State Auditor's Office Performance Audit

Department of Commerce

State Energy Program

American Recovery and Reinvestment Act of 2009

June 13, 2011

Washington
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State Auditor

Report No. 1005601

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Why we did this audit

When they enacted the American Recovery and Reinvestment Act in early 2009, the President and Congress directed recipients of stimulus funds to award and spend the money as quickly as possible to maximize the Act's economic impact. Agencies like the State Department of Commerce, which had to execute a complex grant management program in an unusually short time, were forced to take actions — and to forego some actions — that they might have handled differently if their deadlines had not been so tight.

In this environment, a thorough, independent audit allows decision-makers and program managers to review program management and processes to identify opportunities for improvement.

Grant management is a core government function. Washington state operates dozens of grant programs that support public health and safety, social services, education, community development and other high-priority services. Lessons learned from our audit of the State Energy Program can and should be applied to other, similar programs across state government.

To find out more about the American Recovery and Reinvestment Act Act of 2009 go to: www.recovery.gov

To evaluate the Department of Commerce's administration of the program, we identified a checklist of management practices for competitive funding programs that have proven effective in Washington state and elsewhere. These "sound practices " are referenced throughout this report and are presented in **Appendix E**.

One of our goals in conducting this audit was to generate information that managers of other, similar state and local government programs could use to improve the efficiency, effectiveness and accountability of their own operations.

Why we selected the state energy program

As of March 31, 2011, Washington had received more than $8 billion in grants, loans, and contracts through the American Recovery and Reinvestment Act of 2009, about 43 percent of which went to state agencies.

Many state programs that received Recovery Act money were well-established and able to handle the influx with relatively little disruption to their normal operations. However, in some cases the new funds represented such a large increase that administrators had to change the nature of their programs to meet strict federal deadlines for distributing and spending the money.

For example, the State Energy Program budget within the Department of Commerce jumped from an average of less than $1 million per year to $60.9 million available for spending from April 2009 through March 2012. As a result, the program expanded from focusing almost exclusively on policy analysis to awarding millions of dollars in grants and loans to businesses and public agencies.

We audited the largest segment of the State Energy Program — the Energy Efficiency and Renewable Energy Loan and Grant Program — because it received more than half of the new program funds and, like all stimulus recipients, faced tight timelines and strict accountability requirements for awarding the money. Based on our risk assessment, we concluded there was a relatively higher risk this program would not achieve the Recovery Act goals.

We conducted the audit to answer the following specific question:

- **Has Commerce established and followed sound processes to award state energy grants and loans, monitor recipients' use of funds and determine if specific program outcomes are achieved?**

During the audit, work on the awarded projects was just getting started. For that reason, we did not audit program outcomes and instead focused on how the State Energy Office awarded and monitored the contracts.

Audit results

Commerce's State Energy Office followed most of the sound practices we identified for competitive loan and grant programs, and program managers met the requirement to obligate all $38.5 million of the stimulus funds by September 30, 2010. For example:

- **The Office's requests for proposals generated** more than 120 proposals that met all minimum qualifications, which is evidence of a strong competitive process.
- **The staff organized evaluation teams** of energy experts to evaluate the proposals.
- **After awarding the funds, the staff developed** project contracts that, in most cases, followed the sound practices we identified.

However, in an effort to meet tight federal funding deadlines, the staff did not follow some sound practices in awarding the funds. For example, the staff:

- **Did not establish specific written policies and procedures** for awarding program funds, as required.
- **Narrowed the scope of work** for three projects from the original proposals to the final contracts.
- **Did not document pre-award risk assessments or conduct reference checks** that might have identified potential problems with a proposed project and averted the need for them to later withdraw the funding award.
- **Did not receive all of the information** they will need to ensure they can appropriately monitor and oversee the completion of the projects.
- **Did not achieve a program goal** to award two-thirds of the stimulus funds as loans instead of grants. As a result, the amount of funds to be repaid will be less than initially planned, which will in turn reduce the amount of revolving funds available for future energy projects.

Summary of recommendations

We identified several opportunities for Commerce and the State Energy Office to improve the program's administration:

- **To ensure the program operates consistently** and transparently, we recommend the Office establish specific written policies and procedures for this program and clearly document its grant processes and award decisions.
- **To ensure funds are awarded fairly and transparently** in the future, we recommend the staff develop project contracts that reflect the original proposals and not significantly narrow their scope.
- **To promote accountability**, we recommend the Office's project contracts include clear standards for measuring the award recipients' performance to ensure that final project outcomes are known and that recipients are accountable for expected job creation and retention and energy savings.
- **To ensure funds are invested effectively and efficiently**, we recommend the Office place a greater emphasis on identifying and assessing risks throughout the funding process.

What's next?

Audits of state agencies and programs are reviewed by the Joint Legislative Audit and Review Committee (JLARC) and other legislative committees whose members wish to consider findings and recommendations on specific topics.

Representatives of the State Auditor's Office will review this audit with JLARC's Initiative 900 Subcommittee in Olympia. The public will have the opportunity to comment at this hearing.

The Department of Commerce will determine whether to accept the audit recommendations. The State Auditor's Office conducts periodic follow-up evaluations to assess the status of recommendations and may conduct follow-up audits at its discretion.

Audit overview

As of March 31, 2011, Washington received more than $8 billion in grants, loans, and contracts funded by the American Recovery and Reinvestment Act. Approximately 43 percent of the money went directly to state agencies for specific programs, including grants and loans to governments, nonprofit organizations and businesses. Recipients of Recovery Act funds, including states, local governments and businesses, must meet the performance and accountability standards specified in the legislation to ensure stimulus funds achieve the economic goals established by the President and Congress.

The Legislature and Governor directed most of Washington's $60.9 million in State Energy Program funding — $38.5 million — to the Energy Efficiency and Renewable Energy Loan and Grant Program in the 2009-11 state operating budget. This program is designed to help public and private organizations develop energy efficiency, clean technology and renewable energy projects. We audited the loan and grant program's fiscal year 2010 operation to answer the following question:

- **Has Commerce established and followed sound processes to award state energy grants and loans, monitor recipients' use of funds and determine if specific program outcomes are achieved?**

Audit scope and methodology

We audited the State Energy Program primarily because of the Recovery Act's dramatic impact on its size and scope and because of the tight timelines for Commerce to award a large amount of funds. Based on our risk assessment, we concluded there was a relatively higher risk this program would not be able to achieve the Recovery Act goals.

We chose the Energy Efficiency and Renewable Energy Loan and Grant Program because it received the majority of energy-related Recovery Act funds and because it is designed to benefit from Recovery Act funds into the future. A portion of the funding was awarded in the form of loans, and when they are repaid with interest, the money can be applied to future energy projects. For this reason, our audit recommendations could have relatively long-term benefits.

We analyzed whether the mix of loan and grant funding met program goals included in federal agreements. We also examined a sample of contracts to see whether the Office's soliciting, awarding and contracting operations were aligned with sound practices. We were not able to compare operations to Office policies and procedures because the Office had not established specific written policies and procedures for this program. Given the newness of this program, our analysis of project monitoring was limited because projects had only recently begun when we conducted the audit.

We conducted the audit under the authority of state law (RCW 43.09.470), approved as Initiative 900 by the Washington voters in 2005, and in accordance with generally accepted government auditing standards prescribed by the U.S. Government Accountability Office. 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 objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix A describes the provisions of Initiative 900 and how the audit addressed the law's specific elements. **Appendix B** describes our audit methodology in detail. **Appendix C** describes the general provisions of the American Recovery and Reinvestment Act and Washington's overall goals for stimulus funding.

The State Auditor's Office Single Audit Report

In March 2011, the State Auditor's Office audit of the state's major federal programs was published by the Office of Financial Management for the fiscal year 2010. The audit assessed compliance with the requirements of laws, regulations, contracts and grants applicable to each of the state's major federal programs, in contrast to this performance audit, which primarily considered whether the grant award and monitoring processes were consistent with sound practices.

The report included three findings related to the State Energy Program. Detailed information on each finding is available in the fiscal year 2010 **Single Audit Report.**

Washington received $60.9 million for energy projects

The Recovery Act authorized the U.S. Department of Energy (USDOE) to distribute $3.1 billion for the State Energy Programs in the 50 states, the District of Columbia and U.S. territories under a funding formula that included a base allocation plus an allocation that reflected population and energy consumption. Washington received $60.9 million for grants and loans to state agencies, local governments and businesses, to be spent between April 2009 through March 2012.

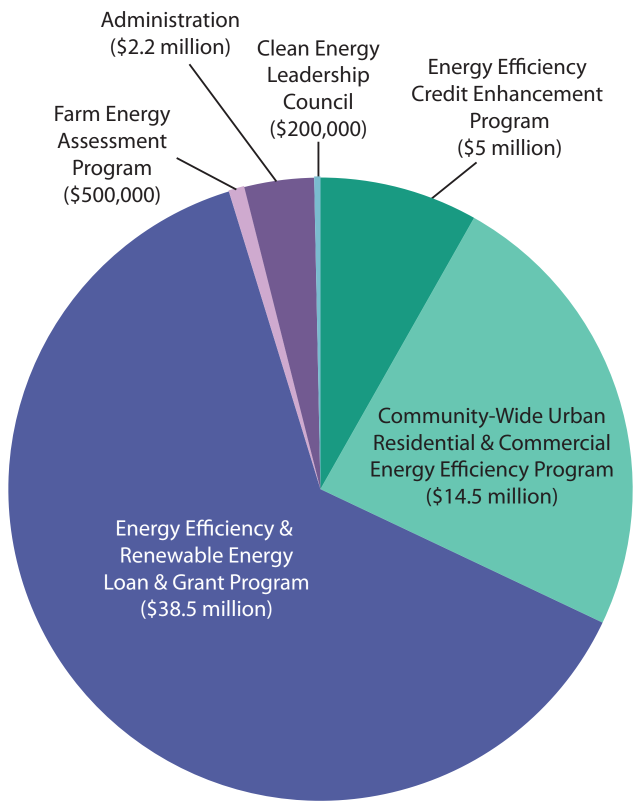
The USDOE goals for the program include:

- Increasing the energy efficiency of the U.S. economy.
- Reducing energy costs.
- Improving the reliability of electricity, fuel and energy services delivery.
- Developing alternative and renewable energy resources.
- Promoting economic growth with improved environmental quality.
- Reducing the nation's reliance on imported oil.

