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April 20, 2002

Hon Blanca S. Bayo
Director, Department of Records and Reporting
Florida Public Service Commission
4075 Esplanade Way
Tallahassee, Fl 32399-0870

In re. Docket 011605-EI

Dear Ms. Blanco;

I enclose the original and 15 copies of a pleading to be filed on behalf of FIPUG in the above styled docket.

Sincerely yours,

John W. McWhirter, Jr.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Review of investor-owned electric utilities' risk management policies and procedures.	))))	DOCKET NO. 011605-EI Filed:

FIPUG'S JOINDER IN REQUEST FOR STATUS CONFERENCE

The Florida Industrial Power Users Group responds to the request for a status conference delineating the issues to be resolved in this work shop and says:

1. In its response to Reliant's request for a status conference FPL joined by FPC alleged that when Reliant sought to compare capacity sharing to fuel cost it was engaging in "sophistry." FPL then referred to the "obsessions" of FIPUG and OPC. The allegations drove the undersigned fairly unsophisticated attorney to the dictionary to satisfy his obsession for knowing the truth. According to *Webster's Ninth New Collegiate Dictionary* sophists were ancient Greek wise men who engaged in "adroit, subtle and allegedly often specious reasoning." Sophistry is defined as "subtly deceptive reasoning or argumentation." An examination of the evolution of the utility risk free cost recovery mechanism sheds light on who may be attempting to engage in sophistry in this docket.

2. In 1972 the Florida Public Service Commission came to the aid of investor owned utilities by ***holding them harmless from all aspects of fuel cost risk***. The Commission guaranteed that the utilities would receive full cost recovery and shifted the total fuel cost risk to consumers. The fuel cost recovery mechanism was born.

3. In 1974 when the fuel cost of oil and gas burning generators was high and the fuel cost of nuclear or coal generated electricity was relatively low, the Florida Public Service Commission in a far sighted move recognized that costs to consumers could be reduced if utilities would share capacity. A state policy was developed to build an electric power transmission grid that would allow utilities to share their capacity. The Florida transmission grid and the Florida Broker system was

born to shave fuel costs by the most efficient use of the state's lowest cost generation. If one utility temporarily had surplus capacity that burned low cost fuel and the power from that capacity could be substituted for high fuel cost capacity of another utility the cost savings could be shared and everyone would benefit. The benefits of using efficient capacity were rewarded. Utilities were authorized to charge customers a GPIF (generating performance incentive factor) for operating efficiently.

4. In the early 1980s the Commission developed the "oil back out rule." This rule authorized utilities to surcharge customers fuel bills and use the proceeds to acquire and build capacity that used less expensive fuels. The Commission even retroactively allowed FP&L to remove the capital cost of a transmission line from base rates and receive accelerated cost recovery through the fuel clause. The endeavor was premised upon anticipated fuel cost savings. FPL surcharged customers $1 Billion to build the "coal by wire" transmission line from the Georgia border to Martin County in south Florida. A review of FPL's pleadings will not find an admission that it was engaging in sophistry when it used a fuel cost surcharge to recover the costs of transmission capacity to access Georgia based generating capacity or when a non fuel energy charge was used to cover the costs of the St Lucie nuclear plant because it would reduce fuel costs.

5. In 1978 congress developed national policies to back out dependence on foreign oil by promoting fuel cost savings through efficient capacity utilization. Among other policies, the Public Utility Regulatory Practices Act (PURPA) act encouraged non utility manufacturers to build electric generation using waste heat from their other processes.

6. After PURPA opened the gates to new developers generating plant technology improved dramatically. In 1980 the average generator in rate base burned 10,000 BTUs of fuel energy to produce a single kwh of electricity with an energy value of 3400 BTUS. Newly developed technology has improved generating efficiency to the degree that today's generators can produce a kwh of electricity burning less than 7000 BTUs of fuel. This amounts to a 30% reduction in the fuel consumed. The energy conversion or "heat rate" of older rate based generation is still very poor and

hovers at the 1980 level. There is an added benefit from the new technology. The more efficient generators burn cleaner fuel and reduce environmental cost.

7. The success of natural gas deregulation and improved generating technology advanced by PURPA caused congress to establish a national policy for wholesale electric deregulation. The Energy Policy Act of 1992 (EPAct92) created a competitive wholesale market for electricity and invited generation developers known as Independent Power Producers (IPPs) and Exempt Wholesale Generators (EWGs) to construct fuel efficient low cost generation. EPAct 92 and FERC's implementing incentives were designed to reduce the cost of electricity by creating increased efficient capacity in a competitive wholesale market. But these incentives backfired in Florida. Florida public utilities dominated a short supply market. While the new law removed the requirement that power be traded at cost in the wholesale market, the act left it up to the states to adopt polices to increase supply.

8. Even though IPPs building fuel efficient generation were encouraged nationally and by the Florida Commission, they were actively opposed by Florida investor owned utilities which controlled the supply of the state's generating capacity. Some IPPs came anyway because Section 210 of PURPA required utilities to buy power from IPPs and EWGs if they could produce power for less than the regulated utilities' avoided cost. Ironically they weren't allowed to build the most efficient generation unless they were under contract to supply it to a regulated utility at a price set by the utility.

