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May 5, 2016



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COMMISSION  
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Mr. Braulio L. Baez  
Executive Director  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Tallahassee, Florida 32399-0850

Re: Accounting recognition of Gulf Power Company's ownership in Plant Scherer as being in service to retail customers

Dear Mr. Baez:

The purpose of this letter is to notify the Florida Public Service Commission ("Commission") of a change in the status of Gulf Power Company's ("Gulf Power", "Gulf" or the "Company") generation resource known as Plant Scherer. As a result of this change in status, this letter also serves as Gulf's request that the Commission take formal action to promptly recognize that Gulf's ownership interest in Plant Scherer Unit No. 3 and related common facilities at Plant Scherer (collectively "Scherer" or "Scherer Unit 3") is now rededicated to serve the native load customers for whom it was planned, acquired and ultimately built. Gulf further requests authorization from the Commission for the Company to (1) stop making adjustments in its monthly surveillance report filed with the Commission designed to remove Gulf's Scherer related investment and expenses from the retail jurisdictional rate of return calculation to the extent that it is not currently committed to off system sales; and (2) reflect the Scherer generation resource as a native load serving resource in all other regulatory filings with the Commission.

The Company has been making adjustments to remove Scherer from the retail jurisdictional filings since 1990 pursuant to the direction of the Commission memorialized in Order No. 23573 issued in Docket No. 891345-EI on October 3, 1990. The action requested by this letter is necessary to avoid significant deterioration of Gulf's financial integrity, to the ultimate detriment of the retail customers which Gulf is obligated to serve under Chapter 366 of the Florida Statutes.

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Gulf is not aware of any disputed issues of material fact with regard to the official Commission action requested by this letter. The Company is not seeking modification or reversal of any proposed Commission action. The relief sought by this letter would allow Gulf to discontinue adjustments that have been made to its monthly surveillance reports since the Commission's decision in Order No. 23573 which the Company received by U.S. Mail shortly after it was issued on October 3, 1990. Gulf became aware of the Commission's decision in Docket No. 891345-EI through its attendance at the Special Commission Conference held on August 9, 1990, at which the Commission's decision was made. If further information is needed regarding this request in order to support Commission action, I request that the Commission work through Gulf Power's General Counsel:

Jeffrey A. Stone  
Beggs & Lane  
501 Commendencia Street  
Pensacola, Florida 32502  
(850) 432-2451

I also request that a copy of all notices and communications with respect to this letter and the official Commission action we are requesting also be sent to:

Robert L. McGee, Jr.  
Regulatory and Pricing Manager  
Gulf Power Company  
One Energy Place  
Pensacola, FL 32520-0780  
(850) 444-6530

### *The Change in Status*

Effective January 1, 2016, for the first time since Scherer Unit 3 began commercial operation on January 1, 1987, a majority of Gulf's ownership in Scherer is now uncommitted to interim long-term off system power sales and no new off system sales are anticipated. This change is a result of the expiration at the end of its term of a purchased power agreement ("PPA") committing 110 megawatts from Gulf's ownership in Scherer Unit 3 to a Florida utility from the summer of 2010 through December 2015. At the end of May 2016, another 50 megawatts to a Florida utility comes out from under the commitment to interim long-term off system sales. This occurs when

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the next contract tied to Gulf's ownership in Scherer Unit 3 expires at the end of its term. Finally, on January 1, 2020, for the first time since Scherer Unit 3 began commercial operation, 100 percent of Gulf's ownership interest in Scherer will be available to serve Gulf's native load customers in Northwest Florida when the last 50 megawatts of Gulf's ownership share comes out from under the commitment to interim long-term off system sales due to the expiration at the end of its term of the third and final PPA in effect since the summer of 2010. Thus, between January 1, 2016, and December 31, 2019, increasing amounts of Gulf's ownership in Scherer are no longer supported on an interim basis by revenues from interim long-term off system sales. It is therefore appropriate for the current investment and related expenses to now be reflected as serving the native load customers for whom it was originally planned, acquired and built for the remaining life of Scherer Unit 3. This was the plan all along as evidenced by the decisions of the Commission when it encouraged Gulf to pursue acquisition of its ownership in Scherer as a prudent and cost effective alternative to generation that Gulf was otherwise planning to construct during the late 1970s and early 1980s at the Company's Caryville site.

