

State of Florida



## Public Service Commission

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**-M-E-M-O-R-A-N-D-U-M-**

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**DATE:** July 10, 2006

**TO:** Director, Division of the Commission Clerk & Administrative Services (Bayó)

**FROM:** Office of the General Counsel (Keating)  
Division of Economic Regulation (Maurey)

**RE:** Docket No. 060038-EI – Petition for issuance of a storm recovery financing order, by Florida Power & Light Company.

**AGENDA:** 07/18/06 – Regular Agenda – Decision on Motion for Reconsideration – Oral Argument Requested

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Deason

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\GCL\WP\060038.RCM.DOC

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### Case Background

On May 30, 2006, the Commission issued Order No. PSC-06-0464-FOF-EI (“Financing Order”) by which it authorized pursuant to Section 366.8260, Florida Statutes (sometimes referred to herein as the “securitization law”), the issuance of up to \$708 million in storm-recovery bonds to be used by Florida Power & Light Company (“FPL”) to finance the after-tax equivalent of: (i) recovery of the estimated unrecovered balance of FPL’s 2004 storm-recovery costs as of July 31, 2006; (ii) recovery of FPL’s unrecovered prudently incurred storm-recovery costs related to the four named storms that affected its service territory in 2005; (iii) replenishment of FPL’s storm reserve to a level of approximately \$200 million; and (iv) recovery of the estimated upfront storm-recovery bond issuance costs.

Pursuant to the Commission's vote on this matter, all parties were provided a draft of the portions of the Financing Order related only to the financing of the amounts approved for recovery through storm-recovery bonds. All parties were provided notice of a meeting/conference call to discuss the draft. The meeting commenced on May 25, 2006, and was continued through May 26, 2006. In all, the parties met for approximately nine hours to discuss the draft order.

Pursuant to Section 366.8260(2)(b)1.b., Florida Statutes, parties to this proceeding were permitted to request reconsideration of the Financing Order within five days after the date of its issuance. As set forth in the Financing Order, requests for reconsideration of the Order were required to be filed by June 6, 2006. On June 6, 2006, FPL filed a motion for reconsideration and request for clarification as to specified portions of the Financing Order related to the issuance of storm-recovery bonds. FPL did not seek reconsideration or clarification of matters associated with the amount of storm-recovery costs or level of storm-recovery reserve authorized for recovery through storm-recovery bonds.

Along with its motion for reconsideration and request for clarification, FPL filed a request for oral argument.

The Commission has jurisdiction over this matter pursuant to Section 366.8260, Florida Statutes.

### **Discussion of Issues**

**Issue 1:** Should the Commission grant FPL's request for oral argument?

**Recommendation:** Yes. Oral argument may aid the Commission in evaluating the issues presented in FPL's motion for reconsideration and request for clarification. (Keating)

**Staff Analysis:** FPL requests oral argument in support of its motion for reconsideration and request for clarification of the Financing Order. In its request for oral argument, FPL states its belief that oral argument will be helpful to the Commission in evaluating the issues raised in its motion. Further, FPL states that: (1) the Office of Public Counsel and AARP support its request for oral argument; (2) the Florida Industrial Power Users Group and the Federal Executive Agencies do not oppose the request; (3) the Florida Retail Federation takes no position on the request; and (4) the Office of the Attorney General takes no position on the request at this time.

The Commission has typically granted requests for oral argument upon a finding that oral argument will assist the Commission in evaluating and resolving the issues presented in the underlying motion. Given the unique nature of the Financing Order, i.e., that it is the first financing order issued under Section 366.8260, Florida Statutes, staff believes that oral argument may aid the Commission in evaluating the issues presented in FPL's motion for reconsideration and request for clarification. Staff recommends that oral argument be limited to 10 minutes per side.

**Issue 2:** Should the Commission grant FPL's motion for reconsideration?

**Recommendation:** The Commission should grant FPL's request for reconsideration with respect to that portion of the Financing Order related to the allocation of partial payments. The Commission should deny FPL's motion for reconsideration in all other respects. (Keating, Maurey)

**Staff Analysis:**

**Standard of Review**

The standard of review for a motion for reconsideration is whether the motion identifies a point of fact or law which was overlooked or which the Commission failed to consider in rendering its Order. See Stewart Bonded Warehouse, Inc. v. Bevis, 294 So.2d 315 (Fla. 1974); Diamond Cab Co. v. King, 146 So.2d 889 (Fla. 1962); and Pingree v. Quaintance, 394 So.2d 161 (Fla. 1st DCA 1981). In a motion for reconsideration, it is not appropriate to reargue matters that have already been considered. Sherwood v. State, 111 So.2d 96 (Fla. 3rd DCA 1959) citing State ex. rel. Jaytex Realty Co. v. Green, 105 So.2d 817 (Fla. 1st DCA 1958). Furthermore, a motion for reconsideration should not be granted "based upon an arbitrary feeling that a mistake may have been made, but should be based upon specific factual matters set forth in the record and susceptible to review." Stewart Bonded Warehouse, Inc. v. Bevis, 294 So.2d 315, 317 (Fla. 1974).

**Items Subject to Motion for Reconsideration**

In its motion for reconsideration, FPL asks the Commission to reconsider six areas of the Financing Order. In this recommendation, staff addresses each point separately.

1. FPL asks the Commission to reconsider the last sentence of Finding of Fact ("FOF") 81. FOF 81 states:

We find that this True-Up Mechanism together with the broad based nature of the State Pledge set forth in Section 366.8260(11), Florida Statutes, constitute a guarantee of regulatory action for the benefit of investors in storm-recovery bonds, and we anticipate that stress case analyses will show that these features will serve to effectively eliminate for all practical purposes and circumstances any credit risk associated with the storm-recovery bonds (i.e., that sufficient funds will be available and paid to discharge all principal and interest obligations when due). We direct that this transaction be structured to achieve this result.

FPL asserts that the directive in the last sentence of this FOF was not proposed by any party to this proceeding, is not reflected in the record, and was not voted on by the Commission. Further, FPL contends it cannot comply with this directive. FPL asserts that the directive is vague and imprecise. FPL also asserts that to the extent that the guarantee of regulatory action through the true-up and the State Pledge do not serve to eliminate all credit risks, FPL cannot independently do so.

