Guam Power Authority
FY 2009 Financial Highlights

April 2, 2010

For Fiscal Year (FY) 2009, the Guam Power Authority (GPA) reported a $14 million (M) loss compared to a $10.4M gain in FY 2008. This loss was attributed to a combination of lower power consumption, higher fuel costs, increased capital costs, and increased operating expenses.

Deloitte and Touche, LLP, rendered an unqualified or "clean" opinion on the financial statements; however, four findings were identified in the Compliance and Internal Control report, one of which has been a material weakness since prior to 2002. A separate Management Letter was issued identifying 19 findings, of which 13 were repeat conditions.

Effects of Rising Oil Prices

GPA's customer base grew by nearly 2% during FY 2009, but kilowatt sales declined as many customers, with the exception of the military, conserved power use. The Navy's power consumption increased by more than 5%, but consumption declined among nearly all other customer classes. Although GPA's revenues appear to have increased by $18.3M, from $370.6M to $388.9M, the increase actually reflects the rising cost of fuel recovered through the Levelized Energy Adjustment Clause (LEAC)[1], and not increased kilowatt usage. The LEAC is adjusted as fuel prices fluctuate. Fuel prices soared from a low of $65 per barrel in 2008 to a high of $110 per barrel in 2009. Correspondingly, production expenses rose by $21.9M, from $257.1M to $279M. As of September 30, 2009, GPA's unrecovered fuel costs amounted to $6.9M, as opposed to the $4.6M over recovered in FY 2008.

In October 2007, GPA filed a petition to implement a two-phased adjustment of the base rate. The first phase, a 3.4% relief, went into effect in March 2008 and was amended in November 2009. The second phase, a 2.8% relief, went into effect in March 2010.

Operating and Maintenance Expenses

GPA's fuel and other production costs increased over the prior year by $21.9M, of which $17.3M can be attributed to increased fuel costs. Other production costs increased by $4.5M from FY 2008 to FY 2009 due to catch-up maintenance on two system overhauls.

In addition to the increase in fuel expenses, all other operating and maintenance expenses increased by $3.4M, from $84.5M to $87.8M. Specifically, administrative and general expenses increased by $1.5M ($25.2M to $26.7M); transmission and distribution expenses increased by $857 thousand (K) ($10.3M to $11.1M); and energy conversion costs increased by $298K ($18.9M to $19.2M).

[1] An adjustable rate approved by the Public Utilities Commission on a bi-annual basis.

Among the reasons for the rise in operating expenses was due to the implementation of GPA's Certified, Technical, and Professional Compensation Plan, which initially cost $3M to implement in January 2008. A second adjustment was made in January 2009 to bring GPA to the high 10^{th} percentile/low 15^{th} percentile, which cost an additional $2.1M to implement. As of September 30, 2009, GPA personnel numbered 534, up from 525 in FY 2008, and had an overall increase of $1.3M in salaries and wages, from $28.8M to $30.1M.

Elimination of Unfunded Liability

In December 2009, the Department of Administration redesignated the Defined Benefit Plan from a single-employer plan to a cost-sharing multiple-employer plan, pursuant to the Government Accounting Standards Board Statement No. 27. As a multiple-employer retirement plan, the unfunded liability would no longer be recorded as a liability. GPA wrote off $10.7M as a prior period adjustment as a result of this measure, which correspondingly increased FY 2008 beginning net assets.

Default of Loan

In March 2009, GPA converted a $20M short-term note to a three-year loan to remedy a default action in November 2008. Principal payments were $5M with an interest rate at the bank's prime rate plus 2% and a floor of 6.5%. This loan was secured by a pledge of revenues subordinate to the revenue pledge under the 1993 and 1999 Bond Series indentures and a $5M deposit in a collateral account. In April 2009, GPA received a second Notice of Default due to the downgrade of their bond insurer's credit rating. The default allows the bank to charge 15% interest on the balance of the loan. However, GPA entered into a temporary rate modification agreement with the bank and will pay the bank's prime rate plus 5% (but no lower than 6.5%) or 8.25% at September 30, 2009. GPA has deposited an additional $3M with the bank as security for the agreement.

Report on Compliance and Management Letter

Four significant deficiencies[2] were identified in the Report on Compliance and Internal Control, of which two were material weaknesses. One material weakness, identified prior to FY 2002, pertains to GPA's inability to maintain detailed cost records of $166M for its property, plant, and equipment. GPA embarked on a plan to reconcile the books in FY 2010. The second material weakness dealt with the failure to regularly assess materials and inventories for obsolescence and usability. The two remaining findings involved:

- Plant and Equipment being depreciated over extended useful lives; and
- Discrepancies in fuel inventory reports between the generation and accounting departments.

The management letter reported 19 findings, of which 13 were repeat findings from FY 2008, including the lack of control over information technology activities, monitoring of fixed assets and maintenance registrar, monitoring of temporary streetlights, reconciliation of claims and collection reports with accounting reports, and defective fuel gauges used to record fuel consumption and issuance. The six new findings included:

- Lack of control over network activities,
- Incorrect late charges assessed,

2 A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects GPA's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles.

- Customer deposit accounts not regularly reviewed,
- Exception reports not designed to facilitate effective and efficient investigations and corrections of actual usage exceptions,
- Lack of review over accounts registering low consumption, and
- Not activating a more stringent security setting in their AS400 system as recommended by best practices.

A separate document to the Consolidated Commission on Utilities was issued by the auditors outlining audit strategies, emphasis, required communications, audit differences, and adjustments. For more details, refer to the Management Discussion and Analysis in the audit report at www.guamopa.org and at www.guampowerauthority.com.