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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Petition for increase ) DOCKET NO. 110138-EI  
in rates by Gulf Power ) FILED: November 22, 2011  
\_\_\_\_\_)

TELEPHONE DEPOSITION OF: MICHAEL P. GORMAN

TAKEN ON BEHALF OF: FLORIDA PUBLIC  
SERVICE COMMISSION

DATE: FRIDAY, DECEMBER 2, 2011

TIME: Commenced at 9:36 A.M.  
Concluded at 10:35 A.M.

LOCATION: 2540 SHUMARD OAK BLVD.  
ROOM 382D  
TALLAHASSEE, FLORIDA

REPORTED BY: MICHELLE SUBIA, RPR  
Notary Public in and for  
the State of Florida  
at Large

\* \* \*

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1 staff.

2 MR. BUYS: Dale Buys with Commission staff.

3 MR. MELSON: Richard Melson on behalf of Gulf  
4 Power Company.

5 MR. YOUNG: And Ms. White, if you want to  
6 introduce yourself and introduce the witness, the  
7 deponent.

8 MS. WHITE: I'm Karen White on behalf of  
9 Federal Executive Agencies and our witness is  
10 Mr. Michael Gorman from Brubaker & Associates.

11 MR. YOUNG: Okay. Is there anyone else on the  
12 line that has not introduced themselves?

13 THE WITNESS: The Notary is on the line with  
14 me right now.

15 MR. YOUNG: Okay. If the Notary can introduce  
16 herself or himself.

17 MS. DECKER: My name is Maria Decker.

18 MR. YOUNG: Okay. And with that, if --  
19 Ms. Ducker you said?

20 MS. DECKER: Ms. Decker.

21 MR. YOUNG: Ms. Decker, can you please swear  
22 the witness in.

23 MS. DECKER: Sure.

24 Thereupon,

25 MICHAEL P. GORMAN  
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1 was called as a witness, having been first duly sworn by  
2 NOTARY PUBLIC MARIA DECKER, Missouri Commission Number  
3 09706793, (present with the witness) was examined and  
4 testified as follows:

5 MR. YOUNG: And Ms. Decker, my fax number is  
6 area code (850)413-6227.

7 MS. DECKER: Okay. I'll send that over.

8 MR. YOUNG: Okay. Thank you.

9 MS. DECKER: Thank you.

10 EXAMINATION

11 BY MR. YOUNG:

12 Q Mr. Gorman, I appreciate you taking time this  
13 morning for this deposition. At this point during the  
14 deposition -- at any point during the deposition -- let  
15 me back up. I want to take care of some preliminary  
16 matters.

17 First at it relates to breaks, at any point  
18 during the course of this deposition, Mr. Gorman, if you  
19 need a break, please let me know and I will gladly  
20 accommodate that, okay?

21 A Thank you.

22 Q Also during the course of this deposition, I  
23 may ask some questions that need to be clarified or you  
24 do not understand. If that's the case, if we're having  
25 problems, what we'll do -- what I suggest we do is go

1 off the record and have a conversation offline, and then  
2 once that's been clarified we can go back on the record  
3 and I'll ask the question and you can answer it, okay,  
4 if you can?

5 A Very good.

6 Q Also during the course of this deposition, I  
7 may ask a question that you did not hear and you may ask  
8 me to repeat it, either myself, or we can ask the court  
9 reporter to repeat the question, okay?

10 A Okay.

11 Q All right. Also during the course of this  
12 deposition, I may use abbreviations, for example, I may  
13 use Gulf or GPC, instead of Gulf Power Company, or ROGs  
14 or POGs instead of interrogatories or request for  
15 production of documents. I'll do my best to use the  
16 entire word, but if you have any questions regarding the  
17 meaning of a term used, please let me know, okay?

18 A Yes.

19 Q All right. With that, Mr. Gorman, can you  
20 please state your full name for the record, please?

21 A My name is Michael P. Gorman.

22 Q And what is your occupation and business  
23 address, Mr. Gorman?

24 A I'm a consultant in the field of regulatory  
25 economics. My business address is 16690 Swingley Ridge

1 Road, Chesterfield, Missouri.

2 **Q Okay. And if you hear something, that's the**  
3 **maintenance guys outside cutting the lawn or doing**  
4 **something outside.**

5 A Okay.

6 **Q So if you hear anything in the background,**  
7 **please excuse us.**

8 A Thank you.

9 **Q Forgive us.**  
10 **What is your current responsibilities in this**  
11 **position?**

12 A To assist clients in energy  
13 procurement-related activities, including regulatory  
14 price proceedings, competitive procurement, forecasting,  
15 and asset utilization studies.

16 **Q Okay. On whose behalf are you appearing in**  
17 **this proceeding?**

18 A The Federal Executive Agencies.

19 **Q And what is the purpose of your testimony in**  
20 **this proceeding?**

21 A The purpose of my testimony is to estimate a  
22 fair return on common equity and overall rate of return  
23 for Gulf Power.

