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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Petition for rate increase by Gulf Power Company	DOCKET NO. 160186-EI
In Re: Petition for approval of 2016 approval of proposed depreciation rates and annual dismantlement accruals and Plant Smith Units 1 and 2 regulatory asset amortization, by Gulf Power Company.	DOCKET NO. 160170-EI FILED February 21, 2017

PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL

The Citizens of the State of Florida, through the Office of Public Counsel (OPC), pursuant to the Order Establishing Procedure in these dockets, Order No. PSC-16-0473-PCO-EI, issued October 20, 2016, hereby submit this Prehearing Statement.

APPEARANCES:

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On behalf of the Citizens of the State of Florida

1. WITNESSES: ISSUES

WITNESSES	ISSUES
James R. Dauphinais	19, 20
Roxie McCullar	8, 9, 10, 11, 13, 18, 29, 74
Donna Ramas	1, 6, 19, 22, 23, 26, 27, 28, 29, 30, 31, 32, 33. 35, 36, 37, 38, 52, 53, 59, 60, 61, 63, 64, 68, 72, 73, 75, 78, 79 80, 82
J. Randall Woolridge	39, 40, 41, 42, 43, 44, 45, 46, 47

2. EXHIBITS:

Through the above mentioned witnesses, the Citizens intend to introduce the following exhibits:

Witness	**Exhibits**	**Title**
James R. Dauphinais	JRD-1	Composite Exhibit Discovery Responses
Roxie McCullar	RMM-1	Proposed Depreciation Rates and Annual Accrual
Roxie McCullar	RMM-2	Impact on Revenue Requirement
Roxie McCullar	RMM-3	Remaining Life for Account 365.00
Roxie McCullar	RMM-4	Remaining Life for Account 369.10
Roxie McCullar	RMM-5	Pages 2-4 of Appendix E-1 to Depreciation Rate Study
Roxie McCullar	RMM-6	Corrected IRR Calculation for Accounts 312, 314, and 315
Roxie McCullar	RMM-7	Pages 11 and 12 of Appendix E-2 to Depreciation Rate Study
Roxie McCullar	RMM-8	Schedule C-29 from Docket No. 110138-EI
Roxie McCullar	RMM-9	Selected Pages from 2008 Q4 FERC Form No. 1
Roxie McCullar	RMM-10	Corrected Net Salvage for Account 390
Roxie McCullar	RMM-11	Selected Pages from Public Utility Depreciation Practices
Roxie McCullar	RMM-12	FERC USOA Sections Referenced
Roxie McCullar	RMM-13	Discovery Responses Referenced
Donna Ramas	DMR-1	Qualifications of Donna Ramas
Donna Ramas	DMR-2	OPC Revenue Requirement Exhibits
Donna Ramas	DMR-3	Composite Exhibit: Discovery and Other References

Witness	Exhibits	Title
J. Randall Woolridge	JRW-1	Recommended Cost of Capital
J. Randall Woolridge	JRW-2	Interest Rates
J. Randall Woolridge	JRW-3	Public Utility Bond Yields
J. Randall Woolridge	JRW-4	Summary Financial Statistics for Proxy Groups
J. Randall Woolridge	JRW-5	Capital Structure Ratios and Debt Cost Rates
J. Randall Woolridge	JRW-6	The Relationship Between Estimated ROE and Market-to-Book Ratios
J. Randall Woolridge	JRW-7	Utility Capital Cost Indicators
J. Randall Woolridge	JRW-8	Industry Average Betas
J. Randall Woolridge	JRW-9	DCF Model
J. Randall Woolridge	JRW-10	DCF Study
J. Randall Woolridge	JRW-11	CAPM Study
J. Randall Woolridge	JRW-12	Gulf Power's Proposed Cost of Capital
J. Randall Woolridge	JRW-13	Gulf Power Company's ROE Results
J. Randall Woolridge	JRW-14	GDP and S&P 500 Growth Rates

3. STATEMENT OF BASIC POSITION

Gulf Power Company's $107 million rate increase request is unwarranted. Instead of the rate increase Gulf asks for, a rate decrease of at least $2,087,000 should be approved. Gulf's request is inflated due, among other things, to an unrealistic cost of equity, an artificially swollen equity ratio, phantom budgeted employment positions, excessive bonuses, unjustified affiliate transactions with its parent company and excessive land and storm repair costs, in addition to other excessive and unsupported costs. In addition, Gulf is asking the Commission to let it put a 30 year-old coal plant in retail rate base after its shareholders had wrung out all of the profit from it in the wholesale market place since it was acquired but never needed for retail rates. The Commission should hold Gulf to its burden of proof and find that the requested rate increase is

unwarranted and order a reduction in rates.

4. STATEMENT OF FACTUAL ISSUES AND POSITIONS

Legal/Threshold Issues

New Issue (OPC): **In the event federal legislation is passed and signed into law between now and a reasonable period after new base rates become effective that results in a change in the corporate income tax rate to which Gulf is subject, or changes in the depreciation allowance for tax purposes associated with plant additions incorporated in test year rate base, what adjustments or provisions, if any, should the Commission make to address such changes? Should the Order in this case require a limited reopening within a reasonable period after new base rates become effective to address income tax expense as well as the accumulated deferred income taxes in the capital structure in the event such legislation is passed that would impact Gulf's revenue requirements?**

