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Superintendent Robert Defour
Members of the Board of Education
Eldred Central School District
600 State Route 55
Eldred, NY 12732

Report Number: P4-13-2

Dear Superintendent Defour and Members of the Board of Education:

The Office of the State Comptroller works to help school district officials manage their resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Education governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard district assets.

In accordance with these goals, we conducted an audit of eight school districts in Broome, Delaware, Schoharie, Sullivan and Tompkins Counties. The objective of our audit was to determine whether energy performance contracts (EPCs) entered into by school districts achieved the cost and/or energy savings projected by the vendor who executed the contract. We included the Eldred Central School District (District) in this audit. Within the scope of this audit, we examined the District's EPCs, including the Energy Service Companies' (ESCO) projections, and reviewed energy consumption and costs for the period October 1998 through June 19, 2013. However, due to the District's lack of records and monitoring of the EPCs, numbers reported here are for illustrative purposes and we could not corroborate some of the key projections.

This report of examination letter contains our findings and recommendations specific to the District. The results of our audit and recommendations have been discussed with District officials. District officials were given an opportunity to respond to our findings and recommendations within 30 days of the exit conference, but they did not respond. At the completion of our audit of the eight school districts, we prepared a global report that summarizes the significant issues we identified at all of the school districts audited.

Summary of Findings

The District has two EPCs currently in place with two ESCOs. A number of records supporting these contracts were not available at the District; therefore, numbers reported here are for illustrative purposes and we were unable to corroborate key pieces of the finding. The District is projected to exceed the energy cost savings guaranteed by the ESCO that executed the 2002 EPC. Over the life of this EPC, the energy cost savings are projected to total approximately \$615,100. Additionally, District expenditures are expected to total \$686,600, for a net loss of \$71,500 before inclusion of any State aid. With the receipt of State aid, the total savings are projected to amount to approximately \$47,700.

However, the District is not projected to achieve the energy cost savings guaranteed by the ESCO that executed the 2008 EPC. Over the life of this EPC, the energy cost savings are projected to total approximately \$407,200 and the operational savings for maintenance are projected to total \$8,000, for a total cost savings of \$415,200. The ESCO guaranteed energy cost savings of \$602,000 and operational cost savings of \$8,000, totaling \$610,000. Additionally, District expenditures are expected to total \$830,300, for a net loss of \$415,100 before inclusion of any State aid. With the receipt of State aid, the total loss is projected to amount to approximately \$190,000.

Background and Methodology

Article 9 of the Energy Law establishes procedures to be used by school districts in initiating and administering EPCs. An EPC is an agreement by an ESCO for the provision of energy services in which energy systems are installed, maintained or managed to improve the energy efficiency of, or produce energy for, a facility in exchange for a portion of the energy savings or revenues. EPCs are not subject to voter approval or competitive bidding requirements and the length of the contract must not exceed the useful life of the building (which the New York State Education Department has established at 18 years). In addition, school districts should establish procedures to monitor these EPCs. The ESCO may agree to guarantee that the improvements will generate cost savings sufficient to pay for the project over the term of the EPC; however, cost savings are not a requirement for a successful contract. After the EPC ends, the school districts may continue to realize additional cost savings as a result of the improvements.

The District is located in Sullivan County and has two buildings in operation. It has approximately 690 students and general fund budgeted appropriations of \$16.3 million for the 2013-14 fiscal year. The District is governed by a five-member Board of Education (Board). The Board is responsible for conducting the business of the District within the laws of the State and regulations of the New York State Commissioner of Education.

In May 2002, the Board entered into an EPC with an 18-year contract term from November 2003 through October 2021. This EPC was completed in October 2003 and included several upgrades to the energy management system, heating and lighting in the high school. The ESCO guaranteed an energy cost savings of \$600,900 over the life of the EPC. The capital cost of this project totaled approximately \$425,800. The ESCO monitored the energy cost savings for the first five years of the EPC until the District canceled this service in December 2008.

Additionally, in December 2008, the Board entered into another EPC with another ESCO with an 18-year contract term from August 2011 through July 2029. This EPC was completed in July 2011 and included window replacements at the high school, transformer replacement at the elementary school and several upgrades to the lighting and insulation at both buildings. The ESCO guaranteed an energy cost savings of approximately \$602,000 and an operational cost savings of almost \$8,000. The capital cost of this project totaled \$600,000. The ESCO went out of business after the project was completed and has not performed any annual monitoring of the savings; therefore, there may be adjustments that may need to be considered. The current District officials were not in their positions when the EPCs were entered into and a number of the records supporting these contracts could not be located during our audit.

To accomplish our objective, we interviewed District officials. We also reviewed the EPCs to obtain the scope of the work, the cost of the project, the length of the contract, the contracted ongoing maintenance and verification costs, and the guaranteed energy cost savings and operational savings over the life of the project. We obtained the utility data, including the consumptions, costs (when available) and rates for the base years for both EPCs. However, due to a lack of records available at the District, we could not verify the reasonableness of either ESCOs' base-year calculations. The 2002 EPC's base year ranged from October 1998 through September 1999, while the 2008 EPC's base year was January 2005 through December 2005. We also verified both ESCOs' projected increases in utility rates, based on utility costs for New York State from the U.S. Energy Information Administration from 1990 to 2000, to verify an average increase in utility costs of 2 percent was reasonable and from 1995 to 2005 to verify an average increase in utility costs of zero percent was reasonable. For the 2002 EPC, to calculate the projected energy cost savings, we used the ESCO's reported realized energy savings for the first four years and the ESCO's guaranteed energy cost savings for the remaining 14 years (November 2007 through October 2021). To calculate the projected energy costs savings for the 2008 EPC, we used the ESCO's reported consumption for the base-year (January 2005 through December 2005) and subtracted the actual energy consumption for the first completed year of August 2011 through July 2012. We then multiplied that savings by the base-year's utility rates with an annual zero percent increase over the life of the project. We used this energy cost savings calculated for August 2011 through July 2012 to project out the remaining 17 years (August 2012 through July 2029) of the EPC. We also attempted to document the lease payments over the life of the contracts; however, we were unable to corroborate the information obtained from the EPCs. We determined the expenditures related to each EPC and subtracted them from the total cost savings calculated to identify any potential savings. We also attempted to obtain any information regarding grants and State aid received or expected to be received for the EPCs to consider the net benefit to the District; however, we were unable to corroborate these figures.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). 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 that the evidence we were able to obtain provides a reasonable basis for our findings and conclusions based on our audit objective. However, there was a lack of evidence available at the District to corroborate some of the key projections reported.