FPL contends that the investment community should and will decide based on the prospectus, the credit ratings assigned by rating agencies and their analysis, and other available information, whether the transaction has been structured to effectively eliminate credit risk. FPL asserts that neither it nor the Commission should substitute its judgment for that of investors through the adoption of this directive. FPL further claims that by ordering FPL to structure a risk free transaction, the Commission may make FPL liable to the bondholders and to others if the storm-recovery bonds are not paid on a timely basis.

FPL asks the Commission to delete the last sentence of FOF 81. As a first alternative, FPL suggests that the sentence be modified to direct that the transaction be structured “so that stress test analyses are at least sufficient to satisfy the requirements for ‘triple-A’ ratings from Moody’s, Fitch, and Standard and Poor’s, or to satisfy such more stringent requirements a determined appropriate by the Bond Team.” As a last alternative, FPL requests that the Commission clarify that the directive is not intended to constitute a payment guarantee on the storm-recovery bonds by FPL and that a violation of the directive will not give rise to any legal actions against FPL. Finally, FPL asks that the Commission state in the Financing Order that approval by the Bond Team of the transaction shall constitute conclusive proof that the transaction has been structured as required by the Financing Order.

Staff recommends that the Commission deny FPL’s request for reconsideration with respect to the last sentence of FOF 81. The Commission expressly found that the true-up mechanism, which was approved in the Financing Order as required by Section 366.8260(2)(b)2.e., Florida Statutes, together with the broad based nature of the State Pledge set forth in Section 366.8260(11), Florida Statutes, constitute a guarantee of regulatory action for the benefit of investors in storm-recovery bonds. Further, in light of the statutory features that create an extraordinary credit for these storm-recovery bonds, the Commission expressed its belief that the storm-recovery bond transaction can be structured such that stress case analyses will show that these features will serve to effectively eliminate for all practical purposes and circumstances any credit risk associated with the storm-recovery bonds. These findings were based on record evidence in this proceeding (TR 1164–1172). The directive expressed in the last sentence of FOF 81 simply requires FPL, exercising the flexibility it was granted in the Financing Order, to structure the transaction in a manner that takes full advantage of the extraordinary credit associated with the storm-recovery bonds. Staff believes that this directive is entirely consistent with the express findings noted above and thus consistent with the Commission’s vote.

At several points throughout its argument on this point, FPL misstates the Financing Order by suggesting that the Commission has directed FPL to structure a transaction in such a manner as to *eliminate all credit risks*.<sup>1</sup> The Financing Order does not provide such a directive. Instead, as quoted above, the Financing Order reflects the Commission’s finding that the true-up

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<sup>1</sup> Examples of FPL’s mischaracterization of this portion of the Financing Order include the following statements from its motion for reconsideration:

- “The transaction cannot be structured to be credit-risk free.” (p. 10) (Emphasis added.)
- “In addition, by ordering FPL to structure a credit risk-free transaction . . .” (p.13) (Emphasis added.)
- “. . . FPL requests that the Commission at least clarify that the direction to structure a credit-risk free transaction . . .” (p.13) (Emphasis added.)

mechanism and the features of the securitization law should “serve to effectively eliminate for all practical purposes and circumstances any credit risk associated with the storm-recovery bonds (i.e., that sufficient funds will be available and paid to discharge all principal and interest obligations when due).” (Emphasis added.) As noted above, this precise language is supported by record evidence. Further, no evidence was offered to rebut this language – after it was proposed through the testimony of Staff witness Joseph Fichera – by suggesting that there were any “practical circumstances” under which principal and interest would not be paid.<sup>2</sup> FPL witness Wayne Olson, in his prefiled rebuttal testimony, stated that this precise language reflected a true statement and that “it is hard to conceive of a scenario in which the bonds will not pay as agreed.” (TR 1501-1502; EXH 167, p. 6) In addition, the record shows that this precise language has been used in previous financing orders authorizing the issuance of ratepayer-backed bonds similar to storm-recovery bonds in other jurisdictions as well as in marketing materials for those bonds (TR 1167-1172).

The last sentence of FOF 81 directs FPL to structure this storm-recovery bond transaction to take full advantage of the extraordinary credit associated with the bonds. The sentence is supported by the record evidence and is consistent with the Commission’s vote. It does not direct FPL to structure the transaction in such a manner as to eliminate all credit risk and is not intended to establish FPL as a guarantor of payments on the storm-recovery bonds.

In sum, the Commission should deny FPL’s motion for reconsideration with respect to the last sentence of FOF 81 in the Financing Order. FPL has not identified a point of fact or law, set forth in the record and susceptible to review, that the Commission overlooked or failed to consider in rendering this portion of the Financing Order.

2. FPL asks the Commission to reconsider the last sentence of the fourth ordering paragraph on page 50 of the Financing Order. The ordering paragraph states:

ORDERED that FPL is authorized to impose, collect, and adjust from time to time (as described in this Order) a storm-recovery charge, which consists of a Storm Bond Repayment Charge and a Storm Bond Tax Charge, to be applied on a per kWh basis to all applicable customer classes over a period of approximately twelve years until the storm-recovery bonds are paid in full and all financing costs and other costs of the bonds have been recovered in full. Such storm-recovery charges shall be in amounts sufficient to guarantee the timely recovery of FPL’s

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<sup>2</sup> In its motion for reconsideration, FPL indicates that the prospectus for these storm-recovery bonds must contain a description of numerous “risk factors,” any one of which could result in a default in the timely payment of the bonds. As examples, FPL lists “acts of the Florida Legislature or the Florida commission required to address public emergencies,” “inaccurate forecasting of consumption,” “unanticipated customer delinquencies,” and “the bankruptcy of FPL.” FPL does not state that any of these circumstances are “practical circumstances” under which principal and interest may not be paid, nor were any of these circumstances offered in FPL’s rebuttal testimony as “practical circumstances” under which principal and interest may not be paid. As noted above, FPL did not rebut Staff witness Fichera’s testimony that the transaction could be structured such that the true-up mechanism and the State Pledge serve to effectively eliminate for all practical purposes and circumstances any credit risk associated with the storm-recovery bonds, and FPL witness Olson characterized this language as a true statement, adding that “it is hard to conceive of a scenario in which the bonds will not pay as agreed.”

storm-recovery costs and financing costs detailed in this Financing Order (including payment of principal and interest on the storm-recovery bonds).