OPC: Yes. The new administration in Washington, D.C. has indicated that it will seek to lower the corporate income tax rate in 2017. While this change in law has not occurred, given that the same party controls the Congress and White House, it is enough of a distinct possibility that it should be given strong consideration in the rate setting process. A ten basis point reduction in the Federal Income Tax rate translates to an estimated $13.9 million reduction in retail revenue requirements proposed by Gulf. This $13.9 million estimate does not include the impact of returning excess deferred taxes currently reflected in Gulf's ADIT balance back to customers. Gulf asks for the Commission to determine the revenue requirements based on a 35% statutory tax rate. Gulf has the burden of demonstrating its entitlement to cost recovery of each element of its rate relief request. Given the credible statements from highly placed officials about prioritizing a change in the corporate tax rate, Gulf shoulders the burden to give the Commission adequate assurances that customers' rates will not be established based on income tax expense that is overstated. Furthermore and to avoid creating a windfall for Gulf's shareholders, the Commission should impose safeguards in its ratemaking actions that isolate the discrete federal (and piggy-backed state) income tax expense effects from offsets due to normal fluctuations in the cost of business. The Commission should establish a reasonable period after its order in this case becomes final over

which it retains jurisdiction to adjust customer rates based on any material change in the tax laws. Any tax rate adjustment mechanism should be a combination of one time refunds and prospective adjustment in customer rates, as circumstances warrant relative to the effective date of such tax law changes.

<u>ISSUE 1:</u> **Should the Commission address Gulf's requests related to electric vehicle charging stations in this case (Issue 13 and Issue 22)?**

OPC: At this time the OPC believes that, given the novel and nascent aspect of this issue, the Commission does not have enough information to establish a policy regarding the final, appropriate accounting and regulatory treatment of the EVCS (electric vehicle charging stations). OPC witness Ramas has removed the impact of the EVCS from the filing. OPC supports this approach. However, to the extent that Gulf effectively imputes up to the minimum revenue requirement of the EVCS (in the event the customer base does not materialize) to insulate the general body of ratepayers from risks of the un-tested approach to the product, while recognizing any revenues that exceed the costs in both the setting of rates and in the surveillance process, the OPC would not object to such a modified approach. (Ramas)

<u>Test Year Period and Forecasting</u>

<u>ISSUE 2</u>: **Is Gulf's projected test year period of the 12 months ending December 31, 2017 appropriate?**

OPC: Gulf has the burden to demonstrate the correctness of its chosen test year and that it is reasonably representative of going-forward operations and circumstances. Gulf has not met its burden on this issue.

<u>ISSUE 3</u>: **Are Gulf's forecasts of Customers, kWh, and kW by rate class, for the 2017 projected test year appropriate? If not, what adjustments should be made?**

OPC: Gulf has the burden to demonstrate the correctness of its forecast and that it is reasonably representative of going-forward operations and circumstances. Gulf has not met its burden on this issue.

<u>ISSUE 4</u>: **Are Gulf's forecasts of billing determinants by rate schedule for the 2017 projected test year appropriate? If not, what adjustments should be made?**

OPC: Gulf has the burden to demonstrate the correctness of its billing determinants and that they are reasonably representative of going-forward operations and circumstances. Gulf has not met its burden on this issue.

<u>ISSUE 5</u>: **Are Gulf's estimated revenues from sales of electricity by rate class at present rates for the projected 2017 test year appropriate? If not, what adjustments should be made?**

OPC: Gulf has the burden to demonstrate the correctness of its estimated revenue from sales of electricity and that it is reasonably representative of going-forward operations and circumstances. Gulf has not met its burden on this issue.

<u>ISSUE 6</u>: **What are the appropriate inflation, customer growth, and other trend factors for use in forecasting the 2017 projected test year budget?**

OPC: Projected costs in the filing based on Gulf's 3.7% inflation factor should be adjusted to recognize the most recently provided inflation factor of 2.5%. A minimum adjustment to reduce O&M expense by $121,000 ($118,000 jurisdictional) should be made with the recognition that Gulf must demonstrate that only 3.2% of the 2017 forecasted O&M expense is based on inflation. A greater adjustment may be warranted if, and to the extent that, Gulf fails to meet this burden. (Ramas)

<u>Quality of Service</u>

<u>ISSUE 7</u>: **Is the quality and reliability of electric service provided by Gulf adequate?**

OPC: The Commission is still taking evidence from customers on the issue of customer service. Gulf's burden is to demonstrate that it provides adequate and reliable customer service at the lowest cost. At this point the OPC cannot take a position pending receipt of all customer comments and complaints and company responses to such.

Depreciation and Dismantlement

ISSUE 8: What are the appropriate capital recovery schedules?

OPC: The burden is on Gulf to show that its requested capital recovery schedules are reasonable and appropriate. To the extent that OPC witness McCullar did not address an issue, method, procedure, or other matters related to Gulf's proposals, it should not be construed that OPC is in agreement with Gulf's proposed issues, methods, or procedures. (McCullar)

ISSUE 9: What are the appropriate depreciation parameters (remaining life [including the production unit retirement date or life span and the interim retirement ratio for production plant accounts], net salvage percentage [including interim net salvage percent for production plant accounts], and reserve percentage) and resulting depreciation rates for each production unit and each production plant account?

OPC: The OPC proposed depreciation parameters and depreciation rates shown on Exhibit RMM-1 as WDA Proposed are appropriate for Gulf's production unit and production plant account. (McCullar)

ISSUE 10: What are the appropriate depreciation parameters (average service life, remaining life, net salvage percentage and reserve percentage) and resulting depreciation rates for each transmission, distribution, and general plant account?

OPC: The OPC proposed depreciation parameters and depreciation rates shown on Exhibit RMM-1 as WDA Proposed are appropriate for Gulf Power's transmission, distribution, and general plant accounts. (McCullar)

ISSUE 11: **Based on the application of the depreciation parameters that the Commission has deemed appropriate to GPC's data, and a comparison of the theoretical reserves to the book reserves, what are the resulting imbalances, if any?**

OPC: Based on the OPC proposed depreciation parameters and depreciation rates shown on Exhibit RMM-1 as WDA Proposed, there is a reserve deficiency of $175 million. ($1,472 million book reserve as of 12/31/2016 less $1,647 million theoretical reserve as of 12/31/2016 based on Exhibit RMM-1 proposed depreciation parameters and depreciation rates). (McCullar)

ISSUE 12: **What, if any, corrective depreciation reserve measures should be taken with respect to the imbalances identified in Issue 11?**

OPC: No position at this time.

