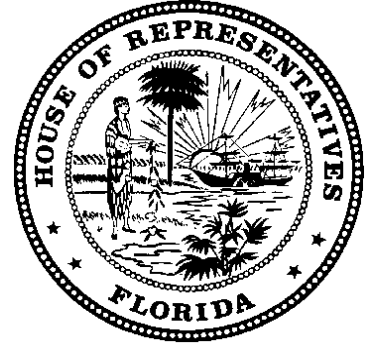


**ANDY GARDINER**  
President of the Senate



**STEVE CRISAFULLI**  
Speaker of the House



# **Joint Legislative Auditing Committee**

**Senator Joseph Abruzzo, Chair**  
**Representative Daniel Raulerson, Vice Chair**

**Meeting Packet**  
Monday, March 30, 2015  
9:00 A.M. to 12:00 P.M.  
301 Senate Office Building

**AGENDA**  
**JOINT LEGISLATIVE AUDITING COMMITTEE**

**DATE: Monday, March 30, 2015**

**TIME: 9:00 a.m. to Noon**

**PLACE: Room 301, Senate Office Building**

**MEMBERS:**

**Senator Joseph Abruzzo, Chair**

**Representative Daniel D. Raulerson, Vice Chair**

**Senator Lizbeth Benacquisto**

**Senator Rob Bradley**

**Senator Audrey Gibson**

**Senator Wilton Simpson**

**Representative Debbie Mayfield**

**Representative Amanda Murphy**

**Representative Ray Rodrigues**

**Representative Cynthia Stafford**

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The Committee is expected to conduct interviews and appoint the next Auditor General

Presentation of the Auditor General's audit of the Florida Municipal Power Agency (FMPA)

Presentation of TaxWatch's FMPA report (if available)

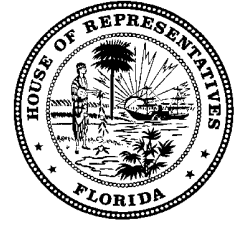


**ANDY GARDINER**  
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**THE FLORIDA LEGISLATURE**  
**JOINT LEGISLATIVE AUDITING COMMITTEE**



Senator Lizbeth Benacquisto  
Senator Rob Bradley  
Senator Audrey Gibson  
Senator Wilton Simpson

**Senator Joseph Abruzzo, Chair**  
**Representative Daniel D. Raulerson, Vice Chair**

Representative Debbie Mayfield  
Representative Amanda Murphy  
Representative Ray Rodrigues  
Representative Cynthia Stafford

## **Final Candidates for the Auditor General**

### **Sam M. McCall**

Sam McCall has been employed by Florida State University as the Chief Audit Officer since April 2013. He previously was employed by the City of Tallahassee as the City Auditor for 13 years and by the Auditor General for 30 years. He served as a Deputy Auditor General for 13 years.

Mr. McCall has been licensed as a Florida CPA since September 1975 (certificate # AC0005187). He is also a Chartered Global Management Accountant, Certified Government Auditing Professional, Certified Government Financial Manager, Certified Internal Auditor, and a Certified Inspector General.

### **Sherrill F. Norman**

Sherrill Norman has been employed by the Auditor General for the past 25 years. Since September 2012 she has served as the Deputy Auditor General for the State Government Audits Division.

Ms. Norman has been licensed as a Florida CPA since April 1992 (certificate # AC0024154).

### **Kathryn D. Walker**

Kathryn Walker has been employed by the Auditor General for the past 24 years. Since April 2006 she has served as an Audit Manager in the State Government Audits Division.

Ms. Walker has been licensed as a Florida CPA since April 1992 (certificate # AC0024025).

# The Florida Legislature

## Auditor General

**Job Title:**

Auditor General

**General Summary:**

The Auditor General is appointed by a majority vote of the Joint Legislative Auditing Committee, subject to confirmation by both houses of the Legislature. The Auditor General is required to take and subscribe to the oath of office required of all state officers by the State Constitution. The Auditor General serves at the pleasure of the Legislature and may be removed from office at any time by a majority vote of both houses of the Legislature. The person appointed will be responsible for a budget in excess of \$35 million and a staff of approximately 350. For statutory duties, see Sections 11.42, 11.45, and 11.47, Florida Statutes. The Auditor General's website is located at <http://www.myflorida.com/audgen/index.htm>. The position is based in Tallahassee and the appointment is expected to begin on July 1, 2015.

**Examples of Work Performed:**

Directs the activities of Auditor General staff as prescribed in Chapter 11, Florida Statutes. This includes conducting financial audits, operational audits, information technology audits, performance audits, and attestations.

Provides independent, unbiased, objective information on the fiscal integrity of State government and other governmental entities, the public resources raised, and the purposes for which they were spent.

Adopts rules, in consultation with the Board of Accountancy, for the form and conduct of financial audits of local governmental entities, district school boards, charter schools, and certain corporations performed by independent certified public accountants in the State.

Participates in various State and National professional accounting and auditing organizations in order to provide input and influence accounting and auditing standards and procedures as they relate to and affect State and local government entities.

Performs other related duties as required.

**Minimum Qualifications:**

Must have been certified under the Public Accountancy Law in Florida for at least 10 years and have at least 10 years experience in an accounting or auditing related field.

**Preferred Qualifications:**

- Experience in governmental accounting and auditing.
- Experience in managing all, or part of, an organization that conducts audits.
- Up-to-date knowledge of current governmental accounting and auditing standards.

**Salary:**

Commensurate with education, skills, and experience. Excellent employee benefits package.

**Application Deadline:**

5:00 p.m., Monday, March 16, 2015.

*Applications received after the deadline will not be accepted.*

**Submission of Application:**

Qualified applicants should submit a resume, [The Florida Legislature Employment Application](#), the [Supplemental Application for Position of Auditor General](#), and a copy of college transcripts. The applications may be completed online. They must be printed, signed, and submitted with the resume and college transcripts by mail or in person to:

Kathy DuBose  
c/o Barbara Gleasman  
Office of Human Resources  
111 West Madison Street  
Room 701, Claude Pepper Building  
Tallahassee, Florida 32399-1400

Candidates for an interview before the full Joint Legislative Auditing Committee will be subjected to a background investigation by the Florida Department of Law Enforcement. Additional personal information will be required to be submitted. Candidates will be responsible for their own travel expenses.

**Accommodation for Disability:**

If an accommodation is needed for a disability, please notify Human Resources at (850) 488-6803.

## **Florida Statutes**

The following two sections of Florida Statutes are provided for your convenience. Although other sections also include language related to the responsibilities of the Auditor General, these are the primary sections.



#### **11.42 The Auditor General.—**

(1) The Auditor General appointed in this section is the auditor that is required by s. 2, Art. III of the State Constitution.

(2) The Auditor General shall be appointed to office to serve at the pleasure of the Legislature, by a majority vote of the members of the Legislative Auditing Committee, subject to confirmation by both houses of the Legislature. At the time of her or his appointment, the Auditor General shall have been certified under the Public Accountancy Law in this state for a period of at least 10 years and shall have had not less than 10 years' experience in an accounting or auditing related field. Vacancies in the office shall be filled in the same manner as the original appointment.

(3)(a) To carry out her or his duties the Auditor General shall make all spending decisions within the annual operating budget approved by the President of the Senate and the Speaker of the House of Representatives. The Auditor General shall employ qualified persons necessary for the efficient operation of the Auditor General's office and shall fix their duties and compensation and, with the approval of the President of the Senate and the Speaker of the House of Representatives, shall adopt and administer a uniform personnel, job classification, and pay plan for such employees.

(b) No person shall be employed as a financial auditor who does not possess the qualifications to take the examination for a certificate as certified public accountant under the laws of this state, and no person shall be employed or retained as legal adviser, on either a full-time or a part-time basis, who is not a member of The Florida Bar.

(4) The Auditor General, before entering upon the duties of the office, shall take and subscribe the oath of office required of state officers by the State Constitution.

(5) The appointment of the Auditor General may be terminated at any time by a majority vote of both houses of the Legislature.

(6)(a) The headquarters of the Auditor General shall be at the state capital, but to facilitate auditing and to eliminate unnecessary traveling the Auditor General may establish field offices located outside the state capital. The Auditor General shall be provided with adequate quarters to carry out the position's functions in the state capital and in other areas of the state.

(b) All payrolls and vouchers for the operations of the Auditor General's office shall be submitted to the Chief Financial Officer and, if found to be correct, payments shall be issued therefor.

(7) The Auditor General may make and enforce reasonable rules and regulations necessary to facilitate audits which she or he is authorized to perform.

(8) No officer or salaried employee of the Office of the Auditor General shall serve as the representative of any political party or on any executive committee or other governing body thereof; serve as an executive, officer, or employee of any political party committee, organization, or association; or be engaged on behalf of any candidate for public office in the solicitation of votes or other activities in behalf of such candidacy. Neither the Auditor General nor any employee of the Auditor General may become a candidate for election to public office unless she or he first resigns from office or employment. No officer or salaried employee of the Auditor General shall actively engage in any other business or profession or be otherwise employed without the prior written permission of the Auditor General.

(9) Sections 11.25(1) and 11.26 shall not apply to the Auditor General.

History.—s. 3, ch. 67-470; s. 3, ch. 69-82; s. 1, ch. 86-217; s. 1, ch. 91-162; s. 1, ch. 94-322; s. 1308, ch. 95-147; s. 2, ch. 95-395; s. 24, ch. 96-318; s. 1, ch. 97-2; s. 71, ch. 97-190; s. 1, ch. 99-4; s. 2, ch. 99-333; s. 14, ch. 2001-266; s. 6, ch. 2003-261.

**11.45 Definitions; duties; authorities; reports; rules.—**

(1) DEFINITIONS.—As used in ss. 11.40-11.51, the term:

(a) "Audit" means a financial audit, operational audit, or performance audit.

(b) "County agency" means a board of county commissioners or other legislative and governing body of a county, however styled, including that of a consolidated or metropolitan government, a clerk of the circuit court, a separate or ex officio clerk of the county court, a sheriff, a property appraiser, a tax collector, a supervisor of elections, or any other officer in whom any portion of the fiscal duties of the above are under law separately placed.

(c) "Financial audit" means an examination of financial statements in order to express an opinion on the fairness with which they are presented in conformity with generally accepted accounting principles and an examination to determine whether operations are properly conducted in accordance with legal and regulatory requirements. Financial audits must be conducted in accordance with auditing standards generally accepted in the United States and government auditing standards as adopted by the Board of Accountancy. When applicable, the scope of financial audits shall encompass the additional activities necessary to establish compliance with the Single Audit Act Amendments of 1996, 31 U.S.C. ss. 7501-7507, and other applicable federal law.

(d) "Governmental entity" means a state agency, a county agency, or any other entity, however styled, that independently exercises any type of state or local governmental function.

(e) "Local governmental entity" means a county agency, municipality, or special district as defined in s. 189.012, but does not include any housing authority established under chapter 421.

(f) "Management letter" means a statement of the auditor's comments and recommendations.

(g) "Operational audit" means an audit whose purpose is to evaluate management's performance in establishing and maintaining internal controls, including controls designed to prevent and detect fraud, waste, and abuse, and in administering assigned responsibilities in accordance with applicable laws, administrative rules, contracts, grant agreements, and other guidelines. Operational audits must be conducted in accordance with government auditing standards. Such audits examine internal controls that are designed and placed in operation to promote and encourage the achievement of management's control objectives in the categories of compliance, economic and efficient operations, reliability of financial records and reports, and safeguarding of assets, and identify weaknesses in those internal controls.

(h) "Performance audit" means an examination of a program, activity, or function of a governmental entity, conducted in accordance with applicable government auditing standards or auditing and evaluation standards of other appropriate authoritative bodies. The term includes an examination of issues related to:

1. Economy, efficiency, or effectiveness of the program.
2. Structure or design of the program to accomplish its goals and objectives.
3. Adequacy of the program to meet the needs identified by the Legislature or governing body.
4. Alternative methods of providing program services or products.
5. Goals, objectives, and performance measures used by the agency to monitor and report program accomplishments.
6. The accuracy or adequacy of public documents, reports, or requests prepared under the program by state agencies.
7. Compliance of the program with appropriate policies, rules, or laws.

8. Any other issues related to governmental entities as directed by the Legislative Auditing Committee.

(i) "Political subdivision" means a separate agency or unit of local government created or established by law and includes, but is not limited to, the following and the officers thereof: authority, board, branch, bureau, city, commission, consolidated government, county, department, district, institution, metropolitan government, municipality, office, officer, public corporation, town, or village.

(j) "State agency" means a separate agency or unit of state government created or established by law and includes, but is not limited to, the following and the officers thereof: authority, board, branch, bureau, commission, department, division, institution, office, officer, or public corporation, as the case may be, except any such agency or unit within the legislative branch of state government other than the Florida Public Service Commission.

(2) DUTIES.—The Auditor General shall:

(a) Conduct audits of records and perform related duties as prescribed by law, concurrent resolution of the Legislature, or as directed by the Legislative Auditing Committee.

(b) Annually conduct a financial audit of state government.

(c) Annually conduct financial audits of all state universities and state colleges.

(d) Annually conduct financial audits of the accounts and records of all district school boards in counties with populations of fewer than 150,000, according to the most recent federal decennial statewide census.

(e) Once every 3 years, conduct financial audits of the accounts and records of all district school boards in counties that have populations of 150,000 or more, according to the most recent federal decennial statewide census.

(f) At least every 3 years, conduct operational audits of the accounts and records of state agencies, state universities, state colleges, district school boards, the Florida Clerks of Court Operations Corporation, water management districts, and the Florida School for the Deaf and the Blind.

(g) At least every 3 years, conduct a performance audit of the local government financial reporting system, which, for the purpose of this chapter, means any statutory provision related to local government financial reporting. The purpose of such an audit is to determine the accuracy, efficiency, and effectiveness of the reporting system in achieving its goals and to make recommendations to the local governments, the Governor, and the Legislature as to how the reporting system can be improved and how program costs can be reduced. The Auditor General shall determine the scope of the audits. The local government financial reporting system should provide for the timely, accurate, uniform, and cost-effective accumulation of financial and other information that can be used by the members of the Legislature and other appropriate officials to accomplish the following goals:

1. Enhance citizen participation in local government;
2. Improve the financial condition of local governments;
3. Provide essential government services in an efficient and effective manner; and
4. Improve decisionmaking on the part of the Legislature, state agencies, and local government officials on matters relating to local government.

(h) At least every 3 years, conduct a performance audit of the Department of Revenue's administration of the ad valorem tax laws as described in s. 195.096. The audit report shall report on the activities of the ad valorem tax program of the Department of Revenue related to the ad valorem tax rolls. The Auditor General shall include, for at least four counties reviewed, findings as to the accuracy of assessment procedures,

projections, and computations made by the department, using the same generally accepted appraisal standards and procedures to which the department and the property appraisers are required to adhere. However, the report may not include any findings or statistics related to any ad valorem tax roll that is in litigation between the state and county officials at the time the report is issued.

(i) Once every 3 years, review a sample of internal audit reports at each state agency, as defined in s. 20.055(1), to determine compliance with current Standards for the Professional Practice of Internal Auditing or, if appropriate, government auditing standards.

(j) Conduct audits of local governmental entities when determined to be necessary by the Auditor General, when directed by the Legislative Auditing Committee, or when otherwise required by law. No later than 18 months after the release of the audit report, the Auditor General shall perform such appropriate followup procedures as he or she deems necessary to determine the audited entity's progress in addressing the findings and recommendations contained within the Auditor General's previous report. The Auditor General shall notify each member of the audited entity's governing body and the Legislative Auditing Committee of the results of his or her determination.

(k) Annually conduct operational audits of the accounts and records of eligible nonprofit scholarship-funding organizations receiving eligible contributions under s. 1002.395, including any contracts for services with related entities, to determine compliance with the provisions of that section. Such audits shall include, but not be limited to, a determination of the eligible nonprofit scholarship-funding organization's compliance with s. 1002.395(6)(j). The Auditor General shall provide its report on the results of the audits to the Governor, the President of the Senate, the Speaker of the House of Representatives, the Chief Financial Officer, and the Legislative Auditing Committee, within 30 days of completion of the audit.

The Auditor General shall perform his or her duties independently but under the general policies established by the Legislative Auditing Committee. This subsection does not limit the Auditor General's discretionary authority to conduct other audits or engagements of governmental entities as authorized in subsection (3).

(3) **AUTHORITY FOR AUDITS AND OTHER ENGAGEMENTS.**—The Auditor General may, pursuant to his or her own authority, or at the direction of the Legislative Auditing Committee, conduct audits or other engagements as determined appropriate by the Auditor General of:

(a) The accounts and records of any governmental entity created or established by law.

(b) The information technology programs, activities, functions, or systems of any governmental entity created or established by law.

(c) The accounts and records of any charter school created or established by law.

(d) The accounts and records of any direct-support organization or citizen support organization created or established by law. The Auditor General is authorized to require and receive any records from the direct-support organization or citizen support organization, or from its independent auditor.

(e) The public records associated with any appropriation made by the Legislature to a nongovernmental agency, corporation, or person. All records of a nongovernmental agency, corporation, or person with respect to the receipt and expenditure of such an appropriation shall be public records and shall be treated in the same manner as other public records are under general law.

(f) State financial assistance provided to any nonstate entity as defined by s. 215.97.

(g) The Tobacco Settlement Financing Corporation created pursuant to s. 215.56005.

(h) Any purchases of federal surplus lands for use as sites for correctional facilities as described in s. 253.037.

(i) Enterprise Florida, Inc., including any of its boards, advisory committees, or similar groups created by Enterprise Florida, Inc., and programs. The audit report may not reveal the identity of any person who has anonymously made a donation to Enterprise Florida, Inc., pursuant to this paragraph. The identity of a donor or prospective donor to Enterprise Florida, Inc., who desires to remain anonymous and all information identifying such donor or prospective donor are confidential and exempt from the provisions of s. 119.07(1) and s. 24(a), Art. I of the State Constitution. Such anonymity shall be maintained in the auditor's report.

(j) The Florida Development Finance Corporation or the capital development board or the programs or entities created by the board. The audit or report may not reveal the identity of any person who has anonymously made a donation to the board pursuant to this paragraph. The identity of a donor or prospective donor to the board who desires to remain anonymous and all information identifying such donor or prospective donor are confidential and exempt from the provisions of s. 119.07(1) and s. 24(a), Art. I of the State Constitution. Such anonymity shall be maintained in the auditor's report.

(k) The records pertaining to the use of funds from voluntary contributions on a motor vehicle registration application or on a driver license application authorized pursuant to ss. 320.023 and 322.081.

(l) The records pertaining to the use of funds from the sale of specialty license plates described in chapter 320.

(m) The acquisitions and divestitures related to the Florida Communities Trust Program created pursuant to chapter 380.

(n) The Florida Water Pollution Control Financing Corporation created pursuant to s. 403.1837.

(o) The school readiness program, including the early learning coalitions under part VI of chapter 1002.

(p) The Florida Special Disability Trust Fund Financing Corporation created pursuant to s. 440.49.

(q) Workforce Florida, Inc., or the programs or entities created by Workforce Florida, Inc., created pursuant to s. 445.004.

(r) The corporation defined in s. 455.32 that is under contract with the Department of Business and Professional Regulation to provide administrative, investigative, examination, licensing, and prosecutorial support services in accordance with the provisions of s. 455.32 and the practice act of the relevant profession.

(s) The Florida Engineers Management Corporation created pursuant to chapter 471.

(t) The books and records of any permitholder that conducts race meetings or jai alai exhibitions under chapter 550.

(u) The corporation defined in part II of chapter 946, known as the Prison Rehabilitative Industries and Diversified Enterprises, Inc., or PRIDE Enterprises.

(v) The Florida Virtual School pursuant to s. 1002.37.

(w) Virtual education providers receiving state funds or funds from local ad valorem taxes.

(x) The accounts and records of a nonprofit scholarship-funding organization participating in a state sponsored scholarship program authorized by chapter 1002.

(4) SCHEDULING AND STAFFING OF AUDITS.—

(a) Each financial audit required or authorized by this section, when practicable, shall be made and completed within not more than 9 months following the end of each audited fiscal year of the state agency or political subdivision, or at such lesser time which may be provided by law or concurrent resolution or directed by the Legislative Auditing Committee. When the Auditor General determines that conducting any audit or engagement otherwise required by law would not be possible due to workload or would not be an efficient or effective use of his or her resources based on an assessment of risk, then, in his or her discretion, the Auditor General may temporarily or indefinitely postpone such audits or other engagements for such period or any portion thereof, unless otherwise directed by the committee.

(b) The Auditor General may, when in his or her judgment it is necessary, designate and direct any auditor employed by the Auditor General to audit any accounts or records within the authority of the Auditor General to audit. The auditor shall report his or her findings for review by the Auditor General, who shall prepare the audit report.

(c) The audit report when final shall be a public record. The audit workpapers and notes are not a public record; however, those workpapers necessary to support the computations in the final audit report may be made available by a majority vote of the Legislative Auditing Committee after a public hearing showing proper cause. The audit workpapers and notes shall be retained by the Auditor General until no longer useful in his or her proper functions, after which time they may be destroyed.

(d) At the conclusion of the audit, the Auditor General or the Auditor General's designated representative shall discuss the audit with the official whose office is subject to audit and submit to that official a list of the Auditor General's findings which may be included in the audit report. If the official is not available for receipt of the list of audit findings, then delivery is presumed to be made when it is delivered to his or her office. The official shall submit to the Auditor General or the designated representative, within 30 days after the receipt of the list of findings, his or her written statement of explanation or rebuttal concerning all of the findings, including corrective action to be taken to preclude a recurrence of all findings.

(e) The Auditor General shall provide the successor independent certified public accountant of a district school board with access to the prior year's working papers in accordance with the Statements on Auditing Standards, including documentation of planning, internal control, audit results, and other matters of continuing accounting and auditing significance, such as the working paper analysis of balance sheet accounts and those relating to contingencies.

(5) PETITION FOR AN AUDIT BY THE AUDITOR GENERAL.—

(a) The Legislative Auditing Committee shall direct the Auditor General to make an audit of any municipality whenever petitioned to do so by at least 20 percent of the registered electors in the last general election of that municipality pursuant to this subsection. The supervisor of elections of the county in which the municipality is located shall certify whether or not the petition contains the signatures of at least 20 percent of the registered electors of the municipality. After the completion of the audit, the Auditor General shall determine whether the municipality has the fiscal resources necessary to pay the cost of the audit. The municipality shall pay the cost of the audit within 90 days after the Auditor General's determination that the municipality has the available resources. If the municipality fails to pay the cost of the audit, the Department of Revenue shall, upon certification of the Auditor General, withhold from that portion of the distribution pursuant to s. 212.20(6)(d)5. which is distributable to such municipality, a

sum sufficient to pay the cost of the audit and shall deposit that sum into the General Revenue Fund of the state.

(b) At least one registered elector in the most recent general election must file a letter of intent with the municipal clerk prior to any petition of the electors of that municipality for the purpose of an audit. Each petition must be submitted to the supervisor of elections and contain, at a minimum:

1. The elector's printed name;
2. The signature of the elector;
3. The elector's residence address;
4. The elector's date of birth; and
5. The date signed.

All petitions must be submitted for verification within 1 calendar year after the audit petition origination by the municipal electors.

