U.S. Department of Energy
Office of Inspector General
Office of Audits and Inspections

Audit Report

The Department's Implementation of Financial Incentive Programs under the Energy Efficiency and Conservation Block Grant Program

OAS-RA-L-13-02

December 2012

Department of Energy

Washington, DC 20585

December 3, 2012

MEMORANDUM FOR THE PROGRAM MANAGER, WEATHERIZATION AND INTERGOVERNMENTAL PROGRAM

FROM: George W. Collard
Assistant Inspector General
for Audits
Office of Inspector General

SUBJECT: INFORMATION: Audit Report on "The Department's Implementation of Financial Incentive Programs under the Energy Efficiency and Conservation Block Grant Program"

BACKGROUND

The Department of Energy's (Department) Energy Efficiency and Conservation Block Grant (EECBG) Program, funded for the first time by the American Recovery and Reinvestment Act of 2009, was intended to help US cities, counties and states develop, promote, implement and manage energy efficiency and conservation projects. The EECBG Program received $3.2 billion in Recovery Act funding for competitive and formula grants. Of the $3.2 billion, approximately $284 million was designated by EECBG recipients for financial incentive programs.

Financial incentive programs include both lending and credit enhancement initiatives. Lending programs provide financing to borrowers, commonly through revolving loan funds. Credit enhancement programs use loan loss reserves, interest rate buy-downs or loan loss insurance to reduce a lender's risk. Both types of programs can be administered by the recipient or by a third-party contractor, e.g., a bank, credit union or community development financial institution.

Since the inception of the Recovery Act, the Office of Inspector General has conducted a series of reviews on the EECBG Program which have identified various weaknesses. In particular, as noted in our report *The Status of Energy Efficiency and Conservation Block Grant Recipient's Obligations*, (OAS-RA-11-16, September 2011), $879 million of the $2.7 billion in formula-based grant funding provided by the Department, or nearly one-third, remained unobligated by recipients at the time of our review. The Department has since focused aggressively on encouraging recipient spending and recipient obligations through phone calls and in-person outreach efforts. In light of the identified weaknesses and the risks inherent in establishing a large new program of national significance, we initiated this audit to determine whether the Department had managed its EECBG financial incentive programs efficiently and effectively.

CONCLUSIONS AND OBSERVATIONS

The Department had taken a number of positive steps to implement and administer EECBG financial incentive programs to ensure accountability for Recovery Act funding and compliance with laws and regulations. For example, with the launch of the Recovery Act, the Department introduced the Solution Center, an online portal for technical assistance resources that included best practices, templates, online trainings and webcasts. However, our review found two major challenges in ensuring the effectiveness of the EECBG financial incentive programs. These challenges included:

- Ensuring grant recipients were on track to meet expenditure goals for their financial incentive programs prior to the end of their grant periods; and,

- Finalizing grant recipient guidance on their responsibilities for long-term monitoring and reporting of financial incentive programs funding.

We found that the Department understood these challenges and had taken action to address them. Additionally, we noted that the Department had identified and was taking action to address a problem with one recipient that had not complied with Federal requirements to segregate Recovery Act funds from other funding sources in its accounting system.

Status of Selected Recipient Expenditures

We found that two of the five recipients we reviewed had experienced difficulties in meeting expenditure goals for financial incentive programs. Specifically:

- As of August 2012, one recipient reported expending only about $660,000 of the total $6.3 million (10.5 percent) in funding allocated to its financial incentive program despite being more than two-thirds through its 36-month award period. The program included credit enhancements paid to third-party lenders for loans made to finance borrowers' retrofits of existing buildings or homes to increase their overall energy efficiency. The recipient reported that over the last several months, in an effort to increase expenditures, it put in place collaboration agreements with local utility companies to expand existing loan and rebate programs. The recipient expects that all EECBG funds will be spent by the end of the grant period, or May 31, 2013; and,

- Another recipient had only expended about $178,000 of the total $351,860 (49.7 percent) allocated to its revolving loan fund as of August 2012, with less than 2 months left under the award. The recipient stated that its proposal to repurpose unused funds to another activity was approved by the Department in September 2012.

