Memorandum

Date: August 26, 2014

To: Michelle Cooke
Deputy Executive Director Administration and Budget

From: **Public Utilities Commission— San Francisco** Kayode Kajopaiye, Branch Chief
Division of Water and Audits

Subject **Financial, Management, Regulatory, and Compliance Examination Report on Southern California Edison Company's (SCE's)Energy Efficiency (EE) Program For the Period January 1, 2011 through December 31, 2012**

The Utility Audit, Finance and Compliance Branch (UAFCB) discovered some material[1] errors when it sampled and tested SCE's data associated with amounts SCE reported spent in 2012 for its EE programs in the areas that the UAFCB examined. Due to the materiality of the errors found in the samples tested and the lack of some source documentation, UAFCB cannot provide full assurance to the reasonableness of all of the amounts SCE reported to the Commission in its EEGA reports.[2] In addition, UAFCB observed certain recordkeeping deficiencies and other non-compliance issues with the EE program.

To determine the amount of incentive award that should be paid to SCE for program year 2012, the Commission should first remove $10,020,334 from its EE expenses before calculating its incentive award for 2012. The following table provides the summary of adjustments that should be excluded from the EE program costs for the calculation of incentive awards for 2012.

Ob. #	Description	Amount
1	10% of Total 2012 SCE's Labor Costs	$ 3,493,080
3	Prior year expenditures	59,394
5	Prior year expenditures	20,239
6	Withheld Invoice Amount	500,000
8	Prior year expenditures	4,357,681
13	Prior year expenditures	1,589,940
	Total	**$10,020,334**

UAFCB conducted this examination pursuant to Decision (D.) 12-12-032.[3] Based on consultation with the Energy Division (ED) and UAFCB's prior experience, this examination was limited in scope and included SCE's 2011 and 2012 EE. For program year 2012: (1) On-Bill Financing program (OBF); (2) Administrative costs; (3) Multi-Family Energy Efficiency Rebate program (MFEER); and (4) EE Contracts. For program years 2011 and 2012: (1) Fund Shifting, (2) EE

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[1] UAFCB considers its observations material because of:: (a) the size of UAFCB's sample; (b) UAFCB could not test any of the labor costs sampled; (c) the cumulative effect of lack of documentation of some samples and, (d) the frequency and multiple types of errors.

[2] SCE's 2012 reports can be found on the Energy Efficiency Groupware Application website (EEGA) at http://eega.cpuc.ca.gov/.

[3] In D.12-12-032, on page 39, the Commission discussed that it anticipates relying on public versions of UAFCB's examination reports when determining the amount of each utility's incentives. In Conclusion of Law (COL) No. 9, Page 48, the Commission indicated that upon completion, UAFCB shall serve a notice of availability of its report on the service list in R.12-01-005, or its successor.

Balancing Accounts, (3) SCE's Internal Audit Reports on EE programs, and (4) Follow-up on Prior UAFCB's Examination recommendations.

Due to the high error rates in UAFCB's samples (discrepancies totaling $93,676,436, which includes $64,882,075 in actual recording and reporting discrepancies and $28,794,361 in potential recording and reporting discrepancies), UAFCB cannot provide full assurance as to the reasonableness of all the costs that SCE reported to the Commission and in its EEGA reports.

A. Summary of Examination Observations and Recommendations

In the following section, UAFCB summarizes and groups its examination observations by type.[4] UAFCB determined that SCE did not demonstrate compliance with Public Utility (PU) Code Sections 314 (a), 581, and 584, the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts (USOA), General Order (GO) 28, the Commission's directives on administrative costs, fund shifting and balancing accounts, the terms of SCE's contracts, and SCE's own policies and procedures. In Appendix A, UAFCB describes its examination observations in detail.

Contractor's Invoice Amount Withheld: SCE withheld $500,000 from a contractor's invoice amount. See Observations 6.

> **Recommendation:** In determining SCE's 2012 incentive amount, the Commission should remove $500,000 from SCE's total reported EE expenses before calculating the incentive for SCE because it withheld this amount from a contractor's payment due to poor quality of work and safety reasons. Additionally, the Energy Division should discuss the treatment of the energy savings claimed by SCE on prior work performed by the contractor with SCE to determine how this should be handled in order to match the amount withheld or damages suffered by it with the energy savings.

Unauthorized Fund Shift: SCE shifted $4.8 million to the On Bill Financing (OBF) program without filing an advice letter as required by the Commission. See Observations 14.

> **Recommendation:** SCE should strengthen its policies and procedures in place to ensure compliance with Commission directives.

Unreliable Fund Shift/Quarterly Reports: SCE's Fund Shift reports contain errors totaling $53,283,704. See Observations 15, 16, 17, and 18.

> **Recommendation:** SCE should exercise due diligence to ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.
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> The Energy Division should provide the necessary guidance to the reporting utilities on where and how to reflect prior corrections to monthly, quarterly, and annual reports in EEGA.

[4] Commissions directives used to measure compliance included, but were not limited to: D.09-09-047; the ruling in R.01-08-028, dated February 21, 2006; and Energy Division's memo, dated October 22, 2009.

Unable to Vouch Sampled Labor Charges: UAFCB requested supporting documentation for the sampled $707,715 SCE's labor charges. Rather than recording labor costs directly, SCE indicated that it uses a process to estimate its labor costs and then corrects those estimates to actual costs. However, the UAFCB could not test SCE's assertions. It seems that SCE is using its Standard Labor Process to allocate labor costs rather than directly charging them to the program areas. The total labor cost of $34,930,800 could be overstated. See Observation 1.

> **Recommendation:** SCE should improve its labor cost processes for recording labor charges to EE programs or implement other accounting methods that would allow the UAFCB to effectively verify each amount listed as a labor cost. SCE does not have the incentive to understate its labor costs. To mitigate the potential of overstatement of its total labor costs, SCE's total labor cost reported at $34, 930,800 should be discounted by at least 10% because the UAFCB was unable to test this amount to its satisfaction.
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> UAFCB recognizes that the 10% discount is arbitrary. However, the Commission should discount SCE's labor charges because it is a major energy company that the UAFCB could not verify its labor charges to any auditable documentation.

Misclassifications: SCE potentially misclassified about $22.3 million of its reported costs in the areas UAFCB examined. Those misclassifications included, but were not limited to SCE:
a) Recording costs in a different program area than it should have; b) using estimated allocation factors, and c) permitting its fixed price contractors to pre-allocate their total costs between direct implementation, administrative and marketing cost categories instead of directly charging them to those areas when work is performed for each cost category. See Observations 4, 7, and 10.

> **Recommendation:** Since the matter of fixed price contract pre-allocation of charges is currently before the Commission, the matter should be decided by it with input from the UAFCB and SCE. A Commission hearing may be needed to resolve the issue. See Observations 4 and 7.
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> **Recommendation:** SCE should provide additional training to employees and/or non-employees entering cost data into its systems to ensure that they are able to input the correct data into the systems. See Observation 10

Expenses Incorrectly Reported in 2012: SCE incorrectly reported $6,027,254 of its prior year expenditures as 2012 expenditures. See observations 3, 5, 8, and 13.

> **Recommendation:** In determining SCE's 2012 incentive amount, the Commission should remove $59,394 from SCE's EE 2012 expenses before calculating the incentive. SCE should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in future year's expenses. See Observation 3.
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> **Recommendation:** In determining SCE's 2012 incentive amount, the Commission should remove $20,239 from SCE's EE 2012 expenses before calculating the incentive. SCE should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in current year's expenses. See Observation 5.
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> **Recommendation** In determining SCE's 2012 incentive amount, the Commission should remove $4,357,681 from SCE's EE 2012 expenses before calculating the incentive. SCE

should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in future year's expenses. UAFCB believes that the Internal Audit (IA) Department of SCE should include this matter in its next scope of audit to clean up this recurring problem. See Observation 8.

Recommendation: In determining SCE's 2012 incentive amount, the Commission should remove $1,589, 940 instead of $1,861,057 as originally recommended from SCE's EE 2012 expenses when calculating the incentive award. SCE should strengthen its policies and procedures that eliminate or significantly reduce the inclusion of prior year's expenses in subsequent year's expenses. See Observation 13.

Inadequate Supporting Source Documentation: SCE failed to provide adequate supporting source documentation for expenditures totaling $126,385 instead of $5,800,602 originally recommended by the UAFCB in its draft report. SCE provided additional documentation in its comments to the draft report to satisfy the UAFCB's concerns. UAFCB's recommendations have been modified to reflect its satisfaction with the latest information provided by SCE. See Observations 2, 9, and 11.

Recommendation: SCE should strengthen its policies and procedures that would ensure that each amount listed as cost for each specific cost center is based on actual cost and can be readily examined and verified by the Commission. See Observation 2.

Recommendation: SCE should always recognize that the burden of proof is on the company and it's its responsibility to readily provide correct and accurate information needed to address the auditor's concerns. See Observation 9

Recommendation: SCE should make sure that amounts accrued are supported by timely information to satisfy the auditor's concerns. See Observation 11.

Inaccurate OBF Total Outstanding Loan Amount Due to Customer Overbillings: SCE overbilled customers in 2012 and did not correct this overbilling until 2013. Consequently, SCE provided inaccurate data for its total 2012 outstanding OBF loan amount. See Observations 12.

Recommendation: SCE should provide supporting documentation to UAFCB to verify that the customer accounts with overbilling did in fact receive the appropriate credit. In addition, SCE should strengthen its policies and procedures to eliminate these types of errors.

UAFCB believes that the Internal Audit (IA) Department of SCE should include this matter in its next audit scope to clean up this recurring problem.

EE Balancing Accounts Errors: SCE's EE Balancing Accounts contain inaccurate data. See Observations 19 and 20.

Recommendation: SCE should follow Commission's directives. In addition, SCE should strengthen its policies and procedures to eliminate or substantially reduce the level of errors included in its reports to the Commission. See Observation 19.

Recommendation: SCE should comply with Commission's directives by correctly applying its authorized and approved regulatory accounts. See Observation 20.

Lax or Internal Controls Not Vigorously Enforced: In view of the multiple kinds of errors UAFCB found during its examination, SCE clearly needs to improve its reporting and record keeping processes. SCE's internal controls are either too lax or SCE is not vigorously monitoring and enforcing them whether they are effectively working as expected. See observation 23.

> **Recommendation** Within 90 days from the date of this report, SCE should strengthen its internal controls for recording and reporting its EE programs to prevent future misreporting and misclassifications of SCE's EE costs, and provide UAFCB a copy of the revised internal controls. In addition, SCE should describe how it will monitor and vigorously enforce these to improve the recording and reporting process to the Commission. While a small percentage of errors can be tolerated, SCE should improve its EE internal controls, minimizing the recording and reporting errors and eliminate the occurrence of widespread errors throughout the recording and reporting process of SCE's EE activities.

B. Examination Process

Based on consultation with the Energy Division (ED), UAFCB's prior experience examining SCE's EE programs, and the results of UAFCB's risk assessment, UAFCB limited its examination to the areas described above and evaluated compliance with accounting, recording, reporting of program expenses during 2012 and the associated procedures to safeguard those activities. Pertinent information about SCE's EE programs is found in Appendix B.

On July 7, 2014, SCE provided UAFCB its comments on its draft report provided to it on June 9, 2014. SCE provided additional information that it believes would be pertinent in supporting its comments. UAFCB made changes in its report where appropriate to reflect its satisfaction with the additional information provided by SCE.

UAFCB conducted its examination in accordance with attestations standards established by the American Institute of Certified Public Accountants (AICPA), and, accordingly, included examining on a test basis, evidence concerning SCE's compliance with the requirements of the energy efficiency programs, Commission directives pertaining to the programs, SCE's internal policies and procedures, and the generally accepted accounting principles and practices.

C. Conclusion

SCE should improve the accuracy of recording and reporting of EE program activities and the related costs within the record period, including the EE internal controls. UAFCB is concerned about the inability to vouch the labor costs and the pre-allocation of major cost categories.

A detailed summary of UAFCB's analysis and observations is attached in Appendix A.

If you have any questions on UAFCB's examination, please contact Kayode Kajopaiye.

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Appendix A
Analysis and Findings

A.1 Introduction

The Utility Audit, Finance and Compliance Branch (UAFCB) discovered several material errors when it sampled and tested Southern California Edison Company's (SCE) data associated with the amounts it reported spent in 2012 for its energy efficiency program in the areas examined by the UAFCB.[1] Due to the proportionality of the errors to the sample and some lack of documentation, as described in the following observations, UAFCB deems SCE's 2012 reports less than accurate and reliable.[2] In addition, UAFCB observed certain recordkeeping deficiencies and some other lack of compliance. UAFCB was also unable to vouch for the labor charges requested in its sample. Consequently, UAFCB questions the correctness of the labor charged to the EE programs.

UAFCB's examination was limited in scope and included SCE's 2011 and 2012 EE specific areas of EE Programs of concern to the Energy Division and UAFCB. They are as follows:

1. SCE Statewide (Investor Owned Utility, IOU), Third Party (TP), and Local Government Partnership (LGP) Administrative Costs - 2012;
2. EE Contracts - 2012;
3. On-Bill Financing (OBF) – 2012;
4. Multi-Family Energy Efficiency Rebates (MFEER) – 2012;
5. Fund Shifting – 2011 and 2012;
6. EE Portfolio Balancing Accounts – 2011 and 2012;
7. SCE Internal Audit Reports – 2011 and 2012; and
8. Follow-up on Prior UAFCB's Examinations – 2010 and 2011.

