SJOBERG EVASHENK
CONSULTING, INC

January 14, 2021

Angie Williams
Director Utility Audits, Risk and Compliance Division (UARCD)
California Public Utilities Commission
400 R Street, Suite 221
Sacramento, CA 95811

Dear Ms. Angie Williams:

Enclosed is the audit report, *Performance Audit of the Electric Program Investment Charge (EPIC) Program*. The report was prepared on behalf of the California Public Utilities (CPUC) Commission by Sjoberg Evashenk Consulting and includes our analysis and recommendations. The draft report was discussed with CPUC and four administrators—California Energy Commission, Pacific Gas & Electric Company, San Diego Gas & Electric Company, and Southern California Edison—prior to completion of our audit fieldwork. Management comments received throughout the audit process were considered in drafting the report.

Sjoberg Evashenk Consulting was pleased to work with the CPUC and four EPIC administrators on this important project.

Respectfully submitted,

Lynda McCallum

Lynda McCallum
Partner
Sjoberg Evashenk Consulting, Inc.

455 CAPITOL MALL, SUITE 700 · SACRAMENTO, CALIFORNIA 95814 · (916) 443-1300 · FAX (916) 443-1350 · WWW.SECTEAM.COM

California Public Utilities Commission

Performance Audit of the Electric Program Investment Charge (EPIC) Program

January 14, 2021

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455 Capitol Mall • Suite 700 • Sacramento, California • 95814 • Tel 916.443.1300 • www.secteam.com

Table of Contents

Executive Summary

Sjoberg Evashenk Consulting, working on behalf of the California Public Utilities Commission (CPUC), completed a performance audit of the Electric Program Investment Charge (EPIC).

Key Findings

Overall, the audit found that CPUC requirements related to collecting, remitting, and expending EPIC funding were generally followed by the four EPIC administrators—the California Energy Commission (CEC) and three Investor Owned Utilities (IOU).

Specifically, the EPIC program is funded with revenues collected from ratepayers by the three IOUs. The audit found that since the inception of the program in 2012 through the end of December 2019, the collection of revenue appeared consistent with CPUC decisions. However, processes employed by CEC and CPUC to seek their portion of EPIC funding resulted in some over-remittances. Also, while CPUC decisions require the EPIC administrators to return interest earned on EPIC funds back to ratepayers, we found that two of the IOUs did not return the earnings following required timelines and CPUC does not have processes in place to return interest earned on oversight funding.

Further, EPIC funding is used to cover project, administration, and oversight expenses. Although our review of EPIC funded expenses found that formal guidance and criteria detailing the allowability of costs or activities was not available, our testing reflected that costs appeared generally reasonable and supported and the four administrators had processes in place that align with general industry practices to ensure adequate controls over expenditures. However, the audit found that some of CPUC's personnel costs charged to EPIC were not always consistent with the actual time spent by staff performing oversight activities.

Lastly, we found that unspent EPIC funding as of December 31, 2019 appeared generally sufficient to complete remaining active and future projects. However, we noted that while CEC's administration expenses were currently within 10 percent of its overall EPIC budget as mandated, required spending may cause CEC to ultimately exceed its administration budget; at least one IOU voiced similar concerns. We noted a similar observation was made in 2019 by CPUC's Utility Audits, Risk, and Compliance Division.

Key Recommendations

To address the findings, 14 recommendations are offered throughout the report for CPUC to consider, including the following summary of key recommendations:

- Ensuring CEC develops a process to reconcile remittance invoices sent to the three IOUs against approved project expenditures before sending additional invoices.
- Directing the CPUC Fiscal Office to assume the responsibilities of invoicing the IOUs for oversight remittances.
- Ensuring the two IOUs to return the remaining interest earned between 2012 and 2017 back to ratepayers.
- Developing processes to return interest earned on CPUC's EPIC oversight funds back to ratepayers.
- Collaborating with the four EPIC administrators to develop cost guidance related to the allowable use of EPIC funding. Guidelines should provide sufficient flexibility given differences in the types of projects undertaken by the administrators while providing adequate parameters reflecting the acceptable use of funding.

Background

In 2011, the California Public Utilities Commission (CPUC) established the ratepayer-funded Electric Program Investment Charge (EPIC) program to develop new, emerging, and pre-commercialized clean energy technologies in California. According to CPUC, EPIC projects must be designed to produce electricity ratepayer benefits in the form of increased reliability, improved safety, and/or reduced electricity costs. EPIC consists of three program areas shown in Exhibit 1.

EXHIBIT 1. DESCRIPTION OF EPIC PROGRAM AREAS

Program Area	Description
Applied Research and Development (Applied R&D)	Applied energy science and technology that provides public benefit, but for which there is no current deployment of private capital.
Technology Demonstration and Deployment (TD&D)	Technology demonstrations at real-world scales and in real-world conditions to showcase emerging innovations and increase technology commercialization.
Market Facilitation	Market research, regulatory permitting and streamlining, and workforce development activities to address non-price barriers to clean technology adoption.

CPUC Decision 11-12-035 requires the State's three largest electrical Investor Owned Utilities (IOU)—Pacific Gas and Electric Company (PG&E), San Diego Gas & Electric Company (SDG&E), and Southern California Edison Company (SCE)— to collect revenues from ratepayers to fund: i) renewables programs, and ii) research, development, and demonstration programs.

The EPIC program is broken into three triennial phases:

- EPIC I—January 1, 2012 through December 31, 2014
- EPIC 2—January 1, 2015 through December 31, 2017
- EPIC 3—January 1, 2018 through December 31, 2020

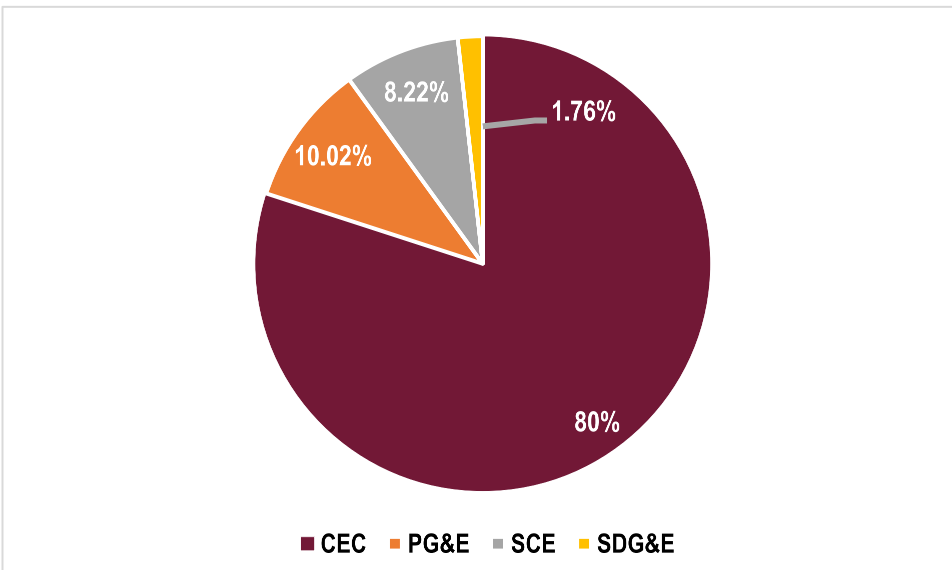
In August 2020, CPUC Decision 20-08-042 authorized two additional five-year investment plan cycles, extending the EPIC program through 2030.

CPUC is responsible for overseeing and monitoring the implementation of the EPIC program. CPUC decisions detail the portion of the $1.5 billion in EPIC funding each IOU must collect from ratepayers during each triennial period of the program, as shown in Exhibit 2.

EXHIBIT 2. REQUIRED EPIC COLLECTIONS BY IOU

IOU	EPIC 1[1]	EPIC 2[2]	EPIC 3[3]	Total
PG&E	$233,967,000	$255,401,133	$278,055,000	$767,423,133
SCE	$191,937,000	$209,520,690	$228,105,000	$629,562,690
SDG&E	$41,096,000	$44,860,878	$48,840,000	$134,796,878
Total	**$467,000,000**	**$509,782,700**	**$555,000,000**	**$1,531,782,700**

CPUC decisions direct the California Energy Commission (CEC), the State's primary energy policy and planning agency, to administer the vast majority of EPIC funding (80 percent) and the three IOUs to administer the remaining (20 percent), as shown below:



The three IOUs submit project and administration remittances to the CEC and oversight remittances to CPUC. The EPIC funds held by each administrator earn interest, which must be returned to ratepayers through annual electricity rate-setting processes.

For each EPIC cycle, the CPUC reviews and approves investment plans submitted by the four administrators outlining the projects and initiatives to be executed during the triennial period.

[1] CPUC D.13-11-025.
[2] CPUC D.15-04-020.
[3] CPUC D.18-01-008.

Objectives, Scope, and Methodology

Sjoberg Evashenk Consulting was hired by the California Public Utilities Commission (CPUC) to conduct a performance audit of the Electric Program Investment Charge (EPIC). The objectives were to:

- Review CEC's internal controls over budget processes to determine reasonableness and compliance with applicable decisions, laws and regulations, advice letters, and CEC's policies and procedures.
- Verify whether interest earned is properly tracked and whether administrators accurately and consistently reduce claims for reimbursement by the total interest earned in previous years.
- Determine the amount of administrative, overhead, and project expenses charged on the research projects and verify whether administrative costs are accurately charged.
- Determine funding status and availability for research, development and demonstration (RD&D) costs, administrative, and overhead costs and percentage of completion for the research projects.

The period of our audit is focused on January 1, 2012 through June 30, 2019. Fieldwork was conducted between January 2020 and October 2020; because work was conducted largely remotely due to the 2020 global pandemic, we were unable to spend time with the auditees on-site.

To answer audit questions and objectives, we specifically reviewed and relied upon the following as part of our work during this audit:

- Obtained an understanding of the EPIC program by reviewing relevant laws, rules, regulations, CPUC Decisions, advice letters, and other CPUC filings.
- Reviewed available EPIC audit and evaluation reports to identify potential risk areas related to the scope of this engagement and CPUC's audit workpapers associated with a 2019 internal audit.
- Reviewed financial audits conducted on each of the IOUs between 2016 and 2019 to determine whether internal controls over financial reporting were consistent with accounting principles and to understand the circumstances surrounding any findings noted.
- Conducted interviews with key EPIC staff from CPUC, CEC, PG&E, SDG&E, and SCE to learn about various processes related to program activities, including budgeting, selecting projects, issuing solicitations, reporting program activity, encumbering monies, remittance schedules, oversight responsibilities, and calculating and returning interest.
- Received accounting and financial system data and EPIC balancing sheet information for each of the four administrators and CPUC to determine the amount of EPIC revenue received for oversight activities and administration of the program, including interest activity. Determined if remittances were made in accordance with CPUC requirements.
- Assessed available guidance related to the types of allowable use of EPIC funding.
- Received accounting data for each of the four administrators and selected expenditure transactions to review and testing, to determine if expenditures were reasonable, supported with underlying

documentation, and related to EPIC. Also, performed a high-level review of the four administrators controls over expenditures.

- Requested and reviewed supporting documentation, such as remittance invoices, project-related invoices, contracts, payroll records, rent schedules, timesheets, receipts, travel expense claims, organizational charts, overhead allocation models, and business plans.
- Assessed CEC's current budget procedures to see if assumptions were reasonable and practices aligned with proper internal controls such as those recommended by leading industry practices and complied with relevant laws and regulations, decisions, and advice letters.
- Reviewed CPUC requirements related to the calculation of interest and verified interest was accurately calculated by EPIC administrators
- Compared interest earnings to amounts returned to ratepayers during the annual rate setting process to verify interest was accurately returned in accordance with CPUC requirements.
- Gained an understanding of overhead costs, including the types and amounts of overhead charges and the basis for the calculations.
- Reviewed administrative overhead costs applied to EPIC invoices by contractors and subcontractors.
- Compared the amount of EPIC funding remaining available against the status of EPIC projects to assess whether funding appears sufficient to complete their planned projects.
- Assessed the oversight funding against oversight activities undertaken and planned.

Sjoberg Evashenk Consulting 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 that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Finding #1: EPIC Collections from Ratepayers Were Consistent with CPUC Decision Requirements, But Processes to Remit Revenues to CEC and CPUC Revealed a Few Problems

Of the $1.5 billion collected by the three IOUs from ratepayers to fund the EPIC program, 0.5 percent is administered by CPUC to perform oversight activities; of the remaining funding, the CEC administers 80 percent and the three IOUs together administer 20 percent, as shown in Exhibit 3. The three IOUs remit the collected revenues to the CEC and the CPUC and keep the remaining funding to administer their individual portions of the EPIC program.

EXHIBIT 3. REQUIRED EPIC FUNDING ALLOCATIONS

	EPIC 1	EPIC 2	EPIC 3	Total
CEC	$368,700,000	$405,787,100	$441,780,000	$1,216,267,100
PG&E	$48,078,465	$50,824,790	$55,332,945	$154,236,200
SCE	$39,441,615	$41,694,588	$45,392,895	$126,529,098
SDG&E	$8,444,920	$8,927,308	$9,719,160	$27,091,388
CPUC	$2,335,000	$2,548,914	$2,775,000	$7,658,914
Total	**$467,000,000**	**$509,782,700**	**$555,000,000**	**$1,531,782,700**

Overall, our review found that EPIC revenue collected by the three IOUs appear consistent with CPUC decisions. However, billing processes employed by CEC and CPUC to seek the required EPIC remittances resulted in over-remittances by the IOUs.

EPIC Revenue Collections Appear Consistent with CPUC Decision Requirements

To generate the EPIC revenues required by CPUC to fund the program, the three IOUs establish a CPUC-approved rate that is assessed through a surcharge on electricity bills and collected from ratepayers. The process to establish rates requires the IOUs to calculate the annual revenue requirement needed to collect the mandated EPIC funding and also includes a process to “true up” future revenue requirements to adjust for any differences between EPIC amounts required to be collected and amounts actually collected in previous years.

Through December 31, 2019, we found that each of the three IOUs generally collected amounts from ratepayers consistent with CPUC decisions and appeared on track to complete the total required EPIC collections by the end of 2020. Exhibit 4 compares the required EPIC collections reflected in Exhibit 2, the amounts actually collected through 12/31/2019, and details the remaining amounts to be collected in 2020 to meet the total EPIC budget requirements.