FPL asserts that the last sentence of this ordering paragraph was not voted on by the Commission and that there is no record support for this language. Further, FPL contends it cannot guarantee that setting, collecting, and adjusting storm-recovery charges alone will guarantee timely payment of the storm-recovery bonds. FPL states that circumstances entirely outside its control, such as delinquencies caused by economic or regional emergencies, could prevent timely payment.

FPL asks the Commission to delete the last sentence of the ordering paragraph. In the alternative, FPL asks at a minimum that the Commission clarify that the sentence does not constitute a payment guarantee of the storm-recovery bonds by FPL.

Staff recommends that the Commission deny FPL's request for reconsideration with respect to the last sentence of the fourth ordering paragraph on page 50 of the Financing Order, which is quoted above. The sentence does no more than reflect the effect of the true-up mechanism approved in the Financing Order as required by the securitization law. FPL witness K. Michael Davis recognized this in his prefiled direct testimony (TR 455-457) where he discussed the nature of the true-up mechanism required by the law.

As noted by FPL witness Davis, Section 366.8260(2)(b)2.e., Florida Statutes, provides that the Commission must include in any financing order:

. . . a formula based mechanism for making expeditious periodic adjustments in the storm-recovery charges that customers are required to pay under the financing order and for making any adjustments that are necessary to correct for any overcollection or undercollection of the charges or to otherwise ensure the timely payment of storm-recovery bonds and financing costs and other required amounts and charges payable in connection with the storm-recovery bonds.

(Emphasis added.) Further, witness Davis noted the requirements of Section 366.8260(2)(b)4., Florida Statutes, with respect to adjustments made under the true-up mechanism:

Such adjustments shall ensure the recovery of revenues sufficient to provide for the payment of principal, interest, acquisition, defeasance, financing costs, or redemption premium and other fees, costs, and charges in respect of storm-recovery bonds approved under the financing order.

(Emphasis added.)

The last sentence of the ordering paragraph quoted above merely reflects the statutory requirements noted by FPL witness Davis with respect to the true-up mechanism. The sentence is supported by the record evidence and the securitization law and is entirely consistent with the Commission's vote approving FPL's proposed true-up mechanism. It is not accurate for FPL to state, as it does in its motion, that this sentence creates a "new requirement that FPL is seeing now for the very first time, embedded in [the Financing Order]." By its plain terms, the sentence

does not establish FPL as a guarantor of payments on the storm-recovery bonds, nor is it intended to do so.

In sum, the Commission should deny FPL's motion for reconsideration with respect to the last sentence of the fourth ordering paragraph on page 50 of the Financing Order. FPL has not identified a point of fact or law, set forth in the record and susceptible to review, that the Commission overlooked or failed to consider in rendering this portion of the Financing Order.

**3.** FPL asks the Commission to reconsider several portions of the Financing Order that specify the role of the Commission's financial advisor, in particular the provisions set forth in FOF 127 and the fifth ordering paragraph on page 56 of the Financing Order. FOF 127 states:

To ensure that customers are represented in the transaction process and that customers' interests in achieving the lowest cost objective will be served, we do not approve the review procedure originally proposed by FPL. Instead, we find that this Commission, as represented by a designated Commissioner, designated Commission staff, the Commission's financial advisor, and the Commission's outside legal counsel, shall be actively involved in the bond issuance on a day-to-day basis as part of a Bond Team that also includes FPL, its financial advisor, and its outside counsel, in all aspects of structuring, marketing, and pricing each series of storm-recovery bonds. This will allow for meaningful and substantive cooperation among FPL and the Commission and its representatives to achieve the lowest cost objective and to protect the interests of customers. Cooperation among FPL and the Commission will promote transparency in the storm-recovery bond pricing process, thereby promoting the integrity of the process and ensuring that the interests of customers are protected in all negotiations with underwriters and investors. In this regard, this Commission's financial advisor needs to be an active and visible participant in the actual pricing process in real time if we are to obtain maximum benefits for ratepayers.

The fifth ordering paragraph on page 56 states:

ORDERED that this Commission, as represented at each stage either jointly or separately by a designated Commissioner, designated Commission personnel, the Commission's financial advisor, and the Commission's outside legal counsel, as these representatives deem appropriate, shall be actively involved as part of a Bond Team with FPL, its financial advisor, and its outside counsel, in all aspects of the structuring, marketing, and pricing of each series of storm-recovery bonds to ensure that customers are represented in the transaction process and that the lowest cost objective is achieved. As a member of the Bond Team, the Commission's financial advisor will advise and represent the Commission on all matters relating to the structuring, marketing, and pricing of the storm-recovery bonds. Through its participation on the Bond Team, this Commission and its representatives will have an active and integral role in, and will participate fully and in advance in all plans and decisions relating to, the structuring, marketing, and pricing of the storm-recovery bonds as discussed in the body of this Order.



FPL contends that these provisions go beyond the Commission's vote and appear to delegate to the Commission's financial advisor ultimate control with respect to the day-to-day activities of the Bond Team and the terms and administration of its contract with the Commission. FPL asserts that the Commission's vote envisioned that the financial advisor would have only an advisory role on the Bond Team, but that the financial advisor's role is elevated in the Financing Order to something beyond that. Further, FPL asserts that the Financing Order does not place any restraints or limitations on the activities of the financial advisor that are eligible for recovery from storm-recovery bond proceeds. Finally, FPL contends that the Financing Order inappropriately provides that the Commission's financial advisor and outside legal counsel may represent the Commission as they alone deem appropriate in all matters related to structuring, marketing, and pricing of the storm-recovery bonds.

