U.S. Department of Energy

Office of Inspector General

Office of Audits and Inspections

AUDIT REPORT

Implementation of Recommendations from the January 2012 Independent Consultant's Review of the Department of Energy Loan and Loan Guarantee Portfolio

DOE/IG-0909

May 2014

Department of Energy
Washington, DC 20585

May 7, 2014

MEMORANDUM FOR THE SECRETARY

FROM: Gregory H. Friedman
Inspector General

SUBJECT: INFORMATION: Audit Report on "Implementation of Recommendations from the January 2012 Independent Consultant's Review of the Department of Energy Loan and Loan Guarantee Portfolio"

BACKGROUND

The Department of Energy's Loan Programs Office (Program) was originally created to accelerate the domestic commercial deployment of innovative and advanced clean energy technologies at a scale sufficient to contribute to the achievement of our national clean energy objectives. The Program executes this mission by guaranteeing loans to eligible clean energy projects and by providing direct loans to eligible manufacturers of advanced technology vehicles and components. As of April 2014, the Program oversaw an approximately $30 billion portfolio of 31 loans and loan guarantees.

In October 2011, the White House Chief of Staff requested an independent review of the Department's loan and loan guarantee programs for alternative energy projects shortly after Solyndra, Inc., a company that had received a loan guarantee from the Department, filed for bankruptcy. Because the requested independent review was to focus on the present and future of the Program, it specifically excluded from its scope evaluation of loans to companies that had recently filed for bankruptcy protection, including Solyndra, Inc. and Beacon Power, LLC. The independent consultant's report, issued in January 2012, identified areas for Program improvement and provided 12 overall recommendations aimed at enhancing the oversight and management of the Program.

We received a complaint alleging that the Program had not fully implemented the consultant's recommendations related to strengthening and restructuring internal oversight. In response, we initiated this audit to determine whether the Department adequately addressed all findings and recommendations from the independent consultant's report.

RESULTS OF AUDIT

The allegations were not substantiated. Overall, we noted that the Department appeared to have taken the consultant's recommendations seriously, and that related actions were generally responsive to the recommendations. Specifically, the Department had completed actions to address 4 of the report's 12 recommendations and initiated actions in response to the remaining 8 recommendations. While the Department had made substantial progress in implementing recommended improvements, we were unable to make a determination as to whether these efforts would ultimately be fully effective to address all of the issues identified by the consultant, because a number of actions, such as clarifying authorities, establishing an external advisory board, and incorporating lessons learned were still ongoing.

Specific Responses to Recommendations

We found that while the Department had not always implemented actions precisely as recommended by the independent consultant, it had considered the specific recommendations and had taken alternative approaches to addressing noted problems. Further, the Department provided its rationale supporting the alternative steps. For example, the Department had created a Risk Management Division, an action supporting the consultant's recommendation to strengthen and restructure internal oversight. However, it had not established a separate reporting structure to senior Department management as suggested by the consultant. Officials indicated that the consultant's suggested reporting structure was considered, but the Department concluded that it would not be effective and that the current reporting structure was comparable to other Federal agencies with similar loan programs.

While actions taken by the Department were generally responsive to recommendations in the consultant's report, our review identified additional opportunities not specified in the consultant's report to enhance management and oversight, and to ensure transparency and accountability. For example, we found that the Program had not finalized changes in policies and procedures necessary to address all of the consultant's recommendations. We also noted that a formal adjudication process for the resolution of professional differences of opinion did not exist. Furthermore, although no negative impact was identified, we concluded that a potential conflict existed regarding membership on the Program's Risk Committee. The Department took corrective action to eliminate the potential conflict of interest after we brought the matter to its attention.

Contributing Factors

Despite generally favorable findings, we noted that the Department had not developed a written and comprehensive action plan for implementing the report's recommendations. Specifically, the Program had not identified specific actions to be implemented, assigned responsibilities for implementation, or developed milestones or goals to track completion. Program officials stated that unlike recommendations made by the Office of Inspector General and the U.S. Government Accountability Office, which are statutorily required to be tracked and implemented, recommendations from independent reviews are not typically tracked, and that no such statutory requirement to implement exists.