This report addresses regulatory and compliance issues for program years 2011 and 2012, including financial compliance regulatory matters pertaining to program year 2012. This report excludes any financial compliance matters that pertain to SCE's EE for program year 2011 since the UAFCB previously addressed such matters in an examination report issued on September 30, 2013.[3]

On June 9, 2014, the UAFCB provided SCE a copy of its draft report and requested that SCE provide its comments. On July 7, 2014 after an extension of time, SCE provided the UAFCB its comments. UAFCB provides a summary of SCE's comments in the following sections and SCE's comments in their entirety as a separate attachment. Along with its comments, SCE

[1] UAFCB considers its observations material because of: (a) the size of UAFCB's sample; (b) UAFCB could not test any of the labor costs sampled; (c) the cumulative effect of lack of documentation of some samples, and (d) the frequency and multiple types of errors.
[2] SCE's 2012 reports can be found on the Energy Efficiency Groupware Application website (EEGA) at http://eega.cpuc.ca.gov/.
[3] Refer to Energy Efficiency Program (EE) Financial Compliance Examination Report of Southern California Edison Company (SCE) For the Period January 1 through December 31, 2011 that is available at the following link: http://www.cpuc.ca.gov/PUC/Water/Available+Documents/Downloadable+Reports/Financial+Compliance+Audit+Reports+for+EE+Programs.htm

provided the UAFCB with additional information that SCE believes would be pertinent in supporting its comments. UAFCB reviewed SCE's comments along with all the additional material submitted by SCE. Based on UAFCB's analysis of SCE's data and information that it supplied with its comments, UAFCB made changes in its report where appropriate to reflect its satisfaction with the additional information provided by SCE.

A.2 Administrative Costs

a) IOU Administrative Costs

Observation 1: SCE did not demonstrate compliance with Public Utility (PU) code §§ 314(a), 581 and 584, General Order (GO 28) and the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts (USOA). SCE did not produce adequate source documentation to support the sampled labor costs.

Criteria: Section 314(a) indicates "The commission, each commissioner, and each officer and person employed by the commission may, at any time, inspect the accounts, books, papers, and documents of any public utility." Sections 581 and 584 require that the utility provide complete and accurate data to the Commission. GO 28 specifically states: "The manner in which these records, memoranda and papers shall be preserved must be such that this Commission may readily examine the same at its convenience." The USOA provides: "Each utility shall keep its books of account, and all other books, records, and memoranda which support the entries in such books of account so as to be able to furnish readily full information as to any item included in any account. Each entry shall be supported by such detailed information as will permit ready identification, analysis, and verification of all facts relevant thereto."

Condition: SCE did not produce adequate source documentation to support the $707,715 or 100% of the sampled labor costs. Instead of providing documentation to support the sample labor charges of 15 employees selected, SCE provided several presentations to demonstrate its process on how its standard labor cost per hour worked plus residual (adjustments distributed in the home cost center to the various cost objects that the employees charged during the period) is equivalent to actual labor per hour worked. SCE failed to provide supporting documentation associated with a specific employee's residual value. Therefore, the UAFCB was unable to determine and verify whether SCE's use of labor cost estimates was equal to actual labor costs.

Cause: SCE does not directly use actual labor costs for recording and reporting its employees' labor costs. SCE asserts that it uses a process whereby it develops standard labor rates which it later adjusts with effective labor rates. SCE claims that the effective labor rate will approximate actual labor rate when the timing differences even out. SCE alleges that resolving the timing differences can take several months.

Effect: Being unable to substantiate any of SCE's labor costs, UAFCB questions the accuracy and reliability of all of SCE's labor costs because of the opportunity to overstate them.

SCE's Representation in the Field: SCE claims it uses a couple of methods to estimate its labor costs. One method is the determination of the labor cost using labor survey where retroactive journal entries are used to transfer labor charges from the current labor allocation to the new labor allocation. Another method is the system determination of labor cost using the aggregate of all the actual labor rates of similar job categories within the same organizational unit and taking the average rate. According to SCE, after all the adjustments are made, the estimated labor cost approximates the actual labor rate. SCE's proposal for labor testing using several presentations was due to the fact that SCE could not provide the supporting documentation to verify that its standard labor cost was equal to actual labor cost for any of the 15 employees that the UAFCB selected for testing. SCE suggested that to effectively verify actual labor rate, UAFCB could select a specific group (i.e. Program Operation, DSM Strategy, Residential, etc.) for a test month.

Response to Field Representation: Section 314(a), GO 28 and the USOA all require that each entry in a utility's books be able to be readily verified. This means that charges should be able to be verified on a stand-alone basis, without having to select an entire group and month to examine and verify a specific charge. SCE's current method used to record its employees' labor costs is unverifiable and does not demonstrate compliance with GO 28 and the USOA. SCE is a major electric utility using some accounting method(s) for its labor charges that could not be verified or tested by the UAFCB. Labor cost testing was an issue in UAFCB's 2011 examination of SCE's EE expenditures.

SCE Comments: SCE asserts that its accounting for labor does not overstate labor costs. SCE indicates that it can demonstrate that the variance between actual Payroll and Labor recorded in the Cost Objects is always zero.

SCE claims its labor charges are reliable and are not estimates. While SCE's accounting system does use estimated labor charges as an interim step, every month it adjusts these estimated costs to actual labor costs. SCE's standard labor cost methodology trues up the labor charged to the Cost Objects to actual Payroll each month through the recalc/reval process. Because the recalc/reval process adjusts standard to actual pay at the *group level* [emphasis added], there is *no employee-specific residual value* [emphasis added] in SCE's labor accounting system.

SCE alleges its labor accounting is auditable. During UAFCB's site visit, SCE demonstrated (1) how SCE's accounting system works generally, (2) how SCE's accounting system calculates labor for an employee within the auditor's sample group, and (3) how the recalc/reval process is calculated in SAP. On December 19, 2013, SCE inquired whether the auditor needed any additional information in order to verify the recorded labor costs. In response, the auditor requested copies of the presentations from the site visit to be used as work papers, but did not request any additional information. SCE received no follow-up data requests from the auditor, and the auditor did not request to test any other aspects of SCE's labor accounting system.

Although SCE did not receive any follow-up data requests, SCE took the initiative to compile additional work papers relating to the 129 samples for the 15 employees, which are provided with its comments. SCE claims that the documentation demonstrates: (a)

SCE is accurately charging labor on an actual (not estimate) basis, and (b) SCE's labor charging process is auditable. In sum, SCE asserts it accurately records labor costs, and correctly accounts for labor costs to the balancing account (i.e., PEEBA).

SCE would appreciate the opportunity to continue to work with the UAFCB to demonstrate through testing that SCE's labor accounting system is recording labor costs accurately.

Rebuttal: Prior to the site visit, UAFCB submitted Data Request 11 to SCE on December 2, 2013, which included among other things; the labor cost sample with specific amounts associated with the 15 employees in question and requested that SCE provide all supporting documents for each amount selected for testing. In its December 12, 2013 email, instead of providing the requested documentation, SCE proposed to take two days to demonstrate how its accounting system calculates labor using 2 of the 15 employees selected for testing. During the site visit, SCE demonstrated how SCE's accounting system generally works, but could not use any of the amounts in UAFCB's sample for the 15 employees selected to demonstrate how the standard labor cost is equal to actual labor cost because it could not identify the portion of the residual value associated with any specific employee. Standard labor costing methodology is not the problem; it's how SCE designed it with its payroll system.

UAFCB is not against standard labor costing methodology as a starting point as alleged by SCE. Pacific Gas and Electric Company (PG&E) uses it and it employs more employees than SCE. UAFCB is satisfied with PG&E's labor costing methodology.

On December 19, 2013 when SCE inquired whether the auditor needed any additional information in order to verify the recorded labor costs, the auditor told SCE that the missing data was the residual value associated with each amount selected. SCE indicated that it could not provide such information. Consequently, the auditor did not find any need to insist that SCE provide the information that it had already stated it was not able to provide. In addition, the auditor did not need to test SCE's labor accounting system after SCE's selected expert in the subject matter confirmed that SCE's system will not identify the residual value for any of the amounts that the auditor selected.

SCE could not provide copies of the presentations to the auditor during the field visit. Instead, SCE promised to send it to the auditor by email later for record keeping purposes.

That the labor amounts for all the cost centers add up to the same amount charged to payroll each month does not prove that the amounts SCE charged to EE reflect the actual labor charges of the SCE EE staff.

SCE itself admits in its comments on UAFCB's draft report that its process did and does not charge actual labor costs to EE:

1. Standard Labor Costing is more complex than basic labor methodologies.

2. It allows SCE to charge programs for the value of labor as opposed to the salary of any particular employee.
3. Because the recalc/reval process adjusts standard to actual pay at the *group level*...[emphasis added]

UAFCB reviewed the additional information SCE provided with its comments to UAFCB's draft report. Although SCE claims that the work papers relate to the 129 samples for the 15 employee selected by UAFCB for testing, the additional workpapers are not supporting documentation for the amount the auditor selected for testing. An audit is an examination of records or accounts to check their accuracy. Since the UAFCB was able to verify its sample, it could not attest to SCE's EE labor charges like other utilities it examined. UAFCB was able to drill down from the generally ledger to the sub-ledger and timesheets of employees including managers of other utilities. All of them are using the same accounting system SCE adopted in 2008.

Recommendation: SCE should improve its labor cost processes for recording labor charges to EE programs or implement other accounting methods that would allow the UAFCB to effectively verify each amount listed as a labor cost. SCE does not have the incentive to understate its labor costs. To mitigate the potential of overstatement of its total labor costs, SCE's total labor cost reported at $34, 930,800 should be discounted by at least 10% because the UAFCB was unable to test this amount to its satisfaction.

UAFCB recognizes that the 10% discount is arbitrary. However, the Commission should discount SCE's labor charges because it is a major energy company that the UAFCB could not verify its labor charges to any auditable documentation.

b) Local Government Partnership (LGP) Administrative Costs

Observation 2: SCE did not demonstrate compliance with PU code §§ 314(a), 581 and 584, GO 28 and the USOA. Of the Distributive Cost Center (DCC) charges of $360,242 sampled by UAFCB, $126,385 was allocated using DCC allocation factors. SCE reported the $126,385 or 35% of the total sample as actual LGP administrative expenses. However, the $126,385 reported DCC charges also included estimated labor charges.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission. The USOA and GO 28 require that the utilities preserve all records, memoranda, and papers supporting each and every entry so that this Commission may readily examine the same at its convenience.

Condition: SCE develops pre-determined allocation factors at the beginning of the budget cycle for allocating its energy efficiency administrative and general (A&G) over the entire period. SCE refers to this factor as DCC, a temporary cost object which allows certain expenses to be allocated on a monthly basis and distributed to other cost objects. The DCC charges are a mixture of actual costs and estimated labor charges.

Cause: SCE's process for recording labor costs does not allow the Commission to verify that the labor costs are accurate.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate.
SCE Comments: See UAFCB's summary of SCE's response in Observation 1.

Rebuttal: See UAFCB's reply in Observation 1 to SCE's response.

Recommendation: SCE should strengthen its policies and procedures that would ensure that each amount listed as cost for each specific cost center is based on actual cost and can be readily examined and verified by the Commission.

Observation 3: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE reported 2010 and 2011 LGP Administrative expenses totaling $59,394 as 2012 expenses. The $59,394 represented 16.25% of the $360,242 that the UAFCB sampled.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: The Commission requires the utilities to conduct their accounting on an accrual basis. Under the accrual method of accounting, transactions are counted when the order is made, the item is delivered, or services rendered, regardless of when the money for them is actually received or paid. Of the $360,242 that the UAFCB reviewed, invoices totaling $59,394 were for the prior year's expenses.[4]

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that may be misleading and less than accurate. Based on UAFCB's sample of $360,242, SCE over-reported its LGP administrative costs by at least $59,394.

SCE Comments: SCE disagrees with UAFCB's recommendations to remove valid EE expenditures before calculating SCE's shareholder earnings incentives. SCE asserts that UAFCB does not dispute that the EE expenditures associated with the draft observations 3, 5, 8 and 13 are valid. SCE asserts that it keeps its accounts on the accrual basis by requiring inclusion in its accounts of all known transactions of appreciable amounts. SCE uses a $5,000 accrual threshold for capturing what SCE believes are appreciable amounts. While SCE believes that it is in compliance with Commission requirements related to accruing expenses, SCE agrees to assess and, if appropriate, enhance its policies and procedures for receipting and tracking year end EE expenses. SCE will describe any changes to its policies and procedures for receipting and tracking EE expenses in the Internal Controls Report due to the UAFCB 90 days after the issuance of the Final Report.

SCE claims that $47,792 of the $59,394 included as an exception in the Draft Report was properly accrued 2011 expenses and SCE accounted for these as expenses in 2011. In

[4] $59,394 = $861.5 from 2010 plus $58,333 from 2011

addition, $862 of the $59,394 alleged exceptions were correcting journal entries made in 2012, which corrected the program being charged for the expenditures. SCE asserts that since a correcting journal entry is not a new expense, the $862 remained accurately recorded as 2011 expenses. Therefore, the unknown 2011 year end expenses that SCE reported in 2012 are $10,740 and not $59,394 as calculated in the Draft Report.

Rebuttal: SCE does not disagree that the $59,394 in question was part of its reported 2012 expenses that UAFCB selected for testing. If $47,792 of the $59,394 in question was properly accrued 2011 expenses, SCE had five months from January to May 2012, when it filed its Annual Report on 2011, to report any properly accrued 2011 expenses and another five months from January to May 2013 when it filed its Annual Report for 2012 to make the appropriate adjustments by removing the expenses associated with the year 2011 from its 2012 reported expenses. In addition, $862 of the $59,394 that SCE claims to be correcting journal entries made in 2012 were 2010 expenses that cannot be added to 2012 expenses for incentive payment purposes even though it does not represent a new expense.