Before states could receive their shares of State Energy Program funding, the Recovery Act required governors and other state executives to formally assure the USDOE their states would take certain actions to promote energy efficiency and conservation, and that they would use Energy Program funding for specific purposes. In Washington's letter to the U.S. Energy Secretary, the Governor said the state would, to the greatest extent practical, prioritize its energy efficiency and renewable energy grants toward existing projects already approved by regulatory agencies, including energy retrofits or buildings and industrial facilities. These commitments were reflected in the State Energy Plan discussed below and included in **Appendix D**.

The Washington Legislature distributed $60.9 million in federal Recovery Act funds among four programs within the Department of Commerce's State Energy Office. The majority, $38.5 million, went

Total SEP Funding = $60.9 million
Fiscal Year 2010



Source: *Commerce's agreement with the USDOE.*

to the Energy Efficiency and Renewable Energy Loan and Grant Program administered by the State Energy Office, so we focused our audit on that program.

Energy Efficiency and Renewable Energy Loan and Grant Program

The Department of Commerce's State Energy Office administers the Washington State Energy Program. In 1996 the former State Energy Office was eliminated and its energy policy responsibilities transferred to the Department of Community, Trade and Economic Development (CTED), which became the Department of Commerce in 2009.

From 1996 through 2008, the Office primarily coordinated state energy policy and strategies and advised the Governor and Legislature on energy matters affecting the state. In recent years the budget ranged from approximately $585,000 to $826,000. In 2009, the influx of Recovery Act funds expanded the Office's responsibilities from its traditional focus on policy analysis to grant- and loan-making.

The Loan and Grant Program is administered by the State Energy Program Manager, assisted by two policy specialists who were brought on after the Recovery Act funding was received. During the loan and grant application process, more than 20 other people helped to review and score the competitive funding proposals. In addition to State Energy Program personnel, this group included three experts from another division at Commerce, three from Washington State University and one each from the departments of Ecology and Agriculture.

Commerce and USDOE negotiated the State Energy Plan

Commerce and the USDOE negotiated an agreement known as the State Energy Plan, which took effect May 1, 2009, to guide the distribution of funds. For the Energy Efficiency and Renewable Energy Loan and Grant Program, Commerce agreed to:

- Provide "interim financing to renewable energy projects, to assist innovative companies that have commercial or near-commercial energy technologies, and to support cost-effective energy efficiency projects."
- "Establish policies and procedures for processing, reviewing and approving applications for funding and enter into agreements with approved applicants to fix the term and rates of funding."
- Hold at least two rounds of competitive awards.
- Have a goal to distribute at least two-thirds of the funds through loans and the remainder in grants. Commerce said it would make 15 to 25 loans for a total of $20 million to $30 million and five to 15 grants for a total of $8.5 million to $18.5 million.
- Use loan repayments and interest to sustain the Energy Recovery Act account as an ongoing source of revolving funds as directed by the Legislature, to support renewable energy and energy efficiency technology.

Elements of the State Energy Plan that apply to the Loan and Grant program appear in **Appendix D**.

As called for in the Plan, the Office held two competitive rounds of funding. First-round applications were due August 17, 2009. Second-round proposals were due February 1, 2010. In addition, the Office awarded $2 million for one project on a sole-source basis, and selected some projects on a non-competitive basis (third round) to redistribute funds that became available after some applications from rounds one and two were withdrawn. As **Exhibit 1** shows, the Office eventually funded 37 projects with the $38.5 million it received in Recovery Act funds, 45 percent through loans and 55 percent through grants. Those projects are described in **Appendix F**.

Exhibit 1
Summary of Loan and Grant Awards
Dollars in Millions

	Eligible Applications	Funding Requested	Contracts Signed	Loans (Amount)	Grants (Amount)	Total Awarded
Competitive Rounds	121*	$132.7	23	$12.4	$13.2	$25.6
Sole-Source	n/a	n/a	1	$0	$2.0	$2.0
Non-Competitive Round	n/a	n/a	13**	$4.8	$6.1	$10.9
Total	**121**	**$132.7**	**37**	**$17.2**	**$21.3**	**$38.5**

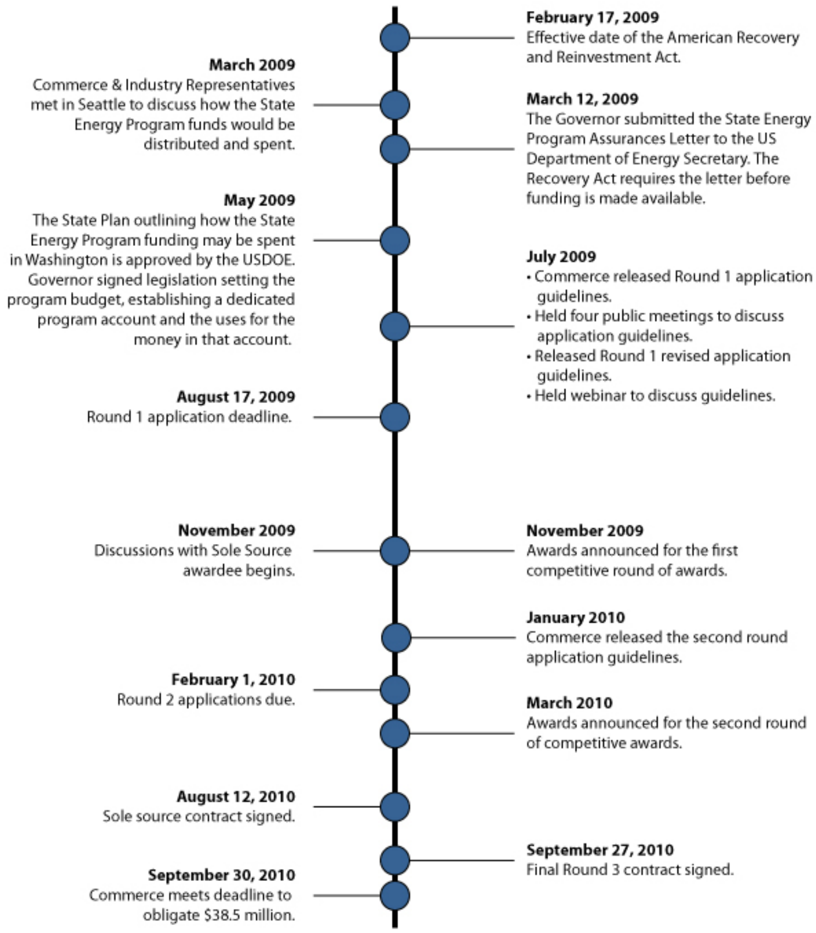
Source: *State Auditor's Office analysis of the State Energy Office data.*

Notes: **174 applications received but 53 did not pass the threshold review.*
*** 6 Round 3 contracts were signed with businesses that applied in Rounds 1 and 2.*

The timeline for awarding the funds was very compressed

Recovery Act fund recipients were directed to award and spend funds as quickly as possible to maximize the Act's economic impact. **Exhibit 2** shows the Office had only about 16 months to solicit applications, award loans and grants and issue contracts before the September 30, 2010, Recovery Act deadline, which it ultimately met.

Exhibit 2
State Energy Program Timeline



Source: *Multiple sources include the Recovery Act, a letter from the Governor, Legislation, the request for proposals, contracts and inteviews with SEP staff.*

It is too early to assess project results

In the State Energy Plan, Commerce estimated the initial Energy Efficiency and Renewable Energy Loan and Grant awards would generate annual energy savings of at least 3.8 million BTUs (British thermal units), create between 300 and 400 jobs and retain 100 jobs. For the quarter ending December 30, 2010, Commerce reported to USDOE that the SEP Grant and Loan Program created a total of approximately 46 jobs. However, as discussed earlier, given the newness of the program, few of the projects had begun when we conducted this audit, so relatively few of the expected results had materialized. All Recovery Act funds were obligated within the required time, and as of March 31, 2011, $10.2 milllion of the $38.5 million had been spent.

Sound Management Practices

A significant portion of government's workload at all levels — federal, state and local — involves distributing funds for specific purposes to public, private and nonprofit organizations. To ensure funding initiatives accomplish their intended objectives, several organizations have identified practices to improve results and ensure public accountability. As described earlier, we reviewed several authoritative sources to identify effective processes for competitive funding and grant management programs.

Competitive funding and grant monitoring processes generally follow similar life-cycles. At each stage, we identified the responsibilities of funding agencies based on those sources. Examples of activities in the three stages of the competitive funding and grant monitoring process are described below.

The pre-award stage includes:

- Defining performance requirements such as services expected, performance standards and measurable outcomes.
- Developing a request for proposal with clear evaluation criteria and weighting factors for scoring proposals.
- Publishing the request for proposals allowing sufficient time for applicants to prepare good proposals.
- Ensuring prospective bidders have equal access to clarifying information about the process through bidders' conferences or other forums.

