



DAVID W. MARTIN, CPA
AUDITOR GENERAL

AUDITOR GENERAL

STATE OF FLORIDA

G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450



PHONE: 850-412-2722
FAX: 850-488-6975

January 21, 2015

The Honorable Bill Conrad
Board Chair
Florida Municipal Power Agency
8553 Commodity Circle
Orlando, Florida 32819-9002

Mr. Howard McKinnon
Executive Committee Chair
Florida Municipal Power Agency
8553 Commodity Circle
Orlando, Florida 32819-9002

Dear Mayor Conrad and Mr. McKinnon:

Enclosed is a list of preliminary and tentative audit findings and recommendations which may be included in a report to be prepared on our operational audit of:

Florida Municipal Power Agency

Pursuant to Section 11.45(4)(d), Florida Statutes, you are required to submit to me within thirty (30) days after receipt of this list a written statement of explanation concerning all of the findings, including therein your actual or proposed corrective actions.

Your written statement of explanation should be submitted electronically to flaudgen_audrpt_lg@aud.state.fl.us (flaudgen_audrpt_lg@aud.state.fl.us) in **source format (e.g., Word or WordPerfect)** and include your digitized signature. For quality reproduction purposes, if you are not submitting your response in source format, please convert your response to PDF and not scan to PDF. If technical issues make an electronic response not possible, then a hard copy (paper) response will be acceptable. If you are submitting a hard copy, address to Auditor General, Local Government Audits/Section 341, 111 West Madison Street, Tallahassee, FL 32399-1450.

Please e-mail this Office at flaudgen_audrpt_lg@aud.state.fl.us to indicate receipt of the preliminary and tentative findings. Absent such receipt, delivery of the enclosed list of findings is presumed, by law, to be made when it is delivered to your office.

The Honorable Bill Conrad
Mr. Howard McKinnon
January 21, 2015
Page Two

If within the 30-day period you have questions or desire further discussion on any of the proposed findings and recommendations, please contact Marilyn Rosetti at (850)412-2881 or at marilynrosetti@aud.state.fl.us.

Sincerely,



David W. Martin

DWM/jk

Enclosures

c: Board of Directors
Executive Committee
Fred M. Bryant, Esq., General Counsel
Jody Lamar Finklea, Esq. Assistant General Counsel
Nick Guarriello, CEO and General Manager

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 joint action agencies.

Finding No. 2: Investment in natural gas exploration and drilling were not consistent with industry practices utilized by other 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 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 all 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.

BACKGROUND

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. 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

As of October 31, 2014, the FMPA had 31 member municipalities, 20 of which participated in one or more power 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

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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

