

**NEW MEXICO MUNICIPAL  
ENERGY ACQUISITION AUTHORITY  
FINANCIAL STATEMENTS  
June 30, 2018 and 2017**

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## **INTRODUCTORY SECTION**

**NEW MEXICO MUNICIPAL  
ENERGY ACQUISITION AUTHORITY  
List of Principal Officials  
(unaudited)  
June 30, 2018**

<u><b>Name</b></u>	<u><b>Title</b></u>
Robert Westervelt .....	Chairperson
Jorge Garcia .....	Vice Chairperson
Patty Holland .....	Secretary
Brandon Hill .....	Treasurer
Richard Matzke .....	Member
Rosie Duran .....	Member
Mario Puentes .....	Alternate Member

## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
New Mexico Municipal Energy Acquisition Authority  
and  
Wayne Johnson, State Auditor

### Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of New Mexico Municipal Energy Acquisition Authority (NMMEAA), and the budgetary comparison as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise NMMEAA's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

## Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the New Mexico Municipal Energy Acquisition Authority as of June 30, 2018, and the respective changes in financial position and where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statements referred to the above present fairly, in all material respects, the respective budgetary comparison for the year ended June 30, 2018 in accordance with accounting principles generally accepted in the United States of America.

## Prior Period Financial Statements

The financial statements of NMMEAA as of and for the year ended June 30, 2017 were audited by other auditors whose report dated February 28, 2018, expressed an unmodified opinion on those financial statements.

## Other Matters

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages iv and viii be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated December 14, 2018, on our consideration of the NMMEAA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering NMMEAA's internal control over financial reporting and compliance.

The logo for Axiom, featuring the word "Axiom" in a stylized, cursive blue font.

Albuquerque, New Mexico  
December 14, 2018

## New Mexico Municipal Energy Acquisition Authority Management's Discussion and Analysis

Management's Discussion and Analysis of the New Mexico Municipal Energy Acquisition Authority (NMMEAA) financial performance provides an overview of NMMEAA's financial activities for the year ended June 30, 2018. Please read this information in conjunction with the accompanying financial highlights, the basic financial statements and the accompanying notes to the financial statements.

NMMEAA was created June 19, 2008 through a Joint Powers Agreement organized pursuant to the laws of the State of New Mexico between the City of Las Cruces and the City of Gallup for the purpose of obtaining a reliable long-term supply of natural gas under favorable terms, conditions and prices to benefit government-owned utilities and their retail customers. The City of Farmington, the City of Las Cruces and the Incorporated County of Los Alamos have 30 year gas supply agreements with NMMEAA, with the gas furnished through a prepaid gas purchase and sale contract with Royal Bank of Canada (RBC).

On November 19, 2009, \$780,965,000 of New Mexico Municipal Energy Acquisition Authority Gas Supply Variable Rate Revenue Bonds, Series 2009 were issued to provide a lump sum payment to RBC for the prepaid gas contract. A total quantity of 171,322,165 MMBtu of natural gas will be delivered at designated delivery points and specified daily quantities over a period of 30 years to NMMEAA under the terms of the prepaid agreement. Due to new guidelines adopted by the Canadian Office of the Superintendent of Financial Institutions ("OSFI") which RBC determined materially affected the 2009 transaction, the Series 2009 bonds were refunded with Series 2014 Refunding Bonds for an initial 5 year period with a potential to continue beyond 5 years. The refunding took place on August 1, 2014.

### Financial Analysis

The following condensed financial statements summarize NMMEAA's financial position and operating results for the years ended June 30, 2018 and 2017.

#### New Mexico Municipal Energy Acquisition Authority Net Position

	FY 2018	FY 2017
Current assets	\$ 42,881,092	41,991,612
Noncurrent assets	1,198,557,664	1,213,117,680
Total assets	1,241,438,756	1,255,109,292
Total deferred outflows of resources	-	1,471,199
Current liabilities	28,524,609	26,847,450
Noncurrent liabilities	640,450,000	668,750,949
Total liabilities	668,974,609	695,598,399
Total deferred inflows of resources	572,438,982	560,980,943
Unrestricted net position	25,165	1,149
Total net position	\$ 25,165	1,149

# New Mexico Municipal Energy Acquisition Authority Management's Discussion and Analysis

## Condensed Statements of Revenues, Expenses, and Changes in Net Position Years ended June 30, 2018 and 2017

	FY 2018	FY 2017
Operating revenues	\$ 44,414,367	43,272,341
Operating expenses	44,390,351	43,299,773
Operating loss	24,016	(27,432)
Change in net position	24,016	(27,432)
Net position - beginning	1,149	28,581
Net position - ending	\$ 25,165	1,149

### **2018 Financial Highlights**

#### Statement of Net Position:

Total assets, deferred outflows of resources, liabilities and deferred inflows of resources result from the issuance of revenue bonds and the purchase of a prepaid gas contract. Derivative financial instruments necessary to make the transaction possible are shown at their fair value as of June 30, 2018.

#### Operating Revenues:

Operating revenues result from gas deliveries which are based on a specified index less a discount from such price, plus a premium.

Income from the commodity swap contract and interest on investments are non-operating revenue. The fixed interest expense from the interest rate swap is offset by net costs to be recovered in future periods. Under GASB 62, certain income and expense items are deferred and not included in the determination of net income until such costs are recoverable.

#### Operating Expenses:

The largest operating expense of NMMEAA is amortization of the prepaid gas supply. Other operating expenses in FY2018 include a savings distribution to the three gas purchasers, credit support expense, the trustee expense and various administrative expenses.



# New Mexico Municipal Energy Acquisition Authority Management's Discussion and Analysis

## Condensed Statements of Revenues, Expenses, and Changes in Net Position Years ended June 30, 2017 and 2016

	FY 2017	FY 2016
Operating revenues	\$ 43,272,341	43,559,987
Operating expenses	43,299,773	43,518,389
Operating loss	(27,432)	(255,402)
Change in net position	(27,432)	(255,402)
Net position - beginning	28,581	283,983
Net position - ending	\$ 1,149	28,581

### **2017 Financial Highlights**

#### Statement of Net Position:

Total assets, deferred outflows of resources, liabilities and deferred inflows of resources result from the issuance of revenue bonds and the purchase of a prepaid gas contract. Derivative financial instruments necessary to make the transaction possible are shown at their fair value as of June 30, 2017.

#### Operating Revenues:

Operating revenues result from gas deliveries which are based on a specified index less a discount from such price, plus a premium.