FPL asks that the Financing Order be amended "to include only the language reflected in the Staff Recommendation and voted on by the Commission" so that: (1) the Commission's financial advisor cannot act independently of Commission staff except in certain specifically identified circumstances; (2) the Commission will have ultimate control over the terms of its contracts with its financial advisor and outside counsel; and (3) the Commission's financial advisor and outside counsel will not be authorized to represent the Commission as they alone deem appropriate.

Staff recommends that the Commission deny FPL's request for reconsideration with respect to these portions of the Financing Order. FPL's motion for reconsideration is misguided on these points because the Financing Order does not permit the Commission's financial advisor and outside counsel to represent the Commission as they alone deem appropriate and quite clearly provides the Commission ultimate control over its contracts with these persons. Further, FPL's motion for reconsideration asks the Commission to restrict the role of its financial advisor and outside legal counsel beyond the level approved by the Commission. Staff believes that the portions of the Financing Order of which FPL seeks reconsideration are consistent with the Commission's vote.

a. Representation of Commission on Bond Team

As noted above, the Commission states at page 56 of the Financing Order (and also on page 7) that the Commission, "as represented at each stage either jointly or separately by a designated Commissioner, designated Commission personnel, the Commission's financial advisor, and the Commission's outside legal counsel, as these representatives deem appropriate," shall be actively involved as part of a Bond Team in all aspects of the structuring, marketing, and pricing of each series of storm-recovery bonds to ensure that customers are represented in the transaction process and that the lowest cost objective is achieved. In its motion for reconsideration, FPL interprets the language quoted above to authorize the Commission's financial advisor and outside legal counsel to determine by themselves what their role will be in the bond issuance process. The language is not intended to convey such authority. Instead, the language is intended to indicate that the Commission's representatives on the Bond Team will decide collectively – not individually – which Commission-designated members of the Bond Team will represent the Commission's interest on the Bond Team at each stage of the transaction process.

This language recognizes that time limitations and scheduling conflicts will likely preclude all of the Commission's designated Bond Team members from participating in every meeting, conference call, or other activity related to the structuring, marketing, and pricing of the bonds. The Commission's designated Bond Team members, either by necessity or by choice, may deem it appropriate for the Commission to be represented by only some of the designated Bond Team members at a particular stage or in particular aspects of the bond issuance process. The language quoted above allows the Commission's designated Bond Team members to collectively determine how to best represent the Commission throughout the bond issuance process without unduly delaying the process.

This language is consistent with the Commission's vote. At the May 15, 2006, Special Agenda Conference, the Commission voted to approve staff's recommendation regarding the appropriate level of regulatory oversight after issuance of the Financing Order, which stated in part that:

The ratepayers should be effectively represented throughout the proposed transaction. The Commission, its staff, its outside counsel, and its financial advisor, along with FPL, FPL's financial advisor, and its counsel should work in a collaborative process to ensure the structuring, marketing, and pricing of the storm recovery bonds result in the lowest costs consistent with market conditions and the terms of the financing order. The Commission should be represented primarily by its staff, who should be advised by the Commission's financial advisor and outside counsel.<sup>3</sup>

The Commission modified this recommendation to authorize a Commissioner to participate on the Bond Team to the degree chosen by that Commissioner.<sup>4</sup>

While the Commission indicated that it would be represented primarily by staff, it did not preclude representation by the Commission's financial advisor or outside counsel consistent with direction from the other Commission-designated members of the Bond Team. In fact, the recommendation approved by the Commission indicated extensive involvement by the Commission's financial advisor, including (1) review of transaction documents and offering documents<sup>5</sup>; (2) active participation in rating agency presentations<sup>6</sup>; (3) active and visible participation in the actual pricing process in real time<sup>7</sup>; (4) provision of a lowest cost certification one business day after pricing<sup>8</sup>; and (5) review of lowest cost certifications provided by FPL and the underwriter(s)<sup>9</sup>. Staff believes that the Commission intended to be able to use its financial advisor and outside counsel in a representative capacity as the Commission – through its designated Bond Team members – deems appropriate.

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<sup>3</sup> Staff Recommendation, May 8, 2006, p. 207.

<sup>4</sup> Transcript of Special Agenda Conference, pp. 138-140.

<sup>5</sup> Staff Recommendation, May 8, 2006, pp. 211-212.

<sup>6</sup> Staff Recommendation, May 8, 2006, p. 213.

<sup>7</sup> Staff Recommendation, May 8, 2006, p. 214.

<sup>8</sup> Staff Recommendation, May 8, 2006, pp. 181, 188, 209-210, and 214-215.

<sup>9</sup> Staff Recommendation, May 8, 2006, pp. 210 and 215.

b. Limitations of Recoverable Costs and Activities of Financial Advisor and Outside Counsel

Staff is puzzled by FPL's assertion that the Financing Order does not place any restraints or limitations on the activities of the financial advisor that are eligible for recovery from storm-recovery bond proceeds. Through the Financing Order, the Commission has clearly and explicitly stated its ultimate control over the services to be performed by its financial advisor and outside legal counsel and placed limits on the activities of those persons that are recoverable from storm-recovery bond proceeds.

As explained above, the Financing Order does not authorize the Commission's financial advisor and outside legal counsel to determine by themselves what their role will be in the bond issuance process. In addition, the Commission has made clear in several portions of the Financing Order that any costs associated with the Commission's financial advisor and its outside legal counsel will be recoverable from the proceeds of storm-recovery bonds only "to the extent such costs are eligible for compensation and approved for payment under the terms of such party's contractual arrangements with the Commission, as such arrangements may be modified by any amendment entered into *at the Commission's sole discretion . . .*"<sup>10</sup> (Emphasis added.) Finally, in the last ordering paragraph on page 56 of the Financing Order, the Commission made clear that "this Commission's financial advisor and its outside legal counsel will assist the Commission *at the Commission's sole discretion.*" (Emphasis added.) These provisions provide clear limitations on the costs associated with the Commission's financial advisor and outside counsel that may be recovered through the bond proceeds and clearly establish the Commission as having ultimate control over its contracts with these persons and thus the scope of activities to be performed by these persons.

In sum, the Commission should deny FPL's motion for reconsideration with respect to these portions of the Financing Order that specify the role of the Commission's financial advisor and outside counsel. FPL has not identified a point of fact or law, set forth in the record and susceptible to review, that the Commission overlooked or failed to consider in rendering this portion of the Financing Order.

