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Xcel Energy, Inc. Franchise Agreement Review

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Date: September 19, 2012

To: Kevin Carpenter, Finance & Property Services (Finance)
Susan Segal, City Attorney's Office

Re: Xcel Energy, Inc. Franchise Agreement Review

The Internal Audit Department (IA) conducted a review of the Xcel Energy, Inc. (Xcel) Franchise Agreement. This review was included in the 2012 Internal Audit Plan and was completed in August 2012.

Background

The City of Minneapolis (the City) passed an [Ordinance](#) (i.e. Franchise Agreement) for the period January 1, 1994 ("Commencement Date") until December 31, 2014 between the City and Northern States Power Company and its successors (currently Xcel). The Franchise Agreement allows Xcel to use the City's streets, alleys, and public grounds to provide electricity to the City and its residents. In return, Xcel pays to the City, on a monthly basis, a franchise fee based off of the gross revenues Xcel received. The franchise fee currently paid to the City for residential service customers is 5% and for commercial and industrial customers is 3% of Xcel's gross revenues; this amounted to approximately \$17.5 million in 2011.

Objectives

The review was performed to assess whether controls are designed and functioning effectively to ensure:

- Franchisee payments received are in accordance to the franchise agreement; and
- Processes or controls exist to communicate and/or address potential financial issues with Xcel as they arise, if any; and to verify a follow-up mechanism is in place.

Scope

This review included gaining an understanding of internal controls, including current policies and procedures, through observation, inquiry, and limited testing surrounding the processes listed above. We performed, on a sample basis, testing of the following processes and transactions for the period January 1, 2010 through July 31, 2012 and for the franchise agreement effective during FY 2012:

- Contract oversight; and
- Payments received from franchisee.

Summary of Findings and Management Action Plans:

1. Franchise Agreement Monitoring

There is no formal monitoring process of the franchise agreement to ensure the completeness and accuracy of the payments received by the City.

Management Response

The City will work with Xcel to ensure detailed backup is provided with each monthly payment. The monthly payment and detailed backup will be reviewed by accounting staff to ensure the payment calculations are correct. The detailed backup which is received and reviewed monthly will be reconciled to Xcel's statement annually.

2. Certified Annual Statement

The Franchise agreement Section 4 states “...the Company shall furnish to said Finance Officer...a statement, certified by the Company's Controller or another officer of the Company, of the amount of the Company's gross operating revenues for the preceding calendar year.” The aforementioned certified statement referenced in the Franchise Agreement is not received by Finance management.

Management Response

As mentioned in the management response above, because the detailed backup will be received and reviewed monthly and reconciled to the annual statement received from Xcel at the end of the year, an annual “certified” statement from Xcel will not be necessary.

Conclusion

Based on our review, we believe there are opportunities for improvements to address risk areas identified in this report. Finance worked collaboratively with IA to develop action plans. However, this report contains a disagreement that Finance management decided no action was necessary.

IA would like to extend our appreciation to Finance and City Attorney's Office personnel who assisted and cooperated with us during this review.

Cc: Paul Aasen, City Coordinator's Office
Mary Dunning, Finance
Peter Ginder, City Attorney's Office
Connie Griffith, Finance

Xcel Energy, Inc. Franchise Agreement Review

Audit Findings and Action Plans

1. Franchise Agreement Monitoring

On a monthly basis, Finance receives a Franchise Fee Report from Xcel that includes the Franchise Fee owed to the City for that particular month of use, along with adjustments¹ made by Xcel. Franchise fee payments to the City are sent securely through wire transfer and deposited in the City's bank account. IA noted there is no monitoring process of the franchise agreement to ensure the completeness and accuracy of the payments received. By not adequately monitoring receipt of Franchise Fees from Xcel, the City could potentially be at risk of not receiving the correct Franchise Fee payment.

Recommendation

IA recommends Finance develop a process to assist in monitoring the Franchise fees and related financial issues to ensure Franchise Fees received are complete and accurate.

Management Response

Currently the City receives a remittance advice with the monthly franchise fee payment from Xcel which provides a summary of payment information. At the end of the year, the City receives a spreadsheet showing more detailed calculations by month providing reconciliation to the payments received during the year. Currently, City Accounting staff review the payments quarterly for reasonableness, unless any monthly payment appears materially different, in which case details are investigated immediately. Xcel also communicates with the City regarding adjustments it will be making to the payments.

The City will work with Xcel to provide more detailed backup for its monthly payments including adjustments. The monthly payment and detailed backup will be reviewed by Accounting staff to ensure the payment calculations are correct. Accounting staff will reconcile the monthly payment information received from Xcel to the detailed payment worksheet received at the end of each year. The detailed backup which is received and reviewed monthly and reconciled to Xcel's statement annually, should provide adequate documentation of adherence to contract terms and additional certification by Xcel should not be necessary.

The expectation is this process will be set up by year-end 2012 with backup detail provided back to the beginning of the year along with a review and reconciliation done for the year by City Accounting staff to be confirmed by the City Controller. The more detailed monthly review will begin in January 2013 followed by the annual review and reconciliation. The City will work with Xcel to incorporate language describing this process in its next contract.

Responsible Party

Connie Griffith, Controller

Expected Completion Date

January 31, 2013 and on-going.

Projected Cost of Implementation

Total Estimated Cost: \$2,340 (one-time), \$672 (recurring annually)
Hours: 36 (one-time), 8 (recurring annually)

¹ Adjustments include exemptions, write-offs, miscellaneous adjustments and rounding.

2. Certified Annual Statement

The Franchise agreement Section 4 states “...the Company shall furnish to said Finance Officer, not later than April 1st of the year, 1994 and of each year thereafter, a statement, certified by the Company's Controller or another officer of the Company, of the amount of the Company's gross operating revenues for the preceding calendar year.” The aforementioned certified statement referenced in the Franchise Agreement is not received by Finance management. Without receipt of proper certification for gross revenues, Finance management is not receiving the proper level of assurance as to the accuracy of franchise fees that was intended when the franchise agreement was put in place.

Recommendation

IA recommends Finance work with Xcel to enforce the terms and conditions of the Franchise Agreement and request Xcel to provide a certified statement of gross revenues for the customers located throughout the City of Minneapolis.

Management Response

As mentioned in the management response above, because the detailed backup will be received and reviewed monthly and reconciled to the annual statement received from Xcel at the end of the year, an annual “certified” statement from Xcel will not be necessary.

Responsible Party

Connie Griffith, Controller

Expected Completion Date

No action is needed.

Projected Cost of Implementation

Total Estimated Cost: \$409 (recurring annually)

Hours: 6 (recurring annually)

Projected Cost of Implementation (contents provided by Finance)					
Audit Finding		Estimated Hours		Total Estimated Cost	
		One-time	Recurring Annually	One-time	Recurring Annually
1	Franchise Agreement Monitoring	36	8	\$ 2,340	\$672
2	Certified Annual Statement	-	6	-	\$409
Totals		36	14	\$ 2,340	\$ 1,081

Abbreviations Used Throughout the Report	
City	The City of Minneapolis
Finance	Finance and Property Services Department
IA	Internal Audit Department
Xcel	Xcel Energy, Inc.