Income from the commodity swap contract and interest on investments are non-operating revenue. The fixed interest expense from the interest rate swap is offset by net costs to be recovered in future periods. Under GASB 62, certain income and expense items are deferred and not included in the determination of net income until such costs are recoverable.

#### Operating Expenses:

The largest operating expense of NMMEAA is amortization of the prepaid gas supply. Other operating expenses in fiscal year 2017 include a savings distribution to the three gas purchasers, credit support expense, the trustee expense and various administrative expenses.

# New Mexico Municipal Energy Acquisition Authority Management's Discussion and Analysis

## Capital Assets and Debt Administration

### Capital Assets

NMMEAA does not hold any capital assets.

### Long-term Obligations

At the end of the current fiscal year, NMMEAA had total debt outstanding of \$667,279,750, of which \$662,350,000 is the refunding bond and \$4,929,750 the bond premium. Obligations decreased by \$25,334,750. Within one year \$21,900,000 will be due for the bond and \$4,929,750 for the bond premium.

	<u>Balance</u> <u>June 30, 2016</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2017</u>	<u>Due Within</u> <u>One Year</u>
Total Revenue Refunding Series 2014	701,810,000	-	(19,055,000)	682,755,000	20,405,000
Bond Premium	14,789,250	-	(4,929,750)	9,859,500	4,929,750
	<u>\$ 716,599,250</u>	<u>\$ -</u>	<u>\$ (23,984,750)</u>	<u>\$ 692,614,500</u>	<u>\$ 25,334,750</u>
	<u>Balance</u> <u>June 30, 2017</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2018</u>	<u>Due Within</u> <u>One Year</u>
Total Revenue Refunding Series 2014	\$ 682,755,000	-	(20,405,000)	\$ 662,350,000	\$ 21,900,000
Bond Premium	9,859,500	-	(4,929,750)	4,929,750	4,929,750
	<u>\$ 692,614,500</u>	<u>\$ -</u>	<u>\$ (25,334,750)</u>	<u>\$ 667,279,750</u>	<u>\$ 26,829,750</u>

### Rating Factors

During the fiscal year, Moody's Investors Service upgraded the credit rating of several Canadian banks, including Royal Bank of Canada, back to Aa2 from A1 in Fiscal Year 2018.

## General Trends and Significant Events

Recent changes in U.S. Treasury regulations and U.S. Tax code has allowed government-owned utilities to issue tax-exempt bonds to pre-pay a natural gas supply which is lower priced and more stable for use by retail customers or for the generation of electricity which is then sold to retail customers. In 2008, negative economic events began to occur in the U.S. which hurt the financial standing of large financial institutions. This was followed by a drop in natural gas prices in 2009, which had been at record highs. Long term prepaid gas contracts reduce the volatility of the natural gas market.

In November 2009, NMMEAA issued tax exempt bonds to purchase a 30 year prepaid supply of natural gas. In August 2014 these bonds were refunded with Series 2014 Refunding Bonds for an initial 5 year period while retaining potential to continue beyond 5 years with a gas discount for the 3 gas purchasers of \$0.2894/MMBtu. Series 2014 consists of floating rate notes (FRNs) with hard maturities, FRNs with a hard put, and fixed rate bonds. In connection with the purchase of the gas supply, NMMEAA entered

## **New Mexico Municipal Energy Acquisition Authority Management's Discussion and Analysis**

into a commodity swap agreement to convert the floating, market-referenced revenues received from gas supply agreements to a fixed revenue stream for the entire gas supply delivered under the prepaid gas agreement. The commodity swap counterparty during fiscal year 2016 was J.P. Morgan Chase Bank NA. The term of the commodity swap agreement is the same term as the prepaid gas agreement and covers the same period and gas delivery points. The commodity swap counterparty had to maintain a credit rating of at least A2 by Moody's or post collateral according to the trust indenture.

NMMEAA also entered into an interest rate swap agreement covering two transactions with RBC to hedge interest rate fluctuations on the bonds and to more closely match payment obligations on the bonds with revenues from the supply agreements and the commodity swap agreement. With the restructure, the original interest rate swap transactions were replaced with a fixed rate swap transaction.

### **Summary of the Financial Statements**

The financial statements, related notes and management's discussion and analysis provide information about NMMEAA's financial position and activities as of June 30, 2018. The statement of net position presents assets, liabilities and net position; the statement of revenues, expenses and changes in net position present operating results and change in net assets; and the statement of cash flows shows sources and uses of cash during the year. The notes to the financial statements provide additional disclosures and information essential to a full understanding of the data provided in the statements.

### **Report of Management**

NMMEAA has prepared and is responsible for the financial statements and related information included in this report. Management believes that its policies and procedures provide guidance and reasonable assurance that NMMEAA's operations are conducted according to management's intentions within an ethical framework. In management's opinion, the financial statements present fairly, in all material respects, the financial position, results of operations and cash flows of NMMEAA in conformity with accounting principles generally accepted in the United States of America. Questions regarding this report or for additional information should be addressed to the manager of NMMEAA, the City of Farmington, at the address shown below.

\*\*\*\*\*

The City of Farmington  
101 N. Browning Parkway  
Farmington, NM 87401-7995  
505-599-8311

## **BASIC FINANCIAL STATEMENTS**

**New Mexico Municipal Energy Acquisition Authority**  
**Statements of Net Position**  
**June 30, 2018 and 2017**

	<b>FY 2018</b>	<b>FY 2017</b>
<b>ASSETS:</b>		
Current assets:		
Cash and cash equivalents	\$ 4,497,042	\$ 4,507,550
Receivables - gas supply agreements	670,621	985,690
Receivables - other	2,879,546	2,271,909
Restricted cash and cash equivalents	10,137,535	9,451,820
Prepaid gas supply, current	24,696,348	24,774,643
Total current assets	42,881,092	41,991,612
Noncurrent assets:		
Prepaid gas supply, long-term	513,501,160	538,119,214
Costs recoverable from future billings	112,617,522	114,017,523
Fair value of derivative instruments	572,438,982	560,980,943
Total noncurrent assets	1,198,557,664	1,213,117,680
Total assets	1,241,438,756	1,255,109,292
<b>DEFERRED OUTFLOWS OF RESOURCES:</b>		
Accumulated decrease in fair value of derivative instrument	-	1,471,199
Total deferred outflows of resources	-	1,471,199
<b>LIABILITIES:</b>		
Current liabilities:		
Accounts payable	68,389	70,827
Accrued interest payable	1,626,470	1,441,873
Current maturities of long-term debt	26,829,750	25,334,750
Total current liabilities	28,524,609	26,847,450
Noncurrent liabilities:		
Fair value of derivative instruments	-	1,471,199
Long-term debt, net of current maturities	640,450,000	667,279,750
Total noncurrent liabilities	640,450,000	668,750,949
Total liabilities	668,974,609	695,598,399
<b>DEFERRED INFLOWS OF RESOURCES:</b>		
Accumulated increase in fair value of derivative instrument	572,438,982	560,980,943
Total deferred inflows of resources	572,438,982	560,980,943
<b>NET POSITION:</b>		
Unrestricted net position	25,165	1,149
Total net position	\$ 25,165	\$ 1,149

