



REVIEW OF
**Florida Public Utilities Company's
Storm Cost Management and
Payment Processing Practices
for Hurricane Michael**

July 2020

By Authority of
**The Florida Public Service Commission
Office of Auditing and Performance Analysis
Performance Analysis Section**

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1.0 Executive Summary

1.1 Purpose and Objectives

The Florida Public Service Commission's (FPSC or Commission) Office of Auditing and Performance Analysis initiated this operational audit at the request of the Commission's Division of Accounting and Finance. The purpose of the audit was to review and examine processes and internal controls in use by Florida Public Utilities Company (FPUC or Company). Commission audit staff assessed FPUC's compliance with its procedures and internal controls and their effectiveness in reviewing, processing, and paying invoices associated with Hurricane Michael.

The objectives of this audit were met by examining and assessing the adequacy of the processes for:

- ◆ Vendor storm cost invoice preparation and submission
- ◆ Review and approval of vendor storm cost invoices
- ◆ Invoice dispute, correction, and resolution
- ◆ Staffing and training of payment processing personnel
- ◆ Consistency of invoice with contract terms and conditions
- ◆ Overrides and exceptions to procedures and contract terms
- ◆ Operating systems supporting invoice payment processing
- ◆ Work planning and deployment of contractors and mutual assistance resources
- ◆ Oversight and work monitoring of contractors and mutual assistance resources
- ◆ Recordkeeping of contractor and mutual assistance work hours and costs
- ◆ Self-assessment and implementation of lessons learned

1.2 Scope and Methodology

The scope of the review focused on the processes by which FPUC incurred these costs, processed the resulting invoices, and paid vendors.

As authorized by Sections 350.117(2) and (3), Florida Statutes, management audits are conducted by staff to assess utility performance and the adequacy of operations and controls:

(2) The commission may perform management and operation audits of any regulated company. The commission may consider the results of such audits in establishing rates; however, the company shall not be denied due process as a result of the use of any such management or operation audit.

(3) As used in this section, "management and operation audit" means an appraisal, by a public accountant or other professional person, of management performance, including a testing of adherence to governing policy and profit capability; adequacy

of operating controls and operating procedures; and relations with employees, customers, the trade, and the public generally.

Commission audit staff's standard of review for internal controls is primarily the Institute of Internal Auditors' *Standards for the Professional Practice of Internal Auditing* and the *Internal Control - Integrated Framework* developed by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Internal controls assessments focus on the COSO framework's five key elements of internal control: control environment, risk assessment, control activities, information and communication, and monitoring. Commission audit staff's work is performed in compliance with Institute of Internal Auditors Performance Standards 2000 through 2500.

The information in this audit report was gathered through responses to document requests and on-site interviews with key employees responsible for processing, verifying, and approving invoices paid for Hurricane Michael. Specific information collected and reviewed from FPUC included:

- ◆ Policies and procedures used for procuring labor, services and materials, and the review and approval of storm cost invoices
- ◆ Governing documents under which Hurricane Michael storm costs were incurred (e.g., master service agreements, contracts, purchase orders, vendor guidelines, and instructions)
- ◆ Analysis of a sample of Hurricane Michael storm cost invoices, including all supporting documentation used for processing and paying contractor costs, logistics, materials, and fuel
- ◆ Internal and external reviews or audits performed to verify Hurricane Michael costs
- ◆ Documents filed in FPSC Docket Nos. 20190156-EI and 20180061-EI¹

1.3 Observations

Commission audit staff developed the following observations regarding FPUC's key areas of operations related to storm cost controls and payment.

1.3.1 Invoice Processing and Payment Procedures

Observation 1: Commission audit staff believes FPUC's invoice requirement procedure provided adequate direction, and that recent revisions to these policies and procedures further improved invoice review and payment processes.

¹ Docket No. 20180061-EI, *In re: Petition for limited proceeding to recover incremental storm restoration costs, by Florida Public Utilities Company.*

Observation 2: Commission audit staff believes FPUC’s invoice checking, correction, and approval processes were effective.