The award stage includes:

- Using fixed, clearly defined criteria and consistent scoring scales to evaluate proposals against criteria in the RFP.
- Establishing criteria to gauge the risk associated with new grantees.
- Negotiating award terms to clarify the terms of the funding agreement. Negotiations should not substantially change the terms of the original proposal.
- Checking applicant references before final award decisions are made.
- Documenting award decisions and keeping supporting materials.
- Clearly defining the scope of work and contract terms.

The post-award stage includes:

- Monitoring projects.
- Monitoring contracts based on a risk assessment of the services provided and the contractor's ability to deliver to ensure program outcomes are achieved.
- Tracking budgets and comparing invoices to contract terms and conditions.
- Ensuring that deliverables are received on time and document the acceptance or rejection of deliverables.

Appendix E identifies specific criteria we used to evaluate whether the Office established and followed sound processes in awarding and monitoring state energy grants.

Issue 1: Program administrators followed many of the sound practices we identified. However, in an effort to meet tight federal deadlines, they did not follow some important practices in awarding the funds.

We reviewed 23 of the 37 projects for which the State Energy Office awarded Recovery Act funds. As shown in **Appendix E**, we found the Office consistently followed 30 of the 40 sound practices we identified and could evaluate. For example, the staff:

- Appropriately advertised the request for proposals (RFP), which provided important information about federal and state requirements and performance standards.
- Only scored applications that met RFP requirements.
- Organized knowledgeable evaluation committees to review and score the proposals, based on the clearly defined criteria from the RFP.
- Notified all successful and unsuccessful applicants.
- Included in contracts such provisions as specific deliverables, reporting requirements, inspection and audit provisions, and provisions for contract termination.
- Provided introductory administrative training to funding recipients.

However, in their efforts to meet the tight timeframes for obligating and spending Recovery Act funds, the staff did not follow several important practices:

A. Office staff did not establish specific written policies and procedures for awarding program funds, as required.

B. Office staff significantly narrowed the scope of work from the original proposals to the final contracts.

C. Office staff did not document pre-award risk assessments or conduct reference checks that might have identified potential problems with proposed projects and prevented an award from later being withdrawn.

D. Nothing prohibited Office staff from awarding funds to some projects on a sole-source basis, but doing so made the process less open and transparent.

E. Although we were able to identify most of the processes program staff followed in soliciting bids and awarding funds, they did not fully document their actions.

A. **Office staff did not establish specific written policies and procedures for awarding program funds, as required.** According to state law (RCW 43.325.040 3(c)) and Commerce's agreement with the USDOE, the State Energy Office was required to establish policies and procedures for processing, reviewing and approving applications for funding. We found the Office did not establish specific written policies and procedures; instead, the staff relied on the evaluation criteria spelled out in requests for proposals and on an Office memorandum for guidance.

   The absence of specific written policies and procedures created a greater risk that applicants would not be treated consistently or that some aspects of the process for awarding and monitoring projects would not be carried out as required or as Commerce management intended.

B. **Office staff significantly narrowed the scope of work from the original proposals to the final contracts.** The State Administrative and Accounting Manual (SAAM) directs agencies not to significantly change the terms of original proposals during contract negotiations, which helps to ensure the competitive review process is scored fairly and funds are awarded only to the best proposed projects. However, we found that Office managers negotiated contracts for three approved projects that substantially narrowed the scope of work from the original proposals:

   - In one case, the applicant asked for $2 million as part of a $55 million project to upgrade an existing boiler and build a new steam turbine generator, creating or retaining 200 jobs. However, the signed contract is for a $2.1 million project ($2 million award and $100,000 match), that only covers making upgrades to the existing boiler, creating no new jobs and retaining only one.
   - The second case involved a separate $55 million project by a different applicant seeking $2 million to replace a boiler with a more energy-efficient system and produce excess renewable energy for sale to a local PUD, creating or retaining 243 jobs. However, the signed contract is for $9.4 million ($2 million award and $7.4 million match), and covers only the purchase of equipment.
   - In the third case, the applicant requested $2 million for a $175 million project to build an airline fuel refinery, creating or retaining more than 480 jobs. However, the signed contract is for a $6.2 million project ($2 million award and $4.2 million match) that covers only preliminary engineering studies and other project planning and oversight.

   Office staff said they narrowed these projects' scope of work with the approval of USDOE to ensure the projects that received awards would meet federal spending deadlines.

   - Under the National Environmental Policy Act, the projects would have had to complete an environmental assessment, and Office officials said they could not have been completed by the contract deadline of December 2011.
   - Under the federal Davis-Bacon Act, one of the projects would have been required to pay at least the prevailing wage rates established by the U.S. Secretary of Labor for all laborers and mechanics employed on

the project. Office staff said the scope of this project was narrowed to cover the purchase of equipment but not wages in an effort to avoid triggering the requirement to follow the Davis-Bacon Act for the entire project.

Office managers also said that, although the scope of work was narrowed in the final contracts for these three projects, the larger projects likely will go forward. However, that is not assured, and these Recovery Act funds are supporting much more modest objectives than those initially proposed.

Although Commerce staff thought there was good reason to take the actions they did, this practice was not in line with the state's SAAM manual and does not meet the Recovery Act's goal of transparency and fairness. For example, if the reduced scope of work had been the basis for the initial competitive evaluation on the first project described above, it would not have been ranked high enough under the Office's RFP requirements to receive funding. Further, Commerce's website still shows the potential impacts for these projects' original proposals, not the less significant impacts that will be achieved under the final contracts.

C. **Office staff did not document pre-award risk assessments or conduct reference checks that might have identified potential problems with proposed projects and prevented an award from later being withdrawn.** Office staff attempted during the application review and evaluation process to identify the best projects for funding. They completed a risk assessment for the State Energy Office as a whole, reviewed proposals to determine whether they met minimum project requirements, and brought in more than 20 people to help review and score the competitive funding proposals based on the criteria in the RFP.

However, Office staff did not formally document the risks of individual projects during the application process to identify potential "red flags," and did not require applicants to include references with their proposals. For those applications that included letters from matching fund sources attesting to the availability of funds, we saw no documentation that the evaluation teams had verified this information.

Carefully checking applicant references and documenting results helps to ensure the accuracy of representations made in the applications, such as an applicant's work history and the availability of matching funds. In addition, the Department of Justice's Office of Inspector General recommends that funding agencies assess risks that could signal potential problems with an applicant's ability to appropriately handle grant awards. These could include the lack of separate accounts for project funds, inadequate accounting procedures, or the lack of performance measures and data.

Such actions may have averted the need for the Office staff to withdraw an award after it was made. For example, one applicant said the proposed project had secured $10 million in equipment to meet the matching-fund requirement, but later could not confirm ownership of the equipment.

If the Office had identified these problems up-front, it would have saved staff time spent negotiating the contract and handling other related tasks.

D. Nothing prohibited Office staff from awarding funds to some projects on a sole-source basis, but doing so made the process less open and transparent. In passing the Recovery Act, the President and Congress stressed the need for accountability, efficiency and transparency over Recovery Act spending and placed a high priority on recipients quickly spending those funds. The Governor's Office also cited "unprecedented accountability and transparency" as one of five core principles guiding state agencies' economic stimulus work.

We found the Office began discussions to award a $2 million sole-source grant to one project in November 2009, between the first and second rounds of competitive bids. This project was for energy-efficient equipment in a plant that will make carbon-fiber material for a car manufacturer. Office staff said this award was made outside the competitive bid process because the project had an imminent timeline and had a major potential energy and economic impact on the state—and the project owners were considering a competing location in Canada.

Office staff said they thought the grant would help keep the project in Washington. The second-round RFP said the reserved funds would be freed up for the second round of bids if the project did not go forward by the end of 2009. A contract was not signed at the end of 2009 but the program manager indicated the project was still going forward, so the funds remained reserved. The contract for the grant eventually was signed in August 2010.

The State Energy Plan is silent on the issue of awarding money outside the competitive process, so nothing prohibited Office staff from awarding these funds on a sole-source basis. However, the process was less open and transparent than it would have been if all awards had been made competitively.

E. Although we were able to identify most of the processes program staff followed in soliciting bids and awarding funds, they did not fully document their actions. The issues we identified are described below.

- There was no documentation—such as a date stamp or dated email—to confirm that one of the 10 applications we reviewed arrived before the application deadline. The Office did not have a formal procedure in place for handling proposals that arrived late or were incomplete.
- Office staff did not document the rationale for continuing to reserve $2 million for the sole-source project beyond the end of 2009, when a note in the RFP said it would be freed up for the competitive bids. As noted above, Office staff told us the project was still going forward at that time, and the contract ultimately was signed in August 2010.
- Office staff documented the scores they awarded to individual projects but did not adequately document the process they used for selecting the successful applicants in the second round. The Office created a memo to describe the process for the first round. The Office reported that it improved the process for the second round, but we saw no documentation explaining how and why the Office changed the process.

- The staff did not document why one evaluator added $4 million to the matching funds for a project application or where those funds had come from. According to the evaluator, when the application was submitted the applicant verbally reported the additional matching funds.
- In two contracts, the staff did not retain documents describing the methods used to score energy savings and jobs. Office staff re-created a spreadsheet for us so we could review the methods used.

Granting agencies should clearly document key aspects of the award process and maintain this documentation to ensure transparency and to demonstrate they conducted a fair and open process. Without adequate documentation, award decisions may not be defensible if they are challenged later.

Recommendations to address Issue 1

1. We recommend the Office establish specific written policies and procedures to guide the Loan and Grant Program in the future to ensure employees understand management's expectations for business processes, record-keeping, personnel responsibilities and day-to-day operations and decision-making. Such policies and procedures also can serve as training tools for employees.
2. We recommend Office contracts include a scope of work similar to the scope of work included in related applications and used as the basis for competitive scoring to ensure a fair and transparent award process. We also recommend the Commerce Department revise the project summaries on its website to more accurately describe the economic impacts of the contracted loan and grant projects when their scope changes significantly.
3. We recommend the Office document pre-award risk assessments and conduct reference checks on future contracts to ensure the best applications receive awards.
4. We recommend the Office clearly document the processes it uses to award funding and the basis for all key award decisions to ensure adequate evidence is maintained to show funds are awarded fairly and objectively.