ISSUE 13: **What is the appropriate depreciation rate for Gulf's electric vehicle charging stations?**

OPC: No position at this time.

ISSUE 14 : **What is the appropriate recovery period for the regulatory asset related to the retirement of Plant Smith Units 1 and 2 approved in Docket No. 160039-EI?**

OPC: The appropriate recovery period for the regulatory asset created by the early retirement of Plant Smith Units 1&2 is the remaining life of the asset indicated in the company's last depreciation study.

ISSUE 15: **What is the appropriate current total estimated cost of dismantling Gulf Power Company's generation fleet?**

OPC: No position at this time.

ISSUE 16: **What, if any, corrective dismantlement reserve allocations should be made?**

OPC: No position at this time.

ISSUE 17: **Based on the decisions in Issues 15 and 16, what is the appropriate annual accrual for dismantlement?**

OPC: No position at this time.

ISSUE 18: **What should be the implementation date for revised depreciation rates, capital recovery schedules, dismantlement accruals, and amortization schedules?**

OPC: July 1, 2017. (McCullar)

Rate Base

Issue 19: **Should the Commission allow recovery through retail rates of any portion of Scherer Unit 3? If so, what adjustments, if any, should be made to the treatment of Scherer Unit 3 in the Company's filing?**

OPC: No. For the reasons stated in the Direct Testimony of OPC Witness James Dauphinais, Gulf has not met its burden to demonstrate why the costs of its share of Scherer 3 should be included in the rates paid by its retail customers. The plant was not needed to serve retail load in Florida from the time Gulf entered into an agreement to own a 25% share of the unit. It has never been needed. In the ensuing 30-plus years, Gulf's shareholders profited from placing the unit into the wholesale market. Only when the coal plant became uneconomical in the wholesale market place did Gulf seek to thrust it upon retail customers who did not need it in the past and do not need it in the foreseeable future. Gulf has not met its burden to show that inclusion of the costs of Scherer Unit 3 are appropriately included in the retail cost of service for its customers. The $19 million base rate retail revenue requirement related to Scherer should be removed as shown in DMR-2 (Dauphinais, Ramas)

ISSUE 20: **Should costs currently approved by agreement and stipulation for recovery through the Environmental Cost Recovery Clause associated with Scherer Unit 3 be included in base rates for Gulf? If so, what adjustments, if any, should be made?**

OPC: No. See position on Issue 19. (Dauphinais)

ISSUE 21: **Are there any capital costs currently being recovered by Gulf through cost recovery clauses that should be moved from the cost recovery clauses to base rates? If so, what capital costs should be moved to base rates and what adjustments should be made, if any?**

OPC: No position at this time.

ISSUE 22: **What is the appropriate amount, if any, to include in Plant in Service for Gulf's electric vehicle charging stations?**

OPC: See position on Issue 1. OPC's primary position as stated in the testimony of witness Ramas is that the amount is $-0-. However, to the extent that Gulf holds customers' harmless while crediting the revenues equal to the cost in the overall revenue requirement, then the amount proposed by Gulf is acceptable. (Ramas)

ISSUE 23: **What is the appropriate amount of Plant in Service for Gulf's Transmission Capital Additions?**

OPC: No position at this time. See OPC's position on Issue 35 with regards to the deferred return on transmission investments regulatory asset. (Ramas)

<u>ISSUE 24</u>: **Has Gulf made the appropriate test year adjustments to remove from rate base costs recovered under the Environmental Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point, it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

<u>ISSUE 25</u>: **Has Gulf made the appropriate test year adjustments to remove from rate base costs recovered under the Energy Conservation Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

<u>ISSUE 26</u>: **Should the Commission allow recovery through rates of the costs associated with the proposed new Gulf Smart Energy Center? What adjustments, if any, should be made to the Gulf Smart Energy Center costs included in the 2017 projected test year?**

OPC: No. Gulf neither conducted a cost-benefit analysis or study relied upon in deciding to build the Smart Energy Center nor provided any evidence demonstrating that the costs of such a facility are cost-effective or reasonable. In rebuttal, Gulf has agreed to remove the Smart Energy Center from the 2017 test year as it decided not to construct the center during the test year. The updated impact on rate base to remove the Smart Energy Center provided in Gulf's rebuttal filing is a $3,181,000 reduction ($3,126,000 jurisdictional) and depreciation expenses should be reduced by $42,000 ($41,000 jurisdictional). (Ramas)

<u>ISSUE 27</u>: **Are Gulf's projected capital expenditures associated with maintenance outages for 2016 and 2017 appropriate? If not, what adjustments should be made?**

OPC: No. The 2016 maintenance capital expenditures are projected to be $7,053,551 ($6,857,000 jurisdictional) lower than the budgeted amount included in the filing. Test year plant in service should be reduced by this amount and corresponding

adjustments (reductions) made to depreciation expense for $280,407 ($272,000 jurisdictional) and accumulated depreciation for $140,204 ($136,000 jurisdictional). (Ramas)

ISSUE 28: **Is Gulf's requested level of Plant in Service for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, the amount should be no greater than $3,290,358,000. (Ramas)

ISSUE 29: **Is Gulf's requested level of Accumulated Depreciation for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, the amount should be no greater than $1,258,995,000. (McCullar, Ramas)

ISSUE 30: **Is Gulf's requested level of Construction Work in Progress for the 2017 projected test year appropriate? If not, what is the appropriate amount?**

OPC: No. After appropriate adjustments, the amount should be no greater than $34,410,000. (Ramas)