24 **Q Have you prefiled direct testimony in this**  
25 **case?**

1 A Yes.

2 Q And included in that testimony -- attached to  
3 that testimony are exhibits, correct?

4 A Correct.

5 Q All right. And subject to check, your  
6 prefiled direct testimony consists of 63 pages, correct?

7 A That's correct.

8 Q And you have several exhibits to your  
9 testimony?

10 A I do.

11 Q All right. And we will go through the -- just  
12 to give you a heads up, we will go through the prefiled  
13 testimony and the exhibits, okay?

14 A All right. Can I make one correction to a  
15 previous answer I just gave?

16 Q Yes.

17 A My testimony also includes comments on the  
18 critical peak pricing proposal of Gulf Power in addition  
19 to rate of return.

20 Q Okay. At this time, Mr. Gorman, do you have  
21 any additions, deletions, or corrections to your  
22 prefiled testimony or exhibits?

23 A I do not.

24 Q Okay. Looking at the electric company proxy  
25 group, can you please turn to page 14 of your prefiled

1 **direct testimony? Are you there?**

2 A I am, yes, I'm sorry.

3 **Q On line 12 -- I mean, line 11, excuse me, can**  
4 **you take a minute to read that to yourself?**

5 A Okay. I've preread it.

6 **Q Okay. You state that you excluded Nextera**  
7 **Energy from electric utility proxy group because the**  
8 **company became engaged in merger and acquisition**  
9 **activity; is this correct?**

10 A Yes.

11 **Q Can you please describe the merger and**  
12 **acquisition activity in which Nextera Energy became**  
13 **engaged in?**

14 A They were acquiring certain assets which I  
15 found to be material, resulting in uncertainty about  
16 whether or not the standalone company parameters were  
17 reflecting -- or the market indicators were reflecting  
18 standalone company principals or the expectation of what  
19 the company would look like after the acquisition took  
20 place.

21 **Q And what assets are you referring to?**

22 A I would have to review my work papers on this.  
23 Can you give me a minute?

24 **Q Sure.**

25 A I list the assets and merger activities of

1 these companies and I would have to refer to that.

2 **Q Okay, sure, take your time.**

3 A I apologize, I've got too many work papers  
4 here. In an S&L document, it states that Nextel (sic)  
5 is actually selling some generating assets to LS Power  
6 Group and the estimated value was a little over a  
7 million dollars, and that was the reason for it.

8 The S&L report states that an affiliate of LS  
9 Power in New York agreed to acquire four natural gas  
10 fired power stations in Juno Beach, Florida from Nextera  
11 Energy Resources, a unit of Nextera Energy. So it was  
12 due to that transaction is the reason I removed that  
13 company from the proxy group.

14 **Q Okay.**

15 A I apologize it took me so long to get that  
16 paper.

17 **Q Not a problem at all.**

18 **On page 14, line 14, you state that "Merger**  
19 **and acquisition activity could significantly skew the**  
20 **equity return for Nextera Energy"; is this correct?**

21 A It could, yes.

22 **Q Can you please explain in your opinion how**  
23 **this M&A activity will skew the equity return estimated**  
24 **for Nextera Energy?**

25 A Well, the market data, the analyst information

1 available to measure the return for Nextera Energy is  
2 based on the future outlook for that company. And the  
3 price -- at the time those forecasts were made, such as  
4 earnings growth forecasts, it was based on the  
5 information available to the analyst.

6 It's not clear whether or not the analysts  
7 reflected this merger, acquisition, or activity in  
8 deriving at those earnings forecasts. However, as soon  
9 as the merger or acquisition is announced to the market,  
10 the market will immediately adjust the stock price.

11 So there's a concern that there is a  
12 discrepancy between the outlook analysts relied on to  
13 form future growth projections for earnings and  
14 dividend-paying ability of the company and the outlook  
15 that the market was considering in forming the valuation  
16 of that same earnings and dividend strength. So that's  
17 the concern is that the observable stock price doesn't  
18 reflect the same information that analysts consider in  
19 forming earnings projections.

20 Also, when a merger or acquisition activity is  
21 undertaken, the stand-alone characteristics of a company  
22 can be modified by that merger or acquisition such as  
23 synergy savings can be realized which can enhance the  
24 earning strength of a company after an acquisition  
25 relative to what it would be before the acquisition. So

1 an earnings growth number can reflect both ongoing  
2 earnings growth opportunities for the companies and also  
3 nonrecurring synergy savings outlooks for the companies  
4 which could temporarily skew the three to five-year  
5 growth outlooks for that company.

6 So those are the general guidelines, which  
7 leads me to believe it's appropriate to exclude  
8 companies that are currently involved in merger and  
9 acquisition activities.

10 **Q Well, let me ask you this, Mr. Gorman. In**  
11 **your opinion, does the sale of the assets you cited**  
12 **affect the stock price of Nextera?**

13 A Well, I can't say for certain it does, but I  
14 can say that it likely has. And as a result, I felt it  
15 appropriate to exclude the company.

16 The issue isn't that I know it did; the issue  
17 is that it likely could. And if it likely could, then  
18 it's less likely that you're going to get an accurate  
19 measurement of what the stand-alone valuation and  
20 earnings strength and then required return will be on  
21 Nextel (sic.)