4. FPL asks the Commission to reconsider the first and third sentences in FOF 105 in the Financing Order. FOF 105 states:

We find that FPL, the bookrunning underwriter(s), and this Commission's financial advisor each are required to certify that the structuring, marketing, and pricing of each tranche of storm-recovery bonds of each series in fact achieved the lowest cost objective. Floating rate bonds and interest rate swap agreements may be utilized to the extent agreed and approved by the Bond Team pursuant to the procedures set forth in Finding of Fact 136. If such a structure is utilized, the certificates delivered by FPL, the bookrunning underwriter(s), and this Commission's financial advisor should confirm that the net interest costs taking into account the interest rate swap agreement(s) and the risks associated with those agreements achieved the lowest cost objective.

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<sup>10</sup> See Financing Order, pp.26-27 (FOF 64), p. 56 (seventh ordering paragraph), and p. 57 (fifth ordering paragraph).

FPL asserts that the first sentence is inconsistent with the Commission's vote and is not in customers' best interests. FPL states that the Commission voted to require certifications that the actual structure, marketing, and pricing of the storm-recovery bonds resulted in the lowest storm recovery charges consistent with then-prevailing market conditions and the terms of the Financing Order and applicable law. FPL contends that requiring certifications that each tranche of storm-recovery bonds meets the lowest cost standard is a new and different standard under which decisions could be made that lower the costs of individual tranches of debt but raise the overall storm-recovery charges. FPL asserts that this standard does not allow for the recognition that there are trade-offs between upfront transaction costs (such as marketing) and obtaining lower interest rates on the bonds. FPL states that the Financing Order does not require certifications that the upfront issuance costs are lowest cost, only that the individual tranches achieved the lowest interest rate. FPL further asserts that the Commission's financial advisor will have no responsibility or incentive to control transaction costs under this standard.

FPL contends that the third sentence of FOF 105 was not approved by the Commission. FPL asserts that this sentence requires a separate certification related to interest rate swaps and that such certification requires a monetary calculation of the risks associated with such swaps. FPL contends that there is no objective way to place a monetary value on such risks.

FPL asks that the Commission reconsider and revise FOF 105 to require certifications that the actual structure, marketing, and pricing of the storm-recovery bonds resulted in the lowest storm recovery charges consistent with then-prevailing market conditions and the terms of the Financing Order and other applicable law.

Staff recommends that the Commission deny FPL's request for reconsideration with respect to FOF 105. In approving and adopting the relevant portions of the staff recommendation on the financing issues in this docket, the Commission voted to adopt a *lowest overall cost* approach for the actual costs of the storm-recovery bond issuance. At page 216, the staff recommendation stated:

Based on the evidence presented, staff believes that it is simply not possible to determine, in a review that takes place after issuance of the bonds and under the limited terms of participation suggested by FPL, whether the interest rates achieved on the bond issuance resulted in lowest overall costs consistent with market conditions at the time of pricing. Thus, staff recommends that the Commission, as an appropriate condition of the financing order, ensure its real time involvement in the pricing of bonds at the time of pricing and adopt a lowest cost approach under which FPL, the bookrunning underwriter(s) involved, and the Commission's financial advisor each individually certifies that lowest overall costs were achieved for the storm recovery bonds under then prevailing market conditions and the terms of the financing order.

This approach was intended to include not only interest rates but also to encompass upfront and ongoing costs associated with the bond issuance<sup>11</sup>, consistent with the standard set forth in Section 366.8260(2)(b)5., Florida Statutes, which requires the Commission to determine if “the actual costs of the storm-recovery bond issuance . . . resulted in the lowest overall costs that were reasonably consistent with market conditions at the time of issuance and the terms of the financing order.”

The staff recommendation also characterized the certifications to be provided by FPL, the bookrunning underwriter(s), and the Commission’s financial advisor, as certifications that the actual structuring, marketing, and pricing of the bonds resulted in the lowest storm recovery charges consistent with then-prevailing market conditions and the terms of the Financing Order and applicable law.<sup>12</sup> Staff sees no real distinction between “lowest overall cost” and “lowest storm recovery charges;” lowest overall cost should result in lowest storm recovery charges.

The approach adopted by the Commission was referred to throughout the Financing Order as the “lowest cost objective.” Under this approach, all costs associated with issuance of the bonds – interest rates, upfront issuance costs, ongoing costs, etc. – would be considered by FPL, the bookrunning underwriter(s), and the Commission’s financial advisor in rendering their separate certifications as to whether the lowest cost objective was achieved. The portions of FOF 105 that FPL asks the Commission to reconsider simply specify two of these items that those persons providing certifications must consider: (1) the structure, marketing, and pricing of each tranche of bonds; and (2) the net interest costs taking into account the interest rate swap agreement(s) and the risks associated with those agreements, if floating rate bonds and interest rate swap agreements.

The first item simply recognizes that these bonds will be marketed and sold in distinct tranches of varying maturities (FOF 93). By its plain language, the Financing Order does not require that each tranche be reviewed solely based on interest rate achieved but also in light of upfront and ongoing costs, including marketing costs.

The second item recognizes that some or all of the tranches may be structured and priced as floating rate bonds with interest rate swap agreements in place to protect customers against increasing interest rates. This flexibility is provided in the Financing Order (FOF 92). The Financing Order does not require FPL or any other person making a certification to place a monetary value on the risks associated with any interest rate swap agreement(s). Instead, the Order requires that the risks be taken into account along with the costs. Staff believes that this portion of the Financing Order is consistent with the Commission’s directive in FOF 91 that “the standard for this Order should be that the structuring, marketing, and pricing of storm-recovery bonds will result in the lowest storm-recovery charges that will achieve the lowest cost objective and the greatest possible customer protections.”

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<sup>11</sup> The Commission approved the staff recommendations in Issues 56-59 which stated that the Commission’s active participation in the transaction would best afford the Commission an opportunity to make an informed decision as to the reasonableness of upfront and ongoing issuance costs.

<sup>12</sup> Staff Recommendation, May 8, 2006, pp. 181 and 188.