ISSUE 31: **Is Gulf's requested level of Property Held for Future Use for the 2017 projected test year, including the North Escambia site, appropriate? If not, what is the appropriate amount?**

OPC: No. After appropriate adjustments, including exclusion of the North Escambia site, the amount should be no greater than $1,666,000. The Commission has already disallowed this site from rate base. OPC witness Ramas recommends that the land included in PHFU be excluded from rate base. There are many additional sites already included in rate base that are available to be used to site future facilities. Gulf has not met its burden of demonstrating that, for this site which has been expressly disallowed, that it has actual plans to construct facilities on the North Escambia site to meet its forecasted 2023 energy needs. Nor has Gulf demonstrated

that the entire 2,728 acres it acquired for a future potential nuclear facility will be needed to fill its forecasted 2023 energy needs. The full $13,043,000 ($12,679,000 jurisdictional) of North Escambia land costs should be excluded from PHFU in rate base. (Ramas)

ISSUE 32: **Is Gulf's requested level of Property Held for Future Use for the 2017 projected test year appropriate? If not, what is the appropriate amount?**

OPC: No. After appropriate adjustments, including exclusion of the North Escambia site, the amount should be no greater than $1,666,000. See position on Issue 31. (Ramas)

ISSUE 33: **Should any adjustments be made to Gulf's fuel inventories for the projected 2017 test year?**

OPC: Yes. Gulf has included in-transit coal in its working capital request. The amount of in-transit coal included in Gulf's working capital request that is in excess of the target level should be disallowed for the reasons stated below. The amount of the McDuffie Coal Terminal inventory included in working capital should be reduced from the $19,826,081 incorporated in the Company's filing to $7,820,596, which is a reduction of $12,005,486 ($11,660,000 jurisdictional). The recommended balance of $7,820,596 is based on the average projected inventory cost provided in the Company's workpapers for the period August 2017 through December 2017. The recommended quantity associated with the $7,820,596 balance of 104,417 tons shown on Exhibit DMR-2 at Schedule B-4 is also consistent with Gulf's 10-burn day inventory target for the McDuffie coal terminal. Witness Ramas has made this adjustment to reduce working capital. (Ramas)

ISSUE 34: **What is the appropriate treatment of the remaining equipment inventory balance resulting from the closure of Plant Scholz?**

OPC: No position at this time.

ISSUE 35: **Is Gulf's proposed Deferred Return on Transmission Investments and the amortization thereof consistent with the terms of the 2013 Settlement Agreement in Docket No. 130140-EI, correctly calculated, and appropriate? If not, what is the appropriate amount?**

OPC: This question is not whether the amortization is consistent with the 2013 Settlement Agreement, since the document is silent on the amortization period. The Commission should require amortization over a period that is in the best interest of the customers while allowing Gulf to preserve and recover the deferred return as agreed to in the Settlement Agreement. Ramas has described the nature of the return as being similar to AFUDC, which is recovered over the life of the associated asset through depreciation expense. In this case such a recovery period would be approximately 40 years. Under this time frame, annual amortization expense should be $652,000 ($634,000 jurisdictional) instead of the proposed $6,525,000 ($6,343,000 jurisdictional) Gulf has requested consistent with its proposed four-year amortization period. This adjustment would require a further change to working capital in the form of a $2,936,000 ($2,860,000 jurisdictional) increase. (Ramas)

ISSUE 36: **Is Gulf's December 19, 2016 pension contribution impacting the 2017 projected test year appropriate? If not, what is the appropriate amount?**

OPC: No. The Company's projected contribution was overstated. Based upon the rebuttal testimony of Gulf witness Garvie, Gulf made a contribution of $55,816,000, consisting of $48 million for Gulf and $7,816,000 as an allocation from SCS instead of the $81,000,000 included in the filing. The Commission should allow no more than $55.816 million actual contribution amount. Gulf Exhibit No.__(SDR-2), Schedule 2, shows that the rate base contained in Gulf's original filing should be reduced by $25,184,000 ($24,498,000 jurisdictional) to reflect the actual funding amount. Additionally, the same exhibit shows that the pension expense incorporated in Gulf's filing should be reduced by $215,000 ($212,000 jurisdictional) to reflect the current 2017 pension cost projections. (Ramas)

ISSUE 37: **Is Gulf's proposed level of Working Capital for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, working capital should be no more than $214,631,000. (Ramas)

ISSUE 38: **Is Gulf's requested rate base for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments to reflect the most recent information provided in Gulf's rebuttal filing, the allowed rate base should be no more than $2,281,405,000. (Ramas)

Cost of Capital

ISSUE 39: **What is the appropriate amount of accumulated deferred taxes to include in the capital structure for the 2017 projected test year?**

OPC: The following amounts of accumulated deferred taxes should be included in the capital structure before reconciliation with rate base adjustments. (Woolridge)

	Capitalization Amounts (Thousands of Dollars)	Cost Rate
Deferred Income Taxes	603,001	0.00
ASC 740 Deferred Taxes	(34,002)	0.00

ISSUE 40: **What is the appropriate amount and cost rate of the unamortized investment tax credits to include in the capital structure for the 2017 projected test year?**

OPC: The following unamortized investment tax credits should be included in the capital structure before reconciliation with rate base adjustments. (Woolridge)

	Capitalization Amounts (Thousands of Dollars)	Cost Rate
Investment Credit – Weighted Cost	721	6.71

ISSUE 41: **What is the appropriate cost rate for customer deposits for the 2017 projected test year?**

OPC: 2.30% (Woolridge)

ISSUE 42: **What is the appropriate cost rate for short-term debt for the 2017 projected test year?**

OPC: 3.02% (Woolridge)

ISSUE 43: **What is the appropriate cost rate for long-term debt for the 2017 projected test year?**

OPC: 4.40% (Woolridge)