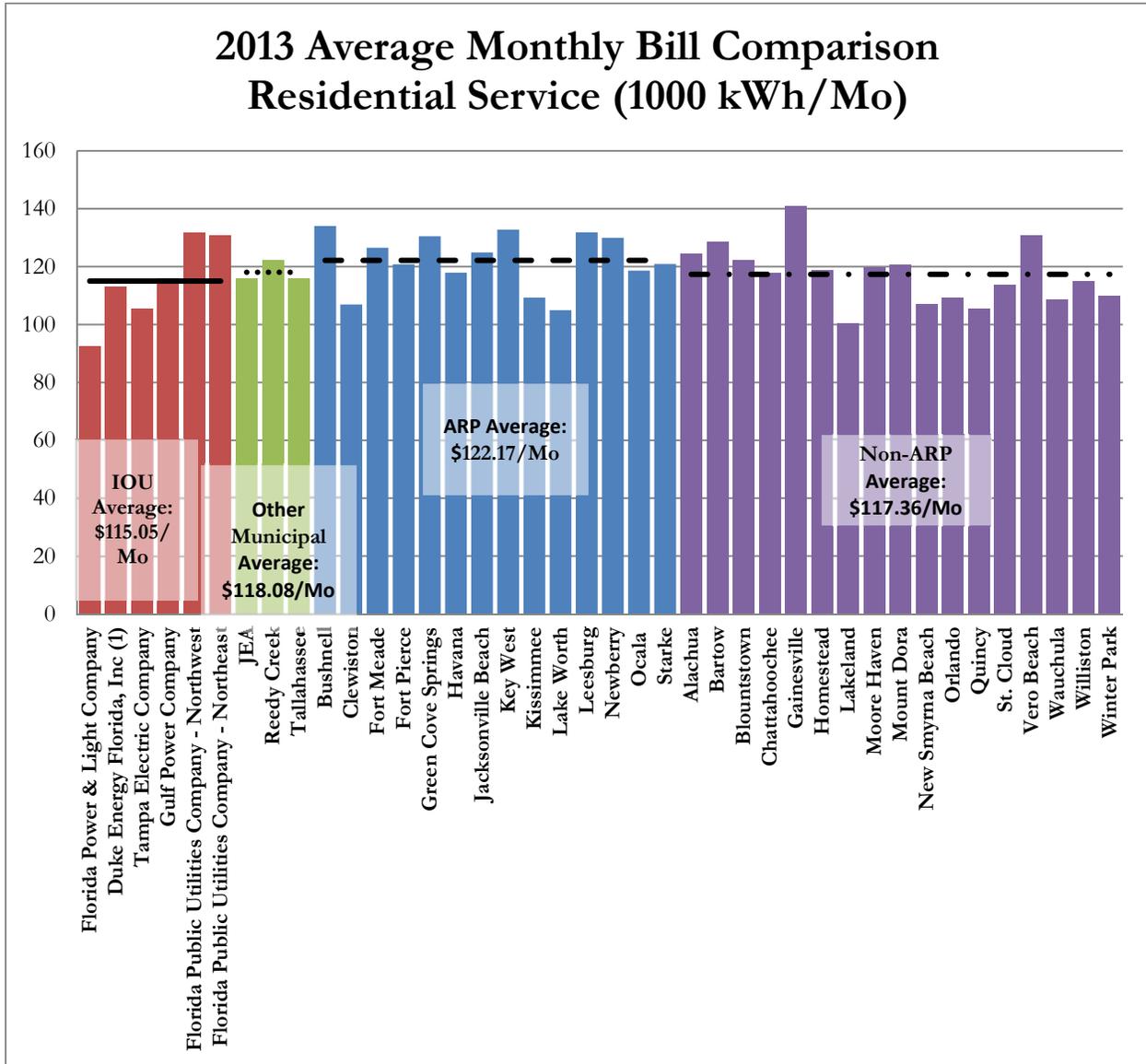
FINDINGS AND RECOMMENDATIONS

The FMPA was created pursuant to interlocal agreements among several municipalities. 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. As noted in the **Background** section, oversight of the FMPA’s activities is provided by the Board composed of member municipalities for non-ARP projects and by an Executive Committee for the ARP project.

Table No. 3 shows comparative monthly residential service bills for the 2013 calendar year for IOUs, non-FMPA member municipal electrical utilities, FMPA ARP members, and FMPA non-ARP members. The FMPA ARP members’ weighted average monthly bills are greater than the weighted average IOU bills and weighted average non-FMPA member municipal electric utilities’ monthly bills by \$7.12 (6 percent), and \$4.09 (3 percent), respectively. Additionally, the weighted average bill for an FMPA ARP member is higher than the weighted 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

