



Florida Municipal Power Agency

July 29, 2015

Ms. Sherrill F. Norman, CPA
Auditor General, State of Florida
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, FL 32399-1450

Re: Auditor General Report No. 2015-165

Dear Ms. Norman:

On May 28, 2015, the Florida Municipal Power Agency (FMPA) filed with the Auditor General a 60-day written corrective action plan detailing FMPA's plans and timetable for addressing findings in the Auditor General's operational audit of FMPA. That filing was made as directed by the Florida Joint Legislative Auditing Committee in a meeting held March 30, 2015.

FMPA's governing boards and member utilities take very seriously the findings of the Auditor General and are committed to addressing each recommendation in a prompt and thorough manner. As evidence of this commitment, FMPA hereby submits another 60-day report to update you regarding our progress and plans for addressing each finding. We will continue to submit reports every 60 days until all findings have been addressed.

The attached report documents that FMPA has completed action on six of the 15 audit findings. The remaining nine items are scheduled for governing board action between now and the end of the calendar year, as described more fully in the report. If you require additional information, please contact Nicholas P. Guarriello, FMPA's General Manager and CEO, at 407-355-7767 or nick.guarriello@fmpa.com.

Sincerely,

A handwritten signature in black ink, appearing to read "Bill Conrad".

Bill Conrad
Chairman
FMPA Board of Directors

A handwritten signature in black ink, appearing to read "Howard McKinnon".

Howard McKinnon
Chairman
FMPA Executive Committee

Enclosure

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



Florida Municipal Power Agency

Re: Auditor General Report No. 2015-165

FMPA Audit Response Report

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SUBMITTED TO

State of Florida
Auditor General
Sherrill F. Norman, CPA

July 29, 2015

Community Power + Statewide Strength

Introduction

The Florida Joint Legislative Auditing Committee (JLAC) met March 30, 2015, and heard a presentation from the Auditor General regarding its operational audit of the Florida Municipal Power Agency (FMPA or the Agency). At the conclusion of that meeting, the JLAC directed FMPA to provide to the Auditor General within 60 days a written corrective action plan detailing FMPA's plans and timetable for addressing each of the 15 audit findings. FMPA filed a report with the Auditor General on May 28, 2015, that responded to the JLAC's directive. FMPA's governing boards and member utilities take very seriously the findings of the Auditor General. As evidence of our commitment to addressing each finding in a prompt and thorough manner, FMPA hereby voluntarily submits another 60-day progress report, and FMPA will continue to submit reports every 60 days until all findings have been addressed.

FMPA has two governing boards: the Board of Directors and the Executive Committee. The Board of Directors is made up of one representative from each of the Agency's 31 member municipal electric utilities. The Board of Directors governs general activities of the Agency and all of its power supply projects except FMPA's All-Requirements Power Supply Project (the All-Requirements Project). The All-Requirements Project is independently governed by the Executive Committee. Each of the 13 municipal electric utilities that are participants and purchase power through the All-Requirements Project appoints a representative to the Executive Committee. Depending on the nature of each audit finding, some recommendations are within the exclusive authority of FMPA's Executive Committee and some findings are, or will be, addressed by both governing boards.

To address each of the Auditor General's recommendations, FMPA's Board of Directors or Executive Committee, or both, will conduct a public discussion and a vote. Action on the Auditor General's findings are or will be scheduled as agenda items for governing board meetings. FMPA's governing boards have a practice of hearing a matter first as an information item and then a second time at a subsequent meeting for action. FMPA's governing boards generally meet once per month.

The following report documents FMPA's actions as of July 29, 2015, and provides an anticipated timetable for addressing each of the findings.

Executive Summary

This report provides a 120-day status update on FMPA's response to the 15 findings and recommendations from the Auditor General. As of July 29, 2015, FMPA's governing boards have completed work on six audit recommendations (Findings No. 3, 4, 8, 9, 10 and 11), as described in the following report. For two recommendations (Findings No. 1 and 14), FMPA's Executive Committee has decided to retain an independent management consulting firm to fully address the Auditor General's recommendations. Due to the time required for a competitive selection process, the consultant's recommendations may not be available until November 2015. Between now and the end of this calendar year, FMPA's governing boards will address the remaining seven recommendations on the estimated timetable described in the following report. Comparing the estimated timetable in this report to the estimated timetable in the prior report of May 28, 2015, FMPA now anticipates that two findings (No. 13 and 15) will be completed one month earlier than originally planned and one finding (No. 2) might take one month longer than originally planned.