**See notes to financial statements.**

**New Mexico Municipal Energy Acquisition Authority**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**For the Years Ended June 30, 2018 and 2017**

	<b>FY 2018</b>	<b>FY 2017</b>
<b>Operating revenues:</b>		
Gas supply agreement income	\$ 11,324,904	\$ 13,902,160
Investment earnings	60,686	8,423
Commodity swap	28,099,027	24,432,008
Amortization of bond premium	4,929,750	4,929,750
Total operating revenues	44,414,367	43,272,341
 <b>Operating expenses:</b>		
Cost of gas sold	24,696,348	24,696,348
Net costs to be recovered in future periods	1,397,598	(78,295)
Gas service administration expense	14,225	13,785
Savings distribution to gas purchasers	43,800	49,723
Trustee expense	22,853	23,590
Rating agency expense	8,292	7,700
Credit support expense	64,960	64,724
Legal expense	1,693	4,029
Audit expense	20,425	20,389
Management fee expense	12,600	12,600
Interest rate swaps:		
Fixed rate	9,357,558	9,735,180
Variable rate	(8,622,766)	(6,221,229)
Total interest rate swap expense	734,792	3,513,951
Interest expense to bondholders	17,372,765	14,971,229
Total operating expenses	44,390,351	43,299,773
 <b>Operating income (loss)</b>	<b>24,016</b>	<b>(27,432)</b>
 <b>Change in net position</b>	<b>24,016</b>	<b>(27,432)</b>
 <b>Net position - beginning</b>	<b>1,149</b>	<b>28,581</b>
<b>Net position - ending</b>	<b>\$ 25,165</b>	<b>\$ 1,149</b>

See notes to financial statements.

**New Mexico Municipal Energy Acquisition Authority**  
**Statements of Cash Flows**  
**For the Years Ended June 30, 2018 and 2017**

	<b>FY 2018</b>	<b>FY 2017</b>
<b>Cash flows from operating activities</b>		
Receipts from customers/users	\$ 11,032,336	\$ 13,628,445
Payments to other suppliers of goods and services	(145,083)	(148,574)
Annual savings distribution to gas purchasers	(43,800)	(49,723)
Interest paid	(17,922,959)	(18,319,232)
Investment income	60,686	8,423
Net cash provided (used) by operating activities	(7,018,820)	(4,880,661)
<b>Cash flows from noncapital and related financing activities</b>		
Principal payments on long-term debt	(20,405,000)	(19,055,000)
Net cash provided (used) by noncapital financing activities	(20,405,000)	(19,055,000)
<b>Cash flows from investing activities</b>		
Net change from commodity swap	28,099,027	24,432,008
Net cash provided (used) by investing activities	28,099,027	24,432,008
Net increase (decrease) in cash and cash equivalents	675,207	496,347
Cash and cash equivalents, beginning of year	13,959,370	13,463,023
Cash and cash equivalents, end of year	\$ 14,634,577	\$ 13,959,370
<b>Reconciliation of operating income to net cash provided (used) by operating activities</b>		
Operating income (loss)	\$ 24,016	\$ (27,432)
Prepaid gas supply amortization	24,696,348	24,696,348
Amortization of bond premium	(4,929,750)	(4,929,751)
Fair value change in commodity swap	(28,099,027)	(24,432,008)
Changes in operating assets and liabilities		
Receivables - gas supply agreement	315,069	(378,863)
Receivables - other	(607,637)	105,149
Accounts payable	(2,438)	(1,757)
Costs recoverable from future billings	1,400,001	(78,295)
Accrued interest payable	184,598	165,948
Net cash provided (used) by operating activities	\$ (7,018,820)	\$ (4,880,661)
Noncash noncapital and related financing activities		
Bond Premium amortization	\$ 4,929,750	\$ 4,929,750

**See notes to financial statements.**

**New Mexico Municipal Energy Acquisition Authority**  
**Schedule of Revenues, Expenses and Changes in Net Position**  
**Budget to Actual**  
**For the Year Ended June 30, 2018**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
<b>Operating revenues:</b>				
Gas supply/Commodity swap less adm	\$ 39,333,964	\$ 39,333,964	\$ 39,409,706	\$ 75,742
Interest income	3,000	3,000	60,686	57,686
Other income	-	-	-	-
Bond proceeds	-	-	-	-
Total operating revenues	<u>39,336,964</u>	<u>39,336,964</u>	<u>39,470,392</u>	<u>133,428</u>
<b>Operating expenses:</b>				
Savings distribution to gas purchasers	60,000	60,000	43,800	16,200
Trustee expense	25,000	25,000	22,853	2,147
Rating agency expense	12,000	12,000	8,292	3,708
Credit support expense	70,000	70,000	64,960	5,040
Legal expense	60,000	60,000	1,693	58,307
Audit expense	21,000	21,000	20,425	575
Management fee expense	12,600	12,600	12,600	-
Principal payment	20,405,000	20,405,000	20,405,000	-
Interest expense	<u>18,250,000</u>	<u>18,250,000</u>	<u>18,107,557</u>	<u>142,443</u>
Total operating expenses	<u>38,915,600</u>	<u>38,915,600</u>	<u>38,687,180</u>	<u>228,420</u>
<b>Operating income (loss)</b>	<b>421,364</b>	<b>421,364</b>	<b>783,212</b>	<b><u>\$ 361,848</u></b>
<b>Adjustments to GAAP:</b>				
Cost of gas sold		-	(24,696,348)	
Net costs to be recovered in future periods		-	(1,397,598)	
Principal payment		-	20,405,000	
Amortization of bond premium		-	<u>4,929,750</u>	
			<u>(759,196)</u>	
<b>GAAP BASIS CHANGE IN NET POSITION:</b>			<b>24,016</b>	
Net position - beginning			<u>1,149</u>	
Net position - ending	<u>\$ 421,364</u>	<u>\$ 421,364</u>	<u>\$ 25,165</u>	

See notes to financial statements.