Audit Results

The District's 2002 EPC is projected to achieve energy cost savings that exceed the \$600,900 in energy cost savings guaranteed by the ESCO, as shown in Table 1.

Projected Energy Cost Savings	\$615,055
Lease Payments Including Interest	\$669,852
Ongoing Maintenance and Verification	\$16,741
Net Benefit Without State Aid	(\$71,538)
Projected State Building Aid	\$119,221
Net Benefit With State Aid	\$47,683

Over the life of the EPC, the energy cost savings¹ are projected to total about \$615,100. District expenditures to implement the terms of the EPC total approximately \$686,600, for a net loss to the District of about \$71,500 before inclusion of any State aid. With the receipt of State aid, the total savings are projected to amount to approximately \$47,700. However, due to a lack of records at the District, we were unable to corroborate this information.

For the 2008 EPC, the District is not projected to achieve the ESCO's guaranteed energy cost savings of \$602,000, but is expected to achieve the guaranteed operational cost savings of \$8,000. However, the District is still projected to achieve energy and operational cost savings of just over \$415,000, as shown in Table 2.

Because the ESCO went out of business, the ESCO did not do any monitoring or verification that the guaranteed savings were met; therefore, we could not determine if there were adjustments that would need to be made. The current District officials were not in their positions when either EPC was implemented and there was a lack of records available for both EPCs, adding to the difficulty in determining if any adjustments were necessary or corroborating any of the information. We calculated that the District had only realized an energy cost savings of approximately \$22,600 for the first measurable year, which was \$10,800 less than the guarantee for that time period. This difference results in our total projected energy cost savings being \$194,800 less than the ESCO's guaranteed savings over the life of the EPC.

Projected Energy Cost Savings	\$407,250
Projected Operational Cost Savings	\$7,974
Total Projected Energy and Operational Savings	\$415,224
Lease Payments including Interest	\$830,295
Net Benefit without State Aid	(\$415,071)
Projected State Building Aid	\$225,030
Net Benefit with State Aid	(\$190,041)

¹ To calculate the 2002 EPC's projected energy costs, we utilized the first four years (November 2003 to October 2007) of the ESCO's reported realized energy savings. We utilized the ESCO's guaranteed energy cost savings to project the cost savings over the remaining 14 years of the EPC (November 2007 to October 2021).

Over the life of the 2008 EPC, the energy cost savings² are projected to total approximately \$407,200 and the operational savings for maintenance are projected to total \$8,000, for a total cost savings of \$415,200. However, District expenditures are expected to total \$830,300, for a net loss of \$415,100 before inclusion of any State aid. With the receipt of State aid, the total net loss is projected to amount to approximately \$190,000. However, due to a lack of records at the District, we were unable to corroborate this information.

The District does not have any monitoring procedures in place. The ESCO for the 2002 EPC had provided reports for years one through five showing the actual realized savings; however, District officials were only able to locate the reports for years one through four. In 2008, District officials canceled the contract with the ESCO to perform ongoing monitoring and verification that the District is achieving the guaranteed savings because they wanted to save the additional cost. The ESCO for the 2008 EPC did not perform any monitoring because it went out of business after the project was completed in 2011. District officials stated that they did not see any reason to monitor the 2008 EPC because they do not think they could seek recourse to recover any of the guaranteed savings.

Recommendations

1. Before considering an EPC in the future, District officials should perform a cost-benefit analysis based on the ESCO's projected energy cost savings and negotiated contractual terms to determine if the investment in energy upgrades is beneficial.
2. District officials should implement monitoring procedures to include timely reviews of the District's electricity, fuel oil and propane consumption and the related costs and compare their reviews to the annual guaranteed energy cost savings to ensure those guarantees are being met.
3. District officials should consider consulting the District's legal counsel if they find that the guaranteed savings have not been met to determine whether they should take action to recoup the difference between the amount of cost savings that was guaranteed by the ESCO and the District's actual savings/losses.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the Education Law, and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and forwarded to our office within 90 days. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft

² To calculate the projected energy costs for the 2008 EPC, we utilized the actual energy consumption prior to the EPC for the base-year (January 2005 through December 2005) and subtracted the actual energy consumption from August 2011 through July 2012. We then multiplied the consumption savings and losses by the base-year utility rates with annual zero percent increase. We then used August 2011 through July 2012 to project out the remaining 17 years of energy cost savings (August 2012 through July 2029) of the EPC, utilizing the zero percent increase.

audit report. The Board should make the CAP available for public review in the District Clerk's office.

Our office is available to assist you upon request. If you have any further questions, please contact H. Todd Eames, Chief Examiner of the Binghamton Regional Office, at (607) 721-8306.

Sincerely,

Gabriel F. Deyo