Further, we noted that several of the areas for improvement identified by the consultant, such as the need for a comprehensive records management system, a lessons learned process, and adequate staffing, were identified in previous Office of Inspector General reviews. In particular, in our report *The Department of Energy's Loan Guarantee Program for Clean Energy*

Technologies (DOE/IG-0849, March 2011) we found that the Program had not adopted a records management system that imposed structure, consistency and discipline in the development and retention of loan documentation. In addition, we found that the Program had not updated its policies and procedures to include improvements in its loan processing. In March 2013, the Program certified that all actions regarding the adoption of a records management system had been completed; however, action items to address the update of its policies and procedures were still pending at the time of our current review. Finally, the need to ensure sufficient staffing was also identified in our report *Loan Guarantees for Innovative Energy Technologies,* (DOE/IG-0777, September 2007).

<u>Path Forward</u>

With approximately $43 billion in remaining loan and loan guarantee authority and about $30 billion in assets to be monitored, we believe the Department has an opportunity to accelerate the implementation of needed program enhancements and internal controls designed to increase the likelihood of successful Program outcomes. In this context, fully addressing the issues raised by the consultant and other independent organizations should reduce the overall risk to the loan portfolio. Thus, we have made several recommendations aimed at improving the Department's management of the Program.

<u>MANAGEMENT REACTION</u>

Management generally concurred with the report's recommendations and indicated that it would take or had already implemented actions to address them. We consider management's comments responsive to the report's recommendations.

However, management expressed concern that we had understated its progress in implementing the consultant's recommendations. In particular, management stated that, in its view, 6 of the 12 independent consultant's recommendations had been fully implemented. Management stated that, except for memorializing its policies and procedures in writing, it had implemented recommendations related to clarifying authorities and timely reporting of critical information as fully as it intended. We agree that the Department has taken some actions in response to these recommendations. However, until procedures and processes are finalized and implemented, there is no assurance that levels of authority will not be exceeded or management will have the data needed to make informed decisions in a timely manner.

Management's official comments and our responses are summarized in the body of the report. Their official comments are included in Appendix 4. Management also provided additional technical comments, which are addressed in the body of the report.

cc: Deputy Secretary
Chief of Staff
Executive Director, Loan Programs Office

Attachment

AUDIT REPORT ON IMPLEMENTATION OF RECOMMENDATIONS FROM THE JANUARY 2012 INDEPENDENT CONSULTANT'S REVIEW OF THE DEPARTMENT OF ENERGY LOAN AND LOAN GUARANTEE PORTFOLIO

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IMPLEMENTATION OF RECOMMENDATIONS FROM THE JANUARY 2012 INDEPENDENT CONSULTANT'S REVIEW OF THE DEPARTMENT OF ENERGY LOAN AND LOAN GUARANTEE PORTFOLIO

DETAILS OF FINDING

The Department of Energy's (Department) Loan Programs Office (Program) was originally created to accelerate the domestic commercial deployment of innovative and advanced clean energy technologies at a scale sufficient to contribute to the achievement of our national clean energy objectives. The Program executes this mission by guaranteeing loans to eligible clean energy projects and by providing direct loans to eligible manufacturers of advanced technology vehicles and components. As of April 2014, there was approximately $43 billion in remaining direct loan and loan guarantee authority and a portfolio of about $30 billion to be monitored.

In October 2011, the White House Chief of Staff requested an independent review of the Department's loan and loan guarantee programs for alternative energy projects shortly after Solyndra, Inc., a company that had received a loan guarantee from the Department, filed for bankruptcy. The purpose of the review was to report on the status of the portfolio and make recommendations for improvement. In particular, the independent consultant conducting the review was tasked with making recommendations for enhancing the future monitoring, management, and oversight of the loan and loan guarantee programs. In addition, the independent consultant was asked to make recommendations, pertaining to early-warning systems to identify and mitigate potential problems with individual loans or loan guarantees.

