



Denali Commission
Office of Inspector General
Anchorage, AK 99501

January 7, 2016

Ms. Sara Fisher-Goad
Executive Director
Alaska Energy Authority
813 W. Northern Lights Boulevard
Anchorage, AK 99503

Dear Ms. Fisher-Goad,

Enclosed is the Denali Commission Office of Inspector General's final audit report, number DCOIG-16-003-A, concerning Denali Commission Grant No. 1199.

This letter is notice of your opportunity and responsibility to review the report and to develop a complete response. If you believe that the report is in error in any respect or if you disagree with any of the findings and recommendations, it is important that you explain the error or your reasons for disagreement and submit evidence that supports your position to us. You should also explain how each documentary submission supports the position you are taking; otherwise, we may be unable to evaluate the information.

Your response must be postmarked no later than 30 days from the date of this letter. There will be no extensions to this deadline, and you will have no other opportunity to submit comments, arguments, or documentation before the Denali Commission makes a decision on the audit findings and recommendations. The Denali Commission will consider your complete response in determining what action to take with respect to our audit. Enclosure 1 explains administrative dispute procedures available to you.

As you prepare your response, if you have any questions about this report or the process by which the Denali Commission reaches a final decision, please call me and reference final audit report number DCOIG-16-003-A. Please send your response (including any documentary evidence) to:

Joel Neimeyer, Federal Co-Chair
Denali Commission
510 L Street, Suite 410
Anchorage, AK 99501

Please send a copy of your response to:

David Sheppard, Inspector General
Denali Commission Office of Inspector General
510 L Street, Suite 410
Anchorage, AK 99501

After evaluation of your response, Commission officials may provide you with further guidance or request clarification. This final report will be posted on OIG's website pursuant to section 8M of the Inspector General Act of 1978, as amended.

Sincerely,

A handwritten signature in blue ink, appearing to read "David Sheppard", with a long horizontal flourish extending to the right.

David Sheppard
Inspector General

cc: Joel Neimeyer, Federal Co-Chair, Denali Commission
David Smith, Acting Inspector General, U.S. Department of Commerce

NOTICE TO AUDITEE
Financial Assistance Audits

1. Audit requirements applicable to a particular financial assistance award may be established by law, regulation, policy, or the terms of the recipient's financial assistance agreement with the Denali Commission.
2. The results of any audit will be reported to the Denali Commission and to the recipient/auditee, unless the Inspector General of the Denali Commission determines that it is in the government's interest to withhold release of the audit report.
3. The results of an audit may lead to adverse consequences for the auditee, including but not limited to any of the following actions (which are subject to applicable laws and regulations):
 - Suspension and/or termination of current awards;
 - Referral of identified problems to other federal funding agencies and entities as deemed necessary for remedial action;
 - Denial of eligibility for future awards;
 - Canceling the authorization for advance payment and substituting reimbursement;
 - Establishment of special conditions in current or future awards; and/or
 - Disallowance of costs, which could result in a reduction in the amount of federal payments, the withholding of payments, the offsetting of amounts due the government against amounts due the auditee, or the establishment of a debt and appropriate debt collection follow-up (including referrals to collection agencies).

Because of these and other possible consequences, an auditee should take seriously its responsibility to respond to audit findings and recommendations with explanations and evidence whenever audit results are disputed.

4. To ensure that audit reports are accurate and reliable, an auditee may have the following opportunities to point out errors (of fact or law) that the auditee believes were made in the audit, to explain other disagreements with audit findings and recommendations, to present evidence that supports the auditee's positions, and to dispute final recommendations:
 - *During the audit*, the auditee may bring to the attention of the auditors at any time evidence that the auditee believes affects the auditors' work.

- *At the completion of the audit on-site*, as a matter of courtesy, the auditee is given the opportunity to have an exit conference to discuss the preliminary audit findings and to present a clear statement of the auditee's position on the significant preliminary findings, including possible cost disallowances.
- *Upon issuance of the draft audit report*, the auditee may be given the opportunity to comment and submit evidence during the 30-day period after the transmittal of the report. (There are no extensions to this deadline.)
- *Upon issuance of the final audit report*, the auditee is given the opportunity to comment and to present evidence during the 30-day period after the transmittal of the report. (There are no extensions to this deadline.)
- *Upon issuance of the Commission's decision (the "Audit Resolution Determination")* on the audit report's findings and recommendations, the auditee has the right to appeal for reconsideration within 30 calendar days after receipt of the determination letter if monies are due to the government. (There are no extensions to this deadline.) The determination letter will explain the specific appeal procedures to be followed.
- *After an appeal is filed*, or after the opportunity for an appeal has expired, the Commission will not accept any further submissions of evidence concerning an auditee's dispute of the Commission's decisions on the resolution of the financial assistance audit. If it is determined that the auditee owes money or property to the Commission, the Commission will take appropriate collection action, but will not thereafter consider the merits of the debts.
- *There are no other administrative appeals available.*

