



MIAMIBEACH

BUDGET AND PERFORMANCE IMPROVEMENT
Internal Audit Division

INTERNAL AUDIT REPORT

TO: Jorge M. Gonzalez, City Manager
VIA: Kathie G. Brooks, Budget and Performance Improvement Director 
FROM: James J. Sutter, Internal Auditor 

DATE: July 30, 2010
AUDIT: Electric Franchise Fees and Utility Taxes Audit (Florida Power & Light Company)
PERIOD: October 1, 2005 through September 30, 2008

This report is the result of a regularly scheduled audit of the revenues derived from franchise fees and utility taxes paid to the City's Finance Department by the Florida Power & Light Company during the specified audit period of October 1, 2005 through September 30, 2008.

INTRODUCTION

FPL Group's two principal subsidiaries are the Florida Power & Light Company (FP&L), the largest investor-owned electric utility in Florida which is the focus of this audit, and NextEra Energy Resources, a leader in producing energy from clean and renewable fuels.

The City Commission through the ratification of Ordinance No. 82-2294 granted Florida Power & Light Company a non-exclusive thirty year franchise to construct, maintain and operate electric light and power facilities in the City. The utility signed an Acceptance of Electric Franchise agreeing to the terms of Ordinance 82-2294. Among other terms of the ordinance valid through January 22, 2012, the contractor is required to pay the City franchise fees equaling 6% of their monthly gross billings; the City is given the right to examine the grantee's books and records; etc.

Meanwhile, City Code Article III (Public Service Tax) Sections 102-151 through 102-158 details the remittance of utility taxes on every purchase in the City of electricity, metered gas, bottled gas and fuel oil. This utility tax of ten percent for electric purchases is to be remitted by the twentieth day of the following month or late charges shall be levied. Other items addressed in the City Code include the need to maintain specific records, the remittance of reports to the City and the depositing of monies received into the City's general operating account.

The Finance Department receives the franchise fee and utility tax payments from FP&L monthly through wire transfers directly to the City's SunTrust bank account. A copy of the returns showing the origin of the payment and the corresponding calculations is provided. The franchise fee and utility tax payments received are entered into the City's general ledger accounts numbered 011-8000-313100 and 011-8000-314100 respectively by journal entry each month.

The City received the following revenues in electricity for franchise fees and utility taxes during the audit period:

	FY 2005/06	FY 2006/07	FY 2007/08	Total
Electric Franchise Fees	\$7,448,932	\$8,169,741	\$8,218,820	\$23,837,493
Electric Utility Taxes	\$7,704,683	\$7,718,812	\$7,930,859	\$23,354,354
Total Remitted Revenues	\$15,153,615	\$15,888,553	\$16,149,679	\$47,191,847

OVERALL OPINION

FPL Group, the parent company of Florida Power & Light Company (FP&L), is a large company with main offices in Juno Beach and Miami, FL whose internal control system complies with the Sarbanes Oxley Act of 2002. Therefore, Internal Audit documented the internal control process but did not perform testing to determine its effectiveness.

Instead, much of our testing focused on the review of requested electronic system generated reports, as well as sampling some individual accounts and monthly billing rates on the company's database. The results were subsequently reconciled with the monthly documents and payments previously submitted to the City. The following findings were identified that are in need of corrective action:

- FP&L's methodology for billing franchise taxes resulted in its Miami Beach customers being billed in excess of 6%. Additionally, this includes the billing and collecting but not remitting of franchise fees on two categories not included in the franchise agreement. If included, the financial impact would have resulted in FP&L remitting an additional amount of \$173,629.74 for the 2006, 2007 and 2008 full calendar years.
- The City did not furnish FP&L with periodic updated address listings in compliance with Florida Statute 166.233(3) so that the accuracy of the designated city codes could be tested. When this analysis was completed in March 2009, seventeen North Bay Village addresses were incorrectly paid to Miami Beach and three hundred Miami Beach addresses were identified that apparently were not being paid to the City. FP&L was forwarded this list whereby they claimed that all addresses were properly reported. Their supporting documentation was given to the City's G.I.S. Manager for review on 02/05/10 and Internal Audit will monitor the analysis to help ensure that the City's and FP&L's listings are in agreement.
- In an effort to renew their agreement with the City, FP&L staff mentioned some possible amendments beneficial to the City during field testing whose financial impact is estimated. Two additional options not discussed are also listed that should be considered if City Administration opt to begin negotiations with FP&L.