The independent consultant's report, released in January 2012, identified a number of areas for improvement. In particular, the report noted that the Department needed to:

- Strengthen and restructure internal oversight of the Program, including creating an independent reporting structure for risk management, revise the functions of the internal committees, and establish an external advisory board;

- Clarify authorities and accountabilities for managers as individuals in the Program, including defining "material" actions and "routine/non-routine" waivers of loan provisions;

- Proactively protect the taxpayers interest and improve reporting to the public;

- Establish and effectively communicate clear goals for portfolio management of the Program, engage in long-range strategic planning, provide long-term funding, and fill key management positions in the Program; and

- Develop an early warning system to identify and mitigate potential concerns in the Program, including a comprehensive management information reporting system and incorporate lessons learned into policies, procedures, reporting, and decision-making.

To address these issues, the independent consultant's report made 12 overall recommendations that included a number of specific actions for implementation aimed at enhancing the oversight and management of the Program.

We noted that several of the areas for improvement, such as the need for a comprehensive records management system, a lessons learned process, and adequate staffing, were identified in previous Office of Inspector General reviews. In particular, in our report *The Department of Energy's Loan Guarantee Program for Clean Energy Technologies* (DOE/IG-0849, March 2011), we found that the Program had not adopted a records management system that imposed structure, consistency and discipline in the development and retention of loan documentation. The report noted that a lack of contemporaneous records could adversely affect the Department's ability to manage loans. In addition, the review found that the Program had not updated its policies and procedures to include improvements in its loan processing to provide for the consistent use of lessons learned. In March 2013, the Program certified that all actions regarding the adoption of a records management system had been completed; however, action items to address the update of its policies and procedures were still pending at the time of our current review. Finally, the need to ensure sufficient staffing was also identified in our report *Loan Guarantees for Innovative Energy Technologies,* (DOE/IG-0777, September 2007).

We received a complaint alleging that the Department had not fully implemented the recommendation related to strengthening and restructuring internal oversight. Given the importance of the Program and the significant amount of funding, we initiated this audit to determine whether the Program adequately addressed all findings and recommendations from the independent consultant's report.

Status of Implementation

We found that the Department had taken actions that were generally responsive to the consultant's recommendations. Specifically, the Department had completed actions to address four of the report's twelve recommendations and initiated actions in response to the remaining eight recommendations. We found, however, that the Department had not always implemented actions as precisely as recommended by the independent consultant. Instead, it considered all specific recommended actions and had, based on supporting rationale, chosen alternative approaches. Finally, our review identified additional opportunities for improving the management and oversight of the Program.

Actions to Address the Independent Consultant's Recommendations

We found that the Department had initiated a number of actions to address the January 2012 independent consultant's recommendations. For example, the Department had filled key management positions such as the Executive Director and Director of Risk Management. In addition, the Program created a detailed Strategic and Operating Plan for its Portfolio Management Division, added upgrades and capabilities to its loan management information system, and adopted a lessons learned process for one of its divisions.

We summarized the status of the Department's implementation of the 12 overall recommendations in Appendix 1, and determined that actions to implement the recommendations were either complete or ongoing for all of the recommendations. Our review found that the Department had completed actions to:

- Provide long-term funding;
- Fill key positions in management with experienced professionals;
- Establish and effectively communicate clear management goals; and
- Engage in long-range strategic planning.

While the Department had initiated a number of actions, we consider its efforts to address the remaining eight recommendations to be ongoing because policies, procedures, and other plans and efforts were not yet complete and in place. Ongoing actions include:

- Clarifying authorities and accountabilities of managers;
- Proactively protecting the taxpayers' interest;
- Improving public reporting;
- Restructuring internal oversight;
- Establishing an external oversight advisory board;
- Creating a comprehensive management information reporting system;
- Establishing a protocol for timely reporting of critical information; and
- Incorporating lessons learned into policies, procedures, reporting, and decision making.