**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 1: Nature of Operations and Summary of Significant Accounting Policies**

**Nature of Operations**

New Mexico Municipal Energy Acquisition Authority (NMMEAA) was established in 2008 through a joint powers agreement to acquire long-term energy supplies by the City of Las Cruces, NM and the City of Gallup, NM. Both cities are New Mexico charter municipalities with municipal home-rule powers created and existing pursuant to the Constitution and laws of the State of New Mexico. NMMEAA was formed to:

- Purchase natural gas to be furnished to retail gas customers within the gas service area of the City of Las Cruces for purposes other than electric generation, or for sale to another municipal or governmentally-owned utility to be furnished to retail gas customers within such utility's natural gas service area for purposes other than electric generation;
- Purchase natural gas to be used to produce electricity to be furnished to retail customers within the electricity service area of the City of Gallup, or for sale to another municipal or governmentally-owned utility to be used to produce electricity to be furnished to retail customers within such utility's electric service area for such use;
- Purchase electricity for distribution and sale of electricity for distribution and sale of electricity by the City of Gallup to its retail customers and to other municipal or governmentally-owned electric utilities for such use; and
- Finance the cost of purchasing natural gas or electricity through the issuance of revenue bonds secured by natural gas supply and related contracts and/or electricity supply and related contracts (Supply Contracts) and revenues received pursuant to such Supply Contracts and other contracts.

Beginning in October 2009, NMMEAA began selling natural gas to the City of Farmington, NM, and in November 2009 to the City of Las Cruces, NM and the Incorporated County of Los Alamos, NM through long-term gas supply contracts. Proceeds received from issuing New Mexico Municipal Energy Acquisition Authority Gas Supply Variable Rate Revenue Bonds, Series 2009 were used to purchase a long-term prepaid gas supply for these contracts, which were refunded with Series 2014 Refunding bonds.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 1: Nature of Operations and Summary of Significant Accounting Policies**  
**(continued)**

***Reporting Entity***

In evaluating how to define a governmental entity, for financial reporting purposes, management must consider all potential component units for which financial accountability may exist. The determination of financial accountability pursuant to Governmental Accounting Standards Board (GASB 14, *The Financial Reporting Entity* and GASB No. 39, *Determining Whether Certain Organizations are Component Units*) includes consideration of a number of criteria, including: (1) the ability to appoint a voting majority of another entity's governing body and to impose its will on that entity, (2) the potential for that entity to provide specific financial benefits to or impose specific financial burdens on others, and (3) the entity's fiscal dependency on others. NMMEAA has determined that it has no reportable component units.

***Accounting Method***

NMMEAA's funds are accounted for on the accrual basis of accounting. NMMEAA's records are maintained in accordance with accounting principles generally accepted in the United States of America for regulated utilities and generally follow the Uniform System of Accounts for Public Utilities and License prescribed by the Federal Energy Regulatory Commission (FERC). NMMEAA prepares its financial statements as a business-type activity in conformity with applicable pronouncements of GASB.

GASB Statement No. 62 incorporated into the GASB's authoritative literature certain accounting and reporting guidance included in the Financial Accounting Standards Board (FASB) Statements and Interpretations that were issued on or before November 30, 1989 which did not conflict with or contradict GASB pronouncements. Under the provisions of GASB Statement No. 62, *Regulated Operations*, NMMEAA has deferred certain income and expense items in the determination of net income until such time as the costs are recoverable.

During fiscal year 2017, GASB Statement No. 77, *Tax Abatement Disclosures*, became effective. NMMEAA does not have any agreements that require disclosure under the standards.

***Use of Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses and other changes in net position during the reporting period. Actual results could differ from those estimates.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 1: Nature of Operations and Summary of Significant Accounting Policies (continued)**

***Cash and Cash Equivalents***

NMMEAA considers all highly liquid investments with original maturities of three months or less at the time of purchase to be cash and cash equivalents. Cash and cash equivalents consist of money market mutual funds invested in government securities and US Treasury Bills.

Restricted cash and cash equivalents also consists of money market mutual fund invested in government securities and US Treasury Bills that is maintained in a separate account at Wells Fargo specifically for meeting NMMEAA's debt service requirement.

***Receivables***

Receivables are stated at the amount billed to customers and interest receivable. Receivables billed to customers are due within 10 days after issuance of the invoice, or by the 20<sup>th</sup> of the month or the business day immediate preceding such day if the 20<sup>th</sup> is not a business day. Management does not believe an allowance for doubtful accounts is necessary at June 30, 2018. There was no allowance as of June 30, 2017.

***Prepaid Gas Supply***

NMMEAA prepaid for deliveries of the natural gas supplies with the proceeds from the revenue bonds. Prepaid gas supplies are stated at average cost, as determined by the prepay contract.

***Costs Recoverable from Future Billings***

NMMEAA's Natural Gas Supply Agreements establish a pricing mechanism outlining the methods for billing customers for the natural gas supply. Expenses in excess of amounts currently billable to customers under the pricing mechanism will be recovered in future billings to customers and are classified as a regulatory asset. These amounts are principally related to long-term supply and include interest expense, amortization, and other costs that are realized at different times than they are billed to customers.

***Deferred Outflows/Inflows of Resources***

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 1: Nature of Operations and Summary of Significant Accounting Policies (continued)**

***Deferred Outflows/Inflows of Resources (continued)***

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

***Net Position Classification***

Restricted assets within net position have externally imposed constraints by creditors (such as debt covenants), contributors, laws or regulations of other governments. There were no restricted assets as of the year ended June 30, 2018 and 2017.

Unrestricted Net Position: Assets without externally or internally imposed constraints. NMMEAA has no restricted assets within net position nor does it have any net investment in capital assets. NMMEAA's net position is completely unrestricted.

***Classification of Revenues***

NMMEAA has classified all revenues as operating revenues according to the following criteria: Operating revenues are derived from deliver of gas supplies to customers and or other revenue sources that are derived from capital and related financing, noncapital financing and investing activities such as net costs to be recovered in future periods and investment income are supporting common operational objectives.

