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September 12, 2003

HAND DELIVERED

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

Re: Fuel and Purchased Power Cost Recovery Clause with Generating
Performance Incentive Factor; FPSC Docket No. 030001-EI

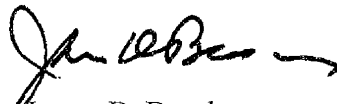
Dear Ms. Bayo:

Enclosed for filing in the above docket are the original and ten (10) redacted copies of Tampa Electric's Company's Fuel Procurement and Wholesale Power Purchases Risk Management Plan 2004. A single confidential version of the Plan with the confidential information highlighted in yellow is being separately filed this date with your office along with a Request for Confidential Classification.

Please acknowledge receipt and filing of the above by stamping the duplicate copy of this letter and returning same to this writer.

Thank you for your assistance in connection with this matter.

Sincerely,



James D. Beasley

JDB/pp
Enclosure

cc: All Parties of Record (w/enc.)

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**BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION**

| | | |
|----------------------------------|---|---------------------------|
| In re: Fuel and Purchased Power |) | DOCKET NO. 030001-EI |
| Cost Recovery Clause with |) | FILED: SEPTEMBER 12, 2003 |
| Generating Performance Incentive |) | |
| Factor |) | |

REDACTED VERSION

**TAMPA ELECTRIC COMPANY'S
FUEL PROCUREMENT AND WHOLESALE POWER PURCHASES
RISK MANAGEMENT PLAN
2004**

**TAMPA ELECTRIC COMPANY
FUEL PROCUREMENT AND WHOLESALE POWER PURCHASES
RISK MANAGEMENT PLAN
2004**

Introduction

Beginning in 2003, Tampa Electric began procuring an increased amount of natural gas for its generation needs due to the repowering of Gannon Station to Bayside Station. In response, the company developed a hedging plan that was presented to the members of TECO Energy's Risk Authorizing Committee (RAC) and received approval for this plan in early 2003. The plan is ongoing, with monthly reports of activities to the RAC. Before Tampa Electric may change the existing plan, the company must present any changes to the RAC for approval.

I. Qualitative and Quantitative Risk Management Objectives

- A. Qualitative objectives:** Tampa Electric's goals in managing risks associated with fuel or power purchases are focused on minimizing supply risk to ensure reliability of electric service to its customers at a reasonable price. To the extent that price risk can be reduced without compromising supply reliability or imposing unnecessary costs on its customers, Tampa Electric is committed to executing strategies to accomplish this.
- B. Quantitative objectives:** Tampa Electric's quantitative objective is to prudently manage its fuel and wholesale energy procurement activities to minimize the variance from projected expenditures while taking advantage of cost-saving opportunities that do not result in increased supply risk. Tampa Electric has established a portfolio of fuel and purchased power products with credit-worthy counterparties for known volumes and prices.

II. Oversight & Reporting of Fuel Procurement Activities

The Company provides its fuel and wholesale energy procurement activities with independent and unavoidable oversight. In support of this, we offer the following observations:

- A.** The TECO Energy Board of Directors established an Energy Risk Management Policy ("Risk Policy"). This policy governs all energy commodity transacting activity at each of TECO Energy's operating units. The scope of the policy includes:
- Roles and responsibilities of various persons and functions with respect to risk management
 - Authorized transacting activity
 - Risk limits
 - Valuation and data management
 - Credit risk management

- Reporting
 - Compliance and enforcement
- B.** The Risk Policy established the TECO Energy Risk Authorizing Committee (RAC). The responsibilities of the RAC include the following:
- Reviewing the Risk Management Policy periodically and recommending changes and enhancements for Board of Directors approval
 - Reviewing corporate risk limits for recommendation to the Board
 - Within Board approved corporate risk limits, establishing the quantitative limits for operating companies. The RAC may, at its discretion, delegate approval of sub-limits to operating company management
 - Approving parameters for counterparty credit limits and the allocation of limits among the operating companies
 - Establishing guidelines for risk management and measurement;
 - Overseeing and reviewing the risk management process and infrastructure
 - Reviewing and approving transacting strategies proposed by the operating companies
 - Understanding and approving methodologies used for valuation and risk measurement
 - Reviewing and approving corporate and operating company risk limits
 - Establishing credit underwriting standards, and monitoring credit risk-taking activities and related exposures
 - Reviewing risk reports, including portfolio risk summaries and profitability and performance summaries
 - Enacting, maintaining, and enforcing limit violation and trader misconduct policies
 - Taking appropriate courses of action when the risk position of a transacting group has exceeded, or is approaching the established limits
 - Reviewing and approving new risk management products
 - Presenting periodic reports to the Board or its committees
- C.** TECO Energy established a corporate risk management function (“middle office”) and hired a Vice President of Energy Risk Management.
- D.** Tampa Electric established additional oversight or control mechanisms to ensure compliance with policies and procedures. The following practices provide checks and balances on procurement activities.
- Fuel and wholesale energy procurement activities are conducted in accordance with Company guidelines, including review by the