(6) REQUEST BY A LOCAL GOVERNMENTAL ENTITY FOR AN AUDIT BY THE AUDITOR GENERAL.—Whenever a local governmental entity requests the Auditor General to conduct an audit of all or part of its operations and the Auditor General conducts the audit under his or her own authority or at the direction of the Legislative Auditing Committee, the expenses of the audit shall be paid by the local governmental entity. The Auditor General shall estimate the cost of the audit. Fifty percent of the cost estimate shall be paid by the local governmental entity before the initiation of the audit and deposited into the General Revenue Fund of the state. After the completion of the audit, the Auditor General shall notify the local governmental entity of the actual cost of the audit. The local governmental entity shall remit the remainder of the cost of the audit to the Auditor General for deposit into the General Revenue Fund of the state. If the local governmental entity fails to comply with paying the remaining cost of the audit, the Auditor General shall notify the Legislative Auditing Committee.

(7) AUDITOR GENERAL REPORTING REQUIREMENTS.—

(a) The Auditor General shall notify the Legislative Auditing Committee of any local governmental entity, district school board, charter school, or charter technical career center that does not comply with the reporting requirements of s. 218.39.

(b) The Auditor General, in consultation with the Board of Accountancy, shall review all audit reports submitted pursuant to s. 218.39. The Auditor General shall request any significant items that were omitted in violation of a rule adopted by the Auditor General. The items must be provided within 45 days after the date of the request. If the governmental entity does not comply with the Auditor General's request, the Auditor General shall notify the Legislative Auditing Committee.

(c) The Auditor General shall provide annually a list of those special districts which are not in compliance with s. 218.39 to the Special District Accountability Program of the Department of Economic Opportunity.

(d) During the Auditor General's review of audit reports, he or she shall contact those units of local government, as defined in s. 218.403, that are not in compliance with s. 218.415 and request evidence of corrective action. The unit of local government shall provide the Auditor General with evidence of corrective action within 45 days after the date it is requested by the Auditor General. If the unit of local government fails to comply with the Auditor General's request, the Auditor General shall notify the Legislative Auditing Committee.

(e) The Auditor General shall notify the Governor or the Commissioner of Education, as appropriate, and the Legislative Auditing Committee of any audit report reviewed by

the Auditor General pursuant to paragraph (b) which contains a statement that a local governmental entity, charter school, charter technical career center, or district school board has met one or more of the conditions specified in s. 218.503. If the Auditor General requests a clarification regarding information included in an audit report to determine whether a local governmental entity, charter school, charter technical career center, or district school board has met one or more of the conditions specified in s. 218.503, the requested clarification must be provided within 45 days after the date of the request. If the local governmental entity, charter school, charter technical career center, or district school board does not comply with the Auditor General's request, the Auditor General shall notify the Legislative Auditing Committee. If, after obtaining the requested clarification, the Auditor General determines that the local governmental entity, charter school, charter technical career center, or district school board has met one or more of the conditions specified in s. 218.503, he or she shall notify the Governor or the Commissioner of Education, as appropriate, and the Legislative Auditing Committee.

(f) The Auditor General shall annually compile and transmit to the President of the Senate, the Speaker of the House of Representatives, and the Legislative Auditing Committee a summary of significant findings and financial trends identified in audit reports reviewed in paragraph (b) or otherwise identified by the Auditor General's review of such audit reports and financial information, and identified in audits of district school boards conducted by the Auditor General. The Auditor General shall include financial information provided pursuant to s. 218.32(1)(e) for entities with fiscal years ending on or after June 30, 2003, within his or her reports submitted pursuant to this paragraph.

(g) If the Auditor General discovers significant errors, improper practices, or other significant discrepancies in connection with his or her audits of a state agency or state officer, the Auditor General shall notify the President of the Senate, the Speaker of the House of Representatives, and the Legislative Auditing Committee. The President of the Senate and the Speaker of the House of Representatives shall promptly forward a copy of the notification to the chairs of the respective legislative committees, which in the judgment of the President of the Senate and the Speaker of the House of Representatives are substantially concerned with the functions of the state agency or state officer involved. Thereafter, and in no event later than the 10th day of the next succeeding legislative session, the person in charge of the state agency involved, or the state officer involved, as the case may be, shall explain in writing to the President of the Senate, the Speaker of the House of Representatives, and to the Legislative Auditing Committee the reasons or justifications for such errors, improper practices, or other significant discrepancies and the corrective measures, if any, taken by the agency.

(h) The Auditor General shall annually compile and transmit to the President of the Senate, the Speaker of the House of Representatives, and the Legislative Auditing Committee by December 1 of each year a report that includes a projected 2-year work plan identifying the audit and other accountability activities to be undertaken and a list of statutory and fiscal changes recommended by the Auditor General. The Auditor General may also transmit recommendations at other times of the year when the information would be timely and useful for the Legislature.

(i) The Auditor General shall annually transmit by July 15, to the President of the Senate, the Speaker of the House of Representatives, and the Department of Financial Services, a list of all school districts, charter schools, charter technical career centers, Florida College System institutions, state universities, and water management districts that have failed to comply with the transparency requirements as identified in the audit



reports reviewed pursuant to paragraph (b) and those conducted pursuant to subsection (2).

(j) The Auditor General shall notify the Legislative Auditing Committee of any financial or operational audit report prepared pursuant to this section which indicates that a district school board, state university, or Florida College System institution has failed to take full corrective action in response to a recommendation that was included in the two preceding financial or operational audit reports.

1. The committee may direct the district school board or the governing body of the state university or Florida College System institution to provide a written statement to the committee explaining why full corrective action has not been taken or, if the governing body intends to take full corrective action, describing the corrective action to be taken and when it will occur.

2. If the committee determines that the written statement is not sufficient, the committee may require the chair of the district school board or the chair of the governing body of the state university or Florida College System institution, or the chair's designee, to appear before the committee.

3. If the committee determines that the district school board, state university, or Florida College System institution has failed to take full corrective action for which there is no justifiable reason or has failed to comply with committee requests made pursuant to this section, the committee shall refer the matter to the State Board of Education or the Board of Governors, as appropriate, to proceed in accordance with s. 1008.32 or s. 1008.322, respectively.

(8) RULES OF THE AUDITOR GENERAL.—The Auditor General, in consultation with the Board of Accountancy, shall adopt rules for the form and conduct of all financial audits performed by independent certified public accountants pursuant to ss. 215.981, 218.39, 1001.453, 1002.395, 1004.28, and 1004.70. The rules for audits of local governmental entities, charter schools, charter technical career centers, and district school boards must include, but are not limited to, requirements for the reporting of information necessary to carry out the purposes of the Local Governmental Entity, Charter School, Charter Technical Career Center, and District School Board Financial Emergencies Act as stated in s. 218.501.

(9) TECHNICAL ADVICE PROVIDED BY THE AUDITOR GENERAL.—The Auditor General may provide technical advice to:

(a) The Department of Education in the development of a compliance supplement for the financial audit of a district school board conducted by an independent certified public accountant.

(b) Governmental entities on their financial and accounting systems, procedures, and related matters.

(c) Governmental entities on promoting the building of competent and efficient accounting and internal audit organizations in their offices.

History.—s. 6, ch. 67-470; s. 6, ch. 69-82; s. 1, ch. 72-6; ss. 1, 2, ch. 73-234; s. 1, ch. 75-122; s. 1, ch. 76-73; s. 1, ch. 77-102; s. 2, ch. 79-183; ss. 1, 3, 6, ch. 79-589; s. 1, ch. 81-167; s. 1, ch. 83-55; s. 1, ch. 83-106; s. 1, ch. 84-241; s. 1, ch. 85-80; s. 14, ch. 86-204; s. 2, ch. 86-217; s. 1, ch. 87-114; s. 4, ch. 89-87; s. 30, ch. 89-169; s. 9, ch. 90-110; s. 19, ch. 90-227; s. 65, ch. 91-45; s. 17, ch. 91-282; s. 2, ch. 91-429; s. 91, ch. 92-142; s. 136, ch. 92-279; s. 55, ch. 92-326; s. 15, ch. 94-249; s. 1309, ch. 95-147; s. 1, ch. 95-214; s. 1, ch. 95-380; s. 12, ch. 95-396; s. 26, ch. 96-318; s. 1, ch. 96-324; s. 21, ch. 97-96; s. 1, ch. 97-111; s. 1, ch. 97-255; s. 26, ch. 97-271; s. 3, ch. 99-333; s. 1, ch. 2000-151; s. 4, ch. 2000-264; s. 31, ch. 2000-355; s. 36, ch. 2000-371; s. 30, ch. 2001-140; s. 15, ch. 2001-266; s. 1, ch. 2002-1; s. 17, ch. 2002-22; s. 880, ch. 2002-387; s. 2, ch. 2004-305; s. 1, ch. 2004-331; s. 3, ch. 2004-484; s. 1, ch. 2005-171; s. 7, ch. 2006-190; s. 5, ch. 2009-68; s. 1, ch. 2009-214; s. 2, ch. 2010-5; s. 13, ch. 2011-34; s. 1, ch. 2011-49; s. 1, ch. 2011-52; s. 36, ch.

2011-142; s. 1, ch. 2012-5; s. 1, ch. 2012-134; s. 1, ch. 2013-15; s. 1, ch. 2013-51; s. 19, ch. 2013-252; s. 1, ch. 2014-17; s. 55, ch. 2014-22; s. 1, ch. 2014-39; s. 15, ch. 2014-184; s. 1, ch. 2014-223.

**FMPA**  
**Auditor General Report**



**Operational Audit of the  
Florida Municipal Power Agency  
No. 2015-165  
March 30, 2015**



# Florida Municipal Power Agency

- The Florida Municipal Power Agency (FMPPA) is a Joint Use Action Agency (JAA) created in 1978.
- The FMPPA finances, acquires, contracts, manages, and operates its own electric power projects.
- Members choose whether to participate in projects and each of the projects are independent from the other projects. Project bond resolutions specify that no revenues or funds from one project can be used to pay the costs of any other project.
- At October 31, 2014, the FMPPA had 31 member municipalities, 20 of which participated in one or more projects.
- Board of Directors govern over all except the All Requirements Project (ARP); Executive Committee governs the ARP. Member municipalities appoint individuals to serve on the Board and Committee.



# Audit Focus

- Our audit of the FMIPA focused primarily on management's performance in establishing and maintaining internal controls and in administering assigned responsibilities in accordance with applicable laws, rules, regulations, contracts, grant agreements, and other guidelines.
- In conducting this audit, we engaged consultants with significant industry expertise to assist us in evaluating the FMIPA's practices, including comparisons to best industry practices and with other comparable JAAs.

# Finding Nos. 1, 2, and 3



## Hedging Activities

- Fuel hedging practices were not consistent with industry practices utilized by other comparable JAAs. Specifically, FMPA used practices more consistent with a strategy for trading gas than a strategy focused on offsetting the changes in fuel costs.
- Investments in natural gas exploration and drilling were not consistent with industry practices utilized by other comparable JAAs and were more complex and involved more risk than alternative forms of hedging commonly practiced.
- Certain interest rate swaps were not employed consistent with industry practices utilized by other comparable JAAs, which resulted in significant termination fees likely to be incurred. These swaps were entered into far in advance of the anticipated issuance of debt and the debt was never issued.

# Finding No. 4



## Investments

- FMIPA's investment policy needed to be enhanced to clarify requirements regarding allowable investment credit ratings and to establish geographic diversification requirements for investments.



# Finding Nos. 5, 6, and 7



## Personnel and Payroll Administration

- Compensated absences (absences for which employees will be paid, such as annual and sick leave) increased by 75 percent in four years, and the cost of future postretirement benefits for certain employees may result in payouts that negatively impact future rates.
- The Board of Directors set the compensation package for the General Counsel through a series of actions over several years rather than through the use of a written employment agreement and FMPA was unable to provide documentation for one of the benefits provided by Board action.
- The Chief Executive Officer's employment contract provides for severance pay and postretirement benefits for life if he is terminated for cause.

# Finding Nos. 8 through 11



## Procurement of Goods and Services

- FMPA records did not always evidence the public purpose served for purchases of goods and services. For example, FMPA records did not evidence the public purpose for \$12,688 expended for holiday parties.
- The FMPA, in some instances, did not obtain quotes or proposals for purchases of goods and services, contrary to FMPA policies.
- FMPA had not recently used a competitive selection process when selecting financial advisors and bond counsel for bond issues, potentially increasing costs associated with bond issues.
- FMPA did not always follow its policies regarding credit card issuance and purchases, and did not employ procedures for monitoring credit limits for reasonableness.

# Finding No. 12



## Travel

- FMPA did not always follow its travel policies or ensure that travel-related receipts were submitted by contractors. Additionally, the FMPA's travel policies could be enhanced.



# Finding Nos. 13 and 14

## All Requirements Project (ARP) Contract Provisions

Demand charge is billed to a member based on the member's relative percentage of power purchased on the monthly coincident peak demand day (during the peak hour of the peak day of demand for the ARP system).

Temporary attempts to control or lower a member's power load at the time of coincident peak demand to reduce demand charges is "peak shaving."

- The ARP power supply project contracts did not address peak shaving.
- At an Executive Committee meeting, members agreed to curtail peak shaving activities; however, the agreement appears primarily voluntary in nature, relies on self-reporting, and contains no consequences for noncompliance.

# Finding Nos. 13 and 14



## All Requirements Project (ARP) Contract Provisions (continued)

- Certain ARP power supply project contract provisions relating to withdrawing members are ambiguous, used a fixed discount rate rather than one associated with current capital costs, and did not provide for independent verification by the withdrawing member.

# Finding No. 15



## Information Technology

- FMPA's disaster recovery plan could be enhanced.

Questions?

# FLORIDA MUNICIPAL POWER AGENCY

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## Operational Audit





**FLORIDA MUNICIPAL POWER AGENCY  
BOARD OF DIRECTORS AND EXECUTIVE COMMITTEE**

The Florida Municipal Power Agency is a Joint Use Action Agency created pursuant to a series of interlocal agreements with Florida municipalities under the authority of Sections 163.01 (Florida Interlocal Cooperation Act of 1969), and 361.10 (Joint Power Act), Florida Statutes, to finance, acquire, contract, manage, and operate its own electric power projects or jointly accomplish the same purposes with other public or private utilities.

The Florida Municipal Power Agency is governed by a Board of Directors, with one Board member appointed by each member municipality. The Board decides all issues concerning each project except for the All Requirements Project. The All Requirements Project is governed by an Executive Committee, with each All Requirements Project member municipality that purchases power from the project appointing one Executive Committee member.

Members that served on the Board of Directors and Executive Committee during the period October 2012 through June 2014 are listed in Exhibit A.

The audit team leader was Jeffrey Brizendine, CPA, and the audit was supervised by Derek Noonan, CPA. Please address inquiries regarding this report to Marilyn D. Rosetti, CPA, Audit Manager, by e-mail at [marilynrosetti@aud.state.fl.us](mailto:marilynrosetti@aud.state.fl.us) or by telephone at (850) 412-2881.

This report and other reports prepared by the Auditor General can be obtained on our Web site at [www.myflorida.com/audgen](http://www.myflorida.com/audgen); by telephone at (850) 412-2722; or by mail at G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450.

## FLORIDA MUNICIPAL POWER AGENCY

### EXECUTIVE SUMMARY

Our operational audit of the Florida Municipal Power Agency (FMPA) disclosed the following:

#### HEDGING ACTIVITIES

**Finding No. 1:** Fuel hedging practices were not consistent with industry practices utilized by other comparable joint action agencies.

**Finding No. 2:** Investments in natural gas exploration and drilling were not consistent with industry practices utilized by other comparable joint action agencies and were more complex and involved more risk than alternative forms of hedging commonly practiced.

**Finding No. 3:** Certain interest rate swaps were not employed consistent with industry practices utilized by other comparable joint action agencies, which resulted in significant termination fees likely to be incurred.

#### INVESTMENTS

**Finding No. 4:** The FMPA's investment policy needed to be enhanced to clarify requirements regarding allowable investment credit ratings and to establish geographic diversification requirements for investments.

#### PERSONNEL AND PAYROLL ADMINISTRATION

**Finding No. 5:** Compensated absences increased by 75 percent in four years, and the cost of future postretirement benefits for certain employees may result in payouts that negatively impact future rates.

**Finding No. 6:** The Board of Directors (Board) set the compensation package for the General Counsel through a series of actions over several years rather than through the use of a written employment agreement and FMPA was unable to provide documentation for one of the benefits provided by Board action.

**Finding No. 7:** The Chief Executive Officer's employment contract provides for severance pay and postretirement benefits for life if he is terminated for cause.

#### PROCUREMENT OF GOODS AND SERVICES

**Finding No. 8:** FMPA records did not always evidence the public purpose served for purchases of goods and services.

**Finding No. 9:** The FMPA did not always follow its purchasing policies regarding competitive selection.

**Finding No. 10:** The FMPA had not recently used a competitive selection process when selecting financial advisors and bond counsel for bond issues, potentially increasing costs associated with bond issues.

**Finding No. 11:** The FMPA did not always follow its policies regarding credit card issuance and purchases, and did not employ procedures for monitoring credit limits for reasonableness.

#### TRAVEL

**Finding No. 12:** The FMPA did not always follow its travel policies or ensure that travel-related receipts were submitted by contractors. Additionally, the FMPA's travel policies could be enhanced.

#### ALL REQUIREMENTS PROJECT (ARP) CONTRACT PROVISIONS

**Finding No. 13:** The ARP power supply project contracts did not address peak shaving and, although the Executive Committee agreed to curtail peak-shaving activities, the agreement appears primarily voluntary in nature, relies on self-reporting, and contains no consequences for noncompliance.

**Finding No. 14:** Certain ARP power supply project contract provisions relating to withdrawing members are ambiguous, used a fixed discount rate rather than one associated with current capital costs, and did not provide for independent verification by the withdrawing member.

#### INFORMATION TECHNOLOGY

**Finding No. 15:** The FMPA's disaster recovery plan could be enhanced.

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**BACKGROUND**

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The Florida Municipal Power Agency (FMPA), is a Joint Use Action Agency (JAA) created in 1978 pursuant to a series of interlocal agreements with Florida municipalities under the authority of Sections 163.01 (Florida Interlocal Cooperation Act of 1969), and 361.10 (Joint Power Act), Florida Statutes. Although the FMPA is a governmental entity, many of the laws applicable to local governments, including municipalities, do not apply to the FMPA. Further, unlike investor owned utilities (IOUs), the FMPA is not subject to any rate-setting authority by the Florida Public Service Commission, which is consistent with JAAs in other states.

The FMPA finances, acquires, contracts, manages, and operates its own electric power projects or jointly accomplishes the same purposes with other public or private utilities. The FMPA's structure allows each member municipality the option to participate in one or more projects or not to participate in any project. Each of the projects are independent from the other projects, and the project bond resolutions specify that no revenues or funds from one project can be used to pay the costs of any other project. Projects are as follows:

- The St. Lucie Project consists of 8.8 percent ownership interest in St. Lucie Unit 2, a 984 megawatt (MW) nuclear power plant located on Hutchinson Island in St. Lucie County and primarily owned and operated by Florida Power and Light.
- The Stanton and Tri-City Projects consist of 14.8 and 5.3 percent ownership, respectively, in a 441 MW coal-fired power plant located in Orlando and primarily owned and operated by the Orlando Utilities Commission (OUC).
- The Stanton II Project consists of 23.2 percent ownership in a 453 MW coal-fired power plant located in Orlando and primarily owned and operated by the OUC.
- The All Requirements Project (ARP) consists of varying ownership interest in several power plants located throughout Florida, including the Stanton Energy Center Units 1 and 2; Indian River Combustion Turbines A, B, C, and D; and Stanton Unit A. In addition, the ARP wholly owns the following units: Treasure Coast Energy Center; Cane Island Units 1, 2, 3, and 4; Key West Units 1, 2, 3, and 4; and Stock Island MS Units 1 and 2.

As of October 31, 2014, the FMPA had 31 member municipalities, 20 of which participated in one or more projects as described in Table 1:

Table 1

Member Municipality	All Requirements Project	St. Lucie Project	Stanton Project	Stanton II Project	Tri-City Project
City of Alachua		X			
City of Bushnell	X				
City of Clewiston	X	X			
City of Fort Meade	X	X			
City of Fort Pierce	X	X	X	X	X
City of Green Cove Springs	X	X			
Town of Havana	X				
City of Homestead		X	X	X	X
City of Jacksonville Beach	X	X			
City of Key West	X			X	X
City of Kissimmee	X	X	X	X	
City of Lake Worth	X (1)	X	X		
City of Leesburg	X	X			
City of Moore Haven		X			
City of New Smyrna Beach		X			
City of Newberry	X	X			
City of Ocala	X				
City of St. Cloud				X	
City of Starke	X	X	X	X	
City of Vero Beach	X (2)	X	X	X	

Notes (1): Member of the ARP, but has not purchased power from the project since January, 1, 2014.

(2): Member of the ARP, but has not purchased power from the project since January, 1, 2010.

Source: FMPA Records

The remaining 11 municipalities, which include the Cities of Bartow, Blountstown, Chattahoochee, Gainesville, Lakeland, Mount Dora, Orlando, Quincy, Wauchula, Williston, and Winter Park, were members of the FMPA and participated in various activities, such as training, but were not participants in any power projects.

The FMPA is governed by a Board of Directors (Board), with one Board member appointed by each member municipality. The Board decides all issues concerning each project except for the ARP. Board members from municipalities that do not participate in any FMPA power projects have one vote each; ARP participants have two votes each; and the remaining Board members have 1.5 votes each. The ARP is governed by an Executive Committee, with each ARP member municipality that purchases power from the project appointing one Executive Committee member. The FMPA’s bond resolutions require that its rate structure be designed to produce revenues sufficient to pay operating, debt service, and other specified costs. The Board and the Executive Committee are responsible for approving the rate structures for the non-ARP and ARP projects, respectively.