22 **Q You mean Nextera?**

23 A Nextera, yes. Thank you.

24 **Q All right. Can you please turn to page 39?**

25 A I'm there.

1           **Q     And it's line 24.**

2           A     I'm there.

3           **Q     Can you read aloud the sentence that begins**  
4 **"Hence, I am attempting."**

5           A     "Hence, I am attempting to determine whether  
6 the rate of return and cash flow generation opportunity  
7 reflected in my proposed rate of return for Gulf Power  
8 will support target investment grade bond ratings and  
9 Gulf Power's financial integrity."

10          **Q     Okay.**

11          A     I have read over to page 40.

12          **Q     Yes. What do you mean by "investment grade**  
13 **bond rating"?**

14          A     Bond ratings are characterized by a series of  
15 bond ratings which are considered to be investment grade  
16 bond ratings, and bond ratings at lower levels are  
17 considered to be non-investment grade bond ratings.

18                 An investment grade bond rating from a rating  
19 agency such as Standard & Poor's and Fitch would include  
20 bond ratings of BBB minus and higher. Higher bond  
21 ratings would be BBB plus, BBB, single A with a plus and  
22 minus designation, AA, and AAA. Below investment grade  
23 bond ratings would be bond ratings of lower than BBB,  
24 which range from a BB bond rating with plus or minus  
25 designations down to a D, which is a default credit

1 rating.

2 **Q Okay.**

3 A It would range from BB, single B, C, down to D  
4 level.

5 **Q And what do you mean by "Gulf Power's**  
6 **financial integrity"?**

7 A Gulf Power's ability to maintain adequate  
8 credit standing such that it will allow it to --  
9 preserve its ability to attract capital under reasonable  
10 terms and prices.

11 **Q Okay. On page 13 of your testimony --**

12 A I'm there.

13 **Q -- you cite the Supreme Court decision, the**  
14 **Hope and Bluefield decision, correct?**

15 A Yes.

16 **Q On line ten of page 13, the first thing that**  
17 **you cite states "be sufficient to maintain financial**  
18 **integrity"; is this correct? Did I read that correct?**

19 A Yes, you did.

20 **Q Is it fair to say that in your analysis, you**  
21 **are not attempting to determine whether the return on**  
22 **equity you are recommending will maintain Gulf Power's**  
23 **current bond rating but rather an investment grade bond**  
24 **rating?**

25 A I'm sorry, can you repeat that question?

1           Q     Would you agree with me that in your analysis,  
2 you are not attempting to determine whether the return  
3 on equity you are recommending will maintain Gulf  
4 Power's current bond rating but rather an investment  
5 grade bond rating?

6           A     Well, no. I'm using investment grade bond  
7 rating metrics, but I'm determining whether or not I  
8 believe that the financial metrics will support Gulf  
9 Power's current bond rating. Gulf Power's current bond  
10 rating is above the minimum investment grade bond  
11 rating.

12          Q     Okay. On page seven of your testimony, lines  
13 20 through 21.

14          A     I'm there.

15          Q     You state that "Gulf Power currently has an A  
16 corporate bond rating from S&P and Fitch and an A3 bond  
17 rating from Moody's"; is that correct?

18          A     Yes.

19          Q     On page 41 of your direct testimony, lines 12  
20 through 14.

21          A     I'm there.

22          Q     You recommended return on equity and Gulf  
23 Power's -- you state that using your recommended return  
24 on equity and Gulf Power's proposed capital structure,  
25 the company's financial credit metrics are supportive of

1 **its current BBB utility bond rating; is that correct?**

2 A It is. But that is a typographical error,  
3 that is not what I intended to do.

4 **Q What was your intent?**

5 A To reference their current bond rating, a  
6 single A. I think somehow I got crossed up with the  
7 proxy group's BBB bond rating there. But that should  
8 say, "maintain Gulf Power's single A bond rating from  
9 Standard & Poor's.

10 **Q So let me have you on page 41, the first**  
11 **paragraph, line seven, the sentence "The FFO/total debt**  
12 **ratio will support an investment grade bond rating." Do**  
13 **you see that?**

14 A Yes.

15 **Q Let me ask you -- I'm having problems with**  
16 **that. Is investment -- does an investment grade bond**  
17 **rating mean a bond rating?**

18 A Well, investment grade bond rating means a BBB  
19 or stronger bond rating.

20 **Q So in that sentence, does the investment grade**  
21 **bond rating mean A?**

22 A Well, see, the standard -- can I give an  
23 explanation --

24 **Q Sure.**

25 A -- to maybe help this?

1           **Q     Sure.**

2           A     Standard & Poor's used to have a very detailed  
3 matrix of credit rating metrics that assigned business  
4 risk and bond ratings designated as BBB, A, and AA.  
5 They have modified their credit metrics calculations  
6 about five years or so ago to eliminate the transparency  
7 they have for assigning metric ranges that correspond  
8 with specific bond ratings given levels of business risk  
9 profile scores made by Standard & Poor's.