- operating stations, Environmental Affairs Department and officers of the company
 - All agreements are formalized in a written contract that is reviewed by the company's Legal Department
 - The contracts are reviewed by the Corporate Credit Manager of TECO Energy's Treasury Department for potential credit risks
 - The Company maintains approval authority restrictions based on term and value of the transaction
 - Payments of invoices under each contract are approved by the Manager(s) and/or Director of the Wholesale Marketing and Fuels Department and reviewed by the Regulatory Accounting Department
 - Each transaction is eligible for review by outside, internal and regulatory auditors
- E. In accordance with the Risk Policy, Tampa Electric established commodity transaction limits for related commodity transactions.
- F. Tampa Electric's Wholesale Marketing and Fuels Department updated and formalized its policies and procedures.
- G. Reports are generated that summarize the fuel procurement activities of the company. These include monthly financial reports produced by Regulatory Accounting, FERC Electric Quarterly Reports, FERC Form 1, FERC Form 580, FERC Form 423, FPSC A schedules and FPSC E schedules. In addition, position and mark-to-market reports are produced and reviewed by the Vice President of Energy Risk Management. The appropriate entries and related disclosures are made in the Company's books and records as required by accounting standards.

III. Risk Assessment

In its Risk Policy, TECO Energy has identified the following types of risks for its commodity portfolio:

Market Risk

Market risk is the potential change in value of a commodity contract caused by adverse changes in market factors (price and volatility). The following are types of market risk.

Price Risk: Price risk refers to the uncertainty associated with changes in the price of an underlying asset. For instance, if a company has a short position in the market (e.g., needs to meet load requirements by purchasing electricity or gas), it will be susceptible to price increases. Conversely, if a company is in a long position (e.g., excess generation or

gas supply), it is exposed to decreases in market prices. Tampa Electric manages its price risk using physical and financial hedges.

In 2004 Tampa Electric is subject to minimal price risk related to variation in coal prices since it has already contracted for its expected coal needs.

The company's expected expenditures for natural gas in 2004 are bounded at approximately [REDACTED], based on the forward price and volatility curves for natural gas and the company's expected usage. This exposure estimate does not take into account any hedges the company may implement to limit its exposure. Tampa Electric's hedging strategy with respect to natural gas is outlined in Section IV of this plan.

Tampa Electric's decision to purchase a portion of its expected purchased power needs on the spot market result in an expected [REDACTED] for 2004. Tampa Electric's hedging strategy with respect to purchased power is outlined in Section IV of this plan.

Tampa Electric requires small quantities of fuel oil and maintains a requirements contract that eliminates its supply risk. Due to the small quantities in question, price risk is minimal and is therefore not quantified.

Time Spread Risk: This is the risk that the relationship between two points (*i.e.*, one month versus six months) on the forward curve changes. Because the shape of the fuel or electricity forward curve changes to reflect the market's expectations of spot and future fuel or electricity prices, the relationship between any two points on the curve is not always constant. Because of the nature of its business Tampa Electric has little reason or opportunity to offset energy commodity requirements in one month with resources delivered in another month. Therefore, time spread risk is not a significant issue for Tampa Electric.

Liquidity Risk: Liquidity risk is associated with the lack of marketability of a commodity. It includes the risk of an adverse cost or return variation stemming from the lack of marketability of a financial instrument. Liquidity risk may arise because a given position is very large relative to typical trading volumes of like commodity and contract tenor, or because market conditions are unsettled. Liquidity risk is usually reflected in a wide bid-ask spread and large price movements in response to any attempt to buy or sell. A firm facing the need to quickly unwind a portfolio of illiquid instruments may find it necessary to sell at prices far below fair value. Tampa Electric is not exposed to liquidity risk since the company does not purchase instruments for resale.

Basis Risk: Basis risk is the risk exposure due to a difference in commodity value between different delivery points. Electricity markets are regional. Prices can be different at different locations because of differences in both supply costs and the cost of transmission between the two locations. These price differences are dynamic, primarily due to changes in transmission availability between the two locations. Due to the stability of the coal market, Tampa Electric's negligible use of oil, and the indexing of its natural gas contract pricing, basis risk is not a significant issue for the company.

Option Risk (Convexity): Option risk is associated with purchasing or writing an option, and represents the risk that the value of an option at expiration or upon exercise is different from the premium paid when the option was purchased or sold. Option risk is an issue for Tampa Electric only to the extent that it chooses to use option contracts in the future to manage its more fundamental price risks.