***Derivative Instruments***

Derivative instruments are utilized by NMMEAA to manage market risk and reduce its exposure resulting from fluctuations in prices of natural gas in order to meet debt service requirements. These instruments include a commodity swap agreement which converts index-priced natural gas revenues to fixed prices for servicing outstanding debt obligations and an interest rate swap agreement in which NMMEAA pays a fixed rate of 1.89403% to RBC and receives in return, an actual variable rate equal to the variable rate paid to holders of the Series 2014 Bonds.

***Income Taxes***

NMMEAA operates as a governmental entity under a joint powers agreement in the State of New Mexico and is exempt from federal and state income taxes.

***Budgets***

The budget is adopted on a cash basis of accounting. The legal compliance for the budget is total expenditures.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 2: Cash and Investments**

As of June 30, 2018 and 2017 NMMEAA had the following cash and investments which are held in trust by Wells Fargo Bank, National Association, as Trustee.

	<u>FY 2018</u> <u>Trust</u>	<u>FY 2017</u> <u>Trust</u>
Wells Fargo Advantage Treasury Plus Money Market Service #454		
Total cash and cash equivalents	\$ <u>14,634,577</u>	\$ <u>13,959,370</u>
	<u>Financial Statements</u>	<u>Financial Statements</u>
Cash and cash equivalents	\$ 4,497,042	\$ 4,507,550
Restricted cash and cash equivalents	<u>10,137,535</u>	<u>9,451,820</u>
Total cash and cash equivalents	\$ <u>14,634,577</u>	\$ <u>13,959,370</u>

***Interest Rate Risk***

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. NMMEAA may only invest in direct obligations of the United States or obligations guaranteed as to full and timely payment both as to principal and interest by the United States; and in investments in a money market fund secured by obligations of the United States. The money market funds are presented as cash and cash equivalents with a maturity of less than one year because they are redeemable in full immediately.

***Credit Risk***

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The trust indenture requires counterparties to have a credit rating by Moody's of at least A1.

***Custodial Credit Risk***

Custodial credit risk is the risk that in the event of a bank failure NMMEAA's deposits with the Trustee may not be returned to it. All monies held under the Indenture by the Trustee are to be held in such manner as required by applicable Federal or State laws and regulations of the state in which the Trustee is located and shall be either continuously or fully insured by the Federal Deposit Insurance Corporation (FDIC), or if not continuously and fully secured by FDIC, by lodging with the Trustee, as custodian, as collateral security, qualified investments having a market value (exclusive of accrued interest) not less than the amount of such moneys. At June 30, 2018 and 2017, NMMEAA's did not have any bank deposits and there was no collateral pledged by the Trustee.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 2: Cash and Investments (continued)**

***Concentration of Credit Risk***

NMMEAA and the trust indenture place no limit on the amount that may be invested in any one issuer.

	<u>FY 2018</u> <u>Portfolio Composition</u>	<u>FY 2017</u> <u>Portfolio Composition</u>
Wells Fargo Advantage Treasury Plus Money Market Service #454	\$ <u>14,634,577</u>	\$ <u>13,959,370</u>

***Fair value measurements***

NMMEAA categorizes its cash equivalents within the fair value hierarchy established by generally accepted accounting principles. Cash equivalents, which are comprised entirely of money market accounts. Money market accounts consist of short-term money market instruments issued by the U.S and do not have a level under the fair value hierarchy.

**Note 3: Restricted Cash and Cash Equivalents**

The following is a summary of restricted assets as of June 30, 2018 and 2017.

	<u>FY 2018</u>	<u>FY 2017</u>
<u>Restricted assets</u>		
Debt Service fund principal - Total restricted asset	\$ <u>10,137,535</u>	\$ <u>9,451,820</u>

**Note 4: Long-term Debt**

In October 2009, NMMEAA issued \$780,965,000 of gas supply revenue bonds to fund the prepayment of 171,322,165 MMBtus of gas from Royal Bank of Canada (RBC) with deliveries beginning November 2009 and ending October 2039. The City of Farmington, NM, and the City of Las Cruces, NM and the Incorporated County of Los Alamos, NM will purchase the scheduled monthly gas at a specified index less a discount from such index price for the entire term of November 2009 through October 2039. The revenue bonds are secured by a pledge of the gas supply revenues derived from the prepay transaction.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 4: Long-term Debt (continued)**

On August 1, 2014 NMMEAA refunded the Series 2009 bonds with Series 2014 Refunding Bonds for an initial 5 year period with a potential to continue beyond 5 years.

With the bond refunding in August, 2014 NMMEAA replaced the original interest rate swap transactions with another rate swap transaction in which the interest rate swap counterpart (RBC) pays NMMEAA a floating amount equal to the amount of interest due on the 2014B Bonds each interest payment date, and NMMEAA pays RBC a fixed amount on each date based on a fixed rate of 1.89403% on the principal amount of the 2014B Bonds then outstanding on such date.

Long-term debt at June 30, 2018 and 2017 consisted of the following:

	<u>FY 2018</u>	<u>FY 2017</u>
<b>Revenue Bonds:</b>		
New Mexico Municipal Energy Acquisition Authority Gas Supply Revenue Bonds, Sub-series 2014A	\$ 175,000,000	\$ 175,000,000
New Mexico Municipal Energy Acquisition Authority Gas Supply Revenue Bonds, Sub-series 2014B (Variable Rate)	487,350,000	507,755,000
Less current maturities of long-term debt	<u>(21,900,000)</u>	<u>(20,405,000)</u>
Long-term debt	<u>\$ 640,450,000</u>	<u>\$ 662,350,000</u>

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 4: Long-term Debt (continued)**

**Changes in Long-term Liabilities**

During the years ended June 30, 2018 and 2017, the following changes occurred in long-term liabilities:

	<u>Balance</u> <u>June 30, 2016</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2017</u>	<u>Due Within</u> <u>One Year</u>
Total Revenue Refunding Series 2014	701,810,000	-	(19,055,000)	682,755,000	20,405,000
Bond Premium	14,789,250	-	(4,929,750)	9,859,500	4,929,750
	<u>\$ 716,599,250</u>	<u>\$ -</u>	<u>\$ (23,984,750)</u>	<u>\$ 692,614,500</u>	<u>\$ 25,334,750</u>
	<u>Balance</u> <u>June 30, 2017</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2018</u>	<u>Due Within</u> <u>One Year</u>
Total Revenue Refunding Series 2014	\$ 682,755,000	-	(20,405,000)	\$ 662,350,000	\$ 21,900,000
Bond Premium	9,859,500	-	(4,929,750)	4,929,750	4,929,750
	<u>\$ 692,614,500</u>	<u>\$ -</u>	<u>\$ (25,334,750)</u>	<u>\$ 667,279,750</u>	<u>\$ 26,829,750</u>

Revenue Bond Series 2009 was refunded with Gas Supply Revenue Refunding Bonds, Series 2014, consisting of Sub-Series 2014A with a principal amount of \$175,000,000 and a fixed interest rate of 5%, and Sub-series 2015B with fixed rate notes (FRNs) with hard maturities and a principal amount of \$98,545,000 and FRNs with hard puts and a principal amount of \$453,450,000 with hard maturities. All FRNs have a coupon rate of 1.89403%. The refunding was made for RBC to comply with regulatory liquidity requirements. It did not result in an economic gain to NMMEA.