UAFCB did not audit 100% of SCE prior year expenses and cannot tell with certainty if SCE recovered these costs in prior years. UAFCB can only rely on the data that SCE provided for 2012 expenses. The $59,394 in question was sampled from SCE's 2012 expenses and was determined to be prior year expenses during the audit. Therefore, for incentive calculation purposes, the $59,394 must be removed from SCE's 2012 expenses.

In addition, SCE's accrual threshold may not capture all costs in the appropriate year. FERC requires the accrual of all known and appreciable amounts. Appreciable is defined as capable of being perceived or measured. SCE's accrual threshold of $5,000 may be too high for being perceived and measured. With SCE's threshold that high, some expenses may not be captured and can be reported in the wrong year. For example, using the threshold, some employees' travel expenses near the end of a year may not reach the $5000 accrual threshold.

Recommendation: In determining SCE's 2012 incentive amount, the Commission should remove $59,394 from SCE's EE 2012 expenses before calculating the incentive. SCE should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in future year's expenses.

c) Third Party (3P) Administrative Costs

Observation 4: SCE did not demonstrate compliance with PU code §§ 581 and 584, GO 28 and the USOA. Of the $1,260,276 3P administrative costs that the UAFCB sampled, 53.6% or $675,528 were either inaccurate or were not adequately substantiated by supporting documents.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission. The USOA and GO 28 require that the utilities preserve all records, memoranda, and papers supporting each and every entry so that this Commission may readily examine the same at its convenience.

Condition: SCE continued to allow invoiced amounts from 3P contractors with fixed price or performance contract to be distributed between direct implementation, administration, and marketing by predetermined allocation factors as it did in 2011. When a 3P contractor bills for its supposedly actual costs, it would use the pre-determined allocation factors to distribute the total cost to the three areas mentioned above. Therefore, the $675,528 allocated to administrative costs in UAFCB's sample could be misclassified, overstated or understated or may not be applicable.

SCE does not audit or verify its contractor's allocation of costs to these cost categories. SCE's policy to allow contractors to use pre-determine allocation factors for the cost categories or split costs in this manner is arbitrary and may not reflect the actual costs for each cost category that the contractor actually incurred.

On May 19, 2014, SCE filed a "MOTION FOR CLARIFICATION PURSUANT TO ORDERING PARAGRAPH #49 OF D.12-11-015" on this matter and others.

Cause: SCE permits its contractors to allocate invoiced amounts to the three cost categories instead of requiring the contractors to bill or track the three cost categories separately by actual costs incurred. SCE does not have a policy that requires it to periodically audit or verify the cost allocations of contractors to ensure if the factors they used or using represent actual experience or charges.

Effect: SCE recorded and reported data to the Commission that are likely misclassified and less than accurate. Allowing vendors to allocate or estimate actual charges for each cost category may result in misclassified/understated/overstated cost category amounts. This defeats the purpose of the soft cap or target established by the Commission for TP administrative costs and allows SCE to game the outcome.

SCE Comments: SCE agreed with UAFCB that the Energy Division should meet with SCE to discuss its contracting practices and determine how the 3P program implementers' invoices for fixed-price (a.k.a. performance) contracts should be presented by SCE for reporting purposes. Following the issuance of the Final EE Audit Report on 2011, SCE further states that it initiated a series of discussions with the Energy Division regarding the issue, and in May 2014, SCE filed a motion requesting Commission clarification regarding the appropriate use of fixed-price contracts.

SCE indicates that it continues to report costs for fixed-price contracts in the same manner as it has, until further clarification is received from the Commission. Notwithstanding this recognized need for clarification, SCE points out that the Commission has consistently directed the utilities to increase the use of fixed-price contracts, recognizing the resulting benefits to ratepayers. SCE asserts that it made its best efforts to comply with Commission direction to implement such contracts while still following Commission-mandated cost allocation reporting requirements. SCE reports cost allocations individually and uniquely for each fixed-price contact. SCE states that the fixed-price contract structure is fundamentally incompatible with the UAFCB's desire to individually verify the components of fixed-priced contract costs.

Rebuttal: SCE's representation that fixed-price contracts are performance contracts can be misleading since SCE's supporting documentation reveals that fixed-price contracts are not always performance based.[5] Even if the Commission consistently directed the utilities to increase the use of fixed-price contracts, ratepayers cannot benefit from it when SCE uses fixed-price contracts to misclassify costs between the administrative, marketing and direct implementation cost categories. For example, as shown in the rebuttal to SCE's comments on UAFCB's draft report in Observation 7, SCE does not deny that it used the fixed-price contract approach to overstate its direct implementation cost by 91% on one of the invoices sampled for testing. Although the vendor invoice noted that there was no direct implementation activities associated with its invoice totaling $1,492,676, SCE automatically allocated $1,358,335 or 91% of the invoice amount to direct implementation because per the vendor's fixed-price contract, 91% was to be automatically allocated to direct implementation and the remaining 9% allocated between marketing and administrative costs. Not only does the fixed-price contract structure leave opportunity for cost allocation manipulation, it defeats the purpose of the cost targets established by the Commission for controlling charges or expenses.

Recommendation: Since the matter of fixed price contract pre-allocation of charges is currently before the Commission, this matter should be decided by it with input from the UAFCB and SCE. A Commission hearing may be needed to resolve the issue. (Observations 4 and 7)

Observation 5: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE reported 2008, 2009, 2010 and 2011 3P administrative expenses totaling $20,239 as 2012 expenses. The $20,239 represented about 2% of the $1,260,276 that the UAFCB sampled.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: The Commission requires the utilities to conduct their accounting on an accrual basis. Under the accrual method of accounting, transactions are counted when the order is made, the item is delivered, or services rendered, regardless of when the money is actually received or paid. Invoices totaling $20,239 were for expenses which occurred prior to 2012.[6] The error rate is small but the principle behind it is significant.

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate. SCE over-reported its 3P administrative costs by at least $20,239.

SCE Comments: See UAFCB's summary of SCE's response in Observation 3.

Rebuttal: See UAFCB's reply in Observation 3 to SCE's response.

[5] SCE's response dated May 1, 2014 to DWA's Email 034.

[6] $20,239 = $1,384 (2008) + $1,333 (2009) + $3,375 (2010) + $14,146 (2011).

Recommendation: In determining SCE's 2012 incentive amount, the Commission should remove $20,239 from SCE's EE 2012 expenses before calculating the incentive. SCE should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in current year's expenses.

A.3 Energy Efficiency Contracts

In total, out of $47 million of direct implementation EE contract costs UAFCB selected for review, 76% or $34 million of the reported and recorded costs were misleading, inaccurate or not adequately substantiated by supporting documents as discussed below.

Observation 6: SCE did not demonstrate compliance with §§ 581 and 584, GO 28 and the USOA. SCE reported that it paid an invoice amount totaling $1,492,676 instead of $992.676 it actually paid because it withheld $500,000 from the invoice due to the quality of work done by the contractor and for safety reasons. As a result, the EE program expenditures for 2012 were over-reported by $500,000.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: For the Purchase Order #[redacted], UAFCB selected $6,641,577 in direct implementation costs to review. Of the $6,641,577, one of the samples was in the amount of $1,492,676. The supporting documentation that SCE provided for this amount revealed that: (1) the original invoice was in the amount of $1,492,676; (2) At SCE's discretion, this invoice was reduced to $992,676 before payment; (3) The amount that SCE paid to the vendor was $992,676; (4) SCE reported to the Commission that it paid the full invoice amount of $1,492,676; (5) In an email communication between the program manager and other SCE's employees provided as part of the supporting documentation, the program manager writes, "The full invoice needs to be processed so we can claim the full savings. The only difference is that SCE, on the backend, is not paying the full amount of the invoice." This communication shows that SCE purposely reduced the payment amount to the vendor by $500,000 and at the same time recognized the full energy savings associated with the invoice.

Cause: By withhold $500,000 from the invoice of a contractor to protect SCE from damages caused by the contractor for prior work done in 2011 and 2012.

Effect: SCE overstated a payment to its vendor by $500,000 or 34% of the invoice amount of $1,492,676 by reporting the full payment to the Commission instead of the net actual amount paid by SCE.

SCE Comments: SCE asserts that the documentation UAFCB refers to doesn't establish a Rule 1.1 violation. SCE concedes that the documentation supporting SCE's $500,000 withhold from the vendor's final payment could have been clearer. The $500,000 withhold was done to mitigate SCE's risk of remediation costs from the vendor. SCE asserts that it appropriately approved the vendor's invoice for $1.492 million after inspecting the installations, and counted the energy savings associated with the installed measures. In addition, it claims that it prudently withheld $500,000 from its final payment to the vendor under the purchase order to account for damages SCE expected to incur because of quality and safety related issues with the vendor's prior work in 2011 and 2012.

Rebuttal: UAFCB was not incorrect when it stated in Draft observation 6 that "SCE reported to the Commission that it paid the full invoice amount of $1,492,676" rather than the $992,676 SCE actually paid the vendor. SCE acknowledged in its response to UAFCB's draft report that it claimed the total energy savings on the full invoice of $1,492,676 and that the supporting documentation it provided during the field examination revealed in an email the communication between the program manager and other employees. The program manager wrote: "The full invoice needs to be processed so we can claim the full savings. The only difference is that SCE, on the backend, is not paying the full amount of the invoice."

SCE is withholding $500,000 to compensate itself from damages caused by its contractor for poor quality of work and safety concerns. It already recognized the full payments to the contractor for the prior work and SCE received incentives for those expenses. The best way to make any corrections to prior payments to the contractor and incentives received by SCE based on its expenditures is to reduce future expenses and incentives to indicate that all is not well with one contractor that did some prior work for SCE.

Recommendation: In determining SCE's 2012 incentive amount, the Commission should remove $500,000 from SCE's total reported EE expenses before calculating the incentive for SCE because it withheld this amount from a contractor's payment due to poor quality of work and safety reasons. Additionally, the Energy Division should discuss the treatment of the energy savings claimed by SCE on prior work performed by the contractor with SCE to determine how this should be handled in order to match the amount withheld or damages suffered by it with the energy savings.

Observation 7: SCE did not demonstrate compliance with PU code §§ 581 and 584, GO 28 and the USOA. Out of the $47 million of direct implementation contract costs that the UAFCB selected, 46% or $21.5 million were either inaccurate or not adequately substantiated by supporting documents and were likely misclassified.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission. The USOA and GO 28 require that the utilities preserve all records, memoranda, and papers supporting each and every entry so that this Commission may readily examine the same at its convenience.

Condition: UAFCB selected $47 million in direct implementation EE contract costs for review. SCE allowed invoiced amounts to be distributed between direct implementation, administration, and marketing cost categories by predetermined allocation factors. When the contractor submitted its invoice to SCE, the charges contained in the invoice were segregated to the three cost categories based on pre-determined allocation factors. Consequently, $21.5 million direct implementation contract costs were based on pre-determined allocated rates instead of actual expenses pertaining to each cost category.

The EE cost categories were likely misclassified individually and misrepresented to the Commission for reporting purposes.

SCE does not audit or verify the contractors' allocation factors for the cost categories. SCE's policy allows contractors to use pre-determine allocation factors to be applied to the total amount of the invoice in order to determine the amount to charge to each cost category. This approach is arbitrary and may not reflect the actual charges for each cost category that the contractor actually incurred or for the work performed.

For example, UAFCB noted that the allocation factors used by a vendor for the invoice that the UAFCB reviewed were 91%, 5% and 4% for direct implementation, administration and marketing costs, respectively. On one of the vendor's invoices totaling $1,492,676, SCE reported $1,358,335 or 91% of this amount as direct implementation however, the vendor noted that there was no direct implementation activities associated with this specific invoice. Using the pre-determined allocation factors, the vendor automatically allocated $1,358,335 or 91% of the invoice to direct implementation but according to the vendor's own narrative on the invoice, no direct implementation activities associated with the invoice. SCE on the other hand recorded and reported the $1,358,335 as direct implementation costs to the Commission.

Cause: SCE's policy to allow contractors to use predetermined allocation factors, among other things, contributed to the misclassification.

Effect: SCE recorded and reported data to the Commission that are likely misclassified and less than accurate. Allowing vendors to allocate or estimate actual charges for each cost category defeats the purpose of cost target for 3P established by the Commission for controlling charges or expenses and leave room and opportunity for gaming.

SCE Comments: See UAFCB's summary of SCE's response in Observation 4.

Rebuttal: See UAFCB's reply in Observation 4 to SCE's response.

Recommendation: Since the matter of fixed price contract pre-allocation of charges is currently before the Commission, this matter should be decided by it with input from the UAFCB and SCE. A Commission hearing may be needed to resolve the issue.

Observation 8: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE over reported its 2012 direct implementation expenses by at least $4,357,681 because the amount reported as EE 2012 expenses included expenses pertaining to the 2011 program year.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: The Commission requires the utilities to conduct their accounting on an accrual basis. Under the accrual method of accounting, transactions are counted when the order is made, the item is delivered, or services rendered, regardless of when the money is actually received or paid. SCE requires its vendors to submit monthly invoices.

However, SCE counted some of its 2011 EE expenses as 2012 EE expenses. UAFCB summarizes its observation in the following table.