The majority of financial activity occurs in the ARP, in which the FMPA is responsible for providing all electricity needs for the ARP members that are not provided by other FMPA projects. In contrast, the other projects have less financial activity, as these projects represent minority ownership in joint electricity projects with other power providers. Revenues and expenses for the various projects for the 2012-13 fiscal year, the most recent audited information available as of December 2014, were as noted in Table 2 (amounts reported in thousands):

Table 2

Description	All Requirements Project	St. Lucie Project	Stanton Project	Stanton II Project	Tri-City Project	Agency Fund (1)
Operating Revenue	\$ 481,573	\$ 46,230	\$ 23,260	\$ 51,003	\$ 9,122	\$ 12,531
Operating Expenses	431,660	44,771	16,539	36,064	6,477	12,718
Nonoperating Net Expense	8,276	11,277	3,102	7,342	1,429	11

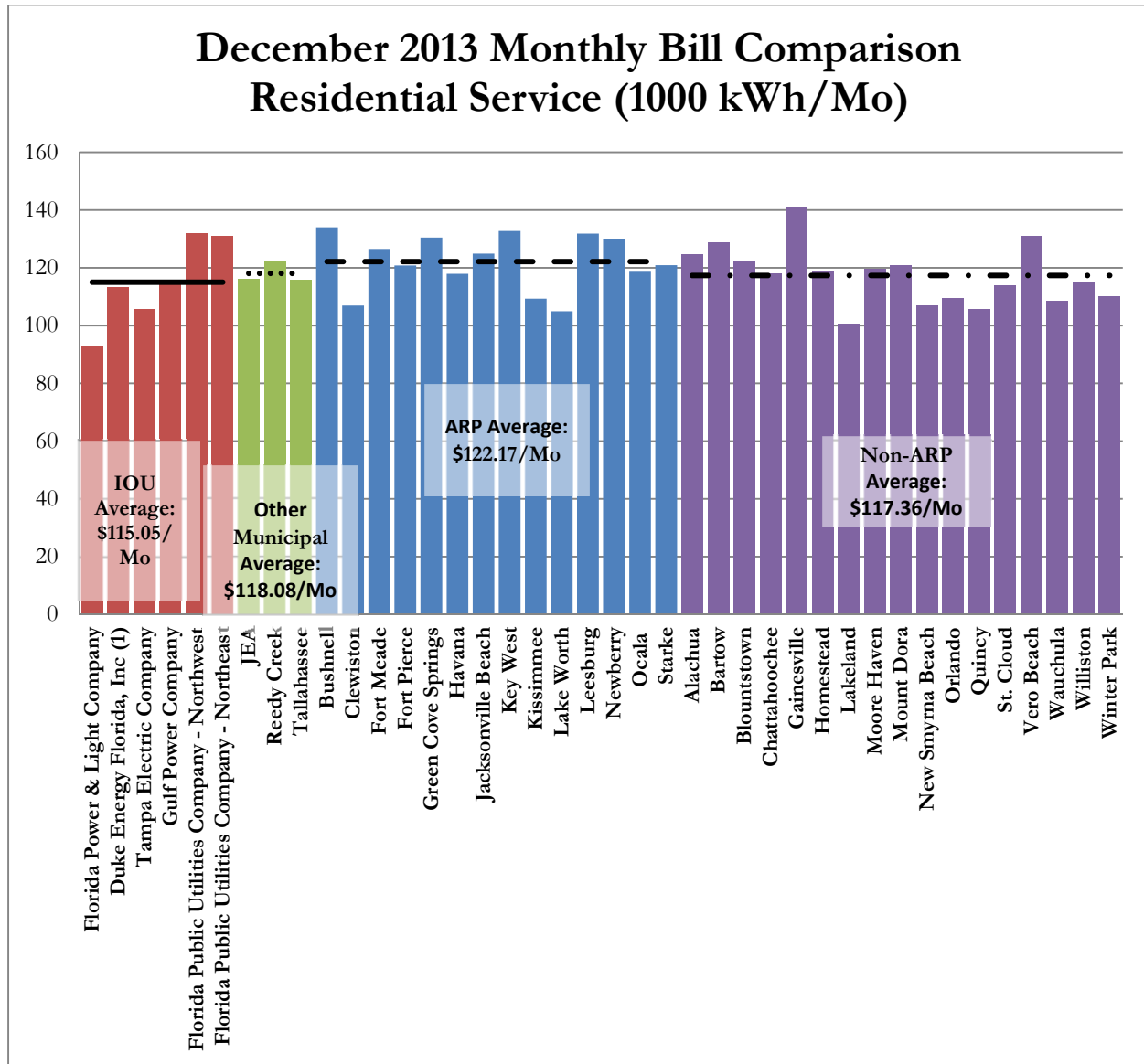
Note (1): The Agency Fund is not associated with a particular project; rather, it accounts for general operations benefiting all projects.

Source: FMPA 2012-13 fiscal year audited financial statements

Table 3 shows comparative residential service bills for the month of December 2013 for IOUs, non-FMPA member municipal electrical utilities, FMPA ARP members, and FMPA non-ARP members. The average FMPA ARP members’ bill is greater than the average IOUs’ bill and average non-FMPA member municipal electric utilities’ bill by \$7.12 (6 percent), and \$4.09 (3 percent), respectively. Additionally, the average bill for an FMPA ARP member is higher than the average bill for an FMPA non-ARP member by \$4.81, or 4 percent. There are multiple factors that impact FMPA ARP members’ residential rates, some of which are not attributable to FMPA, including:

- Several ARP members also participate in non-ARP projects. Consequently, the ARP member receives power from multiple sources at differing wholesale rates, which are factored into customer billings.
- ARP members add additional costs, such as electrical service costs associated with delivery of power, to customer billings.
- According to Moody’s Investors Service, “Many FMPA member electric utilities have sizable transfers of electric fund revenues to their municipal General Funds which can sometimes contribute to above average retail rates for some members.”

Table 3



Notes:

- (1) Duke Energy completed a merger with Progress Energy on July 2, 2012. Upon completion of the transaction, the new entity operates in Florida as Duke Energy Florida, Inc.
- (2) IOU amounts do not include franchise fees and certain other taxes, both of which vary by locality, as such information was not readily available.

Source: Florida Public Service Commission

Charges billed to individual ARP members vary based on FMPA cost allocations, member-owned capacity credits, and other factors. Table 4 shows the weighted average cost per MWh or kilowatt (kW) month, as applicable, over the last ten years for the primary monthly billing components invoiced to ARP members.

Table 4

Fiscal Year	Demand Charge (1)	Energy Charge (2)	Transmission (1)
2015 (Budgeted)	\$ 22.46	\$ 32.62	\$ 2.60
2014	21.98	30.80	2.25
2013	20.98	32.53	2.00
2012	19.92	29.59	1.79
2011	17.86	39.44	1.85
2010	18.16	52.04	1.39
2009	16.08	64.48	1.82
2008	13.08	65.49	1.24
2007	11.12	55.56	1.25
2006	10.81	54.82	1.37

Notes: (1) Per Kilowatt month

(2) Per Megawatt hour

Source: FMPA Records

As shown in Table 4, the demand and energy charge components are the two largest components on ARP member billings. From the 2005-06 fiscal year to the 2013-14 fiscal year, the energy charge, which represents the cost of purchased fuel, decreased from \$54.82 per MWh to \$30.80 per MWh, a decrease of 44 percent. In contrast, the weighted average demand charge increased from \$10.81 per MWh to \$21.98 per MWh, a 103 percent increase, over the same time period. The demand charge is composed of fixed costs allocated to members based upon a member’s peak demand during the peak hour of the peak day of the ARP monthly coincident peak demand (i.e., the peak demand for the ARP system as a whole). The largest component of the demand charge is for debt service principal and interest payments, the total of which were budgeted at \$108.3 million during the 2014-15 fiscal year, an increase of \$88.5 million, or 447 percent, over \$19.8 million in the 2005-06 fiscal year. Much of the increase in debt cost is attributable to the recently constructed Treasure Coast and Cane Island Units.

Demand cost allocation among members may fluctuate, but total demand costs for the ARP as a whole do not increase or decrease based upon the amount of electricity generated by the FMPA. As Table 5 shows, electricity demand has decreased steadily from the 2008-09 fiscal year to the proposed budget for the 2014-15 fiscal year. Specifically, average monthly billed MW has decreased by 18 percent from 13,919 to 11,455 MW over the past six years primarily due to a weaker economy, energy conservation programs, and the cessation of ARP power delivery by the Cities of Vero Beach and Lake Worth in January 2010 and January 2014, respectively. Consequently, increased fixed demand costs are being allocated to a decreasing number of billed MW, which increases member billing rates.

Table 5

Fiscal Year	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15 (Proposed Budget)
MW Billed - Demand	13,919	12,739	12,157	12,379	12,218	11,331	11,455

Source: FMPA Records

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## FINDINGS AND RECOMMENDATIONS

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Insofar as the FMPA must recover all costs of providing power to members through billings, decisions as to the level of spending and the nature of specific activities undertaken, such as hedging, investment, and debt issuance activities by the FMPA have an impact on the amounts charged to FMPA members. We have disclosed several FMPA activities or practices in this report that may have contributed to higher costs billed to FMPA members.

<b>Hedging Activities</b>
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Given the volatility in fuel prices, hedging using derivatives, such as commodities futures contracts, is a common industry practice. The usage of interest rate swaps to hedge interest rate volatility on variable rate debt is also a common industry practice. However, as indicated in finding Nos. 1 through 3, the FMPA's risk tolerance for usage of derivative hedging instruments was higher than the industry norm.

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### **Finding No. 1: Fuel Hedging**

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Governmental Accounting Standards Board (GASB) Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, addresses the goal of effective hedging, saying, "effectiveness is determined by considering whether the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item." The goal of effective hedging, therefore, should be to offset changes in the cost of fuel, not to reduce fuel costs. The simplest effective fuel price hedge vehicle would be to have a payout that increases dollar-for-dollar with the increase in spot fuel prices (i.e., fuel prices purchased at market price rather than a contracted futures price), thereby offsetting variability in a utility's fuel costs. Forwards, futures, and swaps are examples of hedging vehicles with characteristics similar to the simplest effective fuel hedge in that their payout approximately increases dollar-for-dollar with the increase in spot gas prices.

The FMPA has implemented its *Natural Gas & Fuel Oil Risk Management Policy* to authorize hedging of fuel prices. Section 3.2 of the FMPA policy states, "FMPA shall implement the FST (FMPA Short-term) Program to mitigate the impact of upward trending natural gas price movements while concurrently allowing participation, to the extent possible, in downward price movements." This statement is inconsistent with the simplest effective fuel hedge in that it contemplates offsetting upward fuel price movement while capturing the cost savings of downward price movement.

The FMPA's policy allows for exchange-based futures, over-the-counter transactions, such as forwards, swaps, and options; forward physical purchases; fixed price physical natural gas purchases of longer than one month; natural gas storage; and fuel oil storage. Given this hedging flexibility and variety of hedging instruments allowed, the FMPA provided for training of applicable staff regarding various hedging practices and mechanisms. From September 2008 through April 2013, the FMPA engaged in complex trading practices utilizing matched combinations of options positions (i.e. spreads) and futures positions that were not consistent with a simple fuel hedge and were inconsistent with industry practices utilized by eight comparable JAAs<sup>1</sup> that employ fuel hedging derivatives. Further, FMPA source documents for derivative trades from July 2008 to June 2013 did not demonstrate that the FMPA's trading program was calculated to offset changes in the spot price of fuel as would a simple effective fuel hedge. As shown in Table 6, the FMPA incurred net total losses of \$247.6 million related to fuel hedging activities over the past 12 fiscal years.

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<sup>1</sup> Comparability to the FMPA was based on reported peak MW load, wholesale electric revenues, the number of member municipalities, total number of retail customers served, and the generation fuel types employed.



Table 6

Fiscal Year Ended September 30	Gain/(Loss) from Fuel Hedging Activity
2003	\$(3,844,385)
2004	6,211,729
2005	19,254,388
2006	482,038
2007	(32,303,698)
2008	11,136,570
2009	(140,564,807)
2010	(41,347,894)
2011	(23,639,173)
2012	(21,899,554)
2013	(18,437,623)
2014	(2,679,175)
<b>Total</b>	<b><u>\$(247,631,584)</u></b>

Source: FMPA Records

Due to losses in fuel hedging, on May 15, 2014, the Executive Committee decided not to hedge fuel prices until natural gas prices reach \$7 per MMBtu (Million British Thermal Units), although prices during May 2014 were approximately \$4.50 per MMBtu. In contrast, general industry practice is to hedge fuel prices at current prices rather than at future predetermined price trading triggers. As a result, the FMPA's natural gas costs were unhedged under this \$7 trigger amount, where industry practice suggests that some hedging would be prudent, meaning that the FMPA was accepting more risk in the form of potential natural gas cost volatility. In October 2014, the Executive Committee adopted a one-time seasonal hedging policy providing hedging of up to 25 percent of projected natural gas demand at trigger prices of \$3.90 and \$4.10 per MMBtu.

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**Recommendation:** The FMPA should consider amending its fuel hedging policies to focus on offsetting changes in the cost of natural gas rather than the benefit from upward and downward price volatility. In doing so, the policy should provide for hedging using only derivative instruments necessary to achieve a simple effective fuel hedge at current natural gas prices rather than at preset trigger amounts.

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#### **Follow-up to Management's Response**

*In its response to finding No. 1, the FMPA indicated that it followed common industry practice with its hedging programs. While the FMPA's fuel hedging policy documents were consistent with general industry practice, the FMPA's fuel hedging program was not consistent with general industry practice due to the FMPA's initial use of unnecessarily complex option spreads and the triggering of its trades based on spot gas prices and trends in spot gas prices. Consequently the FMPA's fuel hedging practices were more consistent with a strategy for trading gas than with a strategy for hedging fuel costs.*

*Also, in its response to finding Nos. 1 through 3, the FMPA indicated that it does not feel that the JAAs used for comparison purposes are comparable to the FMPA. The FMPA refers to the “75 JAAs and more than 3,000 electrical utilities,” and indicates that 8 JAAs are insufficient for comparability purposes. However, insofar as JAAs are public governmental entities and are not subject to the same level of regulatory oversight, comparison to investor owned utilities would not be appropriate. Additionally, insofar as the FMPA is governed by a Board of Directors (Board), with one Board member appointed by each member municipality, and the ARP is governed by an Executive Committee with each ARP member municipality that purchases power from the project appointing one Executive Committee member, it is not directly governed by elected officials. Consequently, comparing the FMPA to non-JAA municipal power providers is similarly not appropriate. The FMPA also notes that the JAAs used for comparison purposes do not use natural gas to generate power to the extent that the FMPA does. However, the same hedging concepts that apply to natural gas also apply to other types of fuels in that all fuel commodities are subject to market volatility. While no two JAAs are identical, based on several attributes that the 8 JAAs have in common with the FMPA, we believe these JAAs are sufficiently comparable to the FMPA for purposes of our audit.*

**Finding No. 2: Natural Gas Supply Agency Participation**

In November 2004, the FMPA signed an agreement with six other public gas and electric utilities in five different states to form a natural gas supply agency called Public Gas Partners, Inc. (PGP). The PGP was created to secure economical, long-term wholesale natural gas supplies for its members to stabilize and reduce the cost of natural gas.

The PGP’s acquisition activities are organized by gas supply pools, and FMPA members elected to participate in two gas supply pools. Each gas supply pool stands alone with rights and obligations separate from the PGP’s other pools. As a member of the PGP, the FMPA is obligated to pay its share of all common costs and 100 percent of any costs incurred by the PGP on FMPA’s behalf. By contract, FMPA also has accepted a step-up provision that requires a maximum additional exposure of 25 percent of its original contracted amount if other PGP members default on any of their obligations. No rights exist to withdraw from the PGP without the unanimous consent of the PGP Operating Committee and the subsequent unanimous consent of the PGP Board of Directors.

In calendar years 2004 and 2005, the FMPA’s ARP became a participant in PGP Gas Supply Pool 1 (PGP1) and PGP Gas Supply Pool 2 (PGP2). Section 12.2 of the PGP agreements indicates that the PGP will acquire interests in gas reserves and that the member shall be responsible for paying its participation share of all such capital expenditures. Pursuant to its participation in the pools, the FMPA has issued ARP revenue bonds as described in Table 7.

**Table 7**

<b>Calendar Year</b>	<b>Bond Issuance</b>
2006	\$45,000,000 (1)
2008	60,000,000
2009	15,000,000
2013	15,000,000
<b>Total</b>	<b><u>\$135,000,000</u></b>

Note (1): The original bond issuance amount was \$50,000,000; however, \$5,000,000 was refunded by the 2008 issue.

Source: FMPA Records

Participation in a natural gas development project, similar to FMPAs’ participation in the PGP, should fix gas costs at a rate equal to operational expenses plus depletion of gas properties, less revenues (e.g., the sale of nonmethane products like ethane and liquid petroleum), such that PGP participation is reasonably expected to be a natural physical hedge to the price of natural gas. An analysis of 17 comparable JAAs<sup>2</sup> disclosed that only one of those JAAs was involved in similar natural gas pool activity. The results of this analysis indicate that the FMPA’s investment in natural gas exploration and production via its participation in PGP was not a common industry practice or common form of fuel hedging, with the most typical forms of such hedging consisting of a combination of long and short-term natural gas purchases, contracted storage, and use of financial hedges. The natural gas procurement strategy most similar to the FMPA’s PGP participation is a prepaid natural gas contract. Table 8 compares the relative risk characteristics of the two natural gas procurement strategies:

Table 8

Comparison of Natural Gas Procurement Strategies		
Characteristic	PGP Participation	Prepaid Natural Gas Contract
Upfront payment of costs?	Yes, majority of costs prepaid	Yes, all costs prepaid
Fixed quantity of natural gas?	Yes, subject to accuracy of forecasts	Yes
Fixed prices of natural gas?	Yes, subject to certain risks	Yes, subject to prepaid contract counterparty risk
Regulatory risk?	Yes, production can be affected by new regulation	No, regulatory risk is borne by counterparty
Duration of production?	Variable, based on continued investment and value of proven reserves	Fixed
Operational risk?	Yes, operational anomaly risk borne by PGP participants	No, the counterparty is responsible for operations
Mandatory future costs?	Yes, subject to future costs associated with capital development of existing wells	No, further purchases of prepaid natural gas contracts not required.
Multiple counterparties?	Yes, the FMPA's goals and risk tolerance are considered along with the goals and risk tolerances of all other PGP participants	No, the prepaid contract has a single counterparty

Source: Contracted consultants and PGP agreements

As shown in Table 8 above, the FMPA’s participation in the PGP is more complex and involves more categories of risk than the alternative of entering into a prepaid natural gas contract.

The FMPA did not actually take delivery of any natural gas provided by the PGP pools; rather, the PGP sold FMPA’s share of the natural gas and remitted the proceeds monthly to the FMPA. Our review of the FMPA’s overall investment in the PGP as of September 30, 2014, found that its investment was valued at a deficit of \$14.6 million, consisting primarily of debt payments for acquisition costs and continual capital development of \$15.8 million in excess of amounts received from the PGP gas pools netted against FMPA’s PGP assets in excess of liabilities of \$1.2 million. The losses primarily resulted from declines in prices of natural gas from approximately \$12 per one million British Thermal Units (MmBtu) in September 2005 to approximately \$4 per MmBtu in September 2014. This deficit caused ARP members to annually subsidize the PGP investment, since the funds generated by the investment were insufficient to cover the ARP’s PGP-related revenue bonds’ required debt service amounts. As the ARP’s participation in PGP continues, the FMPA’s financial position will be subject to changes in the valuation of estimated natural gas reserves to be recovered and any additional debt required to fund ongoing PGP capital development costs.

<sup>2</sup> Comparability to the FMPA was based on reported peak MW load, wholesale electric revenues, the number of member municipalities, total number of retail customers served, and the generation fuel types employed.

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**Recommendation:** The FMPA should establish written policies regarding future gas production investments. These policies should state the circumstances under which the FMPA may consider participation in further PGP projects or other gas production investments, and the circumstances under which the FMPA may consider exiting its PGP participation. Additionally, these policies should identify the categories of risk that must be considered by the FMPA when deciding on new or increased gas production investments and place an appropriate value on risk.

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### **Follow-up to Management's Response**

*In its response, the FMPA indicated that its investment in fuel production is common industry practice and cites examples of investor owned utilities (IOUs) that have invested in fuel production. Notwithstanding the practices of selected IOUs, given the extensive difference in the regulatory environment between IOUs and the FMPA and considering that gas development investments by utilities is not universally accepted, we remain of the opinion that the FMPA should establish written policies clearly describing the circumstances and risk conditions under which such investments are to be determined appropriate.*

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### **Finding No. 3: Interest Rate Swaps**

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As previously noted, GASB Statement No. 53, in addressing the goal of effective hedging, states “effectiveness is determined by considering whether the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item.”

In December 2002, the FMPA joined a group of municipal power agencies for the planned construction of a coal powered plant in Taylor County, Florida, for an estimated total cost of \$1.6 billion. The FMPA had planned to provide this power to the ARP. The FMPA's anticipated share of the cost of the project was \$624 million, which would be funded by a bond issuance. In June 2006, the Board approved issuance of bonds and the issuance of interest rate swaps up to a \$700 million notional amount (Taylor swaps). The meeting presentation provided by FMPA staff indicated that the swaps would “lock in financing rates for a project that might not need permanent funding until the 2012 to 2015 timeframe” under the assumption that future interest rates would rise. The FMPA's expectation was that the issuance of variable interest rate debt with an accompanying pay-fixed swap would create synthetically fixed interest rate debt that would be economically advantageous to the FMPA. In September 2006, a Need for Power Determination was filed with the Florida Public Service Commission (PSC) for licensing of the Taylor County coal project.

In November 2006, the FMPA entered into 14 pay-fixed interest rate swaps (Taylor swaps), with notional amounts totaling \$700 million, whereby the FMPA agreed to pay interest on the notional predetermined rate and to receive interest on the notional amount at a variable benchmark rate. In the case of these swaps, the FMPA agreed to pay fixed interest rates ranging from 3.699 to 3.849 percent and receive variable payments of 72 percent of the 30-day LIBOR (London Interbank Overnight Rate), a variable interest rate benchmark. In February 2007, the PSC postponed the decision on the Taylor County coal project licensing, and in July 2007, the Governor issued an Executive Order prohibiting new coal plant construction. Consequently, no bonds were issued as the coal powered plant was never constructed, and the FMPA entered into swap agreements without associating those swaps with any underlying debt. Insofar as the Taylor swaps were not associated with a specific hedgeable item (bonds), the swaps were not serving to effectively manage interest rate risk.

In June 2009, when the Taylor swaps were valued at negative \$34 million, the Executive Committee voted to exit from its Taylor Swap positions but only when the exit would not result in a realized loss (i.e., a loss requiring cash outflow from the FMPA). During January through April 2010, five swaps issued for notional amounts totaling \$250

million were terminated at a gain of \$84 thousand in accordance with the Executive Committee’s directive, leaving swaps with a notional amount of \$450 million outstanding. In September 2014, when the nine remaining Taylor swaps were valued at negative \$99 million, the Executive Committee authorized staff to automatically pay the termination fee to exit the swaps when the net termination costs did not exceed \$5 million per swap contract. In the October 2014 Executive Committee meeting, staff presented several options for exiting the Taylor swaps when the value was negative \$108 million, but no official action was taken.

A review of source documents from 17 comparable JAAs<sup>3</sup> indicated that 4 of those JAAs have issued variable rate bonds with accompanying pay-fixed interest rate swaps. While issuing variable rate bonds with corresponding pay-fixed interest rate swaps is a standard industry practice, none of the 17 JAAs reported an interest rate derivative position absent an underlying bond. Entering into an interest rate derivative position absent an accompanying bond issue is more consistent with a bet that prevailing bond interest rates will rise before any accompanying bond may be issued than a hedge against interest rate changes, which represents risk-taking in excess of industry practice. Further, the Executive Committee minutes discussed above indicated that discussion of exiting the Taylor swaps was focused on avoiding the appearance of a significant realized loss rather than focused on prudent risk tolerance and projections of future changes in the fair value of the swaps.

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**Recommendation:** The FMPA should refrain from employing interest rate swaps in the future without concurrently issuing debt to bring its interest rate hedging practices more in line with industry standard risk tolerance. Further, such activities should not be undertaken before required approvals for projects are obtained from regulatory bodies. In addition, the Executive Committee should consider, without regard to prior unrealized losses incurred, developing and executing an exit strategy for the Taylor swaps that removes the ongoing risk to the ARP members.

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**Follow-up to Management’s Response**

*In its response, the FMPA asserts that interest-rate swaps are common industry practice. However, we found no evidence that employing interest rate swaps in advance of debt issuance is a practice common to other JAAs. While the FMPA may have had good reason to expect it would issue variable rate debt to match its Taylor swaps, it was taking a substantial risk based on expectation of the need for funding six years in advance. Further, when the construction of the coal plant was canceled, leaving the FMPA with an interest rate swap not attached to any underlying debt, prudent behavior suggests that the FMPA should have exited from its entire swap position expeditiously rather than remain exposed to interest rate changes against the entire \$700 million in notional principal.*

Investments
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**Finding No. 4: Investment Policy**

The FMPA reported investments with a fair value of approximately \$587 million at September 30, 2014. The FMPA promulgated a comprehensive investment policy to establish requirements for investment of idle funds, which includes the required elements specified in Section 218.415, Florida Statutes. However, some elements of the investment plan could be enhanced as described below:

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<sup>3</sup> Comparability to the FMPA was based on reported peak MW load, wholesale electric revenues, the number of member municipalities, total number of retail customers served, and the generation fuel types employed.