ISSUE 44: **What is the appropriate cost rate for preference stock for the 2017 projected test year?**

OPC: 6.15% (Woolridge)

ISSUE 45: **What is the appropriate capital structure for the 2017 projected test year?**

OPC: Dr. Woolridge adjusted the Company's capital structure so as to provide a capitalization from investor-provided capital with a 50.0% common equity ratio. The resulting capital structure from investor-provided capital consists of 1.67% short-term debt, 42.80% long-term debt, 5.53% preferred stock, and 50.00% common equity. This capital structure includes a common equity ratio (50.0%) that is above the averages of the two proxy groups (46.8% and 46.0%) utilized by OPC witness Woolridge and Gulf witness Vander Weide. When other capital sources are included, OPC's recommended capital structure is as follows. (Woolridge)

Capital	Capitalization Ratios
Short-Term Debt	**1.26%**
Long-Term Debt	**32.29%**
Preferred Stock	**4.17%**
Common Equity	**37.72%**
Customer Deposits	**1.01%**
Deferred Income Taxes	**24.93%**
ASC 740 Deferred Taxes	**-1.41%**
Investment Credit - Weighted Cost	**0.03%**
Totals	**100.00%**

ISSUE 46: **What is the appropriate return on equity (ROE) to use in establishing Gulf's revenue requirement?**

OPC: The appropriate ROE is 8.875%. Gulf's requested 11% ROE is excessive under current market conditions. Both interest rates and awarded ROEs have decreased since 2012. Applying the Discount Cash Flow (DCF) method checked by the Capital Asset Pricing Model (CAPM) method with a proposed capital structure of 50% and also applying the electric proxy groups, the appropriate ROE for Gulf is 8.875%. Utilizing an 8.875% ROE would result in an approximately $38.9 million reduction from Gulf's 2017 request. (Woolridge)

ISSUE 47: **What is the appropriate weighted average cost of capital including the proper components, amounts and cost rates associated with the capital structure for the 2017 projected test year? (Fallout Issue)**

OPC: 5.09% (Woolridge)

Net Operating Income

ISSUE 48: **Has Gulf made the appropriate test year adjustments to remove fuel revenues and fuel expenses recoverable through the Fuel Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

ISSUE 49: **Has Gulf made the appropriate test year adjustments to remove conservation revenues and conservation expenses recoverable through the Energy Conservation Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

ISSUE 50: **Has Gulf made the appropriate test year adjustments to remove capacity revenues and capacity expenses recoverable through the Capacity Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

ISSUE 51: **Has Gulf made the appropriate test year adjustments to remove environmental revenues and environmental expenses recoverable through the Environmental Cost Recovery Clause?**

OPC: Gulf has the burden to demonstrate that it has appropriately included costs in both base rate and clause classifications. At this point it is OPC's position that Gulf has not adequately demonstrated proper attribution of costs.

ISSUE 52: **Is Gulf's projected level of Total Operating Revenues for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments Test Year revenues, and prior to the impacts of the recommended rate reduction, should be at least $592,699,000. (Ramas)

ISSUE 53: **Is Gulf's proposed electric vehicle charging station expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: See position on Issue 1. (Ramas)

ISSUE 54: **Is Gulf's proposed tree trimming expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. Gulf has the burden of proof to demonstrate that its expenses are reasonably and prudently incurred, especially when estimated so far in advance. The OPC takes the position that Gulf has not met its burden on this issue with respect to its projection of expenses, especially with respect to, but not necessarily limited to, the impact of an overstated inflation factor. The Commission at least should consider using the 2.5% inflation factor where indications are that Gulf used an inflation factor to develop its estimated test year expenses.

ISSUE 55: **Is Gulf's proposed pole inspection expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. Gulf has the burden of proof to demonstrate that its expenses are reasonably and prudently incurred, especially when estimated so far in advance. The OPC takes the position that Gulf has not met its burden on this issue with respect to its projection of expenses, especially with respect to, but not necessarily limited to, the impact of an overstated inflation factor. The Commission at least should consider using the 2.5% inflation factor where indications are that Gulf used an inflation factor to develop its estimated test year expenses.

ISSUE 56: **Is Gulf's proposed production O&M expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. Gulf has the burden of proof to demonstrate that its expenses are reasonably and prudently incurred, especially when estimate so far in advance. The OPC takes the position that Gulf has not met its burden on this issue with respect to its projection of expenses, especially with respect to, but not necessarily limited to, the impact of an overstated inflation factor. The Commission at least should consider using the 2.5% inflation factor where indications are that Gulf used an inflation factor to develop its estimated test year expenses.

ISSUE 57: **Is Gulf's proposed transmission O&M expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. Gulf has the burden of proof to demonstrate that its expenses are reasonably and prudently incurred, especially when estimate so far in advance. The OPC takes the position that Gulf has not met its burden on this issue with respect to its projection of expenses, especially with respect to, but not necessarily limited to, the impact of an overstated inflation factor. The Commission at least should consider using the 2.5% inflation factor where indications are that Gulf used an inflation factor to develop its estimated test year expenses.

ISSUE 58: **Is Gulf's proposed distribution O&M expense for the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. Gulf has the burden of proof to demonstrate that its expenses are reasonably and prudently incurred, especially when estimate so far in advance. The OPC takes the position that Gulf has not met its burden on this issue with respect to its projection of expenses, especially with respect to, but not necessarily limited to, the impact of an overstated inflation factor. The Commission at least should consider using the 2.5% inflation factor where indications are that Gulf used an inflation factor to develop its estimated test year expenses.