DENALI COMMISSION

Denali Commission Ruby Rural Power System Upgrade Grant



FINAL REPORT

January 7, 2015

DCOIG-16-003-A

DENALI COMMISSION
OFFICE OF INSPECTOR GENERAL

Contents

Introduction 1

Objectives, Findings, and Recommendations 2

 Questioned costs total \$1,040 2

 The method of construction was reasonable 2

 The Rural Power System Upgrade is working and delivered as intended 3

 Recommendations 3

 Summary of Agency Response and OIG Comments 4

Appendix A: Objectives, Scope, and Methodology 5

Appendix B: Summary of Source and Application of Funds 7

Appendix C: Agency Response 8

Introduction

The Denali Commission has made energy its primary infrastructure theme since 1999 because of the critical role energy plays in the quality of life and economic development of Alaska's communities. The Commission's Energy Program funds the design and construction of replacement bulk fuel storage facilities, upgrades to community power generation and distribution systems, energy efficiency measures, and alternative energy projects. One of the Commission's major program partners on rural fuel storage and power generation needs is the Alaska Energy Authority (AEA).

AEA is an independent corporation of the state of Alaska's Department of Commerce, Community, and Economic Development. With the mission to reduce the cost of energy in Alaska, AEA is the state's energy office and lead agency for statewide energy policy and program development. AEA emphasizes community-based project management by using a combination of contractors and local residents for the construction of projects such as modern and code-compliant bulk fuel tank farms, upgrading to high-efficiency generators in rural power systems, or integrating renewable energy projects. AEA's core programs work to diversify Alaska's energy portfolio, lead energy planning and policy, invest in Alaska's energy infrastructure, and provide rural Alaska with technical and community assistance.

In September 2009, the Denali Commission awarded a grant of \$2,800,000 to AEA to upgrade the rural power system in Ruby, Alaska. In July 2010, the award was amended to reduce the funding by \$128,175, for a final award amount of \$2,671,825. Ruby, Alaska, is an Athabascan village of approximately 160 residents and 103 homes. The village is situated in the Kilbuck-Kuskokwim Mountains along the Yukon River and is accessible only by airplane, boat in the summer, and snowmobile in the winter. Ruby is on the western border of the Nowitna National Wildlife Refuge and is one of two villages that serve as a staging point for expeditions into the 1.56 million-acre preserve.

The Ruby rural power system upgrade included construction of a new power plant and heat recovery equipment, as well as upgrades to the existing power distribution system. The grant's original period of performance was September 2009 through March 2012, but was later amended to extend through September 2014.

Objectives, Findings, and Recommendations

The objectives of the audit were to determine whether (1) costs incurred under the award were allowable, allocable, and reasonable; (2) the method chosen for obtaining construction services was effective and efficient; and (3) the power system is working and delivered as intended.

Questioned costs total \$1,040

We found that 1 of 64 sampled expenditure transactions, valued at \$1,040,¹ was not allowable under federal costs principles.² We sampled 64 of the 1,292 total expenditure transactions incurred on the grant and traced the transactions to supporting documentation, such as invoices, timesheets, labor rates, and procurement documentation. We reviewed the transactions to determine whether they were allowable and authorized under federal cost principles, allocable and incurred specifically for the award, and reasonable in terms of amount and necessity. The unallowable transaction was for promotional water bottles purchased to give out at a summit with native community leaders; however, Federal cost principles prohibit the purchase of promotional items and memorabilia for the purposes of advertising or public relations. AEA staff stated that this type of purchase would typically come out of their own operating budget and that it was incorrectly purchased with federal grant funds, resulting in \$1,040 in questioned costs.