**Credit Ratings.** Appendix A of the investment policy provides that credit risk shall be mitigated by establishing minimum credit ratings for securities purchased by the FMPA and requires that securities be rated in either of the two highest credit rating categories, depending upon security type. However, the policy does not define “two highest credit ratings,” which could be interpreted two ways. As shown in Table 9, based on ratings used by Moody’s Investors Service (Moody’s), Standard & Poor’s (S&P), and Fitch, the two highest ratings are AAA and AA+ for both S&P and Fitch and Aaa and Aa1 for Moody’s. However, while the highest ratings description for “prime” investments includes only AAA investments for S&P and Fitch and Aaa investments for Moody’s, the next highest description of “high grade” investments includes securities rated AA+, AA, and AA- for S&P and Fitch and Aa1, Aa2, and Aa3 from Moody’s.

Table 9

Moody’s Ratings	S & P Ratings	Fitch Ratings	Rating Description
Aaa	AAA	AAA	Prime
Aa1	AA+	AA+	High Grade
Aa2	AA	AA	
Aa3	AA-	AA-	

Source: Rating agencies

Consequently, the policy could be interpreted as allowing only the top two highest ratings of AAA and AA+ for S&P and Fitch and Aaa and Aa1 for Moody’s, or it could be interpreted as allowing any investments within the prime and high grade descriptions, which would include any securities rated at or above AA- for S&P and Fitch and at or above Aa3 for Moody’s.

Based on a September 30, 2014, monthly Treasury investment compliance report prepared by FMPA personnel, securities rated AA by S&P and Fitch and securities rated Aa2 by Moody’s were listed as exceptions, which implies that FMPA personnel interpret the investment policy to only allow investments in bonds rated AA+ or higher for S&P and Fitch securities and Aa1 or higher for Moody’s rated securities. In contrast, an e-mail from the FMPA’s Treasurer to us indicated that the policy is interpreted to allow any investments rated as prime or high grade. The September 30, 2014, report indicates that FMPA investments included bonds with a face value of \$6 million that were rated lower than AA+ by S&P and Fitch and lower than Aa1 by Moody’s, which would require the Treasurer to submit a rationale to the Risk Management Department for maintaining the security if it had not been sold if the policy were interpreted to only allow AAA and AA+ for S&P and Fitch and Aaa and Aa1 from Moody’s. However, if the policy were interpreted based on the Treasurer’s e-mail, then only two bond issues, totaling \$1.1 million, one rated A+ by both S&P and Fitch, and one rated A by S&P would require reporting by the Treasurer to the Risk Management Department for maintaining the security if it had not been sold. Amending the policy to clarify the Board’s intention regarding the precise ratings allowable for various types of securities would help ensure that future investments are purchased with ratings consistent with Board intent.

Additionally, the September 30, 2014, report indicated that FMPA investments included two bond issues totaling approximately \$1.9 million, one of which was rated AA by S&P but only rated A+ by Fitch, and one rated AA-by Fitch but only rated A+ by S&P. Because the investment policy does not specifically indicate how many rating firms are required to assign a rating, and there are multiple rating agencies that sometimes assign different ratings, the policy may be subject to inconsistent application.

**Diversification.** Section 5.5 of the investment policy addresses diversification of investments, both by type of investment and by issuer, by establishing maximum percentages by type and by issuer; however, it does not address

whether the percentage limitation applies for investments held by the FMPA in its entirety or by each individual project. In practice, FMPA personnel interpret the maximum percentages as applying to individual projects; however, amending the policy to clarify the Board's intention, regarding whether the diversification percentages apply to the FMPA as a whole or to each individual project, would reduce the risk that diversification requirements may not be implemented consistent with Board intent.

Additionally, the policy does not address diversification based upon geography. Pursuant to an agreement with a forward paying agent, in which the purchasing agent would purchase and provide securities to the FMPA to pay debt associated with the St. Lucie project at a future date, the FMPA has been investing in capital appreciation bonds (CABs). CABs are deep discount debt, which do not pay interest because they are issued at steep discounts to face value and redeemed for face value at maturity. As of September 30, 2014, the FMPA had CAB investments with a face value of approximately \$155 million and fair market value of approximately \$114 million. While the CABs are diversified across several issuers, they are predominantly issued by California school districts, resulting in increased risk that a large natural disaster or localized economic conditions could impact multiple CABs simultaneously, increasing the FMPA's exposure to investment losses.

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**Recommendation:** The FMPA should enhance its investment policy to clarify the application of credit ratings. Additionally, the FMPA should enhance its investment policy to clarify that the investment diversification requirements are to be applied at the individual project level and to establish requirements for geographical diversification.

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#### Personnel and Payroll Administration

As of September 30, 2014, the FMPA employed 73 full and part-time staff and maintained 5 vacant positions. Salary and benefit expenditures for the fiscal year ended September 30, 2014, totaled \$7.2 million for administrative and general salaries and \$2.4 million for benefits.

#### Finding No. 5: Employee Benefits

The Government Finance Officer Association's (GFOA) best practice titled *Measuring the Full Cost of Government Service* (2004) indicates that it is important for all costs of government services that may not be fully funded in the current period, such as compensated absences, be used appropriately in decision making.

The FMPA has provided OPEB benefits and compensated absences benefits to its employees through its *Manual*, in employment contracts, and by Board motions. As discussed below, FMPA needs to periodically evaluate the reasonableness of these benefits and their impact on wholesale electricity rates charged to members.

**Postretirement Healthcare.** For retiring full-time employees hired prior to October 1, 2004, who are at least 55 years of age and have a total of at least 900 cumulative months of age plus months of active service, the FMPA will continue to pay the health insurance premiums, and all but \$600 of the \$5,000 (single coverage)/\$10,000 (family coverage) deductibles for qualifying retirees and dependents through FMPA's then existing group health carrier, or, if not applicable, through an equivalent insurance product. Group health insurance is also available for the retiree's eligible dependents, provided the retiree had dependent coverage prior to retirement; however, the retiree must pay the dependent's premium. In the event the retiree and covered dependents are not able to continue on the FMPA's then-current insurance policy for contractual reasons by the carrier, the FMPA will ensure that the retiree (and dependents if covered at the time of retirement) does not suffer any loss of benefits through retiree coverage.

Additionally, the FMPA will purchase a Medicare supplemental plan for retirees age 65 and above with partial coverage for prescriptions and allow the retirees and their covered dependent to submit receipts for unreimbursed medical expenses and prescription payments for reimbursement by the FMPA of up to \$3,000 each per calendar year.

In an effort to contain costs, the FMPA discontinued these benefits for employees hired on or after October 1, 2004. As of September 30, 2014, 7 FMPA retirees receive at least some of these benefits and another 26 active employees hired prior to October 1, 2004, are vested to receive benefits or will potentially vest to receive benefits, depending upon when they retire. As of October 1, 2004, none of the 26 active employees met the qualifications for these benefits, and as of December 8, 2014, 22 of the 26 employees had not vested. While these OPEB benefits are no longer available to employees hired on or after October 1, 2004, the future costs of providing the benefits to the employees that have not vested with regard to these benefits should be periodically reevaluated to determine the long-term impact these benefits will have on member rates.

**Annual and Sick Leave.** Absent contract provisions to the contrary, full-time employees earn annual leave of 10 to 20 days per year, depending upon the number of years of service, and 12 days of sick leave per year. Part-time employees also earn annual and sick leave prorated based on hours worked. The *Manual* provides that, upon termination, an employee will be paid for 100 percent of accumulated annual leave at the employee's hourly rate on the last day of employment. Employees with five or more years of service are also eligible to be paid for unused sick leave hours, at percentages ranging from 25 percent to 50 percent based on years of service at their regular salary rate as of the last day of employment in good standing. The following policies apply to usage and accumulation of leave.

- The *Manual* provides that employees may not carry forward more than two times their annual leave accrual amount into the subsequent year; however, sick leave may be accumulated without limit.
- Additionally, while hourly employees must account for annual and sick leave usage in 15-minute increments, salaried employees are not required to use annual or sick leave for absences from the office for personal business of less than 4 hours.
- Salary and benefits for the Chief Executive Officer (CEO) and General Counsel are established by the Board. The CEO's salary and benefits are delineated by contract, but as indicated in finding No. 6, the General Counsel's salary and benefits are not set forth in a contract but are established through Board actions. Neither the CEO nor General Counsel<sup>4</sup> are subject to any annual leave caps, and the CEO's sick leave is to be paid out at 100 percent of his rate of pay, rather than the 25 to 50 percent caps established for other FMPA personnel. Additionally, the CEO was awarded a total of 600 additional hours of annual leave to be added to his leave balance as part of contract amendments dated February 16, 2012, October 1, 2013, and October 16, 2014.

Based on these leave usage and accumulation policies, total hours of annual and sick leave that will be paid upon employee resignation or retirement have steadily accumulated over time and may result in significant future payouts as employees retire. For example, as of September 30, 2014, had the CEO and General Counsel resigned or retired, the FMPA would have been required to pay approximately \$355,000 for accumulated annual and sick leave attributable to these two individuals.

The compensated absences liability, by annual and sick leave balances by fiscal year for all employees, including the CEO and General Counsel, are included in Table 10.

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<sup>4</sup> According to FMPA personnel. As discussed in finding No. 6, FMPA records did not evidence the official Board action establishing the General Counsel's annual leave provisions.



Table 10

Fiscal Year Ended September 30	Total Accrued Sick Leave Hours	Sick Leave Liability	Total Accrued Annual Leave Hours	Total Annual Leave Liability	Total Compensated Absences Liability
2010	17,961	\$252,695	8,991	\$470,240	\$ 722,935
2011	19,402	315,904	10,163	535,345	851,249
2012	20,963	407,794	10,886	617,411	1,025,205
2013	22,778	477,271	11,711	675,254	1,152,525
2014	23,545	491,675	12,941	771,757	1,263,432

Source: FMPA Records

As shown in the table above, from the 2009-10 fiscal year to the 2013-14 fiscal year, the projected compensated absences liability has increased by \$540,497, or 75 percent, from \$722,935 to \$1,263,432. Insofar as the ongoing growth in the compensated absences liability will ultimately result in actual cash payouts in the future, current leave provisions established by policy and contract provisions should be periodically reevaluated for reasonableness and to determine the long-term impact these benefits will have on member rates.

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**Recommendation:** The FMPA should periodically evaluate the impact of projected increases in benefit package costs provided to employees.

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**Finding No. 6: General Counsel Contract**

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The *Manual* states, “The Board shall set the position level, pay range, and specific components of the total compensation package for the General Counsel and the CEO.” The CEO and General Counsel have received benefits, such as additional annual leave and contributions to retirement health savings accounts, which are not afforded to other FMPA employees. While the Board has documented this process for the CEO through the establishment of a contract and associated amendments, no contract has been established for the General Counsel; rather, the General Counsel’s compensation package has been established pursuant to a series of Board-approved motions spread over several years, making it difficult to identify all benefits provided. For example, the General Counsel’s annual leave is not subject to the cap established for regular employees in the *Manual*; however, although requested, FMPA personnel did not provide us Board minutes evidencing the Board action that exempted the General Counsel from caps on annual leave accrual. While Board minutes from September 17, 2010, clearly indicate that the Board was aware that the General Counsel could earn unlimited annual leave, lack of a contract enumerating compensation provisions creates difficulty in verifying that the General Counsel’s pay and benefits are in accordance with the Board’s intent and increases the risk of error due to inability to locate Board motions establishing specific aspects of salary and benefits and misinterpretation of same.

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**Recommendation:** The FMPA should enter into a contract with the General Counsel encompassing all Board-approved compensation arrangements cumulatively provided to the General Counsel and implement any further compensation changes as contract amendments.

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**Finding No. 7: Severance Pay and Benefits**

As indicated in finding No. 5, the Board sets the CEO’s compensation package based upon a Board-approved contract and amendments thereto. Paragraph 3(d) of the contract in effect as of September 30, 2014, indicated that the CEO would receive six months of base salary if terminated for cause. Under these contract provisions, if the CEO was terminated with cause as of September 30, 2014, the CEO would have received a one-time payout equal to 50 percent of his annual salary, totaling \$137,500. Contract provisions also indicate that certain healthcare benefits are to be retained after termination for a certain number of months based upon the termination date. The contract provides that the FMPA will either pay for, or reimburse, the CEO’s health insurance premiums for life and fund the CEO’s health reimbursement account (HRA) for life. The current annual costs of health insurance and HRA contributions, to be provided for life, are \$4,946 and \$9,400, respectively.

While including severance compensation and postretirement benefits in the CEO’s employment contract for termination without cause may serve a valid business purpose, it is not apparent why the FMPA would extend these provisions to instances in which the CEO is terminated for cause.

**Recommendation:** The FMPA should consider amending the CEO’s contract to remove any severance compensation and postretirement benefits associated with termination for cause.

**Procurement of Goods and Services**

**Finding No. 8: Questioned Expenditures**

Expenditures of public funds must be shown to be authorized by applicable law or resolution; reasonable in the circumstances and necessary to the accomplishment of authorized purposes of the governmental unit; and in pursuit of a public, rather than a private, purpose. The Attorney General has indicated on numerous occasions that documentation of an expenditure in sufficient detail to establish the authorized public purpose served, and how that particular expenditure serves to further the identified public purpose, should be present at the point in time when the voucher is presented for payment of funds. The Attorney General has further indicated that unless such documentation is present, the request for payment should be denied.

We judgmentally selected and reviewed 59 expenditures made during the period October 2012 through June 2014 totaling \$358,029 and noted 16 expenditures totaling \$28,297 for which FMPA records did not evidence the public purpose, as follows.

**Employee Activities, Awards, and Recognitions.** The FMPA charged and coded \$82,354 to “Employee Activities” or “Awards and Recognition.” Of the 59 expenditures tested, 11 expenditures totaling \$23,844 were charged to these accounts for which FMPA records did not evidence the public purpose served, as noted in Table 11.

Table 11

Expenditures Coded to Employee Activities or Awards and Recognition	
Amount	Description
\$12,688	Holiday parties
4,627	Purchase of 86 adult and 13 child tickets to a local tourist attraction for FMPA's summer picnic
3,270	Gift cards given to staff for birthdays, anniversaries, overall appreciation
2,098	For 2 Orlando Magic season tickets to be used each game by an employee and guest
905	Luncheon to raise funds for charity purchases
256	Retirement party
<b>\$23,844</b>	<b>Total</b>

Source: FMPA Records

- **Flowers.** The FMPA charged and coded \$12,030 to “flowers.” One of the 59 expenditures tested of \$1,517 was for rental of a Christmas tree and decorations for the FMPA’s office building. The FMPA’s records did not evidence the public purpose served by this expenditure.
- **Meetings.** The FMPA charged and coded \$106,850 to “meetings.” Of the 59 expenditures tested, one expenditure for \$1,206 was a payment to a refreshment services company for one month of beverages, and another was a \$965 payment to another vendor for various utensils, paper products such as plates and cups, and other various supplies, all of which are monthly recurring expenditures for stocking the FMPA catering and break rooms. A total of \$44,809 was paid to these two companies during the period October 2012 through June 2014.
- **Other.** One of the 59 expenditures tested was a \$616 payment to a restaurant for an employee fun day/field day for which FMPA records did not evidence the public purpose.

Absent documentation evidencing how expenditures serve an authorized public purpose, there is an increased risk that expenditures may not be reasonable or necessary to serve a public purpose.

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**Recommendation:** The FMPA should strengthen its procedures to require documentation that expenditures serve an authorized public purpose and retain such documentation in its records prior to payment.

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**Finding No. 9: Competitive Selection**

The FMPA’s Purchasing Policy, as part of the *FMPA Policy and Employee Manual* (Manual) establishes thresholds for the purchase of goods and services as follows: purchases with a value above \$1,000 and below \$5,001 require a minimum of three quotes obtained via the internet, e-mail, written, or verbal communication (verbal requires documentation); purchases with a value above \$5,000 and below \$10,001 require three written quotes; and purchases with a value above \$10,000 require three formal bids or proposals, unless less than three bids or proposals are received. In addition, purchases with a value above \$25,000 require approval of the Executive Committee (for FMPA administrative and ARP transactions) or Board of Directors (for non-ARP transactions), as appropriate.

We reviewed 18 purchases of goods or services exceeding \$1,001 during the period October 2012 through June 2014 for compliance with FMPA’s Purchasing Policy and noted the following:

- For four purchases above \$1,000 and below \$5,001, consisting of furniture repairs, an ice machine purchase, Christmas tree decoration and rental, and embroidered jackets, FMPA records did not evidence that three

quotes were obtained. The FMPA obtained one quote for each of the first three items and FMPA records did not evidence proper justifications for not obtaining the required three quotes for these purchases. The FMPA did not obtain any quotes for the fourth item, which FMPA personnel indicated was a sole source purchase; however, it was not evident why jacket embroidery would entail a sole source exemption.

- For a purchasing arrangement, exceeding \$10,000 annually but not \$25,000 annually, for break room supplies, only one proposal was obtained. FMPA records did not evidence proper justification for not obtaining the required three bids or proposals.
- During the period October 2012 through June 2014, the FMPA expended \$189,062 for financial audit services. The contract, dated May 8, 2009, with the FMPA's financial statement auditors was for the 2008-09, 2009-10, and 2010-11 fiscal years with optional renewals for the 2011-12 and 2012-13 fiscal years. The FMPA Accounting and Internal Controls Policy Section 5.2 provides that no audit firm shall be selected for more than a five-year term with two additional one-year optional extensions. However, the FMPA Board, at its April 17, 2014, meeting voted to accept the recommendation from the Audit Risk Oversight Committee and "deviate from the Accounting and Internal Controls Policy" and the FMPA's Purchasing Policy and issued a new contract for an additional three years with two optional renewals, expiring with the 2017-18 fiscal year audit. Failure to follow established competitive selection processes increases the risk that the FMPA will not acquire goods and services at the lowest cost consistent with acceptable quality.

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**Recommendation:**     **The FMPA should ensure that goods and services purchased through contractors are competitively procured in accordance with established policies and procedures.**

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#### **Finding No. 10: Selection of Bond Professionals**

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Governments typically employ a number of professionals to assist them in the bond issuance process; primarily a financial advisor, an underwriter, and bond counsel. Financial advisors can be used in determining the bond sale method and may have various other roles depending on which sale method is selected.<sup>5</sup> The primary role of the underwriter in a negotiated sale is to market the issuer's bonds to investors. Assuming that the issuer and underwriter reach agreement on the pricing of the bonds at the time of sale, the underwriters are likely to provide ideas and suggestions with respect to structure, timing, and marketing of the bonds being sold.<sup>6</sup> Bond counsel renders an opinion on the validity of the bond offering, the security for the offering, and whether and to what extent interest on the bonds is exempt from income and other taxation. The opinion of bond counsel provides assurance both to issuers and to investors who purchase the bonds that all legal and tax requirements relevant to the matters covered by the opinion are met.<sup>7</sup>

The GFOA recommends that issuers selecting financial advisors, underwriters, and bond counsel employ a competitive process using a Request for Proposal (RFP) or Request for Qualifications (RFQ). A competitive process allows the issuer to compare the qualifications of proposers and to select the most qualified firm based on the scope of services and evaluation criteria outlined in the RFP or RFQ. A competitive process also provides objective assurance that the best services and interest rates are obtained at the lowest cost possible and demonstrates that marketing and procurement decisions are free of self-interest and personal or political influences. Furthermore, a competitive process reduces the opportunity for fraud and abuse and is fair to competing professionals.<sup>8</sup> The GFOA's best practice further recommends that debt issuers review their relationships with bond professionals periodically.

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<sup>5</sup> GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014)

<sup>6</sup> GFOA Best Practice: *Selecting and Managing Underwriters for Negotiated Bond Sales* (2014)

<sup>7</sup> GFOA Best Practice: *Selecting Bond Counsel* (1998 and 2008)

<sup>8</sup> GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014); GFOA Best Practice: *Selecting and Managing Underwriters for Negotiated Bond Sales* (2014); GFOA Best Practice: *Selecting Bond Counsel* (1998 and 2008)

- **Financial Advisor Services.** Contrary to the GFOA's best practice, the FMPA contracted with its current financial advisor since 1978 without utilizing effective competitive selection. In April 2007, the FMPA did undertake a financial advisor selection process by forming a Financial Advisor Committee (Committee) and issuing an RFQ for financial advisor services. Four firms responded and gave presentations in July 2007 to the Committee. Subsequently, the Committee sent the firms a list of questions and requested written responses. The existing financial advisor did not provide written responses and withdrew from the selection process. The Committee met on August 24, 2007, to select a financial advisor from the remaining three firms, and unanimously recommended a new financial advisor to be presented to the Board for approval. However, on September 27, 2007, the Board voted to table the RFQ and to issue a new RFQ to the initial four firms to be awarded solely on a retainer and hourly fee basis, retaining its existing financial advisor in the interim. On October 5, 2007, the Committee evaluated the retainer and hourly fees submitted by the four financial advisors and selected its existing financial advisor, although the rates were higher than the other three respondents, because the Committee members felt comfortable working with the financial advisor.<sup>9</sup> At the December 6, 2007, Board meeting, the Committee recommendation was presented to the Board for approval. Despite FMPA staff recommendations to consider two of the other financial advisors, the Board voted to continue contracting with its existing financial advisor.

In addition, the RFQ indicated that the resulting contract would be for a three-year period, with two optional one year extensions, for a total of five years; however, the contract signed with its existing financial advisor dated December 6, 2007, indicated that "the term of this contract is for so long as the parties continue to both desire to be bound by this contract." Accordingly, as of September 30, 2014, the FMPA has made no additional effort to competitively select a financial advisor

- **Bond Counsel Services.** Contrary to the GFOA's best practice, the FMPA last contracted with its bond counsel in 1996 and had not, as of November 2014, issued an RFP or RFQ for bond counsel services.

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**Recommendation:** To ensure that qualified financial and professional services are acquired at the lowest possible cost consistent with the size, nature, and complexity of the bond issue, the FMPA should select financial advisors and bond counsel using a competitive selection process whereby RFPs or RFQs are solicited from a reasonable number of professionals.

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### Finding No. 11: Credit Cards

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During the period October 2012 through June 2014, the FMPA had 51 active credit cards, including 42 issued to its own employees and 9 issued to employees of member municipalities. The 9 credit cards issued to employees of member municipalities were issued to allow individuals with responsibility for power plant maintenance to purchase small tools and supplies and to travel for FMPA business purposes, such as preventive maintenance at the Stock Island plant. FMPA policies require credit card users to sign user agreements indicating their understanding of the credit card policy and responsibilities regarding credit cards before the user is issued a card.

For the period October 2012 through June 2014, We reviewed 21 user agreements and tested 29 credit card expenditures totaling \$52,331, and noted the following:

- Of 21 credit card agreements selected for review, FMPA records did not evidence signed agreements for 3 (14 percent) credit cards issued. Upon our inquiry, FMPA personnel indicated that user agreements were signed prior to credit card issuance but had been misplaced. Subsequently, in September 2014, all three users signed new user agreements. Failure to obtain signed user agreements prior to issuing credit cards increases the risk that inappropriate purchases could occur.
- Good business practice requires that credit card users attest to their respective purchases by signed monthly credit card activity reports. Of the 29 credit card purchases tested, we noted 5 instances related to 3 employees, in which the employees did not sign the monthly activity reports. While the reports were signed

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<sup>9</sup> The financial advisor provided services to four of the five member municipalities.

by the employees’ supervisors in accordance with FMPA policy, when employees do not review and attest to their purchases, there is an increased risk that errors or unauthorized purchases could occur without timely detection.