10                     So unfortunately when they did that, it's not  
11 as direct to be able to state that the credit metrics at  
12 this range with this business risk corresponds with  
13 either a BBB or a single A bond rating because the  
14 metrics themselves simply are not that transparent any  
15 longer.

16                     But the metrics can be used to determine  
17 whether or not the rate of return and other costs of  
18 service components in the rate filing generally produce  
19 a credit metrics which are generally indicative of  
20 investment grade bond ratings by Standard & Poor's. So  
21 with that test, I used that to determine not only does  
22 my recommended return on equity represent fair  
23 compensation in today's capital market environment, but  
24 it also appears to be generally consistent with  
25 producing credit metrics which will maintain the

1 utility's current investment grade bond rating.

2 Because Standard & Poor's changed their  
3 methodology, that's about as close as I can get to  
4 showing that my rate of return will maintain the single  
5 A bond rating versus maintain credit metrics that are  
6 consistent with maintaining investment grade bond  
7 ratings, which includes Gulf Power's current single A  
8 bond rating.

9 **Q Okay. Can you turn to page 40, the beginning**  
10 **of page 40 of your direct testimony?**

11 A I'm there.

12 **Q The question on line 22 says -- on line 22 you**  
13 **describe the results of your calculation using S&P**  
14 **financial credit metric criteria for Gulf Power,**  
15 **correct?**

16 A Yes.

17 **Q On page 42 of your direct testimony, lines**  
18 **four through seven, you concluded that an authorized**  
19 **return on equity of 9.75 will support internal cash flow**  
20 **that will be adequate to maintain Gulf Power's current**  
21 **investment grade bond rating; is this correct?**

22 A Yes.

23 **Q So it is your testimony that an authorized ROE**  
24 **of 9.75 will allow Gulf Power to maintain its current**  
25 **S&P credit rating of A?**

1           A     Yes.  But based on that credit metric test  
2 where you are comparing the credit metrics for Gulf  
3 Power's regulated cost of service and the credit metric  
4 benchmarks published by Standard & Poor's, which don't  
5 clearly delineate business risks and credit ratings and  
6 the related credit metrics associated with those two.

7                     But generally the credit metrics produced at  
8 my recommended rate of return fit within the investment  
9 grade guidelines published by Standard & Poor's and  
10 therefore I believe that they are generally consistent  
11 with supporting Gulf Power's current investment grade  
12 bond rating.

13           **Q     And does that include an A bond rating?**

14           A     It does.

15           **Q     Looking at your DCF model, page 17,**  
16 **specifically line three, can you take a minute to read**  
17 **that sentence to yourself?**

18           A     Okay, I've read it.

19           **Q     Okay.  You said, "As shown in equation two**  
20 **above, the DCF model requires a current stock price,**  
21 **expected dividends, and expected growth rate in**  
22 **dividends"; is this correct?**

23           A     Yes.

24           **Q     Keep it on page 17 of your direct examination,**  
25 **lines 20 through 24, you state that the adjusted -- that**

1 you adjusted the dividends in your DCF model for next  
2 year's growth; is this correct?

3 A Yes.

4 Q Can you please explain the adjustment to which  
5 you refer to?

6 A Well, I took the last dividend paid and  
7 adjusted for the level of dividend expected to be paid  
8 in the following period. So that was done by taking the  
9 most recently quarterly paid dividend and adjusting it  
10 by the growth rate to convert it to an expected dividend  
11 in the following 12 months.

12 Q On page 18, line 14, you state that "For my  
13 constant growth DCF analysis, I have relied on the  
14 consensus, or means, of professional security analysts'  
15 earning growth estimates as a proxy for investor  
16 consensus dividend growth expectations"; is this  
17 correct?

18 A Yes.

19 Q Why do you rely on the forecasts of earning  
20 growth when you state that DCF analysis requires  
21 expected dividend growth?

22 A Well, I do that under the constant growth DCF  
23 model. Under the constant growth DCF model, from a  
24 mathematical standpoint, the growth and earnings has to  
25 equal the growth in dividends, which has to equal the

1 growth in book value. If the growth rate for all three  
2 of those factors is not the same, then the constant  
3 growth DCF model is not applicable.

4           And that's a concern I have, as discussed at  
5 the end of this constant growth equation because I  
6 believe that earnings growth is abnormally high, which  
7 will retract a lower sustainable level later on. But  
8 for purposes of my constant growth model, the  
9 mathematical requirement is to assume that earnings,  
10 dividends, and book value all grow at the same rate. So  
11 if earnings is projected to grow at a certain rate, then  
12 dividends and book value would have to grow at that same  
13 rate.

14           **Q    Are all utility earnings paid out as dividends**  
15 **when they are earned?**

16           A    All utilities that pay out dividends pay them  
17 out from earnings. And if the payout ratio stays the  
18 same, which it would have to if earnings, dividends, and  
19 book value all grow at the same rate, it's a  
20 mathematical fact, it would have to be the same, then  
21 earnings and dividends would grow at the same rate.

22           **Q    Okay. Are there any sources of expected**  
23 **dividends such as Value Line?**

24           A    Value Line does have dividend growth  
25 projections out over the next three to five years.

1 There are no sources of consensus dividend growth  
2 projections. But Value Line is a single analyst  
3 projection and it does project dividend growth.