### *The Regulatory Compact*

This Commission, through its numerous decisions related to Plant Scherer from 1978 through 1990, established a clear and binding regulatory compact with Gulf regarding the Company's investment in Plant Scherer. Since 1978, when the alternative of acquiring ownership in Plant Scherer in lieu of constructing a generating unit at Caryville was first developed, Gulf has kept the Commission informed of its efforts with respect to this investment. In a variety of forms, Gulf received the Commission's approval of the Company's endeavors to acquire an ownership interest in Plant Scherer in order to ultimately serve Gulf's territorial or native load customers. Through numerous proceedings at the Commission, the following are matters of record regarding the Commission's approval of Gulf's investment in Plant Scherer as the ultimate plan to serve native load customers:

1. By letter dated August 25, 1978, from E. L. Addison, Gulf Power President, to David Swafford, Commission Executive Director, the Company notified the Commission of Gulf's opportunity to purchase an interest in the four units then under construction at Plant Scherer as an alternative to construction of the proposed Caryville electric generating plant. This letter requested that the Commission approve the cancellation of Caryville and authorize Gulf to amortize the resulting cancellation charges above the line through retail rates. The purpose of this request was to receive the regulatory

assurance needed to enable Gulf to negotiate for the purchase of an ownership interest in Plant Scherer.

2. In October 1978, the Commission held a workshop to review Gulf's plans regarding the anticipated acquisition of an ownership interest in Plant Scherer in lieu of continued construction of Caryville. At that workshop, the Commissioners recognized that the purchase of an interest in Plant Scherer appeared to be in the best interest of Gulf's retail customers and, under the circumstances presented, would be the appropriate course of action for Gulf to pursue. Although this was an informal workshop, it was clear from the following exchange that Gulf needed and expected a continuity of commitment from the Commission:

COMMISSIONER MAYO : ...Suppose that this Commission, as it is presently constituted, gave you some type of encouragement but, as we have already explored it, this thing could not be finalized to a point of being quite positive perhaps until a rate case, but if this Commission gave you that encouragement and then come January in all probability there are certainly going to be changes of some kind, it would probably be in effect at the time your next rate case came about. This Commission would no longer be here, another one having taken its place, how much strength and confidence could you put in the encouragement that you got from this Commission?

MR. ADDISON: I would put a great deal in it because, contrary to what I heard Judge Mann say a couple of times, I believe that there is some continuity of commitment by this Commission. If you will pardon me, sir.

COMMISSIONER MANN: Sure.

MR. ADDISON: And we have to operate like that. I think we have to operate that way, that there is a continuity of commitment by this Commission.

3. In a letter dated December 4, 1978, William D. Talbott, Accounting Director of the Commission, acknowledged and accepted the Company's proposed accounting and amortization of the plant cancellation costs beginning January 1, 1979, as consistent with the prescribed accounting under the Commission's adoption of the Federal Energy Regulatory Commission's Uniform System of Accounts and stated that no further approval was necessary. Mr. Talbott's letter noted that ultimate approval of the recovery of cancellation costs would necessitate further Commission review. It also noted, however, that given the long-run savings associated with the acquisition of an

ownership interest in Plant Scherer in lieu of the continued construction of Caryville, regulatory approval should be anticipated.

4. Negotiations with Georgia Power over Gulf's proposed acquisition of interests in Plant Scherer evolved over the next 14 months. By letter dated January 22, 1980, Mr. Addison informed the President of Georgia Power of Gulf's desire to purchase a 25 percent interest in Scherer Units 3 and 4. In that letter, Gulf acknowledged that construction plans indicated Unit 3 would begin commercial operation in 1987 and Unit 4 would begin commercial operation in 1989. These scheduled completion and commercial operation dates were ultimately met.
5. In Gulf's 1980 rate case, Docket No. 800001-EU, the Commission did not question whether Gulf should invest in the Plant Scherer units, but rather focused on potential issues in Georgia that might prevent Gulf's acquisition of the Plant Scherer units. As a result, the Commission placed a "subject to refund" condition on the recovery of the amortization of the Caryville cancellation charges pending finalization of the contract between Gulf and Georgia Power.
6. On February 16, 1981, executives of Gulf Power once again met with the Commission, the Commission Staff and the Office of Public Counsel regarding the proposed acquisition of ownership in Plant Scherer Units 3 and 4. At that meeting, Gulf pointed out that the commercial operation dates for the two units preceded the anticipated need of the generation for Gulf's retail customers by several years. It was clear that Gulf's planned acquisition of the units was exclusively for the ultimate long-term needs of its native load customers in Northwest Florida. To bridge the gap between the commercial operation date and the anticipated need of the generation for native load customers, Gulf proposed to commit the Plant Scherer units to interim long-term off system power sales through contracts with other unaffiliated utilities, including several in Florida. Gulf sought assurances from the Commission before committing the Company by contract to purchase the proposed ownership interests. Gulf's concerns were twofold. First, given that Plant Scherer is located outside of Florida, Gulf did not have the benefit of an order from the Commission in a formal need determination under the Florida Electrical Power Plant Siting Act as a basis for moving forward with the planned acquisition. Second, Gulf was also concerned about the possibility that inconsistent treatment might be afforded Gulf's investment in Plant Scherer due to the fact that there would be interim periods between the date the units entered commercial operation and the time the units would be released from the interim commitment to wholesale off system power sales and, therefore, would be available to serve Gulf's native load customers. In the February 1981 proceeding, the Commissioners discussed their prior

decisions relative to the Caryville cancellation charges pending consummation of the Plant Scherer purchase:

