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Florida Power
A Progress Energy Company

ASSOCIATE GENERAL COUNSEL

JAMES A. MCGEE

June 4, 2002

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COMMISSION CLERK

Ms. Blanca S. Bayó, Director
Division of the Commission Clerk
and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Docket No. 011605-EI

Dear Ms. Bayó:

Pursuant to Order No. PSC-02-0428-PCO-EI, enclosed for filing in the subject docket are an original and fifteen copies of Florida Power Corporation's risk management incentive plan proposal for consideration at the Commission workshop scheduled for June 17, 2002. Florida Power has filed under separate cover a Notice of Intent to Request Confidential Classification with respect to a supporting document for the proposal containing methodology details and examples.

Please acknowledge your receipt of the above filing on the enclosed copy of this letter and return to the undersigned. Also enclosed is a 3.5 inch diskette containing the above-referenced document in Word format. Thank you for your assistance in this matter.

Very truly yours,

James A. McGee

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JAM/scc
Enclosure

cc: Parties of record

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FLORIDA POWER CORPORATION

DOCKET NO. 011605-EI

FLORIDA POWER CORPORATION'S RISK MANAGEMENT INCENTIVE PLAN PROPOSAL

In accordance with the directive of the Prehearing Officer in Order No. PSC-02-0428-PCO-EI, issued March 28, 2002 in the above docket, Florida Power Corporation (Florida Power or the Company) submits the following Hedging Program overview description as its proposed risk management incentive plan for discussion at the Commission workshop scheduled for June 17, 2002. If appropriate, based on the outcome of the workshop, Florida Power will prepare and file a detailed plan document for Commission approval.

Two preliminary comments are warranted. First, the Company wishes to be clear that its Hedging Program is a Florida Power-specific proposal and carries no suggestion that it is the appropriate risk management plan for the other investor-owned utilities. To the contrary, Florida Power believes it to be highly desirable that each of the utilities have the latitude to tailor a risk management plan to its own circumstances and comfort level when entering this new and potentially high risk area of fuel procurement.

Second, the description of Florida Power's proposed Hedging Program below is, of necessity, lacking in details and specifics due to the highly sensitive nature of this information. To aid the Commission's understanding of the proposed program's workings, Florida Power has separately filed supporting documentation that provides details and examples of the hedging methodology that is subject to protection under the Commission's confidentiality rule.

The Proposed Hedging Program

Program Objective

Minimize fuel price volatility for customers through the use of hedging strategies that allow customers and shareholders to share in the risks and benefits of implementing the program, with the understanding that an effective price volatility mitigation program will not necessarily result in lower costs to customers.

Key Program Elements

- The Hedging Program will be applied to the procurement of natural gas and residual (No. 6) oil, the two primary fuels used by Florida Power that display the greatest price volatility.

- Prices will be fixed for a predetermined portion (at least 20%) of the Company's forecasted annual natural gas and residual oil requirements. The percentage for each fuel will be established early in the year prior to the forecast year and the resulting quantities of fixed price fuel will remain constant and unaffected by changes in the actual quantities of fuel required.

- The fixed prices will be established for the predetermined quantities of natural gas and residual oil at phased, or staggered, time intervals based on indices of future commodity market prices. An average of the prices established for each time interval, plus a risk premium, will determine the final fixed price for natural gas and residual oil. Because Florida Power anticipates entering the market at these same intervals for risk mitigation purposes, the intervals will be varied in the future as a safeguard against potential predictability and market manipulation.

- After this methodology has been approved by the Commission at the outset of the Hedging Program, Florida Power will then include the fixed natural gas and residual oil prices established by the methodology in its filed projections used to calculate the Company's fuel factors for each subsequent cost recovery period. (A supplemental filing may be necessary for the initial implementation, depending on the timing of program approval.) These fixed prices will be charged to customers through the fuel clause for the predetermined quantities of each fuel, irrespective of the prices actually paid by Florida Power. Additional volumes of natural gas and residual oil above these fixed price quantities will be charged to customers in the traditional manner based on the Company's actual costs, subject to true-up.

- The fixed natural gas and residual oil prices established under the Hedging Program will apply only to the two fuel commodities themselves. Non-commodity costs related to the procurement of these fuels (*e.g.*, demand and transportation charges, taxes, etc.) will be recovered in the traditional manner based on Florida Power's actual costs. Traditional fuel clause recovery will also apply to hedging transaction costs (*e.g.*, commissions and fees, margin requirement costs, basis charges, risk premiums, etc.). However, the costs associated with speculative trading (*e.g.*, contracts for futures, forwards, options, swaps, etc.) in amounts greater than the quantity of each fuel consumed annually on the Company's system will not be recoverable through the fuel clause. A force majeure clause will also be included.

Expanded Wholesale Power Sharing Mechanism

Substantial incremental costs will have to be incurred to establish the infrastructure necessary for the implementation and administration of the Hedging Program. These costs include the hiring of high salaried, experienced professionals needed to implement the hedging strategies and execute the related financial transactions, as well as the mid and back office personnel needed to perform the monitoring, accounting, and risk assessment functions associated with these financial transactions, and the enhancement of sophisticated software trading systems.

As a means to partially offset to these incremental infrastructure costs, Florida Power's Hedging Program proposal includes an expansion of the current mechanism for the sharing of gains on non-separated wholesale sales established by Order No. PSC-01-2371-FOF-EI. The expanded sharing mechanism would apply to the Company's savings from non-separated wholesale purchases, as reported on Schedule A9, as well as to the gains from its wholesale sales, as reported on Schedule A6. Under this proposal, all of the savings and gains from non-separated wholesale transactions would be shared between customers and shareholders on a 2/3-1/3 basis.

Program Term

Florida Power considers its Hedging Program to be in the nature of a pilot project, where the decision on the project's ultimate duration is based in large part on the experience gained over an initial pilot period. Given the lack of actual hands-on operational and regulatory experience by Florida Power or the Commission with the more extensive and sophisticated hedging practices contemplated by the Company's proposed program, it is likely that neither has a sufficient comfort level to undertake a long term commitment.

Florida Power therefore proposes an initial two-year term for its Hedging Program, beginning with the 2003 fuel cost recovery period. For the 2005 cost recovery period, the Company or the Commission, on its own motion or upon the request of an intervenor, would have the option to unilaterally terminate the program outright or subject to modification at the fuel cost recovery hearing in 2003. (This lead time is needed because the Company would have implemented its Hedging Program for 2005 prior to the hearing in 2004.) The same option would be available at each fuel cost recovery hearing thereafter.

6/4/02

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true copy of Florida Power Corporation's risk management incentive plan proposal has been furnished to the following individuals by regular U.S. Mail this 5th day of June, 2002:

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