Florida Municipal Power Agency

FMPA Audit Response Report

July 29, 2015

FINDING 1: Fuel Hedging

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

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

FMPA Status Report: On May 21, 2015, FMPA's Executive Committee voted to cease its fuel hedging program known as FST (FMPA Short-term) Program. On May 21, 2015, FMPA's Executive Committee also approved issuing a Request for Qualifications (RFQ) to retain an independent management consulting firm to provide analysis and recommendations on this finding. Responses to the RFQ were received on June 26. Interviews with respondents are planned on July 30. FMPA anticipates making a consultant selection by mid-August and having a contract executed with the consultant by mid-September. The consultant is expected to present its initial results to FMPA's Executive Committee in November 2015, and FMPA will begin addressing the consultant's recommendations at that time.

FINDING 2: Natural Gas Supply Agency Participation

Finding: 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.

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

FMPA Status Report: This recommendation will be discussed by the FMPA Executive Committee in the August or September timeframe, and final action is anticipated in September or October 2015.

FINDING 3: Interest Rate Swaps

Finding: 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.

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

FMPA Status Report: Action on this recommendation is complete. On May 21, 2015, FMPA's Executive Committee approved amendments to its Debt Risk Management Policy that implemented two of the three Auditor General's recommendations: 1) prohibiting the employment of interest rate swaps without concurrently issuing debt, and 2) prohibiting interest rate swaps before required approvals for projects are obtained from regulatory bodies. The Auditor General's third recommendation about developing an exit strategy for Taylor swaps also has been addressed. FMPA's Executive Committee approved actions on April 16, 2015, and May 6, 2015, providing policy direction on when and how to exit the Taylor swaps, and then on May 21, 2015, the Executive Committee approved resolutions authorizing the permanent financing structure for the Taylor swap termination costs. All nine swaps contracts were terminated as of June 16, 2015, removing the ongoing risk to ARP members, and FMPA closed June 30, 2015, on the permanent financing for the Taylor swap termination costs.

FINDING 4: Investment Policy

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

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

FMPA Status Report: Action on this recommendation is complete. On May 21, 2015, FMPA's Board of Directors and Executive Committee approved amendments to the Agency's Investment Policy that fully address all three of the Auditor General's recommendations: 1) clarifying the meaning of the "two highest credit rating categories," 2) clarifying that the Investment Policy applies individually to each Project, not in any combination of Projects, and 3) establishing an investment limit based on geographic concentration.

FINDING 5: Employee Benefits

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

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

FMPA Status Report: FMPA staff is preparing a policy analysis to evaluate the impact of projected increases in benefit package costs, which will be presented to FMPA's governing boards in August, and final action is anticipated in September 2015.

FINDING 6: General Counsel Contract

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

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

FMPA Status Report: This recommendation will be discussed by the FMPA Board of Directors in the August and September timeframe during the General Counsel's annual performance review, and final action is anticipated by October 2015.

FINDING 7: Severance Pay and Benefits

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

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

FMPA Status Report: This recommendation will be discussed by the FMPA Board of Directors in the August and September timeframe during the General Manager and CEO's annual review, and final action is anticipated by October 2015.

FINDING 8: Questioned Expenditures

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

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

FMPA Status Report: Action on this recommendation is complete. On June 18, 2015, FMPA's Board of Directors and Executive Committee approved a new Public Purpose Policy and a new Public Purpose Determination Procedure. The new policy and procedure provide that FMPA's governing bodies will specifically provide a public purpose finding for certain expenditures and retain such documentation in FMPA's records before and after payment. In addition, FMPA's budgets will include language stating that all expenditures have been authorized and approved for a public purpose.

This follows FMPA's immediate action, after the preliminary and tentative audit report was issued in January, to discontinue several expenditures questioned by the Auditor General, including Orlando Magic tickets, an indoor plant service, Christmas tree rental and an annual conference dinner for members in Washington, D.C.