Issue 2: The State Energy Office did not require or receive all the information it will need to ensure it can appropriately monitor and oversee these projects.

Sound practices for handling grant projects stress the importance of monitoring projects to help ensure that contractors are doing the work proposed, that payments are made only for appropriate expenditures, that deadlines will be met, and that program outcomes are achieved. Although work had begun on relatively few of the 37 loan and grant projects at the time of our audit fieldwork, we identified the following issues that could impact the Office’s ability to effectively monitor those projects:

A. The contracts we reviewed did not specify all the information Office staff will need to effectively monitor contractors’ performance.

B. Office staff made payments on several contracts based on limited information.

C. The Office had not conducted formal post-award risk assessments to determine the level of monitoring needed for projects of differing risks.

D. Contracts were not monitored to ensure jobs and hiring decisions were reported to Washington’s WorkSource system.

A. The contracts we reviewed did not specify all the information Office staff will need to effectively monitor contractors’ performance. None of the 23 contracts we reviewed included performance measures for the contractors. The Office required applicants to include performance measures in their loan and grant applications related to such elements as job creation and retention, matching funds leveraged and energy savings or energy conservation. Projects also were scored based on these measures. However, those performance measures were not incorporated into the contracts. As a result, contractors cannot be held accountable for achieving the results for which they received Recovery Act funding.

The Recovery Act requires Commerce to report the number of jobs created and retained in addition to program outcomes such as energy savings, new energy-generating capacity or emission reductions. However, that reporting is only required while the contracts are in place. Because the final outcomes and impacts for many of the 37 projects the Office awarded funding to may not be known for several years, this information may not be captured through Recovery Act reporting, but will be helpful for future decision-making. The Program Manager said performance measures would be included in future loan and grant contracts, as required by an executive order signed by the Governor in November 2010.

Two contracts also did not include timelines associated with specific contract tasks. Although all contracts we reviewed included completion dates, two did not include timelines associated with the tasks in the scope of work. Such timelines allow Office staff to ensure projects are on schedule. Without them, it is difficult for the contract manager to determine whether all expected work is likely to be completed before the contract deadline.

B. **Office staff made payments on several contracts based on limited information.** An important element of project monitoring is the ongoing review of contract invoices. Although few of the contracted projects were under way when we conducted this audit, we did review the invoices for all four of the 10 projects in our sample for which invoices had been submitted. In two of those cases, the descriptions contractors submitted on the invoices were at too high a level (i.e., salaries, benefits, and travel) to determine which tasks they were linked to in the contracts' scope of work. As a result, we could not confirm which contracted tasks those invoiced expenses were related to in the contracts. When we brought this information to the attention of Office staff, they indicated invoices from other contractors will be required to break down expenses by the tasks listed in the contracts.

   Three contracts' invoices we reviewed also did not indicate the contractors' progress in completing tasks required under the contracts, so the Office could not effectively monitor the overall project and determine whether there were discrepancies between planned activities, costs and actual accomplishments.

C. **The Office had not conducted formal post-award risk assessments to determine the level of monitoring needed for projects of differing risks.** State Energy Office management completed a risk assessment for all five of the Office's Recovery Act programs. However, they had not completed a post-award risk assessment for the 37 individual grant and loan projects. The Program Manager indicated she had completed an informal risk assessment of these individual projects but had not documented the results.

   With limited resources for monitoring progress and payments for 37 energy projects—all of which are required by the contracts to spend the Recovery Act funds they received by December 31, 2011—a formal risk assessment can help ensure that high-risk projects are adequately monitored, and lower-risk projects are monitored at an appropriate level.

D. **Contracts were not monitored to ensure jobs and hiring decisions were reported to Washington's WorkSource system.** In looking at the Office's compliance with the requirements of the requests for proposals and contracts, we noted that Office staff did not check to ensure that contractors listed all job openings and hiring decisions with the Employment Security Department's WorkSource system, as required for all jobs supported by Recovery Act funds. As a result, the Governor and the U.S. Department of Labor may not have received consistent information about jobs preserved and created with Recovery Act funds.

Recommendations to address Issue 2

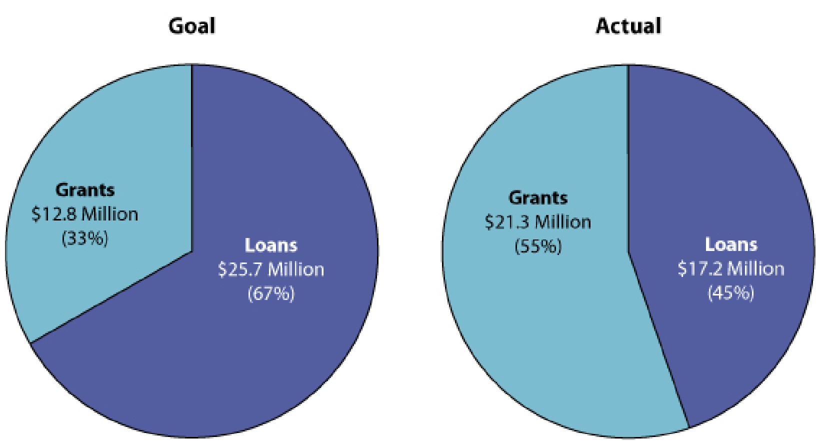
1. We recommend Office contracts include clear standards for measuring the award recipients' performance to ensure final project outcomes are known and award recipients are held accountable for expected job creation/retention and energy savings.
2. We recommend Office personnel thoroughly review all invoices to ensure payments for deliverables are clearly linked to contract tasks. They also should track the completion status of each task to ensure payments are related to contract tasks and projects are on schedule.
3. We recommend the Office place a greater focus on assessing risks to ensure limited resources are used efficiently during the monitoring phase.

Issue 3: Commerce did not meet a goal to loan two-thirds of the Recovery Act funds provided to the Loan and Grant Program, which will reduce by $ 8.5 million, the amount of funds available for future energy projects.

One of nine goals in the State Energy Plan negotiated between Commerce and the USDOE to guide the use of Recovery Act funds was for the state to distribute at least two-thirds of the Loan and Grant Program funds — a minimum of $25.6 million — as loans, with the remainder as grants. Commerce said it would strive to make 15 to 25 **loans** for a total of $20 million to $30 million, and another five to 15 **grants** for a total of $8.5 million to $18.5 million. The Legislature had established a revolving loan fund to collect repayments and interest on the Recovery Act funds and make them available for additional investments in the future.

As **Exhibit 3** shows, the Office ultimately awarded only $17.2 million in loans, or 45 percent of the total amount it received. That amount is $8.5 million short of its goal of distributing two-thirds of the energy funds as loans.

Exhibit 3
SEP Loans and Grants
Actual vs. Goal



Loans are $8.5 million below goal.

Source: *State Auditor’s Office analysis of the State Energy Office information.*

At least two factors reduced the percentage of funds awarded as loans:

- **Program administrators said the proportion of loans** was reduced after the first round on the advice of the state's Clean Energy Leadership Council, an industry-based advisory committee created through legislation in 2009. The council's primary job is to prepare a strategy for expanding Washington's clean energy technology sector, and lawmakers required Commerce to consult with the Council before awarding federal stimulus funds. The council members urged Commerce officials to emphasize grants over loans because they said they would be more helpful in stimulating innovative projects.
- **After the competitive award decisions were made**, in November 2009 and March 2010, several projects were withdrawn. In eight cases, the applicants declined the awards. Those projects would have received $9.1 million in loans and $1.9 million in grants. We were able to contact six of these eight applicants. They cited several factors, including an inability or unwillingness to meet specific federal requirements, unfavorable loan terms, an unwillingness to accept a loan instead of a grant, not receiving expected matching funds, and poor project feasibility that became apparent after funds were awarded. In one case, a state agency was awarded a loan but declined after its assistant Attorney General questioned whether it could accept a loan without legislative authorization. When the funds for the withdrawn projects were reobligated, the projects subsequently funded were primarily grants. The sole-source project the Office funded also was a grant.

Appendix G provides a detailed breakdown of the initial awards and actual contracts compared to the goals included in the agreement with the USDOE.

We are making no recommendations for this issue.

STATE OF WASHINGTON

June 6, 2011

The Honorable Brian Sonntag
Washington State Auditor P.O. Box
40021
Olympia, WA 98504-0021

Dear Auditor Sonntag:

Thank you for the opportunity to provide this official management response to the performance audit on the State Energy Program at the Washington State Department of Commerce (Commerce).

The purpose of the American Recovery and Reinvestment Act of 2009 was to aid the economy by creating and saving jobs through investments in areas such as infrastructure and energy. The State Energy Program received a grant of $60.9 million of which $38.5 million was allocated to the Energy Efficiency and Renewable Energy Loan and Grant Program. As your audit confirms, the State Energy Program met the federal requirement to obligate all of these funds by September 30, 2010. In doing so, Commerce received an award from the U.S. Department of Energy (DOE) for getting funds into our local economy quickly and responsibly. Commerce also met the legislative intent to invest in high- quality, newer technology projects in the private sector through open, competitive bidding.

Given the extremely tight timelines, changing federal guidance, and strict accountability requirements, we are also pleased the audit found that this program followed the majority of practices for competitive loan and grant programs as identified by the Auditor during the audit. A programmatic and financial evaluation, as well as a Davis-Bacon compliance review, by DOE stated the program met the standards, and therefore, received zero findings. The evaluation commended Commerce for its excellent work with the State Energy Program, specifically on the monitoring process for sub-recipients.