4 **Q Okay. On page 19 of your testimony, lines 16**  
5 **through 17, you state that "The three to five-year**  
6 **growth rate exceeds the long-term sustainability growth**  
7 **rate as required by constant growth DCF model"; is this**  
8 **correct?**

9 A Yes.

10 **Q What part of the DCF model requires a limit on**  
11 **long-term sustainability growth?**

12 A What part of the model?

13 **Q Yes.**

14 A Well, it's part of the mathematical  
15 construction of the model. The DCF model was originally  
16 designed to value a stock, so the model is designed to  
17 reflect the investment horizon of the security, which in  
18 the case of the stock is an indefinite investment  
19 horizon. So the growth rate that is used in a constant  
20 growth DCF model has to correspond with the investment  
21 horizon. And with respect to common stock, that's an  
22 indefinite period of time.

23 The reason it's indefinite is unlike a stock  
24 or unlike a bond investment which may have a ten or  
25 20-year maturity period, common stock will stay

1 outstanding until the company repurchases the stock or  
2 the company goes bankrupt, so it's considered an  
3 indefinite investment horizon.

4 **Q Okay. Can you please turn to page 16?**

5 A I'm there.

6 **Q Looking at the equation two on line 15, isn't**  
7 **the only limit on growth in the DCF model that requires**  
8 **the return exceed the growth rate; that is, that K is**  
9 **greater than G?**

10 A Well, no, not if you're trying to -- not if  
11 you accept the premise that it's an efficient  
12 marketplace and investors make rational investment  
13 decisions. And under an efficient market, investors  
14 would look for realistic, achievable growth outlooks for  
15 a company and would only value the company stock based  
16 on what that growth outlook is.

17 You know, from a simple mathematical  
18 standpoint, I agree that  $G$  cannot exceed  $K$ ; otherwise,  
19 there would be negative yield. And that's not a  
20 plausible assumption in this model.  $K$  can equal  $G$  if  $G$   
21 is the only return expected by investors. But  $G$  itself  
22 has to reflect realistic, rational outlooks; otherwise,  
23 you're making the assumption that the market is not  
24 efficient and investors are not making rational  
25 investment decisions.

1           So, no, there is more limitations. The  
2 limitation is is the growth has to be a rational outlook  
3 for future growth of the company.

4           **Q     On page 21 -- rather on page -- if you look on**  
5 **page 22, at the end of page 22, line 21.**

6           A     Okay.

7           **Q     And the quote -- and continuing on page -- you**  
8 **can look on page 20, go to page -- and it continues on**  
9 **page 21. You cite Brigham and Houston --**

10          A     Right.

11          **Q     -- from the financial text, correct?**

12          A     Yes.

13          **Q     That quote states that "The mature firms are**  
14 **often expected to grow in the future at about the same**  
15 **rate as a nominal GDP"; is that correct?**

16          A     Yes.

17          **Q     Would you agree that the quote does not say**  
18 **that it is impossible for a firm to grow at a rate above**  
19 **nominal GDP for an extended period of time?**

20          A     For an extended period of time I agree, but  
21 not for an indefinite period of time. And that's the  
22 distinction you have to make when you're using the  
23 constant growth DCF model, is the growth rate has to be  
24 in effect for an indefinite period of time, not just an  
25 extended period of time, but indefinitely. And if that

1 growth rate does not reflect a reasonable assessment of  
2 indefinite growth, then it's skewing the results of the  
3 DCF model. And that's consistent with the author's  
4 presentation and Morningstar's market participant  
5 outlook.

6 **Q On page 20, line eight.**

7 A I'm there.

8 **Q You state "Utilities cannot sustain**  
9 **indefinitely a growth rate that exceeds the growth rate**  
10 **of their overall economy"; is this correct?**

11 A Yes, indefinitely, yes.

12 **Q Okay. How many years does indefinitely**  
13 **entail?**

14 A Well, I mean, I can't narrow it down but, I  
15 mean, from a mathematical standpoint, I've looked at  
16 that with respect to water utilities and from that  
17 analysis I estimate that the higher growth can be  
18 sustained for roughly a ten-year period even if there's  
19 a sustained high level of capital improvement and growth  
20 to rate base. So that's one study I've done that  
21 suggests that a ten-year period is an appropriate period  
22 reflecting abnormally high growth.

23 I can explain that if you would like. But  
24 from the studies I've done, I think ten years is a  
25 reasonable period for expecting abnormally high growth,

1 and that's the period used in my multi-growth state DCF  
2 study.

3 **Q One second, please.**

4 **Let me ask you this question. Would you agree**  
5 **then that it is possible for a company to grow at a rate**  
6 **greater than nominal GDP for 100 years and not violate**  
7 **your statement that utilities cannot sustain**  
8 **indefinitely a growth rate that exceeds the growth rate**  
9 **of the overall economy"?**

10 A Based on the studies I've done, I think that's  
11 an unrealistic outlook. I would not agree with that.

12 **Q But it's not mathematically impossible,**  
13 **correct?**

14 A It's not mathematically impossible, but it is  
15 highly unlikely and in my view an irrational outlook.

16 **Q All right. Do you know if during any period**  
17 **in the past the earnings of the electric utilities in**  
18 **Florida have grown at a rate greater than the national**  
19 **GDP?**

20 A I think there have been periods where Florida  
21 utilities and utilities outside of Florida that have  
22 grown above the real GDP, but that's a relatively short  
23 period of time.