CHAIRMAN CRESSE: I think there is, what got this thing to us, Commissioner, was that during the course of the last rate hearing, we got some word through one of the publications and so forth that the terms and conditions and the explanations which were given in 1978 for writing it off may not be able to be accomplished because of some reluctance on the part of going ahead to construct the Scherer Plant which they would have an interest in. Essentially, in '78 they said, "We've got a better idea. We'll cancel Caryville and buy Scherer. And in '80 we had a deal that says, 'that was a great idea to cancel Caryville, but we're not so sure they're even going to build Scherer.'"

And Commissioner Gunter is an avid reader, and he read that there was a little something going on up there and that they may not build Scherer and we said, "Wait a minute. If it was a good deal, if the concept, terms, and conditions of which we allowed to write it off in '78 aren't going to come to some successful conclusion, maybe we ought not let you write it off." So we said, "We'll put that under bond and give you 12 months to come in and tell us what you're going to do or to otherwise justify the decision to cancel Caryville was a wise decision."

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.

COMMISSIONER GUNTER: 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: We looked at it as encouragement.

CHAIRMAN CRESSE: 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.

7. Based upon all of the above, Mr. Addison, in a memo dated February 18, 1981, directed Earl Parsons to move with dispatch to complete the negotiations with Georgia relative to the purchase of an interest in Plant Scherer. 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 agreements were signed, committing portions of the Plant Scherer units to interim long-term off system sales through 1992. Those initial contracts were subsequently amended in 1982 to extend the off system sales through 1995.
8. At the conclusion of Gulf's 1981 rate case, Docket No. 810136-EU, in Order No. 10557, the Commission stated that:
  - ... the decisions involving the expansion of Gulf Power are based on the long-term best interest of Gulf's customers. The cost savings associated with Gulf's participation in Plant Daniel and Plant Scherer in lieu of Caryville are examples of Gulf's coordination with the Southern Company.[Order, page 41]

In this order the Commission again held recovery and amortization of the Caryville cancellation charges subject to refund pending finalization of the agreement to purchase the ownership interest in Plant Scherer.

9. In Gulf's next rate case, Docket No. 820150-EU, Order No. 11498, the Commission continued the allowance of recovery of the cancellation charges associated with the Caryville site, holding:
  - This issue has also been thoroughly examined in the Company's previous two rate cases. In both of those cases we found that the Company'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". (Docket No. 810136-EU, Order No. 10557, p. 13.)[Order, page 15]

In this same order the Commission reviewed the Unit Power Sales contracts, of which Plant Scherer was a significant part, and determined that the sales would cause Gulf's "retail ratepayers" to "benefit handsomely" from the sales.

10. Throughout the remainder of 1982 and 1983, Gulf continued to perform cost benefit analyses relative to its investment in Plant Scherer Units 3 and 4. As a result of these analyses, Gulf's financial condition, and declining load growth, Doug McCrary, Gulf Power President, wrote the president of Georgia Power on December 9, 1983, seeking to limit Gulf's participation in Plant Scherer to 25 percent of Unit 3. Georgia Power agreed to this limitation by letter dated December 13, 1983.
11. On March 1, 1984, Gulf executed the Purchase and Ownership Participation Agreement and the Operating Agreement between Georgia Power Company and Gulf Power Company for a 25 percent interest in Scherer Unit 3. The closing occurred on October 18, 1984, following SEC approval on October 10, 1984. Gulf's acquisition was already committed in varying amounts to interim long-term off system power sales through 1995.
12. On January 1, 1987, Scherer Unit 3 began commercial operation, and Gulf began including the portion of its Scherer ownership not then committed to the interim long-term off-system sales in its calculation of the retail rate of return presented to the Commission in monthly surveillance reports.
13. In 1988, an additional round of Unit Power Sales contracts with other utilities extended the commitment of Gulf's ownership in Scherer to interim long-term off system power sales to the summer of 2010.
14. In 2004, a third and final round of PPAs for interim long-term off system power sales involving Gulf's ownership in Scherer were executed between Gulf and other non-affiliated utilities. The 2004 agreements extended the commitment to interim long-term off system sales from the summer of 2010 through December 2015 for 110 megawatts to one Florida utility; an additional 50 megawatts to another Florida utility through May 2016; and an additional 50 megawatts to a Georgia electric membership cooperative through December 2019. Together, the 2004 PPAs provided revenues to fully cover all of Gulf's revenue requirements associated with its ownership in Scherer. Two of the three 2004 PPAs that were to become effective in the summer of 2010 were subject to "regulatory out" clauses that required approval by the Commission for retail cost recovery by the purchasing utilities before the contracts would be effective. The