We recognize there is always room for improvement. Several actions to strengthen practices have already been completed. We agree that better documentation would have been helpful in certain areas. Although it is unlikely this program will have to manage a similar influx of funds in the near future, Commerce staff will evaluate where better-documented policies and procedures are warranted and implement as necessary.

Sincerely,

Rogers Weed, Director
Department of Commerce

Marty Brown, Director
Office of Financial Management

The Honorable Brian Sonntag
June 6, 2011
Page 2 of 2

cc: Jay Manning, Chief of Staff, Office of the Governor
Jill Satran, Deputy Chief of Staff, Office of the Governor
Wendy Korthuis-Smith, Director, Accountability & Performance, Office of the Governor
Kimberly Cregeur, Governor's Liaison on Performance Audits, Accountability & Performance, Office of the Governor

Official Agency Response to the Performance Audit on Commerce's State Energy Program

June 2011

This coordinated management response is provided by the Department of Commerce (Commerce) and the Office of Financial Management (OFM) for the audit report received on May 23, 2011.

Issue 1: Program administrators followed many of the sound practices we identified. However, in an effort to meet tight federal deadlines, they did not follow some important practices in awarding the funds.

COMMERCE RESPONSE: Commerce's plan for distributing $38.5 million in American Recovery and Reinvestment Act (Recovery Act) funds included an aggressive schedule both to conduct two competitive solicitations to the private sector and to ensure we would meet the critical U.S. Department of Energy (DOE) deadline to have all funds obligated by September 30, 2010. **Commerce met this deadline and successfully obligated all of the $38.5 million available to the State Energy Program.**

We agree that some steps were not thoroughly documented and some best practices were not followed, due in part to extremely tight timelines and changing federal guidance. Despite not having the information identified in *Appendix E: Sound Processes* prior to awarding the funding, Commerce still met 75 percent of the elements identified in the audit report.

Several of the items marked as "did not follow" in the appendix were in fact followed by staff throughout the process; however, they were not documented specifically as unique steps. This information will be beneficial going forward for any future competitive grant and loan program that might be administered by the State Energy Office.

Given the aggressive schedule and one-time nature of the award, the program-specific application guidelines developed for Rounds 1 and 2 were used by the program manager and office staff in conjunction with agency policies and procedures, rather than developing a program-specific policy and procedure manual. Commerce has agency-level policies and procedures in place for awarding program funds. Divisions within Commerce follow these rather than establish numerous new program-specific policies and procedures. This helps prevent silos and ensure continuity across the agency. Using agency policies and procedures in conjunction with the application guidelines ensured the award process was consistently communicated to the applicants and applied during the award process.

Risk assessment was included in the application review and scoring process; however, it was not a specific scoring category or formally documented. As documented in the State Energy Office sub- recipient monitoring plan, risk assessment is an ongoing component of our monitoring process, and we now track risk level in our monitoring documents.

In consultation with and approval from DOE, the statements of work in three projects cited in the audit were narrowed to allow for early use of the Recovery Act funds in a much larger project to accommodate time constraints associated with the funding. These projects were still required to meet all applicable federal environmental and wage requirements. All three projects have met the National Environmental Policy Act (NEPA) requirements and received approval from DOE. One project is completing a full environmental assessment, and the project subject to Davis-Bacon is in full compliance.

As noted in the audit, one sole-source project was awarded a $2 million grant for energy-efficient equipment in a plant that will make carbon fiber material for a car manufacturer. With the support of this award, this $100 million manufacturing facility was successfully located in Washington rather than in Canada, bringing an estimated 80 jobs by the end of 2011. While this process was outside the original plan to issue awards through two competitive rounds, it was consistent with Commerce's goals in the State Energy Plan and was fully approved by DOE. The project is expected to create jobs, reduce energy consumption in manufacturing through the purchase of energy-efficient equipment, and reduce energy use in the transportation sector through a new approach to building vehicles. The company recently announced the production facility has been completed and its plan is to start producing carbon fiber in the third quarter of this year.

Action Steps and Time Frame

- Incorporate and document risk assessment as part of monitoring plan. Completed.
- Review website documentation and update with current information. By August 1, 2011.

OFM RESPONSE: Given the extremely tight timelines, changing federal guidance, and strict accountability requirements of the Recovery Act, we are pleased that the State Energy Program followed the majority of practices for competitive loan and grant programs as identified by audit staff. DOE conducted a programmatic and financial evaluation, as well as a Davis-Bacon compliance review. It stated the program met the standards, and therefore, received zero negative findings.

ISSUE 2: The State Energy Office did not require or receive all the information it will need to ensure it can appropriately monitor and oversee these projects.

COMMERCE RESPONSE: We agree that during the initial period of monitoring, not all information was received to support detailed monitoring. This was very early on in the process, and since that time, the State Energy Office has implemented tighter controls specifically related to Recovery Act sub-recipient monitoring.

To ensure greater control over invoice monitoring and documentation, Commerce implemented the following measures:

> On September 1, 2010, monitoring of invoice payments on the Energy Office's Recovery Act contracts was transferred to Commerce's Contracts Administration Unit (CAU). CAU has experienced staff dedicated to reviewing all requests for payments and the supporting documentation before payments are approved.
>
> All requests for reimbursement are reviewed and approved by the program manager for consistencies with the statement of work and project activities, and for ongoing status tracking.
>
> Invoices are also monitored by the invoice payer in the CAU prior to approval for payment to ensure all costs are allowable and the appropriate level of documentation has been provided for verification.

All recipients from Rounds 1 and 2 were monitored on-site by the program manager and technical staff, when available, to review the contract template and discuss each project, including the federal and state requirements associated with the award. This was part of our post-award risk assessment. We agree more detailed documentation would have been appropriate for the sub- recipient file. The information gained from this process has informed the contracting process and ongoing monitoring activities.

Since completion of the award process, staff efforts have been focused on desktop and on-site monitoring. The State Energy Office has conducted at least one on-site monitoring visit for all State Energy Program loan and grant recipients in Rounds 1 and 2. Seven of these visits were in conjunction with DOE as part of the federal agency's monitoring of the Recovery Act grant. After reviewing our sub-recipient monitoring plan and observing successful execution of the plan on several visits, DOE found Commerce to be in compliance with the general administration of the Recovery Act grant. In a letter to Commerce in March of 2011, **DOE commended the Energy Office for its "excellent work with the State Energy Program…specifically on your sub- recipient monitoring process."** No corrective action was recommended.

Action Steps and Time Frame

- Document risk assessment as part of monitoring plan. Completed.
- Strengthen desktop monitoring for review and approval of invoices. Completed.

OFM RESPONSE: We support the use of sound practices to monitor all projects administered by the state. We appreciate the steps taken by Commerce staff to strengthen their oversight of these projects.

ISSUE 3: Commerce did not meet a goal to loan two-thirds of the Recovery Act funds provided to the Loan and Grant Program, which will reduce by $8.5 million the amount of funds available for future energy projects.

COMMERCE RESPONSE: As part of the application for Recovery Act funding, Commerce set an agency goal to maximize loans by distributing two-thirds of the funding via loans and one third via grants. This was one of nine goals identified in the plan based upon the information available at the time. It was unclear at that time if private sector applicants would be willing to accept loans and meet the stringent requirements of federal funding. Commerce achieved its original target for the loan-to-grant award ratio in the first competitive round by awarding $13.6 million in loans and
$6.5 million in grants.

Unfortunately, because of a variety of factors including significant federal requirements, complexity, timing, and an unwillingness on the part of the applicants to accept loan terms, several applicants dropped out. This resulted in funding for Round 1 at $9.0 million in loans and $6.5 million in grants, reducing the level of funding awarded for loans.

The Legislature required Commerce to consult with the Clean Energy Leadership Council (CELC), whose primary job is to prepare a strategy for expanding Washington's clean energy technology sector. As the guidelines for Round 2 were being developed, the CELC urged Commerce to emphasize grants over loans, indicating grants would be more helpful in stimulating innovative projects.

Based on these factors, along with the sense of urgency on the part of Commerce to meet the DOE obligation deadline, Commerce chose to award a higher percentage of awards as grants rather than risk losing the funding altogether. While this reduces the funding available for similar future projects, achieving the deadline to obligate all of the Recovery Act funds allowed Commerce to provide more immediate and essential funding to private businesses in Washington to create and save jobs.

Action Steps and Time Frame

- No recommendations made in the audit report.

OFM RESPONSE: The issue cited in the report gives the impression that Commerce missed a primary goal of the Recovery Act – which it did not. On the contrary, Commerce's State Energy Program **met the overarching goals set by the Recovery Act and the Governor** to quickly distribute funds to communities to preserve and create jobs. By successfully obligating all the funds on time, the program avoided having to return any of the $38.5 million awarded by the federal government.

Likewise, the program successfully responded to the Legislature's direction for investing in high- quality, newer technology projects in the private sector. Other goals in the plan, such as leveraging Recovery Act funds and selecting projects across a range of risk, were also met.

As noted in the State Energy Plan, funds for the State Energy Program can be used for a broad range of energy efficiency and renewable energy loans and grants. Setting an original goal of distributing more funds through loans made sense given the limited information both federal and state program staff had to work with at the time.

Commerce did strive to meet its original goal, and in fact, did meet the goal of awarding more loans than grants in the first competitive round (see Appendix G). The report explains why the number of loans was less than originally planned. Despite a rapidly changing environment, staff responded quickly and appropriately to ensure the primary goals of the Recovery Act were met. As a result, none of the $38.5 million in Recovery Act funding for the State Energy Program was forfeited.

