

Audit Report

Maryland Energy Administration

December 2020



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber
Executive Director

Gregory A. Hook, CPA
Legislative Auditor

December 16, 2020

Senator Clarence K. Lam, M.D., Senate Chair, Joint Audit and Evaluation Committee
Delegate Carol L. Krimm, House Chair, Joint Audit and Evaluation Committee
Members of Joint Audit and Evaluation Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Maryland Energy Administration (MEA) for the period beginning July 1, 2016 and ending March 15, 2020. MEA manages programs which help reduce energy consumption and provides grants and loans for these programs.

Our audit disclosed a lack of formal documentation for the evaluation and awarding of discretionary grants. Specifically, although eligibility criteria for such grants existed, MEA did not have written policies and procedures addressing how this criteria was to be applied when evaluating discretionary grant applications and for determining the related amounts to be awarded. During fiscal year 2017 through 2019, MEA awarded discretionary grants totaling approximately \$85.6 million.

Our audit also included a review to determine the status of the finding contained in our preceding report. We determined that MEA satisfactorily addressed this finding.

MEA's response to this audit is included as an appendix to this report. In accordance with State law, we have reviewed the response and noted that although MEA disagrees with one of the recommendations in this report, the corrective actions identified are sufficient to address all audit issues. In accordance with generally accepted government auditing standards, we have included an "auditor comment" within MEA's response to explain our position.

We wish to acknowledge the cooperation extended to us during this audit by MEA and its willingness to address the audit issues and implement appropriate corrective actions.

Respectfully submitted,

A handwritten signature in black ink that reads "Gregory A. Hook". The signature is written in a cursive style with a prominent initial "G".

Gregory A. Hook, CPA
Legislative Auditor

Background Information

Agency Responsibilities

The Maryland Energy Administration (MEA) manages programs which help reduce energy consumption in State facilities and operations; encourage the use of renewable energy resources; and promote energy efficiency in the industrial, commercial, and residential sectors. MEA also provides grants and loans for State agencies, local governments, nonprofit organizations, and the commercial sector. MEA advises the Office of the Governor on energy policy and managing energy disruptions and emergencies. MEA is the state conduit for federal energy programs from the United States Department of Energy. According to the State's records, MEA's total expenditures for fiscal year 2019 were \$33.2 million, including grants and loans of \$26.7 million.

The majority of MEA's funding comes from the Maryland Strategic Energy Investment Fund (SEIF). In this regard, State law established the Maryland Strategic Energy Investment Program for the purpose of decreasing energy demand and increasing energy supply to promote affordable, reliable, and clean energy to fuel Maryland's future prosperity. By law, MEA administers the Program, as well as the SEIF, which was established to implement the Program.

The SEIF funds various programs, including the promotion, development, and implementation of cost-effective energy efficiency and conservation programs; renewable and clean energy resources; climate change programs; and demand response programs that are designed to promote changes in electric usage by customers. In addition, SEIF funds are used to supplement funds for low-income energy assistance, to provide rate relief by offsetting electricity rates, and to provide grants and loans to implement energy-related public education and outreach initiatives. SEIF also provides funding for programs in certain other State agencies, such as the Department of Human Services. SEIF is funded primarily by quarterly auctions of carbon allowances through the Regional Greenhouse Gas Initiative. According to its annual report, SEIF revenues and expenditures totaled approximately \$97.1 million and \$76.8 million, respectively, during fiscal year 2019.

Maryland Clean Energy Center

The Maryland Clean Energy Center (MCEC) was established in 2008 as an instrumentality of the State to promote economic development and jobs in the clean energy industry, and to facilitate the deployment of clean energy technology in Maryland. According to MEA records, since its inception, MCEC has received

approximately \$8.9 million in grants and loans from MEA for the purpose of start-up funding and operating costs. In our preceding audit report, we noted that MCEC had been unable to make current payments on certain loans from MEA. In addition, we noted the certified public accounting firm that audited MCEC's financial statements for the years ended June 30, 2014 and June 30, 2015 stated that there was substantial doubt about MCEC's ability to continue as a going concern, due in part to its reliance on MEA grants and loans to meet cash flow demands.