Table A-1
2011 Expenses Included in 2012

Purchase Order	Description	Total Sample	Exception	% of Sample
[redacted]	2011 Expenses	$ 132,731.22	$ 69,416.51	52%
	2011 Expenses	3,989,075.69	805,316.11	20%
	2011 Expenses	6,363,235.85	1,018,286.31	16%
	2011 Expenses	987,254.61	246,174.15	25%
	2011 Expenses	10,865,022.48	1,193,825.39	11%
	2011 Expenses	6,641,577.41	766,977.60	12%
	2011 Expenses	243,723.19	144,479.38	59%
	2011 Expenses	2,334,730.71	113,205.25	5%
Total		**$31,557,351.16**	**$4,357,680.70**	**14%**

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate. Allowing its employees to include 2011 expenses in its 2012 report results in misleading information in its 2012 report filed with the Commission.

SCE's Representation in the Field: SCE asserts that it keeps its accounts on the accrual basis, which it believes requires the inclusion in its accounts of all known transactions of appreciable amounts. SCE alleges that some of its 2011 invoices were unknown to SCE in 2011. In addition, some of SCE's 2011 invoices represent "catch up" invoices.

Response to Field Representation: A simple solution would be for SCE to set up policies and procedures that require its employees to keep track of expenses as they occur in order to make the appropriate adjustment on a timely basis to assure that all expenses associated with a specific year is properly accounted for before filing its report with the Commission. SCE filed its 2011 Energy Efficiency report in May 2013. Therefore, SCE had enough time to track its 2011 expenses and make all necessary adjustments before filing its report.

SCE Comments: SCE alleges that $2,203,749 of the $4,357,680 in exceptions was properly accrued 2011 expenses and SCE accounted for these as expenses in 2011. Therefore, the unknown 2011 year end expenses that SCE reported in 2012 are $2,153,931 and not $4,357,680 as calculated in the Draft Report. Further, data in UAFCB's Table A-1 has two errors. First, the table does not accurately reflect the total invoices sampled for all direct implementation contracts and therefore overstates the percent of the sample that the auditor identifies as an exception. Second, the table includes the $2,203,749 of 2011 expenses that were properly accrued and accounted for in 2011. Also, see UAFCB's summary of SCE's response in Observation 3.

Rebuttal: SCE does not disagree that the $4,357,680 in question was part of its reported 2012 expenses that the UAFCB selected for testing. UAFCB sampled the $4,357,680 in question from SCE's 2012 expenses and determined the full amount to be prior year expenses. Therefore, for the incentive calculation purposes, the $4,357,680 must be removed from SCE's 2012 expenses. UAFCB's Table A-1 accurately reflects the total invoices sampled for the purchase order in question and does not overstate the percent of the sample that the auditor identifies as an exception. Also, see UAFCB's rebuttal to SCE's response in Observation 3. They are not worth repeating here.

Recommendation: In determining SCE's 2012 incentive amount, the Commission should remove $4,357,681 from SCE's EE 2012 expenses before calculating the incentive. SCE should strengthen its policies and procedures that would eliminate or significantly reduce the inclusion of prior year's expenses in future year's expenses.

UAFCB believes that the Internal Audit (IA) Department of SCE should include this matter in its next audit scope and clean up this recurring problem.

Observation 9: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE paid more than $2,434,561 to one of its vendors without substantiation of the service provided.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: A contractor performs certain functions for SCE, including paying incentives to SCE's distributors. SCE reimburses the contractor for incentive payments to distributors without requesting or verifying any invoice that the distributors submit to the contractor. In 2012, SCE paid a contractor $313,682 as a processing fee. The "Processing Fee" is a fixed rate negotiated to cover the vendor's cost to process the incentive payment to SCE's distributors. In addition, SCE paid the contractor $2,434,561 as "pay for performance." The agreement between SCE and the contractor defines "pay for performance payments as "payments subject to the satisfactory completion by consultant of the installation of projects/measures." SCE explained to UAFCB that "the pay for performance payment is the actual cost of installing the equipment." However, after UAFCB's analysis determined that the contractor never installed any equipment and that there was no justification for SCE to pay the contractor the amount for installation of equipment as performance fees, SCE revised its explanation from "pay for performance is the actual cost of installing the equipment" to "pay for performance is the fixed cost per ton to deliver the program." When requested to explain the terminology it used in its revised explanation, SCE did not elaborate on what "delivery of the program meant." UAFCB's analysis reveals that SCE's payments to the contractor for processing fees to process the incentive payments are reasonable payments to the contractor as a middle man stepping in SCE's shoes to pay incentive payments to the distributors.

Cause: SCE's failure to properly explain the program and provide the appropriate information and documentation about the contract at the right time. SCE did not provide additional information to the UAFCB until it saw its draft report.

Effect: SCE recorded and reported data for services that could not be substantiated and verified by the UAFCB during the engagement or prior to the issuance of its draft report.

SCE Representation in the Field: SCE claims that the contractor is stepping into its shoes to make incentive payments to the distributors. SCE further said that it negotiated a contract with the contractor that provided reimbursement of incentive payments to the distributors and a fixed cost per ton to deliver the program.

Response to Field Representation: Since the contractor is stepping into SCE's shoes to make incentive payments to the distributors, a reasonable fee for the services is appropriate. However, SCE's pay for performance to the contractor, unless substantiated by SCE with specific installation services fully documented to the satisfaction of UAFCB, should be refunded to the EE program by SCE's shareholders or recovered from the contractor by SCE in order to refund the program.

SCE Comments: SCE disagrees with the UAFCB recommendation that the Commission remove $2,434,561 from SCE's EE 2012 expenses before calculating SCE's program year 2012 EE incentive claim. SCE indicates that it can substantiate the services provided by "the contractor" and provided additional documentation to the UAFCB for its review. In addition, SCE asserts that the UAFCB's Draft Report contains several errors in the condition, effect, and rebuttal statements. According to SCE, these inaccuracies lead to an incorrect conclusion for this program and its implementer. SCE claims it does not reimburse "the contractor" for incentive payments to distributors without verifying the invoice submitted by "the contractor."

At one point during the audit, SCE conceded that it incorrectly did explain to the UAFCB that, "the pay for performance payment is the actual cost of installing the equipment." In a follow-up discussion with the auditor, it was apparent that the response submitted was in error. SCE reviewed the information submitted and discovered an incorrect attachment to the data response. SCE amended the response the following day with the corrected statement, "The Pay for Performance Payment is the fixed cost per ton to deliver the program."

Rebuttal: The draft report did not contain errors in the condition, effect, and rebuttal to field representation statements since those sections were based on the supporting documentation and explanation that SCE provided at the time. UAFCB's conclusion in the draft report was accurate based on the information UAFCB analyzed at the time.

With its comments on UAFCB's draft report, SCE provided additional documentation to substantiate the services provided by the contractor, which UAFCB reviewed. Based on SCE's additional documentation and explanation, UAFCB revised its previous recommendation.

Recommendation: SCE should always recognize that the burden of proof is on the company and it's its responsibility to readily provide correct and accurate information needed to address the auditor's concerns.

Observation 10: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE over-reported its direct implementation cost by at least $65,329 or 8% of the sample selected in the amount of $816,612.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: UAFCB selected and tested $816,611 in direct implementation (DI) costs from purchase order #[redacted]. The invoices reviewed revealed that SCE reported more DI costs than the amount represented as DI on the actual invoices. The over-reported amount was either a marketing or administrative cost.

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate.

SCE Comments: SCE agrees with UAFCB and indicates that it will make correcting entries to transfer the appropriate amount to the correct reporting categories and will provide the UAFCB an internal controls report describing improvements and changes to its internal controls for EE within 90 days of the issuance of UAFCB's final report.

Rebuttal: None

Recommendation: SCE should provide additional training to employees and/or non-employees entering cost data into its systems to ensure that they are able to input the correct data into the systems.

Observation 11: SCE did not demonstrate compliance with PU code §§ 581 and 584, GO 28 and the USOA. SCE provided less than adequate supporting documentation to justify the accrual of an invoice totaling $3,239,657 at the end of 2012.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission. The USOA and GO 28 require that the utilities preserve all records, memoranda, and papers supporting each and every entry so that this Commission may readily examine the same at its convenience.

Condition: In Purchase Order #[redacted], UAFCB selected a sample totaling $4,215,551 in direct implementation costs for review. Of the $4,215,551, one of the samples was in the amount of $3,239,657, representing 88% of the sample. The supporting documentation that SCE provided was one invoice titled "Installation of Energy Efficiency Measures/Projects." According to the invoice, the vendor installed 96,792 measures including, but not limited to, vending machine controls during a two week period from December 7 to December 21, 2012 for approximately 13 schools. However, the invoice's details only listed the school's names and the quantity of measures associated with each school. There was no installation date on the invoice's details or indication that the listed measures were in fact installed. This seems to be inadequate supporting documentation to substantiate the amount charged for the listed measures installed.

Cause: SCE's failure to provide supporting documentation to the auditor as requested.

Effect: UAFCB wasted valuable time that could have been devoted to other audit matters.

SCE Representation in the Field: When this discrepancy was first brought to SCE's attention, SCE requested several days to contact the vendor and get additional information. However, SCE later stated that the $3,239,657 was properly accrued because all work was completed and that the only relevant information on the invoice was the time period and the total amount of the project.

Response to Field Representation: Without proper documentation demonstrating that the 96,792 measures were actually installed, UAFCB doubts the accuracy of the data provided. In addition, the quantity of the measures installed in two weeks is questionable. SCE should reconsider contacting this vendor and provide detailed supporting documentation to allow UAFCB to verify if the measures were in fact installed during the two week period. Support for the work completed is also needed.

SCE Comments: SCE asserts that it did confirm the amounts accrued were supported by information that could be verified. SCE claims that it uses a contractor to verify SCE's commercial upstream program. SCE indicated that it provided the UAFCB during the audit with the invoice and supporting documents it had received prior to December 31, 2012, detailing why this expense was appropriately accrued. SCE points out that although it did not have the final invoice, it accrued the invoice based on the information provided in the preliminary invoice package, which stated the period for when the work was performed (December 2012).

SCE indicates that it received the final invoice from the vendor in 2013. SCE noted that since UAFCB did not request the supporting documents for the 2013 expense; SCE did not provide the UAFCB with the final invoice. With its comments on the draft report, SCE provided additional work papers to support what was paid in 2013.

Rebuttal: According to UAFCB's data requests, SCE was to provide all supporting documentation associated with each amount selected for testing. The fieldwork was not completed until May 2014. Therefore, SCE should have provided the supporting documentation associated with the $3,239,561 in its possession during the audit but failed to do so, wasting valuable time of the auditor and other staff of the UAFCB.

UAFCB reviewed the additional supporting documentation that SCE provided with its comments on UAFCB's draft report and revised its previous recommendation.

Recommendation: SCE should make sure that amounts accrued are supported by timely information to satisfy the auditor's concerns.

A.4 On-Bill Financing (OBF)

Observation 12: SCE did not demonstrate compliance with PU code §§ 581 and 584. SCE did not properly account for its OBF funds and provided UAFCB with data associated with the $32 million OBF revolving loan pool that was inaccurate.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: SCE provided UAFCB with the information shown in the following table.

Table A-2
2012 OBF Loan Composition per SCE

Description	Total Reported
Total Loans in 2012	$ 9,369,014
Collected on Outstanding Loans	(2,418,149)
Total Outstanding Loans	6,950,865
Available Funds	25,049,135
Total OBF Funds	**$32,000,000**[7]

SCE's 2012 outstanding loans in the amount of $6,950,865 were associated with 269 accounts. UAFCB selected 30 or 11% of the 269 accounts for review. Seven or 23% out of the 30 accounts reviewed contained billing errors. SCE claims it reversed some of the overbilled amounts in 2013. In the following tables, UAFCB shows the amounts it determined to be exceptions.

Table A-3
OBF Loan Sample - Overbilled

Loan #	Monthly Payment	Total Loan Principal	Total Payments As of 12/31/12	Error Amount	% of Monthly Payment	Description of Exception
[redacted]	$ 614.10	$ 7,034.50	$ 7,648.60	$ 614.10	**100%**	Overbilled
[redacted]	908.35	5,636.22	6,544.57	908.35	**100%**	Overbilled
[redacted]	9,239.01	45,853.72	64,331.74	18,478.02	**200%**	Overbilled
	$10,761.46	**$58,524.44**	**$78,524.91**	**$20,000.47**	**133%**	**Overbilled**

[7] Pursuant to Resolution E-4473, dated March 8, 2012, SCE was authorized to shift $16 million from its pre-2010 unspent, uncommitted energy efficiency funds to support additional OBF loans for commercial, industrial and government/industrial non-partners. Per SCE's records, SCE shifted the $16 million during the month of June 2012, thereby increasing total OBF by $32 million.

Table A-4
OBF Loan Sample - Errors

Loan #	Monthly Payment	Reported Outstanding Loan as of 12/31/12	Actual Outstanding Loan As of 12/31/12	Error Amount	% Monthly Payment	Description of Exception
[redacted]	$ 7,315.80	$210,026.32	$234,105.80	$24,079.48	**329%**	Error
	3,243.06	33,382.36	33,598.37	216.20	**7%**	Error
	1,654.51	73,042.43	72,798.44	243.99	**15%**	Error
	1,172.00	37,602.82	37,846.81	243.99	21%	Error
Total	**$13,385.37**	**$354,053.93**	**$378,349.42**	**$24,783.66**	**185%**	**Error**

*Total Errors = $44,784 ($20,000+$24,784)

Cause: Lax internal controls or internal controls that are not enforced can lead to recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that could be less than accurate and reliable. Although SCE stated that it corrected some of the errors in 2013, however, the 2012 reported total OBF outstanding loan amount of $6,950,865 was inaccurate by at least $44,000 based on 11% of the loans sampled.

SCE Representation in the Field: SCE reversed some of the overbilled amounts.