Observation 3: Commission audit staff believes FPUC provided adequate staffing and expertise for invoice and payment processing and oversight to provide acceptable accuracy and efficiency.

1.3.2 Contractor Deployment and Management

Observation 4: Commission audit staff notes that FPUC’s stated intention to avoid standby and minimum daily hour charges may reduce costs, but could also be advanced by executing contracts on more favorable terms prior to the storm season.

Observation 5: Commission audit staff believes that FPUC’s contractor work monitoring and recordkeeping policies and procedures require acceptable levels of oversight.

Observation 6: Commission audit staff believes FPUC’s planned implementation of closer controls over vendor costs may reduce meal and fueling costs.

Observation 7: FPUC indicated that it will continue to participate in the Southeastern Exchange (SEE) and Edison Electric Institute (EEI) Mutual Assistance Committee meetings.

1.3.3 Lessons-Learned Assessment and Implementation of Improvements

Observation 8: FPUC has agreed to implement several storm restoration cost process improvements that emerged as best practices in three recent Commission storm cost recovery dockets. Commission audit staff believes these improvements will enhance the Company’s ability to manage costs incurred in future storms.

2.0 Background and Perspective

2.1 Impacts of Hurricanes Michael and Dorian

Florida Public Utilities Company (FPUC), a subsidiary of Chesapeake Utilities Corporation, acquires electricity for approximately 32,000 customers through purchased power agreements. FPUC operates a Northeast Division in Nassau County and a Northwest Division in Calhoun, Jackson, and Liberty counties. In October 2018, Hurricane Michael severely impacted FPUC's Northwest Division, which serves 47 percent of FPUC's electric customers. The eye of the Hurricane crossed the entirety of FPUC's Northwest Division, resulting in major damage to not only to FPUC's electric system, but also to the homes and businesses of the Company's approximately 15,355 customers in the Northwest Division. The extensive damage required repairs to nearly 100 percent of the system, including a complete rebuild of approximately 10 to 12 percent of the Company's distribution system.

Less than a year later, Florida was faced with the impending threat of Hurricane Dorian. While FPUC's Northeast Division was spared a direct hit from this hurricane, it did experience tropical storm force winds, which resulted in outages for approximately 790 customers on Amelia Island. According to FPUC, the Company incurred incremental storm costs associated with its preparations for the storm, and the limited damage caused by the storm for which it seeks recovery. The Company believes the Hurricane Dorian-related costs are appropriate for inclusion in Docket No. 20190156-EI since the expenses for Hurricane Dorian occurred prior to hearing or a final decision, and including these costs in this limited proceeding docket would be administratively efficient.

2.2 Storm Settlement Agreement 2016-2017

In February 2018, in Docket No. 20180061-EI, FPUC filed a Petition for Limited Proceeding to recover costs incurred for Hurricane Hermine, Hurricane Matthew, Hurricane Irma, Tropical Storm Cindy, Tropical Storm Julia, and other un-named storms whose costs exceeded \$5,000. The Office of Public Counsel intervened in this docket on March 22, 2018. By Order No. PSC-2019-0114-FOF-EI, issued March 26, 2019, the Commission approved a storm recovery surcharge effective with the first billing cycle for April 2019 through the last billing cycle for March 2021 (two-year recovery period). The Commission found that the appropriate amount of prudently-incurred storm restoration costs for FPUC to recover was \$427,648, and the appropriate amount to replenish the level of FPUC's storm reserve to \$1.5 million was \$1,927,648.

2.3 FPUC Invoice Review and Payment Processes

FPUC follows Chesapeake Utilities Corporation's *Contractor Invoice Requirements and Approval Documentation* procedures for the processing, verification, and approval of contractor invoices. Contractors must provide invoices for work completed, and include specified information and

documentation, such as a description of completed work, labor charges supported by employee time sheets, vehicle and equipment charges, lodging, meals, and travel costs.

Invoices are received and initially reviewed by field Operations Management to ensure reasonableness, and are approved for further Accounts Payable processing. An Accounts Payable Analyst reviews invoices, the supporting documentation, and the Operations approval, and inputs the invoice information into FPUC's Doclink system for payment approval. Approval by managers within individual designated dollar limits then triggers final payment.