PURPOSE

The purpose of this audit is to determine whether compliance existed with selected provisions in the signed agreement (Ordinance No. 82-2294) and City Code Article III Section 102 for Public Service Tax; which includes testing for inadvertently omitted Miami Beach addresses; determining that correct fees are charged, collected, remitted and recorded in the City's Financial System; and whether delinquencies are effectively and timely pursued.

OBJECTIVES

1. Confirm by examination of the contractor's records that remitted franchise fee and utility tax payments were accurately calculated in accordance with the signed agreement and City Code.
2. Confirm that monthly franchise fee and utility tax returns were received timely. If not, were interest and/or penalties levied accordingly.

3. Confirm that the Finance Department reviews the received returns for accuracy and correctly enters the payments into the City's Financial System.
4. Confirm that the signed agreement and City Code are in agreement with the Florida Statutes.

FINDINGS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

1. Finding: *Amounts billed to customers and inclusion of two other categories in collection of franchise fees*

Internal Audit determined that FP&L annually billed the City's electrical customers (in combination with the property taxes, licenses and permits taken) in excess of 6% for the 2006, 2007 and 2008 full calendar years although they remitted only 6% to the City. The reasons for this excess are the following:

- The franchise agreement is silent on the percentage rate that can be billed;
- The Florida Public Service Commission or FPSC has authorized FP&L to pass through all collected franchise fee monies to the applicable governing bodies;
- The franchise fees component includes approximately 2.5% in state gross receipt taxes and .72% in a regulatory assessment fee used to fund the FPSC's operations;
- The billed franchise fee percentage rate is adjusted as needed so that the collected amounts approximate the 6% remitted amounts.

FP&L provided sufficient supporting documentation to confirm these statements accuracy whereby it was found that FP&L had cumulatively remitted \$104,604.91 more than they had collected from the City's electrical customers through 12/31/09. This under collected amount has been decreasing continually since FP&L last raised the billed franchise fee percentage rate in August/September 2009. The FPSC scrutinizes FP&L's over/under cost recovery during the year to ensure that it does not get too far out of balance.

However, it was determined that FP&L charged the same variable franchise fee percentage rate during the audit period to five different categories of Miami Beach users but only remitted monies to the City based on 6% of the following three categories' reported billings: residential, commercial and industrial in accordance to the franchise agreement. These other two categories that are not addressed in the franchise agreement are called public street & highway lighting and other sales to public authorities (represents electric sales to municipal ball parks, sports fields, etc.) but authorized by the FPSC.

The associated franchise fees collected from these other two categories are remitted to the City to help offset any uncollectible accounts from residential, industrial and commercial billings. Furthermore, the City pays much of these two categories' invoices and associated franchise fees thereby in effect subsidizing the Miami Beach residential, industrial and commercial customers by helping keep the franchise fee rates slightly lower than they would normally be.

Internal Audit subsequently requested and obtained the values for these two unreported categories for the tested period from FP&L. These monthly values were then multiplied by the corresponding billed franchise fee percentage to determine the amount of franchise fees collected for each month. As a result, the amount of franchise fees originating from the omission of the public street & highway lighting and other sales to public authorities

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categories equaled \$173,629.74 for the full 2006, 2007 and 2008 calendar years.