EXHIBIT 4. REQUIRED TOTAL EPIC COLLECTIONS, AMOUNTS COLLECTED THROUGH 12/31/2019, AND REMAINING AMOUNTS TO BE COLLECTED IN 2020

IOU by Calendar Year		EPIC 1 1/1/2012 - 12/31/2014	EPIC 2 1/1/2015 - 12/31/2017	EPIC 3 1/1/2018 - 12/31/2020	Total
PG&E	Total Amount Required to be Collected Through 12/31/2020	$233,967,000	$255,401,133	$278,055,000	$767,423,133
	Amount Collected Through 12/31/2019[4]	$234,191,456	$260,276,696	$193,528,238	$687,996,390
Amount Remaining to be Collected by PG&E in 2020:					**$79,426,743**
SCE	Total Amount Required to be Collected Through 12/31/2020	$191,937,000	$209,520,690	$228,105,000	$629,562,690
	Amount Collected Through 12/31/2019[5]	$191,651,000	$209,397,492	$157,189,602	$558,238,094
Amount Remaining to be Collected by SCE in 2020:					**$71,324,596**
SDG&E	Total Amount Required to be Collected Through 12/31/2020	$41,096,000	$44,860,878	$48,840,000	$134,796,878
	Amount Collected Through 12/31/2019[6]	$40,982,636	$41,711,504	$31,439,309	$114,133,449
Amount Remaining to be Collected by SDG&E in 2020:					**$20,608,273**

Processes to Remit EPIC Funding to CEC and CPUC Revealed a Few Issues

Overall, the processes to remit EPIC funding resulted in the three IOUs over-remitting funding to CEC and CPUC. Specifically, CEC and CPUC receive the required remittances from the three IOUs through a variety of mechanisms. Specifically, the following describes how the IOUs remit EPIC funding to support CEC's EPIC project and administrative costs:

- **CEC's Project Costs**—A total of $1,094,184,500 is required to be remitted to CEC to support CEC's EPIC project costs, as shown in Exhibit 5. After CEC formally approves EPIC projects at monthly business meetings and encumbers the associated expenditures, CEC issues invoices to the IOUs for their proportional share of the approved costs. These remittances are generally transmitted via wire transfers.
- **CEC's Administrative Costs**—A total of $122,082,600 is required to be remitted to CEC for costs associated with administering CEC's EPIC program. This portion of EPIC funding is due from the three IOUs in equal quarterly payments in the same proportions as described for project cost remittances. In

[4] Includes interest earned on EPIC funds retained by PG&E, which is offset by reducing future revenue collections.
[5] Does not include some interest earnings that SCE returned to ratepayers.
[6] Includes interest earned on EPIC funds retained by SDG&E, which is offset by reducing future revenue collections.

2019, to reduce confusion related to when administrative remittances were due and the required payment amounts, CEC began issuing formal quarterly invoices due the first day of January, April, July, and October. These remittances are generally transmitted via wire transfers.

Exhibit 5 compares the amounts required to be remitted to CEC and CPUC through 12/31/2020, the amounts IOUs remitted through 12/31/2019, and the remaining amounts to be remitted in 2020 to meet CPUC requirements.

EXHIBIT 5. REQUIRED TOTAL EPIC REMITTANCES TO CEC AND CPUC, AMOUNTS REMITTED THROUGH 12/31/2019, AND REMAINING AMOUNTS TO BE REMITTED IN 2020

IOU by Remittance		Required Total Remittances Through 12/31/2020	Remittances Through 12/31/2019		Remainder to be Remitted in 2020
			Required	Actual	
CEC Project Remittances	PG&E	$548,186,435	$352,723,101	$355,228,016	$192,958,419
	SCE	$449,709,830	$289,359,669	$291,361,800	$158,348,030
	SDG&E	$96,288,236	$61,955,357	$62,395,343	$33,892,893
Total		**$1,094,184,501**	**$704,038,127**	**$708,985,159**	**$385,199,342**
CEC Administrative Remittances	PG&E	$61,163,383	$55,096,728	$55,096,728	$6,066,655
	SCE	$50,175,949	$45,217,702	$45,217,702	$4,958,247
	SDG&E	$10,743,269	$8,002,679	$8,002,679	$2,740,590
Total		**$122,082,601**	**$108,317,109**	**$108,317,109**	**$13,765,492**
CEC Total		**$1,216,267,102**	**$812,355,236**	**$817,302,268**	**$398,964,834**
CPUC Oversight Remittances	PG&E	$3,837,116	$3,373,691	$3,358,070	$479,046
	SCE	$3,147,813	$2,767,638	$2,806,660	$341,153
	SDG&E	$673,984	$592,584	$660,280	$13,704
CPUC Total		**$7,658,913**	**$6,733,913**	**$6,825,010**	**$833,903**

As shown in Exhibit 5, while the three IOUs were required to remit a combined $812,355,236 to CEC from inception of the EPIC program in 2012 through 12/31/2019 for project and administrative expenses, the IOUs actually remitted $817,302,268—a combined over-remittance of $4,947,032 resulting from the following issues:

- **$4,999,830**—CEC overbilled the three IOUs a combined total of $4,999,830 as a result of invoicing the IOUs twice for the same EPIC project. Specifically, CEC invoiced the IOUs initially when the project was first approved at an October 2018 business meeting and invoiced the IOUs again in error when the project was approved a second time at a September 2019 after the project site location changed requiring the additional approval.

- **$52,800**—CEC reduced SCE's September 29, 2017 project invoice by $52,800 for an apparent prior overpayment; however, comparing invoices against remittances revealed that there was no overpayment.

According to CEC, corresponding credits and additional charges were reflected on invoices sent to the IOUs in 2020 to correct these issues to ensure the IOUs remit the amounts required by 12/31/2020.

Related to oversight remittances due to CPUC, a process was not in place to seek oversight remittances from the IOUs; rather, the IOUs were responsible for initiating payment. While the three IOUs were required to remit $6,733,914 to CPUC from inception through 12/31/2019, as reflected in Exhibit 5, the IOUs actually submitted a combined $6,825,010—an over-remittance of $91,096 resulting from the following:

- **$122,258**—SDG&E over-remitted $70,436 and SCE over-remitted a combined $51,822 during EPIC 2. Due to the lack of formal payment requests, reasons for the over- and under-remitted oversight monies could not be determined.
- **$31,162**—The three IOUs remitted a combined total of $2,303,852 to CPUC for oversight during EPIC 1, which was $31,148 less than the required 0.5 percent of the total EPIC budget. The under-remittance was the result of conflicting guidance provided in CPUC Decision 12-05-037 where IOUs were directed to remit 0.5 percent of the EPIC budget in the text of the decision, but guidance in a summary table in the same Decision reflected that the remittance should equal 0.494 percent of the EPIC budget. CPUC later acknowledged the error in Decision 15-04-020. Further, According to CPUC staff, since the IOUs submitted the dollar amount indicated in the table of the Decision, they do not view it as an under-remittance that CPUC would need to recoup. In addition, PG&E under-remitted $14 over EPIC 2 and 3.

It is unclear how CPUC plans to correct the remittance issues in 2020 to ensure the IOUs remit the amounts required by 12/31/2020.

<u>Recommendations</u>:

To improve the processes related to seeking remittances from the IOUs, CPUC should consider:

1. Ensuring CEC develops a process to reconcile remittance invoices sent to the three IOUs against approved project expenditures before sending additional invoices.
2. Directing the CPUC Fiscal Office to assume the responsibilities of invoicing the IOUs for oversight remittances.
3. Determining the best method to address the remittance errors related to CPUC oversight funding.

Finding #2: CEC's Budget Processes and Controls were Reasonable and Complied with Applicable Requirements

CEC's budget process followed the typical California state cycle where costs are estimated for a July 1 through June 30 fiscal year; funding for those costs are identified, and budget authority to spend is approved by the State Legislature. CEC's budget development process was reasonable, consistent with industry practices, and complied with administrative cost provisions included in CPUC decisions. Below, we describe CEC's budgetary processes and conclude that its processes appear appropriate and effective. Therefore, in this section, we make no recommendations specific to CEC's budgetary processes.

CEC's Budget Development Process Appears Reasonable

CEC's EPIC program developed rapidly after it was established by CPUC in 2011—as part of the 2012 budget, the Legislature approved $1 million and 4.5 positions to complete CEC's first EPIC investment plan and the 2013 budget approved $160 million and 55 positions from IOUs ratepayer funds for the implementation of CEC's EPIC program. As additional EPIC investment periods have been implemented and more projects added, CEC has requested incremental budget authority to meet program needs. The budget process is aligned with the state budget process requirements for state agencies where program administration dollars approved in various CPUC decisions are proportionally allocated to fiscal year budgets to align with the state budget process. Funding for EPIC program administration is appropriated to the CEC on a fiscal year basis through the annual State Budget Act. CEC investment plans approved by the CPUC indicated that the CEC converts the three-year investment plan into three fiscal budget allocations.

Overall, the CEC's administrative budget consists of the following:

1. Personal service (labor) expenditures
2. Discretionary (non-labor) operating expenditures and equipment
3. Discretionary (non-labor) travel expenditures
4. Nondiscretionary CEC indirect department overhead
5. Nondiscretionary statewide central service department charges (like corporate parent company overhead)

Some items are captured and tracked centrally by CEC's Budget and Accounting Offices including labor, department overhead, and central service department costs, while other direct, discretionary items are captured and tracked by Energy Research and Development Division (ERDD) in its Operating Expenses and Equipment (OEE) budget.

CEC's central Budget Office initiates the budget process, but works closely in collaboration with ERDD to estimate program needs. Annually, the Budget Office provides ERDD a total non-labor budget to allocate into specific expenditure categories (printing, communications, postage, travel, etc.), which is loaded into the State's financial system (CALSTARS or FI$Cal). Personal service labor budgeted positions are also provided and reconciled between the Budget Office and ERDD—although the Budget Office estimates the related labor costs. In addition to the approximate 82 positions within ERDD, CEC informed us of eight additional positions in other areas of the organization that are also fully EPIC funded related to accounting, contracts, legal, and information technology.

CEC receives authorized EPIC positions through the state budget process and assigns unique position numbers to the positions, which includes an identifier for the funding source. The positions are managed through standard position control processes jointly by CEC's Human Resources and Budget Offices. For the non-labor expenditures managed by ERDD, a Fiscal Liaison uses past expenditure history to estimate and budget for the current year between the various expenditure categories and ERDD division offices, units, and sections. CEC's administrative budget plan is reviewed and approved by ERDD's management and Deputy Director.

CEC's Process to Manage Costs Against its Budget is Aligned with Industry Practices

According to CEC, budget categories are tracked against actual spending—as is suggested by leading industry practices. CEC's Budget and Accounting Offices monitor personal service labor expenditures, while ERDD monitors non-labor expenditures.

Using the approved budget, ERDD's Fiscal Liaison uses an automated spreadsheet to track expenditures incurred against the budget plan. When ERDD processes transactions for purchase orders, travel, training, or IT work order requests, an administrative assistant assigns the appropriate budget code on the requests/orders and expenditures. Each item is given to the Accounting Office for official processing and is recorded in the automated budget tracking spreadsheet. On a monthly basis, ERDD reconciles its budget-to-actual spreadsheet with the Accounting Office's monthly budget report based on transactions recorded in the State's financial system (CALSTARS or FI$Cal). Moreover, on a quarterly basis, ERDD and the Accounting Office meet to review labor expenses.

Given our knowledge of the State's financial system as well as confirmation from CEC, administrative costs charged cannot exceed annual fiscal year budgets established by CEC and approved by the Legislature. If EPIC administrative costs are expected to be more than 10 percent over a particular budget category, CEC's Accounting Office must prepare a plan of financial adjustment (PFA) to move expenditures out of the EPIC fund to another funding source. According to CEC, if its EPIC administrative costs are lower than amounts budgeted, the costs can be encumbered for two fiscal years and have an additional four fiscal years to liquidate.

CEC's Administrative Processes Complied with Laws, Regulations, and Decisions

Generally, CPUC decisions and laws, regulations, and legislation generally focus on the programmatic elements of EPIC, areas for program investment, the IOUs role and surcharges, or public benefits—rather than administrative budgets or expenditures. However, a few CPUC decisions spoke to budgets, administrative costs, and funding. As shown in Exhibit 6, we found that CEC generally complied with all relevant administrative-related requirements.

EXHIBIT 6. CEC COMPLIANCE WITH ADMINISTRATIVE BUDGET AND COST REQUIREMENTS

Authority	Requirement	Assessment of CEC Actions
D.12-05-037 **D.15-04-020**	- 10% Administrative Cap (p.100)	As of June 2019, CEC expended about 6 percent of its administration budget; however, administration expenses accounted for 18 percent of its total EPIC expenses (Exhibit 33) and had outpaced its project expenses 29 percent to 57 percent. See Finding #7 on page 40-42 of this report.
	Admin Costs include the following as related to preparing investment plans, conducting solicitations, selecting funding recipients, and monitoring/overseeing the progress of projects and investments (p. 69): - Staffing cost of the administrators - Associated general and administrative expenses and overhead - Related contracting costs Definition of Admin Costs to include (p.39 & p.64): - Staffing of administrators - Project management and internal coordination - Research consortia membership fees - Reporting General and admin expense to prepare investment plans, conduct solicitations, contracting, select funding recipients, and monitor and oversee the progress of projects and investments.	Costs for the CEC staff performing these activities are captured in direct labor and indirect charges. We tested 18% of costs totaling nearly $14.6 million and found that costs were generally supported, reasonable, and accurate. See Finding #5 on page 30 of this report for results of our testing.
	Administration is accounted for separately from other EPIC activities (p. 62)	Admin is charged to state operations budget and fiscal line items; program costs charged to local assistance budget/fiscal line items
SB 96	Justify actual admin and overhead costs	CEC submits annual reports and uses CALSTARS/FI$Cal to track administrative and overhead costs. As we found through our testing, CEC did not always maintain underlying support to justify its costs. See Finding #5 on page 30 of this report for results of our testing.

Recommendations: None.

Finding #3: Two IOUs Did Not Always Return EPIC Interest Earnings to Ratepayers Following Timelines Required by CPUC Decisions

CPUC decisions require the four EPIC administrators to return all interest earned on EPIC funds back to ratepayers. Specifically, interest earned during EPIC periods 1 and 2 (2012-2014 and 2015-2017) must be returned to ratepayers in the form of reduced collections during the EPIC 3 period (2018-2020). The decisions also state that interest earned during EPIC 3 must also be returned to ratepayers, but a specific timeframe for doing so is not specified. We found that the three IOUs did not always return its interest earnings during EPIC periods 1 and 2 following the required timelines.

SCO is Responsible for Calculating Interest Earned on CEC's EPIC Funds

On a quarterly basis, the State Controller's Office (SCO) provides reports to CEC and CPUC detailing the amount of interest earned on their EPIC funds during the previous quarter. As such, CEC and CPUC rely on the SCO to calculate the interest earned on their EPIC funds. The total interest earnings on CEC's EPIC funds from 1/1/2012 through 6/30/2019 was $19,193,896.

IOUs Accurately Calculated Interest Earnings on EPIC Funds Using CPUC Guidance

CPUC Advice Letter 3182-E provides the specific calculation that the three IOUs must use to determine the interest earnings on their EPIC funds that must be returned to ratepayers. Specifically, IOUs are directed to calculate the monthly interest earnings by averaging the beginning and ending EPIC fund balances (driven by revenue and expenditure activity) multiplied by one-twelfth of the Federal Reserve's three-month Commercial Paper Non-Financial rate (FRED). For example, if an IOU has an average beginning and ending EPIC fund balance for a particular month of $27,937,474 and it is multiplied by one-twelfth of a FRED rate of 2.52, the interest earning calculation for the month would equal about $58,669.