3.0 Commission Audit Staff Analysis

The overall focus of storm cost recovery dockets is to ensure that only prudently-incurred costs are reimbursed to utilities by customers. Of necessity, charges billed by vendors and contractors must be examined to ensure that the proper amounts were paid.

Commission audit staff notes that in addition to ensuring that invoices and payments were accurate, it is also important to ensure that the costs were incurred under appropriate oversight and controls provided by the utility. A systemic lack of effective contractor management can inflate costs well beyond the impact of even numerous smaller invoicing or payment processing errors.

At the same time, during storm recovery efforts, Commission audit staff recognizes the tension between the utility's urgent need to efficiently marshal resources while simultaneously prioritizing rapid restoration of service to customers. It is unavoidable that these two needs compete, posing difficult choices for Florida's investor-owned utilities.

Commission audit staff believes process improvements identified in prior cost recovery dockets for 2017 and 2018 storms have focused on contractor and work management issues more than on the actual invoice payment processes. In any event, the cumulative impact of lessons learned, agreements to implement Storm Restoration Cost Process Improvements to control costs, and creative initiatives by the utilities should yield substantial benefits in mitigating the cost impacts of future storms. By addressing these issues, the Commission and Florida utilities are appropriately rethinking embedded industry practices to the benefit of ratepayers.

3.1 Review of Invoicing and Contractor Management Controls

Commission audit staff closely reviewed the records of Docket No. 20180061-EI, as well as other recent storm cost recovery cases. This allowed the audit team to develop perspective on utility practices and the issues that arise regarding storm costs.

Audit staff issued numerous data requests to obtain information regarding FPUC's Hurricane Michael restoration work management and invoice processing practices. These requests yielded copies of written procedures, descriptions of process internal controls, copies of paid invoices, and associated supporting documentation.

On-site interviews with key FPUC management personnel were used to document how the restoration work and associated storm recovery costs were managed. This provided a foundational understanding of how costs were incurred, how vendors' work was tracked, and how payment processing was executed. Audit staff gathered information on Company post-mortem analysis and lessons-learned, and documented FPUC's process improvements either implemented to date, or under consideration for future implementation.

Throughout the review, Commission audit staff sought to identify differences between practices employed during Hurricanes Irma and Matthew in 2017 and those in use during 2018 for

restoration work following Hurricanes Michael and Dorian. Data requests and teleconferences with Company personnel and consultants continued as Commission audit staff completed detailed examination of invoices and Company documentation.

3.2 Invoice Sample Review

To observe and verify the processes and controls described by the Company in interviews and data request responses, Commission audit staff used a sampling approach. This detailed examination of vendor invoices included the following tasks:

- ◆ Testing adherence to procedures
- ◆ Assessing adequacy of documentation used during invoice review and payment
- ◆ Evaluating FPUC's success in preventing and correcting processing errors
- ◆ Assessing adequacy of internal control protections

To provide coverage of FPUC's storm cost dollars, audit staff selected its sample of vendor invoices from FPUC's four highest incremental cost categories: contractor costs, logistics, materials, and fuel. Together, these four categories account for 93 percent of FPUC's requested \$69.9 million of costs. To maximize its focus on more complex and impactful invoices, Commission audit staff's sample selection excluded all invoices of \$25,000 or less within these four selected categories.

After removing the \$25,000 and below invoices, audit staff determined the necessary sample size. Applying parameters of a 95 percent confidence level and an error rate of plus-or-minus 10 percent, a sample size of 66 invoices was calculated. Commission audit staff selected the sample invoices using a random number generator. FPUC provided each selected invoice and the supporting documentation used in processing and payment.

For purposes of its review, Commission audit staff determined that FPUC's costs related to Hurricane Dorian were incurred by the Company and paid for by means of the same procedures and practices as those of Hurricane Michael. None of the sample invoices selected represented Dorian costs; however, audit staff believes this does not impact the validity of its sample review because of the parameters above.

