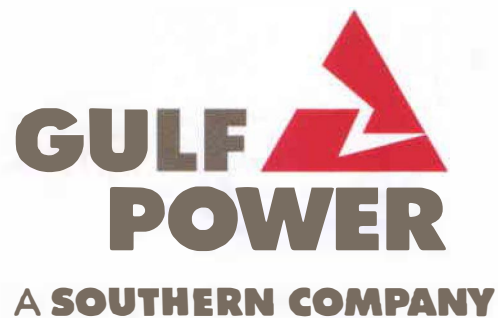


**BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION**

DOCKET NO. 130140-EI



**TESTIMONY
OF
S. W. CONNALLY, JR.**

1 GULF POWER COMPANY

2 Before the Florida Public Service Commission
3 Prepared Direct Testimony of
4 S. W. Connally, Jr.
5 Docket No. 130140-EI
6 In Support of Rate Relief
7 Date of Filing: July 12, 2013

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

9 A. My name is Stan Connally. My business address is One Energy Place,
10 Pensacola, Florida, 32520. I am President and Chief Executive Officer of
11 Gulf Power Company (Gulf or the Company).

12 Q. Please summarize your educational and professional background.

13 A. I graduated with a Bachelor of Mechanical Engineering from The Georgia
14 Institute of Technology in 1993. In 2004, I completed the Goizueta
15 Executive Education Program at Emory University. I began my career with
16 the Southern Company in 1989 as a co-op student at Georgia Power's Plant
17 Yates. Since that time, I have held positions of increasing responsibility in
18 Customer Operations, Sales and Marketing, and Power Generation at
19 Georgia Power, Alabama Power, and Mississippi Power. Immediately prior
20 to coming to Gulf Power, I served as the Senior Vice President of
21 Generation and Senior Production Officer at Georgia Power. In July 2012, I
22 assumed my current role as President and Chief Executive Officer of Gulf
23 Power.

24 Q. What is the purpose of your testimony?

25 A. The primary purpose of my testimony is to provide an overview of our

1 filing and to introduce our witnesses and case. I will summarize Gulf's need
2 for timely rate relief and describe the major factors causing this need. As
3 our other witnesses describe in greater detail, we have taken steps to defer
4 the need for rate relief as long as we can but have now reached the point
5 where further delay is no longer possible without risking our ability to reliably
6 and efficiently serve our customers over the long term. I will outline our
7 efforts to continue controlling costs and describe recent initiatives
8 implemented to sustain the level of customer service that our customers
9 expect and deserve.

10

11 Q. As President of Gulf Power what do you view as critical to the success of
12 the Company?

13 A. Our core values begin with safety. We want our employees to work safely
14 every day in every job so that they can go home to their families at the end
15 of the day in the same condition they were in when they came to work. A
16 safe work environment also creates a productive work environment which
17 benefits the employees, the Company and certainly our customers.

18

19 Further, as you will hear over and over again from the testimony of our
20 witnesses, customers are at the center of everything we do. The decisions
21 we make and the actions we take every single day are a reflection of that
22 belief. This belief drives us to continually invest in our employees and our
23 electric infrastructure, to be responsive and effective in our customer
24 contacts, and to deliver value through the services we provide.

25

1 **Lastly, we have an obligation to provide value to our investors who provide**
2 **us with the funds necessary to build and service our growing infrastructure**
3 **and customer base.**

4

5 **Q. Would you please provide an overview of the case that will be presented by**
6 **Gulf's witnesses?**

7 **A. Our case will be presented by a number of witnesses testifying in detail on**
8 **behalf of the Company. These witnesses include Company officers and**
9 **employees, as well as consultants from outside the Company with expertise**
10 **on specific subject matters. Collectively, these witnesses will demonstrate:**
11 **that our focus is on our customers; that Gulf's costs of providing retail**
12 **service are reasonable, prudent, and have outpaced Gulf's revenues; that**
13 **Gulf's actual and projected rate of return are well below any reasonable**
14 **level necessary to serve customers and attract capital for the long term; and**
15 **that the rates Gulf has proposed in this case are just and reasonable.**
16 **Simply stated, our witnesses demonstrate that a base rate increase is**
17 **necessary now if Gulf is to maintain customer satisfaction and the quality of**
18 **service our customers expect and deserve.**

