



Guam Power Authority FY 2012 Financial Highlights

April 11, 2013

The Guam Power Authority (GPA) closed fiscal year (FY) 2012 with a \$2 million (M) decrease in net assets, more than double FY 2011's \$1M decrease. GPA's consumer base continues to see growth despite of the decline in kilowatt hours (KWH) sales of 64M KWH or 4% below prior year levels. GPA ended the year with a decrease in gross margin of \$4M largely due to higher cost of fuel. The production cost of fuel increased by 18%, going from \$244M in FY 2011 to \$289M in 2012. The increase in production cost coupled with other operating and maintenance expense offset \$46M in sales growth. In October 2012, the U.S. Department of Energy designated GPA as a high-risk recipient due to a two year delay with the implementation of the Smart Grid Project funded with American Recovery Reinvestment Act (ARRA) Grant. GPA's delayed implementation was a result of issues of system wide change and organizational alignment.

Deloitte and Touche, LLP, rendered an unqualified or "clean" opinion on the financial statements, and reports issued for compliance for major programs; however, the auditors identified three significant deficiencies pertaining to procurement, general computer controls, and equipment and real property management. Additionally, a management letter identified 11 findings.

Increase in Sales of Electricity offset by Increased Fuel Production Cost

Due to the higher cost of fuel per KWH in FY 2012, all categories of GPA's electricity experienced an increase in sales. Total sales increased by 12% or \$46M. Sales to the U.S. Navy saw the most significant increase by 20%, or \$14M. Commercial sales increased by 12% or \$17M. GPA sales of electricity to residential customers and the Government of Guam (GovGuam) increased both by 9% or \$10M and \$5M, respectively. While there is an increase in sales of electricity, actual KWH sales declined. GPA's fuel and other production cost increased by \$49M, from \$265M to \$314M over the prior year. Other operating and maintenance expenses increased by \$5M, from \$92M to \$97M. GPA's operating and maintenance expenses have steadily increased by 21% over the last six years from \$80M in FY 2006 to \$97M in FY 2012.

Other notable increases in expenses stemmed from depreciation and amortization by \$3M, general administrative expenses by \$946 thousand (K), and transmission and distribution by \$476K. Overall, GPA recorded operating earnings totaling \$28M a decrease of 23%, or \$9M compared to operating earnings of \$37M in FY 2011. After interest expense of \$45M and other expenses totaling \$299K, GPA closed the year with a net decrease in net assets of \$2M.

Impact of Rising Cost of Fuel

GPA's energy is provided solely by fossils fuels, leaving them vulnerable to the increasing and volatile fuel prices. Cost of production of fuel represents 70%, or \$289M of total expenses in FY 2012. The increasingly volatile world-wide market on fuel has had a negative impact on GPA customers and on budgets for families and businesses throughout the island. Although GPA's residential customer base grew from 37K in FY 2005 to over 41K in FY 2011, the overall power consumption declined by 64M KWH, or 4% from 1.62 billion (B) KWH to 1.55B KWH during the

year. GPA's KWH sales have not been able to exceed its FY 2006 sales totaling 1.67B in any of the last five years as all of GPA's customer classes have taken significant actions to improve efficiency and monitor power usage. Actions taken by customers that contribute to preserving natural resources on a global level is in line with green energy initiatives.

Extension of Environmental Protection Agency Regulatory Actions

In FY 2012, the U.S. Environmental Protection Agency (USEPA) issued strict regulatory standards requiring an investment in excess of \$600M to bring GPA's baseload plants into compliance with the new regulations. In anticipation for the National Emissions Standards for hazardous air pollutants which take effect as early as May 2013, GPA is currently negotiating with USEPA for an extension for the installation of the equipment at some of its small diesel plants. GPA is also seeking a negotiated agreement wherein GPA would commit to pursuing liquefied natural gas facilities in lieu of complying with the regulations while it continues to operate its baseload plants using fuel oil.

Capital Improvement Program

GPA's capital improvement program consists largely of on-going improvements and upgrades to existing generating and transmission and distribution facilities, extension of transmission lines and the construction of associated substations, and the addition of Smart Grid technologies. GPA has projects of approximately \$280M that will be funded through FY 2016. Other projects funded from the 2010 bonds include the construction of a consolidated office complex to house both GPA and the Guam Waterworks Authority (GWA) estimated at \$35M. GPA is more than 50% completed with the installation of smart meters, whose total project cost is \$33.2M which should be completed by the summer of 2013.

Three Significant Deficiencies Identified

The auditors rendered an unqualified opinion on internal control and compliance, but identified three significant deficiencies. One significant deficiency pertained to the procurement of services on two major ARRA programs related to the GovGuam Buildings Retrofit totaling \$8M from the Retrofit Government-Owned Street Lights of \$2M. GPA was noncompliant with procurement regulations for ARRA federal awards subgranted by the Guam Energy Office (GEO). GPA utilized two existing vendors working on nonfederal projects rather than following competitive procurement practices. Although GEO concurred with GPA's procurement actions, documentation supporting such activities was not evident in GPA's procurement files. Other deficiencies identified in the report on internal control and compliance included:

- General Computer Controls: This is a prior year audit finding for GPA's general computer controls system. GPA's system allows user access rights that enable them to "delete and/or update" meter readings and billing information.
- Equipment and Real Property Management: GPA has not performed the required comprehensive physical inventories of its property and equipment in FY 2012 or in the two prior years. Thus, the auditors were not able to assess the overall cumulative monetary value of this deficiency.

Management Letter Comments

A management letter reported eight findings, of which one was indentified in the prior year. These findings included:

- Electricity Sales: reconciliations between the PayPal and merchant accounts are not being performed. Further, electricity accounts tested included errors related to reclassifications, undercharged late fees, and overcharges.
- Cancellation and Rebills: One of five customer accounts tested was subject to multiple cancellations due to improper termination of the account.
- Allowance for Doubtful Accounts: GPA has long outstanding balances from Department of Public Works and GWA totaling \$390K and \$216K, respectively. Both balances are in dispute.
- Utility Plant Account: One item under the general plant account was obsolete and no longer supported. However, this item was not fully depreciated in the plant asset ledger.
- Water and Sewer Billings: GPA paid GWA for water and sewer charges handled through the navy, but at an incorrect rate. As a result, GPA recorded a payable to GWA.
- Bid Deposits: Bid deposits totaling \$111K remain outstanding. GPA does not have a policy for recognizing unclaimed bid deposits; therefore, the amount remains as a liability.
- Customer Deposits: These include improper credits, improper refunds to customer accounts and negative balances.
- Annual Leave: Monitoring of leave is still being completed through the use of manual records and Excel spreadsheets.

A separate section in the management letter concerning three other matters involved GPA's liquidated damages, and defective fuel auto gauges.

For more details, refer to the Management Discussion and Analysis in the audit report at www.guamopa.org and at www.guampowerauthority.com.