3.3 Invoice Sample Evaluation Criteria

To evaluate the sample invoices, Commission audit staff developed a set of attributes and checkpoints to assess process adequacy in the two key areas: adherence to Company procedures and adequacy of internal controls. Overall, the attributes considered encompassed general best business practices employed in purchasing and project management.

Additionally, evaluation of the sample invoices was performed considering Storm Restoration Cost Process Improvements included in Settlement Agreements² between three IOUs and the Office of Public Counsel during 2019. This gave perspective regarding the sufficiency of processes used during Hurricanes Michael and Dorian, and also gave an indication of the potential value of FPUC implementing these Storm Restoration Cost Process Improvements.

3.3.1 Compliance with FPUC Procedures

A basic evaluation of invoice processing accuracy involved simple verification of adherence to FPUC's applicable procedures. During Hurricanes Michael and Dorian, FPUC's *Contractor Invoice Requirements and Approval Documentation* procedures governed this process. These procedures were developed and implemented following Hurricanes Irma and Matthew, and were revised again following Hurricane Michael. They lay out basic guidelines for acquiring labor forces, work quality assurance oversight, invoice package content requirements, and invoice verification process responsibilities.

Typically, an invoice package contains the vendor's itemized invoice, and some form of records validating charges such as labor timesheets, materials used, and receipts for purchases to be reimbursed. It also usually includes evidence of materials received or approval of work by utility personnel. A key component of the package is evidence that the charges and itemizations in the invoice match applicable agreed-upon rates and terms. Last, an invoice package should contain evidence of approval for payment and a record of that payment being made.

After verifying the presence of necessary supporting documentation, Commission audit staff reviewed the package for evidence of compliance with applicable FPUC standards, requirements, and procedures. Where audit staff noted apparent exceptions, discussions were conducted with FPUC personnel to obtain needed reconciliations. Generally, explanations of transaction details clarified staff's concerns.

Commission audit staff verified that invoiced rates for hourly labor and equipment rentals matched current contract rates and terms. Time records were reviewed for evidence of authorization of work and contractor oversight. Similarly, evidence of supervisory approvals of the verification process was examined, and dual-control protection was verified for final payment.

3.3.2 Adequacy of Internal Controls

Beyond verifying that invoice processing comported with the Company's existing procedures, Commission audit staff also sought to assess the adequacy of internal process controls. To prevent payment errors or fraud, internal controls must secure each step of transactions that incur costs ultimately passed on to ratepayers. Primarily, the work or materials must be verified as having been provided and acceptable. FPUC processes include requirements for acceptance and related approvals and were observed to be functioning properly.

²*In re: Petition for recovery of costs associated with named tropical storms during the 2015, 2016, and 2017 hurricane seasons and replenishment of storm reserve subject to final true-up, Tampa Electric Company, Docket No. 20170271-EI; In re: Application for limited proceeding for recovery of incremental storm restoration costs related to Hurricanes Irma and Nate, by Duke Energy Florida, LLC., Docket No. 20170272-EI; In re: Evaluation of storm restoration costs for Florida Power & Light Company related to Hurricane Irma, Docket No. 20180049-EI.*

Commission audit staff believes internal controls must secure each step in purchasing to prevent payment errors or fraud. From the moment mutual aid labor is engaged or materials are ordered, FPUC must complete several verifications. FPUC states contractor work must be verified by an FPUC employee assigned to review each contractor team. Documentation reviewed indicates these controls appear to have functioned properly.

Prior storm cost recovery dockets demonstrate that vendor invoicing deficiencies and errors are problematic, particularly during the extraordinary challenges of storm recovery work. Commission audit staff believes that vendor training on invoicing procedures can greatly improve invoicing accuracy and therefore prevent payment errors. During Hurricanes Michael and Dorian, FPUC required vendors to include specific basic information in invoices. During 2019, FPUC prepared a more extensive set of guidelines to be distributed to vendors and contractors to guide future cost charging and invoicing.