ISSUE 59: **Is Gulf's proposed Incentive Compensation (also referred to by Gulf as variable pay or at-risk pay) included in the 2017 projected test year appropriate? If not, what adjustment should be made?**

OPC: No. The commission should make several adjustments to long term and short term incentive based compensation, including compensation embedded in affiliate charges, totaling $14,191,000 ($13,974,000 jurisdictional), as recommended in the testimony of OPC witness Ramas. These adjustments are as follows:

Earnings based incentive compensation or (long-term incentive compensation) in the amount of $3,798,496 ($3,740,000 jurisdictional). OPC witness Ramas recommends that 100% of the PSP (Performance Share Plan) expenses, Stock Option expenses and "Other" incentive compensation expenses be removed from the test year. The costs of the PSP, as well as the Stock Options expense, should be removed from adjusted test year O&M expenses since the goals under the plan are tied to the Southern Company total shareholder return, Southern Company earnings per share, and Southern Company equity weighted return on equity. This means that the plan is focused on aligning the interests of the upper level executives that participate in the plan with Southern Company's shareholders, not Gulf's Florida ratepayers. Therefore test year O&M expenses should be reduced by $2,143,000 ($2,110,000 jurisdictional). Further, test year O&M expenses should also be reduced by an additional $1,655,496 ($1,630,000 jurisdictional) to remove the projected test year affiliates' charges to Gulf associated with: (1) PSP in the amount of $1,579,617, (2) stock options of $65,410 and (3) "other" variable pay of $10,469. (Ramas)

Excessive short-term incentive compensation in the amount of $7,334,756 ($7,223,000 jurisdictional).

- Incentive compensation associated with vacant positions ($1,124,141). Gulf's Performance Pay Plan (PPP) expenses should be reduced by $1,124,141 to remove the portion associated with the 120-position vacancy adjustment addressed in Issue 60. (Ramas)
- Short-term incentive compensation associated with artificially low targets ($3,089,703). Gulf has assumed that the payouts under the PPP will exceed the PPP targets in the test year by 33%, which suggests that the targets are being set artificially low in order to increase pay or to overstate the revenue requirement. Accordingly test year PPP expenses remaining in the test year, after removal of the costs associated with the 120 vacant positions, should be reduced by $3,089,703 to reflect only the targeted payout level in base rates. (Ramas)
- Short-term incentive compensation associated with shareholder earnings goals ($3,120,912). Since the goal of the PPP is partially focused on increasing shareholder earnings, or Southern Company EPS goals, one-third of the remaining PPP expense (i.e., amount remaining after removal of vacant positions and reduction to reflect payout at target level) should be

removed from the test year, resulting in an additional $3,120,912 reduction to the PPP expense. (Ramas)

Excessive short-term incentive compensation embedded in affiliate's charges in the amount of $3,057,713 ($3,011,000 jurisdictional). OPC witness Ramas further recommended an adjustment that consistently removes excessive short-term incentive costs related to artificially low targets and shareholder earnings goals, amounting to $3,057,713 of the PPP expenses charged to Gulf by affiliated entities. (Ramas)

ISSUE 60: Are Gulf's proposed employee levels and salary and wage expenses included in the 2017 projected test year appropriate? If not, what adjustments should be made?

OPC: No. As OPC witness Ramas recommends that the most recent number of vacant positions, or 120 positions, be removed from the 2017 test year at the average per employee O&M expense of $64,448, resulting in a recommended reduction to test year labor O&M expense of $7,733,760 ($7,616,000 jurisdictional). This results in the adjusted test year labor costs, exclusive of the incentive compensation portion (See position on Issue 59), being based on the most recent employee levels coupled with Gulf's anticipated employee reductions for 2017, such as the employee reductions associated with Gulf's implementation of the self-service kiosks for which the associated capital expenditures are incorporated in the Company's filing. Corresponding fallout adjustments to payroll taxes for this adjustment should also be made. (Ramas)

ISSUE 61: Is Gulf's proposed Pension Expense for the 2017 projected test year appropriate? If not, what adjustment should be made?

OPC: No. The pension expense incorporated in the Company's original filing should be reduced by $215,000 ($212,000 jurisdictional) to reflect the most recent 2017 pension expense projections based on information provided in Gulf's rebuttal filing. (Ramas).

ISSUE 62: Is Gulf's proposed Other Post-Employment Benefits Expense for the 2017 projected test year appropriate? If not, what adjustment should be made?

OPC: No position at this time.

ISSUE 63: Is Gulf's proposed employee benefit expenses for the 2017 projected test year appropriate? If not, what adjustment should be made?

OPC: SERP costs ($2,655,000). To the extent the Company decides to provide additional benefits that exceed the generous IRS limitations on qualified pension plans, the shareholders should fund the cost of the additional non-qualified plans. Witness Ramas recommends that test year expenses be reduced by $2,655,000 ($2,615,000 jurisdictional) to remove the SERP expense from the test year. (Ramas)

Unsubstantiated Other Employee Benefits ($268,432). Witness Ramas recommends that the 58% increase projected in the test year expense be held at the actual 2015 expense level of $461,749. The Company has not supported the substantial projected increase in these costs. Other Employee Benefits costs should be reduced by $268,432 ($264,000 jurisdictional). (Ramas)

ISSUE 64: Is Gulf's proposed annual storm damage accrual for the 2017 projected test year appropriate? If not, what is the appropriate amount?

OPC: No. Gulf's current accrual of $3.5 million, experience and reserve balance, coupled with mechanisms available to Gulf, create a strong presumption against any increase in the annual storm accrual. Gulf has not demonstrated an entitlement to any increase in the annual accrual. (Ramas)

ISSUE 65: Is Gulf's property damage reserve target appropriate? If not, what is the appropriate property damage reserve target?

OPC: Yes, in the sense that the target established in 2012 does not need to be increased and Gulf's current accrual and experience have evinced a steady progress toward achieving the target.

ISSUE 66: Is Gulf's proposed expense related to Directors and Officers Liability Insurance appropriate? If not, what adjustment should be made?