9. After EPACT92 was eviscerated by the law of supply and demand in Florida. The Florida broker system was supplanted by utility trading departments engaging in confidential bilateral sales at rising market prices. The tight capacity supply and the dearth of competition to the utilities' generating units in the wholesale generation market drove prices to astronomical heights during peak periods. **The Commission once again came to the aid of utilities and shifted the total risk of purchased power to consumers.** The Capacity cost recovery clause was born. This year FPL will

collect $428 million and FPC will collect $336 million from consumers to cover the net cost of purchased power. Some purchased power comes from manufacturers and IPPs, but a large amount of the cost is the result of regulated utilities trading with one another and their own affiliated merchant power plants in Florida's capacity constrained market. There is a tremendous impact on the fuel and capacity cost recovery dockets, but without the entry of IPPs there is very little competition to reduce this price.

10. The further development of competition in the wholesale market, and the willingness of developers of independent power projects to devote their private capital to the wholesale enterprise, compete to enter pay-for-performance contracts, and bear the construction and operating risks that customers otherwise would shoulder for the life of a rate based unit, introduce an additional dimension to the subject of risk management. It appears that wholesale power, when included in a portfolio of resources is an important a risk management tool. FIPUG supports the idea of giving consideration to competitive generation as an important risk management opportunity.

11. What about "sophistry?" When the lawyer's arguments are examined with full knowledge of the facts sophists can frequently be identified. The evolution of regulatory policies over the past two decades make it readily apparent that fuel cost is governed to a great degree by the generating capacity that burns the fuel. It is therefore ludicrous to conclude that it is sophistry for a party to suggest fuel cost is affected by capacity. Capacity utilization is the very essence of fuel cost savings. While FIPUG counsel would never suggest that it might be sophistry for the attorneys representing FPL and FPC to argue that the selection of efficient capacity has nothing to do with fuel cost today in spite of their companies' argument to the contrary in the past, independent analysts might have less difficulty in identifying the sophists in this docket.

12. As to the obsessions of the OPC and FIPUG; this docket is a spin off from the fuel and purchased power cost recovery docket in which utilities sought to recover their risk management costs. The OPC was the first to recognize that the subject of risk management needs to be carefully explored because as seen above utilities have no fuel cost or purchased power risk. FIPUG believes

the OPC is correct. Any hedging done therefore by definition must be done exclusively for the benefit of customers. Never the less there is a potential problem. Utilities are not eleemosynary institutions. Today they are affiliated with utility holding companies. Regulated utilities are no longer simply buyers of fuel to hedge against fuel cost risk. They buy fuel from their affiliates. Regulated utilities and their affiliates are actively engaged in trading electricity, fuel, financial derivatives representing these commodities and other risky transactions in their responsibility to grow earnings for their holding company parent.

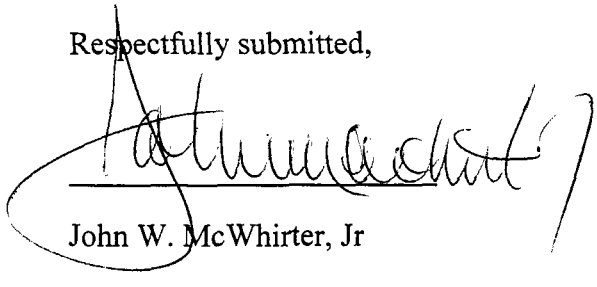
13. This workshop should explore what hedging is all about. Historically farmers and then other commodity purchasers used the technique known as hedging to reduce risk by finding a person willing to pay a fixed price today for a commodity to be delivered at a future time. There are numerous risks to be avoided, price risk, credit risk, weather risk, delivery risk, machine failure risk, transmission and pipeline capacity constraint risk, middle east war risk, and market manipulation risk among others. Risks vary based upon whether delivery of the commodity is on peak or off-peak, comes soon or is postponed. As commodity markets mature it quickly becomes apparent that buyers and sellers of the commodity have difficulty in arriving at a fair price for a commodity to be delivered in the future when there are so many unknown risks. This difficulty is resolved by the entry of middlemen who are willing to gamble by speculating on the risks involved. Some of these middlemen are wholesale traders, retail traders, basis traders, banks, brokers, market makers, power merchants, marketers and numerous others. They operate in the spot market or the forwards market through exchange traded derivatives, over the counter derivatives, physical derivatives, in secret bi-lateral deals or through publically traded exchanges. They engage in basis swaps, contract differences, swaptions, options, puts, calls, daily swing options trigger deals, EFPs and a multitude of creative financial derivatives to whet every speculators taste. Each speculator sets his profit based on the amount of risk assumed and gets out of the derivative contract as soon as it can be sold to another for a profit or to avoid further loss. The monetary value of the financial derivatives attributable to the underlying commodity can exceed the value of the commodity a hundredfold.

There is a great deal of money to be made or lost.

14. In this proceeding FIPUG is extremely interested in finding out why utilities which have no risk in the cost of the fuel and electricity they buy need further protection. FIPUG also wants to know who the players will be in the hedging transactions, what positions the utilities will play and the extent to which their affiliates will be involved, the impact on utility holding company earnings, the potential for gaming the system and whether consumers will obtain the profits as well as the losses from hedging transactions.

FIPUG strongly suggests that a Status Conference be convened to determine the parameters of this docket and recommends that risk management embrace the real world of electricity capacity trading which may be the single most important factor in risk management for Florida's future. The docket status conference should also establish the parameters for the work shop so that it will fully discover the risk management policies regulated utilities intend to follow. The work shop can serve as the basis for a rule to protect consumers from secret speculative derivative trading especially when trading is conducted between affiliated companies.

Respectfully submitted,



John W. McWhirter, Jr

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by United States mail this 20th Day of April, 2002 to the following:

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