SCE Comments: With its comments on UAFCB's draft report, SCE provided additional supporting documentation that it claims verifies that the customer accounts with the overbillings did in fact receive the appropriate credit. SCE noted that it implemented a new procedure after the September 30, 2013 Audit Report was issued.

SCE believes Tables A-3 and A-4 on page A-13 of UAFCB"s draft report contained incorrect information. SCE states that it provided updated amounts to the UAFCB during discovery, but the original (incorrect) value remains. SCE points out that it updated the "Reported Outstanding" value as of December 31, 2012 to be ($216.01).

Rebuttal: Tables A-3 and A-4 in UAFCB's draft report did not contain incorrect information:

1) Table A-3 Loan #[redacted] correctly showed an error of two monthly payments totaling $18,478.02. The supporting documentation that SCE provided for this loan showed that the loan principal amount was $45,853.72. On April 8, 2014, SCE explained with additional supporting documentation that the customer's initial payment was $8,897.68 with the remaining balance to be repaid in equal monthly payments of $9,239.01. In addition, SCE acknowledged that it set the account to bill for 6 monthly payments of $9,239.01 by mistake. In the following table UAFCB shows the error of two monthly payments totaling $18,478.02, based on SCE's documentation.

Table A-5
Billing Over-collection

Principal Amount	Initial Payment	Monthly Payment	Cumulative Payment
$45,853.72	$8,897.68	$9,239.01	$18,136.69
		$9,239.01	$27,375.70
		$9,239.01	$36,614.71
		$9,239.01	**$45,853.72**
		$9,239.01	$55,092.73
		$9,239.01	$64,331.74

As shown in the table above, the customer's loan was paid off with the fourth monthly payment. When SCE mistakenly set the account to six monthly payments, it charged an additional two monthly payments.

2) Table A-4 Loan #[redacted] did not contain outdated values because UAFCB relied on the spreadsheet SCE provided on April 8, 2014. In its comments, SCE claims that it provided updated amounts to UAFCB in its response, dated July 10, 2013, to Data Request 5. UAFCB used the latest data provided by and discussed with SCE on April 8, 2014.

Recommendation: SCE should provide supporting documentation to UAFCB to verify that the customer accounts with overbilling did in fact receive the appropriate credit. In addition, SCE should strengthen its policies and procedures to eliminate these types of errors.

UAFCB believes that the Internal Audit (IA) Department of SCE should include this matter in its next audit scope to clean up this recurring problem.

A.5 Multi-Family Energy Efficiency Rebates (MFEER)

Observation 13: SCE did not demonstrate compliance with PU code §§ 581 and 584, and the USOA. SCE did not make timely adjustments to its 2011 expenses for MFEER, resulting in SCE overstating its MFEER expense in 2012 by at least 31% or by $1,861,057 of the $6,061,917 that the UAFCB sampled.

Criteria: Sections 581 and 584 require the utilities to provide complete and accurate data to the Commission. The USOA prescribes that "The utility is required to keep its accounts on the accrual basis. This requires the inclusion in its accounts of all known transactions of appreciable amount which affect the accounts. If bills covering such transactions have not been received or rendered, the amounts shall be estimated and appropriate adjustments made when the bills are received."

Condition: Of the $1,861,057 at issue, $1,851,709 represented expenses associated with MFEER incentive payments and $9,348 was the total sample selected as temporary labor cost associated with MFEER. SCE's supporting documentation that the UAFCB reviewed revealed that the $9,348 temporary labor costs were for services provided in 2011. Likewise, the $1,851,709 incentive payments were for expenses that also occurred during 2011. SCE received the original incentive payment invoice sometime in 2011 and created a report associated with each invoice.

Cause: SCE's policies require it to wait until an inspection is done for some of the invoices to record the adjusted invoice amount as actual incentive payment cost based on the inspector's finding. SCE received the adjusted invoice amount early in 2012 and failed to adjust its records to properly include these 2011 expenses in its 2011 Energy Efficiency report. Because SCE filed its 2011 Energy Efficiency report in May 2012, SCE had enough time to make the appropriate adjustments to include these 2011 incentive payments in its 2011 Energy Efficiency report.

Effect: SCE recorded and reported data to the Commission that could be less than accurate and reliable.

SCE Comments: SCE claims that of the $1,861,057 in exceptions: (a) $111,703 was properly accrued 2011 expenses and SCE accounted for these as expenses in 2011; and (b) $271,117 was for projects installed in 2012 and, therefore, properly recorded as 2012 expenses. Thus, the correct starting point on SCE's Multi-family Energy Efficiency Rebate (MFEER) program alleged accruals exceptions should be $1,478,237 and not $1,861,057, SCE claims. The remaining $1,478,237 in alleged accrual errors is based on UAFCB's recommendation that SCE should change its accrual methodology for the MFEER program. SCE asserts that it only accrues MFEER measures that have been confirmed as installed through an inspection. SCE claims that UAFCB recommends SCE accrue these measures based on customer applications without confirming the measures were installed. However, because the UAFCB has not applied its methodology consistently at the beginning of the year and the end of the year, the $1,478,237 alleged accrual error is overstated and should be $651,386.

Rebuttal: If $111,703 of the $1,861,057 in question was properly accrued 2011 expenses, SCE had five months from January to May 2013 when SCE filed its Annual Report on 2012 to make the appropriate adjustments by removing expenses associated with the year 2011 from its 2012 expenses. With its comments on UAFCB's draft report, SCE provided additional supporting documentation showing that the $271,117 of the $1,861,057 of UAFCB's original exceptions was for projects installed in 2012. Consequently, UAFCB revised its recommendation and subtracted $271,117 from the $1,861,057, originally reported as total exceptions, leaving $1,589,940 as an exception.

UAFCB's recommendation for the accrual errors should not be the basis for SCE changing its accrual methodology for MFEER program but this should be according to a sound and practical policy. SCE claims it only accrues MFEER measures that have been confirmed as installed through an inspection. This is not accurate since SCE does not inspect all MFEER installed measures. According to SCE's MFEER Policies and Procedures Manual, pages 102-8, SCE only selects a percentage of total installations (about 20% confirmed during the field examination) for inspection and inspectors will inspect every new contractor's first two installations, if the first two installations meet the standard, the inspector will only check one out of every 20 installations from the contractors. UAFCB is not recommending that SCE accrue for measures based on customer applications without confirming the measures were installed.

SCE also claims that the $1,478,237 accrual error is overstated and should be only $651,386 because UAFCB did not apply its methodology consistently at the beginning and end of the year. UAFCB's findings are based on the sample selected for testing. Based on the sample selected, the remaining $1,589,940 accrual errors are not overstated.

Instead of removing $1,861,057, the Commission should remove $1,589,940 ($1,861,057 - $271,117) before the calculation of SCE's 2012 incentive award.

Also, see Observation 3 for UAFCB's reply to SCE's response that is not worth repeating here.

Recommendation: In determining SCE's 2012 incentive award, the Commission should remove $1589, 940 instead of $1,861,057 as originally recommended from SCE's EE 2012 expenses when calculating the incentive award. SCE should strengthen its policies and procedures that eliminate or significantly reduce the inclusion of prior year's expenses in subsequent year's expenses.

A.6 Fund Shifting

Observation 14: SCE failed to demonstrate compliance with OP 43(b) of D.09-09-047. SCE shifted $4.8 million into the On Bill Financing (OBF) without filing an advice letter with the Commission as required by it. In addition, SCE incorrectly reported the $4.8 million shifted as funds authorized when authorization was not granted by the Commission.

Criteria: OP 43(b) of D.09-09-047 provides that IOUs "shall file an Advice Letter for shifts of funds of more than 15% per annum for specific programs... for the entire portfolio cycle." The referenced provisions are further clarified in the Assigned Commissioner's Ruling in Rulemaking (R.)09-11-014.

Condition: Resolution E-4473, dated March 8, 2012, approved a transfer of $16 million from SCE's pre-2010 unspent, uncommitted efficiency funds to support additional OBF loans for Commercial, Industrial and government/institutional non-partners. During the second quarter of 2012, SCE transferred the approved $16 million per Resolution E-4473. However, SCE transferred an additional $4.8 million from various programs to OBF without filing an advice letter as required. UAFCB summarizes its observations in the following table.

Table A-6
Fund Shift Into Without Advice Letter

Funds Transferred From	Amount	Fund Transferred To
California Advance Homes	$ 700,000	OBF
IGREEN Partnership Program	2,000,000	OBF
Industrial Calculated Energy Efficiency	2,100,000	OBF
Total	**$4,800,000**	

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors.

Effect: SCE shifted funds without Commission authorization. SCE recorded and reported data to the Commission that are likely misleading and less than accurate.

SCE Representation in the Field: SCE will revise its 2012 quarterly report to remove the $4.8 million fund shift. SCE claims the $4.8 million fund shift was based on a revised authorized budget of $32 million for the Financial Solution Program. The revised authorized budget was based on the $16 million fund shift approved by CPUC in Resolution E-4473. SCE alleges that it initiated the $4.8 million fund shift in October 2012 since it was expecting a level of demand in the Financial Solutions Program which did not materialize. SCE realized now that it did not need to shift the $4.8 million.

Response to Field Representation: SCE's comments contradict its own records and previous statements. SCE's supporting documents and filed report for the second quarter in 2012 revealed that the shift took place in the second quarter and not in October 2012. In addition, in July 10, 2013, when UAFCB requested SCE's 2012 OBF loan wait list, SCE replied as followed, "There was not a wait list implemented as of December 31, 2012. In March 2012, a $20.8 million fund shift to the OBF loan budget provided the funding necessary to clear the 2011 wait list and allowed the program to accept additional projects for 2012." The $20.8 million fund shift included the additional $4.8 million SCE shifted into OBF without Commission authorization. After making the additional $4.8 million fund shift into OBF in March 2012 in order to clear its 2011 wait list, SCE's latest comment that the $4.8 million was not needed because the level of demand did not materialize contradicts its own records.

SCE Comments: In response to UAFCB's Observations 14, 15, 16, 17 and 18, SCE agrees that SCE caught and corrected five fund-shifting reporting errors during 2012, prior to the UAFCB audit, demonstrating the effectiveness of SCE's self- monitoring detective control environment. SCE agrees to provide UAFCB an internal controls report describing improvements and changes to them for the energy efficiency programs within 90 days of the issuance of UAFCB's Final Report.

SCE disagrees with UAFCB's assertion that "SCE's comments contradict its own records and previous statements." The statements of "a $20.8 million fund shift to OBF loan budget provided the funding necessary to clear the 2011 wait list and allowed the program to accept additional projects for 2012" and "$4.8 million was not needed because the level of demand did not materialize" are not contradictory. At the time of the fund shift, SCE claims that the expectation of program demand was that the $20.8 million would be needed to fund all loans requested. SCE points out that the expected demand did not materialize. SCE was able to fund all projects that existed on the wait list at the time of the fund shift, and due to the absence of demand, no further loans were placed on a wait list, which SCE reported to UAFCB on July 10, 2013, as stated in the draft report.

Rebuttal: SCE states that its self- monitoring detective control environment is effective because it caught and corrected five fund-shifting reporting errors. However, UAFCB identified twenty (20) fund shifting errors in the sample, demonstrating SCE only caught 25% of the errors. Consequently, UAFCB does not consider SCE self- monitoring detective control environment effective. UAFCB looks forward to SCE internal controls report describing improvements and changes to them for energy efficiency programs within 90 days of the issuance of the Final Report.

SCE disagrees with UAFCB's assertion that SCE's comments contradict its own records and its previous statements. However, the supporting documentation that SCE provided reveals the contradiction. In its supporting documentation dated July 10, 2013, SCE stated that the $4.8 million fund shift took place in March 2012. However, in its supporting documentation dated March 14, 2014, SCE stated that the $4.8 million fund shift was initiated in October 2012.

Recommendation: SCE should strengthen its policies and procedures in place to ensure compliance with Commission directives.

Observation 15: SCE failed to demonstrate compliance with PU code §§581 and 584. In its first quarter 2012 EEGA Report, SCE incorrectly reported that Resolution E-4474 authorized fund shifts totaling $29,000,000.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: SCE's first quarter 2012 report refers to Resolution E-4474 as the document approving fund shifts totaling $29 million. UAFCB's review of Resolution E-4474 revealed that no such approval was granted.

Cause: According to SCE, Resolution E-4474 was referenced in error as the document authorizing the fund shifts in SCE's 2012 Q1 Energy Efficiency Fund Shift report.

Effect: SCE's first quarter 2012 fund shift report filed with the Commission is inaccurate and misleading.

SCE Comments: See UAFCB's summary of SCE's response in Observation 14.

Rebuttal: See UAFCB's reply in Observation 14 to SCE's response.

Recommendation: SCE should exercise due diligence to ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.

The Energy Division should provide the necessary guidance to the reporting utilities on where and how to reflect prior corrections to monthly, quarterly, and annual reports in EEGA.

Observation 16: SCE failed to demonstrate compliance with Resolution E-4474 and §§581 and 584. In its second quarter fund shift report for 2012, SCE reported a fund shift of $14.8 million from the Commercial Deemed Incentive sub- program to the Industrial Calculated Incentive sub program instead of reporting the $14.8 million from the Industrial Calculated Incentive sub-program to the Commercial Deemed Incentive sub-program as provided by Resolution E-4474.

Criteria: Resolution E-4474 provides that SCE shall shift $14.8 million from the Industrial Calculated Incentive sub-program to Commercial Deemed Incentive sub program. Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: SCE incorrectly reported its fund shift activities in its 2012 second quarter report and referred to Resolution E-4474 as the document approving the $14.8 million fund shift from the Commercial Deemed Incentive sub- program to the Industrial Calculated Incentive sub program.

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors.