The total interest earnings calculated by each IOU from 1/1/2012 through 12/31/2017 was:

- PG&E—$2,414,991
- SCE—$2,100,927
- SDG&E—$468,610

To determine if the three IOUs had processes in place to correctly calculate monthly interest earnings on EPIC funds, we reviewed the details behind their monthly interest calculations for calendar years 2015 and 2019 and found IOU interest calculations during these two years appeared accurate.

CEC Interest Earnings Returned to Ratepayers in Accordance with CPUC Decisions

As part of the requirement to return interest earned on EPIC funds back to ratepayers, CPUC decisions require the collection amounts IOUs must remit to CEC be reduced by the interest earned. Specifically, as described earlier, CEC sends the three IOUs invoices to collect remittances related to project expenses. CEC reduces the remittances due on the invoices by the interest earned on its EPIC funds—the invoices are reduced by the same proportion that the IOUs collect EPIC revenue from ratepayers. Because the amounts the IOUs must remit to CEC is reduced, the amount of EPIC funding the IOUs must collect from ratepayers is reduced by the same amount.

To determine if the $19,193,896 CEC earned on its EPIC funds between January 1, 2012 and June 30, 2019 was appropriately returned, we reviewed the 15 project invoices CEC sent to the three IOUs between Fiscal Years 2014-2015 and 2019-2020. Our review found that the interest earned during the period was appropriately reduced from the project invoices sent to the IOUs as required, as shown in Exhibit 7.

EXHIBIT 7. CEC EPIC FUNDS INTEREST EARNINGS REDUCTIONS APPLIED TO IOU PROJECT INVOICES

Fiscal Year	Interest Earned on CEC Epic Funds	EPIC Project Invoice Interest Reductions			
		PG&E	SCE	SDG&E	Total Invoice Reductions
2014/15[7]	$174,368[8]	$87,358	$71,665	$15,344	$174,368
2015/16	$884,987	$443,379	$363,730	$77,879	$884,987
2016/17	$2,841,836	$1,423,760	$1,167,995	$250,082	$2,841,836
2017/18	$5,659,448	$2,835,384	$2,326,033	$498,031	$5,659,448
2018/19	$9,633,257	$4,826,262	$3,959,269	$847,727	$9,633,257
Total	**$19,193,896**	**$9,612,142**	**$7,888,691**	**$1,689,063**	**$19,193,896**

Two IOUs Did Not Always Return Interest Earnings to Ratepayers in Accordance with CPUC Decisions

Similar to CEC, CPUC decisions also require the three IOUs to return all interest earned on EPIC funds during EPIC periods 1 and 2 (2012-2017) to ratepayers in the form of reduced rates and collections for the EPIC 3 period (2018-2020). Specifically, each year, CPUC approves all rates that electric utilities charge ratepayers, which are set based on estimated revenue requirements for the upcoming year, including the revenue needed to be collected for the EPIC program. To return the interest earnings back to the ratepayers, the three IOUs reduce their revenue requirements by the amount of interest earned. Although 2018 was the first year of the EPIC 3 period, 2019 was the earliest the three IOUs could reduce revenue requirements for interest earned 1/1/2012 through 12/31/2017 due to timing of interest earning calculations and rate setting processes.

We reviewed the processes used by the three IOUs to return interest earned to determine if the earnings were appropriately returned to ratepayers following CPUC requirements. We found that PG&E has not yet returned any interest earned on EPIC funds during EPIC 1 and 2 back to ratepayers and SCE inadvertently excluded small portions of their interest earnings from the amounts they returned back to ratepayers. Specifically:

- PG&E's interest rate calculation reflected that $2,414,991 was earned on its EPIC funds between January 1, 2012 and December 31, 2017; however, PG&E's 2019 rate setting processes did not

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[7] CEC began sending project invoices to the IOUs in Fiscal Year 2014-2015.

[8] Total includes interest earnings beginning in July 2012 through June 30, 2015.

reduce revenue requirements to offset the earnings. According to PG&E, the interest earnings will be considered as part of their 2021 rate setting processes.

- SCE's interest rate calculation reflected that $2,100,927 was earned on its EPIC funds between January 1, 2012 and December 31, 2017; however, SCE's 2019 rate setting processes reduced revenue requirements by $2,073,273 to offset the earnings. According to SCE, $27,654 was unintentionally excluded and will be considered as part of their 2021 rate setting processes.

While the PG&E and SCE intend to make the needed corrections during their 2021 rate setting processes, the adjustments will occur outside of CPUC's required timeframe. Specifically, CPUC decisions required the interest earned for the EPIC 1 and 2 periods be returned to ratepayers in the form of reduced collections for the EPIC 3 period, which covers the 2018 through 2020 rate setting processes.[9]

Lastly, although CPUC decisions do not specify the treatment of interest earned on CPUC's EPIC balances related to oversight funding, we noted that CPUC earned approximately $75,485 between July 1, 2012 and June 30, 2019. According to CPUC staff, a process is not in place to return the interest earned on CPUC's EPIC balances to ratepayers.

Recommendations:

To improve processes to return interest earned on EPIC funds, the CPUC should consider:

4. Ensuring SCE and PG&E return the remaining interest earned between 2012 and 2017 back to ratepayers.
5. Developing processes to return interest earned on CPUC's EPIC oversight funds back to ratepayers.

[9] D.18-01-008 OP 9

Finding #4: Project Costs Appear Generally Supported and Reasonable, Cost Guidelines Are Needed

As described earlier, CPUC decisions detail the approved EPIC budgets for each of the four administrators, including funding slated to be spent on direct project costs, as shown in Exhibit 8. While the three IOUs retain their portion of EPIC collections for project funding, the Legislature must grant spending authority to the CEC to disburse its EPIC funds for project awards.

EXHIBIT 8. EPIC PROJECT FUNDING BUDGET BY ADMINISTRATOR

Administrator	EPIC 1	EPIC 2	EPIC 3	Total
CEC	$331,800,000	$365,004,500	$397,380,000	$1,094,184,500
PG&E	$43,270,618	$45,742,311	$49,799,651	$138,812,580
SCE[10]	$35,497,454	$39,570,129	$40,853,605	$115,921,188
SDG&E[11]	$7,600,428	$8,293,578	$8,747,244	$24,641,250
Total	**$418,168,501**	**$458,610,518**	**$496,780,501**	**$1,373,559,518**

CPUC decisions also require each of the four administrators to submit triennial EPIC investment plans outlining the projects that will be funded for the given three-year investment period; the investment plans are approved by the CPUC:

- EPIC 1—All Four Administrator Investment Plans Approved 11/14/2013
- EPIC 2—All Four Administrator Investment Plans Approved 4/9/2015
- EPIC 3—CEC's Investment Plan Approved 1/11/2019; Three IOU Investment Plans Approved 10/25/2018

The four administrators charge costs against the EPIC project budget category that are direct project expenses in that they relate to a specific EPIC project. The majority of direct project expenses for all four administrators focused largely on contracted services, which generally relate to contractors hired to develop and implement some or all aspects of the EPIC projects depending on the level of involvement of the staff of the four administrators. Because IOU employees perform aspects of project work, the three IOUs also charge direct project labor expenses to its EPIC projects.

Additionally, the IOUs also charge internal overhead expenses, which are expenses that relate directly to EPIC project or administrative work, but not to a specific EPIC project, such as payroll taxes, benefits, and materials burden. Although CEC employees perform some technical aspects of the work on their EPIC projects, it does not charge internal overhead expenses to its EPIC projects.

[10] Includes a $2,045,000 shift from SCE's administration to project budget.
[11] Includes a $259,000 shift from SDG&E's administration budget to project budget.

Overall, while CPUC has not issued formal guidance detailing the allowability of costs or activities, we found the direct project expenditures charged to the EPIC projects by the four administrators appeared generally reasonable and supported. We also noted that the amounts and types of overhead expenses charged to the projects by the three IOUs varied due to their individual organizational requirements and protocols. Further, overhead cost allocation processes are based on company overhead models and are not necessarily specific to EPIC.

Lack of Formal Guidance to Administrators Related to Expending EPIC Project Funding

We noted a lack of formal guidance developed, provided, or available to the administrators delineating parameters for expending EPIC funding. In particular, other than broad category descriptions, CPUC decisions did not provide sufficient descriptions related to the allowability of costs or activities to control the utilization of EPIC project funding and ensure appropriate spending of project-related monies in accordance with the intent of program goals. Providing such guidance establishes compliance criteria by which CPUC could assess consistency, strengthen accountability, and ensure a prudent use of ratepayer funds.

Direct Project Expenditures Appeared Generally Reasonable and Supported

Because we did not have cost guidelines to use as criteria to determine if EPIC project expenses were allowable, we focused our efforts on determining if the costs charged to EPIC projects appeared reasonably related to project efforts and activities, were associated with a vendor contract, and adequately supported with underlying documentation. The majority of direct project expenses for all four administrators largely involved contracted services, which generally related to contractors hired to develop and implement some or all aspects of the EPIC projects depending on the level of involvement of the staff of the four administrators.

It is important to note that we did not assess if the approved projects met EPIC program goals or whether invoiced amounts were appropriate for the scope of the project. CPUC hired a consultant to conduct a comprehensive evaluation of EPIC to identify opportunities to improve program management and effectiveness and determine if the program was implemented in a manner consistent with the program objectives, requirements and intent of the CPUC and the California Legislature as set forth in a series of CPUC decisions; the report was released in 2017. That report found that the four administrators were in compliance with EPIC requirements and goals of the program, but could enhance certain administrative practices related to areas such as stakeholder engagement, coordination, project selection and information sharing.

Overall, our review of a sample of projects and activities found the direct project costs charged by the four administrators appeared generally reasonable and largely supported with underlying documentation. Below, we describe the results of our review of project costs for each of the four EPIC administrators.

<u>CEC's Direct Project Expenses Appeared Generally Reasonable and Most Were Adequately Supported with Underlying Documentation</u>

As of June 30, 2019, CEC expended $318,230,653 on direct project costs associated with 346 individual EPIC projects. We reviewed expenditures associated with 13 projects totaling $36,996,387, or 12 percent of total project costs, as shown in Exhibit 9.

EXHIBIT 9. CEC EPIC PROJECTS TESTED

Projects Reviewed	Direct Project Costs	Amount tested	Percent Tested
1	$1,817,671	$416,296	23%
2	$5,000,000	$2,795,077	56%
3	$1,431,911	$711,243	50%
4	$1,844,906	$707,791	38%
5	$1,794,690	$1,673,530	93%
6	$4,983,459	$1,341,928	27%
7	$2,274,513	$1,140,758	50%
8	$3,000,000	$1,975,000	66%
9	$3,943,801	$586,915	15%
10	$4,816,314	$932,049	19%
11	$4,776,171	$1,528,347	32%
12	$488,097	$413,604	85%
13	$824,854	$217,843	26%
Total	**$36,996,387**	**$14,440,381**	**39%**

The expenditures associated with each of the 13 projects reviewed related to contracted services only. For each project, we selected a variety of contractor invoices to verify costs appeared reasonably related to the project activities, were associated with a vendor contract, and were reasonably supported with underlying documentation, such as contractor invoices, timesheets, and receipts.

Overall, out of the 65 invoices reviewed associated with the 13 projects, we found CEC's project expenses reviewed appeared generally reasonable, related to EPIC project activities, and were supported by underlying documentation; however, we noted that CEC's agreement terms and conditions do not require minor subcontractors to submit detailed supporting documentation, such as employee timesheets, for expenses under $100,000.

Further, approximately $37 million related to the 13 projects, $6.7 or 18 percent—ranging from 4 percent to 44 percent—was budgeted for administrative overhead costs of prime contractors and subcontractors. We found that contractor invoices clearly identified the administrative overhead costs separate from the direct project costs, allowing CEC to monitor these expenses against the assigned budgets. According to CEC, awards to University of California entities are allowed a maximum cap of 25 percent for administrative overhead costs. Otherwise, CEC does not have caps on contractor administrative overhead charges, but, stated that their proposal evaluation processes provide higher scores for applicants reflecting lower administrative overhead cost requirements. CEC believes capping overhead rates could have a negative impact on startup organizations that have higher administrative costs than established entities and on research facilities that generally require higher administrative allowances.

PG&E Direct Project Expenses Appeared Generally Reasonable and Supported with Underlying Documentation

As of December 31, 2019, PG&E charged $81,954,421 in direct project and overhead costs against 42 individual EPIC projects. To review PG&E's direct project expenditures, we selected four projects totaling about $9.2 million (or 11 percent) of total project costs, of which, $8.6 million related to direct project expenditures. As shown in Exhibit 10, we focused testing on the following expenditure categories: contracted services, direct project labor, employee reimbursables/travel, and materials/purchasing card.

EXHIBIT 10. PG&E EPIC PROJECTS TESTED—DIRECT PROJECT COSTS

Expenditure Category	Direct Project Costs	Percent of Total	Amount Tested	Percent Tested
Project 1				
Contracted Services	$1,809,356	86%	$855,266	47%
PG&E Direct Project Labor	$262,298	12%	$36,522	14%
Employee Reimbursables/Travel	$40,986	2%	$3,776	9%
Total Direct Project Expenditures	*$2,112,640*	100%	$895,564	42%
Project 2				
Contracted Services	$696,300	18%	$27,580	4%
PG&E Direct Project Labor	$167,507	4%	$16,658	10%
Employee Reimbursables/Travel	$4,450	0%	$2,546	57%
Materials/Purchasing Card	$3,075,361	78%	$99,997	3%
Other Costs	$5,139	0%	$0	0%
Total Direct Project Expenditures	*$3,948,759*	100%	$146,781	4%
Project 3				
Contracted Services	$230,331	51%	$228,271	99%
PG&E Direct Project Labor	$193,344	43%	$42,499	22%
Employee Reimbursables/Travel	$36	0%	$53	147%
Materials/Purchasing Card	$29,811	7%	$22,728	76%
Total Direct Project Expenditures	*$453,522*	100%	$293,551	65%
Project 4				
Contracted Services	$1,545,782	71%	567,816	37%
PG&E Direct Project Labor	$499,467	23%	$161,166	32%
Employee Reimbursables/Travel	$3,394	0%	$1,228	29%
PG&E IT Inventory	$127,055	6%	$0	0%
Total Direct Project Expenditures	*$2,175,697*	100%	$730,210	33%
Grand Total	**$8,690,618**		**$2,066,106**	**24%**

For each direct project cost category tested, we:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to contractors hired to develop and implement aspects. Verified costs were reasonably supported with underlying documentation such as contractor invoices, timesheets, and receipts, and associated with a vendor contract.

Further, the majority of the contracted services invoices did not separately identify administrative overhead charges. However, one contractor separately identified a 15 percent allowance related to travel and living expenses, as permitted by the contract agreement with PG&E. According to PG&E, contractor overhead charges are not typically separately identified, but are included in the hourly rates reflected in the cost proposals submitted in response to solicitations and in contract terms and conditions. As a result, we were unable to identify the administrative overhead costs charged by contractors separate from the direct project costs.