The FMPA *Policy and Employee Manual* requires employees to return their credit cards upon termination but is silent as to where they are to be returned. The FMPA’s informal procedure is that either the terminated employee’s supervisor or the Human Resources Department is to notify the credit card administrator, the Chief Financial Officer, so that the card may be canceled electronically. No FMPA employees with credit cards terminated employment during the period October 2012 through June 2014; however, one employee of a member municipality terminated in April 2014, but the employee’s credit card had not been canceled at the time of our review in September 2014. Subsequent to our inquiry, the FMPA canceled the card in October 2014. FMPA personnel informed us that the card was not timely canceled because the member municipality had not notified the FMPA credit card administrator of the employee’s termination. Untimely cancellation of credit cards of terminated individuals increases the risk of unauthorized credit card activity.

The FMPA established a monthly credit limit for each individual assigned a credit card, and the credit limits ranged from \$2,500 to \$15,000. However, the FMPA had not established procedures to periodically monitor the reasonableness of credit card limits, such as comparing credit card limits to actual credit card activity. Effectively monitoring the reasonableness of credit card limits would reduce the FMPA’s dollar exposure in the event that the credit cards are used for unauthorized purchases.

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**Recommendation:** The FMPA should enhance its procedures to ensure compliance with its policies regarding credit card user agreements. The FMPA should also enhance its existing policies to clarify responsibilities regarding notification of credit card user termination and associated card cancellation, including notification requirements of member municipalities; require all credit card users to sign the monthly credit card activity reports; and require periodic reviews of credit card user credit limits for reasonableness.

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Travel
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**Finding No. 12: Travel Expenditures**

Section 166.021, Florida Statutes, provides that the governing body of a municipality or an agency thereof may provide for a per diem and travel expense policy for its travelers that varies from the provisions of Section 112.061, Florida Statutes. Accordingly, the FMPA, as a municipal agency, has established policies and procedures related to travel in its *Per Diem and Travel Expense Policy (Travel Policy)*. During the period October 2012 through June 2014, FMPA charged and coded a total of \$591,999 to account codes “travel,” “Board of Director travel,” “government relations events,” and “training.” We tested 26 expenditures charged to these account codes during this period totaling \$95,543 and noted the following:

- **Meal Cost.** The *Travel Policy* provides that “Each employee or officer will be reimbursed for his or her actual meal expenses incurred that are just and reasonable as determined by the General Manager (or Chairman of the Executive Committee in the case of the General Manager).”<sup>10</sup> Insofar as there are no ranges or limitations on meal costs individually or in aggregate in the *Travel Policy*, the potential exists for inconsistency in determining what qualifies as “just and reasonable” and for excessive meal costs to occur. Specifically, we noted 2 payments of \$3,453 and \$3,830, coded as “travel” and “government relations events,” respectively, paid to the same restaurant during the annual legislative rallies in Washington, D.C., in March 2014 and March 2013, respectively. The average expenditure per meal per person of \$105 in 2014 and \$109 in 2013,

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<sup>10</sup> The term General Manager and Chief Executive Officer are used interchangeably by the FMPA.

appear to be excessive. Additionally, \$1,022 and \$1,207 of the bills from 2014 and 2013, respectively, included alcoholic beverages, which are not expressly prohibited by the *Travel Policy*, and associated taxes and tips.

- **Family Travel Expenses.** The *Travel Policy* provides that if any expense of a spouse is paid in conjunction with the travel expense of an officer or employee, FMPA will invoice the officer or employee who shall promptly reimburse FMPA for such expense.

In connection with the 2013 Florida Municipal Electric Association (FMEA)/FMPA Annual Conference, FMPA paid \$14,420 for hotel rooms and meeting rooms for its employees including three hotel rooms costing \$1,080 for family members of the FMPA's CEO, General Counsel, and former Chairman of the Board. The FMPA also paid \$42 for valet charges for the family of the Chairman of the Board. For the 2014 FMEA/FMPA Annual Conference, FMPA paid \$14,163 for hotel rooms and meeting rooms for its employees including two hotel rooms costing \$1,295 for family members of the CEO and General Counsel. Contrary to the *Travel Policy*, these hotel expenses and associated valet expenses were not initially invoiced to officers and employees and reimbursed to the FMPA. Subsequent to our inquiry, the FMPA researched personal use of rooms for the CEO and General Counsel from 2010 through 2014 and received reimbursement totaling \$5,727 from the CEO and General Counsel for such personal use of these rooms.

- **Most Economical Class of Air Travel.** The *Travel Policy* states, "If transportation other than the most economical class is provided by common carrier, the officer or employee must reimburse FMPA for charges in excess of the most economical class." An exception may be authorized by the CEO, Chairman of the Executive Committee, or a designated representative when "there is no reasonable alternative." We noted five departures from this policy as follows:

- One instance in which the most economical seat on an airline was not purchased. A reimbursement to the CEO for his trip to the 2014 Keys Strategic Planning Workshop included \$626 for roundtrip airfare from Orlando to Key West. However, the tickets were for "Business Select," while a fellow FMPA employee purchased a standard ticket on the same flight for \$495. FMPA records did not evidence the lack of a reasonable alternative (i.e., purchase of a standard ticket), contrary to the *Travel Policy*. In response to our inquiry, FMPA staff indicated that the "Business Select" tickets were fully refundable and were purchased by the CEO in case he was not able to attend the event; however, such explanation was not documented in the FMPA records at the time of the ticket purchase.
- Four instances, totaling \$287, of charges for "preferred" or "choice" seating, three of which were paid to the employees as travel reimbursements and one paid directly to the airline using an FMPA credit card. FMPA records did not evidence the lack of a reasonable alternative (i.e., standard seating), contrary to the *Travel Policy*.

- **Contractor Travel.** The FMPA paid \$6,343, coded as "travel" in its accounting system, for consultant's fees of \$4,950 and travel costs of \$1,393. The contract with the consultant stated that, "All invoices shall be accompanied by reasonable supporting information in a manner sufficient for FMPA to verify the services performed by the Consultant." However, the travel costs invoiced, which were comprised of \$833 for airfare, \$236 for rental car and gas, \$272 for lodging, \$36 for meals, and \$16 for miscellaneous expenses, were not supported by receipts or other documentation. Absent such documentation, the FMPA could not substantiate the reimbursement requested and paid.

- **Vehicle Allowances and Mileage Reimbursements.** The FMPA has authorized ten employee positions to receive vehicle allowances, which are paid in biweekly installments. Of these ten positions, nine are authorized at the annual rate of \$5,877, and one position is authorized at the annual rate of \$9,396. In addition, the *FMPA Policy and Employee Manual* allows for these employees to also receive mileage reimbursement in the amount of half of the approved mileage rate paid to employees not receiving a vehicle allowance, although the employment contract of the employee authorized a vehicle allowance at an annual rate of \$9,396 indicated the employee should receive full mileage reimbursement at the approved rate. During the period October 2012 through June 2014, the employees were paid a total of \$93,495 for vehicle allowances and \$47,052 for travel reimbursements, which includes other travel reimbursements in addition to mileage reimbursements. FMPA records did not evidence the basis for the established travel allowance amounts. In addition, it is not apparent why employees receiving vehicle allowances to compensate them for

business use of their personal vehicles also receive full or partial mileage reimbursement for business use of their personal vehicles.

**Recommendation:** The FMPA should consider amending its *Travel Policy* to include a cap on per-meal costs. The FMPA should also enhance its procedures to ensure compliance with its policies regarding family member travel expenses and most economical cost of air travel, and to require supporting receipts for out-of-pocket expenses incurred by contractors. In addition, the FMPA should discontinue providing mileage reimbursements to employees who also receive vehicle allowances.

### All Requirements Project (ARP) Contract Provisions

#### Finding No. 13: Peak Shaving

ARP monthly rates are primarily comprised of three components: demand charge, energy charge, and transmission charge. The demand charge is comprised of fixed costs, the largest of which, is debt service costs. Schedule B-1, Part 5, of the ARP power supply project contract specifies that the demand charge cost component is to be allocated based on electricity consumption during the peak hour of the peak day of integrated demand for the entire ARP system, which the FMPA refers to as “coincident peak demand.”

The demand charge is allocated among ARP members based on the relative percentage of power purchased from the FMPA on the monthly coincident peak demand day. The coincident peak demand day is the day of the month for which overall ARP power usage is highest, and because the demand component of the monthly FMPA electricity bill is based solely on a member’s percentage share of power usage on the coincident peak demand day, members have financial incentive to predict the day of coincident peak demand and reduce electricity consumption on that day. Temporary attempts to control or lower the ARP member’s load at the time of the ARP’s coincident peak demand to reduce the demand cost component on an ARP member’s monthly bill is termed “peak shaving.” However, the total ARP demand costs are fixed, so any actions taken by one ARP member to lower its power consumption on the coincident peak demand day adds a dollar-for-dollar cost increase to other members’ demand costs. The ARP power supply project contracts do not address peak shaving.

The FMPA submitted surveys to ARP members regarding management of their local electric systems, and the minutes of the February 7, 2014, Executive Committee meeting, noted that the Cities of Fort Meade, Fort Pierce, Jacksonville Beach, and Leesburg indicated that they conducted peak shaving activities such as utilizing their own power rather than power obtained through the FMPA to reduce their FMPA demand on peak days. Examples of these peak shaving activities are as follows:

- According to minutes of the FMPA’s Executive Committee meetings, in 2013, the City of Fort Meade began utilizing a City-owned generator to shave peak and planned to connect an additional generator to its system.
- A review of the Fort Pierce Utility Authority’s February 19, 2013, meeting minutes disclosed that the Authority consistently shaves peak as follows: staff monitors ARP load in real time with a one-hour delay, and concurrently monitors weather forecasts to predict ARP peak demand days and then shaves peak through load management, generators, and customer generators.
- The City of Jacksonville Beach City Council meeting minutes from March 1, 2010, and a memorandum dated February 25, 2011, describe an arrangement in which the City contracted with an energy services provider and issued memoranda of understanding with certain commercial power companies whereby the energy services provider would continually monitor ARP load and would remotely activate City-owned generators and commercial customer generators during peak periods. The minutes indicate that the City’s intent in taking these actions was to shave peak through the use of alternative power sources. .



- A review of the City of Leesburg's January 21, 2014, Commission Report, indicated that the City consistently and intentionally shaved peak through use of its own generators, commercially owned generators, solar stations, and load control devices such as programmable communicating thermostats. Usage of these items at times of predicted ARP peak, lowers usage on the ARP coincident peak demand day, thereby lowering the demand component of the FMPA bill and shifting the costs to other members.

Under the coincident peak demand methodology, ARP members with the resources to monitor and manage demand (whether peak shaving or a broader program of demand side management) to reduce their monthly peak demand coincident with FMPA's coincident peak demand have a distinct advantage over members without such resources. In an attempt to address the effects of peak shaving and demand side management, the FMPA formed a Business Model Working Group to evaluate alternative rate structures. On February 24, 2011, the Executive Committee approved an alternate demand cost rate calculation methodology by an 8 to 6 vote; however, the City of Leesburg called for a supermajority vote pursuant to Article IV, Section 5 of the Executive Committee Bylaws, and the resulting 9 to 5 vote in favor of changing the cost methodology failed to achieve the required 75 percent supermajority affirmation. Subsequently, at the May 15, 2014, Executive Committee meeting, a motion passed whereby certain peak shaving practices would be curtailed as follows:

- By September 30, 2014, ARP members will not engage in intermittent voltage reduction methods to shave peak or to deploy ARP member-owned emergency generation to intentionally reduce system demand costs.
- By September 30, 2014, ARP members must notify the FMPA within ten days each time any of its emergency generators are operated above or beyond routine operational testing.
- By September 30, 2015, ARP members will not deploy customer emergency generation to intentionally reduce the ARP member's demand costs.

While the policy addresses certain peak shaving activities, it appears primarily voluntary in nature and relies on self-reporting of ARP members, although FMPA personnel has informed us that the FMPA will be reviewing hourly meter data for potential peak shaving. Additionally, no consequences for noncompliance are specified in the approved motion, and according to FMPA personnel, any consequences would be within the Executive Committee's discretion.

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**Recommendation:** If the FMPA desires to affirmatively eliminate peak shaving activities of its members, the FMPA should consider amending the power supply project contracts to prohibit such activities and establish consequences for noncompliance.

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#### **Finding No. 14: ARP Termination Provisions**

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The FMPA has issued revenue bonds to finance the cost of generating units planned and constructed or procured to supply the total power and energy requirements for the ARP. Power supply project contracts between the FMPA and ARP members were utilized to provide the underlying security for repayment of the bonds. The bond resolution establishes the specific obligations of the FMPA related to bond issuance and specific performance requirements over the life of the bond issue, and describes the substantive provisions of the underlying power supply project contracts. These types of bond resolution and power supply project contract provisions are typical of other JAAs.

The power supply project contracts between the FMPA and ARP members are 30-year contracts that are automatically extended annually so that the contractual period remains at 30 years. However, Sections 2 and 29 of the ARP power supply project contracts provide that members may terminate participation in the project. Section 2 provides for a long-term termination through elimination of the automatic extensions to the contract with a specified notice period. Section 29 provides the participant the right to terminate its contract and withdraw from the ARP in

three years with at least three years prior written notice. Section 29(c) identifies the fixed costs, defined as two categories, which must be paid by the participant in the event of withdrawal, as follows:

- **Debt.** Section 29(c)1. establishes the member's responsibility to pay a portion of the ARP's outstanding bonds as of the termination notice or withdrawal date. Such payment is based on the greater of the ARP member's load ratio share of the outstanding bonds as of the date of its termination notice, or its load ratio share as of its withdrawal date. Specifically, these fixed costs are calculated as the amount needed to retire the member's current share of all bond principal and interest paid to maturity or redemption, bond premiums, and lines of credit. The member's excluded resources and ARP's excluded resources<sup>11</sup> are subtracted from the coincident peak demand calculation to estimate the member's share.<sup>12</sup> The calculation estimating the withdrawing ARP member's share to retire debt assumes that the bonds are serviced to maturity. A percentage (applicable to the member and rounded to the minimum allowable denomination) of each series, and each maturity within each series, is applied to calculate the member's obligation. The member's share of interest cost is calculated from termination notice or withdrawal date to maturity date of the debt. The FMPA calculates the load ratio share percentage using a single summer coincident ARP peak demand. However, since the ARP fixed cost component of revenue requirements are calculated using monthly coincident peak demands, using a 12-month average of coincident peak demand would more accurately estimate the withdrawing member's share of fixed costs.
- **Stranded Costs.** Section 29(c)2. establishes the withdrawing ARP member's responsibility to pay for "all of the additional costs reasonably paid or incurred, reasonably anticipated to be paid or incurred, or reasonably projected to be incurred by FMPA (as determined by FMPA in its sole discretion) as a result of the withdrawal of the Project Participant," which is commonly referred to in the electrical utilities industry as "stranded costs." Further, such costs are based on the assumption that, "during the remaining term of such Project Participant's All-Requirements Power Supply Project Contract, FMPA was unable to make use of or sell any generating, transmission or other resources (or portions thereof) which FMPA had anticipated would be used to supply, or had acquired with the intention of supplying, all or any portion of the withdrawing Project Participant's electric load" Specifically, these costs are calculated as the member's share, as of the date of notice termination, of all operational fixed costs applicable to the member and projected through the remainder of the power supply project contract term, expressed in current dollars. Consequently, the ARP contract termination provisions place all risk on the withdrawing member. The concept of assessing stranded costs to withdrawing customers is an established utility industry concept.<sup>13</sup>

The calculation of projected operational fixed costs to be paid by a participant in the event of withdrawal employs the most recently approved fiscal year budget with an assumption for inflation of 2.4 percent per annum applied to each ARP operational fixed cost applicable to the member, including deposits to the Renewal and Replacement and the General Reserve Funds. Known ARP project costs applicable to the member and expected in future years (such as expiration of purchased power agreements and major plant overhauls) are applied in addition to the projections of the recent budget. The present value of the member's share of all projected operational fixed costs on the withdrawal date is calculated at the discount rate of 6 percent per year, which was set in the initial ARP power supply project contract with no provision to calculate a current cost of capital for a current discount rate. In utility rate-setting, discount rates are typically related to the current average embedded cost of debt rather than being fixed over the term of the contract. Over the extended period of the contract, the average embedded cost of debt may vary substantially from the fixed 6 percent rate. Each ARP power supply project contract provides for:

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<sup>11</sup> Excluded resources are the amount of electric capacity and energy that an ARP member is entitled to receive (a) from its percentage of undivided ownership interest in a generation unit (based on the seasonal net capability of the unit), (b) pursuant to a power supply project contract determined in accordance with its power entitlement share under said contract, or (c) any other member-owned generation projects such as hydro projects. Excluded resources may require back-up and support services under the member's ARP power supply project contract with FMPA.

<sup>12</sup> Based on industry practice, this is a reasonable form of practice to employ in this form of calculation.

<sup>13</sup> The Federal Energy Regulatory Commission (FERC), which has jurisdiction over wholesale electricity sales, issued a ruling in May 1996 (Ruling No. 888) that certain utilities could recover 100 percent of their wholesale stranded costs.

- An annual “true-up” to actual costs. The “true-up” provision for the withdrawing ARP member would be applied in each year following withdrawal to adjust the projected operational fixed costs applicable to the withdrawing member with actual fixed costs; however, the application is at the sole discretion of the FMPA.
- An annual payment to the member of “additional benefits” actually received by the FMPA during the preceding year as a result of such withdrawal as calculated by the FMPA in its sole discretion, which is capped at 90 percent of the withdrawal payment. However, the power supply project contract does not provide any rationale for the 90 percent cap on “additional benefits” and does not clearly specify what constitutes “additional benefits.”
- Any annual payments to the withdrawing member for “additional benefits” to be made from a separate account established for withdrawal payments, or recognized as an ARP expense if the funds are no longer available in the separate account.
- An accounting treatment to pay these annual amounts to the member from the separate account maintained for withdrawal payments.
- Use of the withdrawal payment funds to temporarily correct deficiencies in other operating funds.
- Provisions for the FMPA to use “excess amounts” of the funds from the withdrawal payment account at its sole discretion. However, there is no clear specification in the power supply project contract of what constitutes “excess amounts.”

Although one ARP member submitted a termination notice that indicated a withdrawal date of September 30, 2016, no ARP members have actually withdrawn from the FMPA. As such, the FMPA has not prepared any such true-up calculations and it is not clear how the FMPA will interpret the terms “additional benefits” and “excess amounts” when the member ultimately withdraws. The FMPA’s sole discretion to determine “additional benefits” to the member and move “excess” amounts to the “General Reserve Fund” enables the FMPA to unilaterally direct the use of withdrawal payments beyond the assurance of the fixed costs responsibility of the withdrawing member.

A review of termination and exit provisions of bond resolutions and power supply project contracts as described in the official statements for eight JAAs’ all requirements service system revenue bond issues<sup>14</sup> disclosed that only four of the eight JAAs’ power supply project contracts contain any exit provisions, such provisions are highly restrictive, and none of these JAAs provided for a three-year notice termination provision. Three of the four JAAs provided for member withdrawal but only when there is no debt outstanding, which is standard industry practice. While debt-free JAA projects can occur, it is not the industry norm for JAA projects to be debt-free. Based on the results of the review, the FMPA’s termination and exit notice provisions are not consistent with common JAA practice because JAA power supply contracts normally do not allow members to exit the contract while any project debt is outstanding. As indicated above, only one other JAA allowed a member to exit while project debt was still outstanding, and the contract required the withdrawing member to pay its share of debt service, which is consistent with the FMPA contract provisions.

The FMPA’s assumptions used in estimating the withdrawing member’s share of costs to retire debt and project operational fixed costs, and the practice of subtracting excluded resources from the coincident peak demand calculation to estimate the member’s share, appear to be reasonable. An evaluation of the FMPA’s calculations of estimated withdrawal payments in April 2012 and June 2014, in the amounts of \$386 million (\$108 million for debt and \$278 million for operational fixed costs) and \$46 million, for the Cities of Key West and Vero Beach, respectively, disclosed that the primary differences in the withdrawal payments for the two Cities are (1) Key West would be required pursuant to its contract with the FMPA to purchase at net value all generation, transmission, and related

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<sup>14</sup> The official bond statements of these JAAs contained summaries of power sales contracts in sufficient detail to identify the relevant termination provisions. While such official statements do not include provisions of power supply project contracts and bond resolutions in their entirety, they do provide summary language covering their most substantive provisions.

assets owned by the FMPA in providing ARP service to Key West, and (2) Vero Beach would not be required to pay the debt component as the City had not, since 2010, obtained any power through the ARP. The FMPA’s calculations of the withdrawal payments in these instances followed the respective ARP power supply power contracts’ withdrawal provisions. However, the fact that the FMPA has the sole discretion in determining the actual severance amount and the substantial cash payment due on withdrawal, in effect, represents a compelling case against the decision for an ARP member to withdraw.

**Recommendation:** Since ARP revenue requirements are calculated using monthly coincident peak demands, the FMPA should consider using a 12-month average of coincident peak to more accurately estimate the withdrawing member’s share of fixed costs. Also, the FMPA should consider amending the power supply project contracts to clarify how withdrawal payments are to be calculated, define “additional benefits” and “excess amounts,” establish a variable withdrawal payment discount rate that fluctuates with the actual cost of debt, and remove the 90 percent cap of an ARP member’s withdrawal payment. Additionally, since the withdrawal payment can be used to temporarily correct deficiencies in other operating funds and for “excess amounts” to be deposited in the “General Reserve Fund,” it should be determined how this ability to use these funds is recognized in the monthly revenue requirement calculation for remaining ARP participants.

**Follow-up to Management’s Response**

*In its response, the FMPA indicated that using a 12-month average of coincident peaks would detach the withdrawal payment from the reality of FMPA’s obligation and could put the non-withdrawing participants at risk of bearing higher debt service. The FMPA is required to fully recover its costs. To this end, the FMPA uses a 12-month coincident peak billing methodology to recover its demand costs. As the FMPA deems the 12-month coincident peak billing methodology to be adequate to fully recover its costs on a monthly and annual basis, it is not apparent why it would use a different methodology (the single highest coincident peak) when calculating the withdrawal payment, essentially penalizing the withdrawing member.*

**Information Technology**

**Finding No. 15: Disaster Recovery Plan**

An important element of an effective internal control system over information technology (IT) operations is a disaster recovery plan to help minimize data and asset loss in the event of a major hardware or software failure. One essential element of a disaster recovery plan is a written agreement for an alternate processing facility that can be utilized for continuity of operations, if necessary, including the specific responsibilities of both parties relating to the availability and use of the facility.

While the FMPA had a disaster recovery plan that included a written agreement with an alternate processing site, the alternate processing site was within the same city as the FMPA. A disaster covering a large geographical area, such as a hurricane, could impact both the FMPA and the alternate processing site simultaneously, increasing the risk that the FMPA may be unable to continue critical operations, or maintain availability of information systems data and resources, in the event of a disruption of IT operations.

**Recommendation:** The FMPA should enter into a written agreement to procure an alternate processing site that is sufficiently geographically distant to minimize the risk of being unable to continue critical operations in the event of a hurricane or other geographically large disaster.

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**OBJECTIVES, SCOPE, AND METHODOLOGY**

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The Auditor General conducts audits of governmental entities to provide the Legislature, Florida's citizens, public entity management, and other stakeholders unbiased, timely, and relevant information for use in promoting government accountability and stewardship and improving government operations.