Future principal and interest payments required to be made are as follows:

<b>Year Ending June 30,</b>	<b>Principal</b>	<b>Fixed Interest</b> <b>Hard Put/Hard Maturity</b> <b>@ 1.89403%; Fixed @ 5%</b>	<b>Total Debt</b> <b>Service</b>
2019	21,900,000	17,702,133	39,602,133
2020	640,450,000	5,109,647	645,559,647
	<u>\$ 662,350,000</u>	<u>\$ 22,811,780</u>	<u>\$ 685,161,780</u>



**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 5: Related Party Transactions**

NMMEAA's natural gas sales to members during the year ended June 30, 2018 were as follows: \$561,350 to the City of Las Cruces, \$9,151,988 to the City of Farmington and \$1,611,566 to Los Alamos County. At June 30, 2018, receivables due from members were as follows: \$14,962 from the City of Las Cruces, \$630,225 from the City of Farmington and \$25,434 from Los Alamos County.

NMMEAA's natural gas sales to members during the year ended June 30, 2017 were as follows: \$698,245 to the City of Las Cruces, \$11,184,738 to the City of Farmington and \$2,019,177 to Los Alamos County. At June 30, 2017, receivables due from members were as follows: \$21,931 from the City of Las Cruces, \$926,475 from the City of Farmington and \$37,284 from Los Alamos County.

**Note 6: Gas Purchase and Sales Agreements**

NMMEAA has entered into long-term gas purchase and supply contracts for which prepayments have been made and amounts remaining of \$538,197,508 and \$562,893,857 at June 30, 2018 and 2017, respectively. Current amounts due as of June 30, 2018 and 2017 were \$24,696,348 and \$24,774,643, respectively. Amounts remaining at Long-term sales agreements also exist with customers, to take delivery of natural gas over a period continuing through 2039. The sale price to the customer for these contracts is at specified index prices less a discount. As discussed in Note 7, swap agreements are used to convert these variable index prices to fixed prices sufficient to meet debt service requirements.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments**

***Composition of Derivative Instruments***

The fair value balances and notional amounts of derivative instruments outstanding as of June 30, 2018 and 2017, classified by type, are as follows:

	<b>Notional Amount</b>		<b>Fair Value</b>	<b>Counterparty Credit Rating</b>
<u>June 30, 2018</u>				
Positive cash flow:				
Natural gas commodity swap	122,550,032	MMBtu	\$ 570,005,853	Aa2
Net positive cash flow:				
Pay fixed interest rate, receive variable	\$ 487,350,000		\$ 2,433,129	Aa2
 <u>June 30, 2017</u>				
Positive cash flow:				
Natural gas commodity swap	128,155,195	MMBtu	\$ 560,980,943	Aa2
Net negative cash flow:				
Pay fixed interest rate, receive variable	\$ 507,755,000		\$ (1,471,199)	A1

All fair values are classified as derivative instruments on the statements of net position. The increase in fair values of the natural gas commodity swap derivative instrument were \$9,024,910 and \$26,028,333 for 2018 and 2017, respectively. The fair value of the interest rate swap at June 30, 2018 was \$2,433,129, with an increase in fair value \$3,904,328 from the previous fiscal year end. For fiscal year 2017, the fair value increased \$9,736,463. As these commodity and interest rate swaps are considered effective hedging derivative instruments, the change in fair value is reflected within deferred outflows and inflows on the statements of net position. The positive and negative fair values of the commodity and interest rate swaps are not netted when the swaps were entered into with different counterparties. The fair values of the commodity swaps are based on forward prices from established indexes for the applicable region and discounted using established rate indexes. The fair values of the interest rate swaps are based on the future yield curve for tax-exempt bonds and discounted using established rate indexes.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

Derivative instruments are utilized by NMMEAA to manage market risk and reduce its exposure resulting from fluctuations in prices of natural gas in order to meet debt service requirements. These instruments include a commodity swap agreement which converts index-priced natural gas revenues to fixed prices for servicing outstanding debt obligations and an interest rate swap with two transactions which effectively convert NMMEAA's variable interest rate to a synthetic fixed rate. Effective with fiscal years beginning after June 15, 2009, GASB Statement No. 53 requires that the fair value of financial arrangements called "derivatives" or "derivative instruments" be reported in the financial statements of state and local governments. If a derivative effectively hedges, or significantly reduces the risk of rising or falling cash flows or fair values, then its annual fair value changes are deferred until the hedged transaction occurs or the derivative ceases to be effective. According to GASB 53, a derivative is defined as a financial arrangement with values or cash payments that are based on what happens in separate transactions, agreements, or rates and have these characteristics:

- The financial arrangements are leveraged. There is minimal or no initial investment, but the arrangement achieves changes in fair value that would have required a far larger investment.
- The financial arrangement can be settled early with a cash payment or the transfer of an equivalent asset.

Even though governments enter into a derivative to minimize an identified risk, the derivative itself can expose the government to the following risks:

- Credit risk is the chance the counterparty to a swap agreement will not make good on its promise to pay the government.
- Interest rate risk refers to the idea that the longer a derivative is in place the greater the potential is that changes in interest rates could reduce the value of the transaction to the government.
- Termination risk refers to a derivative ending earlier than planned, thereby depriving a government of risk protection and potentially requiring a significant termination payment. This can happen if the credit rating of either the government or the counterparty falls below the agreed upon level.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

- Basis risk is the idea that in some derivatives the amount received by the government from the counterparty is based on one market rate, and the amount it pays to bondholders is based on another index. An example of this is one payment being based on the Securities Industry and Financial Markets Association (SIFMA) index and the other payment based on the London Interbank Offered Rate (LIBOR). If the rate on which the bondholder payments going out increases more than the rate determining the receipts to the government, less money will be received than payments going out.
- Rollover risk happens when the derivative does not last as long as the associated debt is outstanding. This would happen if the interest rate swap was for 15 years, but the variable rate debt was for 30 years. At the end of the 15 years, the government may not be able to get another interest rate swap derivative and would no longer be protected from rising interest rates.
- Market-access risk is the chance a government will not be able to issue debt, or in doing so it would become more expensive.
- Foreign currency risk is the chance that changes in foreign exchange rates will adversely affect the value of the derivative if it is denominated in a foreign currency.

