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Commissioner	:	C.S.K. Sandoval
Admin. Law	:	A. Colbert
Judge	:	A. Cole
ORA Witness.	:	

OFFICE OF RATEPAYER ADVOCATES
CALIFORNIA PUBLIC UTILITIES COMMISSION

REPORT
ON THE CONSOLIDATED PROCEEDINGS REGARDING ENERGY SAVINGS ASSISTANCE PROGRAM (ESA) AND CALIFORNIA ALTERNATE RATES FOR ENERGY PROGRAM (CARE)

San Francisco, California
April 27, 2015

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QUALIFICATIONS AND PREPARED TESTIMONY OF ALEXANDER COLE

TESTIMONY ON AUDITING REPORTS

(Witness: Alexander Cole)

I. Background and Introduction

Auditing is a tradition at the California Public Utilities Commission (CPUC).[1] The California utilities Energy Savings Assistance (ESA) program has a total budget in excess of $300 million. The program involves dozens of prime contractors and subcontractors working on marketing, program administration and service delivery. It is critical that ESA programs are administered in compliance with Commission directives, that recordkeeping and tracking of program funds is complete and accurate, and that proper oversight mechanisms are in place to assure that programs are delivering services to qualified homes.

The last audit of the ESA and CARE (California Alternative Rate for Energy) by the CPUC's Department of Water and Audits, Utility Audit, Finance and Compliance Branch (UAFCB hereafter) examined the 2009-2010 programs. Previous to that, D.06-12-038, ordered audits of the CARE and Low Income Energy Efficiency[2] (LIEE) Programs for each IOU for the 2006 and then 2007-2008 program years. All of the aforementioned audits were conducted by the Utility Audit, Finance and Compliance Branch (UAFCB) of the Commission's Division of Water and Audits.[3]

This testimony includes the Office of Ratepayer Advocate's (ORA) summary of findings in the 2007-2008 and 2009-2010 auditor reports. ORA finds that these audits have played a useful role in highlighting potential issues, ensuring that programs are

[1] PUC Code section 314.5 says "The commission shall inspect and audit the books and records for regulatory and tax purposes (a) at least once in every three years in the case of every electrical, gas, heat, telegraph, telephone, and water corporation serving over 1,000 customers, and (b) at least once in every five years in the case of every electrical, gas, heat, telegraph, telephone, and water corporation serving 1,000 or fewer customers. An audit conducted in connection with a rate proceeding shall be deemed to fulfill the requirements of this section. Reports of such inspections and audits and other pertinent information shall be furnished to the State Board of Equalization for use in the assessment of public utilities."

[2] In D.12-08-044 (2012), the Low Income Energy Efficiency program (LIEE) was given its current name, the Energy Savings Assistance Program (ESAP).

[3] This testimony references eight auditing reports conducted by the UAFCB, one for each utility for the 2007-2008 program period and one for each utility for the 2009-2010 period.

complying with Commission directives, that administration and oversight are consistent with best industry practices, and that funds are being applied in the prescribed manner. ORA finds that a trained auditor with full access to company records can identify irregularities that would be extremely difficult to identify under the typical regulatory discovery process.

The 2007-2008 and 2009-2010 program year audits looked at four areas[4]:

1. *Process compliance* – the Standard Practice Manual, Commission decision and directive pertaining to the LIEE and CARE programs, the IOU's own policies and program guidelines for the implementation of LIEE program, customer applications documentations, in-home energy education documentation, and post-inspections reports.
2. *Existence of Safeguards* – the existence of IOU internal controls, including its own policies and procedures.
3. *Integrity of Reporting* –IOU's ESA (or LIEE) and CARE annual reports, accounting systems and balancing accounts.
4. *Oversight Adequacy – the relevant IOU organization chart, duties and responsibilities, and internal monitoring practices over the ESA (LIEE) program.*

II. Summary of Recommendations

ORA recommends the following with respect to CARE/ESA audits:

1. ORA recommends that the Commission order that a Financial, Management and Regulatory Compliance Audit be conducted of each funding cycle. Auditing for the 2015-2017 program cycle should begin in 2016.
2. To assure the maximum access to needed documentation and be of maximum use for the next program cycle, these audits should begin as soon as the 2016 program year is over.
3. There needs to be an institutionalized means for the auditor's findings to enter the public record and for Utilities to respond to the reports. Auditing reports should be posted to the relevant Low Income webpages on Energy Division's website for easy access by all parties.