Appendix A: Initiative 900

Initiative 900, approved by Washington voters in 2005 and enacted into state law in 2006, authorized the State Auditor's Office to conduct independent, comprehensive performance audits of state and local governments. Specifically, the law directs the Auditor's Office to "review and analyze the economy, efficiency, and effectiveness of the policies, management, fiscal affairs, and operations of state and local governments, agencies, programs, and accounts." Performance audits are to be conducted according to U.S. General Accountability Office government auditing standards.

In addition, the law identifies nine elements that are to be considered within the scope of each performance audit. The State Auditor's Office evaluates the relevance of all nine elements to each audit. The table below indicates which elements are addressed in the Energy Efficiency and Renewable Energy Loan and Grant Program Audit.

I-900 Element	Addressed in audit
1. Identification of cost savings	No. The focus of the audit was to identify practices to improve the effectiveness of the awarding and contract monitoring practices to help ensure the best projects are funded and intended outcomes are achieved. We did identify one funding award that did not appear to be justified when compared to the requirements of the Office's Request for Proposal.
2. Identification of services that can be reduced or eliminated	No. The audit examined the operation of a newly created program, not an existing one.
3. Identification of programs or services that can be transferred to the private sector	No. Federal law requires the state to administer the State Energy Program.
4. Analysis of gaps or overlaps in programs or services and recommendations to correct gaps or overlaps	Yes. We identify gaps in program documentation and practices and recommend strategies to address them.
5. Feasibility of pooling information technology systems within the department	No. There are no information technology systems associated with the processes we reviewed.
6. Analysis of roles and functions of the department, and recommendations to change or eliminate departmental roles or functions	Yes. We recommend the Commerce Department revise the way it administers Recovery Act funds through the State Energy Program.
7. Recommendation for statutory or regulatory changes that may be necessary for the department to properly carry out its functions	No. Statutory or regulatory changes are not required to implement our recommended program improvements.
8. Analysis of departmental performance data, performance measures, and self-assessment systems	Yes. We found the Department did not make full use of performance measures and data and we recommend specific improvements.
9. Identification of best practices	Yes. We extensively reviewed best practices for funding awards, contract development and project monitoring. We found the State Energy Office did not follow sound practices in several important areas.

Appendix B: Methodology

We chose to audit State Energy Program after reviewing all of the Washington State government programs that had received Recovery Act funds as of March 2010 to identify Recovery Act programs of high risk. We considered the following risk factors:

- Total Recovery Act money awarded.
- New federal programs created by the Recovery Act receiving more than $5 million dollars.
- Existing programs whose funding increased by more than 100 percent from 2008 to 2009 due to Recovery Act funding.
- Major high-risk programs identified by the State Single auditors for fiscal year 2010.
- Prior audit findings or risks identified by other organizations, from audits from Kansas and California, the Washington State Single Audit, accountability audits of Washington State agencies, the United States Government Accountability Office, and the USDOE Inspector General.
- Interest from the Governor's Office and the Legislature.

Additionally, we considered whether programs would continue after Recovery Act funding is no longer available to ensure our recommendations are useful and directly applicable to future program operations.

Using that approach, we selected the State Energy Program as the focus of this audit. Our performance audit focuses on the State Energy Program Energy Efficiency and Renewable Energy Loan and Grant Program. Because the program was so new, our analysis of project monitoring was limited because projects had only recently commenced when we conducted the audit. As of March 31, 2011, $10.2 million of the $38.5 million in Recovery Act funding was spent. Because most projects had barely begun work, the audit focused on the pre-award and award stage but did not focus on the post-award stage including monitoring and reviewing project outcomes.

To gain an understanding of the program requirements, we obtained and reviewed federal and state laws, rules, regulations, and guidance from federal oversight agencies that are relevant to the State Energy Program and significant to the audit objectives. We also reviewed the terms and conditions attached to the federal grant award, and the federally approved state plan to evaluate the requirements for receiving and administering the funds.

We interviewed key management and staff of the Office and reviewed documents they provided to support the status of the Office's process for awarding state energy grants and loans, monitoring recipients' use of funds and determining outcomes. Additionally, we accompanied Office staff to two on-site visits where contract provisions were reviewed with awardees. We also contacted several awardees of the Energy Efficiency and Renewable Energy Grant and Loan funds who withdrew prior to signing a contract.

We intended to review the Office's policies and procedures to determine if they met sound practices, and analyze whether the Office followed these policies and procedures. However, when we conducted the audit, the Office had not formally documented its process for soliciting, awarding, monitoring and determining outcomes for the state energy grants and loans. As a result, we focused on analyzing the process the Office followed to award the grants and loans, monitor recipients' use of funds, and determine if specific program outcomes were being achieved, and compared these processes to sound practices where applicable.

To determine whether Commerce followed sound processes, we identified sound practices based on the 2005 "Guide to Opportunities for Improving Grant Accountability" published by the U.S. Domestic Working Group. Chaired by the U.S. Comptroller General, the group included representatives of the U.S. Government Accountability Office, 18 federal inspector general offices, four state auditors' offices and two local audit offices. We also reviewed the National State Auditors Association report, "Best Practices in Contracting for Services," the U.S. Department of Justice Office of the Inspector General report "Improving the Grant Management Process " and the Washington State Administrative & Accounting Manual (SAAM).

To determine whether the department followed established processes we reviewed 23 projects. We judgmentally selected ten projects from both grant and loan award competitions, from both rounds 1 and 2. We selected two of the 10 competitively awarded contracts because they were signed without a scope of work and we considered them relatively high-risk. We selected the other eight to include awards made in both competitive rounds; projects in Eastern and Western Washington; all project types (energy efficiency, renewable energy, clean-tech, waste to energy); and projects receiving grants, loans or both.

We also reviewed 13 of the 14 projects that were awarded outside of the two formal competitive rounds. We did not review the remaining project because the funds were provided through a letter of intent and not a contract.   For each selected project, we reviewed the Contract Administration Unit's file, the Program Manager's file, and the electronic files.

Appendix C: Recovery Act

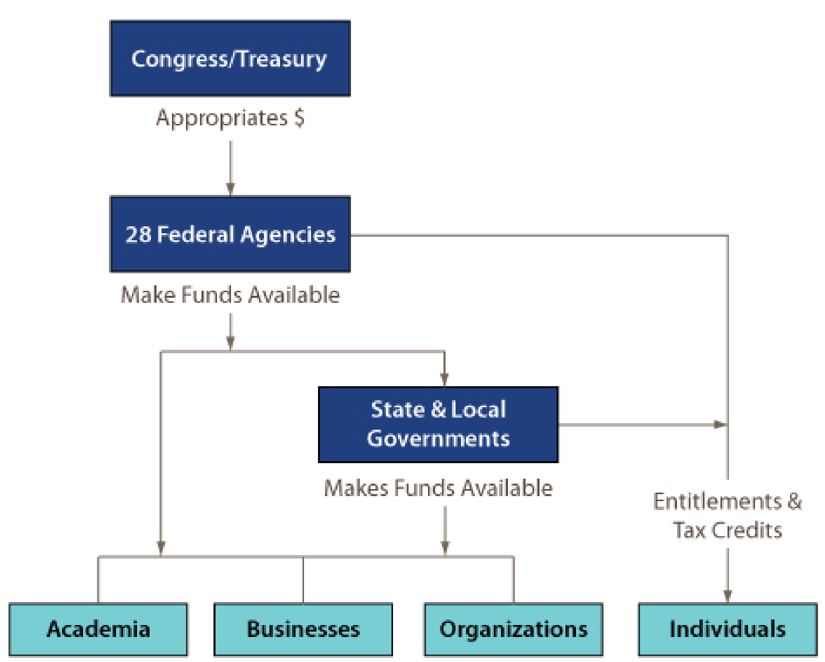
The American Recovery and Reinvestment Act of 2009 (Recovery Act) was passed by the 111th Congress, and signed into law on February 17, 2009. The Act contains $787 billion in domestic spending of which Washington State received more than $8 billion in grants, loans and contracts. The stated purpose of the Recovery Act includes:

- Preserving and creating jobs and promoting economic recovery;
- Assisting those most impacted by the recession;
- Providing investments needed to increase economic efficiency by spurring technological advances in science and health;
- Investing in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits; and
- Stabilizing state and local government budgets in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

The need for accountability, efficiency and transparency over Recovery Act spending coupled with a sense of urgency is emphasized by the President and Congress and are central principles of the Act. Specifically, the Recovery Act states funds are used to achieve Recovery Act purposes as quickly as possible, consistent with prudent management.

The figure illustrates the path of Recovery Act funds from the federal government to the local level.

Recovery Act Funds
Federal Government to Local Level



Source: *Recovery.gov website.*

A February 2009 memorandum issued by the Office of Management and Budget (OMB), which is responsible for the monitoring and oversight of the Recovery Act compliance requirements, reinforces the commitment to swiftly invest Recovery Act funding with an unprecedented level of transparency and accountability so Americans know where funding is going and how it is spent. The accountability objectives outlined by OMB for Recovery Act spending include ensuring that:

- Funds are awarded and distributed fairly, promptly and in a reasonable manner.
- Information about recipients and uses of all funds is available to the public, and that public benefits are reported clearly, accurately and in a timely manner.
- Funds are used for authorized purposes and that fraud, waste, error and abuse are mitigated.
- Projects funded under this Act avoid unnecessary delays and cost overruns.
- Program goals are achieved, including specific program outcomes and improved results on broader economic indicators.

Similarly, in Washington state the Governor's office, which was required to certify and accept responsibility for the appropriate use of the Recovery Act funds, created five core principles to guide state agency work on the federal recovery process incorporating the need spend promptly while adhering to a high standard of transparency. The principles include:

- Get money in people's pockets immediately.
- Create or save jobs in the near-term.
- Make innovative investments in areas that lay the foundation for Washington's 21st century economy.
- Create strategic alliances with the private sector, non-profits, local governments and other state agencies that align goals and leverage resources.
- Apply unprecedented accountability and transparency principles.