As of June 30, 2018 NMMEAA had the following derivative instruments:

Item	Type	Objective	Notional Amount	Effective Date	Maturity Date	Terms	Fair Value
A	Natural gas commodity swap	To enable NMMEAA to receive a fixed revenue stream with respect to the sale of the entire gas supply delivered under the prepaid gas agreement.	122,550,032 MMBtu	October 1, 2009	September 30, 2039	Receive fixed price, pays Inside FERC El Paso SJ index	\$ 570,005,853
B	Pay-fixed interest rate swap	Hedge exposure to interest rate fluctuations on bonds and match with expected revenues from supply agreements and the commodity swap.	\$ 487,350,000	August 1, 2014	August 1, 2019	Pay fixed coupon rate of 1.89403% and receive variable rate equal to interest rate to bond holders	\$ 2,433,129

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

The fair value of the commodity swap was provided by the commodity swap counterparty, J.P. Morgan Chase Bank NA. The fair value of the interest rate swap was provided by the interest rate swap counterparty, Royal Bank of Canada (RBC).

Item	Type	Changes in Fair Value		Fair Value at June 30, 2018		Notional Amount
		Classification	Amount	Classification	Amount	
A	Natural gas commodity swap	Deferred inflow	\$ 9,024,910	Derivative instruments	\$ 570,005,853	122,550,032 MMBtu
B	Pay fixed interest rate swap	Deferred outflow	\$ 3,904,328	Derivative instruments	\$ (2,433,129)	\$ 487,350,000

NMMEAA evaluated the effectiveness of its derivative instruments using the consistent critical terms method. Following are tables showing the derivative instruments and critical terms of the hedging instrument and the item that it is hedging. Since the critical terms are the same it is assumed the instruments are effective, and any changes in the fair value are deferred in fiscal year 2018.

Consistent Critical Terms	Commodity Swap NMMEAA and J.P. Morgan	Natural Gas Supply Agreements (COF,LA,LC with NMMEAA) - is Revenue in NMMEAA	Prepaid Natural Gas Purchase and Sale Agreement NMMEAA and RBC
Commodity	Natural Gas	Natural Gas	Natural Gas
Beginning Gas Delivery Date	October 1, 2009	October 1, 2009	October 1, 2009
Ending Gas Delivery Date	September 30, 2039	September 30, 2039	September 30, 2039
Notional Total Quantity Gas (MMBtu)	171,322,165	171,322,165	171,322,165
Natural Gas Spot Market Index	Inside FERC Gas Market Report El Paso San Juan Basin Index	Inside FERC Gas Market Report El Paso San Juan Basin Index	Inside FERC Gas Market Report El Paso San Juan Basin Index
Price	Swap counterparty pays fixed price per Appendix A-1,2,3; NMMEAA pays at inside FERC; Amt is netted	Index-discount+premium	\$4.406 per MMBtu fixed
Delivery Point (#1) City of Farmington (COF)gas	The interconnection between Transwestern and Public Service Company of New Mexico with the Transwestern Blanco Hub	The interconnection between Transwestern and Public Service Company of New Mexico with the Transwestern Blanco Hub	The interconnection between Transwestern and Public Service Company of New Mexico with the Transwestern Blanco Hub
Delivery Point (#2) Las Cruces (LC) gas	El Paso Natural Gas Company's Blanco Pool, DRN 216748	El Paso Natural Gas Company's Blanco Pool, DRN 216748	El Paso Natural Gas Company's Blanco Pool, DRN 216748
Delivery Point (#3) Los Alamos (LA) gas	El Paso Natural Gas Company's Blanco Pool	El Paso Natural Gas Company's Blanco Pool	El Paso Natural Gas Company's Blanco Pool

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

Consistent Critical Terms	Interest Rate Swap	Variable-Rate Bonds
Notional Amount (Debt outstanding Sub-Series 2014 B at June 30, 2018)	\$ 487,350,000	\$ 487,350,000
Effective Date	August 1, 2014	August 1, 2014
Maturity Date	August 1, 2019	August 1, 2019
Variable interest rate	Bond interest rate (calculated by Remarketing Agent)	calculated by Remarketing Agent
Variable rate reset dates	1st of month	1st of month
Frequency of rate resets	Monthly	Monthly

**Risks**

*Credit risk:* NMMEAA's derivative instruments are held with two separate counterparties. Should the credit rating drop below A2 as issued by Moody's Investors Service, collateral must be posted. On July 1, 2010, J.P. Morgan Chase Bank NA became the commodity swap counterparty due to a drop in the credit rating of the original commodity swap counterparty, BPCNA. On June 21, 2016, Moody's Investor Services downgraded both counterparties to the NMMEAA derivative instruments two notches, but with a stable outlook, due to significant exposure to the volatility and risk of outsized losses from the firms' global capital market operations. As a result of the downgrade, Moody's also downgraded the NMMEAA Gas Supply Variable Rate Revenue Bonds, Series 2009, to Aa3 from Aa1. In July 2018, Moody's upgraded the bond to Aa2.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

Derivative Instrument	Type	Counterparty	Required Credit Rating of Counterparty (Moody's)	Actual Credit Rating of Counterparty (Moody's) on June 30, 2018	Counterparty Collateral Posted with NMMEAA
A	Natural gas commodity swap	J.P. Morgan Chase Bank NA	A2	Aa2	\$ -
B	Pay-fixed interest rate swap	Royal Bank of Canada (RBC)	A2	Aa2	\$ -

The aggregate fair value of hedging derivative instruments in asset positions at June 30, 2018 and 2017 was \$572,438,982 and \$560,980,943. This represents the maximum loss that would be recognized at the reporting date if all counterparties failed to perform as contracted.

*Interest rate risk:* NMMEAA is exposed to interest rate risk on its interest rate swap. NMMEAA pays a fixed interest rate and receives a variable rate equal to the bondholder rate. NMMEAA also pays a fixed interest rate of 5% on Sub-Series 2014A, and a fixed coupon rate of 1.89403% on Sub-Series 2014B.