19

20 **During the presentation of our case, you will hear from a group of witnesses**
21 **who manage operational areas within our company that focus directly on**
22 **service to our customers. Margaret Neyman, Customer Service General**
23 **Manager, will discuss Gulf's commitment to customer service and**
24 **satisfaction. Angela Strickland, Marketing General Manager, will discuss**
25 **the Company's measurement of customer satisfaction and the Company's**

1 marketing and economic development activities. Andy McQuagge,
2 Distribution General Manager, will address Gulf's electric distribution
3 system, including distribution performance and distribution system
4 investment. Chris Caldwell, Transmission General Manager, will discuss
5 the Company's transmission system, including Gulf's transmission
6 performance and transmission investment. Gulf's Senior Production Officer,
7 Michael Burroughs, will address the operation and performance of Gulf's
8 generation fleet and fuel inventory levels necessary for Gulf's continued
9 provision of reliable generation. Ray Grove, Power Generation Services
10 Manager, will discuss the Company's generation resources used in the
11 production of electricity, Gulf's resource planning process, and production
12 investment. These witnesses will also discuss their operations and
13 maintenance (O&M) budgets for the 2014 test year.

14
15 In addition to the witnesses who discuss those aspects of our operations
16 focused more directly on service to our customers, Gulf will present a
17 number of other professionals who provide testimony related to the
18 Company's finances and financial needs which are also critical to our ability
19 to serve our customers. Rhonda Alexander, Forecasting Supervisor, will
20 address the Company's forecast methodologies and results for customers,
21 energy sales, peak demand and base rate revenue. She will also discuss
22 the lingering effects of the "Great Recession" in Gulf's service area. Scott
23 Teel, Vice President and Chief Financial Officer, will address the overall
24 need for rate relief, the importance of maintaining the Company's financial
25 integrity and the resulting benefit to customers, Gulf's capital structure and

1 related cost of capital, and other financial matters pertinent to our request
2 for rate relief. Dr. Vander Weide, Research Professor of Finance and
3 Economics at Duke University and President of Financial Strategy
4 Associates, will discuss Gulf's cost of common equity. Mr. Harris, Vice-
5 President of EQECAT – ABS Consulting, will present the results of the
6 Company's most recent storm study that focuses on the risk of uninsured
7 loss to Gulf's transmission and distribution assets. Mr. Huck, Senior
8 Manager of the electric and gas utility practice at American Appraisal
9 Associates, Inc., will present the results of the Company's recent
10 depreciation study. Gulf's Comptroller, Connie Erickson, will explain Gulf's
11 2014 O&M budget within the Administrative and General (A&G) function.
12 She will outline the need to increase the accrual to the Company's property
13 damage reserve and support the depreciation and income tax expenses
14 included in the test year. James Garvie, Compensation and Benefits
15 Director for Southern Company Services (SCS), will discuss Gulf's
16 compensation and benefit programs which are designed as a total
17 compensation package to attract and retain qualified personnel and
18 motivate employees to achieve higher levels of performance, customer
19 satisfaction, and productivity. Richard McMillan, Forecasting, Budgeting,
20 and Corporate Performance Manager, will discuss the calculation of Gulf's
21 O&M expense benchmark, how Gulf utilizes SCS and the other Southern
22 Company affiliates to supplement Gulf's employee complement, and the
23 calculation of a hiring lag adjustment related to normal employee turnover at
24 Gulf. Susan Ritenour, Corporate Secretary, Treasurer, and Corporate
25 Planning Manager, will describe the Company's rigorous planning and

1 budgeting process and present the calculation of the rate relief requested in
2 this case.

3

4 The final group of witnesses to present testimony on Gulf's behalf will
5 discuss the cost-of-service study and rate design. Mr. O'Sheasy, a Vice-
6 President at Christensen Associates, will address the cost-of-service study
7 presented in this case. Jim Thompson, Supervisor of Pricing, Costing &
8 Load Research, will address rate design and other tariff issues. He will also
9 address the load research performed by and used by Gulf in this
10 proceeding.