With regard to the complaint, we found that the Department considered each of the recommendations, implemented responsive actions in many cases, and had an explanation as to why other actions were not completed as envisioned in the consultant's report. For example, the Department created a new, separate risk management organization with primary functions as outlined in the consultant's report. Also, the Department hired an experienced risk manager to lead the division. Although certain recommendations such as creating direct reporting authority from the Risk Management Director to the Deputy Secretary had not been implemented, officials indicated that the decision regarding the most effective reporting structure had been given substantial consideration before making a determination that the recommended structure would not be effective and the existing structure would be maintained. Officials also stated that this structure it had in place was comparable to other Federal agencies with similar loan programs. This explanation appeared reasonable given that we contacted two Federal agencies (Small Business Administration and Export-Import Bank) and confirmed that their risk management functions did not have a separate reporting structure. Finally, while the consultant's report recommended abolishing the Program's Risk and Credit Committees once the Risk Management Division was in place, Department officials advised that they continued to utilize these committees to ensure loans were fully vetted and as a system of checks-and-balances.

While we recognize the Department has made substantial progress in addressing the consultant's recommendations, we were unable to make a determination as to whether these efforts will be fully effective to alleviate all the issues identified by the consultant because a number of actions, such as clarifying authorities, establishing an external advisory board, and incorporating lessons learned, were still ongoing.

Management and Oversight

Our review identified additional opportunities for improving the management and oversight of the Program. Specifically, we noted the Department:

- Had not finalized changes in policies and procedures necessary to address the report's recommendations. At the time of our review, almost 2 years after the consultant's report was issued, revisions to the Program's overall policy manual were not yet finalized. Additionally, we reviewed a draft of the Program's revised overall policy manual and determined that the Program had removed many of the detailed procedures. Officials indicated that the detailed procedures would be incorporated into division level policies. However, we noted that a number of division specific procedures were either still in draft or had not yet been developed. In addition, our review of the draft policy also found that some aspects of the loan management process, such as defining what actions are "material," whether waivers of loan provisions were "routine" or "non-routine," and establishment of clear lines of authority remained unclear. The need to define these terms was identified in the independent consultant's report. While the Program has taken several actions as part of its effort to address the recommendation related to clarifying authorities and accountabilities of managers, finalizing division specific policies and procedures and defining certain actions is crucial in implementing the recommendations so that the entire organization understands how materiality of an event is determined, the types of routine and non-routine waivers and the lines of authority. Additionally, the Office of Management and Budget (OMB) revised its policy for Federal credit programs in January 2013 and emphasized the importance of risk management. In particular, OMB stated individuals engaged in risk management should have well-defined roles and clear reporting lines to senior officials that provide for sufficient independence and ability to raise issues that may not have been identified by Program management.

- Had not developed a formal adjudication process for resolving differences of professional opinion between divisions. Given that one of the duties of the Risk Management Division is to perform compliance reviews of other divisions, a well-defined process for resolving professional differences of opinion is essential. During our audit, the Program's Executive Director initiated an internal risk management task force to review functions within the Risk Management Division, an effort which resulted in recommendations to establish an adjudication process.

- Had created a potential conflict-of-interest by appointing the Director of Portfolio Management as a member of the Program's Risk Committee. One of the committee's functions is to evaluate risks associated with individual loans monitored by the Portfolio Management Division and make recommendations for changes in risk evaluations as appropriate. The loans in question are presented to the committee by the Portfolio Management Division. However, the Director of the Portfolio Management Division was a voting member of the Risk Committee and had the authority to accept or decline the committee's recommendations on loans that had been submitted for review by the Director's division. In contrast, the Program's Project Review Committee, which makes recommendations regarding the readiness of a loan to be considered for conditional loan approval, did not include the Director of the Origination Division as a participating voting member, nor did the Director have the authority to accept or decline the committee's recommendations. We concluded that the Risk Committee, as structured at the time of our audit, had not initially allowed for a fully independent evaluation process to occur. To its credit, as a result of our audit, management revised the charter for the Risk Committee and removed the Director of Portfolio Management as a committee member.