Fundamentally, market risk is created by the existence of "open" positions. An open position is the difference between an existing requirement and the ability to meet that requirement with existing resources.

Volume Risk

Volume risk is the potential adverse economic impact of unanticipated changes in supply or demand. Tampa Electric faces supply risk, because there is uncertainty associated with the availability of generating units or fuel availability for those units. If a generating unit fails, Tampa Electric must replace the power with another unit's generation or with purchased power at market prices. Tampa Electric also faces demand risk since there is uncertainty associated with customer demand, and thus uncertainty in the determination of the fuel or energy purchase volumes necessary to supply such demand. Tampa Electric's volume risk for fuel and purchased power in 2004 is managed operationally and through contract terms enforcement, including appropriate legal remedies, should a party default.

Credit Risk

Credit risk is the risk of financial loss due to a counterparty's failure to fulfill the terms of a contract on a timely basis. It includes both settlement risk associated with payment for fuel or energy received, as well as potential risk, which reflects the risk that the counterparty defaults on an obligation to provide or receive fuel or energy. Credit risk depends on the probability of counterparty default, the concentration of credit exposure with a small number of counterparties, the total amount of exposure, and the volatility of markets. Tampa Electric's credit risk commodity price hedging will vary based on the number of its trading

counterparties and the mark-to-market value of its hedge transactions. Tampa Electric's existing credit risk is minimal.

Administrative Risk

Administrative risk is risk of loss associated with deficiencies in a company's internal control structure and management reporting due to human error, fraud or a system's inability to adequately capture, store and report transactions.

Tampa Electric's internal control infrastructure for power marketing and fuel procurement is changing to reflect the company's increased use of natural gas. However, current transaction volumes of natural gas and power are small, and therefore related administrative risk is minimal. The company has consistently maintained appropriate administrative controls for entering and administration of coal and oil contracts.

IV. Risk Management Strategy and Current Hedging Activity

Tampa Electric's risk management strategy is designed to limit exposure to different types of risk that are applicable to the company's operation.

Market Risk

Tampa Electric's potential market risk is the result of open positions in four commodities:

- Coal
- Natural Gas
- Fuel Oil
- Purchased Power

On an energy basis, expected generation during 2004 will be served in the proportions shown in the following table.

| Commodity | Percent of Generation |
|------------------|------------------------------|
| Coal | 54% |
| Natural Gas | 39% |
| Fuel Oil | 1% |
| Purchased Power | 6% |

Based on Tampa Electric's assessment of market risk factors, the company has implemented the market risk management strategies described below.

Coal. Tampa Electric has contracted for all of its expected coal needs for 2004 through bilateral agreements with coal producers. Therefore, Tampa Electric's coal price risk in 2004 has been virtually eliminated. The company provided the projected amounts in both tons and dollars in its 2004 projection filing submitted September 12, 2003. Tampa Electric's contracts with suppliers incorporate legal remedies in the event of default, which addresses its volume risk. In addition, the coal market is expected to remain stable in 2004 with available supply should any parties not deliver according to contracted requirements. As a result, Tampa Electric's coal volume risk in 2004 is minimal. Lastly, due to the financial difficulties many counterparties have encountered of late in the energy sector, Tampa Electric has strengthened its credit review process. Newly established agreements incorporate stricter credit provisions; and as older contracts expire, the company plans to include the stricter provisions in future coal supply agreements.

Fuel Oil. In 2004, Tampa Electric will continue to purchase its fuel oil needs at spot market prices. Oil represents only one percent of the company's needs on a GWH basis, and therefore, associated price risk is minimal. Tampa Electric maintains a requirements contract with a local supplier to deliver all of its needs, which mitigates supply risk.

Natural Gas. Tampa Electric continues to implement prudent financial hedging strategies for natural gas requirements. The company has used swap agreements, or the exchange of a payment tied to the value of a natural gas index for a fixed payment. Tampa Electric plans to hedge a significant percentage of its projected natural gas usage in 2004, using swaps, collars—the exchange of a price floor for a price cap, and futures contracts.

Tampa Electric uses the forward pricing information of the New York Mercantile Exchange natural gas forward price curve in developing natural gas price hedging strategy.

The purpose of Tampa Electric's natural gas hedge plan is to minimize natural gas price volatility by utilizing financial instruments relying on three key variables: price, volume and time.

Tampa Electric projects price during the company's annual fuel budgeting process. [REDACTED]

[REDACTED]

Volume is another forecasted variable. It is determined by expected demand and supply fundamentals: customer load and energy use, Tampa Electric generation and statewide generation levels. Expected natural gas consumption establishes the basis for the amount of financial hedging instruments or contracts to be entered. Expected minimum and maximum volumes are set according to shoulder and peak month consumption.