11

12 Q. Why is rate relief critical for Gulf at this time?

13 A. Rates approved in Gulf's 2011 base rate case have not been and are not
14 projected to be adequate to cover Gulf's cost of providing electric service.
15 As projected in Gulf's 2011 base rate case, the Company has continued to
16 invest heavily in infrastructure required for us to serve our customers,
17 particularly transmission assets. Additionally, the recession has had a
18 lingering effect in our service area resulting in far less sales growth than
19 was expected. Gulf is requesting rate relief in order to continue to fulfill the
20 public service requirements set forth in the Florida Statutes and to fulfill the
21 needs and expectations of our customers in a safe, reliable, and efficient
22 manner.

23

24 While Gulf has continued and will continue to seek out and achieve
25 appropriate cost reductions in many areas of the business, the ability to

1 maintain Gulf's historically high standards of both operational performance
2 and customer service remains our priority. To achieve these priorities, our
3 investments for current and future customers must be adequately supported
4 by present rates. Without adequate rate relief at this time, we are
5 compelled to consider restrictions on capital investment and O&M expenses
6 that will have a detrimental effect on the system, the reliability of our service
7 to customers, and our ability to meet federal compliance requirements in a
8 timely manner.

9
10 Even with the cost containment measures the Company has employed
11 since the last base rate case, Gulf's return on equity has consistently been
12 below the bottom of the allowed range. In April 2013, the return was 9.14
13 percent and is projected to decline in the second half of 2013. Such low
14 achieved rates of return are simply not in the best long-term interests of
15 Gulf's customers, or fair to Gulf's investors who are integral to providing the
16 capital needed to serve customers.

17
18 Q. Please describe some of the actions Gulf has taken to control costs since
19 the last base rate case.

20 A. As described in greater detail by Gulf's other witnesses, the Company
21 continues to take reasonable steps to control costs addressed through base
22 rates. One such example involves operating decisions for our generation
23 fleet. Mr. Grove outlines actions taken to optimize the maintenance cycles
24 of our generating units during the last two years and in the future where
25 forecasted production levels are less than we have experienced in the past.

1 **These steps have resulted in immediate cost reductions and, based on**
2 **forecasted operating schedules of our coal-fired generating units, will**
3 **continue producing cost reductions over the long term.**

4

5 **As discussed by Mr. Teel, Gulf has also taken advantage of low interest**
6 **rates in the current market to refinance long-term debt which has resulted in**
7 **lower interest expense. These savings have a short- and long-term positive**
8 **benefit for customers and are a component of Gulf maintaining a lower**
9 **weighted average cost of capital.**

10

11 **These are examples of our continuing commitment to control costs.**

12

13 **Q. Can this Commission be assured that Gulf seeks to continually improve our**
14 **service as measured through the eyes of the customer?**

15 **A. Absolutely. Gulf's employees continuously listen to our customers and look**
16 **for advances in processes and technologies that will benefit our customers.**
17 **Through face-to-face contact, letters, emails, phone calls, focus groups and**
18 **surveys, the Company garners feedback from customers. This feedback**
19 **makes us think critically about our performance and leads to creative**
20 **responses by employees to meet customers' expectations. Since arriving at**
21 **Gulf, I have personally been active in visiting with and seeking to**
22 **understand the needs of our customers. I believe my personal engagement**
23 **with customers – large and small – sets the right tone for the rest of the**
24 **Company.**

25

1 Q. Please describe some of the steps that Gulf has taken to improve its
2 operations and customer service.

3 A. Keeping our system reliable remains a strong driver of customer
4 satisfaction, and our ongoing investments in the system are bringing value
5 to customers. The installation of intelligent electronic devices on our
6 transmission and distribution infrastructure has resulted in reduced outage
7 times and fewer interruptions in service. Mr. McQuagge discusses
8 distribution investments, and Mr. Caldwell discusses transmission
9 investments and their respective benefits to our customers.