Appendix D: State Energy Plan

This appendix contains the portion of the Washington State Energy Plan that addresses the Loans and Grants Program.

U. S. Department of Energy
State Energy Program (SEP) Narrative Information Worksheet

Grant Number EE00139

State Title: Energy Efficiency and Renewable Energy Loans and Grants Program Fund

1. Market: Energy Efficiency and Renewable Energy

2. State: WA

3. Program Year: 2009 Term: 4/1/2009 - 3/12/2012

4. Topics Involved in the Overall Program Market: Residential Buildings, Commercial Buildings, State and Local Government Facilities, Electric Power and Renewable Energy, Alternative Fuels, Bioenergy and Bio-based products, Financing Energy Programs

5. Estimated Annual Energy Savings: At least 3,850,000 million BTU

6. Description:

This fund can be used for a broad range of energy efficiency and renewable energy loans and grants. The Washington Department of Community, Trade and Economic Development (CTED) will directly administer the program. The loans, loan guarantees, and grants from this fund will encourage the establishment of innovative and sustainable industries for renewable energy and energy efficient technology.

CTED will solicit project proposals through at least two separate requests for proposals (RFP) rounds. The need to move rapidly on distributing these funds has put us on a fast track to issue our first request for proposals (RFP) and we will be prepared to issue an RFP in June 2009 subject to DOE approval of this proposal. This RFP will be for a first round of loans and grants. Applications will be reviewed and contract negotiations started within 30 days of receipt of proposals. CTED plans to issue a second RFP based on the information gained regarding the levels of success of different projects or programs from the first round in January 2010. This round of applications will also be
reviewed and contract negotiations begun within 30 days of receipt. All initial funds will
be obligated by September 2010 and disbursed by March 31, 2012. The State Legislature has established an account that can be used as a revolving loan fund to leverage these monies for long-term uses. Because some of the monies will be awarded as loans, the loan repayments and interest will continue to sustain the account. CTED's director will establish policies and procedures for processing, reviewing, and approving applications

for funding and enter into agreements with approved applicants to fix the term and rates of funding.

Offering both loans and grants to high quality projects will allow us to achieve the energy and jobs goals of the ARRA while also providing funds to more innovative, higher risk projects such as the development of near commercial, new efficiency, and clean energy technologies.

In designing this program, CTED met with many stakeholders to receive input. CTED considered the input of Washington's cities and counties, state agencies, the Washington State University Extension Energy Program, the Bonneville Power Administration, utilities, and attendees of an Energy Summit CTED held to get input and provide information on ARRA opportunities. Over 750 people attended the Summit and there was unprecedented interest in developing an array of solid projects.

We also recognize that some projects may require assistance with regulatory compliance. On February 13, 2009 Washington's Governor Gregoire issued an executive order to streamline capital stimulus projects. The Governor identified the Governor's Office of Regulatory Assistance (ORA) to "help funding agencies ascertain the level of permit readiness for qualifying projects, to advise agencies on how best to educate project proponents about readying their projects for permit and to insure status of permit reviews." CTED will work with applicants to engage ORA, a state agency providing services to ensure that state and national policies are followed when considering likely environmental consequences of proposals. ORA can guide staff and businesses through state and national environmental permitting processes, including the State Environmental Policy Act (SEPA) and National Environmental Policy Act (NEPA).

Goals and Objectives: CTED has undertaken a comprehensive RFP development process for the loan and grant fund that will be completed in June. The evaluation protocol is under development but will likely include, at least, the following elements:

- o Maximize loans (goal is to distribute at least two-thirds of the funds via loans)
- o Leverage ARRA funds by favoring projects that have at least a one-to-one financial match
- o Select projects across a range of risk
- o Create or retain as many jobs as possible
- o Reduce energy consumption
- o Produce renewable energy
- o Reduce greenhouse gas emissions
- o Supplement other funds available from governments, utilities, or private financing
- o Ensuring transparency and accountability

7. Milestones	**Planned Number**
Complete the Design of the Program	1
Develop and Issue Request for Proposals	2
Review Proposals	40-60

Obligate Funds	25-35
Develop and Execute Contracts	25-35
Monitor Contracts (quarterly)	120
Administer Program (ongoing)	1
Receive and Submit Quarterly Reports	12

8. Standard Metrics (required):

Jobs Created: 300-400

Jobs Retained: 100

9. Specific Metric Activity (required):

Number and monetary value of loans given: 15-25 loans, $20-30 million

Number and monetary value of grants given: 5-15 grants, $8.5-18.5 million

Number of renewable energy systems installed: to be determined based on projects chosen

10. Program Year Funds by Source

DOE ARRA Funds	$38,500,000
State Funds	$0
Other Matching Funds	$0
Leveraged Funds Anticipated	$38,500,000

Appendix E: Sound Processes

We identified sound practices based on the 2005 "Guide to Opportunities for Improving Grant Accountability" published by the U.S. Domestic Working Group. Chaired by the U.S. Comptroller General, the group included representatives of the U.S. Government Accountability Office, 18 federal inspector general offices, four state auditors' offices and two local audit offices. We also reviewed the National State Auditors Association report, "Best Practices in Contracting for Services," the U.S. Department of Justice Office of the Inspector General report "Improving the Grant Management Process" and the Washington State Administrative & Accounting Manual (SAAM). The table below summarized our analysis of sound practices and includes our determination of whether or not the State Energy Office implemented the sound practices we identified.

Process	Elements of a Sound System	Commerce did ✓ or did not ✕ follow
	Pre-Award Stage	
Develop Performance Requirements	Clearly identify the service expected.	✓
	Define performance standards and measurable outcomes.	✓
	Identify how vendor performance will be evaluated.	✓
	Ensure that sufficient staff resources are available to handle vendor/ contract management properly.	✓
Request for Proposal	Requires notification or advertising of the solicitation.	✓
	Clearly state the performance requirements and the scope of the services that are to be provided.	✓
	Identify constraints, schedules, deadlines, mandatory items and allowable renewals.	✓
	Specify required deliverables, reporting obligations and payment terms.	✓
	Clearly state grant submission expectations, including closing time, date and location. Clearly state the evaluation criteria and weighting factors for scoring proposals.	✓
	Allow sufficient time for vendors to prepare good proposals.	✓
	Identify federal and state requirements that govern the contracting process and the delivery of services.	✓
	Outline all procurement communication devices to ensure all appropriate grantees or potential grantees have access to the same information, i.e. per-bid conferences, question & answers, whom to contact with questions, etc.	✓
Review and Decision	Grantee screening to ensure only applications that meet solicitation objectives and requirements are sent to review group.	✓
	Application process should identify potential "red flags."	✕
	Establish criteria to gauge the risk associated with new grantees.	✕
	Have appropriate procedures for handling late or incomplete proposals.	✕
	Ensure that an adequate number of proposals were received.	✓

Process	Elements of a Sound System	Commerce did ✓ or did not ✕ follow
	Award Stage	
Review and Decision	Use an evaluation committee, composed of individuals who are trained on how to score and evaluate the proposals and who are free of impairments to independence.	✓
	Use fixed, clearly defined, and consistent scoring scales to measure the proposal against the criteria specified in the RFP.	✓
	Carefully check grantee references.	✕
	Document the award decision and keep supporting materials.	✕
	Based on evaluation team's recommendation, notify unsuccessful and successful applicants in writing.	✓
	Negotiations should not substantially change the terms of the original proposal, but should eliminate any ambiguities in the contract and clarify the terms.	✕
Contract Provisions	Clearly state and define the scope of work, contract terms, allowable renewals and procedures for any changes.	✓
	Provide for specific measurable deliverables and reporting requirements, including due dates .	✓
	Describe the methods of payment, payment schedules and escalation factors if applicable.	✓
	Contain performance standards, with a dispute resolution process.	✕
	Contain inspection and audit provisions.	✓
	Include provisions for contract termination.	✓
	Include provisions for contract renegotiation and/or price escalations if applicable.	✓
	Contain all standard or required clauses as published in the RFP.	✓
	Contain appropriate signatures, approvals, acknowledgements, or witnesses.	✓
	As necessary, allow for legal counsel's review of the legal requirements for forming the contract, which may include a review of the contracting process; legal sufficiency of the contract; the contract terms; etc.	✓

Process	Elements of a Sound System	Commerce did ✓ or did not ✗ follow
Post-Award Stage		
Monitoring and Oversight	Set-up opportunities for training and grantees.	✓
	Assign a contract manager with the authority, resources and time to monitor the project.	✓
	The level of monitoring should be based on a risk assessment of the services provided and the contractor's ability to delivery those services.	✗
	Track budgets and compare invoices and charges to contract terms and conditions.	✗
	Ensure that deliverables are received on time and document the acceptance or rejection of deliverables.	✗
	Retain documentation supporting charges against the contract.	✓
	After contract completion the agency evaluated the contractor's performance on this contract against a set of pre-established, standard criteria and retains this record of contract performance for future use.	(See note)
	As part of completing contract work under the terms of the contract, the contractor may be required to submit a final written report. Upon contract completion, the agency contract manager may want to prepare a contractor evaluation.	(See note)
	Documentation in the contract file, at a minimum, includes the executed contract and all attachments and exhibits incorporated into the contract.	✓

Sources: *State Auditor's Office review of contract files at the Department of Commerce and analysis of the following:*
- *2005 "Guide to Opportunities for Improving Grant Accountability" published by the U.S. Domestic Working Group*
- *National State Auditors Association 2003 report, "Best Practices in Contracting for Services"*
- *U.S. Department of Justice Office of the Inspector General 2009 report "Improving the Grant Management Process"*
- *Washington State Administrative & Accounting Manual (SAAM)*

