OFFICE OF THE PUBLIC AUDITOR

GUAM POWER AUTHORITY

FY 2006 Financial Highlights

May 01, 2007

After posting a positive net assets last year, the Guam Power Authority (GPA) posted a loss of $1,745,169 for fiscal year 2006. This loss is lower than the previous years' losses: $23.9 million in 2003 and $9.2 million in 2004.

Although revenues are up by $42 million from $247.3 million in 2005 to $289.3 million in 2006, it is primarily due to the increase in the Levelized Energy Adjustment Clause (LEAC),[1] an adjustable rate that allows GPA to recover its fuel costs, approved by the Public Utilities Commission (PUC). Fuel prices have been surging in the last few years, and per barrel price has increased from $36.55 in 2005 to $52.45 in 2006.

Compared to other islands, GPA's residential rate of 17.86 cents/Kilowatt hour (KWh), as of February 2007, is relatively low. Other island rates are as follows: Commonwealth of the Northern Marianas Islands at 31.00 cents/KWh; and the Hawaiian Islands ranging from 20.60 cents/KWh to 24.10 cents/KWh. The cost to Guam consumers is lower than those of the other islands' due to the high rate of generation of GPA's baseload units, and because many of GPA's plants burn sulfur oil rather than diesel. However, compared to the mainland United States', such as San Diego Gas and Electric's 16.60 cents/KWh and Southern California Edison's 12.95 cents/KWh, Guam's rates are relatively higher. The comparison is not parallel, however, because Guam is dependent on fossil fuel as its source of energy, while the states have alternative energy sources such as hydroelectricity, gas, coal, wind, and have greater economies of scale.

Other revenue sources, such as fees charged for reconnections and service establishments, decreased by $402,399 from $2.1 million in 2005 to $1.7 million in 2006. Additionally, GPA incurred $885,242 in bad debt expense in 2006 as opposed to the $278,627 recovery in 2005.

While total revenues appear to have increased in 2006, total operating and maintenance expenses also increased. Total production expenses increased by 33% in 2006 largely due to a $44.4 million increase in production fuel expenses. Operating margin, revenues minus production expenses, declined by $1.7 million in 2006. Non-production costs, such as administration, transmission and distribution, energy conversion, and customer accounting increased by $1.5 million from $78.2 million in 2005 to $79.7 million in 2006. Operating earnings, total revenues minus total operating and maintenance expenses, decreased by $3.2 million from $37.0 million in 2005 to $33.8 million in 2006. Interest, Cost of Living Allowances (COLA) / supplemental annuities, and various others expenses nominally decreased from $37.8 million in 2005 to $37.7 million in 2006.

GPA received $2.1 million in Federal Emergency Management Agency (FEMA) Grants, which helped offset its $1.7 million operating loss in 2006.

As of September 30, 2006, GPA maintains $34.7 million in receivables from government of Guam agencies. A breakdown follows: $13.2 million from the Guam Public School System (GPSS); $10.9

[1] Reviewed and adjusted by the PUC on a bi-annual basis.

million from the Department of Public Works (DPW) for streetlights; $9.8 million from the Guam Waterworks Authority (GWA);[2] and $759,724 from the Guam Memorial Hospital Authority (GMHA).

For the last several years, the independent auditors have, in their audit opinion, expressed significant uncertainty of the collectability of the $30 million[3] in receivables from the various government of Guam agencies, whose payments are dependent on appropriations from the General Fund or the government of Guam's issuance of bonds or like financial instruments. In March 2007, Standards & Poors rating agency placed the government of Guam on a credit watch with negative implications and indicated that the government has a "liquidity crisis."

The $14 million DPW note and accounts receivable is mainly for power service to public streetlights from 1999 to 2003; DPW has not made any payments on the note receivable and has approximately $3 million in unpaid accounts receivables. GPA's bond covenants require that "electric power not be provided to any entity free of charge." To date, the DPW receivables "are significantly delinquent" and questions as to the legality of the note have risen. For the first time, the independent auditors identified the DPW receivables as a material weakness, because it has constrained cash flow and GPA has been required to borrow on the commercial paper market to make up for the shortfall.

The Independent Auditors' Reports on Compliance and On Internal Control identified nine findings, equal to the number of findings in 2005. Of the nine, two are material weaknesses and four are repeat findings. One material weakness is the absence of detailed property, plant and equipment listings or subsidiary ledgers for its production, transmission, and distribution plants. GPA does not have detailed accounting information, such as original costs and related improvements, for $598 million of its $810 million in capital assets. GPA is one of the few utilities in the country not to have a detailed accounting of its capital assets. The other material weakness is the collectability of the previously discussed DPW note receivables.

In 2006, GPA implemented a new billing system, the Utiligy. During the conversion, problems with various accounts, such as revenues, customer accounts, receivables, and aging were encountered. Report-generation was also affected. A finding indicated that GPA's trade account receivables were not being properly aged, because balances uploaded into Utiligy from the old system defaulted to "current" aged category. These issues caused delays in the audit.

Other findings include discrepancies between fuel inventory consumption based on the generation reports and accounting department volume, and a $2 million annual conversion of receivables into inactive accounts. As of September 30, 2006, total inactive accounts amounted to $19.7 million.

OPA received a Hotline tip concerning the amounts expended at Consolidated Commission on Utilities (CCU)[4] meetings. The CCU Board is the only paid Board in the government of Guam where members are provided with a monthly stipend of $1,000, equally paid for by GPA and GWA. GPA expenditures for board meetings were $3,163 in 2005 and $4,448 in 2006.

For a detailed commentary of GPA's operations, see the Management Discussion and Analysis portion of the audit report.

[2] The GWA receivable is being paid for by an 11.5% water surcharge.
[3] $34.7 million less current portion of $4.9 million.
[4] The governing body for GPA and GWA.