FPUC's invoice review includes checking accuracy of invoiced labor hours, materials quantities, equipment charges, fuel costs, and lodging/meal expenses. Such controls include preparation of a spreadsheet by FPUC's financial analyst to check computations within invoices. Commission audit staff noted several instances of incorrect vendor invoicing that involved undercharging. These errors had been detected by FPUC staff and reviewed by management.

Supporting documentation for each invoice sampled included comparison of invoiced charges to applicable rates and other governing contract specifications. Contract provisions may direct the applicability of overtime labor rates, specify limits on meal and lodging costs, and address dispute resolution. Audit staff's sample review raised no concerns regarding adequacy of contract protections and compliance with terms and conditions.

Additionally, controls over the payment function after invoice review must guard against fraud and errors. Final approval for payment requires multiple reviews and appears to be executed in keeping with this procedure.

3.3.3 Settlement Agreement Storm Cost Process Improvements

During 2019 within their respective storm cost recovery dockets, three Florida IOUs entered into Settlement Agreements with the Office of Public Counsel.³ Beyond the dollar amounts to be recovered, these settlements included agreement for each utility to implement Storm Restoration Cost Process Improvements. Most pertain to practices intended to constrain storm costs and improve recovery work efficiency. In its evaluation, Commission audit staff compared FPUC's processes in place during Hurricane Michael to the settlement process improvements. This approach sought to determine the existence of an equivalent practice or control at the time Michael struck, and also to highlight any existing gaps these practice improvements could fill.

FPUC did not enter into such a settlement agreement during its prior storm cost recovery docket. However, the Company presently recognizes many of these process improvements could benefit both FPUC and its ratepayers. During the course of audit staff's review, FPUC voluntarily initiated some of these improvements. Of the ten "Contracting and Vendor Engagement, Travel, and Work

³ Order No. PSC-2019-0234-AS-EI, issued on June 14, 2019; Order No. PSC-2019-0232-AS-EI, issued on June 13, 2019; and Order No. PSC-2019-0319-S-EI, issued on August 1, 2019.

Policies” included in some IOU storm settlement agreements to cover future storms, FPUC has already voluntarily established policies for Billing Start Point, Travel Time Billing, Pace of Travel Guidance, Anti-Poaching, Daily Time Sheet Review and Documentation, 16 Hour Work/8 Hour Rest, and Meal and Fuel Policy. The Company stated it would initiate both a Contracting Policy and a GPS Tracking Capability Policy to the extent possible, and will continue its Mutual Assistance Committee participation. FPUC included these new policies in its Emergency Operating Procedure (EOP) E-16, *Contractor Invoice Requirements and Approval Documentation*, which was revised May 27, 2020.

3.4 Commission Audit Staff Observations

Based upon its review of processes, procedures, internal controls, and sampled invoices, Commission audit staff developed the following observations regarding storm cost controls and payment operations.

3.4.1 Invoice Processing and Payment Procedures

Vendor Invoicing Instructions

In processing invoices, the Company relied upon procedures it developed in August 2018 following Hurricanes Irma and Matthew. Subsequent to Hurricanes Michael and Dorian, during 2019 and 2020, FPUC prepared more thorough guidelines addressing labor charge procedures, reimbursable charges such as lodging and meals, and invoicing requirements and documentation.

Observation 1: **Commission audit staff believes FPUC’s invoice requirement procedure provided adequate direction, and that recent revisions to these policies and procedures further improved invoice review and payment processes.**

Invoice Checking, Correction, and Approval Procedures

During Hurricanes Michael and Dorian, FPUC used a multi-layered review process to validate invoices and approve them for payment. FPUC’s invoice review process detected discrepancies which were examined by Company management and/or corrected by contractors prior to invoice payment.

Observation 2: **Commission audit staff believes FPUC’s invoice checking, correction, and approval processes were effective.**

Personnel Staffing and Training

To handle increased numbers of invoices submitted by vendors for Hurricane Michael recovery work, FPUC added one employee dedicated to this function. The Company also acquired the services of an accounting consultant, who performed some review of documentation attached to the invoices.