SCE Representation in the Field: According to SCE, its 2012 second quarter fund shift report incorrectly reflected the $14.8 million fund shift. SCE corrected this error in its 2012 Third Quarter Fund shifting Report. However, this still leaves the second quarter report misleading and inaccurate.

Effect: SCE's second quarter 2012 fund shifting report filed with the Commission is inaccurate and misleading.

Recommendation: SCE should exercise due diligence to ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.

The Energy Division should provide the necessary guidance to the reporting utilities on where and how to reflect prior corrections to monthly, quarterly, and annual reports in EEGA

SCE Comments: See UAFCB's summary of SCE's response in Observation 14.

Rebuttal: See UAFCB's reply in Observation 14 to SCE's response.

Observation 17: SCE failed to demonstrate compliance with §§581 and 584. SCE reported a negative balance of ($2,822,212) in its Commercial Utility building Efficiency (CUBE) program during the second and third quarter 2012 without filing an advice letter.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: SCE's Quarter 2 and Quarter 3 fund shift report for the year 2012 showed a negative operating budget balance of ($2,822,212) for the Commercial Utility Building Efficiency (CUBE) program.

Cause: According to SCE, in 2011, SCE shifted and correctly reported a $7,290, 000 fund shift from CUBE (third-party program) to the Commercial Direct Install (third-party program). However, in subsequent 2012 fund shift reports, SCE mistakenly reflected the $7,290,000 fund shift again, which caused the fund shift report to incorrectly show a negative operating budget balance for the CUBE program.

Effect: SCE second and third quarters fund shift reports filed with the Commission are inaccurate and misleading.

Recommendation: SCE should ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.

The Energy Division should provide the necessary guidance to the reporting utilities on where and how to reflect prior corrections to monthly, quarterly, and annual reports in EEGA

SCE Comments: See UAFCB's summary of SCE's response in Observation 14.

Rebuttal: See UAFCB's reply in Observation 14 to SCE's response.

Observation 18: SCE failed to demonstrate compliance with §§581 and 584. During the second and third quarter of 2012, SCE incorrectly reported a total fund shift of $6,661,492, which was previously authorized and it already shifted in 2011.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: SCE was authorized to make several fund shifts in 2011. SCE repeated the fund shifts in 2012. In the following table, UAFCB summarizes the fund shift that SCE incorrectly reported.

Table A-7
2011 Fund Shift Repeated in 2012 By Mistake

Programs/Sub-Programs Transferred Out	Programs/Sub-Programs Transferred In	Amount
MFEER	[redacted]	$4,425,492
Calculated Incentives Program		638,000
HVAC Workforce E. & Training		176,000
Energy Leader Partnership		422,000
Integrated Marketing	WE&T Centergies	1,000,000
Total		**$6,661,492**

Cause: According to SCE, the $6,661,492 in fund shifts were repeated by mistake.

Effect: SCE's second and third quarter fund shift reports filed with the Commission were inaccurate, misleading and inaccurate.

Recommendation: SCE should exercise due diligence to ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.

The Energy Division should provide the necessary guidance to the reporting utilities on where and how to reflect prior corrections to monthly, quarterly, and annual reports in EEGA.

SCE Comments: See UAFCB's summary of SCE's response in Observation 14.

Rebuttal: See UAFCB's reply in Observation 14 to SCE's response.

A.7 EE Balancing Accounts

Observation 19: SCE did not demonstrate compliance with §§ 581 and 584. SCE's 2012 On-Bill Financing balancing account contains inaccurate data.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: The On-Bill Financing Balancing Account (OBFBA) is a one-way balancing account used to record the difference between the authorized On-Bill Financing (OBF) funding and the actual amount of OBF loaned amounts net of recorded loan repayments.[8] SCE's OBF authorized funding as of March 8, 2012 was increased to $32 million for its 2010-2012 cycle.[9] According to SCE's OBFBA preliminary statement, SCE shall make a

[8] UAFCB considers its observations material because of: (a) the size of UAFCB's sample; (b) UAFCB could not test any of the labor costs sampled; (c) the cumulative effect of lack of documentation of some samples, and (d) the frequency and multiple types of errors.

[9] See Resolution E-4473. This resolution increases SCE's OBF funding by $16 million. Prior to this increase, SCE's OBF funding was set at $16 million per D.09-09-047.

credit entry equal to one-twelfth of the annual authorized OBF funding.[10] In 2012, SCE failed to update its annual OBF authorized funding after the increase from $16 million to $32 million. SCE's OBFBA shows that the annual authorized budget is $5.3 million based on the original $16 million authorized for OBF funding. Excluding the discrepancy associated with its authorized OBF funding, SCE's 2012 summary of its OBFBA is still inaccurate because: 1) it does not reflect the adjustment that SCE discovered during the reconciliation of its OBF transactions and 2) it does not reflect overbilling errors to several customers during 2012 that it did not correct until 2013.

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate.

SCE Representation in the Field: Regarding SCE's overbilling of several of its customers, SCE stated that it made the appropriate corrections in 2013. Regarding the increase of its OBF funding from $16 million to $32 million, SCE stated that it did not need to revise its annual authorized budget because Resolution E-4473, which increased funding to OBF, did not authorize SCE to follow the preliminary statement associated with the original loan amount of $16 million. SCE also stated that since the additional $16 million increased the OBF funding to $32 million that was already being collected from ratepayers; it did not seek any additional collection from ratepayers.

Response to Field Representation: SCE's explanations are not in compliance with the known and existing preliminary statement authorized by the Commission. Record keeping and ratemaking are two different things.

SCE Comments: SCE asserts that Observation 19 is incorrect and should be removed from the final audit report. The Draft Report states that "SCE's OBF authorized funding as of March 8, 2012 was increased to $32 million for its 2010-2012 cycle," and that "In 2012 SCE failed to update its annual OBF authorized funding after the increase from $16 million to $32 million."

SCE asserts that the Draft Report misinterprets what the Commission ordered in Resolution E-4473. SCE alleges that the Commission did not order the authorized funding be increased by $16 million, but rather required SCE to "...transfer $16 million in pre-2010 unspent, uncommitted energy efficiency funds to support additional OBF loans for commercial, industrial and government/institutional non-partners." SCE points out that an authorized shift/transfer of funds is not the same as an authorized increase in revenue requirement for additional funds.

[10] The annual authorized funding is the authorized budget for the cycle 2010-2012 divided by the three years. For a $16 million budget, the annual budget equal $5.333 million; for $32 million authorized budget, the annual budget is $10.666 million.

SCE indicates that its Preliminary Statement DDD (On Bill Financing Account) allows SCE to make a debit or credit entry, as appropriate, to record the transfer of amounts to or from other accounts as approved by the CPUC, which SCE did, correctly, as demonstrated in the next paragraph. Because SCE was never authorized to increase OBF funding by an additional $16 million through an increase in the revenue requirement, but only to transfer previously collected unspent funds, the calculation using a $32 million authorized budget is incorrect.

In compliance with Resolution E-4473, SCE transferred $16 million from the Procurement Energy Efficiency Balancing Account (PEEBA) (i.e. uncommitted energy efficiency funds) to the OBF Balancing Account (OBFBA) in June 2012. In doing so, this achieved the Commission's objective to have more funds available to support additional OBF loans.

The draft observation states that SCE's 2012 OBFBA is wrong because it "1) does not reflect the adjustment that SCE discovered during the reconciliation of its OBF transactions and 2) it does not reflect overbilling errors to several customers during 2012 that did not correct until 2013." SCE claims that this is precisely why the Commission establishes balancing accounts. From time to time, there are adjustments, such as the adjustments discovered during SCE's reconciliation, which need to be made to entries that have previously been recorded in a balancing account. When an adjustment must be made, the company does not go back and "restate" the balancing account, but rather records correcting entries in the account once the need for the adjustment is known.

Rebuttal: The Draft Report did not misinterpret what the Commission ordered in Resolution E-4473. UAFCB did not state or imply that the additional $16 million transfer to increase OBF loans was an increase in revenue requirement for additional funds. According to SCE's Preliminary Statement DDD (On Bill Financing Account), "SCE shall maintain the OBFBA by making… a credit entry to one-twelfth of the annual authorized OBF loan funding." Preliminary Statement DDD does not appear to distinguish the source of funding. Therefore, when SCE transferred an additional $16.0 million as required by Resolution E-4473, SCE had $32.0 million available to fund its OBF loans. This $32.0 million is the new authorized funding amount as a result of the transfer of the $16.0 million to fund OBF loans. SCE may consider filing an advice letter to revise its Preliminary Statement DDD to define what "annual authorized OBF loan funding" means. How would SCE reflect the funding level increase to OBFBA of $16.0 million in the OBFBA if it would not increase the amount of funding level for it to $32.0 million because this is not a new revenue requirement increase?

If this were a transfer from one balancing account to another balancing account, one balancing account would up and the other down by the same amount, a zero sum.

SCE also states that it was the Commission's objective according to Resolution E-4473 to have more funds ($16 million more) available to support additional OBF loans. Disregarding the source of funding, this statement alone shows that the UAFCB correctly interpreted Resolution E-4473 when it stated that SCE's OBF loan funds increased from $16 million to $32 million.

UAFCB's draft report did not state that SCE's OBFBA was wrong because SCE did not go back and "restate" its balancing account. This would be SCE's interpretation.

The audit of SCE's 2012 OBF balancing account was not concluded until May 2014. The adjustments and reconciliation errors in question took place early 2013. So, the need for the adjustment was known to SCE in 2013. Prior to fieldwork conclusion, SCE did not provide any record or data showing that it made the appropriate adjustments. In addition, in its response to UAFCB's draft report, SCE had the opportunity to provide any supporting data to support its assertions that the adjustments to its OBFBA were made in 2013 but it did not do so.

Recommendation: SCE should follow Commission's directives. In addition, SCE should strengthen its policies and procedures to eliminate or substantially reduce the level of errors included in its reports to the Commission.

Observation 20: SCE did not demonstrate compliance with §§ 581 and 584. SCE's 2012 Procurement Energy Efficiency Balancing Account (PEEBA) and Public Purpose Program Adjustment Mechanism (PPPAM) did not include accurate data. SCE did not reflect the revised annual authorized amount for OBF in the PPPAM. Labor costs captured in PEEBA were estimated.

Criteria: Sections 581 and 584 require that the utility provide complete and accurate data to the Commission.

Condition: OBF's authorized funding should be reflected in the PPPAM account. Through the PPPAM, SCE trues-up recorded revenue received from customers to authorized funding amounts. Collections more than authorized are refunded to customers and collections less than authorized are recovered from customers. In 2012, SCE's annual authorized funding increased from $5.3 to $10.6 million, representing one-third of the new authorized budget of $32 million (see observation 19). SCE did not reflect the updated OBF authorized annual funding in its PPPAM account. In addition, SCE's PEEBA should record the difference between its procurement related energy efficiency funding and the actual amount of procurement related energy efficiency expenses. SCE's acknowledgment that it used estimated labor cost in its PEEBA shows that not all expenses recorded in its PEEBA are actual costs.

Cause: SCE failed to follow-up with budget changes to its EE regulatory accounts.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate.

SCE Comments: SCE disagrees that SCE has errors in PPPAM and PEEBA. First, the data included in PPPAM is accurate. As mentioned in its comments on UAFCB's draft report for Observation 19, there wasn't any need to reflect updated authorized funding in the PPPAM because the $16 million was a Commission-approved fund shift (i.e. transfer) of pre-2010 unspent, uncommitted energy efficiency funds from the PEEBA to the OBFBA. This transfer was made in June 2012 as approved by Resolution E-4473 and

Advice Letters 2710-E/2710-E-A. The authorized amounts for PEEBA and OBFBA remained unchanged until the Commission issued D.12-11-015 for the 2013-2014 authorized funding levels.

Second, the labor data included in PEEBA was not estimated. As described its response to UAFCB's draft Observations 1, 2, and 20 regarding labor, SCE does not record estimated labor costs. SCE records the amount that goes out of HCCs (standard labor + recalc/reval) to SCE's Cost Objects which tie to the balancing accounts. This amount is equal to what goes into HCCs (actual labor) which ties to SCE's audited General Ledger.

Rebuttal: See the Rebuttal for Observations 1, 2, 20 and 19.

Recommendation: SCE should comply with Commission's directives by correctly applying its authorized and approved regulatory accounts.

A.8 SCE's Internal Audit Reports

Observation 21: In SCE's Internal Audit reports, dated March 14, 2012, April 25, 2012 and February 12, 2013, UAFCB noted that each internal report revealed control weaknesses. The observations associated with the control weaknesses as indicated in its internal audit reports for the year 2011 and 2012 are similar to observations UAFCB noted during its examination of 2011-12 EE accounting, recording, and reporting activities, with respect to directives from the Commission and SCE's policies, processes, and procedures.

Criteria: SCE's Internal Auditing section conducted several audits and their objectives among other things, were to: 1) review EE programs and savings; and 2) assess and review non-incentive expenditures recorded to the balancing accounts for selected EE programs and evaluate compliance with CPUC program guidelines and the program's policies and procedures.

Condition: SCE's Internal Audit group observed in 2011 that SCE inadvertently reported inaccurate energy savings data to the Commission's Energy Division. In 2012, SCE's internal audit team concluded that SCE no longer had any weakness with respect to the reporting of inaccurate energy savings data to Energy Division. However, UAFCB noted that during its 2012 EE examination that SCE intentionally reported inaccurate energy savings to the Commission (see Observation 6).