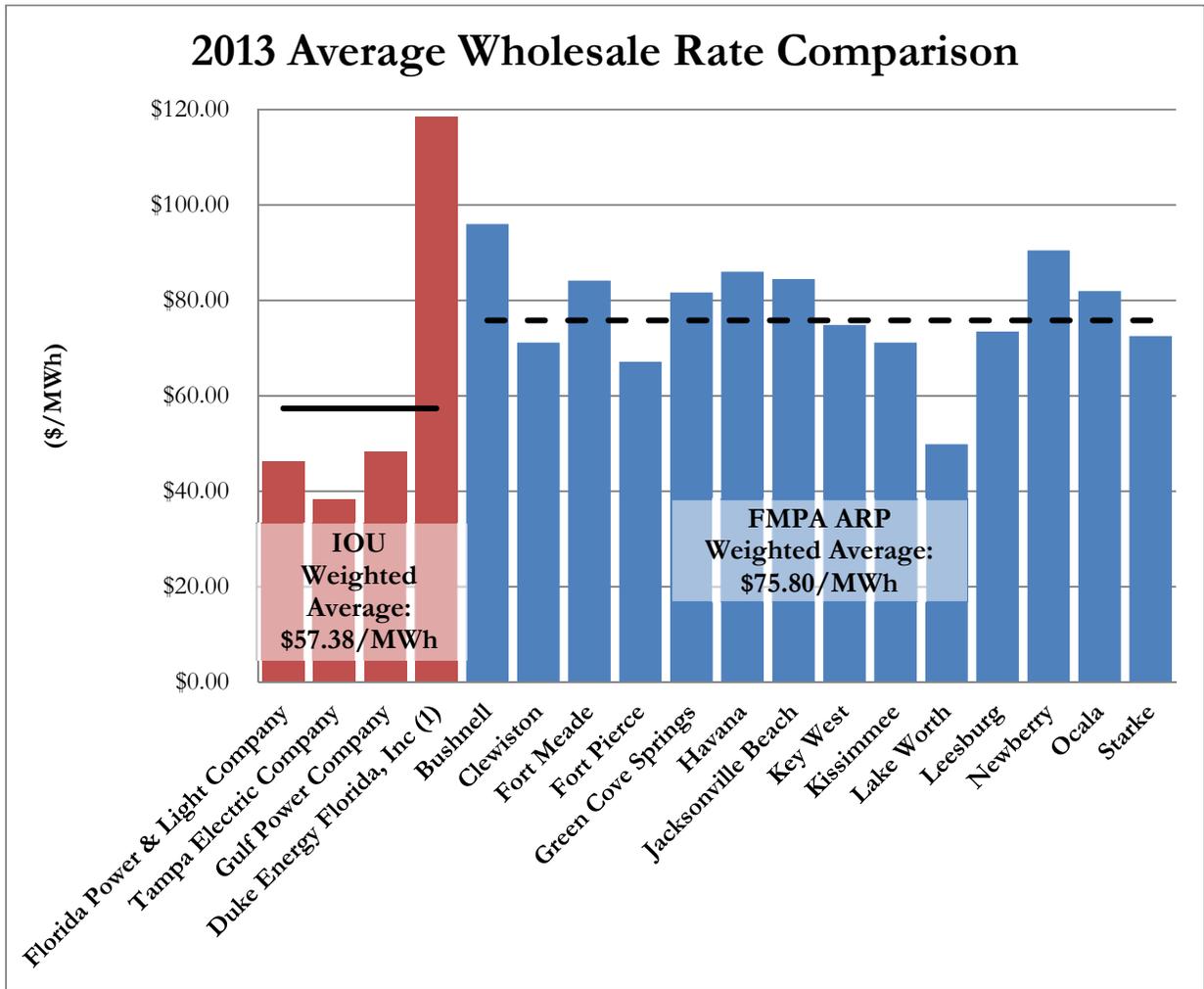


Note (1) Duke Energy completed a merger with Progress Energy on July 2, 2012. Upon completion of the transaction, the new entity operates in Florida as Duke Energy Florida, Inc.

Source: Florida Public Service Commission

While the FMPA ARP residential weighted average bill in Table 3 is 6 percent higher than the IOU residential weighted average bill, the weighted average wholesale rate for ARP members exceeds the IOU weighted average wholesale rate by a much greater percentage. Table No. 4 shows wholesale rates for ARP members and the wholesale rates for IOUs that sell power on a wholesale basis in Florida. The weighted average cost per Megawatt Hour (MWh) for ARP members in calendar year 2013 was \$75.80, which is \$18.42, or 32 percent, higher than the IOU amount of \$57.38.

Table 4



Note: (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.