Recommendation(s):

The City should specify in future franchise agreements that FP&L only bill and collect franchise fees from those listed categories specified in the agreement. If FP&L continues to bill Miami Beach electrical customers franchise fees on the two aforementioned categories or any others, then these categories should be included in the franchise agreement.

FP&L Response:

FPL does not agree with City's recommendation of specifying in future agreements that FPL should bill specific classes of customers whose revenue base is used to calculate the franchise payment. FPL collects a franchise charge on all bills sent to retail customers receiving service within the City of Miami Beach. This includes not only the Commercial, Industrial and Residential accounts, but also the Public Street and Highway Lighting accounts. This procedure was instituted many years ago following a series of rulings by the Florida Public Service Commission and the courts of this state.

From these collections, FPL accurately calculates and remits to the City franchise fees that equal 6% of revenues from Residential, Commercial and Industrial accounts after the enumerated adjustments have been made. FPL also pays from these funds the required gross receipts taxes and regulatory assessments. Finally, FPL analyzes and compares the amounts received by FPL from retail customers to the amounts remitted to the City under the franchise agreement, and based upon this comparison and analysis, the billing factor is adjusted accordingly. The billing factor is then applied to the bills of all retail customers and reviewed and adjusted as necessary.

City Response:

The City will endeavor to clarify the FPL practice in the upcoming renegotiation of the franchise.

2. Finding: Address Listings

Florida Statute 166.233(3) requires municipalities to furnish FP&L with an updated listing of all their addresses as changes occur. Each update shall specify an effective date which should be the next ensuing quarter. FP&L compares any data received to their database to help ensure that accounts are properly coded so that the correct amount of franchise fees and utility taxes are remitted to the appropriate governmental units. Otherwise, electric customer accounts set-up incorrectly for whatever reason (input errors, erroneous service addresses given by the customer, etc.) will most likely go undetected thereby resulting in either under or overpayments for the affected governmental units.

Errors occurring during the creation or set-up of accounts represent FP&L's main exposure for incorrect franchise fee and utility tax payments as they assume that the data entered is correct. Numerous individuals (FP&L internal auditors, external auditors, Federal regulators, etc.) review the subsequent billings, collections and FP&L payments to help ensure their accuracy.

Testing showed that the last address listing submitted by the City of Miami Beach was in March 2008. Furthermore, the 3.5" diskette provided by the City was incomplete as it did not list each individual address/location but only a range for each street. Therefore, this listing was beneficial to FP&L primarily to search for any outliers or addresses not between the

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beginning and ending addresses and did not fully satisfy the Florida Statute.

A comparison of addresses was conducted during the audit and found the following:

- a. Internal Audit's review of the address listing provided by FP&L revealed that seventeen different units located at 7930 East Drive in North Bay Village were incorrectly included in Miami Beach's franchise fee and utility tax payments. These accounts only opened in October 2008 so the financial impact was nominal to the City.
- b. The City's G.I.S. Manager compared FP&L's address listing to the City's database and identified 300 parcels having a structure on them that apparently did not appear on the list received from FP&L. These differences were sent via e-mail on 11/20/09 to FP&L for review. They presented their analysis at a 01/22/10 meeting which showed that the City was properly receiving payment on these 300 parcels. They claimed that the discovered differences were due primarily to address differences resulting from structures located on the corners of two cross streets, second meters associated with a property for a boat, pool, etc. The results of their analysis were forwarded to the City's G.I.S. Manager on 02/05/10 for his review and comments but nothing has been received to date.

Rather than delay this audit until a consensus is reached on these 300 parcels, it was decided to complete the audit with the information at hand. Internal Audit will monitor the progress with this list so that any subsequently agreed upon miscodings are corrected and the City compensated accordingly.

Recommendation(s):

The City should comply with Florida Statute 166.233(3) and furnish periodic updates of address listings to FP&L. Furthermore, the City's G.I.S. Manager and FP&L need to complete their review of the differences between listings so that a consensus can be reached as to any existing miscodings.