Accountability for Implementation

Timely finalization of policies and procedures has been adversely impacted because the Department had not developed a written and comprehensive action plan for implementing the report's recommendations. Specifically, we found that the Program had not identified specific actions to be implemented, assigned responsibilities for implementation, or developed milestones or goals to track completion. Without an action plan, the Department cannot ensure that all actions are fully and timely implemented and that individuals responsible for implementing the actions can be held accountable. However, Program officials stated that they do not typically track recommendations from independent reviews. Nevertheless, in March 2012, the Program, in conjunction with senior Department leadership, identified which recommendations would and would not be implemented. However, neither senior Department leadership nor the Program established an oversight mechanism to adequately track the progress of implementation.

With approximately $43 billion in remaining loan and loan guarantee authority and about $30 billion in assets to be monitored, we believe the Department has an opportunity to implement needed Program enhancements and internal controls designed to increase the likelihood of successful Program outcome. In addition, we believe that, if the Department does not take timely actions to address the issues we identified, the achievement of its goals could be jeopardized. Specifically, without a clear definition of authorities and a path to finalize implementation of the recommendations, the Program cannot ensure accountability and transparency in its operations. Further, by fully addressing the issues raised by the consultant and other independent organizations, overall risk to the loan portfolio, moving forward, should be reduced.

RECOMMENDATIONS

To address the issues identified in our report, we recommend that the Executive Director of the Loan Programs Office take the following actions to improve the management and oversight of the Program:

1. Create an action plan with milestones and planned activities for addressing of the remaining recommendations from the independent consultant's report;

2. Ensure that detailed procedures for activities within the Program and its divisions are developed and implemented. These policies should ensure clarity in authorities for certain transactions, including defining material actions and routine or non-routine requests for waivers of loan provisions; and,

3. Implement a formal adjudication process for resolving differences of professional opinion between divisions.

MANAGEMENT RESPONSE AND AUDITOR COMMENTS

Management generally concurred with the report's recommendations and indicated that it would take or had already implemented actions to address them. Management stated that it had created an action plan with milestones and planned activities to complete the steps required to address the issues raised in the consultant's report. In addition, management stated it was in the process of finalizing detailed procedures for activities within the Program. Further, although it does not believe that additional specific guidance on materiality was necessary, management indicated that it can further develop a process for making a determination on materiality to ensure that the results are documented. Finally, management stated that it would evaluate whether a formal adjudication process was warranted and indicated that it would work to ensure that procedures on documentation requirements evidencing resolution of differing opinions were developed.
We consider management's comments responsive to our recommendations.

Management did not fully agree with several of the report's findings and assertions. In particular, management stated that, in its view, 6 of the 12 independent consultant's recommendations had been fully implemented. Management stated that, except for memorializing its policies and procedures in writing, it had implemented recommendations related to clarifying authorities and timely reporting of critical information as fully as it intended. In addition, management stated that the implementation of the recommendation regarding proactively protecting the taxpayers' interest always would be, by its very nature, ongoing and no additional specific action items would be taken to address this recommendation. We agree that the Department has taken some actions in response to these recommendations. However, until procedures and processes are finalized and implemented, we consider the recommendations ongoing. Without formal, written policies and procedures, the Department cannot ensure that levels of authority will not be exceeded or management will have the data needed to make informed decisions in a timely manner.

Management's official comments are included in Appendix 4. Management also provided technical comments that have been addressed in the body of the report, where appropriate.