During the 2017 Legislative Session, the Maryland General Assembly passed legislation (Chapters 364 and 365, Laws of Maryland 2017, effective July 1, 2017) which converted loans totaling \$1.3 million to grants resolving any outstanding loans. The legislation also established the Maryland Energy Innovation Fund (MEIF) as a funding source for MCEC and required \$1.5 million to be transferred from the SEIF to MEIF annually for fiscal years 2018 through 2022¹.

Finally, this legislation directed MCEC to establish a plan to become self-sustaining by fiscal year 2023. In December 2019, MCEC advised the Governor and the General Assembly that it will require a continued commitment of funds from the SEIF beyond fiscal year 2022 in order to achieve self-sustainability.

Status of Finding From Preceding Audit Report

Our audit included a review to determine the status of the finding contained in our preceding audit report dated January 11, 2017. We determined that MEA satisfactorily addressed this finding.

¹ The MEIF is used jointly by MCEC and the Maryland Energy Innovation Institute. MCEC reported that it receives approximately \$900,000 of the \$1.5 million transferred annually from the SEIF to MEIF.

Findings and Recommendations

Discretionary Grants

Finding 1

The Maryland Energy Administration (MEA) did not have written policies and procedures for applying grant criteria when evaluating discretionary grant applications and for determining the amounts to be awarded.

Analysis

MEA did not have written policies and formal procedures for applying grant criteria when evaluating discretionary grant applications and for determining the amounts to be awarded. MEA awards discretionary grants to government and private organizations throughout Maryland to help increase renewable energy resources and to promote energy efficiency. According to MEA records, during fiscal year 2017 through 2019, MEA awarded discretionary grants totaling approximately \$85.6 million, which accounted for the majority of the \$88.2 million in grants awarded by MEA.

We reviewed the grant award process used by MEA for all discretionary grants. In addition, we reviewed MEA's evaluations of grant applications which resulted in 125 grant awards from the Clean Energy Communities Low-to-Moderate Income (LMI) Program totaling \$19.8 million between fiscal years 2017 and 2019. We noted that MEA subject matter experts evaluated discretionary grant applications based on certain criteria included in the related grant solicitations. However, MEA lacked written policies and formal procedures for conducting these evaluations, and did not document how the criteria were used to select grantees and determine the specific amounts awarded.

For example, our review of MEA's evaluation of all 55 LMI grant applications received for fiscal year 2019 disclosed that MEA did not document how the factors noted in the solicitation were used to select the 24 applications that were ultimately awarded grants totaling approximately \$4.8 million. In this regard, the solicitation stated that the grant applications were to be evaluated primarily based on two factors: the project's potential energy savings per dollar of MEA investment and the number of LMI residents served. However, MEA did not document how those factors were considered in selecting award recipients, and there was no evidence that they assigned more significance to those two primary factors versus other less significant factors such as prior performance.

In addition, MEA did not document how it used those factors to determine the amounts awarded to the 24 grantees, which ranged from 18 to 100 percent of the

amounts requested in the respective grant applications. In this regard, we noted a grantee that proposed to serve 30 residents was awarded the entire \$100,000 requested (\$3,333 per resident to be served), while another grantee that proposed to serve 53,415 residents was awarded \$368,000 of the \$640,000 requested (\$6.88 per resident to be served).

MEA management advised us that it believed the existence of the aforementioned criteria was sufficient. However, without adequate written policies and procedures describing how the criteria should be evaluated and resultant grant decisions reached, assurance was lacking that grant decisions were justified and consistent, as demonstrated by the examples in this analysis.

Recommendation 1

We recommend that MEA

- a. establish written policies and procedures for the application of grant criteria when evaluating discretionary grant applications and for determining the amounts to be awarded, and**
- b. ensure discretionary grants are awarded in compliance with the newly established policies and procedures and that documentation is retained for audit purposes.**

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Maryland Energy Administration (MEA) for the period beginning July 1, 2016 and ending March 15, 2020. The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine MEA's financial transactions, records, and internal controls, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included grant programs, cash receipts, contract procurement and monitoring, and special funds including the Strategic Energy

Investment Fund. We also determined the status of the finding contained in our preceding audit report.

Our audit did not include certain support services provided to MEA by the Executive Department – Office of the Governor. These support services (such as maintenance of FMIS accounting records and related fiscal functions) are included within the scope of our audits of the Executive Department - Office of the Governor. In addition, our audit did not include an evaluation of internal controls over compliance with federal laws and regulations for federal financial assistance programs and an assessment of MEA’s compliance with those laws and regulations because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including MEA.