Observation 3: Commission audit staff believes FPUC provided adequate staffing and expertise for invoice and payment processing and oversight to provide acceptable accuracy and efficiency.

3.4.2 Contractor Deployment and Management

Standby Hours and Minimum Daily Labor Hours

During Michael and Dorian, FPUC did not have a policy in place regarding vendors billing for standby hours or a guaranteed minimum number of labor hours per day. FPUC management indicated that in some cases, minimum charges of 16 hours per day and standby hours were billed and paid.

Commission audit staff notes that billing for both standby hours and for minimum guaranteed hours is a long-standing industry practice. The Company indicated that the extensive damage throughout its system provided more than enough work for every crew each day, normally resulting in 16 hours of productive work being completed.

FPUC states that during recovery efforts, scarcity of labor resources may leave no alternative but to use contractors whose standard contractual terms include specified minimum daily hours and standby time. It has now adopted a policy that it will make its best efforts to avoid “minimum number of hours to be paid daily, per diems, pay for rest time, standby time, or any other requirements than hourly charges.” The Company states that when accepting terms such as these is unavoidable, it will fully document the circumstances and conditions involved.

Observation 4: Commission audit staff notes that FPUC’s stated intention to avoid standby and minimum daily hour charges may reduce costs, but could also be advanced by executing contracts on more favorable terms prior to the storm season.

Contractor Work Monitoring and Recordkeeping

FPUC procedures require contractor work to be supervised by a qualified FPUC employee for assurance that work meets or exceeds FPUC’s expectations and standards. Each contractor crew is to be assigned a dedicated FPUC employee to coordinate and monitor assigned work. FPUC procedure requires contractor employees be formally checked in and out each day by an FPUC operations employee who documents the hours as regular time or overtime and the type of work performed.

Observation 5: Commission audit staff believes that FPUC’s contractor work monitoring and recordkeeping policies and procedures require acceptable levels of oversight.

Utility-Provided Meals and Fuel

During Michael, FPUC housed some mutual aid and contractor workers at base camp facilities. FPL brought its own self-contained base camp to the site to house and feed its workers. Once a contractor is on site, the Company states it normally provides lodging, meals, and fuel. Base camp provision of meals and fuel are addressed in FPUC’s Emergency Operating Procedure. It now

states that outside lodging, meals, or fuel will only be reimbursed with documented prior Company approval.

Observation 6: Commission audit staff believes FPUC’s planned implementation of closer controls over vendor costs may reduce meal and fueling costs.

Coordination with SEE and EEI

FPUC participates in the SEE Mutual Assistance Committee which focuses on locating transmission and distribution labor forces for member companies. During Hurricane Michael, FPUC made use of SEE services for obtaining mutual aid forces. With Hurricane Dorian, FPUC was able to manage restoration with the use of only contractors. FPUC observed discussion of proposed mutual aid changes at the Fall 2019 SEE member meeting. FPUC is also a member of EEI which provides guidance regarding mutual aid agreements.⁴

Observation 7: FPUC indicated that it will continue to participate in the SEE and EEI Mutual Assistance Committee meetings.

3.4.3 Lessons-Learned Assessment and Implementation of Improvements

Through four hurricanes in two years, FPUC’s experiences have allowed the Company to consider numerous lessons learned. As a result, the Company states it has implemented changes and refined policies relating to contractor record keeping, contractor onboarding, resource staging, vendor outsourcing, and supply inventory.

During this review, Commission audit staff and FPUC extensively discussed the various storm restoration cost process improvements agreed to by three Florida IOUs in settlements of recent storm cost recovery dockets. FPUC considered the benefits these process improvements provide for the Company and its ratepayers, has implemented some improvements, and has committed to consider others.

Observation 8: FPUC has agreed to implement several storm restoration cost process improvements that emerged as best practices in three recent Commission storm cost recovery dockets. Commission audit staff believes these improvements will enhance the Company’s ability to manage costs incurred in future storms.

⁴https://www.eei.org/issuesandpolicy/electricreliability/mutualassistance/Documents/MAAgreement+GovPrinc_FINAL_090717.pdf