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Commission granted that approval in separate orders for each affected purchasing utility in 2005.

In addition, to the above referenced reviews and determinations as to the prudence of Gulf's decisions to pursue Plant Scherer as a cost effective alternative to continueing to construct a unit at Caryville, the Company reflected its intent to participate in Plant Scherer in Gulf's annual Ten Year Site Plan filings with the Commission. At no time, to the knowledge of the Company, did anyone take issue with the prudence of the Company's decision to participate in Plant Scherer on behalf of its native load customers in Northwest Florida. Based on the Commission's repeated confirmation of the prudence of the Company's decision to acquire ownership in Plant Scherer, Gulf took the appropriate steps to secure this generation resource, and it is now available to serve Gulf's native load customers.

#### ***Transition Back to Retail Service***

For the past 29 plus years, the revenue requirements for Scherer have been almost exclusively supported by revenues received from interim long-term off system sales, primarily to other Florida utilities. During the period that Gulf's ownership of Scherer has been committed to interim long-term off system sales, the Company has retired seven of its older and smaller fossil-fired generation units. Between 2003 and 2006, Gulf retired Crist Units 1, 2 and 3 representing approximately 94 megawatts of generating capacity (Generation Maximum Nameplate capacity as reflected in Gulf's Ten Year Site Plan filings). Between April 2014 and April 2016, Gulf retired its two oldest coal-fired generation units (Scholz 1 and 2) and the two coal-fired units at Plant Smith (Smith 1 and 2), representing approximately 397 megawatts of generating capacity. Gulf's Scherer Unit 3 is effectively the long-term replacement for approximately 45 percent of this retired generation (approximately 223 megawatts replacing approximately 491 megawatts measured on a Generation Maximum Nameplate basis).

Since the unit was built to serve retail customers and is now available to serve these customers, it is timely and appropriate for the Commission to acknowledge that the unit is now in service to the customers for whom it was planned, acquired and built. Scherer Unit 3 was purchased for the long-term best interest of Gulf's native load customers. A decision by the Commission not to allow the newly uncovered investment and related expenses to be reflected in retail service through monthly surveillance reports and in other regulatory matters under its jurisdiction would constitute a reversal of the Commission's earlier decisions that the purchase

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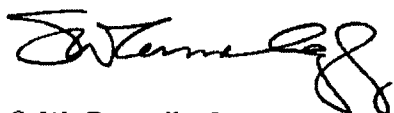
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of an interest in Plant Scherer was prudent and in the long-term best interest of Gulf's native load customers.

Recognition of Scherer Unit 3 as a retail serving resource is in the long-term best interest of Gulf's retail customers. Every decision which Gulf has made with respect to Plant Scherer has been made for the retail customers' long-term benefit. The Commission's prior decisions recognized that Gulf's actions were for the benefit of the customers it is statutorily obligated to serve. The Commission should reaffirm its earlier decisions recognizing the prudence of Gulf's decision to purchase an interest in Plant Scherer and grant the relief Gulf is requesting through this letter.

For the foregoing reasons, Gulf respectfully requests that the Commission enter its order reaffirming the prior decisions encouraging Gulf to acquire Scherer Unit 3 for the long-term best interests of the Company's retail customers. The Commission should therefore allow Gulf to promptly recognize that the Company's ownership interest in Scherer Unit 3 serves Gulf's native load customers when and as the unit comes out from under its previous commitments to interim long-term off system sales. The requested order would allow Gulf to reflect Scherer Unit 3 as a retail resource in the Company's monthly surveillance report and other regulatory filings to the extent that it is not currently committed to off system sales.

Sincerely,



S. W. Connally, Jr.

Chairman, President and Chief Executive Officer  
Gulf Power Company

cc: Chairman Julie Imanuel Brown  
Commissioner Lisa Polak Edgar  
Commissioner Art Graham  
Commissioner Ronald A. Brisé  
Commissioner Jimmy Patronis  
Keith Hetrick, General Counsel  
Commission Clerk  
J. R. Kelly, Public Counsel