Even though the Department had provided program guidance to recipients throughout the grant period, recipients indicated that they had experienced difficulties in expending funds for various reasons. For example, one official noted that even at low interest rates, potential borrowers were reluctant to take on additional debt because of economic conditions. While we acknowledge that valid reasons may have existed, the slow pace and pressure of spending funds within the period of performance may potentially affect the Department's ability to meet the goals of the Recovery Act.

To address the challenges in meeting expenditure goals, during the course of our review and in response to a previous Office of Inspector General recommendation, the Department conducted an initial assessment of recipients' financial incentive programs[1], including data collection and analyses of dollars spent to date and factors impacting lending environments. The results of the assessment were being used to evaluate the relative success of the programs within the award period. Additionally, the Department used the data to determine whether funds needed to be reprogrammed or if no-cost time extensions needed to be put in place prior to the end of the award period. Through October 2012, the Department had granted 324 no-cost extensions ranging from 6 to 14 months, of which 63 included financial incentive programs. Continued Department oversight is needed to meet Recovery Act goals.

Long-Term Monitoring and Reporting

We noted the Department had not initially developed a plan to address long-term monitoring and reporting of financial incentive programs. These types of program funds have the potential to remain under the control of the recipient well beyond the expiration of the Recovery Act award. For example, revolving loan funds are structured so that repayments can be used to make more loans. Additionally, loan loss reserve funds are placed in escrow until expended as result of borrower defaults.

According to Department guidance, Federal funds, as described above, generally retain their Federal character in perpetuity. As a result, Federal requirements apply for the life of a revolving loan fund, as funds are paid back by existing borrowers and then lent out to new borrowers. Additionally, Federal requirements apply to residual funds from loan loss reserves that are returned by lenders because they are not needed to offset loan defaults. Accordingly, monitoring and reporting requirements will remain in force until funds are completely exhausted (through loan defaults and interest rate buy-downs) or returned to the Federal government.

During the course of our audit, the Department began working with the Office of General Counsel and the Office of Management and Budget to develop guidance on periodic long-term monitoring and financial incentive program reporting. Examples of reporting information under consideration included the number and dollar amount of loans issued, paid back, and defaulted. In mid-October 2012, the Department issued final guidance to recipients on periodic long-term monitoring and financial incentive program reporting. While we agree that this represents a positive step, the Department will need to provide oversight of recipient compliance with the long-term monitoring and reporting responsibilities.

Accountability For EECBG Funds

One of the five recipients we reviewed had not properly segregated EECBG funds, as required by the Recovery Act. Specifically, the recipient had deposited over $350,000, the total amount allocated to its revolving loan fund, into a pre-existing bank account already used to fund loans to low income homeowners. Additionally, it had not set up a separate account for the EECBG funds within its accounting system. While the recipient maintained a record of EECBG loans outside of its accounting system, it could not provide any reconciliations of revolving loans funded by the Recovery Act grant to the amount of such funds remaining in the bank account.

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[1]In our report *The Status of Energy Efficiency and Conservation Block Grant Recipient's Obligations*, (OAS-RA-11-16, September 2011), we recommended the Department complete an analysis to identify those recipients who were unlikely to expend funds within the grant period and consider alternatives for managing EECBG Recovery Act funds.

Under the terms and conditions of its award, the recipient was prohibited from commingling EECBG funds with any other funds and was required to revise its financial and accounting systems to segregate, track, and maintain these funds apart and separate from other revenue streams.

In September 2011, the Department conducted a site visit and found that a separate EECBG fund had not been set up within the recipient's accounting system. Even though the recipient subsequently indicated it had established a new accounting system which would allow for (future) segregation of EECBG funds, officials stated that they did not have the manpower, nor were they going to conduct a formal reconciliation of the previously comingled funds. By not reconciling these (previously comingled) funds, we remain concerned that the goals of the Recovery Act may not have been met, and funds may not have been spent on approved EECBG projects.

Path Forward

Given the significance of the Recovery Act, we believe the Department should continue monitoring project performance to ensure that funds are expended to meet Recovery Act goals and requirements.