24 **Q Over the past ten years?**

25 A It's possible. I mean, Value Line tracks

1 that.

2           Would you like me to specifically comment on  
3 that? I haven't looked at that today, but it is  
4 referenced in the Value Line documents.

5           **Q     Okay. No, you don't have to comment on that.**

6           A     Okay.

7           **Q     Over the past 20 years or 30 years?**

8           A     Are you asking me has growth exceeded GDP?

9           **Q     Yes.**

10          A     I mean, I didn't specifically look at that in  
11 the last ten years, but I offered to, so I haven't  
12 looked at it in 20 or 30-year periods either.

13          **Q     Okay.**

14          A     I mean, I'm happy to look at that because  
15 based on the industry in general, I've looked at it, and  
16 I know that that is not an accurate statement. And that  
17 includes a period where rate base had accelerated growth  
18 during the 1980s when nuclear plants were being  
19 developed and rate base was growing by substantial  
20 measures followed by a period in the '90s where  
21 investment was relatively mild and growth rates were  
22 relatively low and largely in part because utilities  
23 were gearing up for possible deregulation and they  
24 didn't want to put money into regulated assets because  
25 they weren't sure whether or not they would become

1 stranded assets in a deregulated transition from  
2 regulated to competition marketplace.

3 After the concern about the deregulation of  
4 the industry started to abate in the early 2000 time  
5 frame, the utilities started investing in utility plant  
6 again. So I know there's been pretty significant swings  
7 in growth from high to low over the last 30 to 40 years.  
8 But on an industry basis, earnings have not exceeded the  
9 growth rate of GDP; in fact, they have trailed the  
10 growth rate of GDP.

11 But I have not looked at that specifically for  
12 Florida utilities. But I would also note that my proxy  
13 group isn't limited to Florida utilities; it's limited  
14 to the proxy group.

15 **Q Do you expect the earnings of electric**  
16 **utilities in Florida to grow at a rate greater than the**  
17 **nominal GDP, the national GDP?**

18 A If they have periods of accelerated rate based  
19 growth, then their earnings growth rates likely will  
20 exceed GDP growth during relatively short periods of  
21 time. And by that I mean five to ten-year periods.

22 **Q Okay.**

23 A The reason I think it's limited to that is  
24 because even with accelerated capital spend programs,  
25 that growth and rate based will slow over time. And

1 that happens if you simply consider the mathematical  
2 development of a growth rate.

3 You know, if you have \$1,000 rate base and  
4 you're adding \$100 to it, then the first year you have a  
5 10 percent growth in your rate base. If that \$100  
6 capital improvement continues for ten years, then your  
7 rate base grows from \$1,000 to 2,000 over that time  
8 period. And with a continued large capital improvement  
9 program of \$100, the growth rate would decline from  
10 10 percent down to 5 percent in ten years.

11 There's limits on growth and rate base because  
12 the utility only has the manpower and the capital  
13 resources to support a capital program of a certain size  
14 so the utility's capital program can't grow indefinitely  
15 because they don't have the human resources or access to  
16 capital to support a continuously growing capital  
17 program. So it can sustain a high level of capital  
18 improvements which can grow its rate base largely over  
19 time, but the percent growth will decline as embedded  
20 rate base grows over time.

21 **Q On page 20 of your direct testimony, lines 18**  
22 **through 19, you state that "GDP growth rate is a**  
23 **conservative proxy for the highest sustainable long-term**  
24 **growth rate of a utility"; Is this correct?**

25 A Yes.

1           **Q     Do you know of any regulatory agency or**  
2 **agencies that use the GDP growth rate as a proxy for**  
3 **growth rate in the DCF model to determine the ROE for**  
4 **electric utility?**

5           A     Well, yes and no. Regulatory commissions have  
6 recognized the nonconstant growth, nature of growth for  
7 utility companies and have recognized the need for a  
8 multi-growth stage model and those commissions have  
9 adopted recommendations by me and staff witnesses in  
10 other jurisdictions that the maximum sustainable growth  
11 rate is proxied by the GDP. Those commissions include  
12 the Illinois Commission, the Missouri Commission, and  
13 the Washington Commission.

14                 They don't explicitly use GDP growth, but they  
15 use it as a proxy to get a sense of what the maximum  
16 sustainable growth rate for a utility company can be.  
17 So from that standpoint, it is a parameter that is some  
18 acceptance by regulatory commissions, but it's  
19 indirectly. It's embedded in the expert witness's  
20 construction of a nonconstant growth DCF model. It's  
21 not an explicit finding by the commission.