OPC: No. Directors and Officers' liability insurance expense should be shared equally between Gulf's shareholders and the customers, consistent with Gulf's last adjudicated rate case order.

<u>ISSUE 67</u>: Is Gulf's proposed Rate Case Expense for the 2017 projected test year appropriate? If not, what adjustment should be made?

OPC: No. The Commission should apply a downward adjustment to rate case expense based on all information that becomes available – in reliable form – at the hearing.

<u>ISSUE 68</u>: Is Gulf's proposed Bad Debt Expense for the 2017 projected test year appropriate? If not, what adjustment should be made?

OPC: No. Based on the four-year average bad debt rate, the appropriate test year uncollectible expense should be $3,149,000, resulting in an expense reduction of $845,000. (Ramas)

<u>ISSUE 69</u>: Is Gulf's proposed Customer Accounts Expenses for the 2017 projected test year appropriate? If not, what adjustments should be made?

OPC: No position at this time.

<u>ISSUE 70</u>: Is Gulf's proposed Customer Service & Information Expenses and Sales Expenses for the 2017 projected test year appropriate? If not, what adjustments should be made?

OPC: No position at this time.

<u>ISSUE 71</u>: Is Gulf's proposed Administrative and General Expenses for the 2017 projected test year appropriate? If not, what adjustments should be made?

OPC: No position at this time.

ISSUE 72: **What adjustment, if any, should be made to account for affiliated activities/transactions for the 2017 projected test year?**

OPC: In addition to adjustments for allocated compensation costs (Performance Share Plan, Performance Pay Plan, Stock Option and the "Other" unidentified variable pay charges) related to Issue 59, further adjustments, totaling $8,375,000, are required to account for Gulf's failure to meet its burden to explain or justify certain costs proposed to be charged to Gulf or to accurately account for reallocation of common costs to newly acquired businesses and account for changes in allocation factors.

Failure to explain or justify affiliate costs, adjustments of $2,013,000 ($1,975,000 jurisdictional):

- Aviation costs: Given the lack of documentation and evidence demonstrating that the use of owned and leased aircraft is more cost effective than publicly available air transportation, 50% of the costs should be disallowed, resulting in an $884,810 reduction to the forecasted test year expenses. (Ramas)
- Unexplained Budget Work Orders: Given the only documentation provided upon request was "Amount represents permanent tax differences for SCS income taxes," Gulf's request for recovery in the amount of $351,672 should be denied based on its failure to meet its burden of proof in its filing. (Ramas)
- Energy Innovation Center: Gulf has failed, in its filing, to demonstrate a benefit to Gulf's Florida customers in the forecasted test year associated with Southern Company's new Energy Innovation Center, nor has it demonstrated that the costs of the center that are forecasted to be charged to Gulf will be outweighed by the benefits to Gulf's Florida customers. Test year expenses should be reduced by $626,080. (Ramas)
- Gulf has testified that it has no plans to build a nuclear reactor to serve Florida customers. Therefore Research & Development costs of $149,968 related to "next generation nuclear" should not be recovered from Gulf's customers. (Ramas)

Failure to allocate common affiliate costs to new business units, adjustments of $6,362,000 ($6,243,000 jurisdictional). As demonstrated by OPC witness Ramas, a reduction factor of 11% should be applied to the applicable allocation-driven O&M expenses forecasted to be charged from SCS in the amount of $57,834,000 (does not include the cost centers that are subject to incentive compensation adjustments and adjustments identified above). This results in a recommended adjustment of $6,362,000 ($6,243,000 jurisdictional) to account for the impacts of the recent Southern Company acquisitions and other impacts of changes to SCS allocation factors used to charge costs to Gulf. To the extent the Commission does not adjust the remaining affiliate costs for the compensation adjustments proposed by the OPC under Issue 59, those categories should also be adjusted by the same 11% factor. (Ramas)

ISSUE 73: **Is Gulf's requested level of O&M Expense for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. O&M expenses included in the test year, after appropriate adjustments, should be no more than $266,614,000. (Ramas)

ISSUE 74: **What is the appropriate amount of depreciation and fossil dismantlement expense for the 2017 projected test year?**

OPC: After appropriate adjustments, depreciation and amortization (including fossil dismantlement) expenses should be no more than $125,195,000. (McCullar)

ISSUE 75: **What is the appropriate amount of Taxes Other Than Income Taxes for the 2017 projected test year? (Fallout Issue)**

OPC: After appropriate adjustments, Taxes Other Than Income Taxes should be no more than $32,732,000. (Ramas)

ISSUE 76: **Should the current amortization of investment tax credits (ITCs) and flow back of excess deferred income taxes (EDITs) be revised to reflect the approved depreciation rates and amortizations?**

OPC: Yes, all appropriate adjustments should be included in the amortization of investment tax credits (ITCs) and flow back of excess deferred income taxes (EDITs).

ISSUE 77: **Is it appropriate to make a parent debt adjustment per Rule 25-14.004, Florida Administrative Code? If so, what adjustment should be made?**

OPC: Yes. Gulf has not met its burden to rebut the presumption that the equity investments by its parent are not supported in part by debt from the parent company.

The parent debt adjustment should be $7,030,000 subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue).