SUGGESTED ACTIONS

To address the issues identified in this report and improve management of EECBG financial incentive programs, we suggest that the Program Manager for the Weatherization and Intergovernmental Program:

1. Continue to collect and analyze recipient data in an effort to ensure financial incentive programs are successful and unused funds are returned or reprogrammed to other programs;

2. Continue to provide oversight of grant recipients to ensure compliance with long-term monitoring and reporting responsibilities; and,

3. Ensure recipient accounting systems properly account for EECBG funds and corrective actions are addressed in a timely manner.

We appreciate the cooperation of the Department and its on-going efforts. Because no recommendations are being made in this report, a formal response is not required.

Attachments

cc: Deputy Secretary
Associate Deputy Secretary
Acting Under Secretary of Energy
Assistant Secretary for Energy Efficiency and Renewable Energy
Acting Deputy Chief Financial Officer
Chief of Staff

OBJECTIVE, SCOPE AND METHODOLOGY

OBJECTIVE

The objective of this audit was to determine whether the Department of Energy (Department) had managed its Energy Efficiency and Conservation Block Grant (EECBG) Program financial incentive programs efficiently and effectively.

SCOPE

The audit was performed between September 2011 and November 2012, at Department Headquarters in Washington, DC. In addition, we visited five recipients that were awarded six grants including: (1) City of Portland, Oregon; (2) City of Providence, Rhode Island; (3) Clackamas County, Oregon; (4) State of South Dakota Department of Tourism and State Development in Pierre, South Dakota; and, (5) Executive Office of the State of New Hampshire in Concord, New Hampshire.

METHODOLOGY

To accomplish the audit objective we:

- Obtained and reviewed relevant laws and regulations related to the implementation of the American Recovery and Reinvestment Act of 2009 (Recovery Act), EECBG Program, and financial incentive programs;

- Reviewed individual grant award files from the Department's Strategic Integrated Procurement Enterprise System;

- Obtained and reviewed selected recipient's policies and procedures related to the administration of financial incentive programs;

- Interviewed Department and selected recipient officials to determine actions taken to implement and administer EECBG financial incentive programs;

- Interviewed officials from third-party administrators contracted to manage selected recipient's financial incentive programs; and,

- Obtained and analyzed documentation from selected recipient and third-party administrators to determine the eligibility of funded projects and the progress made in implementing financial incentive programs.

We conducted this performance audit in accordance with generally accepted Government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Accordingly, we assessed significant internal controls and compliance with laws and regulations necessary to satisfy the audit objective. In particular, we assessed the Department's implementation of the *GPRA Modernization Act of 2010* and found the Department had established performance measures related to the EECBG Program. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We conducted an assessment of computer-processed data relevant to our audit objective and found it to be reliable.

Management waived an exit conference.

PRIOR AUDIT REPORTS

Under the American Recovery and Reinvestment Act of 2009, the Office of Inspector General has initiated a series of audits designed to evaluate the Department's Energy Programs. Our series of audit reports include the following:

- Audit Report on *The Department of Energy's Energy Efficiency and Conservation Block Grant Program Funded under the American Recovery and Reinvestment Act for the City of Philadelphia* (OAS-RA-12-09, April 2012).

- Audit Report on *The State of Nevada's Implementation of the Energy Efficiency and Conservation Block Grant Program* (OAS-RA-12-02, November 2011).

- Management Alert on *The Status of Energy Efficiency and Conservation Block Grant Recipients' Obligations* (OAS-RA-11-16, September 2011).

- Audit Report on *The Department of Energy's Energy Efficiency and Conservation Block Grant Program Funded under the American Recovery and Reinvestment Act for the State of Pennsylvania* (OAS-RA-L-11-11, September 2011).

- Audit Report on *The Department of Energy's American Recovery and Reinvestment Act – California State Energy Program* (OAS-RA-11-10, July 2011).

- Audit Report on *The Department of Energy's Energy Implementation of the Energy Efficiency and Conservation Block Grant Program under the Recovery and Reinvestment Act: A Status Report* (OAS-RA-10-16, August 2010).

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