[4] The Audit Scope as described in each of the reports is identical. An example can be seen in the 2007-2008 program year report for SDG&E, p. 5. Include the complete citation to the SDG&E Audit report

4. In addition, the Utilities should be ordered to file a response to the Auditors findings including a plan for addressing the auditors' recommendations in an advice letter to Energy Division within 30 days of the conclusion of audit. If the Utility does not plan to contest the audits findings, the response should be file in a Tier 2 advice letter. In the event they do plan on contesting the findings of the auditors' report, they should be required to do so in a Tier 3 advice letter.

A. Audit Report on 2007-2008 programs

UAFCB conducted audits of the 2007-2008 CARE and ESA programs for all four IOUs. The scope of each audit was identical across IOUs:

A. Program Accounting and Reporting: To determine whether expenditures and regulatory accounts were being properly recorded and reported to the Commission and whether program expenditures were being excluded from GRC requests.
B. Program Implementation, Processes and Control: *Whether internal controls were in compliance with Commission directives and whether contracts were in compliance with program requirements.*
C. Program Expenditures Analysis and Testing: *To determine and test whether charges, including general administration, were relevant to the programs and supported with appropriate documentation.*
D. Program Oversight*: To determine if internal reporting systems and management oversight processes were in place, executed and working.*

The audits give a reassuring assessment of LIEE program management: with certain exceptions, which are noted in the reports, the LIEE and CARE programs were mostly operated consistently with Commission directives. For example, the Independent Accountant's cover letter introducing the report on PG&E states: "In the opinion of the UAFCB, PG&E complied, in all material respects, with the aforementioned requirements for the two years ending in December 31, 2008."[5] Similarly, the report on SoCal Gas reports no major exceptions to compliance. The reports for the San Diego Gas & Electric Company and Southern California Edison note a single exception: in the case of SDG&E this was the replacement of 916 refrigerators manufactured after 1992[6]; in the case of

[5] Audit of PG&E 2007-2008 program years (Published June 17, 2011), p. ii.

[6] Audit of SDG&E 2007-2008 program years (Published May 13, 2011), p. i.i

SCE it was a failure to comply with the Three Measure Minimum Rule requiring that a house must be eligible to receive at least three measures in order to be treated.[7] Each audit reports audits found sufficient processes in place to assure that LIEE expenditures were not finding their way into general rates cases.

However, the 2007-2008 audits did turn up several potential issues involving Program Implementation, Process and Controls:

- The SCE audit found that SCE failed to demonstrate compliance with Section 4.4 of the SPPM when it provided only CFLs and energy education to 44 % of LIEE participants in 2007 and only 50% in 2008. This was the aforementioned deviation from the "Three Measure Rule" in which a home was only eligible for treatment if it qualified for at least three measures.
  - In their application for the 2015-2018 funding cycle, SCE argues that their actions were not in violation of the Three Measure Rule and that in fact they represented a prudent use of LIEE funds since providing energy education during an initial visit meant that additional trips could be avoided while providing a useful service to households that were not otherwise eligible for treatment. ORA finds this argument convincing. At the same time, we note the usefulness of the audit in bringing this kind of issue to the attention of the Commission.
- The SDG&E audit found that contractors were not taking sufficient measures to deal with potentially hazardous conditions found in the field and recommended that future agreements with contractors should underscore that safety issues requiring urgent attention must be dealt with promptly. A similar issue was noted in the audit of Southern California Gas Company.[8] Both SDG&E and SCE agreed with the auditor's recommendation in this regard and agreed to institute it.[9]
- The SoCalGas audit noted that the SoCalGas had failed to comply with code when its contractors performing in-home assessment failed to adequately assess the need to repair or replace doors.[10]

[7] Audit of SCE 2007-2008 program years (Published June 17, 2011), p. ii.

[8] Audit of SDG&E 2007-2008 program years p. 9-11.

[9] Audit of SDG&E 2007-2008 program, p. C-3; Audit of SoCalGas 2007-2008 program years, p. 12.

[10] Audit of SoCal Gas 2007-2008 program years (Published July 20, 2011), p. 9-13.