SCE's Internal Audit team also observed in its 2011 and 2012 balancing accounts review that some contractors' invoices lack supporting documents. For example, there was insufficient documentation to verify the actual hours worked and reported on invoices; vendors did not comply with purchase orders (PO) terms and conditions; SCE's management did not properly enforce the contracts; and there was misclassification of EE program expenditures within the balancing accounts resulting in inaccurate data filed with the Commission on EEGA. UAFCB noted similar observations in its 2011 and 2012 reports.

Cause: Lax internal controls or internal controls that are not enforced can cause recording and reporting errors. Employees who are not properly trained and supervised can also contribute to recording and reporting errors.

Effect: SCE recorded and reported data to the Commission that are likely misleading and less than accurate.

Recommendation: SCE should exercise due diligence to ensure that its reports are accurate before submitting them to the Commission and posting them to EEGA.

A.9 Follow-Up on Prior UAFCB's Examinations

Observation 22: SCE demonstrated compliance with most of UAFCB's recommendations from its prior two examinations, with the exceptions discussed below.

Criteria: Pursuant to UAFCB's examination reports, SCE is required, among other things, to: [11]

1) Exercise due diligence in reviewing and approving all invoices and ensure that the EE expenditures are accurately classified and properly recorded in its accounting system

2) Strengthen its internal controls for recording and reporting its EE to prevent future misreporting and misclassifications of SCE's EE.

Condition: Judging by the magnitude of the discrepancies found during this examination, (Observations 1 through 21 of this report), SCE failed to sufficiently strengthen its internal controls for recording and reporting the EE expenses and prevent future misreporting and misclassification of EE expenditures. In addition, SCE does not seem to be exercising due diligence in reviewing and approving its invoices to ensure that the EE expenditures are accurately classified and properly recorded in its accounting system.

Recommendation: SCE should work on strengthening and enforcing its internal controls for recording and reporting its EE to prevent future misreporting and misclassifications of SCE's EE, and exercise due diligence in reviewing and approving all invoices to ensure that the EE expenditures are accurately classified and properly recorded in its accounting system

A.10 Internal Controls

Observation 23: As shown throughout this report, SCE did not demonstrate compliance with the Commission's EE reporting requirements, its own policies and procedures, the

[11] *Interim Financial, Management and Regulatory Compliance Examination of Southern California Edison Company's Energy Efficiency (EE) Programs for the Year Ended December 31, 2010,* issued on March 23, 2012.*and Energy Efficiency (EE) Financial Compliance Examination Report of Southern California Edison (SCE) For the Period January through December 31, 2011*, issued on September 30, 2013.

USOA, GO 28, §§ 581 and 584 and accounting best practices. As demonstrated in previous observations, SCE does not adequately control its data for EE reporting and record keeping.

Criteria: The Commission prescribes what administrative costs can be recovered and how they should be reported. The USOA and GO 28 require that the utilities preserve all records, memoranda and papers supporting each and every entry so that this Commission may readily examine the same at its convenience. The USOA also requires that the utilities use the accrual method of accounting. Section 581 requires that "... Every public utility receiving from the commission any blanks with directions to fill them shall answer fully and correctly ..." Section 584 requires utilities to provide reports to the Commission as specified by the Commission. Accounting best practices dictate the use of effective internal controls that are monitored and vigorously enforced.

Condition: The samples that UAFCB tested during the examination reveal that SCE's reports to the Commission contain material errors. SCE needs to improve its reporting and record keeping processes. It needs to monitor and vigorously enforce its existing internal controls.

Internal controls are used to provide a company's management reasonable assurance about the:

1. Effectiveness and efficiency of operations;
2. Reliability of financial reporting; and
3. Compliance with applicable laws and regulations.

Internal controls are put into place in these types of situations to prevent and identify accounting and reporting errors and the violation of laws and regulatory requirements.

The Committee of Sponsoring Organizations (COSO) is a nationally recognized group that provides thought leadership through the development of comprehensive frameworks and guidance on risk management, internal control and fraud deterrence.[12] COSO indicates that internal controls consist of five interrelated components:

- Control Environment: Includes the integrity, ethical values and competence of the entity's people; and management's philosophy and operative style.
- Risk Assessment: The identification and analysis of relevant risks to the achievement of objectives and forms the basis of how the risks should be managed.
- Control Activities: Policies and procedures that help ensure management directives are carried out.

[12] COSO was organized in 1985 to sponsor the National Commission of Fraudulent Financial Reporting, an independent private-sector initiative that studies the causal factors that can lead to fraudulent financial reporting. It also developed recommendations for public companies and their independent auditors, for the SEC and other regulators, and for educational institutions.

- Information and Communication: Pertinent information must be identified, captured and communicated, including, but not limited to, external parties such as regulators.
- Monitoring: Internal controls need to be monitored to assess the system's performance over time.

A first step in improving SCE's EE reporting processes should be for SCE to constantly monitor and vigorously enforce its internal controls for its EE reporting, including but not limited to, requiring audits of its own reporting processes and the reporting and processes of its contractors with respect to invoicing. When designing and implementing its new EE internal controls, SCE should consider all of the factors discussed above and throughout this report.

Cause: UAFCB and SCE found several errors that SCE made in recording its EE activities. Some of these were quite substantial, such as but limited to, SCE's errors associated with its fund shifts totaling $53 million. Clearly SCE's internal controls are not effective to prevent many errors or they are not being vigorously enforced.

Effect: Without adequate internal controls that are vigorously monitored and enforced, SCE's recording and reporting errors are likely to continue.

Recommendation Within 90 days from the date of this report, SCE should strengthen its internal controls for recording and reporting its EE programs to prevent future misreporting and misclassifications of SCE's EE costs, and provide UAFCB a copy of the revised internal controls. In addition, SCE should describe how it will monitor and vigorously enforce these to improve the recording and reporting process to the Commission. While a small percentage of errors can be tolerated, SCE should improve its EE internal controls, minimizing the recording and reporting errors and eliminate the occurrence of widespread errors throughout the recording and reporting process of SCE's EE activities.

Appendix B
Program Compendium

B.1 Introduction

On September 24, 2009, the California Public Utilities Commission (Commission) issued Decision (D.) 09-09-047 which, among other things, authorized Southern California Edison Company (SCE) a total budget of approximately $1.23 billion in ratepayer funds to administer and implement its Energy Efficiency (EE) programs for the years 2010 through 2012, including $49 million dedicated to Evaluation, Measurement and Verification (EM&V). Since SCE estimated that it had $35 million of unspent and uncommitted funds by the end of 2009, SCE subtracted the $35 million from the $1.23 billion in order to determine how much additional money was needed for recovery from customers during the funding cycle 2010-2012. SCE set rates over the three year-period to recover $1.19 billion ($1,228 billion - $35 million). In this decision, the Commission also set energy savings goals, established cost-effectiveness requirements, placed a cap of 10 percent on utility administrative costs, authorized types of programs, and set targets for certain programs.

B.2 EE Funding Components

SCE's total Commission authorized EE budget (net of EM&V of $49 million) was $ 1.18 billion for budget cycle 2010-2012. As of December 31, 2012, excluding EM&V expenditures, SCE spent $ 907 million, or 77%, of its total authorized budget for the 2010-2012 budget cycle. In the following table, UAFCB shows the authorized budget, the actual expenditures for SCE during 2012 as reported on the Energy Efficiency Groupware Application (EEGA)'s website, the funds available for spending, and the amount carried forward to 2013.

Table B-1
Summary of 2012 Ratepayer Funded EE Programs
(Excluding EM&V)

Description	Amount
Authorized Budget per D.09-09-047	$1,178,880,003
Less: Actual 2010 EE Expenditures	271,131,995
Available for Spending in 2011	907,748,008
Less: Actual 2011 EE Expenditures	334,633,524
Amounts Carried Forward to 2012	573,114,484
Less: Actual 2012 EE Expenditures	301,286,112
Amounts Carried Forward to 2013	**$ 271,828,372**

SCE's Customer Service Operating Unit (Customer Service) is responsible for the operation of the energy efficiency programs, among other things. Within Customer Service, the Customer Programs & Services Division's (CP&S) primary function is to assure that energy efficiency programs are properly managed and in compliance with Commission's directives. Within the CP&S are the Customer Energy Efficiency and Solar Division (CEES), which manages the implementation and the day-to-day operation of SCE's energy efficiency programs, along with other Demand Side Management (DSM) Programs. The CEES groups include: 1) Program and Operations, 2) Regulatory, Controls and Solicitations, 3) Strategic Planning and Technical Services and 4) Measurement and Evaluations. As of December 31, 2012, the CEES employed 158 fulltime employees, not including consultants and contract workers, primarily focused on energy efficiency.

B.3 Administrative Costs

Pursuant to D.09-09-47 Ordering Paragraph (OP) 13, the Commission limited the utilities' administrative costs for managing the EE programs to 10% of the total EE budget for years 2010-2012. For 2012, SCE's EE Budget was $439.6 million and its total EE portfolio expenditure (net of EM&V) was $301.3 million. SCE's total EE administrative expenditures (excluding EM&V) incurred in 2012 amounted to $22.7 million.

SCE classifies EE administrative expenses into three cost categories: (1) program costs that are expenses related to EE program activities internally handled by SCE, (2) vendor costs that are non-IOU EE program activities from strategic partners, and (3) allocated costs that are indirect costs incurred by SCE's internal units that provide support services to the EE programs.

SCE uses two methods to allocate indirect costs to its EE programs- (1) the Distribution Cost Centers (DCC) method and the Internal Market Mechanism (IMM) method. The DCC method allocates Customer Service Organizational Unit (Customer Service) costs incurred by EE programs which cannot be directly assigned to each program. DCC costs include financial support, regulatory support, internal audit, training, etc. The IMM involves the allocation of competitively procured services by internal providers and includes services such as telephone moves, telephone toll and long distance calls, pager services, and device repairs.

In the following table, UAFCB shows a summary of SCE's EE administrative cost cap and target expenditures that demonstrates that SCE stayed within the 10% cap required by the Commission during the budget cycle.

Table B-2
Energy Efficiency Administrative Cost Cap and Expenditures
For Budget Cycle 2010 – 2012

Expense Category	2010	2011	2012	Total	% to Total Budget Portfolio	% Cap	% Target
Non SCE (Excl. LGP) Admin Costs	$ 3,805,609	$ 5,970,685	$ 7,006,970	$16,783,264	1.61%		10%
LGP Admin Costs	$317,385	$667,653	2,957,643	3,942,681	0.38%		10%
SCE Admin	24,342,016	20,487,100	12,765,922	57,595,038	5.51%	10%	
Total Admin (Excluding EM&V)	**$28,467,020**	**$27,127,449**	**$22,730,535**	**$78,325,004**	**7.49%**		
Total Operating EE Budget (Excl. EM&V)	**$271,131,995**	**$334,633,524**	**$439,618,561**	**$1,045,384,080**			

B.4 Energy Efficiency Contracts

The CPUC requires that 20% of the energy efficiency portfolio budget, including administration, marketing, and Evaluation, Measurement, and Verification (EM&V) should be administered by contractors or consultants. As part of SCE's proposed 2010-2012 portfolio, SCE is required to identify those Third Party programs, which should count towards meeting or exceeding the 20% requirement. The Commission confirms as part of its compliance review and adoption of SCE's 2010-2012 that it met this requirement.

To manage costs associated with these Third Party (3P) program implementers and other vendors, SCE maintains contracts with 3P Implementers, LGP and Others.

Contracts that are associated with 3P program implementers generally target stand-alone programs. A distinct feature of 3P program implementer contracts is that the contractors are responsible for administering all aspects of the program including, administration, marketing and implementation. SCE identified and the Commission approved all the 3P program implementers as part of the 2010-2012 Energy Efficiency Program Plans.

The focus of the LGP vendors is to build capacity by implementing program activities within the local government area. The LGP is responsible for administering all aspects of the programs. The third vendor type consists of contracts between SCE and "Other Contractors or Vendors". The vendor or contractor reaches out directly or through SCE to assist customers with EE projects to access rebate or incentive programs.

A summary of SCE's EE contractor costs for program year 2012 by payment type and cost category is provided in the following table.

Table B-3
Contractor Costs by Payment Type
January 1, 2012 through December 31, 2012

Description	Time & Material	Performance Based	Fixed Rate	Hybrid	Total	%
Administration	$ 3,326,393.49	$ 2,697,979.76	$ 49,464.58	$1,194,634.81	$ 7,268,472.64	4.08%.
Marketing	3,178,572.33	2,238,167.99	2,797,003.54	947,659.75	9,161,403.61	5.14%
Direct Implementation	52,166,986.06	94,608,408.99	4,046,268.95	7,512,237.79	158,333,901.79	88.89%
EM&V	3,356,320.69	0	10,005.00	0	3,366,325.69	1.89%
Total	**$62,028,272.57**	**$99,544,556.74**	**$6,902,742.07**	**$9,654,532.35**	**$178,130,103.73**	**100%**

A summary of SCE's EE contractor costs for program year 2012 by contractor type and cost category is provided in the following table.

Table B-4
Contractor Costs by Contractor Type
January 1, 2012 through December 31, 2012

Description	3P	Core[1]	LGP	Total	%
Administration	$ 3,985,003.83	$ 2,344,881.87	$ 938,586.94	$ 7,268,472.64	4.08%
Marketing	3,513,123.65	4,796,409.02	851,871.25	9,161,403.61	5.14%
Direct Implementation	35,744,064.65	104,706,324.81	17,883512.33	158,333,901.79	88.89%
EM&V	0	3,366,325.59	0	3,366,325.69	1.89%
Total	**$43,242,191.82**	**$115,213,941.39**	**$19,673,970.52**	**$178,130,103.73**	**100%**

For the budget cycle 2010 – 2012, the Commission set the target for direct implementation expenditures at 20% of total portfolio expenditures. Per SCE's reports on EEGA, the direct implementation expenditures were 23.2% for the cycle 2010 – 2012. Therefore, SCE exceeded this target by 3.2%.