The method of construction was reasonable

Although we did not determine whether a fully contracted method of construction, or another alternative, would be more cost effective, we found AEA's current method of construction to be reasonable and therefore did not make any recommendations to improve the construction services. We reviewed the performance of the grant, involvement of AEA staff and Ruby residents, and competitive procurement of materials and services. In addition, we interviewed both AEA staff and city of Ruby officials involved with the grant to determine the benefits of the chosen method of construction. AEA used a combination of AEA-managed construction and force-account labor. AEA-managed construction includes the purchase or competitive procurement of supplies and services in accordance with federal procurement standards, as well as AEA employee labor. Force-account labor includes labor costs for hiring Ruby residents to participate in the construction of the power plant. To perform the grant, AEA managed the construction and contracted out some aspects of the grant, such as construction of the modular building. In addition to contracting, they also hired Ruby residents to assist in the construction of the modular building and to work on the ground in Ruby. According to AEA, there are numerous

¹ The results of the sample were extrapolated to the population of untested transactions. Based on testing, we are 90 percent confident that the compliance rate for the entire population is 98.3051 percent with a margin of error of 2.783 percent. As a practice, OIG uses the most conservative end of the margin of error for assessing the dollar value of potential additional unallowable transactions. Since the margin of error indicates that there may be no additional unallowable transactions, we question costs totaling \$1,040, the amount identified through testing.

² Office of Management and Budget Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, Attachment B, 1.f.3 prohibits the purchase of promotional items and memorabilia, including models, gifts, and souvenirs, for the purposes of advertising or public relations, and 1.f.4 prohibits the cost of advertising and public relations designed solely to promote the governmental unit.

benefits to the current construction method, including increased community involvement and ownership of the power plant as well as increased project flexibility. AEA staff stated that they are currently undergoing a cost-benefit analysis to determine whether a fully contracted method would be more effective and efficient. We look forward to reviewing the results of that analysis.

The Rural Power System Upgrade is working and delivered as intended

We found that the power system is working and delivered as intended in accordance with the performance objectives identified in the grant.³ We traveled to Ruby, Alaska, to view the power plant and interview the power plant operator and city of Ruby personnel in order to determine whether the power system is working and delivered as intended. The city clerk of Ruby stated that the community is happy with the results of the grant and the reliability of the new power system. In addition to power generation, the excess heat from the operation of the power plant is now routed to the washeteria,⁴ clinic, and public safety buildings in order to heat those facilities independently. From October 2010 through May 2014, the City spent approximately \$40,000 on oil and delivery charges to heat those facilities, but because of the new heat recovery equipment, the city has not had to purchase oil for those facilities since May 2014.

According to AEA and the power plant operator, AEA funded, outside of the Commission grant and through the Alaska Vocational Technical Center (AVTEC) in Seward, Alaska, training for a power plant operator to learn to operate and maintain the facility. AEA also has two field technicians on staff to assist operators in the villages with operations and maintenance questions. When additional assistance is needed, AEA has a “circuit rider” program for Alaska state technicians to travel to the villages when necessary. As a result of AEA’s performance of the grant, the city of Ruby has an improved working power plant and a resource for assistance with operation and maintenance of the facility.

Recommendation

We recommend that the Commission:

1. Disallow and recover \$1,040 in unallowable costs.

³ Per the grant, “The project will upgrade the electrical power generation and distribution systems in the community of Ruby, Alaska. The project scope included construction of a gravel pad and elevated post and pad foundation; a new 15-foot x 40-foot modularized power plant with generators, switchgear, and heat recovery equipment; electrical distribution system upgrades including new step-up transformers at the power plant, sectionalizing equipment, overhead primary and secondary conductors, and service connections; and installation of piping to the existing washeteria and installation of a heat exchanger and controls in the washeteria mechanical room to utilize recovered heat.”

⁴ The city does not have in-home piped water or sewage. The washeteria is the only structure providing public access to laundry, showers, and flush toilets.

Summary of Agency Response and OIG Comments

The OIG received AEA's response to the draft report, which we included as Appendix C of this final report. AEA concurs with all findings and the recommendation in this report and stated they are taking corrective action to reimburse the Denali Commission for the questioned costs totaling \$1,040.

Appendix A: Objectives, Scope, and Methodology

Our objectives were to determine whether (1) costs incurred under the award were allowable, allocable, and reasonable; (2) the method chosen for obtaining construction services was effective and efficient; and (3) the power system was working and delivered as intended. We conducted our fieldwork from July 2015 to September 2015 in Anchorage and Ruby, Alaska.