10

11 Gulf is focused on making it easy for customers to do business with us by
12 identifying meaningful and relevant options that fit our customers' lifestyles.
13 For example, a growing number of our customers are demonstrating their
14 preference to conduct business with us through the internet. Through our
15 website, GulfPower.com, we offer innovative solutions to help serve our
16 customers. Ms. Neyman will discuss several service requests that can be
17 conducted online. Many of these same services are now offered through a
18 mobile application available for smart phones.

19

20 Gulf is now using social media applications such as Facebook and Twitter
21 as additional pathways to connect with our customers on service issues, to
22 keep customers updated about the our storm restoration efforts, and to
23 provide other important Company and customer information. Based on the
24 growing number of customers who engage with us through social media,
25 these communication channels are becoming more and more important.

1 In addition to the traditional methods of payment via the mail or visiting a
2 local office, Gulf offers the following other options: paying online, paying
3 electronically through Auto Pay, using a third party vendor that accepts
4 credit cards, or, the newly established method of making a cash payment
5 through kiosks located in certain convenience stores.

6
7 Based on direct customer feedback, enhancements are scheduled for 2013
8 to the Company's Voice Response Unit system. These changes will allow
9 both speech and touch tone responses, improve the menu design, and
10 permit a caller to speak directly to a Customer Care Representative earlier
11 in the process.

12
13 These are just a few examples of the actions taken to improve operations
14 and customer service described by Gulf's other witnesses.

15
16 Q. How does Gulf rank in customer value as compared to its peer utilities?

17 A. When measured against a peer group of utilities, Gulf was in the top quartile
18 of overall performance for 2012 and has been every year since 2000. Our
19 goal is to be among the best utilities in the country in regards to customer
20 service, and we are proud of our performance when compared to these
21 peers. This outstanding performance is a testament to the continued efforts
22 of Gulf's employees to exceed our customers' expectations each and every
23 day. Ms. Strickland will discuss Gulf's performance in more detail as well as
24 describe how we compare the Company's performance to our utility peers.

25

1 Q. Does Gulf monitor other operational measures as part of the Company's
2 commitment to performance, reliability, and ultimately customer
3 satisfaction?

4 A. Yes. For example, the reliability of our generation fleet is critical to our
5 ability to deliver electricity to our customers. Mr. Burroughs describes in his
6 testimony the excellent performance achieved by Gulf's generation fleet
7 during the last several years, including the Company's best ever Equivalent
8 Forced Outage Rate in 2012. Limiting the number and duration of outages
9 on the distribution and transmission systems also helps us to maintain or
10 improve reliability through the eyes of our customers. Both Mr. McQuagge
11 and Mr. Caldwell discuss the role of operational performance measures in
12 their respective areas of functional responsibility. These are examples of
13 how we use operational measures monitored on a continuous basis to
14 ensure we are meeting our commitment to maintaining the reliability of our
15 electric system, strong customer service and high customer satisfaction.

16
17 Q. Earlier you mentioned the lingering effects of the "Great Recession." Are
18 there complementary ways to improve the economic health of both
19 Northwest Florida and the Company?

20 A. Simply stated, job growth and expanding business investment are vital to
21 communities across Northwest Florida. As our communities and local
22 economic development leaders work to create these expansions, they look
23 to Gulf as a partner for several reasons. Any new or expanding business is
24 going to need electric service, and generally they want to engage with their
25 power provider early in the process to understand service options and

1 ensure reliable, timely delivery. Gulf also plays a vital role in creating a
2 regional focus because our footprint spans multiple counties and diverse
3 economic sectors. In summary, Gulf provides a service that is critical to all
4 customers, and we are among the very few companies that have a regional,
5 strategic focus in the area we serve.

6

7 Additional customers gained through economic development efforts provide
8 us with an opportunity to maximize the use of our electric infrastructure.

9 Utilizing this infrastructure efficiently results in more economic cost
10 allocations to all customers and produces new revenue that helps to
11 mitigate future cost pressures.