In sum, the Commission should deny FPL's motion for reconsideration with respect to the first and third sentences of FOF 105 in the Financing Order. FPL has not identified a point of fact or law, set forth in the record and susceptible to review, that the Commission overlooked or failed to consider in rendering this portion of the Financing Order.

5. FPL asks the Commission to reconsider those portions of FOF 114b and 116 that require FPL to apply to its storm reserve all amounts it will receive for ongoing costs under the Servicing Agreement between FPL and the special purpose entity ("SPE") that issues the storm-recovery bonds and all amounts it will receive under the Administration Agreement between FPL and the SPE. FOF 114b states:

FPL's proposed form of Servicing Agreement provides for a \$350,000 servicer set-up fee to adapt FPL's existing systems to bill, collect, and process storm-recovery charges and set up the reporting function. The evidence shows that this amount represents an incremental cost to FPL. FPL's proposed form of Servicing Agreement also provides for an annual fee of up to .05 percent of the initial principal amount of the storm-recovery bonds for ongoing services. We find that the activities associated with the annual fee for ongoing services – billing and collecting storm-recovery charges, remitting funds to the SPE, and developing storm-recovery charges – are tightly bound with operations already performed by FPL in the normal course of business. FPL has not justified that the annual fee is necessary to cover any incremental costs to be incurred by FPL in performing ongoing services as servicer. Thus, we find that FPL shall apply to the Reserve all amounts it will receive under the Servicing Agreement for ongoing services.

FOF 116 states:

FPL's proposed form of Administration Agreement provides for a \$125,000 annual fee for performing the services required by the Administration Agreement. We find that FPL has not demonstrated that this annual fee is necessary to cover any incremental costs to be incurred by FPL in performing services as administrator. Thus, we find that FPL shall apply to the Reserve all amounts it will receive under the Administration Agreement for its services.

FPL asserts that these portions of the Financing Order overlook or fail to consider that preventing FPL from recovering incremental costs associated with servicing and administering the bonds pursuant to its agreements with the SPE could be detrimental to bankruptcy law opinions that are needed to accomplish the storm-recovery bond issuance. FPL asserts that it is uncontroverted in the record of this proceeding that FPL in its role as servicer and administrator must be adequately compensated for the services provided in order to create a bona fide arm's length relationship between FPL and the SPE and thereby preserve the integrity of the bankruptcy remote structure of the SPE. FPL states that in an arm's length transaction, it is presumed that parties will ensure that all actual costs can be recovered, this FPL must be paid an amount that is deemed to cover its actual costs of performing its servicing and administration functions during the term of the transaction.

FPL asks the Commission to amend the Financing Order to provide that any incremental costs associated with FPL's role as servicer or administrator of the storm-recovery bonds will be subject to recovery as part of FPL's retail base rate proceedings. FPL states that such an amendment would not prejudice the amount, reasonableness, or prudence of any incremental costs subject to approval by the Commission.

Staff recommends that the Commission deny FPL's request for reconsideration with respect to FOF 114b and FOF 116. First, it is clear that FPL will receive from the SPE the full amount of compensation provided for under the terms of the Servicing Agreement and Administration Agreement. In FOF 106 and FOF 107, the Commission recognized that this arm's length compensation is necessary to preserve the bankruptcy-remote structure of the SPE. The question answered in FOF 114b and FOF 116 was how much of these amounts FPL should be permitted to retain to cover actual incremental costs. Based on the evidence presented, the Commission determined that FPL had not demonstrated that the annual servicing and administration fees were necessary to cover any incremental costs to be incurred by FPL in performing ongoing services as servicer or administrator. Thus, the Commission determined that FPL should apply these fees as a credit to its storm reserve. Implicitly, the Commission determined that applying these fees to the storm reserve would not disturb the bankruptcy remote structure of the SPE. The Commission's expert outside counsel in this matter has indicated to staff that the Commission's decision will allow the transaction to comply with the necessary bankruptcy law requirements.

In sum, the Commission should deny FPL's motion for reconsideration with respect to FOF 114b and 116 in the Financing Order. FPL has not identified a point of fact or law, set forth in the record and susceptible to review, that the Commission overlooked or failed to consider in rendering this portion of the Financing Order.

6. FPL asks the Commission to reconsider its decision to require FPL to allocate partial payments received from customers first to the storm-recovery charge as set forth in FOF 77 and the second ordering paragraph on page 55 of the Financing Order. FOF 77 states:

To protect the interests of customers, we find that partial payments should be allocated first to the Storm Bond Repayment Charge, including any past-due Storm Bond Repayment Charge.

The second ordering paragraph on page 55 of the Financing Order states:

ORDERED that, to protect the interests of customers, partial payments shall be allocated first to the Storm Bond Repayment Charge, including any past-due Storm Bond Repayment Charge, unless, pursuant to the process set forth in Finding of Fact 136, it is determined by the Bond Team that such allocation would result in undue delay and cost.

FPL asserts that there is no record evidence to support FOF 77 and the associated ordering paragraph. FPL states that the only evidence on the subject of allocation of partial payments is found in the direct testimony of FPL witness Davis, which provides "that partial payments will be allocated to Storm Bond Repayment Charges in the same proportion that such

charges bear to the total bill.” Further, FPL asserts that FOF 77 will result in substantial cost and delay in implementing the storm charge. FPL states that its billing system allocates customer payments on pro-rata basis and this system would require substantial modification to accommodate the requirement of FOF 77. FPL estimates that the necessary rewrite of its payment application system would cost at least \$1.5 million and delay implementation of the storm-recovery charges by up to a year. FPL states that none of these costs were included in its estimate of upfront issuance costs in this docket and would need to be recovered through a charge against its storm reserve or some other form of incremental recovery. In addition, FPL contends that the application of payments on the priority basis set forth in FOF 77 could make it more difficult and expensive to maintain the necessary bankruptcy and lien opinions required by the rating agencies. FPL contends that while the related ordering paragraph allows a pro-rata application of funds if the Bond Team determines that a priority application will result in undue delay and cost, leaving such a determination to the Bond Team is not appropriate given the lack of record support.