[1] Not classified as TP or LGP

B.5 On-Bill Financing (OBF) Program

SCE's OBF program is a non-resource program offered to eligible non-residential customers to offset the up-front cost of purchasing and installing qualified energy efficiency retrofit measures for approved projects participating in energy efficiency programs such as the statewide commercial, industrial, and agricultural customized, express pending programs, LGP or qualifying third party implemented programs. Through OBF, qualified non-residential customers receive a zero-interest, no fee unsecured financing.

Financing is available for up to 100% of the total actual installed costs (minus the incentive), including related contractor labor charges. The minimum loan amount per service account is $5,000 for commercial customers. Government and institutional customers may bundle projects to meet the $5,000 minimum. The maximum loan amount available per service account is $100,000 for commercial customers and $250,000 for governmental and institutional customers. However, government and institutional customers are eligible for loans of up to $1 million and may designate one service account per facility to receive the $1 million maximum loan amount.

In D.09-09-047, OP 40, the Commission set the commercial loans terms to up to five years or the expected useful life (EUL) of the bundle efficiency measures proposed, whichever is less. For institutional customers, a maximum loan term of 10 years or the EUL of the bundle efficiency measures proposed, whichever is less.

SCE's OBF budget for the 2010-2012 EE programs cycle is approximately $40 million, as set forth in D.09-09-047 and Resolution E-4473. The budget provides for operating expenses of $8 million funded by the Public Goods Charge (PGC) and a revolving fund loan pool of $32 million funded by non-PGC revenues pursuant to D.09-09-047 and approved in SCE's Advice Letters (AL) 2456-E and 2456-E-A.

AL 2456-E and AL 2456-E-A authorized SCE to set up an On-Bill Financing Balancing Account (OBFBA) for the 2010-2012 EE budget cycle to track OBF loan disbursement and repayment activities.

The OBFBA is used to record the difference between the authorized On-Bill Financing funding of $32 million and the actual amount of On-Bill financing loaned amounts net of recorded loan repayments

As of December 31, 2012, SCE reported that its $32 million revolving loan pool consisted of an outstanding loan balance in the amount of $6.9 million and the remaining $25 million balance was available to accept additional projects as shown in the following table.

Table B-5
2011 - 2012 OBF Loan Composition per SCE

Description	2011 Total Reported	2012 Total Reported
Total Loans in 2012	$ 4,304,677	$ 9,369,014
Collected on Outstanding Loans	(390,975)	(2,418,149)
Total Outstanding Loans	**$ 3,913,702**	**$ 6,950,865**
Committed / Available Funds in Loan Pool[2]	12,086,298	25,049,135
Total OBF Funds	**$16,000,000**	**$32,000,000**

In 2012 SCE spent $0.9 million on the OBF program, of which 77% was charged to Direct Implementation. In D09-09-047, page 50, the Commission allows for non-resource programs such as OBF to treat as Direct Implementation those costs associated with activities that are a direct interface with the customer or program participant or recipient. In the following table, UAFCB shows the breakdown of the 0.9 million spent by SCE in 2012.

Table B-6
2012 On-Bill Financing Program Expenditures

Expenditure Type	Labor	Non-Labor	Allocated Overheads	Total
Admin-IOU	$ 2,072	$ (3,944)	$193,700	$191,828
Marketing/Outreach		5,389		5,389
Direct Implementation	226,274	384,133	59,069	669,476
Total Expenditures	**$228,346**	**$385,578**	**$252,769**	**$866,693**

In 2011, SCE's OBF total program expenditures were about $1.47 million as shown in the following table:

Table B-7
2011 On-Bill Financing Program Expenditures

Expenditure Type	Labor	Non-Labor	Allocated Overheads	Total
Admin-IOU	$ 15,491	$296,335	$226,342	$ 538,168
Marketing/Outreach		602		602
Direct Implementation	291,604	582,995	60,320	934,919
Total Expenditures	**$307,095**	**$879,932**	**$286,662**	**$1,473,689**

B.6 Multi-Family Energy Efficiency Rebates (MFEER)

The Multi-Family Energy Efficiency Rebate Program (MFEER) offers prescribed rebates for energy efficient products to motivate multi-family property owners/managers to install energy efficient products in both common and dwelling areas of multifamily complexes and common areas of mobile home parks and condominiums. The desired outcome of MFEER implementation is to

[2] Per SCE, in 2011, the $12, 086,298 represented committed loans; in 2012, the $25,049,135 represented funds available for new loans.

realize long-term energy savings. Property owners and managers of existing residential multi-family complexes with two or more dwellings may qualify.

SCE MFEER's operating budget for 2012 was $19.4 million. SCE's 2012 total MFEER expenditures were $8.0 million. A detailed summary of SCE's 2012 MFEER expenses and list of rebates paid are shown in the following tables.

Table B-8
2012 MFEER Program Expenditures

Expenditure Type	Labor	Non-Labor	Rebates/ Incentives	Allocated Overheads	Total
Admin-IOU	$ 28,393	$ 2,548		$450,489	$ 481,430
Marketing/Outreach		27,041		19,587	46,628
Direct Implementation	399,870	67,806	$6,867,679	125,348	7,460,703
Total Expenditures	**$428,263**	**$97,395**	**$6,867,679**	**$595,424**	**$7,988,761**

In 2011, SCE's total MFEER expenditures were about $5.1 million as shown in the following table:

Table B-9
2011 MFEER Program Expenditures

Expenditure Type	Labor	Non-Labor	Rebates/ Incentives	Allocated Overheads	Total
Admin-IOU	$ 21,989	$ 11,179		$505,946	$ 538,168
Marketing/Outreach		52,580		18,533	71,113
Direct Implementation	391,711	459,318	$3,497,721	122,390	4,471,140
Total Expenditures	**$307,095**	**$879,932**	**$3,497,721**	**$646,869**	**$5,081,364**

Table B-10
Summary of 2011 - 2012 MFEER Rebate Payments

Measure	2011 Incentive	2012 Incentive
Clothes Washer	$ 0	$ 200.00
Electric Water Heater	780.00	810.00
ES Ceiling Fan w/CFL	0	4,360.00
ES CFL Reflector Lamps	62,697.74	65,867.00
ES Exterior Hardwired Fixtures	718,836.28	915,852.00
ES Interior Hardwired Fixtures	1,752,893.03	3,038,531.00
ES Room Air Conditioner	2,050.00	650.00
Exit Sign LED	28,628.00	17,836.00
LED Pool Light	0	6,450.00
Occupancy Sensor	335,265.00	718,809.00
Photocell	0	50.00
Refrigerator	22,500.00	15,650.00
T-8 Linear Fluorescent Fixtures	550,148.46	2,076,331.00
High Performance Dual-Pane Windows	25,102.17	6,283.00
Total 2012 MFEER Rebate	**$3,498,900.68**	**$6,867,679.00**

B.7 Fund Shifting

In Decision (D.) 09-09-47, Ordering Paragraph (OP) 43(b), utilities are required to file an Advice Letter for shifts of funds of more than 15% per annum within and between any of the twelve statewide energy efficiency programs, third-party programs, or governmental programs for the entire portfolio cycle. The twelve state programs are identified on pp.104 and 105 of D.09-09-047 as: 1) Residential, 2) Commercial, 3) Industrial, 4) Agricultural, 5) New Construction, 6)Lighting Market Transformation, 7) Heating, Ventilation and Air Conditioning (HVAC), 8) Codes and Standards (C&S), 9) Emerging Technologies (ET), 10) Workforce Education and Training, 11) Marketing Education and Outreach (ME&O), and 12) Demand Side Management Coordination and Integration (IDSM). Also, in Rulemaking (R.) 09-11-014-*"Assigned Commissioner's Ruling Clarifying Fund Shifting Rules and Reporting Requirements,"* dated December 22, 2011, the Assigned Commissioner states that the utilities shall comply with the energy efficiency fund-shifting rules reflected in Attachment A of the Ruling, which explains in detail the fund shifting requirements.

An exception to the 15% rule is made for fund shifts in categories C&S, ET and ME&O. In Attachment A of R.09-11-014, the utilities are required to file an Advice Letter for fund shifts that would reduce any of the programs by more than 1% of budgeted levels among programs within these categories or among the three categories. Furthermore on page 2, it states that, "*the fund shifting changes adopted in D.09-09-047 are not intended to change Section II, Rule 11 of the Energy Efficiency Policy Manual (version 4) as applied to EM&V and ME&O, [or] to change the fund shifting rules for C&S and Emerging Technologies programs.*"

SCE's 2012 fund shift reports were materially misstated. See Appendix A, Observations 14 to 18.

B.8 EE Balancing Accounts

After reviewing SCE's EE funding proposal filed in its application, the Commission authorized SCE to spend up to $1.19 billion over the 2010 - 2012 period. SCE recovered one-third, or $397.7 million each year from its customers. SCE uses Commission approved balancing accounts to ensure that it recovers its EE expenses up to the authorized amount of $1.19 billion over the three year period. Any "over-collection" will either be refunded to customers or be used to offset future EE funding requirements.

Recovery of the amount of EE program funding that SCE actually spends is a three-step process.

1. Step 1: SCE includes in rates an annual amount of the authorized EE funding.
2. Step 2: Ensure recovery of the authorized EE funding amount each year.
3. Step 3: Record differences between authorized EE funding and the actual.

In 2011, EE funding of $397.67 million was allocated to three individual buckets:

a. Legacy mandated Public Goods Charge (PGC) Energy Efficiency funding of $100.42 million
b. Additional funding entitled Procurement Energy Efficiency funding of $291.92 million
c. On-Bill Financing funding of $5.33 million (the third of the $16 million authorized amount for the 3-year budget cycle)

The Energy Efficiency Program Adjustment Mechanism (Preliminary Statement Part GG) is used to record the difference between the PGC Energy Efficiency funding of $100.42 million and the actual amount of PGC-related EE expenses.

The Procurement Energy Efficiency Balancing Account (Preliminary Statement, Part S) is used to record the difference between the Procurement-related Energy Efficiency funding of $291.92 million and the actual amount of procurement-related EE expenses.

The On-Bill Financing Balancing Account (Preliminary Statement, Part DDD) is used to record the difference between the authorized On-Bill Financing funding of $5.33 million and the actual amount of On-Bill financing loan amounts net of recorded loan repayments.

In 2012 - The legacy Public Good Charge Energy Efficiency funding was eliminated pursuant to statute, and the Procurement Energy Efficiency was increased by an equal amount in order to retain the same total of Energy Efficiency in 2012. In addition, Resolution E-4473 increased the OBF funding from $16 million to $32 million. However, SCE did not take into consideration the additional $16 million increased for its OBF funds and continued to allocate the prior EE funding of $397.67 million to two buckets

1. Procurement Energy Efficiency funding of $392.34 million
2. On-Bill Financing funding of $5.33 million

The Procurement Energy Efficiency Balancing Account (Preliminary Statement, Part S) is used to record the difference between the Procurement-related Energy Efficiency funding of $392.34

million and the actual amount of procurement-related Energy Efficiency expenses. The over-collected balance recorded in the Energy Efficiency Program Adjustment Mechanism associated with the legacy Public Goods Charge Energy Efficiency funding transferred to the Procurement Energy Efficiency Balancing Account.

The On-Bill Financing Balancing Account (Preliminary Statement, Part DDD) is used to record the difference between the authorized On-Bill Financing funding and the actual amount of On-Bill financing loaned amounts net of recorded loan repayments.

B.9 SCE's Internal Audit Reports

SCE provide a copy of its internal audit reports that pertained to the utilities EE program activities for the 2011-2012 audit periods and also provided related management responses thereto.

The internal audit reports provided to the UAFCB included the following:

1. 2011 Energy Efficiency (EE) Programs and Savings Review, dated March 14, 2012.
2. 2011 Energy Efficiency (EE) Programs Balancing Accounts, dated April 25, 2012.
3. 2012 Energy Efficiency (EE) Savings Review, dated February 7, 2013.
4. 2012 Energy Efficiency (EE) Programs Balancing Accounts Review, dated February 12, 2013.

SCE also provided the UAFCB with a status update on management's actions in implementing the findings and recommendations contained in each internal audit reports listed above.

B.10 Follow-Up on Prior UAFCB's Examinations

UAFCB performed a follow-up examination on each finding and recommendation included in its prior reports.[3]

For the audit on SCE's EE for the year ended December 31, 2010 and 2011, there was no additional follow-up required. However, during these examinations, UAFCB recommended, among other things, that SCE should exercise due diligence in reviewing and approving all invoices and ensure that the EE expenditures are accurately classified and properly recorded in its accounting system, and strengthen its internal controls for recording and reporting its EE to prevent future misreporting and misclassifications of SCE's EE.

Judging by the magnitude of the discrepancy found during this examination (see observations 1 through 21 of Appendix A), SCE has not strengthen its internal controls for recording and reporting its EE to prevent future misreporting and misclassification of SCE's EE. In addition, SCE does not appear to be exercising due diligence in reviewing and approving its invoices to ensure that the EE expenditures are accurately classified and properly recorded in its accounting system.

[3] *Interim Financial, Management and Regulatory Compliance Examination of Southern California Edison Company's Energy Efficiency (EE) Programs for the Year Ended December 31, 2010, which was* issued on March 23, 2012. *For the audit of SCE's EE program for program year 2011, UAFCB included its findings and recommendations in a report entitled, Energy Efficiency (EE) Financial Compliance Examination Report of Southern California Edison (SCE) For the Period January through December 31, 2011,* issued on September 30, 2013.