We conducted this operational audit from July 2014 to December 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. In conducting this audit, we engaged a consulting firm that provides engineering, economic, financial and management consulting services to utilities, insurance and financial institutions, law firms, private developers, governmental utilities (including municipal and JAA utilities), and industrial entities involved in the energy industry. The consulting firm assisted us in developing certain comparative information provided in the **Findings and Recommendations** section of this report, and in evaluating the FMPA's practices, including comparisons to similar JAAs or industry practices as reported in finding Nos. 1, 2, 3, and 14.

We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of this operational audit were to:

- Evaluate management's performance in establishing and maintaining internal controls, including controls designed to prevent and detect fraud, waste, and abuse and in administering assigned responsibilities in accordance with applicable laws, rules, regulations, contracts, grant agreements, and other guidelines.
- Examine internal controls designed and placed in operation to promote and encourage the achievement of management's control objectives in the categories of compliance, economic and efficient operations, reliability of records and reports, and the safeguarding of assets, and identify weaknesses in those controls.

This audit was designed to identify, for those programs, activities, or functions included within the scope of the audit, deficiencies in management's internal controls, instances of noncompliance with applicable laws, rules, regulations, contracts, grant agreements and other guidelines, and instances of inefficient or ineffective operational policies, procedures, or practices. The focus of this audit was to identify problems so that they may be corrected in such a way as to improve government accountability and efficiency and the stewardship of management. Professional judgment has been used in determining significance and audit risk and in selecting the particular transactions, legal compliance matters, records, and controls considered.

For those programs, activities, and functions included within the scope of our audit, our audit work included, but was not limited to, communicating to management and those charged with governance the scope, objectives, timing, overall methodology, and reporting of our audit; obtaining an understanding of the program, activity, or function; exercising professional judgment in considering significance and audit risk in the design and execution of research, interviews, tests, analyses, and other procedures included in the audit methodology; obtaining reasonable assurance of the overall sufficiency and appropriateness of the evidence gathered in support of our audit's findings and conclusions; and reporting on the results of the audit as required by governing laws and auditing standards.

The scope and methodology of this operational audit are described in Exhibit B. Our audit included selection and examinations of various records and transactions from October 2012 through June 2014, and selected actions taken prior and subsequent thereto. Unless otherwise indicated in this report, these records and transactions were not selected with the intent of statistically projecting the results, although we have presented for perspective, where

practicable, information concerning relevant population value or size and quantifications relative to the items selected for examination.

An audit by its nature does not include a review of all records and actions of agency management, staff, and vendors, and as a consequence, cannot be relied upon to identify all instances of noncompliance, fraud, waste, abuse, or inefficiency.

**AUTHORITY**

Pursuant to the provisions of Section 11.45, Florida Statutes, I have directed that this report be prepared to present the results of our operational audit.



David W. Martin, CPA  
Auditor General

**MANAGEMENT'S RESPONSE**

Management's response is included as Exhibit C.

**EXHIBIT A  
FLORIDA MUNICIPAL POWER AGENCY  
BOARD OF DIRECTORS AND EXECUTIVE COMMITTEE  
DURING THE PERIOD OCTOBER 2012 THROUGH JUNE 2014**

Municipality	Board of Directors	Executive Committee
City of Alachua	Gary Hardacre	
City of Bartow	Vacant	
City of Blountstown	Vacant to 12-11-13 Emory Pierce from 12-12-13	
City of Bushnell	Vince Ruano to 7-31-13, Chair to 7-18-13 Vacant from 8-1-13 to 8-4-13 Bruce Hickle from 8-5-13	Vince Ruano to 7-31-13 Vacant from 8-1-13 to 8-4-13 Bruce Hickle from 8-5-13
City of Chattahoochee	Elmon Lee Garner	
City of Clewiston	Kevin McCarthy, Vice Chair to 12-13-12 <b>(1)</b> Vacant from 12-14-12 to 4-16-14 Danny Williams from 4-17-14	Kevin McCarthy to 12-13-12 Vacant from 12-14-12 to 4-17-13 Jimmy Pittman from 4-18-13 to 4-16-14 Danny Williams from 4-17-14
City of Fort Meade	Fred Hilliard	Fred Hilliard
City of Fort Pierce	Bill Thiess, Treasurer from 7-19-13	Bill Thiess
City of Gainesville	Robert Hunzinger to 10-17-13, Vice Chair from 7-19-13 to 10-17-13 <b>(1)</b> Vacant from 10-18-13 to 12-11-13 David Beaulieu from 12-12-13	
City of Green Cove Springs	Gregg Griffin to 1-23-13 Robert Page from 1-24-13 to 6-17-13 Ray Braly from 6-18-13	Gregg Griffin to 1-23-13 Robert Page from 1-24-13 to 6-17-13 Ray Braly from 6-18-13
Town of Havana	Howard McKinnon	Howard McKinnon, Chair
City of Homestead	Barbara Quinones, Vice Chair from 1-23-14 <b>(1)</b>	
City of Jacksonville Beach	Roy Trotter	Roy Trotter
City of Key West	Lou Hernandez, Secretary to 7-18-13 Lynne Tejada, Secretary from 7-19-13	Lynne Tejada
City of Kissimmee	Jim Welsh to 1-22-14 Larry Mattern from 1-23-14	Larry Mattern
City of Lake Worth	Clay Lindstrom	Clay Lindstrom to 12-31-13 <b>(2)</b>
City of Lakeland	Alan Shaffer	
City of Leesburg	Paul Kalv to 1-3-14 Vacant 1-4-14 to 1-22-14 Patrick Foster from 1-23-14	Paul Kalv to 1-3-14 Vacant from 1-4-14 to 1-22-14 Patrick Foster from 1-23-14
City of Moore Haven	Harry Ogletree	
City of Mount Dora	Charles Revell	
City of Newberry	Bill Conrad, Treasurer to 7-18-13, Chair from 7-19-13	Bill Conrad
City of New Smyrna Beach	William Mitchum	
City of Ocala	Matt Brower	Matt Brower, Vice Chair
City of Orlando	Claston Sunanon	



**EXHIBIT A (CONTINUED)**  
**FLORIDA MUNICIPAL POWER AGENCY**  
**BOARD OF DIRECTORS AND EXECUTIVE COMMITTEE**  
**DURING THE PERIOD OCTOBER 2012, THROUGH JUNE 2014**

Municipality	Board of Directors	Executive Committee
City of Quincy	Mike Wade	
City of St. Cloud	Michael Turner	
City of Starke	Marc Oody	Marc Oody
City of Vero Beach	Pilar Turner	
City of Wauchula	Vacant to 7-18-13 Terry Atchley from 7-19-13	
City of Williston	CJ Zimoski to 3-5-13 Scott Lippman from 3-6-13	
City of Winter Park <b>(3)</b>	Jerry Warren	

(1) Vice Chair position was vacant from 12-14-12 to 7-18-13 and from 10-18-13 to 1-22-14.  
 (2) The City of Lake Worth ceased membership in the Executive Committee when it stopped purchasing power from the All Requirements Project on 1-1-14.  
 (3) Became a member of the FMPA on 10-13-12.

**EXHIBIT B**  
**AUDIT SCOPE AND METHODOLOGY**

Scope (Topic)	Methodology
Organizational Structure, Public Records, and Minutes	Reviewed organizational structure of the FMPA and assessed the functional responsibilities within the organizational structure to determine whether they were adequately separated to provide effective internal controls. Our contracted consultants compared the FMPA’s governance structure to other comparable JAAs. Examined and reviewed Board of Director and Executive Committee meeting notices and related minutes, and other FMPA records, to determine compliance with applicable laws and other guidelines. Reviewed usage of the Executive Committee’s supermajority voting provision.
Audit Findings Disclosed by the FMPA’s 2012-13 Fiscal Year Financial Audit	Reviewed findings reported in the FMPA’s 2012-13 fiscal year financial audit relevant to the scope of our audit and determined the status of the FMPA’s corrective actions.
Written Policies and Procedures	Determined whether the FMPA had written policies and procedures in place for major business functions.
Related-Party Transactions	For selected FMPA officials, reviewed Florida Department of State, Division of Corporation, records and FMPA records to identify any potential relationships that represent a conflict of interest with FMPA vendors.
Information Technology	Reviewed recent findings included in consultant reports and determined the status of the FMPA’s corrective actions.
Investments	Determined whether the FMPA established investment policies and procedures, whether those policies and procedures were reasonable, and whether investments were in accordance with those policies and procedures.
Long-Term Debt	Determined whether the FMPA established debt policies and procedures and whether debt issued or refunded during the audit period was executed in accordance with those policies and procedures. Determined whether the FMPA followed GFOA best practices regarding selection of bond professionals when issuing long-term debt. Also, evaluated whether debt refundings were undertaken for valid business purposes.
Interest Rate Swaps	Our contracted consultants compared the FMPA’s usage of interest rate swaps to standard industry practices. Evaluated the FMPA’s management of the swaps and decisions regarding ultimate disposition.
Natural Gas Hedging	Our contracted consultants compared the FMPA’s natural gas hedging activity to standard industry practices.
Natural Gas Supply Agency Participation	Evaluated the FMPA’s management of the Public Gas Partners, Inc., investment. Our contracted consultants compared the FMPA’s participation in such arrangement to other comparable JAAs.
Revenues	Reviewed policies and procedures for billing project members and tested accuracy of calculations and compliance with governing contract provisions.
Power Projects Rates	Our contracted consultants compared the FMPA’s rates, rate structure, and billing practices to other comparable JAAs.

**EXHIBIT B (CONTINUED)**  
**AUDIT SCOPE AND METHODOLOGY**

Scope (Topic)	Methodology
Power Capacity Management	Our contracted consultants evaluated the FMPA’s effort to mitigate overcapacity issues relative to standard industry practices.
Personnel and Payroll Administration	Reviewed the FMPA’s procedures for completion and maintenance of key payroll records. Tested compensation, new hires, payroll transactions, and evaluation procedures for compliance with the FMPA’s policies and procedures. Evaluated reasonableness and sustainability of employee termination benefits. Also, reviewed contracts of contracted employees for reasonableness.
Employee Bonuses	Reviewed bonuses awarded to employees for compliance with FMPA policies and procedures.
Postretirement Healthcare	Evaluated the FMPA’s policies and procedures regarding postretirement healthcare benefits for reasonableness and sustainability.
Procurement and Expenditures	Reviewed the FMPA’s assignment and use of credit cards. Reviewed the FMPA’s travel policies for reasonableness. Tested disbursements, including charge account payments and travel-related payments, to determine whether they were properly authorized, served a public purpose, and were in accordance with applicable laws, FMPA policies and procedures, and other guidelines.
Contractual Services	Tested selected contracts and contract and service arrangement payments to determine compliance with competitive selection requirements; whether contracts clearly specified deliverables, time frames, documentation requirements, and compensation; and whether the FMPA complied with its policies regarding competitive procurement.
ARP Contract Termination Provisions	Our contracted consultants compared the FMPA’s ARP contract termination provisions to those of other JAAs. Additionally, they evaluated the FMPA’s provisions related to “stranded cost” recovery for reasonableness and reviewed withdrawal payment calculations for reasonableness.
Non-ARP Contract Termination Provisions	Our contracted consultants compared the FMPA’s non-ARP contract termination provisions to those of other JAA’s.
Environmental Protection Agency (EPA) Requirements	Our contracted consultants evaluated the FMPA’s financial exposure to upcoming EPA requirements and FMPA’s efforts to comply.
Legal Environment	Our contracted consultants compared powers and duties established by Florida law to laws applicable to JAAs in other states.
Long-term Capital Planning and Debt Management Activities	Our contracted consultants compared the FMPA’s long-term capital planning and management of associated debt to other comparable JAAs.

**EXHIBIT C  
MANAGEMENT'S RESPONSE**



Florida Municipal Power Agency

VIA: Email

March 25, 2015

Substitute to February 20, 2015 response letter

Mr. David W. Martin, CPA  
Auditor General  
State of Florida  
G74 Claude Pepper Building  
111 West Madison Street  
Tallahassee, FL 32399-1450

RESPONSE TO PRELIMINARY AND TENTATIVE FINDINGS

Dear Mr. Martin:

Per your request, this letter provides responses of the Florida Municipal Power Agency (FMPA) to the Auditor General's preliminary and tentative findings related to its operational audit of FMPA.

The Board of Directors and the Executive Committee of FMPA have reviewed and discussed the preliminary and tentative findings and recommendations (P&T Report) and have approved this response. As representatives of the member city owners of FMPA, and as officers of the Board of Directors and Executive Committee, we appreciate the Auditor General's review of the FMPA's practices and policies, and we welcome the opportunity to improve efficiency and control costs for the member city owners of the Agency. The Board of Directors, Executive Committee and FMPA staff appreciate the professionalism and independence of the Auditor General's staff in conducting its audit of the Agency.

*Note that this response is a substitute for the previous response dated February 20, 2015, and is based on draft revisions to the P&T Report that have been provided by the Auditor General (in e-mails on March 13 and March 20). This substitute response addresses these draft revisions provided to FMPA, which were reflected in a draft red-lined P&T Report provided on March 25.<sup>1</sup> We presume that the final report will simply be the clean version of the redline provided March 25; however, to the extent that the P&T Report may be changed in ways that FMPA is not aware of, this substitute FMPA response dated March 25, 2015 cannot reflect those changes.*

<sup>1</sup> Note that the provided redlined P&T Report did not have page numbers; hence, references to quotes from the P&T report are made by section instead of page numbers.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 2

1. INTRODUCTION

FMPA was created in 1978, and every year since its formation, FMPA has had a financial audit conducted by an independent auditor in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those audits have been filed with the State of Florida. FMPA values independent reviews that promote transparency, accountability, and continuous improvement.

We understand that the Auditor General performed an operational audit of FMPA, as defined in section 11.45(1)(g), Florida Statutes. The objectives of this type of audit are, in general, to evaluate management's performance in establishing and maintaining internal controls, including controls designed to detect fraud, waste and abuse, as well as to evaluate management's performance in administering assigned responsibilities in accordance with applicable laws, rules, regulations, contracts and other guidelines. Your multi-person audit staff began work on July 28, 2014, and your P&T Report was released six months later on January 21, 2015. During the audit, your staff requested unrestricted access to FMPA's records and personnel. As will be discussed in greater detail in the following pages, many of your audit inquiries, though not all, were for the 20-month period of October 2012 through June 2014. During that audit period, FMPA had total expenses of nearly \$1 billion for the Agency and its power supply projects.

FMPA's member city owners have placed tremendous trust and received great value from FMPA's power supply and other services. The Agency plays an important role providing competition in the Florida wholesale power market. The Agency has a history dating back to 1978. In the past 37 years, FMPA has helped its members diversify their wholesale supply options with cost-effective power resources, reduced municipal power costs by hundreds of millions of dollars,<sup>2</sup> and represented municipals in regulatory forums, which led to even greater savings. FMPA's All-Requirements Project (ARP) has reduced wholesale power costs 23% from its all-time peak in 2009, and today, rates are close to the average wholesale rates of Florida's investor-owned utilities, as ARP has been for most of its existence.

For five of the Auditor General's findings, FMPA's Executive Committee took action on February 19, 2015, in addition to FMPA's responses and clarifications contained in this letter, approving beginning a process to retain an independent management consulting firm to advise the Executive Committee concerning Finding 1 (Fuel Hedging), Finding 2 (Natural Gas Supply Agency Participation), Finding 3 (Interest Rate Swaps), Finding 13 (Peak Shaving), and Finding 14 (ARP Termination Provisions).

For the other 10 findings, action to address the recommendations will require public discussion and a vote by FMPA's Board of Directors or Executive Committee, or both. To accomplish this,

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<sup>2</sup> Conservatively, FMPA's consulting engineer estimated that FMPA's All-Requirements Project (ARP) saved its cities approximately \$100 million during its first 10 years of operation from 1986 through 1996. In addition, ARP saved \$34 million for nine municipals whose wholesale power supplier agreed to match ARP's rates from 1986 through 1998. Later, negative fiscal impacts were felt or arose out of decisions made in the 2006-2009 timeframe. However, FMPA is now again the competitive voice of Florida's municipal electric utilities.

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**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 3

the findings will be scheduled as agenda items for governing board meetings. FMPA's governing boards have a practice of first hearing a matter as an information item and then scheduling the matter for action at the next meeting. Considering FMPA's meeting schedule and approval process, FMPA is committed to addressing each finding as soon as practical. Some responsive actions have already been taken by FMPA, as are noted later in this response.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 4

2. EXECUTIVE SUMMARY

**FINDING 1 (Fuel Hedging):** FMPA's Executive Committee will consider the Auditor General's recommendations. A review of fuel hedging policies will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**FINDING 2 (Natural Gas Supply Agency Participation):** FMPA's Executive Committee will consider the Auditor General's recommendations for establishing written policies regarding future gas production investments. An assessment of fuel production investments will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**FINDING 3 (Interest Rate Swaps):** FMPA's Executive Committee will consider updating FMPA's existing Debt Policy, taking the Auditor General's recommendations under consideration. FMPA's Executive Committee has developed a strategy for exiting the interest rate swaps before September 30, 2015. A review of the Debt Policy and exit strategy will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**FINDING 4 (Investment Policy):** FMPA's governing boards will consider updating FMPA's existing Investment Policy consistent with the Auditor General's recommendations as soon as practical.

**FINDING 5 (Employee Benefits):** FMPA's Board of Directors will address how to periodically evaluate the projected costs of employee benefits, specifically post-retirement healthcare and annual leave, as soon as practical.

**FINDING 6 (General Counsel Contract):** FMPA's Board of Directors will consider its employment arrangements with the General Counsel and consider how to document it as soon as practical.

**FINDING 7 (Severance Pay and Benefits):** FMPA's Board of Directors will discuss and review this matter with its General Manager and CEO as soon as practical.

**FINDING 8 (Questioned Expenditures):** FMPA's governing boards will discuss how to more fully document the authorized public purpose as soon as practical. In the meantime, FMPA will discontinue, as soon as contract commitments allow, expenditures for Orlando Magic tickets, an indoor plant service and a Christmas tree.

**FINDING 9 (Competitive Selection):** FMPA will strengthen internal controls to ensure that purchases are made in accordance with the existing Procurement Policy and other policies related to competitive selection as soon as practical.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 5

**FINDING 10 (Selection of Bond Professionals):** FMPA's governing boards will review its Debt Policy and consider the modifications of its current language to address the Auditor General's recommendation for a competitive selection process of qualified financial services in the future to include but not be limited to financial advisors and bond counsel as soon as practical.

**FINDING 11 (Credit Cards):** FMPA will enhance its policies, procedures and documentation for credit cards consistent with the Auditor General's recommendations as soon as practical.

**FINDING 12 (Travel Expenditures):** FMPA's Board of Directors will consider updating FMPA's existing Travel Expense Policy, taking the Auditor General's recommendations into consideration as soon as practical. In the meantime, FMPA will stop hosting a dinner during the annual legislative rally in Washington, D.C., which will eliminate this meal cost and the rare occasion where alcoholic beverages were provided. As part of updating FMPA's Travel Policy, FMPA will expressly prohibit reimbursement for alcohol, although FMPA has had a practice of "no alcohol" for many years.

**FINDING 13 (Peak Shaving):** The issues identified by the Auditor General concerning the value of peak shaving and monitoring compliance with contract/policy were considered by FMPA's Executive Committee when the policy was approved in 2014. FMPA currently has some capability to verify compliance and options to address any non-compliance. Amending the contract is a lengthy process and is not within FMPA's sole discretion. A review of the peak shaving policy and enforcement options will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**FINDING 14 (ARP Termination Provisions):** FMPA's Executive Committee will discuss the Auditor General's comments. Amending the contract is a lengthy process and is not within FMPA's sole discretion. A review of the Auditor General's recommendations will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**FINDING 15 (Disaster Recovery Plan):** FMPA will investigate an alternate data processing facility, consistent with the Auditor General's recommendations as soon as practical.



**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 6

3. AUDITOR GENERAL'S FINDINGS

**A. Background (Rate Comparison)**

The P&T Report provides a Background section which includes a retail rate comparison among FMPA's member city owners and Florida's Investor Owned Utilities (IOUs) (Table 3), and a table (Table 4) of FMPA's All-Requirements Project (ARP) rates in different years from 2006 through 2015. FMPA has several comments regarding the information presented, particularly Table 3 and Table 4.

FMPA questions why retail rate comparisons are appropriate in an operational audit of a wholesale power provider, like FMPA. A more appropriate rate comparison would be FMPA's wholesale rates compared to comparable wholesale rates of other utilities. As the P&T Report states in the Background section, "There are multiple factors that impact FMPA ARP members' residential rates, some of which are not attributable to FMPA ...." The report lists three examples of city decisions affecting retail rates that have nothing to do with FMPA's wholesale costs. FMPA agrees with these examples. FMPA provides wholesale power to some municipal utilities that sell at retail rates comparable with the lowest cost retail provider in Florida, while other cities that FMPA serves have higher retail rates.

The P&T Report Background section confirms FMPA's ARP Member average retail rates are competitive with IOU average retail rates, and based on the data presented in Table 3, the rates are almost identical. A footnote to Table 3 states that the IOU rates exclude franchise fees and certain other taxes that are billed as a separate line item. The actual costs that customers pay include franchise fees and those fees should be included in the IOU rates in order to make an appropriate comparison to the municipal residential rates. Franchise fees are paid by IOUs to local governments for granting the IOU the right to utilize local government rights-of-way and other property to serve the electric customers within the local government area. Municipal rates include a transfer to the general fund, as described in the Auditor General's P&T Report in the third bullet on the bottom of page four, which is used to help fund the operation of the local government in a similar fashion as the franchise fee. To make an "apples-to-apples" comparison, the \$115 per 1,000 kilowatt hour (kWh) average IOU residential retail reported in Table 3 should be increased by an average 6% franchise fee (taken from the document entitled "Comparison of Residential Electric Rates Compiled by the Florida Municipal Electric Association dated December 2013) which would equal \$122 per 1,000 kWh. This comparable IOU average rate is essentially equal to the \$122 per 1,000 kWh FMPA ARP average rate reported in Table 3.

The time period can also make a difference in a rate comparison. For example, the more recent December 2014 comparison shows the ARP average residential rate is about \$124 per 1,000 kWh whereas the average IOU residential rate is about \$125 per 1,000 kWh<sup>3</sup> (includes an average 6% franchise fee).

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<sup>3</sup> Source: Florida Municipal Electric Association rate comparison for 2014. <http://publicpower.com/2015/fmea-releases-december-2014-rate-comparison-report/>

**EXHIBIT C (CONTINUED)  
MANAGEMENT’S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 7

The P&T Report Background section also presents data that, if presented in a way that shows over-all rates to FMPA’s ARP participants, shows that FMPA’s rates have declined from 2006 through 2014. Table 4 presents a summary of FMPA ARP rates. The table presents how FMPA demand and energy rates have changed over time, but, does not present how FMPA’s overall rates have changed over time. Note that Table 4 presents budgeted rates for 2015. Unlike other utilities, FMPA adjusts its rates monthly to match its actual costs plus 60 days of working capital and as such, FMPA’s budgeted rates cannot be presumed to be the actual rates experienced by FMPA members. Also note that FMPA’s actual rates have been significantly lower than budget since 2010 because of falling fuel prices. As such, FMPA offers a replacement Table 4 that presents FMPA’s average overall rates and removes the budget projections for 2015.