FP&L Response:

FPL received 299 address exceptions from the City of Miami Beach. FPL researched and found only one true exception. This address located at 1015 Fairway Dr was not in FPL records. In March 2010, this account was activated and customer was back billed for one year. Total revenue subject to franchise is \$1,478.64, and the franchise fee that will be paid to the City is \$88.72. This will be paid with March 2010 revenues.

Below is a summary of other 298 exceptions identified by the City:

- 18 addresses were included in the original list provided to the City, thus no exceptions found.
- 39 addresses were not included in the original list provided to the City due to delimiters. Delimiters in FPL records represent additional meters for the same physical address, such as a customer has multiple meters for one account, one meter for the house and a separate one for the pool pump. These records were not originally provided to avoid duplication of addresses. These records were reviewed and they were all coded as Miami Beach. FPL implemented a process change to include them in future audits to avoid exceptions.

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- 90 addresses had listing discrepancies between FPL and Miami Beach. Properties in question were the same in both FPL and City's systems. Addresses were reviewed and were all coded as Miami Beach. FPL records were updated when applicable to match City's records to avoid future exceptions.
- 25 addresses were not included in the original address list as FPL has no meters, i.e. these were vacant lots, parking lots etc...
- 126 addresses had folios that did not match addresses FPL provided to the City. After further review these group of addresses matched the folio information in the Property appraiser's website and matched FPL records. They were all coded as Miami Beach, thus no exceptions found.

City Response:

Florida Power and Light Company, in a letter dated February 15, 2008, requested the City to send according Section 166.231 - 234 of the Florida Statutes a list of addresses located within the boundaries of the City of Miami Beach. This letter contained a description of the format of the address data requested in a street range format and not in individual address/location as stated in the findings. The City's GIS Manager sent on March 27, 2008 the requested listing on a 3.5" diskette to FP&L which did not response to this delivery and did not inform the City's GIS Manager that this delivery did not meet the expectations.

On February 26, 2009 the City's GIS Manager received a request from the Internal Audit to compare a list of accounts with know addresses within the city limits of the City of Miami Beach. The City's GIS Manager used to following process to investigate the addresses in the provided listing:

- Geocoded all active accounts in this file. Five (5) accounts could not be located and do not exist in The City of Miami Beach:
 - 0 JULIA TUTTLE CSWY
 - 1901 VENETIAN WAY
 - 2663 S LAGUNA PATH
 - 2800 N MERIDIAN AVE
 - 4000 JULIA TUTTLE CSWY
- Compared the active accounts with the city name "MIAMI BEACH" with the GIS Address database.
- Created a listing of addresses within parcel with improvements and no active Florida and Power Account.
- Special attention was given to a group of addresses on Pine Tree Dr Cir. None of these addresses are in the FPL Account List and a map was submitted for review of this addresses. No response was received about this map and addresses.

The review was completed on March 12, 2009 with the following result:

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Description	Amount	Note
Total Accounts	68882	
Accounts not in Miami Beach	19	
Accounts in North Bay Village	18	
Accounts in Surf Side	1	Should be MB Account
Active Accounts in MB	59830	
Located Active Accounts in MB	59825	
Not Located Active Accounts in MB	5	
Inactive Accounts	6764	
Removed Accounts	2269	
Addresses within Parcels with Improvement not on FLP Account List	299	Delivered in spreadsheet

On April 27, 2009 Florida Power and Light requested the Parcel ID (Folio) for the exception listing. The listing was submitted on November 20, 2009. A response was received on February 10, 2010 without any request for further investigation. On July 9, 2010 the Public Works Director requested the City's GIS Manager to review the exception listing and the responses from Florida Power and Light.