Our assessment of internal controls was based on agency procedures and controls in place at the time of our fieldwork. Our tests of transactions and other auditing procedures were generally focused on the transactions occurring during our audit period of July 1, 2016 to March 15, 2020, but may include transactions before or after this period as we considered necessary to achieve our audit objectives.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, tests of transactions, and to the extent practicable, observations of MEA’s operations. Generally, transactions were selected for testing based on auditor judgement, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State’s Financial Management Information System (such as revenue and expenditure data). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from this source were sufficiently reliable for the purposes the data were used during this audit. Finally, we performed other auditing procedures that we considered necessary to achieve our objectives. The reliability of data used in this report for background or informational purposes was not assessed.

MEA’s management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records;

effectiveness and efficiency of operations, including safeguarding of assets; and compliance with applicable laws, rules, and regulations are achieved. As provided in *Government Auditing Standards*, there are five components of internal control: control environment, risk assessment, control activities, information and communication, and monitoring. Each of the five components, when significant to the audit objectives, and as applicable to MEA, were considered by us during the course of this audit.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes a finding relating to a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect MEA's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. This condition is also a significant instance of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to MEA that did not warrant inclusion in this report.

MEA's response to our finding and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise MEA regarding the results of our review of its response.

APPENDIX



Maryland
Energy
Administration

Larry Hogan, Governor
Boyd K. Rutherford, Lt. Governor
Mary Beth Tung, Director

December 3, 2020

Gregory A. Hook, CPA
Legislative Auditor
State of Maryland
Office of Legislative Audits
State Office Building, Room 1202
301 West Preston Street
Baltimore, Maryland 21201


Dear Mr. Hook:

Maryland Energy Administration (MEA) has reviewed the draft legislative audit report for the period covering July 1, 2016 to March 15, 2020. Please find MEA's response to the finding and recommendations identified in the draft legislative audit report.

I would like to take this opportunity to thank the members of the Office of Legislative Audits for their professionalism, patience and support extended to our team during this tumultuous period of COVID-19 telework.

If you have any questions or need further information, please do not hesitate to contact me directly or my Chief of Staff, Chris Rice, at 410-537-4134.

Sincerely,

DocuSigned by:

8320E614D8504CC...
Mary Beth Tung, Ph.D., Esq.
Director

Attachment
MEA Agency Response Form

cc: C. Rice; W. Shiflett

Maryland Energy Administration

Agency Response Form

Discretionary Grants

Finding 1

The Maryland Energy Administration (MEA) did not have written policies and procedures for applying grant criteria when evaluating discretionary grant applications and for determining the amounts to be awarded.

We recommend that MEA

- a. establish written policies and procedures for the application of grant criteria when evaluating discretionary grant applications and for determining the amounts to be awarded, and**
- b. ensure discretionary grants are awarded in compliance with the newly established policies and procedures and that documentation is retained for audit purposes.**

Agency Response

Analysis	
Please provide additional comments as deemed necessary.	<p>MEA clearly outlines grant policy at the individual program level, including evaluation criteria and the range of possible award amounts, within program announcements at the beginning of each grant funding cycle. Upon receipt of grant applications, MEA has a process by which a selection team reviews the applications and makes funding recommendations using the evaluation criteria defined in the notice of opportunity coupled with the review team's technical expertise; these recommendations are documented in a formal memo that routes first to MEA's Program Director, then the Chief of Staff, and finally the Director of MEA. Finally, this formal memo, which contains both award recommendations and a summary of any award not receiving funding, is retained for audit purposes.</p> <p>While MEA currently employs a documented, structured grant review process at the program level as described above, the auditor has identified some possible weaknesses in MEA's existing grant award selection process. In regards to the auditor's finding, MEA has some uncertainty on what would be considered sufficient to cure the finding on a future audit. It is MEA's understanding that the auditor is recommending that MEA should produce an overarching formal written document that specifies the grant review processes used to select awardees and determine grant award amounts. Additionally, MEA understands that the auditor is further recommending that MEA provide additional detail about how individual grant award decisions have been</p>