**FMPA Proposed Replacement to Table 4  
Rates Based on Actual ARP Billed Revenues and Load**

<b>Fiscal Year</b>	<b>Demand Charge (\$/kW-month)</b>	<b>Energy Charge (\$/MWh)</b>	<b>Average Overall Rate<sup>1</sup> (\$/MWh)</b>	<b>Transmission Charge (\$/kW-month)</b>
2014	21.98	30.80	75.50	2.25
2013	20.98	32.53	79.27	2.00
2012	19.92	29.59	73.69	1.79
2011	17.86	39.44	76.84	1.85
2010	18.16	52.04	89.05	1.39
2009	16.08	64.48	98.67	1.82
2008	13.08	65.49	92.94	1.24
2007	11.12	55.56	78.90	1.25
2006	10.81	54.82	76.70	1.37

<sup>1</sup> Excluding transmission and losses. Each ARP participant’s monthly bill varies due to participant load factor and other considerations.

The offered replacement to Table 4 shows that from 2006 to 2014 Demand Charges increased by 103% and Energy Charges decreased by 44%. This is because FMPA invested in efficient, clean, new gas-fired combined cycle generation that, while increasing FMPA ARP’s demand charge, decreased FMPA ARP’s energy charge such that the overall rate *decreased* from 2006 (\$77 per MWh) to 2014 (\$76 per MWh).

The Great Recession with subsequent demand reduction caused most utilities in Florida to have surplus generation. A surplus in generation causes an increase in demand rates since the fixed costs of the generation is spread over lower demand. As the economy recovers and FMPA ARP’s demand grows into its surplus, FMPA ARP’s demand rate will be reduced because those fixed costs will be spread over a larger demand.

At the same time FPL was planning on building its proposed Glades Power Park coal plant, FMPA was planning on investing in partial ownership in the proposed Taylor Energy Center coal plant. Due to changes in state government, both projects were cancelled at about the same time and both utilities decided to instead invest in clean, efficient natural gas-fired combined cycle

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 8

plants. Consequently, FMPA is now better-positioned, as is FPL, for a possible regulation of greenhouse gas emissions.

In summary:

1. The average of FMPA ARP Participants' retail rates is equal to the average IOU retail rates (December 2013 both averaged \$122 per MWh).
2. FMPA invested in clean, efficient natural gas-fired plants that reduced FMPA ARP wholesale rates from 2006 to 2014 and positioned FMPA for likely greenhouse gas regulation.

**B. Findings and Recommendations**

**FINDING 1: Fuel Hedging**

**Finding:** Fuel hedging practices were not consistent with industry practices utilized by other comparable joint action agencies.

**Recommendation:** The FMPA should consider amending its fuel hedging policies to focus on offsetting changes in the cost of natural gas rather than the benefit from upward and downward price volatility. In doing so, the policy should provide for hedging using only derivative instruments necessary to achieve a simple effective fuel hedge at current natural gas prices rather than at present trigger amounts.

**FMPA Response:** FMPA did follow common industry practice and continues to do so with its hedging programs. FMPA's old hedge-and-hold program is common industry practice and is a practice used by JAAs within the Auditor General's sample. FMPA's use of derivatives such as options and swaps is common practice as is identified in the summary of GASB Statement No. 53 on which the finding relies.<sup>4</sup> And, FMPA's new cash-flow-at-risk hedge program (FST) is also common industry practice.

More than 95% of the natural gas hedging premium above market price occurred due to decisions made in early 2008 and as a result of the dramatic price paradigm shift that began in summer 2008 when natural gas prices plunged from approximately \$13 per million British thermal unit (MM Btu), ultimately falling near \$2 per MM Btu and remaining far below FMPA's then existing hedge contract prices (see chart of natural gas prices below). Note that many utilities had comparable results to FMPA; while FMPA lost \$245 MM mark-to-market from 2003 to 2013 as a result of its hedge-and-hold program, FPL lost \$3.6 billion during the same time frame (see table below), and all of

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<sup>4</sup> "Common types of derivative instruments used by governments include interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), swaptions, forward contracts, and futures contracts" (<http://www.gasb.org/st/summary/gstsm53.html>).

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 9

the IOUs in Florida except Florida Public Utilities Company experienced mark-to-market losses in the tens to hundreds of millions of dollars in 2007 alone.<sup>5</sup>

**Florida Power and Light Gains/Losses Due to Natural Gas Hedging Program  
(from FPSC data)<sup>5</sup>**

Year	Gain / (Loss) (\$MM)
2003	\$6
2004	\$247
2005	\$610
2006	(\$463)
2007	(\$856)
2008	\$101
2009	(\$1,661)
2010	(\$509)
2011	(\$404)
2012	(\$672)
2013	\$18
Total	(\$3,583)

From the perspective of the FPSC policymakers, reduction in volatility of rates to customers is more important than mark-to-market losses. At the December 18, 2014 FPSC Conference, Commissioner Balbis stated: “... *but this is something that we needed to look at because the hedging activities that the companies engaged in, that this commission encouraged, that this commission approved, actually resulted in billions of dollars lost to customers. And it was a heated discussion and a thorough discussion of that. And this commission decided that that reduction in volatility was worth that on a much larger issue.*”<sup>6</sup>

As a result of this dramatic reset in market prices, further natural gas hedging was suspended by FMPA’s current General Manager and CEO. Later, the Executive Committee took official action to stop the original hedging program as natural gas prices and forecasts of future prices remained at acceptable price levels. The Executive Committee has continued to have extensive discussions about fuel hedging. FMPA has worked its way out of all of those hedges with the last few positions having expired in October 2013. Natural gas hedging, of the sort and magnitude referenced in the P&T Report, is no longer impacting electricity rates. At this time, the current hedging policy

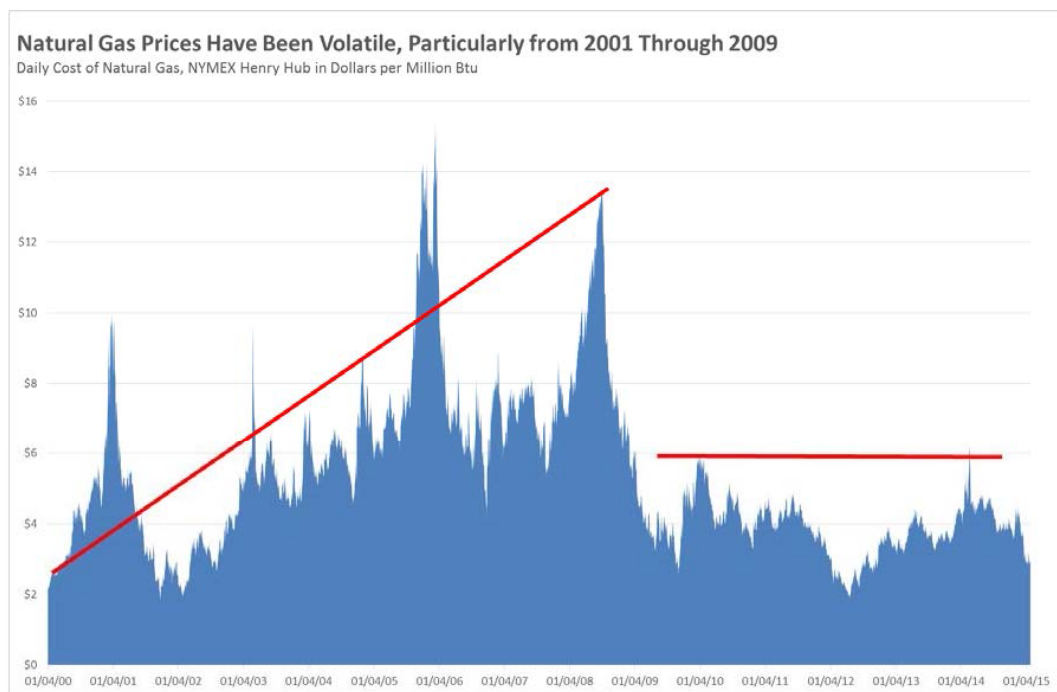
<sup>5</sup> See Fuel Procurement Hedging Practices of Florida’s Investor Owned Electric Utilities (<http://www.psc.state.fl.us/publications/reports.aspx>); and FPSC Dockets 080001, 090001, 100001, 110001, 120001 and 130001 (<http://www.floridapsc.com>)

<sup>6</sup> Transcript of December 18, 2014 Florida Public Service Commission Conference, pgs. 47-48 (docket no. 140001-EI, document no. 06823-14, available at the PSC website (<http://www.floridapsc.com>)).

**EXHIBIT C (CONTINUED)  
MANAGEMENT’S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 10

has very conservative limits, as explained in the Auditor General’s narrative, to better match the hedge program mechanics and focus on the current and anticipated natural gas price environment, as well as to significantly limit the dollar size of any out-of-market price differences between hedge positions and current market prices. The Executive Committee will consider the Auditor General’s recommendations. A review of fuel hedging policies will be included in the Executive Committee’s proposed scope of work for an independent management consulting firm.



**Other Clarifications:** FMPA’s total natural gas expense from fiscal 2003 through fiscal 2014 was approximately \$4 billion,<sup>7</sup> so the premium above market was 6%.

FMPA had a long history of providing the most competitive wholesale power until the price of natural gas became more volatile in 2001 and dramatically increasing fuel prices put pressure on ARP’s wholesale rate. The chart above shows the dramatic cost swings in natural gas over the timeframe of FMPA’s hedging program.

In 2002, FMPA hired an experienced gas hedging and risk management trader as it began efforts to implement a gas hedging program. In 2003, FMPA developed its first Energy Risk Management Policy (ERM), allowing FMPA to enter into financial transactions to hedge the price of natural gas. FMPA hired Deloitte & Touché to review and make recommendations on the ERM. Starting in 2004, The Energy Authority, Inc. (TEA) advised FMPA on hedging strategies and the continued development of the ERM. TEA

<sup>7</sup> Total natural gas expense during the 12 fiscal years shown in Table 7 of the Auditor General’s P&T Report.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 11

remained in this advisory role until September 30, 2009. Additional hedging program staff were added by FMPA to create mid-office and front-office functions.

In September 2007, the price of natural gas began steadily increasing. Through this increase, staff kept the hedged levels at the minimums required in the ERM. However, in May 2008—when natural gas was priced at about \$11 per million Btu and there was more than \$100 million of cumulative benefit in the hedging program to date—the hedge levels were raised to mitigate rate increases from increasingly high natural gas prices. A new three-way option structure for hedging was implemented, as permitted by the ERM, through July 2008. During this period, FMPA hedged much of its natural gas needs through October 2013 at an average NYMEX hedge position of \$9.50 per MM Btu.

In July 2008, the price of natural gas began steadily falling. At the direction of FMPA's new General Manager and CEO, no new hedges were put in place after September 2008.

In March 2009, the Executive Committee approved a new ERM which, among other changes, limited future hedges to no more than 24 months. As previously noted, no new hedges were put in place after July 2008. In August 2009, the Executive Committee officially suspended the hedging program. After months of review, workshops and debate, a much narrower hedging program was approved in September 2010. In February 2011, the hedging program was further modified, and in August 2013 it was again suspended. Today, FMPA has a limited, short-term hedging program (limited to no more than four months and no more than 50% of the ARP's expected natural gas needs), which is only triggered if prices rise above \$7 per million Btu.

A municipally-owned utility, Colorado Springs Utilities (CSU), experienced similar losses (\$200 MM) in its hedge-and-hold program during the same time frame as FMPA, FPL and other utilities. Similar to FMPA, CSU was audited by the City Auditor of the City of Colorado Springs.<sup>8</sup> Similar to FMPA's audit, the City Auditor hired a consultant to assist with the audit. That audit report found that the hedge-and-hold program *"and the corresponding result, was not unusual for utility companies at the time and of similar size to Colorado Springs Utilities."*

The consultant to the City Auditor went on to opine on industry norms for hedging: *"Industry Norms: There is no broadly recognized GAAP-like standard for how to establish a hedge strategy or why to make hedge decisions. There is no bright line as to what constitutes a prudent structure. There are standards as to program controls, but hedge decisions are intrinsically tied to the hedging entity's objectives and those are dependent on a host of factors which can vary dramatically from one entity to another."*

The consultant to the City Auditor then opines on different categories of hedging. One of those categories: *"hedging in response to explicitly quantified and monitored risk*

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<sup>8</sup> The City Council's Office of the City Auditor of the city of Colorado Springs audit report can be found at [http://coloradosprings.gov/sites/default/files/city\\_clerk/city\\_auditor/13-12\\_natural\\_gas\\_hedging\\_program\\_audit\\_report.pdf](http://coloradosprings.gov/sites/default/files/city_clerk/city_auditor/13-12_natural_gas_hedging_program_audit_report.pdf)

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 12

*metrics*” is described by that consultant as “*typically pursued by large entities with a naturally high risk profile and the scale to support more comprehensive programs, or those who have experienced heightened stakeholder sensitivity to past results. These programs deploy quantitative finance principles to measure and monitor risk, and then respond to specific circumstances in a pre-planned manner.*” This category describes FMPA’s current cash-flow-at-risk (FST) hedging program. FMPA has a high-risk factor and sensitivity to the price of natural gas because FMPA generates 80% of its energy from natural gas and 60% of FMPA’s generating capacity is base-load natural gas combined cycle generation. FMPA has heightened stakeholder sensitivity due to past results.

The City Auditor recommended to CSU that they consider this category of hedging: “*the Office of the City Auditor recommends that Colorado Springs Utilities research and consider implementing enhanced quantitative financial methods, or similar metrics and tolerance levels, to assist with decision making regarding the gas hedging program.*” FMPA has already transitioned to this recommended hedging program through its cash-flow-at-risk hedging program.

As FMPA understands the Auditor General’s recommendations (with the additional material provided to FMPA during the first two weeks of March concerning the hedging programs employed by the sample JAAs used as a comparison with FMPA), it is the same “hedge and hold” approach as FMPA’s original hedging policy. Such an approach may reduce or eliminate price volatility but at the expense of exposing the ARP to being out of the market on natural gas costs (and resultant rates). FMPA’s current hedging approach avoids this situation while protecting against ever-rising prices.

The Auditor General’s P&T Report states in a few places (first appearing in this section) that FMPA’s practices were compared with eight or sometimes 17 other JAAs. These comparative groups, within a small segment of the utility industry, lead the Auditor General to make conclusions about what are standard industry practices. In the United States, there are more than 75 JAAs and more than 3,000 electric utilities of all types (more than 2,800 of which are self-regulated). FMPA has been provided the sample used by the Auditor General in making these observations and FMPA finds that the sample is not comparable to FMPA. The guideline used by the Auditor General to select the sample appears in footnotes stating, “Comparability to the FMPA was based on reported peak MW load, wholesale electric revenues, the number of member municipalities, total number of retail customers served, and the generation fuel types employed.” The sample of eight JAAs used for gas hedging observations and findings; however, does not meet this guideline (see Table A).

FMPA has a high-risk profile and sensitivity to the price of natural gas because FMPA generates 80% of its energy from natural gas and 60% of its capacity is efficient base-load natural gas combined cycle generation. Three (3) of the eight (8) JAAs used in the sample do not have base-load gas-fired combined cycle generation, and all eight (8) JAAs within the sample have 35% or less of their generating capacity in base-load natural gas

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 13

fired generation, representing a risk exposure of half, or less than half, of FMPA's risk exposure to the price of natural gas.

In addition, Table 6 and the discussion of Table 6 within the P&T Report is inconsistent with Finding 1. Finding 1 and GASB Statement No. 53 state that the purpose of hedging is to manage the change in the cost of fuel to the entity and change in cash flow to that entity over time. Table 6 does not measure the change in cost of fuel to an entity, nor the change in cash flow to that entity, but only the difference between the price of fuel at which the entity hedged (mark) to the spot-market price (market). To draw an analogy, a fixed rate loan of 6% would keep cash flow and cost of the loan constant and would therefore be a successful hedge in accordance with Finding 1 and GASB Statement 53. Comparing costs of a 6% fixed rate loan (mark) to a 3% variable rate loan (market) would result in a loss. That is essentially what Table 6 measures, which is an inconsistent metric to the Finding and GASB Statement.



**EXHIBIT C (CONTINUED)  
MANAGEMENT’S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 14

**Table A: FMPA Generation Fuel Types Compared to Finding 1 Sample of JAA Generation Fuel Types Capacity in megawatts (MW), Source: company website data**

	Base Load NGCC (1)	Inter-mediate NGCC (2)	Coal	Nuclear	Hydro	Dispatchable Renewables (3)	Intermittent Renewables (4)	Peaking (gas or oil fired)	Energy Storage (5)	Percent of Capacity Base Load NGCC (6)
FMPA	962	109	178	0	0	0	0	382	0	59%
<b>Sample used to compare with FMPA</b>										
SCPPA	310	0	204	230	103	30	700	200	63	29%
PRPA	0	0	434	0	90	0	78	388	0	0%
MEAG	500	0	750	800	0	0	0	0	0	24%
IMPA	0	0	518	0	NA	0	0	419	0	0%
MPPA	26	0	274	0	0	NA	0	50	0	7%
AMP	450	0	372	0	189	51	7	215	0	35%
GRDA	443	0	1010	0	234	0	0	0	260	26%
UAMPS	0	140	352	0	NA	0	56	0	0	0%

NGCC Natural Gas fired Combined Cycle

NA Not available, but the missing information does not change the percent of capacity of base load NGCC for that JAA

- (1) Base Load NGCC generally are 50% or more efficient (for comparison, a typical car engine is less than 25% efficient), and typically consists of F-Class gas turbines or higher (G, H, J) combined with a heat recovery steam generator (HRSG). These base load NGCCs will typically have capacity factors greater than 50%.
- (2) Intermediate NGCC are generally older and, in the case of both FMPA and UAMPS, consists of a less efficient combination of an E-Class gas turbine combined with a HRSG. These intermediate NGCC's will typically have efficiencies of 40% or less, significantly less efficient than base load NGCC. As a result, the capacity factors of these units are typically less than 25%.
- (3) Dispatchable renewables include landfill gas generation and geothermal generation
- (4) Intermittent renewable generation includes wind and solar
- (5) Energy storage consists of pumped hydro and ice storage
- (6) Percent capacity of NGCC excludes intermittent renewables and energy storage in the calculation

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 15

**FINDING 2: Natural Gas Supply Agency Participation**

**Finding:** Investment in natural gas exploration and drilling were not consistent with industry practices utilized by other comparable joint action agencies and were more complex and involved more risk than alternative forms of hedging commonly practiced.

**Recommendation:** The FMPA should establish written policies regarding future gas production investments. These policies should state the circumstances under which the FMPA may consider participation in further PGP projects or other gas production investments, and the circumstances under which the FMPA may consider exiting its PGP participation. Additionally, these policies should identify the categories of risk that must be considered by the FMPA when deciding on new or increased gas production investments and place an appropriate value on risk.

**FMPA Response:** FMPA's investment in fuel production is common industry practice. It is common industry practice for generating utilities to employ vertical integration strategies into fuel exploration, production and transportation, as is evidenced by FPL's investments in natural gas exploration and production in Oklahoma, and similar investments by other IOUs in Florida. Sixty percent (60%), or 3 of 5 IOUs in Florida, have invested in fuel production.

The last time FMPA's Executive Committee made a decision to participate in a Public Gas Partners (PGP) project was October 2005 when natural gas prices were experiencing great volatility and beginning to surge to unprecedented levels. Since then, FMPA declined participation in another PGP project and has been monitoring its existing investments with frequent updates and reports to the FMPA Executive Committee. The Executive Committee has considered exit options, but those are not currently viable. New PGP project participation is doubtful at this time. However, FMPA's investment in PGP is not unusual for a natural gas reliant utility company. The Florida Public Service Commission (FPSC) approved on December 18, 2014, a request from FPL to recover the cost of investments in natural gas drilling projects. From news accounts, FPL plans to invest \$191 million in drilling projects in southeastern Oklahoma and recover the investment through its fuel cost recovery clause. The FPSC delayed until March 2015 a decision on FPL's request to set guidelines for future production projects, which might cost up to \$750 million annually. The Executive Committee will consider the Auditor General's recommendations for establishing written policies. As assessment of fuel production investments will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**Other Clarifications:** PGP is a long-term investment. The value of this investment fluctuates with the price of oil and natural gas. The prices for these commodities currently are at historically low levels. If prices rise or production volumes increase, the value of this investment will improve. This investment represents less than 10% of the annual natural gas demand for FMPA's All-Requirements Project, so it is part of a diversified portfolio and not a materially significant investment to the ARP's total assets of \$1.5 billion as of September 30, 2014.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 16

Over the same fiscal year period that produced the PGP cash flow deficit of \$14.6 million, the ARP billed 53.9 million MWh; therefore, the average rate impact of PGP is 27 cents per MWh. This is equivalent in impact to a price movement in natural gas of 5.4 cents. On the lowest average, all-in ARP billed rate of \$80.34 (fiscal 2012) for this same time period, the 27 cents per MWh represents a rate impact of one-third of one percent.

As also discussed in FMPA's response to Finding 1, FMPA believes that the sample used by the Auditor General to develop Finding 2 consists of JAAs that are not comparable to FMPA. In addition, a sample of one small segment of the electric utility industry consisting of more than 3,000 utilities is insufficient to reliably opine on common industry practices. FMPA's research demonstrates that generating utilities use vertical integration strategies for fuel production and transportation is a common industry practice, as is evidenced by FPL's investments in gas production. Sixty percent (60%) of the Florida IOUs have engaged in vertical integration strategies and invested in fuel production facilities.

In addition, of the four (4) JAAs within the sample that have more than 20% of their generating capacity in base-load natural gas fired combined cycle generation, one (SCPPA) has made significant investments, well in excess of FMPA's PGP investments, in natural gas production.

**FINDING 3: Interest Rate Swaps**

**Finding:** Certain interest rate swaps were not employed consistent with industry practices utilized by other comparable joint action agencies, which resulted in significant termination fees likely to be incurred.

**Recommendation:** The FMPA should refrain from employing interest rate swaps in the future without concurrently issuing debt to bring its interest rate hedging practices more in line with industry standard risk tolerance. Further, such activities should not be undertaken before required approvals for projects are obtained from regulatory bodies. In addition, the Executive Committee should consider, without regard to prior unrealized losses incurred, developing and executing an exit strategy for the Taylor swaps that removes the ongoing risk to the ARP members.

**FMPA Response:** FMPA's Executive Committee will consider updating FMPA's existing Debt Policy, taking the Auditor General's recommendations under consideration. Regarding the final comment about an exit strategy, FMPA's Executive Committee has such a plan. For more than two years, FMPA's Executive Committee has had extensive discussions and a number of workshops about the different termination alternatives. The members have agreed on an exit strategy, and FMPA plans to execute that strategy no later than September 30, 2015. A review of the Debt Policy and exit strategy will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 17

**Other Clarifications:** Interest-rate swaps and to a lesser degree forward-starting swaps are used industry-wide when interest rate certainty is desired on an anticipated project or capital financing, as it was with the Taylor coal plant project. Locking in an interest rate and thus interest cost can be and was a key factor in creating some certainty for the favorable rate economics for FMPA's \$740 million investment share in this power generation project.

The Taylor project came to an abrupt halt when newly elected Governor Charlie Crist terminated the project's permitting activities, reversing previous Governor Jeb Bush's political directive to build coal generation in Florida. This surprise decision was the initial reason for not utilizing the forward interest rate swap commitments, although projected growth in electricity consumption indicated that FMPA still needed to construct additional power generation to serve the projected growth in electric demand. The second seismic shift came when the economy in Florida, the nation and the world started a now six-year decline, during which interest rates tumbled and financial liquidity dried up.