22           **Q     Okay. On page 33, lines ten through 12, you**  
23 **state that you use Blue Chip Financial Forecasts'**  
24 **projected 30-year Treasury bond yield of 4.2 percent for**  
25 **your CAPM analysis; is this correct?**

1 A Yes.

2 Q Can you please turn to page 37 of your direct  
3 testimony, lines six through seven. You state that your  
4 CAPM analysis produces a return of 8.82 percent; is this  
5 correct?

6 A Yes.

7 Q And on line eight, you state that you are  
8 concerned with a lower estimate produced by your CAPM  
9 analysis; is this correct?

10 A Yes.

11 Q Do you know what Blue Chip's current forecast  
12 is for the 30-year Treasury bond yield?

13 A 3.8 percent, so it's gone down.

14 Q Would you agree, subject to check, that if you  
15 were to use the up-to-date 30-year Treasury bond yield  
16 of 3.8 percent in your CAPM analysis, it would produce a  
17 return below 8.82 percent?

18 A Well, yeah, if you hold all of the other  
19 factors constant, yes, I would accept that subject to  
20 check.

21 Q Would you still stand by the results of your  
22 CAPM analysis if the return produced -- if the return it  
23 produced was below 8.82 percent using the most current  
24 information?

25 A Well, I would have the same concern then that

1 I have now, that I'm recommending that the Commission  
2 not act too quickly to reduce the authorized return on  
3 equity. That's why I gave minimal weight to the results  
4 of the CAPM in this study. The CAPM went down even  
5 further because of a decline in Treasury bond yields.

6 I would have the same recommendation. I would  
7 show the Commission what the result is, but I would have  
8 the same recommendation that the ROE should be based  
9 predominantly on the DCF and risk premium studies.

10 **Q Okay. So in your opinion, should the**  
11 **Commission rely on the most current information that is**  
12 **available at the time it makes a decision in this case?**

13 A Yes, it should. But, you know, consistent  
14 with my testimony, I think the Commission needs to be a  
15 little conservative in recommending a return which is  
16 fair because if the authorized return on equity is  
17 decreased too fast, then there could be problems with  
18 the utility's ability to maintain credit metrics to  
19 maintain its financial integrity.

20 And I tried to recognize all of those factors  
21 in recommending a point estimate which I believe is a  
22 reasonable estimate of fair compensation in today's low  
23 cost capital market but also is a return which will help  
24 support the utility's ability to maintain its investment  
25 grade bond rating.

1           Q     All right. On page 34 of your direct  
2 testimony, lines four through six.

3           A     I'm there.

4           Q     You state that "For companies with betas less  
5 than 1.0 using the Treasury bond yield as a proxy for  
6 the risk-free rate in the CAPM analysis can produce an  
7 overstated estimated CAPM return"; is this correct?

8           A     Yes.

9           Q     Have you read Dr. Vander Weide's direct  
10 testimony in this case?

11          A     Yes.

12          Q     Are you aware that in his direct testimony,  
13 Dr. Vander Weide states that the historical CAPM tends  
14 to underestimate the cost of equity for companies whose  
15 beta is less than one?

16          A     I have read that.

17          Q     Would you please explain the apparent  
18 contradiction in your testimony with Dr. Vander Weide's  
19 regarding the results of the CAPM analysis for companies  
20 with betas less than one?

21          A     Well, Dr. Vander Weide's analysis, I think,  
22 fails to recognize that Value Line adjusts its betas  
23 just to correct for this potential underestimation of  
24 required returns for lower -- for companies with risks  
25 below market.

1 Value Line takes out raw data estimates and it  
2 adjusts it for a forward look and tendency to converge  
3 on the market beta of one. So the measured beta from  
4 the regression statistic Value Line completes is  
5 increased for companies with betas lower than one to  
6 move it closer to the market beta of one.

7 Had it not done that, then I would agree with  
8 Dr. Vander Weide that below-market betas would have a  
9 tendency to understate CAPM return estimates. But that  
10 beta adjustment made by Value Line is designed  
11 specifically to correct for that underestimation bias.

12 So I disagree with his conclusions if you're  
13 using Value Line adjusted betas. However, in this  
14 instance, I have concerns with the results of the CAPM  
15 being used to support my authorized return on equity.

16 **Q In your direct testimony, page two.**

17 A Okay.

18 **Q One second, please. On page two you**  
19 **recommended an adjustment to Gulf's regulatory capital**  
20 **structure based on an adjustment to the deferred tax**  
21 **balance; is this correct?**

22 A Yes.

23 **Q In your direct testimony, page 11, you further**  
24 **state that as discussed in your testimony -- as**  
25 **discussed in the testimony of Meyer, of Greg R. Meyer,**

1 you could not verify the total company amount of  
2 accumulated deferred income tax -- excuse me, I got  
3 confused with that -- accumulated deferred income tax  
4 and therefore recommend to include 536.6 million rather  
5 than 492.1 million in the company's filing; is this  
6 correct?

7 A Yes.

8 Q In addition, on page 11 of your direct  
9 testimony, you said that FEA would consider to remove  
10 the proposed capital structure adjustment provided that  
11 the company explains the difference between the  
12 492.1 million shown on schedule 12 and the 13-month  
13 average balance of accumulated deferred income tax  
14 obtained from Gulf's MFR Schedule B3; is this correct?

