

FPL Group, Inc., P. O. Box 14000, Juno Beach, Florida 33408-0420

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Director of Major Projects and Technical Activities Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116 Director@fasb.org

Re: Exposure Draft, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities"

Dear Sir:

FPL Group, Inc. (FPL Group) is pleased to respond to the Exposure Draft on the amendment of Statement 133 on Derivative Instruments and Hedging Activities. FPL Group is a public utility holding company. Its operations are primarily conducted through Florida Power & Light Company, one of the largest investor-owned electric utility companies in the nation, serving about half the population of Florida. FPL Group also owns and operates independent power facilities through its unregulated power generation subsidiary, FPL Energy, LLC.

We support the Board's decision to amendment FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities" (FAS 133) to incorporate the guidance contained in certain implementation issues for FAS 133. In particular, we appreciate the Board's efforts in Implementation Issue C15 to develop a framework whereby normal power purchase and sale contracts used in the electric energy industry can qualify for the normal purchases and normal sales exception. In applying the guidance in C15 during the second quarter of 2002, we discovered that certain "normal" long-term contracts for the physical delivery of power from our power plants may still not qualify for the normal exception. This is a result of the Board's addition of language to the final version of C15 to require that the price based on an underlying be clearly and closely related to the electricity being sold or purchased. Specifically, our concerns are with contracts which have a component of their price indexed to the Consumer Price Index (CPI) and certain contracts with Qualifying Facilities (described below) that are based on a standard offer price which may be indexed to a fuel other than that used in the plant.

Implementation issue No. C11 provides guidance in determining whether an underlying is clearly and closely related to the asset being sold. Overall, the Board's conclusions related to what constitutes *clearly and closely related* are based on an "ingredient" or "direct factor" in production notion. One example given in Implementation Issue No. C11 indicates that forward purchases and sales agreements that include pricing provisions that contain pricing adjustments due to changes in the rate of inflation, such as CPI, are not eligible for the normal purchases and

sales exception because CPI is not an ingredient or a direct factor in the production of the commodity. Rather, the Board believes that the CPI is a broad market index that reflects the general level of price changes of certain items in the economy as a whole and is not a direct factor in the production of the particular commodity being purchased or sold. However, predominantly fixed price power contracts, with that fixed price or components of that price designed to adjust with inflation in order to better match changes in costs incurred to produce the power, are common in the energy industry. This is particularly common in power sales contracts from plants that do not burn a fossil fuel (which is typically the primary cost of production), but generate electricity from renewable resources, such as wind.

FPL Energy is the nation's largest owner and operator of wind generation, with more than 1,400 net-megawatts of capacity. Five new wind power projects were completed in 2001, which was approximately 50 percent of the wind power installed in the United States during the year. As of December 31, 2001, approximately 28% of FPL Energy's generating portfolio was powered by wind. Essentially all of FPL Energy's wind electricity contracts contain pricing adjustments based on the CPI index. A literal interpretation of the current FAS 133 rules would preclude these contracts from receiving the normal purchase and sales treatment due to the CPI adjuster. We contend that CPI for wind contracts is an appropriate price adjuster as the costs of production in wind power generation (labor and operating and maintenance expenses) are expected to be driven by inflation.

Application of the *clearly and closely related* requirement has also called into question the normal purchases and sales treatment for certain of our contracts involving Qualifying Facilities. Qualifying Facilities came into existence due to the Public Utility Regulatory Policy Act, 1978 (PURPA). Section 210 of PURPA was designed to encourage non-utilities to generate electric power. These non-utilities or Independent Power Producers (IPPs), operating as Qualifying Facilities (QFs), upon meeting certain criteria, were exempt from most utility regulation. To ensure that IPPs had a stable environment in which to operate in, they are given several protections by the PURPA:

- (1) QFs have access to transmission facilities so they could sell to any purchasing utility, and
- (2) The host utility is required to purchase all power generated by a QF located in its service territory at the utility's incremental or avoided cost. Avoided cost varies from state to state, but in general, is the price that the utility would have to pay for the next kilowatt of power generated at its own facility, or at the next incremental facility planned to be built, including the utility's return on capital and projection of energy prices. As a result, energy payments in QF contracts are indexed to the fuel costs avoided by the host utility rather than the fuel actually burned by the QF.

Again, a literal interpretation of Implementation Issue No. C11 would indicate that QF contracts with prices indexed to the host utility's avoided cost are, in many cases, not eligible for the normal purchases and normal sales exception. For example, we have an ownership interest in a QF which burns wood to produce electricity. However, the avoided cost for the utility is based on coal generation. Avoided cost pricing is a common pricing convention for QF contracts and represents the standard offer price of electricity for QFs in a given region. We believe that these contracts should not be precluded from meeting the normal purchases and normal sales exception due to the fact that the pricing essentially was the price of electricity at the time of execution.

We respectfully request that the Board consider this argument and clarify its position in the proposed amendment to FAS 133.

The concerns expressed above relate to specific circumstances where very "normal" contracts in the energy industry could be required to be marked to market. As we have expressed in past letters to the Board regarding FAS 133, we continue to have an overall concern that long term contracts for the physical delivery of power generated in our power plants should not be accounted for as derivative instruments. Marking these contracts to market distorts the earnings process for contracts that require performance over five to twenty years in the future. Although, financial models can be developed to predict market values in the future, these values are simply estimates and may not be a fair and accurate representation of the actual market values in the future since no developed markets exist for extended periods in the future. We ask the Board to remain diligent to ensure that contracts for physical delivery of non-financial assets in quantities to be used or sold in the ordinary course of business be eligible for the normal purchases and normal sales exception.

We thank you for the opportunity to respond to this Exposure Draft. Your consideration of our comments is greatly appreciated.

Sincerely,

Controller and Chief Accounting Officer