FMPA disagrees with the Auditor General's negative characterization of excessive risk-taking with regard to FMPA's previous action to use forward starting interest rate swaps to hedge its significant interest rate risk. As a regular issuer of debt to fund its capital projects, FMPA ultimately faces the judgment of the national credit rating agencies who apply, perhaps, the strictest of standards of review in developing their rating evaluation – one that takes into account a broad view of "industry" practice. FMPA's ratings record is consistently positive and reflects on all of its major decisions. In 2006, one of those major decisions was to participate in the building a coal fired power plant, the Taylor Energy Center, whose total cost would approach \$2 billion before being curtailed by action of the Florida Governor's Office. While the cost estimate grew over the time the project was in development, interest rates were still attractive, even as the Federal Reserve had just made its 17th increase in the Federal Funds rate. FMPA was concerned whether interest rates would remain within a range to support the then positive economics of this needed project. After considerable discussion and analysis, FMPA decided to use forward starting swap agreements to hedge this risk of future increases in interest costs.

To the point the Auditor General makes about comparability, excessive risk taking and industry practices, consider the opinion of one of our toughest critics: Moody's Investor Service. After FMPA's presentation to Moody's of its plan to hedge the interest rate risk associated with the financing of the Taylor County Coal Plant, Moody's issued a ratings update (October 2006) affirming the ARP's rating of A1 and its stable outlook. Included in this rating affirmation, Moody's stated:

*"FMPA utilizes interest rate swaps in managing its debt. FMPA has a reasonable swap policy accepted by its board; has clear authorization to enter into swaps; and includes an assessment detailing risk exposures and policy oversight in its financial statements. FMPA intends to enter into qualified swaps permitted under its bond resolution in connection with the financing of FMPA's share of the Taylor Energy Center. The intent is to lock in interest rates now as a hedge*

**EXHIBIT C (CONTINUED)  
MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 18

*against increasing rates as the new coal fired power plant is constructed. FMPA has the authorization in place to issue the bonds that will finance its share of the Taylor Energy Center.*

*The swaps will include a diverse group of counterparties with no counterparty representing more than 9% of total project. FMPA has a \$100 million line of credit and can access the rate process without external regulation to meet unforeseen interest cost exposure."*

As also discussed in FMPA's response to Findings 1 and 2, FMPA believes that the sample used by the Auditor General to develop Finding 3 consists of JAAs that are not comparable to FMPA.

**FINDING 4: Investment Policy**

**Finding:** The FMPA's investment policy needed to be enhanced to clarify requirements regarding allowable investment credit ratings and to establish geographic diversification requirements for investments.

**Recommendation:** The FMPA should enhance its investment policy to clarify the application of credit ratings. Additionally, the FMPA should enhance its investment policy to clarify that the investment diversification requirements are to be applied at the individual project level and to establish requirements for geographical diversification.

**FMPA Response:** FMPA's governing boards will consider updating FMPA's existing Investment Policy consistent with the recommendations as soon as practical.

**Other Clarifications:** FMPA staff regularly monitors and reports on its investment portfolio to its governing boards. FMPA staff performed extensive research in 2014 on the St. Lucie Forward Sale Agreement investments in capital appreciation bonds (CABs). The next update is planned no later than May 2015 to FMPA's Audit and Risk Oversight Committee (AROC). Based on AROC input, an update will then be presented at a future meeting of FMPA's Board of Directors. Of note, the CABs held for FMPA have always had credit ratings of investment grade or higher.

**FINDING 5: Employee Benefits**

**Finding:** Compensated absences increased by 75 percent in four years, and the cost of future postretirement benefits for certain employees may result in payouts that negatively impact future rates.

**Recommendation:** The FMPA should periodically evaluate the impact of projected increases in benefit package costs provided to employees.

**FMPA Response:** FMPA's post-employment benefits are disclosed annually in FMPA's audited financial statements. FMPA's Board of Directors will address how to periodically

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 19

evaluate the projected costs of employee benefits, specifically post-retirement healthcare and annual leave, as soon as practical.

**Other Clarifications:** In FMPA's 2013 audit report, footnote XII B. Post-Employment Benefits other than Retirement, FMPA reported a net obligation at September 30, 2013, of \$2.039 million, which is less than 0.1% of total assets and deferred outflows. The actual cost of such expenditures for eight retirees in fiscal 2013 was \$43,518, which is less than 0.3% of the Agency's 2013 budget of \$13.3 million and 0.007% of the Agency and Project's fiscal 2013 total operating revenues of \$623.7 million. The number of employees who can participate in this benefit is capped by current policy. As of February 2015, only 25 active employees have the potential to meet the qualifications.

FMPA's analysis of compensated absence liability shows the largest percentage of the increase is due to the fact that more employees are qualified upon resignation or retirement in good standing to be paid for accumulated sick leave benefits and more people are qualified at a higher payout rate based on their increased years of service to FMPA, in accordance with FMPA's Policy and Employee Manual. For example, 30 people qualified for sick leave payout in 2010 compared to 52 people in 2014.

**FINDING 6: General Counsel Contract**

**Finding:** The Board of Directors (Board) set the compensation package for the General Counsel through a series of actions over several years rather than through the use of a written employment agreement and FMPA was unable to provide documentation for one of the benefits provided by Board action.

**Recommendation:** The FMPA should enter into a contract with the General Counsel encompassing all Board-approved compensation arrangements cumulatively provided to the General Counsel and implement any further compensation changes as contract amendments.

**FMPA Response:** FMPA's current General Manager and CEO was the first executive employee at FMPA to have a contract when it was originally signed in 2009. At that time, the Board of Directors discussed creating a contract for the General Counsel, and they decided against it. FMPA's Board of Directors will again consider its employment arrangements with the General Counsel and consider how to document it as soon as practical. All current salary and benefits information for the General Counsel are documented in his personnel file.

**Other Clarifications:** Note that the benefits described in the finding are in lieu of salary increases. The CEO has not received any salary increase since he joined FMPA in 2009. The General Counsel's last salary increase was in 2008.

FMPA had documentation for all except one benefit provided by Board action, the original decision to remove the vacation cap, though subsequent Board of Directors minutes confirmed this action.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 20

**FINDING 7: Severance Pay and Benefits**

**Finding:** The Chief Executive Officer's employment contract provides for severance pay and postretirement benefits for life if he is terminated for cause.

**Recommendation:** The FMPA should consider amending the CEO's contract to remove any severance compensation and postretirement benefits associated with termination for cause.

**FMPA Response:** FMPA's Board of Directors will discuss and review this matter with its General Manager and CEO as soon as practical.

**FINDING 8: Questioned Expenditures**

**Findings:** FMPA records did not always evidence the public purpose served for purchases of goods and services.

**Recommendation:** The FMPA should strengthen its procedures to require documentation that expenditures serve an authorized public purpose and retain such documentation in its records prior to payment.

**FMPA Response:** FMPA's governing boards will discuss how to more fully document the authorized public purpose as soon as practical. The Attorney General of Florida, relying on Florida Supreme Court decisions, has concluded that such expenses meet a public purpose test if approved as a public purpose by a government's legislative body. *See Op. Att'y Gen. Fla. 83-5 (1985)*. In conformity with this, FMPA's governing bodies will closely scrutinize and specifically provide a public purpose finding for expenditures. In the meantime, FMPA will discontinue, as soon as contract commitments allow, expenditures for Orlando Magic tickets, an indoor plant service and a Christmas tree.

**Other Clarifications:** The P&T Report states, "The FMPA charged and coded \$12,030 to 'flowers.'" The charges coded to this account need clarification. First, FMPA contracts with a service provider to maintain live plants in FMPA's office. The service provider is contracted to visit FMPA's office twice per month to water, trim and maintain the plants. During the 20-month audit period, FMPA paid approximately \$7,300 for this service, which was charged to this account. Second, FMPA rents a Christmas tree for its office lobby from Thanksgiving to New Years. The vendor delivers the artificial tree, sets it up, decorates it, and removes the tree at the end of the holiday season.<sup>9</sup> During the 20-month audit period, two holiday seasons occurred, and FMPA paid a total of \$3,034 for this service, which was charged to this account. Finally, FMPA sent flowers arrangements to governing board members or staff for occasions such as bereavement and hospitalization. During the 20-month audit period, FMPA spent \$1,735 on flowers or donations in lieu of flowers. FMPA's governing bodies will review the budget again for these expenditures during this year's budget process, which commences with the first meetings of the Business Planning and Budget Committee in April 2015.

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<sup>9</sup> It is a common practice for governments around the country to celebrate the season.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 21

The P&T Report states, "The FMPA charged and coded \$106,850 to 'meetings.'" This is the largest expenditure cited in this finding where the Auditor General questioned the public purpose of some expenses. The vast majority of these meetings are with FMPA's member city owners. The meetings with members include governing board and committee meetings, such as the Board of Directors, Executive Committee, Business Planning and Budget Committee, Policy Makers Liaisons Committee and others. In addition, the meetings with members include topics such as member services, training programs, plant operations, NERC compliance, cyber security, safety training, round table groups and others. As a joint action agency, FMPA hosts a large number of meetings and training sessions to coordinate joint action on a myriad of topics that are a service and benefit to its member city owners. The in-office meeting costs during the 20-month period include food, coffee, soft drinks and associated supplies (i.e., paper plates, plastic wear, napkins, cups, table cloths, serving utensils, etc.).

**FINDING 9: Competitive Selection**

**Finding:** The FMPA did not always follow its purchasing policies regarding competitive selection.

**Recommendation:** The FMPA should ensure that goods and services purchased through contractors are competitively procured in accordance with established policies and procedures.

**FMPA Response:** FMPA will strengthen internal controls to ensure that purchases are made in accordance with the existing Procurement Policy and other policies related to competitive selection as soon as practical.

**Other Clarifications:** FMPA's financial auditors were initially selected through a competitive process. The firm was selected based on its extensive auditing experience with electric utilities and local governments, as well as its competitive price as evidenced in the competitive selection process. In 2014, after deliberations by FMPA's Board of Directors and Executive Committee, the audit contract was extended based on high quality of past performance and after negotiating a fee decrease from the existing 2013 audit fee of \$110,000 to the new 2014 fee of \$107,500. FMPA believes that its processes have led to procure an industry-leading financial auditing firm at a competitive price.

The P&T Report states that for purchases above \$1,000 and below \$5,001, FMPA records did not evidence that three quotes were obtained for "an ice machine purchase." FMPA's nine-year-old ice machine was not working properly, so a service call was placed. The service provider gave FMPA three options: (1) replace the malfunctioning part for \$2,284.78, (2) purchase a replacement ice-maker component for \$3,787.83, or (3) lease a unit for eight years at a cost of \$12,960. FMPA evaluated the alternatives and decided the best overall choice was replacing the ice-maker component.



**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 22

**FINDING 10: Selection of Bond Professionals**

**Finding:** The FMPA had not recently used a competitive selection process when selecting financial advisors and bond counsel for bond issues, potentially increasing costs associated with bond issues.

**Recommendation:** To ensure that qualified financial and professional services are acquired at the lowest possible cost consistent with the size, nature, and complexity of the bond issue, the FMPA should select financial advisors and bond counsel using a competitive selection process whereby RFPs or RFQs are solicited from a reasonable number of professionals.

**FMPA Response:** FMPA previously utilized a competitive selection process in selecting its current bond counsel and financial advisor. FMPA's governing boards will review its Debt Policy and consider the modifications of its current language to address the Auditor General's recommendation for a competitive selection process of qualified financial services in the future to include but not be limited to financial advisors and bond counsel as soon as practical.

**FINDING 11: Credit Cards**

**Finding:** The FMPA did not always follow its policies regarding credit card issuance and purchases, and did not employ procedures for monitoring credit limits for reasonableness.

**Recommendation:** The FMPA should enhance its procedures to ensure compliance with its policies regarding credit card user agreements. The FMPA should also enhance its existing policies to clarify responsibilities regarding notification of credit card user termination and associated card cancelation, including notification requirements of member municipalities; require all credit card users to sign the monthly credit card activity reports; and require periodic reviews of credit card user credit limits for reasonableness.

**FMPA Response:** FMPA will enhance its policies, procedures and documentation for credit cards consistent with the Auditor General's recommendations as soon as practical.

**FINDING 12: Travel Expenditures**

**Finding:** The FMPA did not always follow its travel policies or ensure that travel-related receipts were submitted by contractors. Additionally, the FMPA's travel policies could be enhanced.

**Recommendation:** The FMPA should consider amending its Travel Policy to include a cap on per-meal costs. The FMPA should also enhance its procedures to ensure compliance with its policies regarding family member travel expenses and most economical cost of air travel, and to require supporting receipts for out-of-pocket expenses incurred by contractors. In addition, the FMPA should discontinue providing mileage reimbursements to employees who also receive vehicle allowances.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 23

**FMPA Response:** FMPA's Board of Directors will consider updating FMPA's existing Travel Expense Policy, taking the Auditor General's recommendations into consideration as soon as practical. In the meantime, FMPA will stop hosting a dinner during the annual legislative rally in Washington, D.C., which will eliminate this meal cost and the rare occasion where alcoholic beverages were provided. As part of updating FMPA's Travel Policy, FMPA will expressly prohibit reimbursement for alcohol, although FMPA has had a practice of "no alcohol" for many years.

**Other Clarifications:** The audit finding referenced as "Family Travel Expenses" was an error on FMPA's part. As soon as the matter was brought to FMPA's attention, it was researched by FMPA staff, as directed by the CEO and General Counsel, beyond the Auditor General's audit period. The expense has been repaid to FMPA, appropriate taxes paid to the State of Florida and an enhanced travel expense approval procedure has been implemented to prevent reoccurrence.

**FINDING 13: Peak Shaving**

**Finding:** The ARP power supply project contracts did not address peak shaving and, although the Executive Committee agreed to curtail peak-shaving activities, the agreement appears primarily voluntary in nature, relies on self-reporting, and contains no consequences for noncompliance.

**Recommendation:** If the FMPA desires to affirmatively eliminate peak shaving activities of its members, the FMPA should consider amending the power supply project contracts to prohibit such activities and establish consequences for noncompliance.

**FMPA Response:** The issues identified by the Auditor General concerning the value of peak shaving and monitoring compliance with contract/policy were considered by FMPA's Executive Committee when the policy was approved in 2014. FMPA currently has some capability to verify compliance and options to address any non-compliance. FMPA's Executive Committee decided to approve the policy because amending the contract requires approval from a number of internal and external stakeholders. The contract states that it cannot be "amended, modified, or otherwise altered in any manner that will adversely affect the security for the Bonds." Any proposed amendments must be certified as having no adverse effect by a consulting engineer and bond counsel. The proposed amendments must also be approved by trustees on behalf of bondholders, then credit rating agencies must agree that the amendments will not affect the credit rating, then the amendments must be approved by bond insurers, if any, then unanimous consent must be received from the governing boards of every project participant (i.e., city council, city commission or utility board), and finally, the amendments must be approved by FMPA's Executive Committee. As should be evident, amending the contract is a lengthy process and is not within FMPA's sole discretion. A review of the peak shaving policy and enforcement options will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 24

**FINDING 14: ARP Termination Provisions**

**Finding:** Certain ARP power supply project contract provisions relating to withdrawing members are ambiguous, used a fixed discount rate rather than one associated with current capital costs, and did not provide for independent verification by the withdrawing member.

**Recommendation:** Since ARP revenue requirements are calculated using monthly coincident peak demands, the FMPA should consider using a 12-month average of coincident peak to more accurately estimate the withdrawing member's share of fixed costs. Also, the FMPA should consider amending the power supply project contracts to clarify how withdrawal payments are to be calculated, define "additional benefits" and "excess amounts," establish a variable withdrawal payment discount rate that fluctuates with the actual cost of debt, and remove the 90 percent cap of an ARP member's withdrawal payment. Additionally, since the withdrawal payment can be used to temporarily correct deficiencies in other operating funds and for "excess amounts" to be deposited in the "General Reserve Fund," it should be determined how this ability to use these funds is recognized in the monthly revenue requirement calculation for remaining ARP participants.

**FMPA Response:** FMPA's Executive Committee will discuss the Auditor General's comments. Recommendations that require an amendment of the contract must complete an approval process involving a number of internal and external stakeholders. The contract states that it cannot be "amended, modified, or otherwise altered in any manner that will adversely affect the security for the Bonds." Any proposed amendments must be certified as having no adverse effect by a consulting engineer and bond counsel. The proposed amendments must also be approved by trustees on behalf of bondholders, then credit rating agencies must agree that the amendments will not affect the credit rating, then the amendments must be approved by bond insurers, if any, then unanimous consent must be received from the governing boards of every project participant (i.e., city council, city commission or utility board), and finally, the amendments must be approved by FMPA's Executive Committee. As should be evident, amending the contract is a lengthy process and is not within FMPA's sole discretion. A review of the Auditor General's recommendations will be included in the Executive Committee's proposed scope of work for an independent management consulting firm.

**Other Clarifications:** When an All-Requirements Project (ARP) participant elects to withdraw from ARP under section 29, it must make two payments under section 29(c)(1) and (c)(2). Generally, the payment made under 29(c)(1) is meant to cover the withdrawing participant's share of ARP debt to protect the remaining participants from incurring higher debt burden because a participant decided to withdraw. FMPA is required to plan and serve the annual coincident peak demand of the ARP. This peak demand is what drives FMPA's planning since FMPA must plan for and have resources sufficient to meet the annual coincident peak. Section 29(c)(1) matches this reality. Therefore, to use a 12-month average of coincident peaks would detach the withdrawal payment from the reality of FMPA's obligation and could put the non-withdrawing participants at risk of bearing higher debt service just because of the choice made by the withdrawing participant.

**EXHIBIT C (CONTINUED)**  
**MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 25

Since this audit came about, fundamentally, due to a dispute over the reasonableness of FMPA's power supply contract provisions, FMPA notes that the Auditor General reviewed the ARP contract and commented in three areas:

1. Whether the general contract terms were typical of other joint action agencies (JAAs),
2. Whether the ARP exit provisions are typical of JAAs, and
3. Whether FMPA calculated the exit cost to Vero Beach consistent with the contracts and consistent with FMPA's calculations for other FMPA members.

As to the first item, the Auditor General found that FMPA's bond resolutions and power supply project contracts "are typical of other JAAs."

As to the second item, the Auditor General found that FMPA's exit options are more lenient than most joint action agencies.

Finally, regarding FMPA's calculation of the exit costs for Vero Beach and another FMPA city, the Auditor General determined FMPA's estimates "appear to be reasonable." The Auditor General stated, "The FMPA calculations of the withdrawal payments in these instances followed the respective ARP power supply power contracts' withdrawal provisions."

**FINDING 15: Disaster Recovery Plan**

**Finding:** The FMPA's disaster recovery plan could be enhanced.

**Recommendation:** The FMPA should enter into a written agreement to procure an alternate processing site that is sufficiently geographically distant to minimize the risk of being unable to continue critical operations in the event of a hurricane or other geographically large disaster.

**FMPA Response:** FMPA will investigate an alternate data processing facility, consistent with the Auditor General's recommendations as soon as practical.

**EXHIBIT C (CONTINUED)  
MANAGEMENT'S RESPONSE**

Mr. David W. Martin  
March 25, 2015  
Page 26

4. CONCLUSION

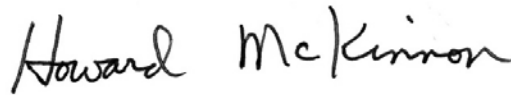
FMPA takes seriously its responsibility to meet its members' needs and expectations. This audit will further FMPA's ability to do that. On behalf of the Board of Directors and Executive Committee, we thank the Auditor General for handling this important task with professionalism. We are certain that FMPA will become a better organization as a result.

If you require additional information about the details of this response, please contact Nicholas P. Guarriello, FMPA's General Manager and CEO, at 407-355-7767 or [nick.guarriello@fmpa.com](mailto:nick.guarriello@fmpa.com).

Sincerely,



Bill Conrad  
Chairman  
Board of Directors



Howard McKinnon  
Chairman  
Executive Committee

cc: Board of Directors  
Executive Committee  
Nicholas P. Guarriello, FMPA  
Frederick M. Bryant, FMPA  
Jody Lamar Finklea, FMPA

MAYOR  
BRIAN M. BAREFOOT

VICE MAYOR  
GERARD A. WEICK

COUNCIL:  
MICHAEL B. OCHSNER  
RICHARD M. HAVERLAND  
THOMAS F. SLATER



TOWN MANAGER  
ROBERT H. STABE, JR.

TOWN CLERK  
LAURA ALDRICH

TOWN ATTORNEY  
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March 27, 2015

The Hon. Senator Joseph Abruzzo, Alternating Chair  
The Hon. Representative Daniel Raulerson, Alternating Chair  
Joint Legislative Auditing Committee

Reference: Auditor General's Audit of the FMPA and Accountability

Dear Senator Abruzzo and Representative Raulerson:

On behalf of my fellow members of the Indian River Shores Town Council and the residents we serve, I want to thank you for scheduling a meeting to review the Auditor General's audit of the Florida Municipal Power Agency (FMPA). Our Town has a direct interest in the FMPA report. Unfortunately, I am unable to attend this meeting in person. If appropriate, our Council would appreciate if this letter could be read into the official record during Monday's meeting.

The Town of Indian River Shores is grateful to the Auditor General and your Joint Committee for beginning to review some of the operations of the FMPA – an unelected, unregulated, monopoly body whose decisions have a direct financial impact on millions of Florida citizens.

The audit review conducted to-date is revealing. The many examples of mismanagement and inappropriate hedging practices found by the auditors continue to drive up the cost of power that the FMPA charges its member utilities, which then pass those high costs on to their customers. Please understand that it is the customers of those FMPA-member utilities who are truly suffering because of the FMPA's poor decisions.

This unfortunately includes our Town's residents. Our Town has a population of about 4,000 people. Roughly 800 of our residents enjoy electric service from Florida Power & Light (FPL), a regulated utility that offers reasonably priced electric service. Our other 3,200 residents are served by the Vero Beach utility, an FMPA member whose rates over the last 10 years have been as much as 45 percent higher than FPL's. For the calendar year 2013, Vero Beach's rates were 41.19 percent higher than FPL's. Over the last decade, the 3,200 Town residents receiving electric service from Vero Beach's utility have collectively paid over \$16 million more than they would have paid if the same electric service had been provided by FPL. This rate crisis is driven in large part by FMPA's high costs and continues to plague our Town and our region.

To its credit, in an effort to comprehensively resolve this rate crisis, Vero Beach reached an agreement with FPL and others which called for Vero to sell its utility to FPL. That sale was overwhelmingly supported by citizens of Vero Beach and its electric customers throughout the region. Unfortunately, that sale has been obstructed by FMPA. FMPA leaders have refused to meet with Vero Beach and FPL to find a mutually beneficial solution, and have shown no willingness to help Vero's electric customers achieve relief from excessive rates.

- more -

It is our hope that your leadership on this issue will encourage the Legislature to continue its review of this unelected and unregulated monopoly, and take the steps necessary to make the FMPA accountable and protect customers around the state from its oppressive and costly practices.

Sincerely,



Brian M. Barefoot  
Mayor  
Town of Indian River Shores

cc: The Hon. Lizbeth Benacquisto, Florida Senate  
The Hon. Rob Bradley, Florida Senate  
The Hon. Audrey Gibson, Florida Senate  
The Hon. Wilton Simpson, Florida Senate  
The Hon. Joe Negron, Florida Senate  
The Hon. Debbie Mayfield, Florida House of Representatives  
The Hon. Amanda Murphy, Florida House of Representatives  
The Hon. Ray Wesley Rodrigues, Florida House of Representatives  
The Hon. Cynthia Stafford, Florida House of Representatives  
Gerard Weick, Vice Mayor, Indian River Shores  
Richard Haverland, Indian River Shores Town Council  
Michael Ochsner, Indian River Shores Town Council  
Thomas Slater, Indian River Shores Town Council





**TaxWatch Report on FMPA is expected to be released March 30, 2015**