FPL asks the Commission to include a pro rata allocation of partial payments in its order on reconsideration.

Staff recommends that the Commission grant FPL’s request for reconsideration with respect to FOF 77 and the second ordering paragraph on page 55 of the Financing Order. Staff agrees that the only evidence on the subject of allocation of partial payments is FPL witness Davis’ direct testimony that partial payments should be allocated to storm-recovery charges in the same proportion that such charges bear to the total bill. Thus, staff recommends that FOF 77 be amended to read as follows:

77. We find that partial payments shall be allocated to the Storm Bond Repayment Charge in the same proportion that such charge bears to the total bill.

Similarly, staff recommends that the second ordering paragraph on page 55 of the Financing Order be amended as follows:

ORDERED that the only evidence on the subject of allocation of partial payments is found in the direct testimony of FPL witness Davis, which provides “that partial payments will be allocated to Storm Bond Repayment Charges in the same proportion that such charges bear to the total bill.”

In sum, the Commission should grant FPL’s motion for reconsideration with respect to FOF 77 and the second ordering paragraph on page 55 of the Financing Order. In rendering these portions of the Financing Order, the Commission overlooked the fact that these portions of the Order were not supported by record evidence. The Commission should amend the Financing Order to reflect the finding and ordering paragraphs set forth above.



**Issue 3:** Should the Commission grant FPL's motion for clarification?

**Recommendation:** The Commission should grant in part and deny in part FPL's motion for clarification as set forth in the Staff Analysis. (Keating, Maurey)

**Staff Analysis:** In its motion for clarification, FPL asks the Commission to clarify four areas of the Financing Order. In this recommendation, staff addresses each point separately.

1. FPL asks the Commission to “clarify that certain language in the Financing Order may reflect conclusions and judgments of the Commission and not the Company and that the inclusion of any such statement in the offering materials must be consistent with the duties and potential liabilities of the issuer and FPL under federal securities laws.”

FPL notes that the Commission has reached certain legal conclusions in the Financing Order that are intended to enhance the possibility of obtaining favorable risk weighting treatment for the bonds by foreign regulators. FPL also notes that the Commission has included in the Financing Order language describing the credit qualities and credit mechanisms supporting the storm-recovery bonds. FPL states that it anticipates the Commission, upon advice of its financial advisor, will request that certain of these statements be included in the prospectus and other marketing materials for the bonds.

FPL asks the Commission to clarify that to the extent the Commission or its advisor request such statements – or any other statements – be included in the offering documents, FPL shall be entitled to reflect such statements as statements of the Commission, not FPL, and to include such statements as the issuer, in its sole discretion, “believes to be consistent with its duties and obligations under applicable securities law and as FPL, as the ‘control person’ believes in its sole discretion will not subject itself to undue potential liability.”

Staff recommends that the Commission deny FPL's request for clarification on this point. The Commission made no findings with respect to what statements should be included in the prospectus and other marketing materials for the storm-recovery bonds. Thus, there is nothing in the Financing Order to clarify in this regard. The Commission instead approved the creation of a Bond Team responsible for working cooperatively to, among other things, educate and expand the market for these bonds to ensure that the lowest cost objective is achieved (FOF 127 and FOF 132). In other words, the Commission gave the Bond Team responsibility to work through the details necessary to implement its Order, i.e., to establish marketing materials and methods for the bonds to ensure achievement of the lowest cost objective. In addition, the Commission established a dispute resolution process whereby any issues that the Bond Team is unable to resolve to their mutual satisfaction will be presented in writing to the Prehearing Officer for resolution, subject to de novo review by the full Commission (FOF 136).

In providing the Bond Team this responsibility, the Commission acknowledged that achieving the lowest cost objective also meant complying with applicable law. On page 6 of the Financing Order, the Commission defined the lowest cost objective as “ensuring that the structuring, marketing, and pricing of storm-recovery bonds will result in the lowest storm-recovery charges *consistent with (i) the terms of this Financing Order and applicable law and*

(ii) the prevailing market conditions at the time of the offering and pricing of the storm-recovery bonds.” (Emphasis added.)

FPL’s request for clarification asks the Commission effectively to remove the prospectus and other offering documents from the collaborative Bond Team process established in the Financing Order and to grant FPL and its affiliated SPE “sole discretion” to determine which statements may be included in these documents. Such action would clearly go beyond a simple clarification; it would gut portions of the consumer protections that the Commission intended through establishment of the Bond Team process and its representation on the Bond Team. Thus, staff believes that FPL’s request is at odds with the Commission’s vote and should be denied.

In sum, staff recommends that the Commission deny FPL’s motion for clarification on this point. Consistent with its vote and Financing Order, the Commission should require the Bond Team to establish offering documents and marketing methods to ensure achievement of the lowest cost objective. Any unresolved dispute concerning the accuracy, legal implications, and marketing implications of specific language that is actually proposed for inclusion in the offering documents should be presented in writing to the Prehearing Officer for resolution, subject to de novo review by the full Commission.

2. FPL asks the Commission to clarify that the Commission has the discretion to allow the storm-recovery bonds to be issued without a lowest overall cost certification from the Commission’s financial advisor if the Commission believes that it is in the customer’s best interests to do so or determines that the financial advisor’s certificate has been unreasonably withheld. Otherwise, FPL asserts, the financial advisor could hold up the issuance of the bonds irrespective of the Commission’s preference.

This issue is addressed in FOF 135 and in the first ordering paragraph on page 58 of the Financing Order, which contain essentially identical language. FOF 135 states:

If this Commission determines that all required certifications have been delivered and the transaction complies with applicable law and the financing order, the transaction proceeds without any further action of this Commission. However, if this Commission determines that the transaction fails to comply with applicable law or this Financing Order, or if FPL, the bookrunning underwriter(s), or this Commission’s financial advisor is unable or unwilling to deliver the required certifications in a form acceptable to this Commission, *we retain discretion to issue an order to stop the transaction.* We will not issue an order to stop the transaction for any other reason, for example, a change in market conditions after the moment of pricing.

(Emphasis added.)