Source: Federal Energy Regulatory Commission's Form-1 and FMPA ARP Invoices

One contributing factor to the higher FMPA wholesale costs is the increase in fixed costs. For the primary monthly billing components invoiced to ARP members, Table 5 shows the weighted average cost per MWh over the last ten years. Charges to individual ARP members may be above or below the average amounts based upon FMPA cost allocations, member-owned capacity credits, and other factors. For example, for the month of September 2014, billed amounts before credits ranged from a low of \$75.28 per MWh for one member to a high of \$96.99 per MWh for another member.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

Table 5

Fiscal Year	Demand Charge (1)	Energy Charge (1)	Transmission (1)
2015 (Budgeted)	\$ 22.46	\$ 32.62	\$ 2.60
2014	22.45	32.11	2.71
2013	21.70	32.44	2.43
2012	19.92	49.09	2.28
2011	18.84	47.90	2.08
2010	17.52	56.65	1.56
2009	15.00	59.95	1.72
2008	13.45	58.65	1.50
2007	11.10	55.00	1.65
2006	11.10	55.00	1.65

Notes: (1) Per Megawatt hour

Source: FMPA Records

As shown in Table 5, the demand and energy charge components are the two largest components on ARP member billings. Since the 2005-06 fiscal year, the energy charge, which represents the cost of purchased fuel, decreased from \$55 per MWh to \$32.62 per MWh, a decrease of 41 percent. In contrast, the weighted average demand charge has increased from \$11.10 per MWh to \$22.46 per MWh, a 102 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 6 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 6

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

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,

PRELIMINARY AND TENTATIVE FINDINGS

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.

Hedging Activities

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.

Finding No. 1: Fuel Hedging

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 JAAs¹ that employ gas 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 7, the FMPA incurred net total losses of \$247.6 million related to fuel hedging activities over the past 12 fiscal years.

¹ 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

Table 7

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)
Total	<u>\$(247,631,584)</u>

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.

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.

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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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 8.

Table 8

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

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 JAAs² 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 9 compares the relative risk characteristics of the two natural gas procurement strategies:

² 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

Table 9

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 9 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.

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.

Finding No. 3: Interest Rate Swaps

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.”

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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 JAAs³ 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.

³ 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

Investments

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:

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 10, 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 10

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

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

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.

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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

- 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 Counsel⁴ 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 11.

Table 11

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.

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

Finding No. 6: General Counsel Contract

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.” In addition to periodic salary increases, the CEO and

⁴ 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

General Counsel have also received benefits such as additional annual leave and contributions to retirement health savings accounts that 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.

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.

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

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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 52 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 12.

Table 12

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
<u>\$23,844</u> Total	

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.

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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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 purchase above \$5,000 and below \$10,001, a hotel for a holiday party, FMPA records did not evidence that three written quotes were obtained or proper justification for not obtaining the required three written quotes.
- 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.

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

Finding No. 10: Selection of Bond Professionals

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.⁵ 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

⁵ GFOA Best Practice: *Selecting and Managing Municipal Advisors* (2014)

PRELIMINARY AND TENTATIVE FINDINGS

suggestions with respect to structure, timing, and marketing of the bonds being sold.⁶ 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.⁷

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.⁸ The GFOA's best practice further recommends that debt issuers review their relationships with bond professionals periodically.

- **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.⁹ 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.

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

⁷ GFOA Best Practice: *Selecting Bond Counsel* (1998 and 2008)

⁸ 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)

⁹ The financial advisor provided services to four of the five member municipalities.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

Finding No. 11: Credit Cards

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 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

Travel

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).”¹⁰ 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, 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

¹⁰ The terms General Manager and Chief Executive Officer are used interchangeably by the FMPA.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

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.

Finding No. 14: ARP Termination Provisions

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 resources¹¹ are subtracted from

¹¹ 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.

PRELIMINARY AND TENTATIVE FINDINGS

the coincident peak demand calculation to estimate the member's share.¹² 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.¹³

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:

- 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.

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

¹³ 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

- 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 issues¹⁴ 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 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.

¹⁴ 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.

*****PRELIMINARY AND TENTATIVE FINDINGS*****

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.

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.

END OF P&T DOCUMENT