[REDACTED]

Purchased Power. As of September 2003, Tampa Electric has physically hedged [REDACTED] of its expected 2004 purchased power needs. Total forecasted purchased power is 1,317,719 MWH. Of this total, firm cogeneration energy purchases account for [REDACTED]. Another 276,513 MWH will be purchased from Hardee Power Partners, at cost-based capacity and energy rates. Finally, [REDACTED]

[REDACTED] The table on the following page shows the expected purchased power amounts by month.

The company's purchased power contracts include a fuel component, therefore, Tampa Electric has exposure to fuel price risk for its wholesale energy purchases, particularly for purchased power supplied from natural gas-fired generation. The fuel component of the price risk could be hedged with financial derivatives, but Tampa Electric does not currently hedge wholesale energy transactions with financial instruments due to the lack of a liquid, published wholesale energy market and appropriate available instruments. The company will continue to evaluate the merits of including this activity in its natural gas hedging strategy.

2004 PURCHASE INFORMATION

| | Total Purchases (MWH) | |
|--------------|--------------------------------------|--|
| JAN | 54,603 | |
| FEB | 53,218 | |
| MAR | 60,500 | |
| APR | 60,401 | |
| MAY | 94,256 | |
| JUN | 176,863 | |
| JUL | 188,234 | |
| AUG | 180,698 | |
| SEP | 161,957 | |
| OCT | 145,796 | |
| NOV | 52,877 | |
| DEC | 88,316 | |
| TOTAL | 1,317,719 | |

In summary, Tampa Electric's planned operations in 2004 result in nominal market risk associated with coal and fuel oil. Non-price risks associated with natural gas and purchased power are also small. Therefore, the company is currently focusing its hedging activities on mitigating the price risk associated with natural gas and purchased power.

Volume Risk

Hedging of volumetric risk is problematic due to a limited number of viable hedge instruments. Tampa Electric has identified the following instruments:

- "Swing" contracts enable the buyer to take variable volumes up to a predefined limit
- Full requirement contracts enable the buyer to take any volume up to total usage
- Weather derivatives enable the buyer to take variable volumes depending on weather temperatures and have significant price premiums

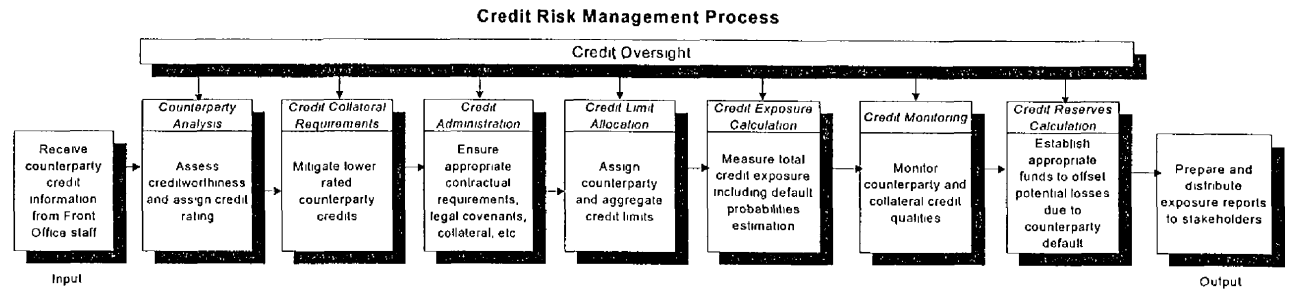
Tampa Electric uses swing contracts and full requirements contracts where needed commodity volumes are small and in situations where commodity volumes are unpredictable in volume and/or timing. The company evaluated weather derivatives as a volume risk hedge and determined that they are not appropriate for Tampa Electric's situation.

Credit Risk

TECO Energy's credit risk management process is composed of the following primary steps. (Also see the figure below.)

- Receive counterparty information for initial processing
- Assess counterparty creditworthiness and assign credit rating (i.e., third-party and internal)
- Determine credit collateral requirements, as needed
- Request, review and monitor contractual requirements, legal covenants, collateral documents and credit provisions
- Establish corporate maximum exposure and allocate appropriate counterparty credit limits to operating companies
- Quantify counterparty exposure and measure against approved limits
- Monitor counterparty and collateral credit qualities
- Calculate appropriate credit reserves to offset losses associated with potential default
- Prepare credit exposure reports that result in updated credit limits for new business transactions entered into by the operating companies

TECO'S Credit Risk Management Process



Administrative Risk

Tampa Electric plans to purchase and implement a software program to more efficiently track, monitor and evaluate hedging activities that would provide greater reporting capability and control functionality. The system implementation will be completed in 2004.