STATUS OF IMPLEMENTATION OF RECOMMENDATIONS FROM THE INDEPENDENT CONSULTANT'S REPORT

Recommendations to Improve Monitoring, Management and Oversight

Recommendation	Status	Details
Provide Long-Term Funding for the Programs.	Complete	Loan Programs Office (Program) officials created a detailed FY2015 budget request, and have estimated funding needs through Fiscal Year 2019.
Fill Key Positions in Management with Experienced Professionals.	Complete	Key positions, including Executive Director and Director of Risk Management have been filled.
Clarify Authorities and Accountabilities of Managers.	Ongoing	The Program has taken several actions to clarify authorities, however, some efforts such as creating division-specific policies and procedures still need to be completed for full implementation of the recommendation.
Establish and Effectively Communicate Clear Goals for Management.	Complete	The Program has created specific, measurable performance standards for administration of the loan programs. Also, the Program had established delegations of authority, developed position descriptions for managers, and created a Strategic and Operating plan for its Portfolio Management Division.
Proactively Protect the Taxpayers' Interest.	Ongoing	Actions such as developing detailed division policies and procedures to implement the recommendation had been taken, but had not yet been completed. Further, the Program was in the process of implementing a lessons learned process.
Engage in Long-Range Strategic Planning for the Programs.	Complete	The Program had created a 3-year Strategic and Operating Plan for its Portfolio Management Division which included strategic goals for activities such as human capital management that extended beyond three years, and called for future evaluations based on changes in the Program's mission.

Improve public reporting.	Ongoing	The Program had made revisions to its website, but was still in the process of completing some public reports.
Strengthen and Restructure Internal Oversight of the Programs.	Ongoing	Internal oversight was not completely implemented as prescribed in the report; however, most aspects of the risk management group were established in accordance with the report. Additionally, the Program was in the process of evaluating and implementing recommendations from a self-initiated risk task force.
Establish external oversight.	Ongoing	The Program was in the process of implementing an external advisory board.

Recommendations for Early Warning Systems

Recommendation	Status	Details
Create a Comprehensive Management Information Reporting System.	Ongoing	The Program made improvements to the functionality and capability of its existing reporting system, and was finishing phase 2 of a four-phase plan.
Establish a Protocol for Timely Reporting of Critical Information.	Ongoing	The Program was working to improve timely reporting through both its reporting system and enhanced policies and procedures.
Incorporate Lessons Learned Into Policies, Procedures, Reporting, and Decision-Making.	Ongoing	The Program had initiated a lessons learned process for one of its divisions, and was in the process of completing policies and procedures for the remainder of the Program.

OBJECTIVE, SCOPE AND METHODOLOGY

Objective

To determine whether the Department of Energy's (Department) Loan Programs Office (Program) adequately addressed all findings and recommendations from the independent consultant's report.

Scope

We conducted the audit from June 2013 to April 2014, at Department Headquarters in Washington, DC. The audit was conducted under the Office of Inspector General Project Number A13PT044.

Methodology

To accomplish the audit objective, we:

- Reviewed and summarized findings from the *Report of the Independent Consultant's Review with Respect to the Department of Energy Loan and Loan Guarantee Portfolio* (January 31, 2012);
- Reviewed applicable Federal and Departmental regulations related to the Program;
- Reviewed Program policies, procedures, planning documents, and other documents related to the implementation of recommendations from the independent report;
- Interviewed Program officials to determine actions taken in response to the report; and,
- Assessed the status of implementation of each recommendation from the independent report.

We conducted this performance audit in accordance with generally accepted Government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Accordingly, we assessed internal controls and compliance with laws and regulations to the extent necessary to satisfy the audit objective. We assessed performance measures in accordance with the *GPRA Modernization Act of 2010* and concluded that the Department had established performance measures related to the Loan Guarantee Program. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. Finally, we did not rely on computer-processed data to achieve our audit objective and, therefore, did not conduct a full reliability assessment of computer-processed data.

An exit conference was held with the Department's Loan Programs officials on May 5, 2014.