Maryland Energy Administration

Agency Response Form

	<p>made, particularly in regards to how the evaluation criteria were applied and the award amount determined, in future auditable documents.</p> <p>MEA always looks for ways to improve processes and as such, acknowledges that an opportunity exists to improve by formally documenting overarching agency-wide policies and procedures for applying evaluation criteria and making award determinations, as well as for documenting MEA’s decision-process at the individual award level, particularly for award requests that receive partial funding.</p>		
Recommendation 1a	Agree	Estimated Completion Date:	1/1/2021
Please provide details of corrective action or explain disagreement.	<p>MEA partially agrees with this finding and appreciates the auditor’s comments. MEA always seeks feedback on how to continually improve its policies and procedures. To respond to the auditor’s findings, MEA has already developed a draft agency-wide policy and standard operating procedure (SOP) outlining a high-level, agency-wide policy for evaluating grants; establishing criteria; and where applicable, requiring a program-by-program approach to how partial grant awards are determined. This document will be in addition to any guidance established at the individual program level. The agency-wide policy and SOP are currently under final review and will be applied to all grant funding announcements issued after January 1, 2021.</p> <p>Some MEA programs have specific award thresholds based on set criteria such as \$ per kilowatt of installed capacity that make award determinations. For example, under the Combined Heat and Power (CHP) program, qualifying projects are awarded on a first come, first serve basis and the incentive is based on the capacity installed, plus set multipliers for specific additional benefits (e.g., resiliency) up to a cap. This program conforms with many of the concerns expressed in the findings and these criteria are appropriate for the CHP program; however, this approach does not address the needs of all programs.</p> <p>In a program like the Low to Moderate Income Energy Efficiency Program (LMI) where qualitative factors such as geography, organizational capacity and innovation are considered, MEA notes that while it is possible to have consistent processes and documentation of decisions, it is not possible to ensure the same outcome for each situation, as the judgement of the review team is a factor, and considers such variables as payback periods, engineering feasibility, amount of energy saved in light of the money saved, and an attempt to spread the</p>		

Maryland Energy Administration

Agency Response Form

	<p>limited funds to as many applicants as possible, getting the most “bang for the state bucks”. Consistent guidance on how to allocate scarce funds across grant applications resulting in one “ideal” outcome is not possible, nor advisable for programs that include a number of qualitative and quantitative aspects. Additionally, as the LMI program in particular, is usually administered through non-profit organizations that have garnered trust in the LMI communities, they are often not aware of the scope of the projects until they begin work. However, a formal review process will exist and decisions recorded. An overarching policy would help improve consistency and clarity evaluations and funding recommendations year-over-year for LMI and similar programs where qualitative factors are considered.</p>		
Recommendation 1b	Disagree	Estimated Completion Date:	
Please provide details of corrective action or explain disagreement.	<p>MEA disagrees with recommendation 1b but acknowledges that there is an opportunity for process improvement. While the audit team has identified opportunities for MEA to better capture the rationale for individual award decisions and to formalize a written procedure that outlines the process undertaken by the agency, the agency does have program-level policies and documents the decision process as described further in the <i>Analysis</i> section above.</p> <p>In the spirit of continuous improvement and based on MEA’s understanding of the auditor’s feedback, moving forward MEA will provide additional detail in grant recommendation memos outlining the review team’s rationale for funding recommendations, particularly focusing on those decisions that result in partial funding relative to the applicant’s funding request. However, it is essential to note that MEA’s grant programs differ considerably in terms of audience, technology, program design, and desired outcome.</p> <p>Through this process, it may not always be possible to have a uniform distribution of funding across a given program, where all eligible applicants receive the same relative percentage of the respective grant request. However, MEA will clearly document how the evaluation criteria were used to recommend a particular application for award, and summarize the decision-making process for any partial award, if applicable.</p>		

Maryland Energy Administration

Agency Response Form

Auditor's Comment: Although MEA purports to disagree with our recommendation that it ensure discretionary grants are awarded in compliance with the newly established policies and procedures and that documentation is retained for audit purposes; in fact there seems to be basic agreement with the recommendation in principle. Specifically, MEA seems to agree that its policies and procedures can be made more comprehensive, and that although it may strive in the future to ensure that discretionary grants are awarded in compliance with the revised policy, there may be a lack of uniformity in the grant award. OLA appreciates that there may be cases for divergence from policy in the grant award process, but would expect such cases to be rare and properly documented.

AUDIT TEAM

Edward A. Rubenstein, CPA
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