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April 11, 2014

Superintendent Dr. Ivan Katz
Members of the Board of Education
Fallsburg Central School District
115 Brinkman Road
Fallsburg, NY 12733

Report Number: P4-13-4

Dear Superintendent Katz 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 Fallsburg Central School District (District) in this audit. Within the scope of this audit, we examined the District's EPC and reviewed energy consumption and costs for the period January 1, 2009 through June 30, 2013.

This report of examination letter contains our findings and recommendations specific to the District. We discussed the findings and recommendation with District officials and considered their comments, which appear in Appendix A, in preparing this report. District officials generally agreed with our recommendation and indicated they planned to take correction action. 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 will likely achieve the energy cost and consumption savings projected by the energy service company (ESCO) who executed the EPC. However, these cost savings are achieved only when grants and State aid are factored into the calculation. Although the energy savings are projected to total approximately \$3.14 million over the life of the EPC, the total expenditures are approximately \$3.45 million, netting to a loss of approximately \$312,700. When the grants and State aid are included, the District is projected to save a total of almost \$851,500.

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 1,490 students and general fund budgeted appropriations of \$36.6 million for the 2013-14 fiscal year. The District is governed by a nine-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 February 2011, the Board entered into an EPC with an 18-year contract term from July 2012 through June 2030. The related project work was completed in June 2012 and included upgrades to the boilers, lighting, heating, ventilation and air controls, and air conditioning units and the installation of a pool cover. The ESCO guaranteed both energy consumption and energy cost savings from these upgrades. The total capital project cost was \$1.99 million.

To accomplish our objective, we interviewed District officials and a representative from the ESCO. We also reviewed the EPC to obtain the scope of the work, the cost of the project, the length of the contract, the contracted ongoing maintenance and verification costs, the guaranteed energy and cost savings and the projected energy cost savings over the life of the project. We obtained utility data including consumption, costs and rates for the base year of January 2009 through December 2009 and verified the reasonableness of the ESCO's base-year calculations. We also verified the ESCO's projected increase in utility rates based on utility costs for New York State from the U.S. Energy Information Administration from 1999 through 2009 and verified an average increase in utilities of 3.5 percent was reasonable. We verified the reasonableness of the ESCO's annual measurement and verification report for July 2012 through June 2013 by subtracting the annual costs and consumption for the same period from the base

year's cost and consumption and comparing it to the ESCO's energy cost and consumption savings in the report. We then utilized the ESCO's reported energy cost savings for July 2012 through June 2013 and the ESCO's guaranteed cost savings from July 2013 through June 2030 to project out the energy cost savings over the life of the EPC. We documented the lease payments over the life of the contract using the payment schedule. We then subtracted the expenditures related to the EPC from the total cost savings calculated to identify any potential savings. We also considered any grants and State aid received or expected to be received relating to the EPC.

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 obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Audit Results

The District's EPC is projected to exceed the guaranteed energy cost savings of \$3.11 million and achieve the guaranteed annual energy consumption savings of 388,590 kilowatt hours, 977 kilowatts and 33,568 gallons of fuel oil. Over the life of the EPC, the energy cost savings¹ are projected to total approximately \$3.14 million as shown in Table 1.

Table 1: Projected Energy Cost Savings Over the Life of the EPC	
Total Projected Energy Cost Savings	\$3,137,862
Lease Payments Including Interest	\$2,595,214
Monitoring and Verification Costs	\$855,377
Net Benefit Without Grants and State Aid	(\$312,729)
Grants Received	\$57,022
Projected State Building Aid	\$1,107,192
Net Benefit With Grants and State Aid	\$851,485

However, District expenditures to implement the terms of the EPC total approximately \$3.45 million, for a net cost to the District of approximately \$312,700 before any grants or State aid. However, with the receipt or potential receipt of grants and State aid, the total savings will amount to \$851,485.

The District has monitoring procedures in place. The District's Business Manager monitors the energy consumption and costs monthly by recording the monthly cost and consumption from the energy bills into a spreadsheet. He reviews any large increases or decreases as they occur, month to month. The ESCO also has prepared a measurement and verification report for the first completed year. The Business Manager plans on reviewing the report and comparing the data used by the ESCO to the data he has been capturing.

¹To calculate the projected energy cost savings, we utilized the actual energy cost savings reported by the ESCO in its measurement and verification report for July 2012 through June 2013. We then used the ESCO's guaranteed energy cost savings to project out the energy savings for the remaining 17 years (July 2013 through June 2030) of the EPC.

Recommendation

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.

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 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

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following page.

FALLSBURG CENTRAL SCHOOL DISTRICT

Ivan Katz, Ed. D., Superintendent of Schools

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PARTNERSHIPS



KEY TO EXCELLENCE

November 18, 2013

Mr. Andrew A. SanFilippo
Executive Deputy
Office of State and Local Government
110 State Street
Albany, NY 12236


Dear Mr. SanFilippo:

The Fallsburg Central School District Board of Education and Administration submit this letter as its official response and corrective action plan for the recent examination of the Energy Performance Contract (EPC). The Board of Education and the Administration agree with the finding in the report.

The report found that the energy costs and consumption saving achieved by the EPC along with grants and state aid on the project will be more over the life of the EPC than the debt service payments for the EPC. The recommendation is that if the district were to consider an EPC in the future, district officials should perform a cost-benefit analysis based on the Energy Service Company projected energy cost savings and negotiated contractual term to justify the District's investment in energy upgrades. The Board of Education and the Administration will perform a cost-benefit analysis before entering into any future EPC.

The Fallsburg Central School District would like to thank the audit team from your office for their diligent work in analyzing the costs and benefits of the EPC and the helpful suggestions they provided to us to improve our operations.

Sincerely,


Joseph Collura
President
Board of Education

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Together, we will make a difference