- **PG&E Direct Project Labor:** Identified the types of activities associated with the expenses, which related to PG&E employees working directly on EPIC projects, including project management/solution consultants, technologists/engineers, and technical business experts. Verified costs were reasonably supported with underlying timesheet documentation.
- **Materials/Purchasing Card:** Identified the types of costs, which related to measuring instruments and automotive materials (one project related to developing exportable power capabilities from a plug-in hybrid electric truck). Verified costs were supported with underlying documentation such as invoices and receipts, and costs appeared reasonable and related to the projects.
- **Employee Reimbursables/Travel:** Identified the types of costs, which related largely to lodging, airfare, and meals. Verified costs were supported with underlying documentation such as travel expense claims, travel receipts, and invoices and costs appeared reasonable and related to the projects. We noted $170 in charges related to a late checkout fee and rollaway beds associated with Project 4 in Exhibit 10 that according to PG&E were associated with a conference on data analysis for an employee working on several EPIC projects that required data analytics—the costs were split between Project 4 and another EPIC project. We also noted a total of $388 in charges related to Projects 1 and 2—according to PG&E these costs were for two separate lunches for nine PG&E employees and seven business associates and contractors.

Overall, we found PG&E's project expenses reviewed appeared generally reasonable, related to EPIC project activities, and were supported by underlying documentation.

SCE Direct Project Expenses Were Generally Reasonable and Supported with Underlying Documentation

As of December 31, 2019, SCE charged $66,864,205 in direct project and overhead costs to 48 individual EPIC projects. To review SCE's direct project expenditures, we selected two projects totaling about $7 million or 10 percent of total project costs, of which, $6.8 million related to direct project expenditures. As shown in Exhibit 11, we focused testing on the following expenditure categories: contracted services, direct project labor, employee reimbursables/travel, and materials.

EXHIBIT 11. SCE EPIC PROJECTS TESTED—DIRECT PROJECT COSTS

Expenditure Category	Direct Project Costs	Percent of Total	Amount Tested	Percent Tested
Project 1				
Contracted Services	$3,329,191	67%	$751,181	23%
SCE Direct Project Labor	$523,947	11%	$7,994	2%
Materials	$1,000,962	20%	$126,050	13%
Employee Reimbursable/Travel	$102,656	2%	$9,547	9%
Other[12]	$2,890	0%	$0	0%
Total Direct Project Expenditures	*$4,959,646*	100%	$894,772	18%
Project 2				
Contracted Services	$1,500,819	84%	$327,437	22%
SCE Direct Project Labor	$87,586	5%	$1,112	1%
Materials	$201,899	11%	$2,281	1%
Employee Reimbursable/Travel	$1,042	0%	$1,042	100%
Total Direct Project Expenditures	*$1,791,346*	100%	$331,872	19%
Grand Total	**$6,750,992**		**$1,226,644**	**18%**

For each direct project cost category tested, we:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to contractors hired to develop and implement aspects of the EPIC projects. Verified costs were reasonably supported with underlying documentation such as contractor invoices, timesheets, and receipts, and associated with a vendor contract.

  According to SCE, contractor overhead charges are not separately identified, but are included in the hourly rates reflected in the cost proposals submitted in response to solicitations and in contract terms and conditions. As a result, we were unable to identify the administrative overhead costs charged by contractors separate from the direct project costs.

- **SCE Direct Project Labor:** Identified the types of activities associated with the expenses, which related to SCE employees working directly on EPIC projects, including engineers, technical specialists, and project managers. Verified costs were reasonably supported with underlying timesheet documentation.
- **Materials:** Identified the types of costs, which generally related to electrical equipment and infrastructure technology. Verified costs were supported with underlying documentation such as invoices and receipts, and costs appeared reasonable and related to the project.

[12] Safety training and employee reimbursements for GPS equipment and networking materials.

- **Employee Reimbursables/Travel:** Identified the types of costs, which generally related to lodging, airfare, and meals. Verified costs were supported with underlying documentation such as travel expense claims, travel receipts, and invoices and costs appeared reasonable and related to the projects. For Project 1, we noted catering charges of $792—these charges relate to breakfast and lunch for thirty attendees during a day-long system demonstration with the prime contractor and Department of Energy. For Project 2, we note catering charges of $1,749—these charges related to breakfast and lunch for sixteen people over three days for a test team, a field crew, and project personnel supporting predictive equipment failure testing.

Overall, we found SCE's project expenses reviewed appeared generally reasonable, related to EPIC project activities, and were supported by underlying documentation; however, we identified a duplicate credit of $50,033 applied to Project 1 where SCE inadvertently credited the project twice related to excess materials that were returned. According to SCE, this entry was corrected in December 2020.

SDG&E Direct Project Expenses Were Generally Reasonable and Supported with Underlying Documentation

As of December 31, 2019, SDG&E charged $16,356,611 in direct project and overhead costs to 15 individual EPIC projects. To review SDG&E's direct project expenditures, we selected two projects totaling about $3.44 million or 21 percent of total project costs, of which, $3.41 million related to direct project expenditures. As shown in Exhibit 12, we focused testing on the following expenditure categories: contracted services, direct project labor, employee reimbursables/travel, and materials.

EXHIBIT 12. SDG&E EPIC PROJECTS TESTED—DIRECT PROJECT COSTS

Expenditure Category	Direct Project Costs	Percent of Total	Amount Tested	Percent Tested
Project 1				
Contracted Services	$1,340,744	96%	$254,004	19%
SDG&E Direct Project Labor	$38,233	3%	$4,273	11%
Employee Reimbursables/Travel	$9,232	1%	$3,766	41%
Materials	$7,615	1%	$5,946	78%
Total Direct Project Expenditures	$1,395,825	100%	$267,989	19%
Project 2				
Contracted Services	$1,721,457	85%	$276,096	16%
SDG&E Direct Project Labor	$33,350	2%	$3,288	10%
Employee Reimbursables/Travel	$2,724	0%	$1,821	67%
Materials	$266,022	13%	$88,150	33%
Total Direct Project Expenditures	$2,023,553	100%	$369,355	18%
Grand Total	**$3,419,378**		**$637,344**	**19%**

For each direct project cost area selected for testing, we:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to contractors hired to develop and implement aspects of the EPIC projects. Verified costs were reasonably supported with underlying documentation such as contractor invoices, timesheets, and receipts, and associated with a vendor contract. We noted catering charges to two projects—$471 related to Project 1 and $400 related to Project 2 that according to SDG&E were required for working business and team meetings.

  According to SDG&E, contractor overhead charges are not separately identified, but are included in the hourly rates reflected in the cost proposals submitted in response to solicitations and in contract terms and conditions. As a result, we were unable to identify the administrative overhead costs charged by contractors separate from the direct project costs.

- **SDG&E Direct Project Labor:** Identified the types of activities associated with the expenses, which related to SCE employees working directly on EPIC projects, including engineers, IT program managers, and team leads. Verified costs were reasonably supported with underlying timesheet documentation and the charges were supported.
- **Materials:** Identified the types of costs, which generally related to electronic equipment and technology. Verified costs were reasonably supported with underlying documentation such as invoices and receipts, and costs appeared reasonable and related to the project.
- **Employee Reimbursables/Travel:** Identified the types of costs, which largely related to lodging, airfare, and rental cars. Verified costs were reasonably supported with underlying documentation such as travel expense claims, travel receipts, and invoices and costs appeared reasonable and related to the projects.

Overall, we found SDG&E's project expenses reviewed appeared generally reasonable, related to EPIC project activities, and were supported by underlying documentation.

Overhead Costs Charged to Projects Varied Across Administrators

For internal overhead costs charged directly to EPIC projects by the administrators—expenses that relate to EPIC project work, but not to one specific project—we performed a high-level review of the costs to gain an understanding the types and amounts of overhead charges and the basis for the calculations.

It is important to note that the amount of overhead charged across EPIC projects can vary, particularly due to amount of time the employees of the administrators spend working directly on the projects versus the use of external contracted services. Specifically, projects relying largely on administrator staff labor involve higher amounts of internal overhead costs charged than projects relying heavily on contracted services as contract labor is not eligible for certain overhead charges, such as paid time off and benefits. Also, overhead cost components charged to EPIC projects can also vary depending on the specific types and amounts of expenditures.

Overall, while CEC did not charge internal overhead directly to projects, the amounts and types of internal overhead costs charged by the IOUs to their EPIC projects varied across the three administrators.

PG&E Applied 15 Percent Internal Overhead on Projects Reviewed

Prior to late 2015, PG&E utilized a fully loaded labor rate where its internal overhead costs were included in employee hourly rates charged to EPIC projects as part of direct labor. Subsequently, to improve the transparency of its overhead charges, PG&E updated its internal overhead cost allocation process to charge these costs separately to EPIC projects via individual overhead components. PG&E's overhead is largely made up of labor overhead related to operation management and support and benefits and payroll taxes. Other components include non-labor overheads, such as building services, IT devices, material burden, and fleet services. PG&E stated that direct labor charges are based on the number of hours worked multiplied by a rate determined by the company and now include only salaries paid to employees without any additional overhead or labor loaders.

Of the four PG&E EPIC projects selected for review (reflected in Exhibit 10), we also reviewed the internal overhead costs charged to two of the projects where the updated overhead cost allocation process was utilized. We found the total internal overhead charged by PG&E on the two EPIC projects reviewed were very consistent, each reflecting 15 percent of project costs, as shown in Exhibit 13.

EXHIBIT 13. PG&E'S INTERNAL OVERHEAD COSTS CHARGED ON PROJECT 3 AND 4

Project	Direct Project	PG&E Overhead Costs	Total Project Costs	Percent OH of Total Project Costs
3	$453,522	$80,592	$534,113	15%
4	$2,175,698	$374,338	$2,550,036	15%

PG&E's internal overhead cost components charged to the two projects are reflected in Exhibit 14.

EXHIBIT 14. PG&E'S INTERNAL OVERHEAD COST COMPONENTS FOR PROJECTS 3 AND 4

Project	PG&E Internal Overhead Cost Components						Total
	Operation Management & Support	Benefits & Payroll Taxes	Fleet Services	Building Services	IT Devices	Material Burden	
3	$10,203	$54,969	$0	$7,006	$3,610	$4,804	$80,592
4	$130,140	$150,946	$60,796	$20,840	$11,616	$0	$374,338

While some overhead costs, such as material burden, are driven by the amount of material costs charged to a project, we found that PG&E's direct labor activity on the EPIC projects, including straight time and overtime, was the driver of the majority of the overhead cost charges. For example, the calculation associated with PG&E's March 2017 fleet overhead costs of $97,359 charged to EPIC Project 4 is shown in Exhibit 15.

EXHIBIT 15. PG&E'S MARCH 2017 FLEET OVERHEAD CALCULATION FOR PROJECT 4

PG&E's Direct Labor Charge for March 2017	PG&E's Fleet Overhead @ 22.69%
$429,084	$97,359[13]

Other types of PG&E's internal overhead costs are also calculated largely based on direct labor costs, but also involve additional cost components that are based on other overhead costs that were charged to the projects. For example, as shown in Exhibit 16, PG&E's March 2017 building services overhead cost of $19,931 charged to EPIC Project 4 includes operation management and support overhead and fleet overhead charges as PG&E's vehicle assets and management support employees utilize building facilities.

EXHIBIT 16. PG&E'S MARCH 2017 BUILDING SERVICES OVERHEAD CALCULATION FOR PROJECT 4

Cost Category	Charge for March 2017	PG&E's Building Services Overhead @ 3.13%
PG&E Direct Labor	$429,084	$13,430
Operation Management and Support Overhead	$110,361	$3,454
Fleet Overhead	$97,359	$3,047
Total		**$19,931**

SCE Applied Between 1 and 4 Percent Internal Overhead on Projects Reviewed

SCE charged internal overhead costs directly to its EPIC projects that include a variety of individual components, but is largely made up of labor overhead related to employee paid absence charges. Other components include non-labor overheads, such as procurement services, building repair and maintenance, and tool expenses. SCE allocates a majority of its overhead costs by applying a fixed percentage to direct labor costs. SCE stated that direct labor charges include only salaries paid to employees and do not include any additional overhead or labor loaders beyond paid absences.

Of the two SCE EPIC projects selected for review (reflected in Exhibit 11), we also reviewed SCE's internal overhead costs charged to the two projects. We found the total internal overhead charged by SCE on the two EPIC projects reviewed were fairly consistent reflecting 1 and 5 percent of total project costs, as shown in Exhibit 17.

EXHIBIT 17. SCE'S INTERNAL OVERHEAD COSTS CHARGED ON PROJECT 1 AND 2

Project	Direct Project Costs	SCE Overhead Costs	Total Project Costs	Percent OH of Total Project Costs
1	$4,959,646	$282,616	$5,242,262	5%
2	$1,791,346	$17,978	$1,809,324	1%

SCE's internal overhead cost components charged to the two projects are reflected in Exhibit 18.

[13] Fleet overhead in March 2017 is higher than total fleet overhead in Exhibit 14 due to a credit in February 2017.

EXHIBIT 18. SCE'S INTERNAL OVERHEAD COST COMPONENTS FOR PROJECTS 1 AND 2

Project	SCE's Internal Overhead Cost Components					Total
	Paid Absences	Procurement Services	Building Repair & Maintenance	Tool Expenses	T & D Overall Supply	
1	$257,259	$5,595	$0	$13,747	$6,015[14]	$282,616
2	$17,785	$1	$192	$0	$0	$17,978

SCE's stated that paid absences overhead, its largest overhead allocation, is a fixed corporate rate labor that is adjusted at the end of the year and is typically around 20 percent of straight time labor. As shown in Exhibit 19, paid absence overhead charged on Project 1 and 2 was 22 percent and 20 percent respectively.

EXHIBIT 19. SCE'S TOTAL PAID ABSENCE OVERHEAD CALCULATION FOR PROJECT 1 AND 2

Project	Project Straight Time Labor Charges	Paid Absences Overhead %	Total Overhead Charge
1	$1,149,679	22%	$257,259
2	$87,538	20%	$17,785

Direct labor charged to Project 1 was $523,947 (see Exhibit 11), which included $1,149,679 in straight time, $37,934 in overtime, and $663,666[15] in labor corrections. However, the correction included only $15,209 in paid absences overhead, or 2 percent of the corrected labor charges. According to SCE, manual processes inadvertently excluded paid absences charges from the labor correction and affected multiple EPIC projects between 2016 and 2017. As a result, an additional total of $558,321 in paid absence overhead charges will be removed from SCE's EPIC program.

SDG&E Applied Less than 1 Percent Internal Overhead on Projects Reviewed; However, Some Overhead Costs Incurred Were Not Charged to the EPIC Program

SDG&E charged internal overhead costs directly to its EPIC projects that involved only vacation and sick leave and payroll taxes—these labor-related overheads are charged by applying a fixed percentage to direct labor costs. SDG&E stated that direct labor charges include only salaries paid to employees and do not include any additional overhead or labor loaders.

Of the two SDG&E EPIC projects selected for review and reflected in Exhibit 12, we reviewed SDG&E's internal overhead costs charged to the two projects. We found the total internal overhead charged by SDG&E on the two EPIC projects reviewed were fairly consistent reflecting less than one percent of total project costs, as shown in Exhibit 20.