12

13 Q. How does Gulf's requested increase compare to Gulf's total revenues
14 before consideration of the increase?

15 A. Gulf is requesting a base rate increase of \$74.4 million, which is a 5.9
16 percent increase over the total revenues produced by today's rates. Gulf's
17 other witnesses in this case provide details regarding how and why many of
18 our costs of doing business continue to increase. We are only asking for
19 those costs necessary to provide safe and reliable service and maintain
20 customer satisfaction over the long term.

21

22 Q. What is Gulf's projected return on equity for the test year without rate relief?

23 A. As shown on Mr. Teel's Exhibit RST-1, Schedule 5, the Company's return
24 on equity has been below the minimum of our authorized range since rate
25 relief was last granted. In fact, it has been below the authorized range since

1 June 2010. Without rate relief in this case, Gulf's return on common equity
2 associated with base rates for the 12 months ending December 31, 2014 is
3 projected to be only 5.14 percent. This is clearly not adequate when
4 compared to the 11.50 percent cost of common equity that Dr. Vander
5 Weide has determined to be reasonable and appropriate for Gulf. Without
6 timely rate relief, Gulf will endure a weakening financial condition which will
7 adversely affect our ability to provide reliable electric service to our
8 customers.

9

10 Q. Gulf's filing in this case includes a possible step increase for compliance-
11 related transmission costs in 2015. Please explain the need for the step
12 increase.

13 A. The requested step increase relates to transmission investments Gulf is
14 making as part of our compliance strategy with regard to the federal
15 Mercury and Air Toxics Standards (MATS) rule. We believe that these
16 costs are most appropriate for recovery through the Environmental Cost
17 Recovery Clause (ECRC). However, if recovery is not provided for through
18 the ECRC mechanism, we believe it is necessary and appropriate to
19 address recovery of these compliance-related costs in this proceeding to
20 avoid the time and expense for all parties of yet another proceeding for a
21 known change in our revenue requirement related to compliance activities in
22 the near future. Details of our request are provided by Mr. Caldwell, Ms.
23 Ritenour, and Mr. Thompson.

24

25

1 Q. Please summarize your testimony.

2 A. Our objective at Gulf is to provide safe, reliable and efficient electric service
3 to customers, while working to improve the communities we serve. We are
4 very proud of our commitment to our customers and Northwest Florida. Our
5 successes are a result of the dedicated employees who serve our
6 customers all across the region. Through the efforts of these employees,
7 we have been successful in keeping operating budgets lean in the face of
8 increasing costs to build, operate and maintain our system.

9

10 We understand that price increases can place an economic burden on our
11 customers; however, the inability to meet our customers' service
12 requirements would place an even greater burden on Gulf's customers and
13 our local economy. Gulf must make capital investments today in the
14 equipment necessary to maintain reliability and strengthen our ability to
15 serve customers both now and in the future. We are not able to defer these
16 investments or our request for this increase in base revenues.

17

18 The price adjustment we are seeking will provide Gulf the ability to continue
19 providing safe, reliable, and efficient service at the levels our customers
20 have come to expect, and to have a reasonable opportunity to earn a fair
21 return which will enable us to maintain access to capital markets at a
22 reasonable cost. Keeping Gulf financially healthy by granting the requested
23 increases in retail revenues is in the best interests of our customers.

24

25

1 Q. Does this conclude your testimony?

2 A. Yes.

3

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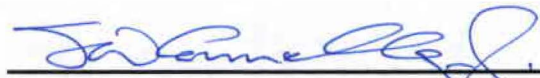
25

AFFIDAVIT

STATE OF FLORIDA)
)
COUNTY OF ESCAMBIA)


Docket No. 130140-EI

Before me the undersigned authority, personally appeared
S. W. Connally, Jr., who being first duly sworn, deposes, and says that he is the
President and Chief Executive Officer of Gulf Power Company, a Florida
corporation, and that the foregoing is true and correct to the best of his
knowledge, information, and belief. He is personally known to me.



S. W. Connally, Jr.
President and Chief Executive Officer

Sworn to and subscribed before me this 0th day of July, 2013.



Notary Public, State of Florida at Large
Commission No. EE166803
My Commission Expires 2/6/16