The audits also flagged issues regarding IOU administrative oversight of the CARE and ESA program. For example:

- The auditor's report on SCE found that controls to assure the accuracy of enrollments in CARE, such as the analysis of error rates and subsequent corrective action need improvement.[11] In response, SCE took corrective actions to improve customer enrollment. It was noted that future audits should review the effectiveness of these actions.[12]
- PG&E was flagged for not having conducted internal audits or generated any internal reports to PG&E senior management for the monitoring and oversight of the LIEE program.[13] In response to this finding, PG&E stated that it had begun preparing a Quarterly Business Report in 2009. The auditors were uncertain about the effectiveness of this report. In addition, PG&E agreed to work with RHA to modify the Field Employee Development Report that RHA prepares to include a section that addresses any LIEE program deficiencies or areas in need of improvement.[14]
- The auditors recommended that SoCalGas needed to improve their post-installation inspection processes, controls for eligibility and enrollment processing, controls over customer resolution, and controls to update the status of its contractors' standing with the California Contractors License Board (CLSB).[15] In response, SoCalGas implemented a number of actions to correct the issues identified by the auditors.

The above examples, taken from the auditing reports of the 2007-2008 programs, show how audits have been used in the past to help identify administrative irregularities and improve administrative and control practices in the ESAP and CARE programs.

[11] Audit of SCE 2007-2008 program years , p. 19.

[12] Audit of SCE 2007-2008 program years, p. 20.

[13] Audit of PG&E 2007-2008 program years , p. 13.

[14] Audit of PG&E 2007-2008 program years , p. 114-15.

[15] Audit of SoCal Gas 2007-2008 program years, p. 16.

B. Audit Report on 2009-2010 programs

The 2009-2010 audits were organized slightly differently than the 2007-2008 audits, and focused exclusively on the ESAP program, not CARE. The 2009-2010 audit of **SoCalGas** focused on:[16]

1. SoCalGas' weatherization program;
2. General Administrative Costs;
3. Compliance with the Modified Three Measure Minimum Rule;
4. Fund Shifting.

The audits of **SCE, SDG&E and PG&E** covered[17]:

1. ESAP Electric Appliance Programs;
2. General Administrative Costs;
3. Reporting;
4. Internal Controls.

Again, the UAFCB introduced each audit with the judgment that the audited utility program offered a "reasonable degree of compliance with Commission Directives for the 2009-2010 program years, given the limited scope of the audits,"[18] but also noted several areas of non-compliance and suggested actions for remedying these.

The Audit Report of SoCal Gas makes 13 specific observations and recommendations. Among these:

- The auditor's report noted that 29 percent of the customers treated did not have proper documentation to support the customer's or landlord's legal home ownership.[19]
- Auditors found that SoCal Gas had exceeded its authorized budget for 2009 by almost $32 million, or 51% of its budget, in 2009, and by $2.1 million or 3 % of budget in 2010.[20]

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[16] Audit of SoCal Gas 2009-2010 program years (submitted to Energy Division on May 31, 2013), p..A-1 to A-13.

[17] Audit of SDG&E 2009-2010 program years (Submitted to Energy Division on May 31, 2013); Audit of SCE 2009-2010 program years (Submitted to Energy Division on July 17, 2013); Audit of PG&E 2009-2010 program years (Submitted to Energy Division on April 16th 3013).

[18] The language in the Audit of SoCal Gas 2009-2010 program years, p. 1, is repeated in each utility's audit.

[19] Audit of SoCal Gas 2009-2010 program years, p. A-1.

- Auditors found issues with SoCalGas's general administration, including the shifting of expenses to time-periods other than when the cost was accrued;[21]
- SoCal Gas failed to properly report funds that it was carrying forward between program periods[22].

SoCalGas agreed with twelve of the auditor's recommendations and has conducted internal audits to

The Audit Report of SDG&E makes 6 specific observations offering recommendations for improvement on 9 of these and no-recommendation on 6 others. Among these:

- SDG&E had provided $1.2 million in ESAP measures to ineligible customers or ineligible measures to customers between 2007 and 2011. This included such things as replacing refrigerators manufactured after the cut-off year from the program.
  - The UAFCB suggested that should SDG&E choose to offer measures to ineligible customers, they should directly pay for these measures.[23] SDG&E argued that it generally agrees with the UAFCB's recommendation to adhere to Commission directives, however asserted that it may be appropriate to charge certain costs on a case by case basis. The auditors replied that legitimate home repairs as to the P&P manual are not an issue.