[14] Costs associated with Technology & Demonstration safety, business planning, metrics and reliability reporting.
[15] The labor correction largely related to reconciling labor costs recovered through the General Rate Case and EPIC program.

EXHIBIT 20. SDG&E'S INTERNAL OVERHEAD COSTS CHARGED ON PROJECT 1 AND 2

Project	Direct Project Costs	SDG&E Overhead Costs	Total Project Costs	Percent OH of Total Project Costs
1	$1,395,824	$10,017	$1,405,841	0.7%
2	$2,023,553	$8,597	$2,032,150	0.4%

SDG&E indicated that the number of hours worked by its employees (organization-wide) determines the vacation and sick leave requirement and corresponding overhead rate to apply against straight time labor hours and the straight time portion of overtime. The payroll tax overhead is based on employee wages and, as such, is consistently applied across all labor charges and reflects SDG&E's tax liability. SDG&E's internal overhead cost components charged to the two projects are reflected in Exhibit 21.

EXHIBIT 21. SDG&E'S INTERNAL OVERHEAD COST COMPONENTS AND TOTAL PAID ABSENCE OVERHEAD CALCULATION FOR PROJECTS 1 AND 2

<table>
<tr><th>Project</th><th>Total Direct Labor Charge</th><th>Overhead Type</th><th>Overhead Charge</th><th>Overhead Percent</th><th>Total Project Overhead</th></tr>
<tr><td rowspan="2">1</td><td rowspan="2">$38,234</td><td>Vacation and Sick Leave</td><td>$6,380</td><td>17%</td><td rowspan="2">$10,017</td></tr>
<tr><td>Payroll Taxes</td><td>$3,637</td><td>10%</td></tr>
<tr><td rowspan="2">2</td><td rowspan="2">$33,350</td><td>Vacation and Sick Leave</td><td>$5,518</td><td>17%</td><td rowspan="2">$8,597</td></tr>
<tr><td>Payroll Taxes</td><td>$3,079</td><td>9%</td></tr>
</table>

Additionally, according to SDG&E, it incurs additional overhead expenses arising from direct labor, but does not charge those costs to the EPIC projects to avoid double recovery. Specifically, all of SDG&E's overhead costs, except payroll taxes and vacation and sick leave, are recovered through a mechanism outside of the EPIC program through the company's General Rate Case fixed cost accounts, which is the process that IOUs go through to request funding for its base business. Because some overhead related to EPIC project work is captured and recovered outside of the EPIC program, the true cost of SDG&E's EPIC overhead is understated as these expenses are not reflected in its EPIC expenditure information. SDG&E stated while direct labor is charged directly to EPIC, they do not have a process that will allow all of its EPIC overhead costs to be captured and recovered separately from its General Rate Case fixed cost accounts.

Controls in Place Over Processes to Approve Project Expenses

Based on discussions with the four administrators and our review of policies, procedures, and documents, we found that processes were in place to control EPIC project expenses. For instance, CEC requires all EPIC projects to be formally approved at business meetings and corresponding project expenditures be encumbered and associated with an executed contract. As CEC's direct project costs relate solely to expenditures arising from invoices submitted by external contractors, CEC tracks its project costs in one special revenue fund under local assistance. Additionally, our review of contractor invoices revealed CEC has a robust invoice review process where invoices are reviewed by a Project Lead to ensure vendor charges align with work performed and noted that CEC routinely excludes invoiced charges deemed unreasonable or not supported. We identified several tools used to evaluate progress and ensure costs are appropriate such as invoice review checklists and monthly progress reports that describes various items such as tasks completed, tasks to be completed in the next period, and significant challenges. We also noted invoices submitted to CEC underwent several levels of supervisory approval, including Energy Research and Development Division (ERDD) management and CEC's Accounting Office, before payments were issued. According to CEC, an internal auditor also reviews and audit EPIC grant and contract expenditures.

Additionally, the three IOUs also have controls in place. For example, the IOUs require EPIC project expenditures to be associated with an executed contract and submitted invoices reviewed by project leads to ensure vendor charges are appropriate and align with work performed. Related to labor costs charged to the EPIC projects, SCE and SDG&E employees enter time worked into a time management system that interfaces with their financial system while PG&E employees submit timesheets directly into their financial system, SAP. Also, employees submit expenses for reimbursement, such as travel, directly into expense management systems. Each IOU has internal authority thresholds and policies to determine the required supervisory and/or management approvals and utilize automated systems to route expenditures through system workflow processes to obtain required approvals.

Overall, EPIC project expenditures revealed that expenses were generally reasonable, supported by underlying documentation, and related to the projects; however, we noted one instance where SCE did not correct a portion of paid absence overhead charged to EPIC, and CEC did not require hourly labor support from minor subcontractors with expenses under $100,000. Additionally, the EPIC program may benefit from additional CPUC guidance related to allowable costs to ensure ratepayer funds are expended prudently and in accordance with program objectives.

Recommendations:

To further improve consistency in controls over EPIC expenses and ensure ratepayer funds are expended prudently and are in line with the intent and goals of the program, the CPUC should consider:

6. Collaborating with the four administrators to develop cost guidance related to the allowable use of EPIC project funding. Guidelines should provide sufficient flexibility given differences in the types of projects undertaken by the administrators while providing adequate parameters reflecting the acceptable use of funding.
7. Requiring CEC to maintain complete support for all project expenses, including subcontractors.
8. Requiring SCE to correct labor overhead amounts charged to their EPIC Project 1 (see Exhibit 19) associated with the labor correction.

Finding #5: Administrative Costs Appear Generally Supported and Reasonable

In addition to costs charged directly to EPIC projects described in Finding #4, the administrators also charge expenses that are administrative in nature—costs support the EPIC programs as a whole, but are not related specifically to performing EPIC project work, such as preparing investment plans, selecting research projects, and reporting on program information to CPUC, among other administrative activities.

CPUC decisions detail the approved EPIC budgets for each of the four administrators, including funding slated to be spent on administrative costs, as shown in Exhibit 22. While the three IOUs retain their portion of EPIC collections for administrative funding, the Legislature must grant the CEC spending authority to use EPIC funds to pay for administrative expenses.

EXHIBIT 22. EPIC ADMINISTRATION FUNDING BUDGET BY ADMINISTRATOR

	EPIC 1	EPIC 2	EPIC 3	Total
CEC	$36,900,000	$40,782,600	$44,400,000	$122,082,600
PG&E	$4,807,847	$5,082,479	$5,533,295	$15,423,620
SCE[16]	$3,944,162	$2,124,458	$4,539,290	$10,607,910
SDG&E[17]	$844,492	$633,731	$971,916	$2,450,139
Total	**$46,496,501**	**$48,623,268**	**$55,444,501**	**$150,564,269**

We reviewed of a sample of administrative costs charged by the four administrators to determine if the expenses were accurate, supported, and reasonably related to the administration of the EPIC program. Overall, we found that the administrative costs were generally supported with underlying documentation such as invoices, receipts, and timesheets, however, we identified one instance one IOU was overcharged a small amount and CEC could enhance its documentation retention practices. In addition, we noted a general lack of guidance from CPUC to the administrators related to administrative costs.

Lack of Formal Guidance to Administrators Related to Expending EPIC Administrative Funding

CPUC decisions provide general guidance related to the types of administrative costs that EPIC funding may be used, including staffing costs, associated general and administrative and overhead expenses, and related contracting costs to prepare the investment plans, conduct solicitations, select funding recipients, and monitor and oversee the progress of projects and investments. CPUC decisions describe administrative activities as those that make the energy innovation investments possible and effective. Along with the related recommendation presented in Finding #4 related to the need for project expenses guidelines, CPUC should consider including additional details and parameters for expending EPIC funding on administrative activities.

[16] Includes a $2,045,000 shift from SCE's administration to project budget.
[17] Includes a $259,000 shift from SDG&E's administration budget to project budget.

CEC's Administrative Costs Charged to EPIC Appeared Generally Reasonable and Supported, Although Better Documentation Would Improve Practices

All of CEC's EPIC administrative expenses are incurred by its internal staff (except for one external professional service contract for technical support). As shown in Exhibit 23, EPIC administrative expenses are charged either directly to the EPIC program via CEC's special revenue fund—Fund 3211—or indirectly through an overhead cost center that is distributed to EPIC Fund 3211 as part of the cost allocation process.

EXHIBIT 23. LISTING OF CEC'S KEY EPIC ADMINISTRATIVE COST CATEGORIES AND CHARGE METHODS

Key Expenditure Categories	Direct Charge	Indirect Charge	Method for Charging Expenditures
Salaries & Benefits	✓	✓	82 positions in ERDD & 8 positions in other areas (accounting, legal, contracts) are directly charged—all hours by these employees are charged to administrative expenses, including technical oversight functions. Other executive positions or department support staff are indirectly charged through the cost allocation process.
General Overhead		✓	Use approved indirect cost rate (ICRP); includes costs related to EPIC grant and contracting efforts provided by Executive Office, Legal, Accounting, Public Communications, Facilities, and Government Affairs.
Facilities Operations; Postage & Printing; Other		✓	Monthly cost allocation process.
Rents & Leases	✓		Based on the number of budgeted positions for the program.
Central Service (Prorata) and FI$Cal Assessment	✓		Annual charges from Department of Finance for administrative functions and services provided by the State.
IT Technology	✓	✓	Some direct costs in Fiscal Year 2016/2017 due to FI$Cal preparation/implementation. Indirect charges through monthly cost allocation process.
Communications	✓	✓	Some direct for ERDD management cell phones. Indirect charges through monthly cost allocation process.
Travel	✓		Employee travel costs through California Automated Travel Expense Reimbursement System (CalATERS).
Training	✓		Minimal Amounts directly charged

As of June 30, 2019, CEC expended $69,355,436 on administrative costs associated with their EPIC program. As shown in Exhibit 24, we reviewed administrative expenditures totaling $14,854,307, or 21 percent of CEC's total administrative costs focusing on larger expenditure categories—rent/leases, salaries and benefits, and central services.

EXHIBIT 24. CEC EPIC ADMINISTRATIVE COSTS TESTED

Expenditure Category	Total Costs	Amount Tested	Percent Tested
Salaries and Benefits	$53,227,193	$10,894,708	20%
General Overhead	$9,015,412	-	-
Rent & Leases	$2,716,370	$2,310,022	85%
Other Miscellaneous	$1,942,293	-	-
Central Service (Prorata)	$1,571,577	$1,571,577	100%
Travel & Vehicle	$229,749	-	-
Office Supplies and Equipment	$185,745	-	-
IT Technology, Software, Etc.	$172,159	-	-
FI$Cal Assessment	$78,000	$78,000	100%
Consulting & Professional Services	$76,210	-	-
Training, Conferences, Tuition	$74,133	-	-
Communications & Phones	$51,077	-	-
Facilities Operations	$15,517	-	-
Total	**$69,355,436**	**$14,854,307**	**21%**

For each administrative cost selected for testing, we:

- **Salaries and Benefits:** Verified employees via employee rosters, org charts, and government salary information. In general, we found that labor charges were appropriate, but one employee could not be identified in support documents. However, CEC provided hire/separation dates to confirm the employee's employment—thus, there is no issue to report.
- **Rent & Leases:** Verified rent charges were supported with rent schedules and documentation showing budgeted positions.
- **FI$Cal Assessment costs:** Validated costs against various CALSTARS reports.
- **Central service costs:** Validated costs against annual Department of Finance letters showing quarterly charges.

Overall, CEC's administrative expenses reviewed appeared generally reasonable, related to the administration of the EPIC program, and supported by underlying documentation.

While we found CEC's administrative costs to be reasonable and supported, CEC should strengthen its document retention practices to maintain additional cost support for its labor distribution and indirect cost allocation processes for non-labor charges to the EPIC program. Specifically, while CEC stated it reviews and adjusts its labor distribution methodology for salary and benefit costs on an annual basis by reviewing system coding/reports to link positions and employees with applicable charge units, it could not provide us access to the system coding either because the legacy system reports could not be accessed or hard copies showing system distributions were destroyed because they included social security numbers.

Similarly, CEC did not retain documentation for its indirect cost allocation process methodology demonstrating the programming for automated system distribution of non-labor costs, such as general overhead, postage, and facilities, captured in overhead object codes to various CEC programs and funds—including EPIC Fund 3211.

To strengthen the integrity of its process and improve retention practices, on a go-forward basis, CEC should investigate how to acquire the needed system reports from the FI$Cal system and/or maintain and secure coding/distribution documentation that supports EPIC charges in the fiscal system.

PG&E's Administrative Costs Appeared Generally Reasonable and Supported with Underlying Documentation

PG&E's EPIC administrative expenses are incurred by its internal staff as well as external consultants. As shown in Exhibit 25, PG&E's EPIC administrative expenses are charged either directly to the EPIC fund or indirectly through a cost allocation process.

Exhibit 25. Listing of PG&E's Key EPIC Administrative Cost Categories and Charge Methods

Key Expenditure Categories	Direct Charge	Indirect Charge	Method for Charging Expenditures
Contracted Services	✓		External contracted services directly charged.
Labor	✓		Program management and administrative support charge time directly based on the hours worked performing general EPIC tasks.
Labor Overhead		✓	Overhead calculated by the system each month based on labor costs and the overhead rate.
Non-Labor Overhead		✓	Overhead calculated by the system each month based on eligible costs and the overhead rate.
Employee Travel/Reimbursements	✓		Related to program management travel directly charged.

As of December 31, 2019, PG&E expended $7,481,361 million on administrative costs associated with their EPIC program. As shown in Exhibit 26, we reviewed administrative expenditures totaling $750,621, or 10 percent of PG&E's total administrative costs focusing on larger expenditure categories—contracted services, labor, and employee reimbursable/travel.

EXHIBIT 26. PG&E EPIC ADMINISTRATIVE COSTS TESTED

Expenditure Category	Total Costs	Amount Tested	Percent Tested
Contracted Services	$1,463,300	$595,407	41%
Labor	$3,157,315	$154,744	5%
Labor Overhead	$2,331,846	$0	0%
Non-Labor Overhead	$525,705	$0	0%
Employee Travel/Reimbursements	$2,810	$384	14%
Conference Facility Charge	$215	$0	0%
Other Expenses[18]	$170	$86	51%
Total	**$7,481,361**	**$750,621**	**10%**

For each administrative cost selected for testing, we:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to consultants conducting business plan development, project approval, and steering committee preparations. Verified costs were reasonably supported with underlying documentation such as contractor invoices, timesheets, and receipts and the costs were associated with a vendor contract.
- **PG&E Labor:** Identified the types of activities associated with the expenses, which related to PG&E employees, including a business analyst, engineer, and EPIC program manager, performing activities, such as participation in stakeholder meetings, EPIC program reporting, and audio-visual technician work. Verified costs were reasonably supported with underlying timesheet documentation.
- **Employee Reimbursable/Travel:** Identified the types of costs, which related largely to program management lodging, airfare, mileage reimbursements, and conferences. Verified costs were reasonably supported with underlying documentation, such as travel expense claims, travel receipts, and invoices and that the costs appeared related to the projects.

Overall, PG&E's administrative expenses reviewed appeared generally reasonable, related to the administration of the EPIC program, and supported by underlying documentation.