The result of this review is as follows:

- **Vacant Lots**
 Only 15 parcels instead of 25 could be identified in the supplied list as vacant lots. The City's GIS Manager agrees to this designation on 9 parcels and disagrees on 6 parcels.
- The remaining exceptions mentioned in the response from Florida Power and Light could not be identified in the supplied listing as categories.
 The City's GIS Manager cannot judge why an address is not on the list. The City's GIS Manager has since the original review in March 2009 updated and added many addresses to the City Addressing System.
 Based on new review done on July 28 and 29, 2010 the City's GIS Manager identified 147 parcels which should not have been on the exception list.
 However 137 parcels are not on the account list provide by Florida Light and Power to the City's GIS Manager although these parcels have valid addresses and improvements (see attached spread sheet for details). Part of these 37 parcels are the parcels on Pine Tree Dr Cir.

Internal Audit Observation

While it appears that the City's recent review of addresses is now current, the City should continue to coordinate with FP&L the clearing of any exceptions and provide listings periodically as changes occur in compliance with Section 166.233 (3).

3. Finding: Possible Agreement Negotiated Changes
 FP&L senior staff approached Internal Audit during testing to state that their company is receptive to renegotiating the City contract which currently expires on 01/22/12. One favorable term available to the City that could be included in a new agreement is the removal of the deduction for the municipal portion of property taxes in return for a decrease in the franchise fee rate from 6% to 5.9%. If implemented, Internal Audit calculated that the City would have retained an additional \$826,648.64 and \$796,624.75 in franchise fees for the 2006 and 2007 calendar years respectively.

Another possible option discussed is to institute a thirty day lag in remitting franchise fee monies rather than the current ninety days listed in Ordinance 82-2294. As a result, the City should receive two additional months' franchise fee and utility tax payments at the time of transition. The average franchise fee monthly payment was \$604,337.00 during the audit period while the average utility tax payment was \$648,732.06. Therefore, reducing the lag to thirty days would result in approximately \$2,526,138.12 $(\$604,337.00 + \$648,732.06) \times 2$ in additional revenues being received by the City during the fiscal year enacted.

The following options were not mentioned by FP&L staff but should be included in the re-negotiated agreement's terms:

- Eliminate the true-up provision at the end of the twelve month reporting period (December) and instead have FP&L remit 6% franchise fees each month on 100% of their billings. This practice will enable the City to receive all the monies due quicker thereby increasing their opportunities to earn interest, invest the monies, etc.

Presently, FP&L complies with Section 7 of Ordinance No. 82-2294 by remitting franchise fees on 90% of their monthly billings (January through November) with franchise fees being paid on the remaining 10% for these months in December. This true-up payment was correctly calculated and properly included with FP&L's remittance of 6% franchise fees on 100% of the December billings during the audit period.

- Specifically list which FP&L categories are excluded from the 6% franchise fee rate rather than those that are included (residential, commercial and industrial) as done in the current agreement. FP&L should charge anyone that falls in these three categories the franchise fee rate and all others should be exempted.

Recommendation(s):

The City Administration should decide whether to re-negotiate with FP&L prior to the end of the current thirty year contract in an effort to obtain more favorable terms, eliminate confusion over contract language and increase revenues.

City Response:

Agree with the recommendation.

EXIT CONFERENCE

An exit conference was held on 01/22/10 at FP&L's Miami offices. Participants included FP&L's Brunilda Hasko (Supervisor, Revenue Accounting) and Frank Soto (Billing Projects & Compliance Supervisor), as well as the City's James Sutter (Internal Auditor) and Mark Coolidge (Senior Auditor). Revisions were subsequently made to the audit report and another meeting was held via telephone on 02/08/10. The audit report was sent again to FP&L on 03/30/10 for their management responses which were solicited and included in our report.

In addition, several meetings were held with City personnel to discuss those issues requiring corrective action by staff. Their management responses were also solicited and are included in our

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report. Response for addresses listing analysis was received July 30, 2010.

JS:MC:mc
(Audit performed by Mark Coolidge, Senior Auditor)

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