PRIOR REPORTS

- Audit Report on *The Department of Energy's Loan Guarantee to Abound Solar Manufacturing, LLC*, (DOE/IG-0907, April 2014). This audit identified several weaknesses in the Department of Energy's administration of the loan guarantee to Abound Solar Manufacturing, LLC. Specifically, the audit found that the Loan Guarantee Program had not consulted with the Credit Review Board concerning a material change in the credit subsidy subsequent to its recommendation to approve the loan. In addition, the report found that the Loan Guarantee Program had not resolved the conflicting opinions of its advisors regarding the company's ability to overcome technical issues or adequately documented the assumptions in the financial modeling used to support loan approval and monitoring. Further, the report noted that ongoing, formal financial and industrial analyses had not been conducted as part of monitoring activities for the loan.

- Audit Report on *Special Report: Inquiry into the Procurement of Law Firm Services and Management of Law Firm-Disclosed Organizational Conflicts of Interest by the Department of Energy's Loan Programs Office*, (OAS-RA-12-14, August 2012). This audit identified opportunities to improve transparency over the Loan Programs Office's management of organizational conflict of interest waiver requests. Specifically, the review noted that the Loan Programs Office had not deployed a tracking system for managing law firm waiver requests and had not documented, in an organized system of records, the rationale for denying or approving waiver requests.

- Audit Report on *The Department of Energy's Loan Guarantee Program for Clean Energy Technologies*, (DOE/IG-0849, March 2011). This audit revealed that the Loan Guarantee Program could not always demonstrate, through systematically organized records, how it resolved or mitigated relevant risks prior to granting loan guarantees. Decision documents summarizing the process did not always describe the actions taken by officials to address, mitigate and/or resolve risks. In addition, loan origination files were not maintained in the Loan Guarantee Program's official electronic information repository, which according to Federal regulations was to contain key documentation to support actions as part of the loan guarantee process. The report noted that the Loan Guarantee Program had not adopted a records management system that imposed structure, consistency and discipline in the development and retention of loan documentation.

- Audit Report on *The Department of Energy's Loan Guarantee Program for Innovative Energy Technologies*, (DOE/IG-0812, February 2009). This report found that while the Loan Guarantee Program had developed and implemented some key programmatic safeguards, it had not completed a control structure necessary to award loan guarantees and to monitor associated projects. Specifically, the review found that the Loan Guarantee Program had not finalized policies and procedures, formally documented portions of its applicant reviews, and formalized procedures for disbursing loan proceeds.

- Audit Report on *Loan Guarantees for Innovative Energy Technologies*, (DOE/IG-0777, September 2007). This report concluded that there were a number of steps that should have been taken to foster the success of the Loan Guarantee Program. These included finalizing a staffing plan, developing risk mitigation strategies, implementing and executing a monitoring system, and promulgating liquidation procedures.

MANAGEMENT COMMENTS

Department of Energy
Washington, DC 20585

April 8, 2014

MEMORANDUM FOR: Rickey R. Hass
Deputy Inspector General for Audits and Inspections
Office of Inspector General

FROM: fa Peter W. Davidson
Executive Director, Loan Programs Office

SUBJECT: Office of Inspector General (OIG) Draft Audit Report on the Implementation of Recommendations from the January 2012 Independent Consultant's Review of DOE's Loan and Loan Guarantee Portfolio

Thank you for the opportunity to comment on the OIG's Draft Audit Report (the Draft Audit Report) regarding the implementation of recommendations from the Independent Consultant's (the Consultant) review of DOE's loan and loan guarantee portfolio (the Consultant's Recommendations). As the Draft Audit Report notes, the Department of Energy (DOE) has taken the Consultant's Recommendations seriously and undertook actions that are responsive to these recommendations.

Additional Draft Audit Report Recommendations
As discussed in the OIG report, the Draft Audit Report, the OIG is making certain recommendations that are not among the 12 Consultant's Recommendations. Those additional recommendations include:

- A formal adjudication process for the resolution of professional differences of opinion; and
- Defining material actions and routine or non-routine requests for waivers of loan provisions. With respect to this recommendation, the Consultant's report noted that LPO's Portfolio Division made the determination of whether a credit action or development is material. It did not recommend that DOE further define the terms.