*Basis risk:* NMMEAA is not exposed to basis risk on its fixed interest rate swap because the variable rate payment received is based on the LIBOR index and so is the bond interest payment.

*Termination risk:* NMMEAA or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. Each party is only required to pay the other party the amounts owed under the contract.

*Rollover risk:* NMMEAA is not exposed to rollover risk because the hedging derivative instruments mature at the same time as the items they hedge.

**New Mexico Municipal Energy Acquisition Authority**  
**Notes to Financial Statements**  
**June 30, 2018**

**Note 7: Derivative Instruments (continued)**

***Fair value measurement***

NMMEAA categorizes its derivative instruments within the fair value hierarchy established by generally accepted accounting principles as follows:

NMMEAA utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels:

**Level 1** consist of quoted prices (unadjusted) in the active markets for identical assets or liabilities accessible at the measurement date.

**Level 2** include inputs other than quote prices in Level1 directly or indirectly observable for the assets or liabilities.

**Level 3** are unobservable inputs for the assets or liabilities.

All of NMMEAA's derivative instruments are classified within Level 2 of the valuation hierarchy.

**Note 8: Significant Estimates and Concentrations**

Generally accepted accounting principles require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

**Major Suppliers**

NMMEAA purchased all of its natural gas supply from one national gas supplier. The total value of prepaid gas purchased from this supplier was \$538,197,508 and \$562,893,857 as of June 30, 2018 and 2017 respectively. The total cost of goods sold associated with this gas supply was \$24,696,348 for the years ended June 30, 2018 and 2017. There are a limited number of national gas suppliers in which NMMEAA could contract with under prepay gas transactions and any disruption of deliveries under the supply contracts could have an impact on NMMEAA's operations.

**Current Economic Conditions**

The current protracted economic decline continues to present energy companies with difficult circumstances and challenges, which in some cases have resulted in large declines in the fair value of financial instruments and other assets, declines in revenues, constraints on liquidity and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to NMMEAA.



## **OTHER INFORMATION**

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON  
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Directors  
New Mexico Municipal Energy Acquisition Authority  
and  
Wayne Johnson, State Auditor

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of the New Mexico Municipal Energy Acquisition Authority (NMMEAA) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise NMMEAA's basic financial statements, and the related budgetary comparison and have issued our report thereon dated December 14, 2018.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered NMMEAA's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of NMMEAA's internal control. Accordingly, we do not express an opinion on the effectiveness of NMMEAA's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, described in the accompanying schedule of findings and responses as item 2017-001 that we consider to be a significant deficiency.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether NMMEAA's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## NMMEAA's Response to Findings

NMMEAA's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. NMMEAA's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

## Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Albuquerque, New Mexico  
December 14, 2018



## **New Mexico Municipal Energy Acquisition Authority Schedule of Findings and Responses Year Ended June 30, 2018**

### **2017-001 Lack of Segregation of Duties and Accounting System, Significant Deficiency (Repeated and Modified)**

*CONDITION:* The Authority relies on one individual to perform all accounting functions. They do not rely upon a general ledger system of any kind, therefore all financial activity is being maintained within an excel workbook that is not regularly reviewed.

The Authority did not make progress in resolving this finding in the current year. The City of Farmington is currently in active recruitment to replace the senior accountant that was in charge of business operations and hopes to have that position filled by the end of the current fiscal year

*CRITERIA:* Good accounting practices require the Authority to implement and follow sound accounting and internal control policies and procedures including segregation of duties over significant transaction cycles. Effective internal controls assist in demonstrating the ability to record, process, summarize and report transactions and support financial statement assertions of completeness. The COSO Internal Control - Integrated Framework outlines the components, principles, and factors necessary for an organization to effectively manage its risks through the implementation of internal control. Insufficient control activities increase the risk of misappropriation of assets.

*CAUSE:* The Authority has not invested in purchasing a formal accounting system and have not hired a replacement for a manager that retired during fiscal year 2017.

*EFFECT:* The Authority has an increased risk of inaccurate or incomplete financial reporting.

*RECOMMENDATION:* Management should consider recording all financial transactions in a formal general ledger system by performing journal entries. Such entries should be subjected to another level of review from the person responsible for posting the entry. All sub ledgers and general ledger activity should be reviewed periodically.

*MANAGEMENT'S RESPONSE:* Management acknowledges the necessity of good internal control, part of which includes independent transactional review. We would need to evaluate the practicality of setting up a complete General Ledger system of the volume and nature of NMMEAA transactions. NMMEAA thinks the more important control feature would be that independent review of transactions. NMMEAA has contracted with the City of Farmington to perform the business operations and accounting for the entity, and would rely on their internal process for determining the best process, method, and system for recording transactions. If the City of Farmington feels implementation of a formal GL system would facilitate accurate and timely record keeping, the recommendation and cost of implementation would be included in the budget they propose for the Business Operations function they perform, for consideration by the Board.

In any case, it is an expectation of the Board that the City of Farmington implement good internal controls, which would include transactional review. The City of Farmington will develop the action plan by the end of the fiscal year as to how and in what time frame they propose to accomplish that, for consideration by the Board.

*CORRECTIVE ACTION PLAN:* The City of Farmington is currently in active recruitment to replace our senior accountant that was in charge of business operations and hopes to have that position filled by the end of the current fiscal year. Once filled, that person will do a full analysis of business practices and make recommendations as to how to ensure all transactions are properly recorded and reviewed. In the meantime, the City of Farmington is implementing a monthly review by senior accounting staff of all transactions to ensure they are captured and recorded timely and properly". Person Responsible: Board Chair.

**New Mexico Municipal Energy Acquisition Authority  
Status of Prior Year Audit Findings  
Year Ended June 30, 2018**

**2017-001 Lack of Segregation of Duties and Accounting System, (Significant Deficiency)  
- Repeated and Modified**

**2017-002 Late Audit Report (Compliance and Other Matters) – Resolved**

**New Mexico Municipal Energy Acquisition Authority  
Exit Conference  
Year Ended June 30, 2018**

An exit conference was held on December 13, 2018. In attendance were:

**NMMEAA**

Brandon Hill, Treasurer  
Jorge Garcia, Vice Chair Person  
Mario Puentes, Alternate Member

**Axiom CPAs and Business Advisors LLC**

Tyler Marshall, Supervisor