15 A Yes.

16 Q Can you please refer to McMillan's -- do you  
17 have witness McMillan's rebuttal testimony in front of  
18 you?

19 A Not in front of me, I do not, no. I do know  
20 that he attempted to answer the questions, and we're  
21 reviewing his response now. And I'm not prepared to  
22 answer whether or not I think he has adequately  
23 explained this difference.

24 Q All right. Thank you. I have no further  
25 questions.

1 MR. MELSON: Gulf has no questions.

2 MR. YOUNG: Ms. White.

3 (No response.)

4 MR. YOUNG: Ms. White.

5 MS. WHITE: I'm here. Sorry, my BlackBerry  
6 just locked up on me. I do not have any questions,  
7 I mean, any redirect for Mr. Gorman.

8 MR. YOUNG: Okay. With that, would you like  
9 to read.

10 MS. WHITE: I'm sorry?

11 MR. YOUNG: Would you like to read? Would you  
12 want Mr. Gorman to read his deposition and make any  
13 corrections he may have?

14 MS. WHITE: Yeah, I would imagine that  
15 Mr. Gorman would like to read over it to make sure  
16 that there's no corrections.

17 Is that fair, Mike?

18 THE WITNESS: Yes.

19 MR. YOUNG: All right. With that, I thank you  
20 all. I don't think that there's anything else.

21 (Whereupon, proceedings were concluded at  
22 10:35 a.m.)

23

24

25

## 1 CERTIFICATE OF REPORTER

2  
3 STATE OF FLORIDA )  
4 COUNTY OF LEON )5 I, MICHELLE SUBIA, Registered Professional  
6 Reporter, certify that the foregoing proceedings were  
7 taken before me at the time and place therein  
8 designated; that my shorthand notes were thereafter  
9 translated under my supervision; and the foregoing  
10 pages, numbered 4 through 37, are a true and correct  
11 record of the aforesaid proceedings.  
1213 I further certify that I am not a relative,  
14 employee, attorney or counsel of any of the parties, nor  
15 am I a relative or employee of any of the parties'  
16 attorney or counsel connected with the action, nor am I  
17 financially interested in the action.18 DATED this 5th day of December, 2011.  
1920 21 \_\_\_\_\_  
22 MICHELLE SUBIA  
23 NOTARY PUBLIC  
24 COMMISSION #DD987077  
25 EXPIRES JUNE 7, 2014

1 I have read the transcript of my deposition, pages 4  
2 through 37 and hereby subscribe to same, including any  
3 corrections and/or amendments listed below.

4 DATE: \_\_\_\_\_

MICHAEL P. GORMAN

5 (In Re: Petition for increase/Gulf Power

6 PAGE/LINE	CORRECTION/AMENDMENT	REASON FOR CHANGE
7	_____	_____
8	_____	_____
9	_____	_____
10	_____	_____
11	_____	_____
12	_____	_____
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20	_____	_____
21	_____	_____
22	_____	_____

23 DATE OF DEPOSITION: 12/2/2011 REPORTER: MICHELLE SUBIA

24

25

1 PREMIER REPORTING  
2 114 W. 5th Avenue  
3 Tallahassee, FL 32303  
4 (850) 894-0828

5 December 6th, 2011

6 TO: KAREN WHITE, ESQ.

7 RE: Petition for increase/Gulf Power

8 Dear Ms. White,

9 Enclosed please find your copy of the deposition of  
10 MICHAEL P. GORMAN taken on December 2nd, 2011, in the  
11 above-styled case.

12 As the witness did not waive reading and signing, I am  
13 also attaching the errata sheet as the last page of the  
14 transcript and request that your office make the  
15 necessary arrangements with your witness to read your  
16 copy of the deposition, noting any corrections on the  
17 errata sheet, then dating and signing the errata sheet,  
18 within 30 days or before commencement of trial,  
19 whichever is first.

20 PLEASE FORWARD THE ORIGINAL, SIGNED AND DATED errata  
21 sheet to KEINO YOUNG. If the errata sheet or a request  
22 for an extension is not received within 30 days, Counsel  
23 may assume that the signature has been waived.

24 It was a pleasure working with you on this matter.

25 Sincerely yours,



MICHELLE SUBIA

Registered Professional Reporter

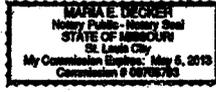
Enclosures (Errata sheet and transcript.)

**CERTIFICATE OF OATH**

STATE OF MISSOURI            )  
  )     SS  
COUNTY OF SAINT LOUIS    )

I, the undersigned authority, certify that Michael P. Gorman personally appeared before me at 16690 Swingley Ridge Road, Suite 140, Chesterfield, Missouri 63017 and was duly sworn by me to tell the truth.

WITNESS my hand and official seal in the City of Chesterfield, County of St. Louis, State of Missouri, this 2nd day of December, 2011.



*Maria E. Decker*  
Notary Public  
State of Missouri

Personally known   X   OR produced identification \_\_\_\_\_  
Type of identification produced \_\_\_\_\_