Status of Implementation of the Consultant's Recommendations
It is LPO's view that 6 of the 12 recommendations have been fully implemented, and that the implementation of one of the recommendations always will be, by its very nature, ongoing.

Clarifying Authorities. The Consultant's Recommendation regarding clarifying authorities of managers as individuals was to eliminate the Credit Committee (now named the Project Review Committee) and the Risk Committee (now named the Risk and Portfolio Management Committee) because of the belief that "collective responsibility can obscure individual accountability".

DOE has made a decision not to implement this recommendation because it determined that the committees were important to the functioning of LPO and to the careful review of projects and the portfolio during origination and monitoring.

With respect to the OIG's more general point of concern regarding the authorities and accountabilities of managers, those authorities and accountabilities are made clear by the following documents:

- re-delegations of authority to division directors, which addresses authorities;
- organizational chart of LPO's senior leadership, which addresses accountability; and
- position descriptions of each of the managers, which also addresses authorities.

Accordingly, except for memorializing these authorities and authorizations in written policies and procedures, this recommendation has been implemented as fully as DOE intends.

Timely Reporting of Critical Information. LPO believes that, except for memorializing its procedures and processes in writing, the reports that LPO currently provides and will begin providing shortly implement the recommendation regarding establishing a protocol for timely reporting of critical information as fully as DOE intends.

Proactively Protect Taxpayers' Interests. One of the Consultant's Recommendations is to proactively protect the taxpayers' interest. The OIG report notes that this recommendation is ongoing. LPO agrees that it is ongoing and its implementation will, by its nature, be a continuous process. However, there are not additional specific action items that DOE intends for LPO to take to address this recommendation.

<u>OIG Recommendations</u>
LPO generally agrees with the OIG's recommendations. However, as discussed in this management response, LPO does not fully agree with some of the findings and assertions made in the OIG's Draft Audit Report.

Recommendation 1: *Create an action plan with milestones and planned activities for addressing the remaining recommendations from the independent consultant's report.*

Concur. LPO has created an action plan with milestones and planned activities to complete the steps required to address the issues raised in the Consultant's report. However, as noted in the Draft Audit Report, DOE does not intend to implement all of the Consultant's Recommendations and has taken alternative approaches in some instances.

Recommendation 2: *Ensure that detailed procedures for activities within LPO and its divisions are developed and implemented. These procedures should ensure clarity in authorities for certain transactions, including defining material actions and routine or non-routine requests for waivers of loan provisions.*

Concur with comment. LPO is in the process of finalizing detailed procedures for activities within LPO and appropriate divisions. Generally the judgment of whether any event, condition or occurrence has or could be materially adverse to the business, operations, condition (financial or otherwise), assets, liabilities or properties of a project is determined on a case-by-case basis; it is not an objective metric that can be easily quantified. While LPO does not believe that additional specific guidance on materiality is necessary, LPO believes that it can further develop the process for making a determination on materiality to ensure that the results are documented. LPO believes that clarity in authorities for transactions already exists. LPO also notes that the Consultant's report did not recommend that DOE further define those terms in its policies and procedures.

Recommendation 3: *Implement a formal adjudication process for resolving differences of professional opinion between divisions.*

Concur with comment. LPO notes that most issues can be resolved through routine discourse and processes. A formal process should not be used as the first step to resolve differences or as a way around those processes. Program employees use customary processes, including discussions with management and a review and comment process as part of its routine work practice. LPO will evaluate whether a formal process is warranted, but agrees that it will work to ensure that procedures on documentation requirements evidencing resolution of differing opinions are developed.

In closing, LPO remains committed to continually improve program operations. DOE will continue to be an active manager, continuously monitoring projects, their market environments, and other identified risks to seize all opportunities to minimize exposure to loss and protect taxpayer interests.

FEEDBACK

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