The Audit Report of PG&E makes 15 specific observations offering recommendations for improvement on 9 of these and no-recommendation on 6 others. Among these:

- Auditors flagged the fact that PG&E reported the costs incurred to administer the ESA program incurred by its prime contractor, Richard Heath Associates (RHA), not as part of it's administrative costs, but instead included them in costs of measures. In doing so, they obscure the overall administrative costs of the program.

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[20] Audit of SoCal Gas 2009-2010 program years, p. A-3.

[21] Audit of SoCal Gas 2009-2010 program years, p. A-8 to A-9.

[22] Audit of SoCal Gas 2009-2010 program years, p. A-13.

[23] Audit of SDG&E 2009-2010 program years, p. A-1 to A-3.

- The audit report cites D.09-09-047, in which Commission discusses the importance of budgetary transparency, particularly in regards to administrative costs and caps administrative costs at 10 % for energy efficiency programs.[24] While the auditors do not recommend a 10 % cap on ESA administrative costs, they do argue that transparency in accounting is necessary in order for the Commission to continue to make informed decisions.
- As a remedy, the auditors recommended that all four utilities need to agree to a common system for accounting for administrative costs under Energy Division guidance, and that PG&E adapt its accounting to conform to this agreed upon system. As of this this testimony, the agreed upon accounting standards have not developed and this issue remains unresolved.[25]

The Audit Report of SCE makes 9 specific observations offering 6 recommendations, including the recommendation that SCE needs to demonstrate to UAFCB whether it is has implemented recommendations from prior examination reports. Among these:

- The UAFCB found that SCE had continued to supply energy education inappropriately to homes that were not eligible or had not passed the Three Measure Minimum.
  - While SCE asserted that D.08-11-031 did not prohibit it from providing energy education to income-qualified customers who did not receive any measures, the auditor argues that they are not entitled to charge the ESA program should they chose to do so. UAFCB recommended at that time that SCE should be required to refund ESAP with shareholder funds for the amount it spent providing only energy education between 2007 and 2011.[26]
- The UAFCB found that SCE inappropriately carried back $4.5 million of funds from 2009 into 2008 when it didn't have Commission authorization to do so. The

[24] D.09-09-047, p. 55-64 discusses budgetary transparency and total administrative costs for Energy Efficiency programs. "TURN and DRA correctly point out that the utilities' administrative costs lack transparency and it is difficult to determine accurately the total cost of the energy efficiency portfolios or whether the utilities' costs were properly classified as administrative costs or direct implementation costs.... Therefore, we adopt the DRA recommendation that we require the utilities to provide a detailed breakdown of all administrative costs required to support energy efficiency programs, including regulatory costs and other partial support functions, in their compliance filing in response to this decision. (D.09-09-047. pp. 55-56)."

[25] Audit of PG&E 2009-2010 program years, p. A-3 to A-5.

[26] Audit of SCE 2009-2010 program years, p. A-3 to A-6.

UAFCB recommended that SCE refund ESA with shareholder funds for the $4.5 million it transferred without authorization and that if SCE does not refund the monies voluntarily, Energy Division or the Commission should require it to do so.

SCE offered an extensive rebuttal to both of these observations.[27] On the issue of whether SCE had violated the Three Measure Minimum rule in providing Energy Education to some customers, SCE argues that there is no rule against providing education during an initial visit to assess a home and that by combining these two visits, the company was providing a valuable service at little additional cost. In response to the charge that SCE had inappropriately carried back funds between program years without authorization, SCE argued convincingly that this kind of carry back was permissible as it allows programs with a long ramp-up time continue between program years with a minimum of disruption.

III. Conclusions and ORA Recommendations

Based on our review of the UAFCB Audits of CARE and LIEE/ESA for the 2007-2008 and 2009-2010 program years, ORA concludes that the IOUs have generally complied with CPUC policies and that reporting and have exercised reasonable oversight over the execution of these policies. These reports do not identify any instances of gross maleficence or non-compliance. In the one item where an IOU seemed to deliberately deviate from PUC policy – SCE's delivery of Energy Education to income qualified households that did not meet the 3-measure minimum rule and therefore could not be 'treated'-- we find SCE's justifications for the actions in their reply to the draft auditing report satisfactory.