FINDING 9: Competitive Selection

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

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

FMPA Status Report: Action on this recommendation is complete. On July 24, 2015, FMPA's Board of Directors and Executive Committee approved revisions to FMPA's Procurement Policy and FMPA's Accounting and Internal Controls Policy. In addition, FMPA staff committed to perform an annual training session on the Procurement Policy to ensure that appropriate FMPA staff are familiar with the policy requirements. Finally, FMPA's governing boards approved on July 24, 2015, an amendment to FMPA's Accounting and Internal Controls Policy that provides for FMPA's Contract Compliance Audit Department to conduct an annual review of compliance with FMPA's Procurement Policy and report the results to FMPA's General Manager and CEO or FMPA's Audit and Risk Oversight Committee. Taken together, these policy updates, annual training, and annual testing are expected to fully address the Auditor General's recommendation to ensure that goods and services are competitively procured in accordance with policies.

FINDING 10: Selection of Bond Professionals

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

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

FMPA Status Report: Action on this recommendation is complete. On May 21, 2015, FMPA's governing boards approved amendments to the Agency's Debt Risk Management Policy that add requirements for a competitive selection process for all professionals associated with FMPA's debt. FMPA will issue its initial competitive selection request for trustee, registrar and paying agent by the end of October 2015. Additional competitive selection processes will be undertaken by FMPA for other bond professionals until all bond professionals have been engaged under the amended Debt Risk Management Policy.

FINDING 11: Credit Cards

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

Recommendation: The FMPA should enhance its procedures to ensure compliance with its policies regarding credit card user agreements. The FMPA should also enhance its existing policies to clarify responsibilities regarding notification of credit card user termination and associated card 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.

FMPA Status Report: Action on this recommendation is complete. On June 18, 2015, FMPA's Board of Directors and Executive Committee approved revisions to FMPA's Credit Card Policy, new Credit Card Procedures, and revised Credit Card Use Agreements for employees and employees of FMPA members that work at power generation facilities contractually under FMPA's operational control. The policy and the procedures fully address all of the Auditor General's recommendations, including: 1) providing for regular checks of credit card user agreements on file, 2) providing notification requirements for credit card user terminations and associated card cancellation, including notification requirements of member municipalities, 3) requiring signatures on monthly activity reports, and 4) requiring periodic review of credit card user credit limits for reasonableness.

FINDING 12: Travel Expenditures

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

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

FMPA Status Report: FMPA staff is preparing a policy analysis to address this recommendation. This recommendation will be discussed by the FMPA governing bodies in September, and final action is anticipated in October 2015.

The audit finding regarding family member travel expenses was an error on FMPA's part. As soon as the matter was brought to FMPA's attention, it was corrected with repayment made to FMPA and appropriate taxes paid to the State of Florida. Since then, FMPA has adopted an enhanced travel expense approval procedure to prevent reoccurrence.

FINDING 13: Peak Shaving

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

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

FMPA Status Report: This recommendation will be discussed by the FMPA Executive Committee in August, and final action is anticipated in September 2015.

FINDING 14: ARP Termination Provisions

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

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

FMPA Status Report: On May 21, 2015, FMPA's Executive Committee approved issuing a Request for Qualifications (RFQ) to retain an independent management consulting firm to provide analysis and recommendations on defining the terms "additional benefits" and "excess amounts" as it relates to the withdrawal payment calculation. Responses to the RFQ were received on June 26. Interviews with respondents are planned on July 30. FMPA anticipates making a consultant selection by mid-August and having a contract executed with the consultant by mid-September. If those deadlines are met, the consultant is expected to present its initial results to FMPA's Executive Committee in November 2015, and FMPA will begin addressing the consultant's recommendations at that time.

FINDING 15: Disaster Recovery Plan

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

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

FMPA Status Report: Following the preliminary and tentative findings issued by the Auditor General on Jan. 21, 2015, FMPA immediately reviewed its relationship with the current alternate processing site. At that time, the agreement for FMPA's alternate data processing site had a March 1, 2015, expiration date. FMPA worked with the incumbent provider to renew the contract for one year, rather than the standard five-year term, and included in the renewed contract a no-cost option of moving FMPA's backup computer equipment and systems from the provider's current location in Orlando, Florida, to one of its other locations in Atlanta, Georgia, or Boise, Idaho. FMPA is currently evaluating additional options for its backup data processing needs. Working with FMPA's governing boards, FMPA staff expects to have a final resolution to this recommendation in August 2015.