SCE Administrative Costs Appeared Mostly Reasonable and Supported with Underlying Documentation

SCE's EPIC administrative expenses are incurred by its internal staff as well as external consultants. As shown in Exhibit 27, SCE's EPIC administrative expenses are charged either directly to the EPIC fund or indirectly through a cost allocation process.

[18] Includes permits and fees, telephone, vehicle rents, and other expenses.

EXHIBIT 27. LISTING OF SCE'S KEY EPIC ADMINISTRATIVE COST CATEGORIES AND CHARGE METHODS

Key Expenditure Categories	Direct Charge	Indirect Charge	Method for Charging Expenditures
Contracted Services	✓		External contracted services directly charged.
Legal Services	✓		External legal services directly charged.
SCE Labor	✓		Program management and administrative support charge time directly based on the hours worked performing general EPIC tasks.
Labor Overhead		✓	Overhead calculated by the system each month based on labor costs and the overhead rate.
Non-labor Overhead[19]		✓	Overhead calculated by the system each month based on eligible costs and applied overhead rates.
Employee Reimbursable/Travel	✓		Related to program management travel directly charged.
Memberships-General	✓		Consortia memberships directly charged.

As of December 31, 2019, SCE expended $4,621,507 million on administrative costs associated with their EPIC program. As shown in Exhibit 28, we reviewed administrative expenditures totaling $474,819, or 10 percent of SCE's total administrative costs focusing on larger expenditure categories—contracted and general support services, labor, and employee reimbursable/travel.

EXHIBIT 28. SCE EPIC ADMINISTRATIVE COSTS TESTED

Expenditure Category	Total	Amount Tested	% Tested
Contracted Services	$3,409,857	$452,084	13%
Legal Services	$43,767	$2,824	6%
SCE Labor	$748,310	$16,994	2%
Labor Overhead	$242,540	-	0%
Non-labor Overhead	$8,004	-	0%
Employee Reimbursable/Travel	$67,896	$2,917	4%
Memberships-General	$75,250	-	0%
Procurement Services	$1,652	-	0%
EIX Only	$20,273	-	0%
Miscellaneous[20]	$3,958		0%
Total	**$4,621,507**	**$474,819**	**10%**

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[19] Includes expenses for tools and support from the Compliance Management Office

[20] Includes A/P accrual/reversals, other general expenses, office support, and material management services

For each administrative cost selected for testing, we tested for accuracy, reasonableness, and underlying support validating the cost as follows:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to consultants working on project management plans, schedules, procurement plans, and financial management. Verified costs were reasonably supported with underlying documentation such as contractor invoices, timesheets, and receipts and the costs were associated with a vendor contract.
- **SCE Labor:** Identified the types of activities associated with the expenses, which related to SCE employees, such as manager, engineer, and accountant/auditor performing project management and IT activities. According to SCE, the EPIC program manager labor is charged outside of the EPIC program through its general rate case. Verified costs were reasonably supported with underlying timesheet documentation.
- **Legal Services:** Identified the types of activities associated with the expenses, which related to legal services to assist with compliance management and matters involving intellectual property. Verified costs were reasonably supported with underlying documentation such as invoices.
- **Employee Reimbursable/Travel:** Identified the types of costs, which related largely to program management lodging, airfare, and a $700 charge related to a catered lunch provided during a monthly EPIC IT collaboration meeting. Verified costs were reasonably supported with underlying documentation such as travel expense claims, travel receipts, and invoices and that costs appeared related to the projects.

Overall, SCE's administrative expenses reviewed appeared generally reasonable, related to the administration of the EPIC program, and supported by underlying documentation with the exception of one minor discrepancy. Namely, an external contractor incorrectly invoiced SCE $101 for a hotel stay when actual charges reflected $91—resulting in a $10 overpayment to the vendor; SCE stated it inadvertently missed this discrepancy during the invoice review and the difference will be credited on the next invoice submitted to SCE.

SDG&Es Administrative Costs Appeared Generally Reasonable and Supported with Underlying Documentation

SDG&E's EPIC administrative expenses are incurred by its internal staff as well as external consultants and are charged to the EPIC program directly, shown in Exhibit 29.

EXHIBIT 29. LISTING OF SDG&E'S EPIC ADMINISTRATIVE COST CATEGORIES AND CHARGE METHODS

Key Expenditure Categories	Direct Charge	Indirect Charge	Method for Charging Expenditures
Contracted Services	✓		External contracted services directly charged.
SDG&E Labor	✓		Program manager and administrative support charge time directly based on the hours worked performing general EPIC tasks.
Labor Overhead		✓	Organization-wide payroll tax and vacation and sick leave overhead indirectly charged based on labor hours.
Dues	✓		Dues directly charged.
Employee Reimbursable/Travel	✓		Related to program management travel (and some local administrative support travel) directly charged.
Materials	✓		Minimal materials purchased directly charged.

As of December 31, 2019, SDG&E expended $1,612,185 on administrative costs associated with their EPIC program. As shown in Exhibit 30, we reviewed administrative expenditures totaling $161,614, or 10 percent of SDG&E's total administrative costs, related to SDG&E labor, contracted services, dues, materials, and employee reimbursable/travel.

EXHIBIT 30. SDG&E EPIC ADMINISTRATIVE COSTS TESTED

Expenditure Category	Total Costs	Amount Tested	% Tested
Contracted Services	$525,536	$105,061	20%
SDG&E Labor	$784,427	$34,679	4%
Labor Overhead	$199,125	$0	0%
Dues	$57,245	$20,200	35%
Employee Reimbursable/Travel	$43,929	$512	1%
Materials	$1,923	$1,162	60%
Total	**$1,612,185**	**$161,614**	**10%**

For each administration cost area selected for testing, we:

- **Contracted Services:** Identified the types of activities associated with the expenses, which generally related to consultants supporting the EPIC program, including maintaining the public EPIC website and SharePoint system, maintaining equipment, and assisting with EPIC workshops. Verified costs were reasonably supported with underlying documentation, such as contractor invoices, timesheets, and receipts and the costs were associated with a vendor contract.
- **SDG&E Labor:** Identified the types of activities associated with the expenses, which related to SDG&E employees, Senior Technical Development Advisor, Team Lead, and EPIC program manager, performing activities, preparing investment plans, reporting information in annual reports, selecting

research projects, responding to data requests, hosting EPIC workshops, overseeing project teams, and providing administrative support. Verified costs were reasonably supported with underlying timesheet documentation.

- **Materials/Dues:** Identified the types of costs, which included fire protection equipment required to keep staff safe during visits to project sites and storage materials. Verified costs were reasonably supported with underlying documentation such as invoices and receipts and that costs appeared reasonable related to the project.
- **Employee Reimbursables/Travel:** Identified the types of costs, which related largely to program management lodging, airfare, and rental cars. Verified costs were reasonably supported with underlying documentation such as travel expense claims, travel receipts, and invoices and that costs appeared related to the projects.

Overall, SDG&E's administrative expenses reviewed appeared generally reasonable, related to the administration of the EPIC program, and supported by underlying documentation.

Controls in Place Over Processes to Approve Administrative Expenses

The four administrators had processes in place that align with general industry practices to ensure controls over administrative expenses. For instance, CEC requires purchase requests related to directly charged administrative expenses to generally be preapproved. Specifically, purchase orders and travel requests are typically approved by supervisors and managers through the purchase requisition system or through the State's on-line travel CalATERS system. Training and IT related requests must be on unique forms, such as the Energy Commission's Training Request Form, and must be approved by a supervisor, manager, Assistant Deputy Director, and Division Liaison. Further, requests over $500 must be approved by the Assistant Deputy Director and requests over $1,000 must be approved by the Deputy Director. The Accounting Office processes payments after performing a three-point match between the approved purchase request, invoice or receipt, and evidence of service provided or good received.

For CEC's administrative costs charged indirectly, an ICRP rate—calculated by dividing total indirect costs by the total direct expenses—is applied to total personal services and operating expenses of CEC's special funds, including EPIC Fund 3211. Further, allocation methodologies are established at the beginning of the fiscal year so that indirect costs coded by the system are automatically distributed to the correct fund based on supervisory approval of timesheets, invoices, or other charges.

The review and approval processes associated with the three IOUs administrative expenses are the same processes involved with approving project expenses as described in Finding #4.

In sum, our review of the administrative expenses charged to the EPIC program revealed expenses were generally reasonable and supported, but there was one instance where SCE was overcharged. In addition, opportunities exist for CEC to improve its documentation retention practices and the EPIC program in general may benefit from enhanced guidance related to administrative costs.

Recommendations:

To further improve consistency in controls over EPIC expenses and ensure ratepayer funds are expended prudently and are in line with the intent and goals of the program, the CPUC should consider:

9. In conjunction with recommendation 6 in Finding #4, collaborating with the four administrators to develop cost guidance related to the allowable use of EPIC project funding. Guidelines should provide sufficient flexibility given differences in the types of projects undertaken by the administrators while providing adequate parameters reflecting the acceptable use of funding.
10. Requiring CEC to maintain sufficient documentation to support labor distribution charges to EPIC.

Finding #6: CPUC EPIC Oversight Personnel Costs Were Not Always Consistent with Actual Time Spent by Staff

As previously described, CPUC decisions established that 0.5 percent of EPIC funding be remitted to CPUC to conduct oversight of the EPIC program. As shown in Exhibit 3, $7,658,914 of total EPIC funding is reserved for oversight activities.

According to EPIC decisions, oversight funding is to be used for CPUC's personnel expenses related to dedicated staff devoted to EPIC oversight as well as the cost of an independent evaluation of the EPIC program. According to CPUC Energy Division management, CPUC's oversight activities have largely related to costs associated with staff reviewing and approving triennial investment plans submitted by the four EPIC administrators as well as time attending EPIC project workshops, facilitating coordination efforts among the administrators, reviewing project changes and status updates, developing a request for proposals and selecting a contractor to facilitate the EPIC Policy + Innovation Coordination Group (PICG). In 2016, CPUC hired an independent contractor to evaluate EPIC program management and effectiveness, focusing on program management and administration as well as program processes related to solicitations, investment plans, and project evaluations.

Our review found that between July 1, 2012 through December 31, 2019, CPUC spent $1,865,519 on oversight activities, most spent on consulting services:

- Consulting Services—$1,246,163, or 67 percent, was expended on an independent evaluation of the EPIC program as required by CPUC decisions.
- Operating expenses and equipment—$45,575, or 2 percent which included indirect distribution costs and travel expenses such as flights, conferences, and rental cars.
- Salaries and Benefits —$573,781, or 31 percent, was expended on CPUC personnel expenses. Between Fiscal Years 2012 and 2019, a total of nine employees dedicated a portion of their time overseeing EPIC activities—a combined total ranging between 0.33 and 0.99 full-time equivalents (FTE) each year. A portion of the personnel costs associated with CPUC Energy Division management and staff assigned to conduct EPIC oversight is automatically charged to the EPIC program based on percentages programmed into the financial system.

To determine if the personnel costs charged to EPIC were consistent with time spent conducting oversight, we compared the time spent by the two staff members performing oversight activities in 2018 and 2019 per timesheets to amounts automatically charged to the program via the pre-set percentages. Because CPUC management does not track time at the individual program level on timesheets, the focus of this comparison was on time spent by staff and those corresponding charges to the program. Our comparison found that the personnel costs charged to EPIC oversight for one of the two employees did not always agree with time spent on the program per hours reflected on their timesheets. Specifically, 20 percent of personnel costs associated with one employee was charged to EPIC oversight in May 2019 and June 2019, but the employee spent an average of 75 percent of their time working on the program in these two months according to timesheets. Specifically, $5,675 was charged to EPIC over the two-month period, but $21,282 should have been charged—an undercharge to EPIC oversight of $15,607.

For the second employee, amounts charged to EPIC was reasonably consistent with the time spent performing oversight activities.

Consequently, our review found that some EPIC oversight was likely charged to CPUC Energy Division due to the labor distribution rules. According to CPUC's Fiscal Office, if the time actually worked is different than the percentage programmed in the financial system, staff are required to submit timesheets to the Accounting Unit so pre-programmed allocations can be overridden; however, this process does not appear to have been followed as the labor distribution rules were not manually adjusted to account for the actual time spent.

Recommendations:

To improve the accuracy of oversight charges to EPIC, CPUC should consider:

11. Requiring CPUC program management to implement a process to review labor distribution rules to ensure charges to the EPIC program reasonably align with the actual time spent by employees on EPIC oversight activities.

Finding #7: Funding Available Appears Sufficient to Complete Projects, but CEC May Exceed Administrative Cap and CPUC Underutilized Oversight Budget

CPUC decisions require that no more than 10 percent of each administrator's total EPIC funding be used on costs that are administrative in nature. Exhibit 31 reflects the composition of each administrator's administrative budget and project budget.

EXHIBIT 31. ADMINISTRATION AND PROJECT BUDGETS AS A PERCENTAGE OF TOTAL EPIC BUDGET

	Administration Budgets	Project Budgets	Total EPIC Budget
CEC	$122,082,600	$1,094,184,500	**$1,216,267,100**
	10%	90%	
PG&E	$15,423,620	$138,812,580	**$154,236,200**
	10%	90%	
SCE[21]	$10,607,910	$115,921,188	**$126,529,098**
	8%	92%	
SDG&E[22]	$2,450,139	$24,641,250	**$27,091,389**
	9%	91%	

We found that unspent EPIC funding appears generally sufficient to complete the remaining program projects. However, we noted that while CEC's administration expenses remain within 10 percent of its overall EPIC budget, its required spending may cause it to ultimately exceed its administration budget prior to the expiration of the EPIC program; at least one IOU voiced similar concerns. We noted a similar observation was made in 2019 by CPUC's Utility Audits, Risk, and Compliance Division.

While Remaining Funding Appears Sufficient to Cover EPIC Projects, CEC Administrative Costs Could Potentially Exceed Administrative Budget

As shown in Exhibit 32, as of December 31, 2019, each of the four administrators had spent well under 10 percent of their total EPIC budgets on administration expenses.

[21] Includes a $2,045,000 shift from SCE's administration to project budget; SCE's total EPIC budget remained unchanged.
[22] Includes a $259,000 shift from SDG&E's administration to project budget; SDG&E's total EPIC budget remained unchanged.

EXHIBIT 32. ADMINISTRATION AND PROJECT EXPENSES AS A PERCENTAGE OF TOTAL BUDGET AS OF 12/31/2019

	Administration Expenses	Project Expenses	Total EPIC Budget
CEC[23]	$69,355,436	$318,230,653	**$1,216,267,100**
	5.7%	26.16%	
PG&E	$7,481,361	$81,954,421	**$154,236,200**
	4.85%	53.14%	
SCE	$4,621,507	$66,864,205	**$126,529,098**
	3.65%	52.84%	
SDG&E	$1,612,186	$16,356,611	**$27,091,389**
	5.95%	60.38%	

Further, as shown in Exhibit 33, the three IOU's administration expenses were under 10 percent compared to total spent on EPIC expenses as of December 31, 2019; however, the CEC's percentage of expenses spent on administration had exceeded 10 percent.