<u>ISSUE 78</u>: **What is the appropriate amount of Income Tax expense for the 2017 projected test year? (Fallout Issue)**

OPC: After appropriate adjustments, Income Tax expense for the test year should be no more than $53,644,000, subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue). To the extent that the income tax rate changes the Commission should direct that rates and customer credits are adjusted consistent with the OPC's position on the new issue. (Ramas)

<u>ISSUE 79</u>: **Is Gulf's requested level of Total Operating Expenses for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue), the Total Operating Expenses should be no more than $478,047,000. (Ramas)

<u>ISSUE 80</u>: **Is Gulf's projected Net Operating Income for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue), Net Operating Income should be at least $114,652,000. (Ramas)

<u>Revenue Requirements</u>

<u>ISSUE 81</u>: **What are the appropriate revenue expansion factor and the appropriate net operating income multiplier, including the appropriate elements and rates for Gulf? (Fallout Issue)**

OPC: No position at this time. [subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue)]

ISSUE 82: **Is Gulf's requested annual operating revenue increase for the 2017 projected test year appropriate? If not, what is the appropriate amount? (Fallout Issue)**

OPC: No. After appropriate adjustments, subject to the corporate income tax rate remaining at 35% (see OPC position on New Tax Rate Reduction Issue), annual operating revenue should be reduced by at least ($2,087,000). (Ramas)

Cost of Service and Rate Design

ISSUE 83: **Is Gulf's proposed separation of costs and revenues between the wholesale and retail jurisdictions appropriate?**

OPC: No Position.

ISSUE 84: **What is the appropriate treatment of production costs within the cost of service study?**

OPC: No Position.

ISSUE 85: **What is the appropriate treatment of transmission costs within the cost of service study?**

OPC: No Position.

ISSUE 86: **What is the appropriate treatment of distribution costs within the cost of service study?**

OPC: No Position.

ISSUE 87: **How should any change in the revenue requirement approved by the Commission be allocated among the customer classes?**

OPC: No Position.

ISSUE 88: **Should Gulf's proposed new methodology to design the residential base and energy charges for the residential rate schedules RS, RSVP, FLAT-RS, and RSTOU that results in an increase from $0.62 to $1.58 per day, or approximately $48 per month, in the base charge and corresponding reduction in the energy charge be approved?**

OPC: No Position.

ISSUE 89: **Is the proposed new optional Residential Service – Demand (RSD) rate schedule appropriate?**

OPC: No Position.

ISSUE 90: **Is the proposed new optional Residential Service – Demand Time-of-use (RSDT) rate schedule appropriate?**

OPC: No Position.

ISSUE 91: **Is the proposed new optional Customer Assistance Program Rider (Rate Rider CAP) appropriate? (Moot if Issue 88 is not approved)**

OPC: No Position.

ISSUE 92: **Is Gulf's proposal to remove the critical peak option for the General Service Demand Time-of-use (GSDT) rate schedule appropriate?**

OPC: No Position.

ISSUE 93: **Is Gulf's proposed new Extra-Large Business Incentive Rider (Rate Rider XLBIR) appropriate?**

OPC: No Position.

ISSUE 94: **Are Gulf's proposed changes to its small, medium, and large Business Incentive Riders appropriate?**

OPC: No Position.

ISSUE 95: **What are the appropriate base charges?**

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 96: **What are the appropriate demand charges?**

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 97: **What are the appropriate energy charges?**

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 98: **What are the appropriate transformer ownership discounts?**

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 99: **What are the appropriate lighting charges?**

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 100: **Should the Commission approve the following modifications to the Outdoor Service (OS) tariff and lighting pricing methodology that have been proposed by Gulf:**

a) Remove certain fixtures from the tariff;

b) Close all Metal Halide, 21 High Pressure Sodium, and 16 LED fixtures for new installations;

c) Revisions to the pole options; and

d) Modification to the Outdoor Service Lighting Pricing Methodology contained in Form 4.

OPC: No Position. The OPC takes no position on the specific design of Gulf's rates and charges; however, in total, the rates and charges should be designed to allow Gulf an opportunity to recover no more than the revenue requirement established by this Commission at the time rates go into effect.

ISSUE 101: **What is the appropriate effective date for Gulf's revised rates and charges?**

OPC: No sooner than July 1, 2017.

Other Issues

ISSUE 102: **Should the Commission approve Gulf's proposed modifications to the existing residential HVAC Improvement program in its Demand-Side Management Plan? (Moot if Issue 88 is not approved)**

OPC: No position.

ISSUE 103: **Should the Commission approve Gulf's proposed modifications to the existing Residential Building Efficiency program in its Demand-Side Management Plan? (Moot if Issue 88 is not approved)**

OPC: No position.

ISSUE 104: **Should the Commission approve Gulf's proposed new residential Insulation Improvement program to be added to its Demand-Side Management Plan? (Moot if Issue 88 is not approved)**

OPC: No position.

ISSUE 105: **Should the Commission approve the following modifications to the Critical Peak Option for the Large Power Time-of-Use (LPT) rate schedule:**

a) Establish the Critical Peak Option as a Demand-Side Management Program;

b) Reduce the minimum critical peak demand notification from one business day to one hour;

c) Eliminate the restrictions on the frequency and duration of the critical peak period.

OPC: No position.

ISSUE 106: **Should Gulf be required to file, within 90 days after the date of the final order in this docket, a description of all entries or adjustments to its annual report, rate of return reports, and books and records which will be required as a result of the Commission's findings in this rate case?**

OPC: Yes.

ISSUE 107: **Should this docket be close**d?

OPC: Yes.

5. STIPULATED ISSUES:

None at this time.

6. PENDING MOTIONS:

None

7. STATEMENT OF PARTY'S PENDING REQUESTS OR CLAIMS FOR CONFIDENTIALITY:

None.

8. OBJECTIONS TO QUALIFICATION OF WITNESSES AS AN EXPERT:

None at this time.

<u>9. STATEMENT OF COMPLIANCE WITH ORDER ESTABLISHING PROCEDURE</u>:

There are no requirements of the Order Establishing Procedure with which the Office of Public Counsel cannot comply.

Dated this 21st day of February, 2017

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing **PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL** has been furnished by electronic mail on this 21st day of February, 2017.

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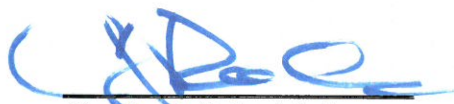

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