The auditor's finding that PGE does not report administrative costs incurred by their main subcontractor, Richard Heath Associates, in a transparent way was accompanied by a recommendation that they seek Energy Division guidance in developing a common system for accounting for Administrative Costs. Our understanding is that no common system or guidelines were ever developed. In light of

[27] SCE has published their response to the Draft Interim Auditor Report in their Energy Assistance Program Plan and Budget Proposal for the 2015-2017 Program Cycle, Appendix C, Attachment C-1.

this inaction, PG&E has continued to include subcontractor administrative costs within specific measure costs, a practice that effectively obscures the total amount that PG&E and RHA are spending on administration. ORA recommends the Commission follow up on the auditor's recommendation to fashion common guidelines for reporting administrative costs both internally and among subcontractors so that parties can easily identify the true amounts being spend on administration and differentiate these from program costs.

These larger issues aside, the last two UAFCB accomplished what audits are intended to do: they identified potential issues of non-compliance or administrative weakness so that these can be corrected. In the absence of follow-up audits, it is difficult to know how effectively the utilities' responses to the issues identified in these reports have been. In light of this, ORA recommends that a new set of audits be ordered for the 2105-2017 funding cycle and that audits be repeated at least once every funding cycle going forward. Given the size of ESA budgets, ORA notes that it is critical for the utilities to be "on notice" that their management practices associated with ESA will be reviewed by the Commission through a regular cycle of audits.

Specifically, **ORA Recommends:**

- The Commission should order that a Financial, Management and Regulatory Compliance Audit be conducted of each funding cycle. This should begin with an audit of each IOU's CARE and ESA program by the Commission's UAFCB in 2016.
- To assure the maximum access to needed documentation and be of maximum use for the next program cycle, these audits should begin as soon as the 2016 program year is over.
- To increase transparency, ORA recommends that a workshop be convened so that UAFCB can educate parties about the purpose and process of auditing and parties can express specific concerns to auditors.
- Final auditing reports should be posted to the relevant Low Income webpages on Energy Division's website in a timely manner for easy access by all parties.

- The Utilities should be ordered to file a response to the Auditors findings including a plan for addressing the auditors' recommendations in an advice letter to Energy Division within 30 days of the conclusion of audit. If the Utility does not plan to contest the audits findings, the response should be file in a Tier 2 advice letter. In the event they do plan on contesting the findings of the auditors' report, they should be required to do so in a Tier 3 advice letter.

APPENDIX A

QUALIFICATIONS AND PREPARED TESTIMONY
OF
ALEXANDER COLE

My name is Alexander Cole, and my business address is 505 Van Ness Avenue, San Francisco, California. I am a Public Utilities Regulatory Analyst II in the Electricity Pricing and Customers Programs Branch of the Organization of Ratepayer Advocates (ORA) at the California Public Utilities Commission.

I joined the Commission in January 2013 to work with Energy Division on the Long Term Procurement Plan and related issues in Generation and Transmission Planning.

My educational background includes a PhD in Innovation and Organizational Economics from the Copenhagen Business School (2014) and a M.A. (1997) and B.A. (1991) from the University of California, Berkeley.

QUALIFICATIONS AND PREPARED TESTIMONY
OF
Alexander Cole

Q.1. Please state your name and business address.

A.1 My name is Alexander Cole, and my business address is 505 Van Ness Avenue, San Francisco, California.

Q.2. By whom are you employed and in what capacity?

A.2. I am a Public Utilities Regulatory Analyst II in the Electricity Pricing and Customers Programs Branch of the Organization of Ratepayer Advocates (ORA) at the California Public Utilities Commission.

Q.3. Please describe your professional experience.

A.3 I joined the Commission in January 2013 to work with Energy Division on the Long Term Procurement Plan and related issues in Generation and Transmission Planning.

Q.4. Please describe your educational background and qualifications

A.4 My educational background includes a PhD in Innovation and Organizational Economics from the Copenhagen Business School (2014) and a M.A.(1997) and B.A. (1991) from the University of California, Berkeley.

Q.5 What is your area of responsibility in this proceeding?
A.5. I prepared ORA's Report on the Audits of the CARE and ESA Programs.

Q.6. Does this complete your testimony
A.6. Yes, it does