EXHIBIT 33. ADMINISTRATION AND PROJECT EXPENSES AS A PERCENTAGE OF TOTAL EXPENSES OF 12/31/2019

	Administration Expenses	Project Expenses	Total Expenses
CEC	$69,355,436	$318,230,653	**$387,586,089**
	17.89%	82.11%	
PG&E	$7,481,361	$81,954,421	**$89,435,782**
	8.37%	91.63%	
SCE	$4,621,507	$66,864,205	**$71,485,712**
	6.46%	93.54%	
SDG&E	$1,612,186	$16,365,611	**$17,977,797**
	8.96%	91.03%	

As reflected in Exhibit 34, the three IOUs had expended nearly or more than 60 percent of their project budgets as of December 31, 2019 and had expended about the same percentage, or less, of their administration budget over the same time period. In other words, the three IOUs expended their project budgets at the same or faster rate than their administration budgets. Conversely, CEC expended less than 30 percent of its project budget, but had already expended 57 percent of its administration budget.

[23] CEC's expenses are as of 6/30/2019.

EXHIBIT 34. PROJECT AND ADMINISTRATIVE BUDGETS EXPENDED AS OF 12/31/2019

Administrator	Budget	Expenses	% of Budget Expended
Total Project Budgets and Expenses			
CEC	$1,094,184,500	$318,230,653	29%
PG&E	$138,812,580	$81,954,421	59%
SCE	$115,921,188	$66,864,205	58%
SDG&E	$24,641,250	$16,356,611	66%
Total Administration Budgets and Expenses			
CEC	$122,082,600	$69,355,436	57%
PG&E	$15,423,620	$7,481,361	49%
SCE	$10,607,910	$4,621,507	44%
SDG&E	$2,450,139	$1,612,186	66%

As such, while CEC's administration costs were within the 10 percent maximum cap with expenditures of approximately $69.4 million of the $122.1 of administrative costs budgeted (Exhibit 32), its administration expenses accounted for 18 percent of its total EPIC expenses (Exhibit 33) and had outpaced its project expenses by a good margin—29 percent to 57 percent—(Exhibit 34). According to CEC, its admin expenses are higher at the beginning of EPIC cycles due to time spent preparing solicitations, conducting grant selection processes, and initiating a project. Thus, it is logical to assume administration costs would be less in the final years of the program.

Additionally, CEC costs can be encumbered for two fiscal years and have an additional four fiscal years to liquidate EPIC funds under the state's budget authority—meaning, for the current EPIC 3 program ending December 2020 (which is state Fiscal Year 7/1/2020 to 6/30/2021), CEC could still spend administration funds as part of its efforts monitoring projects for an additional three fiscal years through 6/30/2024. Since the beginning of the EPIC program in Fiscal Year 2013/2014 (excluding Fiscal Year 2012/2013 as minimal costs were expended at start up), CEC spent approximately $11.5 million per fiscal year on average through Fiscal Year 2018/2019. If that spending rate continues, CEC's administration expenses could total $126.9 million[24] by the end of its EPIC 3 spending authority cycle in Fiscal Year 2023/2024—slightly more than $4.8 million, or almost 4%, of its $122.1 million administrative budget. A 2019 audit performed by CPUC's Utility Audits, Risk, and Compliance Division also observed that CEC may exceed its 10 percent administrative expenses cap prior to the expiration of the EPIC program.

Further, CEC indicated that not all administrative costs incurred are charged to their EPIC program due to the ten percent cap placed on the program and different funding sources may be used to pay administrative expenses to ensure the maximum cap is not exceeded. Even still, CEC acknowledges that it is possible

[24] Projection based $69.3 million in administration expenses as of the end of Fiscal Year 2018/19 + $57.5 million estimation of 5 years of average administration costs of $11.5 million annually from Fiscal Year 2019/20 through Fiscal Year 2023/24.

that the administrative funds for its EPIC projects may run out before all projects are complete and, in that case, CEC would request an increased administrative cap or would investigate utilizing additional alternative funding sources to complete the projects. CEC should closely monitor and report on the utilization of its actual administration expenses—specifically, its actual expenditures and not budgetary encumbrances or adjustments—in comparison with its $122.1 million administration budget.

EPIC Funding Available to Complete Current and Future Projects

The four EPIC administrators appear generally on track to complete their EPIC projects within the funding provided; however, a few administrators expressed concerns about having sufficient administration funding to support the program before the projects are completed.

CEC

As of June 30, 2019, CEC committed its entire EPIC 1, 2, and 3 project budgets totaling $1,094,184,550 for project solicitations, of which CEC had encumbered $714,638,745 on 346 specific projects through executed contracts. Exhibit 35 reflects CEC's total project commitments, funds encumbered, and amounts not yet encumbered.

EXHIBIT 35. CEC'S PROJECT BUDGETS AND ENCUMBRANCES AS OF 6/30/2019

Total Project Budgets	Funding Encumbered	Not Yet Encumbered
$1,094,184,500	$714,638,745	$379,545,755

As of June 30, 2019, CEC had $318,230,653 expended on the 346 projects:

- 147 were closed (or terminated) and reflected $192,802,088 in expenditures; these projects did not utilize $31,472,955 in encumbrances.
- 199 were still active and reflected $125,428,565 in expenditures, leaving $364,935,137 in available encumbrances for the remaining costs to complete these projects.

As such, CEC had $775,953,847 in project funding available to be used on current projects and encumbered on additional projects—$379,545,755 in approved project funding not yet encumbered (Exhibit 36) plus the $31,472,955 in unused encumbrances from the 147 closed projects noted above, plus $364,935,137 remaining encumbrances on active projects. Of the $775,953,847:

- $364,935,137 needed to complete the 199 active project contracts.
- $411,018,710 for future EPIC project contracts. According to CEC, it has planned solicitations to cover this amount.

If CEC consumes the $775.9 million available on completing currently active projects and future projects, $52.7 million will be available to cover additional administration expenses, which agrees with CEC's remaining administration budget as of June 30, 2019.[25]

[25] $122 million administration budget less $69.3 million in administration expenses as of June 30, 2019.

PG&E

As of December 31, 2019, PG&E expended $81,954,421 on project expenses associated with 42 projects, of which 9 were still active and required an estimated $18,034,906 to complete, leaving available $38,823,254 of its total EPIC project budget of $138,812,580 to spend on additional project activities. According to PG&E, an additional six or eight EPIC 3 projects are expected to be launched in 2020. As of the same time period, PG&E had expended $7,481,361 on administration expenses, leaving $7,942,259 remaining funding to spend on administrative expenses through the end of the program. PG&E is not currently concerned that the remaining administrative funding will be insufficient.

SCE

As of December 31, 2019, SCE expended $66,864,205 on project expenses associated with 48 projects, of which 23 were still active and required an estimated $45,461,659 to complete, leaving available $3,595,294 of its EPIC $115,921,188 total project budget to spend on additional project activities. According to SCE, while no additional projects are planned, some active EPIC 3 projects are still in the planning phase and the remaining available funding is earmarked to further support completing these projects. As of the same time period, SCE expended $4,621,507 on administration expenses, leaving $5,986,403 remaining funding to spend on administrative expenses through the end of the program.

According to SCE, $2,045,000 of their EPIC 1 administration budget was transferred to their project budget in 2018 as a result unspent administration funding due to timing issues between the EPIC phases. While SCE's total EPIC 1 budget remained unchanged as the shift occurred just between their administration and project budgets, SCE has $2,045,000 less in total administration funding available to complete their projects than originally anticipated; however, SCE is not currently concerned that the remaining administrative funding will be insufficient.

SDG&E

As of December 31, 2019, SDG&E expended $16,356,611 on project expenses associated with 15 projects, of which four were still active and required an estimated $8,286,180 to complete, resulting in SDG&E estimated to spend the entirety of its total EPIC project budget of $24,641,250. As of the same time period, SDG&E expended $1,612,186 on administration expenses, leaving $837,953 remaining funding to spend on administrative expenses through the end of the program. According to SDG&E, no additional EPIC 3 projects are planned.

According to SDG&E, $259,000 of their EPIC 2 administration budget was transferred to their project budget in 2017 as a result of unspent administration funding. While SDG&E's total EPIC 2 total budget remained unchanged as the shift occurred just between their administration and project budgets, SDG&E has $259,000 less in total administration funding available to complete their projects than originally anticipated and is concerned the remaining administrative funding will not be sufficient.

Overall, unspent EPIC funding appears generally sufficient to complete the remaining program projects. However, we noted some concerns related to the sufficiency of administration funding, particularly related to the administrative reporting requirements. At the outset of each investment period, CPUC should consider providing expanded guidance related to the types of administrative activities that will be required of the administrators by CPUC so that the parties can collectively determine if the administrative funding budgeted is sufficient to cover all required activities.

CPUC's Oversight Budget was Underutilized, but Additional Expenditures Expected

As mentioned earlier, the EPIC program dedicated 0.5 percent to CPUC to perform oversight activities, which equates to $7,658,914 in funding during EPIC 1 through EPIC 3 (2012 through 2020). Between July 1, 2012 and December 31, 2019, $6,825,010 was remitted by the IOUs to CPUC to fund EPIC oversight activities and an additional $833,904 slated to be remitted in 2020. We found that actual oversight expenses incurred between July 1, 2012 and December 31, 2019 totaled $1,859,597, or just 27 percent of the amount remitted during the period.

According to CPUC staff involved with performing oversight activities, additional expenditures will be incurred in 2020 in addition to on-going CPUC personnel costs, including a $1.1 million contract that was executed in December 2019 to establish and facilitate the PICG to enhance information sharing and increase coordination between EPIC administrators and CPUC. However, even with these additional expenditures, CPUC could have significant unspent oversight funding at the end of December 2020 associated with EPIC 1 through EPIC 3 remittances. CPUC stated that EPIC funding dedicated to oversight can continue to be expended beyond 2020 as additional EPIC cycles were approved in August 2020.

CPUC staff acknowledged that it is possible that too much EPIC funding may have been allocated to oversight efforts or that additional oversight activities could have been conducted with the additional funding—however, no guidance was available related to how oversight funding should be utilized, the types of activities that should be performed, or how to handle unspent oversight funds.

<u>Recommendations</u>:

To ensure optimal use of the allocated EPIC funding and full compliance with CPUC Decisions, the CPUC should consider:

12. Providing expanded guidance related to the types of administrative activities required of the administrators so that the parties can collectively determine if the administrative funding budgeted is sufficient to cover all required activities.
13. Requiring CEC to report on the utilization of its actual expenses rather than budgetary encumbrances or adjustments.
14. Ensuring any guidance available to CPUC staff charged with EPIC oversight responsibilities is sufficient regarding the types and frequency of required activities and assess whether the 0.5 percent oversight budget is appropriate.

Appendix A: Audit Response Letters

STATE OF CALIFORNIA Gavin Newsom, Governor

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

January 12, 2021

Angie Williams
Director, Utility Audits, Risk and Compliance Division
California Public Utilities Commission
400 R Street, Suite 221
Sacramento, CA 95811

CALIFORNIA PUBLIC UTILITIES COMMISSION RESPONSE TO PERFORMANCE AUDIT OF THE ELECTRIC PROGRAM INVESTMENT CHARGE (EPIC) PROGRAM

Dear Ms. Williams:

The California Public Utilities Commission (CPUC) Energy Division and Fiscal Office has reviewed the findings and recommendations of Sjoberg Evashenk draft report entitled, *Performance Audit of the Electric Program Investment Charge (EPIC) Program*.

The CPUC is pleased that the report found that the EPIC program is operating well and that the four EPIC administrators are generally following CPUC requirements. Energy Division staff will work with the CPUC's Fiscal Office and program administrators to determine which recommendation or recommendations from the audit can be most readily implemented. The CPUC may also consider whether to address any audit recommendations in the open proceeding (R.19-10-005) that is examining possible administrative improvements to EPIC. The CPUC is committed to continuous improvement of its program oversight.

The CPUC appreciates the work performed by Sjoberg Evashenk. If you have any further questions, please contact me at 415-757-7844.

Sincerely,

Rachel Peterson

Rachel Peterson
Executive Director

Pacific Gas and Electric Company
77 Beale St., Mail Code B13U
P.O. Box 770000
San Francisco, CA 94177

January 5, 2021

Angie Williams
Director Utility Audits, Risk and Compliance Division (UARCD)
California Public Utilities Commission
400 R Street, Suite 221
Sacramento, CA 95811

Dear Ms. Williams,

PG&E has received and reviewed the audit report, *Performance Audit of the Electric Program Investment Charge (EPIC) Program*. As described on p.3-4 of the report, Sjoberg Evashenk Consulting (the auditor), working on behalf of the California Public Utilities Commission (CPUC), conducted a comprehensive review of PG&E's EPIC program through a nearly year-long process. PG&E appreciates the mutual transparency and extensive collaboration employed throughout the process and generally supports the resultant findings.

Regarding Finding #3 of the audit and PG&E's treatment of accumulated interest from unspent EPIC 1&2 funds, the auditor accurately finds that PG&E had not yet returned accumulated interest to ratepayers at the onset of the EPIC 3 cycle. It should be noted that PG&E had not yet completed all of its EPIC 1&2 projects and associated expenditures at the onset of EPIC 3, and thus did not close the programs and return remaining EPIC 1&2 funds at that time. PG&E has since completed EPIC 1&2 work and expenditures and is in the process of returning the remaining EPIC 1&2 balances, inclusive of accumulated interest, to ratepayers through its 2021 rate setting process. This issue is solely one of timing and does not otherwise impact costs to ratepayers.

Beyond the few findings pertaining specifically to PG&E, PG&E looks forward to collaborating as appropriate to consider the broader set of findings and recommendations applicable to the CPUC, CEC and other utility EPIC administrators.

Sincerely,

Dan Gilani

Interim Sr. Manager
PG&E Electric Operations
Emerging Technology Strategy & Programs

SDG&E

A Sempra Energy utility®

Frank R. Goodman, Jr.
EPIC Program Manager
tel: 858 472-3783
email: fgoodman@sdge.com

January 5, 2021

Angie Williams
Director Utility Audits, Risk and Compliance Division (UARCD)
California Public Utilities Commission
401 R Street, Suite 221
Sacramento, CA 925811

Dear Ms. Williams:

SDG&E has reviewed the report on the Performance Audit of the Electric Program Investment Charge. We support the recommendations offered in the report and look forward to working with the California Public Utilities Commission to implementing the recommendations for future Electric Program Investment Charge cycles.

SDG&E thanks the Commission and the audit team for the careful and thorough work done on this audit. If you have questions or need additional information, please feel free to contact me.

Sincerely,

Frank R Goodman, Jr.

Frank R. Goodman, Jr.
SDG&E EPIC Program Manager

SOUTHERN CALIFORNIA
EDISON
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Southern California Edison response to

Performance Audit of the Electric Program Investment Charge (EPIC) Program Findings

Date: 12/17/2020

DocuSigned by:
Russell Ragsdale
CF48C1CCE26241F...

