Straight Time Labor Costs	4,717,000		
12	Company-Owned Vehicle Costs	400,000	*	
13	Other Normal Operating Costs	600,000	*	
14	Additional Accrual to Property Reserve in 2004	14,000,000	*	
15	Total Exclusions from Ivan Deficit Cost Recovery Surcharge (Lines 9 thru 14)			$ 44,654,000
16	Recoverable Ivan Deficit Before Interest & Revenue Taxes (Line 7 - Line 15)			$ 51,135,000
17	Retail Jurisdictional Factor		x	0.9939036
18	Jurisdictional Recoverable Ivan Deficit Before Interest & Revenue Taxes (Line 16 x Line 17)			$ 50,823,000
19	Interest on Jurisdictional recoverable Ivan Deficit April 2005 through August 2006			1,962,000
20	Jurisdictional Recoverable Ivan Deficit Including Interest (Line 18 + Line 19)			$ 52,785,000
21	Less: Revenues Billed Through December 2005 (Excluding Revenue Taxes)			21,215,000
22	Less: Projected Billings January - August 2006 (Excluding Revenue Taxes)			17,987,000
23	Ivan Deficit to be Recovered through Securitization (Line 20 - Lines 21 thru 22)			$ 13,583,000

* Fixed Amounts As Agreed Between Parties to Stipulation and Settlement and approved by the FPSC in Order No. PSC-05-0250-PAA-EI.

Note: Lines 1 - 18 based on true-up filed January 31, 2006.
Based upon Transmission & Distribution known ($120,578,000) and estimated ($1,111,000) costs.
Based upon Generating Plants and Office Facilities known ($14,432,000) and estimated ($1,604,000) costs.

Storm-Recovery Costs Related to Hurricanes Dennis and Katrina

		Dennis [A]	Katrina [B]	Total
	<u>Estimated Transmission and Distribution Costs</u>			
1	External Costs including Contractors and Equipment	$ 41,253,000	$ 2,056,000	$ 43,309,000
2	Food, Lodging, Transportation, & Other	9,470,000	375,000	9,845,000
3	Materials	2,777,000	530,000	3,307,000
4	Company - Labor, Payroll Taxes and Benefits	2,647,000	973,000	3,620,000
5	Fuel	912,000	91,000	1,003,000
6	**Total Estimated Transmission and Distribution Costs (Lines 1-5)**	**$ 57,059,000**	**$ 4,025,000**	**$ 61,084,000**
	<u>Estimated Generating Plants and Office Facilities Damages</u>			
7	Crist Plant	2,043,000	-	2,043,000
8	Other Damages to Plants	73,000	237,000	310,000
9	Office Buildings	198,000	30,000	228,000
10	**Total Estimated Generating Plants and Office Facilities (Lines 7-9)**	**$ 2,314,000**	**$ 267,000**	**$ 2,581,000**
11	**Total Estimated Hurricane Dennis & Katrina Costs (Line 6 + Line 10)**	**$ 59,373,000**	**$ 4,292,000**	**$ 63,665,000**
12	**Less: Estimated Insurance Reimbursement**	**669,000**	**261,000**	**930,000**
13	Estimated Costs net of Insurance Reimbursement (Line 11 - Line 12)	$ 58,704,000	$ 4,031,000	$ 62,735,000
14	**Less: Company Voluntary Exclusions**			
15	**Estimated Capital Costs Under Normal Operating Conditions**	6,139,000	997,000	7,136,000
16	**Estimated Cost of Removal Under Normal Operating Conditions**	553,000	75,000	628,000
17	**Straight Time Labor Costs**	1,026,000	363,000	1,389,000
18	**Company-Owned Vehicle Costs**	60,000	18,000	78,000
19	**Other Normal Operating Costs (C)**	105,000	43,000	148,000
20	**Total Exclusions from Hurricane Cost Deficit (Lines 15 thru 19)**	7,883,000	1,496,000	9,379,000
21	**Total Dennis & Katrina Cost Deficit (Line 13 - Line 20)**	**$ 50,821,000**	**$ 2,535,000**	**$ 53,356,000**
22	**Interest on Reserve Deficiency January 2006 through August 2006 (D)**			**905,000**
23	**Total Dennis & Katrina Cost Deficit Including Interest (Line 21 + Line 22)**			**$ 54,261,000**

[A] Based upon Transmission & Distribution Known ($56,211,000) and Estimated ($848,000) costs.
Based upon Generating Plants & Office Facilities Known ($1,892,000) and Estimated ($422,000) costs.

[B] Based upon Transmission & Distribution Known ($3,586,000) and Estimated ($439,000) costs.
Based upon Generating Plants & Office Facilities Known ($3,000) and Estimated ($264,000) costs.

[C] Includes tree trimming costs, Company overtime labor costs, and materials and supplies.

[D] Interest was included in accordance with Section 366.8260 (1) (n) of the Florida Statutes. Interest was calculated by applying the projected interest rate (based on the short-term bank note being used to temporarily finance the costs of the storms) to the after-tax balance of the reserve deficiency for January 2006 through August 2006.

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Normal Operation & Maintenance Expenses Excluded from Storm-Recovery Costs

Cost by Category		Dennis		Katrina		Total	
Company Straight-Time Labor Costs	$	1,026,000	$	363,000	$	1,389,000	
Company-Owned Vehicle Costs		60,000		18,000		78,000	
Tree Trimming		48,000		19,000		67,000	(A)
Company Overtime Labor Costs		41,000		17,000		58,000	(B)
Materials & Supplies		16,000		7,000		23,000	(C)
TOTAL	**$**	**1,191,000**	**$**	**424,000**	**$**	**1,615,000**	

(A) Based upon the budgeted level for tree trimming contract labor for the number of restoration days (5 days for Dennis and 2 days for Katrina).
(B) Based upon the budgeted level for Company overtime labor for the number of restoration days (5 days for Dennis and 2 days for Katrina) including associated payroll taxes.
(C) Based upon the budgeted level for transmission and distribution materials and supplies for the number of restoration days (5 days for Dennis and 2 days for Katrina).