Staff believes the highlighted language above makes clear that the Commission has provided itself the discretion to allow the storm-recovery bonds to be issued in the absence of a certification from FPL, the bookrunning underwriter(s), or its financial advisor. Further, the

Financing Order is clear that the Commission must affirmatively issue a stop order if it wishes to stop the transaction. The last ordering paragraph on page 59 of the Financing Order reads:

ORDERED that, if the Commission does not, prior to 5:00 p.m. Eastern Time on the third business day after pricing, issue an order finding that the proposed issuance does not comply with the terms of this Financing Order and applicable law, this Commission, without the need for further action and pursuant to our authority under this Financing Order, will affirmatively and conclusively be deemed to have (i) authorized FPL and an SPE to execute the issuance of the proposed series of storm-recovery bonds on the terms set forth in the Issuance Advice Letter, and (ii) approved FPL's recovery of the upfront bond issuance costs proposed to be financed from the proceeds of the storm-recovery bonds subject to review pursuant to Section 366.8260(2)(b)5., Florida Statutes.

Given the language already present in the Financing Order, staff believes the clarification sought by FPL is unnecessary. Although the Commission has provided itself the discretion to allow the storm-recovery bonds to be issued in the absence of a lowest overall cost certification from FPL, the bookrunning underwriter(s), or its financial advisor, staff believes the members of the Bond Team should work through the collaborative process established in the Financing Order to ensure that these parties are able to render the lowest cost certifications described in the Order.

**3.** FPL asks the Commission to clarify that FPL is not required to deposit to the storm reserve all moneys received pursuant to the Servicing Agreement and Administration Agreement between FPL and the SPE. FPL states that the staff recommendation approved by the Commission provided that the full amount of the annual servicing and administration fees received by FPL be applied to the storm reserve. FPL asserts that the Financing Order should provide that FPL shall not be required to apply to the storm reserve amounts it will receive under these agreements to the extent they reflect amounts paid by FPL to other parties.

FPL requests clarification that it is required to apply to its storm reserve only the annual servicing and administration fees received pursuant to its Servicing and Administration Agreements with the SPE, but not other amounts such as reimbursements from the SPE for amounts paid to third parties by FPL on the SPE's behalf, including SEC filing fees and audit fees. Otherwise, FPL asserts, this could jeopardize the necessary bankruptcy opinions discussed under Issue 2, above, because these expenses would be paid by FPL on behalf of the SPE without reimbursement, which is inconsistent with an arm's length transaction.

The intent of the staff recommendation, which was approved by the Commission, was not to necessarily require that all amounts received under the Servicing and Administration Agreements be applied to the storm reserve. Rather, staff recommended only that the annual fees for ongoing services collected under these agreements (.05 percent of the initial principal amount under the Servicing Agreement and \$125,000 under the Administration Agreement) should be applied to the storm reserve. To more accurately reflect the Commission's vote, staff recommends that FOF 114b and FOF 116 be amended to read as follows:

114.b. FPL's proposed form of Servicing Agreement provides for a \$350,000 servicer set-up fee to adapt FPL's existing systems to bill, collect, and process

storm-recovery charges and set up the reporting function. The evidence shows that this amount represents an incremental cost to FPL. FPL's proposed form of Servicing Agreement also provides for an annual fee of up to .05 percent of the initial principal amount of the storm-recovery bonds for ongoing services. We find that the activities associated with the annual fee for ongoing services – billing and collecting storm-recovery charges, remitting funds to the SPE, and developing storm-recovery charges – are tightly bound with operations already performed by FPL in the normal course of business. FPL has not justified that the annual fee is necessary to cover any incremental costs to be incurred by FPL in performing ongoing services as servicer. Thus, we find that FPL shall apply to the Reserve the annual fee specified in the Servicing Agreement for ongoing services.

116. FPL's proposed form of Administration Agreement provides for a \$125,000 annual fee for performing the services required by the Administration Agreement. We find that FPL has not demonstrated that the \$125,000 annual fee is necessary to cover any incremental costs to be incurred by FPL in performing services as administrator. Thus, we find that FPL shall apply to the Reserve the \$125,000 annual fee specified in the Administration Agreement for its services.

4. FPL asks the Commission to clarify the portion of the Financing Order addressing the authorized investments for moneys in the General Subaccount, Capital Subaccount, and Excess Funds Account. Citing pages 10 and 11 and FOF 112, FPL states that the Financing Order requires these moneys to “be invested by the Indenture trustee in short-term high-quality investments with minimum management and other fees.” FPL asks the Commission to clarify that this requirement is not intended to constrain the Bond Team to consider only management and other fees in selecting the Indenture trustee. FPL notes that the selection of the Indenture trustee will be the subject of a competitive solicitation conducted by the Bond Team and will include evaluation of all of the costs of the trustee as well as potential quality of service.

This subject is addressed in FOF 129 and the last ordering paragraph on page 57 of the Financing Order, which contain essentially identical language. FOF 129 states:

Subject to the procedures set forth in Finding of Fact 136, the Bond Team shall oversee the development of the competitive solicitation and selection of underwriters, underwriters' counsel, and other transaction participants other than issuer's counsel to ensure that the process is truly competitive, will provide the greatest value for ratepayers, and will result in the selection of transaction participants that have experience and ability to achieve the lowest cost objective.

Staff believes this language makes clear that any transaction participants selected by the Bond Team, including the Indenture trustee, must be selected not just on the basis of a particular fee or cost associated with the service provider, but on the basis of whether selection of the service provider will provide the greatest value for ratepayers, taking into consideration the entire cost involved and the experience and ability (quality) of the service provider. Given the language already present in the Financing Order, staff believes the clarification sought by FPL is unnecessary.

Docket No. 060038-EI

Date: July 10, 2006

**Issue 4:** Should this docket be closed?

**Recommendation:** No. Consistent with the Financing Order, this docket should remain open through completion of this Commission's review of the actual costs of the storm-recovery bond issuance conducted pursuant to Section 366.8260(2)(b)5., Florida Statutes. (Keating)

**Staff Analysis:** Consistent with the Financing Order, this docket shall remain open through completion of this Commission's review of the actual costs of the storm-recovery bond issuance conducted pursuant to Section 366.8260(2)(b)5., Florida Statutes.