Note: *We could not evaluate these elements because the program was so new and, as expected, our analysis of project monitoring was limited because projects contracted for had only recently gotten under way at the time of our audit.*

Appendix F: Funding Awards

Competitive Awards Round 1						
Entity	**Location of Project**	**LOAN**	**GRANT**	**Total Awarded**	**Total Est. Project Cost**	**Project Description**
Barr-Tech	**Lincoln**	**$1.5 M**	**$500,000**	**$2 M**	**$11.7 M**	**Build an *anaerobic digester***
Cedar Grove Composting	**King**	**$0**	**$1 M**	**$1 M**	**$9 M**	**Not yet defined**
City of Federal Way	King	$323,000	$0	$323,000	$646,000	Energy efficiency upgrade at City Hall
Farm Power Lynden, LLC	Whatcom	$0	$1.1 M	$1.1 M	$4.7 M	Build an *anaerobic digester*
General Biodiesel Seattle, LLC	King	$1 M	$0	$1 M	$11 M	Upgrade and expand current *biodiesel* facility
GR Silicate Nano-Fibers & Carbonates	**Grays Harbor**	**$1.4 M**	**$0**	**$1.4 M**	**$7 M**	**Expand prototype *nanomaterial* mill at Grays Harbor Paper to a full plant**
Green Energy Today, LLC	Franklin	$0	$898,000	$898,000	$4.5 M	Complete small *hydro-electric generation station* at Esquatzel Canal
MacDonald-Miller Facility Solutions	King	$1.5 M	$0	$1.5 M	$12 M	Improve energy efficiency for Seattle Steam Co. customers
NCS Power Inc.	**Clark**	**$2 M**	**$0**	**$2 M**	**$9 M**	**Establish a plant in Washington to create LED energy-efficient lights**
Port Townsend Paper Corporation	**Jefferson**	**$0**	**$2 M**	**$2 M**	**Application: $55 M**	**Application: Retrofit of boiler & installation of 30MW steam turbine generator**
					Contract: $2.1 M	**Contract: Hardware and software to make current boiler more energy-efficient**
Renewable Energy Composite Solutions, LLC	Clark	$0	$1 M	$1 M	$6.3 M	Prepare vertical wind turbines for commercial sale
Seafreeze Inc.	King	$562,000	$0	$562,000	$1.7 M	Energy efficiency measures
Spokane Intercollegiate Research and Technology (SIRTI) Foundation	Spokane - statewide	$250,000	$0	$250,000	$2.5 M	Establish local equity program to make qualified energy loans and grants
Venoil, LLC	Skagit	$500,000	$0	$500,000	$1.4 M	Complete a *bio-refinery*

Notes: *Bold – Project included in audit.*

Words in italic: Defined on page 41.

Competitive Awards Round 2						
Entity	**Location of Project**	**LOAN**	**GRANT**	**Total Awarded**	**Total Est. Project Cost**	**Project Description**
AltAir Fuels, LLC	**King**	**$0**	**$2 M**	**$2 M**	**Application: $175 M**	**Application: Build refinery to produce renewable aircraft fuel from Camelina**
					Contract: $6.2 M	**Contract: Preliminary engineering for refinery**
Borgford Bioenergy	**Stevens**	**$540,000**	**$231,000**	**$771,000**	**$4.0 M**	**Expand energy park into a state-of-the-art energy production facility**
CAMPS	King — Statewide	$0	$1 M	$1 M	$4.1 M	Transform manufacturing supply chains for solar and wind energy
Clark Public Utilities	Clark	$282,000	$120,000	$402,000	$1.2 M	Improve efficiency of water-cooling process
Demand Energy Networks	**Spokane**	**$0**	**$1.5 M**	**$1.5 M**	**$7.2 M**	**Prepare energy storage units for commercial sale**
FPE Renewables, LLC	Whatcom	$224,000	$96,000	$320,000	$800,000	Construct an *anaerobic digester*
Gen-X Energy Group, Inc.	Grant	$0	$720,000	$720,000	$2.9 M	Develop a *biodiesel* production unit for first stage of a *bio-refinery*
Nippon Paper Industries	**Clallam**	**$1.4 M**	**$600,000**	**$2 M**	**Application: $55 M**	**Application: Replace existing *biomass* boiler with 20MW *cogeneration* boiler**
					Contract: $9.4 M	**Contract: Buy equipment for the *cogeneration* boiler**
Rainier Biogas, LLC	**King**	**$975,000**	**$418,000**	**$1.4 M**	**$6.1 M**	**Not yet defined**

Notes: *Bold — Project included in audit*
Italic — Defined on page 41.

Non-competitive Awards — All projects included in audit Round 3

Entity	Location of Project	LOAN	GRANT	Total Awarded	Matching Funds	Project Description
Cascade Community Wind	Whatcom	$700,000	$300,000	$1 M	$5.7 M	Install wind turbines
EnerG2	Spokane	$1.3 M	$540,000	$1.8 M	$5.5 M	Prepare high performance energy storage device for commercial sale
Dept. of General Administration	Thurston — Statewide	$0	$1.2 M	$1.2 M	$0	Energy efficiency projects at several state agencies
Kadlec Regional Medical Center	Benton	$1.4 M	$600,000	$2 M	$5.5 M	Improve medical center's energy efficiency
SIRTI	Spokane-statewide	$500,000	$750,000	$1.3 M	1.3 M	Additional funds for clean-tech grant/loan program (Round 1)
SGL	Grant County	$0	$2 M	$2 M	$2 M	Design, fabricate and install energy efficiency products
Snohomish PUD	Snohomish	$0	$154,000	$154,000	$495,000	Install turbine to create energy in City of Everett water system
Dept. of Transportation: Ferry Fuel Blending	King	$0	$200,000	$200,000	Approx. $350,000	Install equipment to blend *biodiesel* into Dept. of Transportation ferry fuel
Dept. of Transportation: I-5	Western Washington	$0	$1.4 M	$1.4 M	$10,000	Install fast-charge sites for electric vehicles on Interstate 5
Van Dyk Dairy	Whatcom	$731,000	$313,000	$1 M	$1.2 M	Build an *anaerobic digester*
Whole Energy Fuels	Skagit	$165,000	$0	$165,000	$0	Install equipment to blend *biodiesel* into Dept. of Transportation ferry fuel
WSU Center for Bio-processing & Bio-products Engineering	Whitman	$0	$500,000	$500,000	$0	Expand research and testing of nutrient recovery technology for farm-based *anaerobic digesters*
WSU Energy Program Blower Doors	Thurston - Statewide	$0	$170,000	$170,000	$0	Distribute blower door equipment and train candidates to implement State Energy Code
WSU (for Dept. of General Administration)	Thurston — Statewide	$0	$51,000	$51,000	$0	Develop state agency energy database

Note: *Words in italic are defined below*

DEFINITIONS:

- **Anaerobic Digester:** Anaerobic bacteria break down organic material in the absence of oxygen and produce biogas as a waste product. Biogas produced in anaerobic digesters consists of mostly methane, the major component of Natural Gas.
- **Biodiesel:** Vegetable oil or animal-fat based diesel.
- **Bio-refinery:** A facility that integrates biomass conversion processes and equipment to produce fuel, power, heat and value-added chemicals from biomass.
- **Biomass:** Biological material from living, or recently living organisms.
- **Hydro-electric generation station:** A type of dam used in rivers or canals where a small water storage pond is used to create hydro power.
- **Cogeneration Plant:** The use of a heat engine or power station to simultaneously generate both electricity and useful heat.
- **Nanomaterials:** Capture CO_2 gas and convert it to calcium carbonate for use in paper.

Appendix G: Loans and Grants

The table below summarizes the breakdown between loan and grant awards made throughout the award process, and compares that breakdown to the goals included in Commerce's agreement with the USDOE.

As the table shows, the Office withdrew two awards. In one case, the applicant said the proposed project had secured $10 million in equipment to meet the matching-fund requirement, but later could not confirm ownership of the equipment. The program manager withdrew another award after discovering the contractor was seeking forgiveness of a loan from another division at Commerce.

Loans and Grants Under the State Energy Program

Dollars in Millions

	Loan Only	Grant Only	Grant and Loan	Total Awarded	Total Loans	Total Grants	Total Awarded
Goals	15-25	5-15	0	20-40	$20-30	$8.5-18.5	$ 38.5
Awards Made First Competitive Round	13	5	1	19	$13.6	$6.5	$20.1
Second Competitive Round	0	4	9	13	$7.9	$8.6	$ 16.5
Round Three (Non-Competitive)	0	7	6	13	$ 4.8	$ 6.1	$10.9
Total Awarded Competitively	13	9	10	32	$21.5	$15.1	$36.6
Applicant Withdrew After First Round	4	0	0	4	($3.6)	0	($3.6)
Commerce Withdrew After First Round	1	0	0	1	($1.0)	0	($1.0)
Applicant Withdrew After Second Round	0	0	4	4	($4.5)	($1.9)	($6.4)
Commerce Withdrew During Round Three	1	0	0	1	($0.5)	0	($0.5)
First Round Contracts Signed	8	5	1	14	$9.0	$6.5	$15.5
Second Round Contracts Signed	0	4	5	9	$3.4	$6.7	$10.1
Sole-Source Award	0	1	0	1	$ 0	$2.0	$2.0
Third Round Contracts Signed	0	7	6	13	$ 4.8	$ 6.1	$10.9
Total Contracted	**8**	**17**	**12**	**37**	**$17.2 million**	**$21.3 million**	**$38.5 million**

Source: State Auditor's Office analysis of State Energy Office information.

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