To accomplish our audit objectives, we did the following:

- Interviewed Denali Commission officials, AEA personnel, and city of Ruby, Alaska, personnel to gain an understanding of the Ruby Rural Power System Upgrade as well as personnel qualifications and training;
- Obtained an understanding of documentation, supervisory, and procedural internal controls over accounting and finance transactions, procurement, property management, records retention, and information systems;
- Reviewed the rules and regulations applicable to the audit objectives, including Denali Commission Grants Management Guidelines, and Office of Management and Budget (OMB) Circulars A-87, *Cost Principles for State, Local, and Indian Tribal Governments*; A-133, *Audits of States, Local Governments, and Non-Profit Organizations*; and A-102, *Grants and Cooperative Agreements with State and Local Government*;
- Analyzed a list of all grant general ledger transactions;
- Stratified AEA's general ledger expenditure data by cost category for a total of six strata. To reach a minimum confidence level of 90 percent and a 5 percent or smaller margin of error, we sampled 59 of 1,296 transactions for review. In addition, we judgmentally selected one transaction from each cost category for initial review. We compared these 64 transactions (1 transaction was part of both the statistical sample and the judgmental sample) to their supporting documentation to determine whether costs were supported, reasonable based on dollar amount and purpose, and allowable under federal cost principles. The results of the sample were estimated for the entire population at a 95 percent confidence level. The total questioned costs in the report fall within the margin of error and are the actual amount determined to be unallowable;
- Reviewed transactions to determine whether the generators were purchased in accordance with AEA policies and federal procurement standards and whether the purchases were allowable, allocable, and reasonable;
- Reviewed the grant files and interviewed AEA and Ruby personnel to determine the method of construction and the basis for selecting that method; and,
- Reviewed the grant's purpose and performance objectives as stated in the grant files. We compared the performance objectives with the current status to determine whether the power system was delivered as intended.

We did not solely rely on computer-generated data for our review. Instead, we established data reliability by reviewing the electronic records for obvious errors and omissions, interviewing AEA officials who were knowledgeable about the records, and directly comparing the electronic general ledger records to supporting documentation. Based on this review, we determined the data were sufficiently reliable to support our audit conclusions.

We did not identify deficiencies in internal controls that are significant within the context of the audit objectives. A deficiency in internal controls that was not significant within the context of the audit objectives was identified and communicated to AEA management. We did not identify any instances of fraud, illegal acts, violations of laws, or abuse that have or are likely to have occurred.

We performed this audit under the authority of the Inspector General Act of 1978, as amended. We conducted this 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 that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix B: Summary of Source and Application of Funds

**Alaska Energy Authority
Final Audit of Grant No. 1199
September 1, 2009 through March 15, 2015**

| | Approved Award Budget ^a | Incurred by Recipient |
|-----------------------------|---------------------------------------|--------------------------|
| Source of Funds | | |
| Federal Share | \$2,671,825 | \$2,671,825 |
| Recipient Share | - | - |
| Total | \$2,671,825 | \$2,671,825 |
| | | |
| Application of Funds | | |
| Personnel | | 279,414 |
| Travel | | 906,569 |
| Supplies | | 1,014,974 |
| Administrative Costs | | 388,716 |
| Other | | 82,152 |
| Total | \$2,671,825 | \$2,671,825 |

Source: OIG based on AEA data.

^a Denali Commission did not require AEA to submit a line-item budget.

Appendix C: Agency Response



December 16, 2015

David Sheppard, Inspector General
Denali Commission Office of Inspector General
510 L Street, Suite 410
Anchorage, AK 99501

Re: Response to draft audit report concerning Denali Commission Grant No. 1199

Dear Mr. Sheppard:

We have reviewed the Denali Commission's draft report of the Ruby Rural Power System Upgrade grant and concur with the finding and recommendation. Specifically, we concur that the purchase of promotional supplies for the community event should not have been made with federal dollars and we understand that the purchase is not allowed under federal cost principles. The Alaska Energy Authority is taking corrective action to reimburse the Denali Commission for the questioned costs totaling \$1,040. This specific purchase, in our opinion, was an error and an isolated instance.

We thank you for the opportunity to work with you and your staff in the performance of the audit of the Ruby project.

Sincerely,

A handwritten signature in purple ink that reads "Sara Fisher-Goad".

Sara Fisher-Goad
Executive Director

cc: Joel Neimeyer, Federal Co-Chair, Denali Commission

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