Russell Ragsdale
Director of Asset and Engineering Strategy
Asset Management, Strategy, and Engineering

P. O. Box 800
2244 Walnut Grove Avenue
Rosemead, CA 91770
626-302-1212

SOUTHERN CALIFORNIA EDISON

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Contents

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2244 Walnut Grove Avenue
Rosemead, CA 91770
626-302-1212

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1 Introduction

This document responds to the California Public Utilities Commission's 2020 Electric Program Investment Charge (EPIC) audit findings with respect to Southern California Edison Company (SCE). This audit was conducted from March through December of 2020, and supervised by Sjoberg Evashenk Consulting, 455 Capitol Mall, Suite 700, Sacramento, CA 95814.

2 Response to findings & recommendations

2.1 Finding #1: EPIC Collections from Ratepayers Were Consistent with CPUC Decision Requirements, But Processes to Remit Revenues to CEC and CPUC Revealed a Few Problems

Auditor's recommendations for SCE: There were no specific recommendations for SCE as a result of this finding.

2.2 Finding #2: CEC's Budget Processes and Controls were Reasonable and Complied with Applicable Requirements

Auditor's recommendations for SCE: There were no specific recommendations for SCE as a result of this finding.

2.3 Finding #3: Two IOUs Did Not Always Return EPIC Interest Earnings to Ratepayers Following Timelines Required by CPUC Decisions

Auditor's finding(s) for SCE: SCE's interest rate calculation reflected that $2,100,927 was earned on its EPIC funds between January 1, 2012 and December 31, 2017; however, SCE's 2019 rate setting processes reduced revenue requirements by $2,073,273 to offset the earnings. According to SCE, $27,654 was unintentionally excluded and will be considered as part of their 2021 rate setting processes.

Auditor's recommendations for SCE:

Ensuring SCE and PG&E return the remaining interest earned between 2012 and 2017 back to ratepayers.

SCE response to recommendation(s):

When this finding was identified, SCE immediately processed an accounting correction in the amount of $27,654, on 7/3/2020, to reconcile the difference.

2.4 Finding #4: Project Costs Appear Generally Supported and Reasonable, Cost Guidelines Are Needed

Auditor's finding(s) for SCE:

P. O. Box 800
2244 Walnut Grove Avenue
Rosemead, CA 91770
626-302-1212

Direct labor charged to Project 1 was $523,947 (see Exhibit 11), which included $1,149,679 in straight time, $37,934 in overtime, and $663,666 in labor corrections. However, the correction included only $15,209 in paid absences overhead, or 2 percent of the corrected labor charges. According to SCE, manual processes inadvertently excluded paid absences charges from the labor correction and affected multiple EPIC projects between 2016 and 2017. As a result, an additional total of $558,321 in paid absence overhead charges will be removed from SCE's EPIC program.

Auditor's recommendations for SCE:

CPUC should consider requiring SCE to correct labor overhead amounts charged to their EPIC Project 1 (see Exhibit 19) associated with the labor correction.

SCE response to recommendation(s):

SCE prepared an accounting correction in November 2020 to remove $558,321 in paid absence overhead charges from SCE's EPIC program. This correction will be implemented in December 2020.

2.5 Finding #5: Administrative Costs Appear Generally Supported and Reasonable

Auditor's recommendations for SCE: There were no specific recommendations for SCE as a result of this finding.

2.6 Finding #6: CPUC EPIC Oversight Personnel Costs Were Not Always Consistent with Actual Time Spent by Staff

Auditor's recommendations for SCE: There were no specific recommendations for SCE as a result of this finding.

2.7 Finding #7: Funding Available Appears Sufficient to Complete Projects, but CEC May Exceed Administrative Cap and CPUC Underutilized Oversight Budget

Auditor's recommendations for SCE: There were no specific recommendations for SCE as a result of this finding.

CALIFORNIA
ENERGY COMMISSION

January 5, 2021

Ms. Angie Williams
Director Utility Audits, Risk and Compliance Division
California Public Utilities Commission
400 R Street, Suite 221
Sacramento, California 95811

Dear Ms. Williams:

We appreciate the opportunity to provide a response to Sjoberg Evashenk Consulting, Inc.'s Performance Audit of the Electric Program Investment Charge (EPIC) Program conducted for the California Public Utilities Commission's (CPUC).

Finding #1: *EPIC Collections from Ratepayers Were Consistent with CPUC Decision Requirements, But Processes to Remit Revenues to CEC and CPUC Revealed a Few Problems.*

The auditor's review of remittance of revenues to CEC from the IOUs for program funds encumbered at business meetings found two instances of errors over a period of 2012 through 2019 - one was an overcharge and one was an undercharge. The CEC corrected the overcharge error when it was discovered. The undercharge error will be applied to the next invoice to the IOUs for project expenditures.

The report recommendation on this finding is for CPUC to consider "Ensuring CEC develops a process to reconcile remittance invoices sent to the three IOUs against approved project expenditures before sending additional invoices." CEC has implemented additional controls to prevent these errors from occurring in the future. These controls include monthly reconciliation of total approved project expenditures (encumbrances) to total funds invoiced and received. Reconciliation is now completed prior to the CEC invoicing the IOUs for project expenditures. This reconciliation is between the accounting office and program office.

Finding #2: *CEC's Budget Processes and Controls were Reasonable and Complied with Applicable Requirements*

The report stated that "CEC's budget development process was reasonable, consistent with industry practices, and complied with administrative cost provisions included in CPUC decisions" and no recommendations were provided.

energy.ca.gov
1516 9th Street, Sacramento, CA 95814

Finding #3: *Two IOUs Did Not Always Return EPIC Interest Earnings to Ratepayers Following Timelines Required by CPUC Decisions*

The report found that CEC interest earnings were returned to ratepayers in accordance with CPUC decisions and no recommendations were provided for the CEC.

Finding #4: *Project Costs Appear Generally Supported and Reasonable, Cost Guidelines Are Needed*

The audit report found "the direct project costs charged by the four administrators appeared generally reasonable and largely supported with underlying documentation." However they also reported that "a lack of formal guidance in CPUC decisions did not provide sufficient descriptions related to the allowability of costs or activities to control the utilization of EPIC project funding and ensure appropriate spending of project-related monies in accordance with the intent of program goals."

Regarding administrative overhead costs of prime contractors and subcontractors, the audit reported noted "that contractor invoices clearly identified the administrative overhead costs separate from the direct project costs, allowing CEC to monitor these expenses against the assigned budgets." Additionally, the audit noted that outside of the University of California awards, which have a maximum cap of 25 percent for administrative overhead costs, the CEC does not have caps on contractor administrative overhead charges. The audit report also acknowledged that CEC carefully considers potential award recipients' administrative costs during the proposal evaluation process, wherein proposals with lower administrative costs receive higher scores under that category.

Under this finding, the audit report recommendation is "To further improve consistency in controls over EPIC project expenses to ensure that ratepayer funds are expended prudently and are in line with the intent and goals of the program" and "Collaborating with the four administrators to develop cost guidance related to the allowable use of EPIC project funding. Guidelines should provide sufficient flexibility given differences in the types of projects undertaken by the administrators while providing adequate parameters reflecting the acceptable use of funding."

The CEC is supportive of initiating a collaborative discussion with the IOU administrators and CPUC on ensuring consistency among administrators on acceptable contractor/grant recipient administrative cost allowances. However, we believe it's important to include potential recipients in these discussions as capping overhead rates could negatively impact some organizations, such as small start-up companies, over larger organizations that have sufficient capital to absorb these costs. The CEC is dedicated to ensuring the process encourages broad participation by all and warns against restrictions may have unintended consequences to the potential application pool. In addition, the following points should be seriously considered before any changes to grant recipient administrative allowances:

1. CEC agreement terms indicate that we only pay for actual expenditures. Thus, a higher overhead does not result in paying profit to the entity. We only pay actual overhead costs.

2. Some small start-ups as well as non-profits might not be able to participate in our programs if they cannot recuperate their actual overhead costs. Some firms cover higher overhead costs with match funding. Match funding is often not available to non-profits or start-ups.

3. The State Administrative Manual, in section 8752, requires state agencies to recover full costs when performing work for others. If we capped admin expenses below a state agency's actual overhead, we could eliminate that agency's ability to participate in the program.

4. National labs, based on the contracts with the Dept. of Energy (DOE), do not usually have discretion in what they charge. Setting an arbitrary cap below what national labs must charge based on DOE requirements could eliminate national labs from participating.

The report further recommends CPUC require CEC to maintain complete support for all project expenses, including subcontractors. As stated, CEC requires extensive documentation to support expenses claimed for all prime recipients and major subcontractors, which is defined as subcontractors receiving more than $100,000 The report recommendation would require the same level of documentation be submitted to the CEC for minor subcontractors, or those receiving less than $100,000.

This recommendation also leads to the false impression that CEC is not providing sufficient oversight, which we strongly disagree with. Currently recipients are required to submit the invoices of minor subcontractors and it is incumbent upon the recipient, or prime contractor, to verify those expenses before submitting to the CEC. EPIC agreement terms require minor subcontractors **to keep all information** relative to their costs in case the CEC wants to audit the expenses or otherwise obtain information about them. The standard EPIC grant terms include the following provisions in Exhibit C, section 11:

> The Recipient will keep separate, complete, and correct accounting of the costs involved in completing the project and any match-funded portion of the project. The Commission or its agent will have the right to examine the Recipient's books of accounts at all reasonable times, to the extent necessary to verify the accuracy of the Recipient's reports.

> The Recipient will maintain books, records, documents, and other evidence, based on the procedures set forth above, sufficient to reflect properly all costs claimed to have been incurred in the performance of this Agreement. The Energy Commission, another state agency, and/or a public accounting firm designated by the Energy Commission may audit the Recipient's accounting records at all reasonable times, with prior notice by the Energy Commission.

Exhibit E, section 7 requires grant recipients to flow these provisions down to its subcontractors and also states these terms survive the end of the agreement. Thus, the CEC currently requires the details of minor subcontractor expenses to be kept in case there is an issue but does not require the information to be delivered unless requested or audited.

The CEC is also concerned that this recommendation could result in a level of effort not commensurate with the level of return and create undue burden to minor subcontractors that could ultimately reduce their desire and ability to participate. As noted in Exhibit 9, these agreements are usually several-million dollars or smaller. Therefore, minor subcontractors represent a relatively minor component and often consist of vendors and services, such as electricians, cement and plumbing contractors, technology transfer consultants, or technical writers. Recipients have already reported that our invoice documentation requirements are overly burdensome and, in response, the CEC is currently in the process of streamlining invoice documentation requirements to align documentation requirements with the major expenses and to put increased emphasis on close monitoring of the research project. This recommendation would derail that effort and likely result in additional concerns by recipients and their subcontractors. It would also add to the already taxed administrative responsibilities required of the CEC, and arguably would not be a good use of ratepayer funds.

Finding #5: *Administrative Costs Appear Generally Supported and Reasonable*

The audit found CEC's administrative expenses were generally reasonable, supported by underlying documentation, and aligned with general industry practices used to ensure controls over administrative practices. The audit report notes that due in part to changes in the state's fiscal accounting systems from CALSTARS to FI$Cal in 2017, the CEC was not able to provide some information requested by the auditors from the state's legacy system because these reports could no longer be accessed. As such, the audit noted that CEC should strengthen retention of documents that support its labor distribution and indirect cost allocation processes for non-labor charges.

With the new statewide financial information system (FI$Cal), the CEC is now able to access prior fiscal years' accounting reports. Additionally, the CEC will retain an electronic file with all documentation supporting annual adjustments to its labor distribution and indirect cost allocation.

Additionally, the audit report noted differences in how the CEC and IOUs charge expenses to administrative versus program funds and indicated that CEC charges all EPIC staff work, including technical functions, to administrative expenses while the IOUs charge a portion of their administrative functions and internal overhead expenses such as payroll taxes, benefits, and materials burden to project expenses.

The recommendation to Finding 5 is "collaborating with the four administrators to develop cost guidance related to the allowable use of EPIC project funding. Guidelines should provide sufficient flexibility given differences in the types of projects undertaken by the administrators while providing adequate parameters reflecting the acceptable use of funding". The CEC supports the audit recommendation to Finding 5 for CPUC to improve consistency on how administrative expenses are expended among the administrators and that this be done collaboratively with the administrators.

Finding #6: *CPUC EPIC Oversight Personnel Costs Were Not Always Consistent with Actual Time Spent by Staff*

This finding does not apply to the CEC.

Finding #7: *Funding Available Appears Sufficient to Complete Projects, but CEC May Exceed Administrative Cap and CPUC Underutilized Oversight Budget*

As noted in the audit report, "...we noted that while CEC's administration expenses remain within 10 percent of its overall EPIC budget, its required spending may cause it to ultimately exceed its administration budget prior to the expiration of the EPIC program; at least one IOU voiced similar concerns."

The report also acknowledged that administrative expenses are front-loaded due to a large amount of time spent preparing solicitations, conducting grant selection processes, and initiating a project, while expenditure of project funds can occur in the middle or end of a project. Therefore, there can often be a misalignment in administrative costs relative to project costs early in the agreement, and early in the investment plan cycle. Additionally, administrative funds are used to prepare required Investment Plans, Annual Reports, research topic area assessments, EPIC Symposiums, Forums, and workshops, responses to data requests from legislatures, CPUC, stakeholders, and others, and conduct program benefits assessments. These tasks (with the exception of project and annual reports) would not be implemented should the program sunset, significantly reducing ongoing administrative expenses. Therefore, a certain amount of misalignment is to be expected and diminishes during program winddown.

That said, the CEC does not believe the 10% cap is sufficient to perform the oversight functions adequately. To stay within this cap, the CEC has had to pay administrative costs with other CEC funds, which is not sustainable in the long-term.

The audit report highlighted the fact that while Investment Plans provide 3-year budgets, expenditures to manage and close out projects extend beyond the 3-year investment cycle. For each budget year, the CEC has two years to encumber the funds and an additional four years to liquidate those funds, which amounts to an actual six-year cycle for each budget year. Demonstration projects often require this full 4-year cycle to design, install and monitor the project. The Covid pandemic has stalled or delayed most research, and nearly all projects have needed an extension to complete their scope of work.

This misalignment of administrative to project expenditures was pointed out by the CEC in the 2019 audit performed by CPUC, which also observed that CEC would likely exceed its administrative cap prior to the end of the period when agreements end.

CEC's response to the 2019 audit was as follows:

"Our budget process is aligned with both the CPUC decisions and state budget process requirements for state agencies. Program administration dollars and project dollars approved in the various CPUC decisions are allocated proportionally to fiscal year budgets to align with the state budget process. Funding for EPIC program administration and projects are appropriated to the CEC on a fiscal-year basis through the state budget act.

Investment plans approved by the CPUC allocate funds for administration over the three-year period of the investment plan. The CEC converts the three-year investment plan approved by the CPUC into three fiscal year budget allocations as part of the annual state budget process, with a separate annual allocation for administrative budget and project budget."

The CEC's three Investment Plans to date, which have been approved by the CPUC, clearly articulate the allocation of 3-year administrative funds on an annual basis. Thus, the CEC has been transparent in its approach. Program administration expenditures are based on actual staff and operating costs and technical support contract funds encumbered during the fiscal year. The CEC's state budget authority provides that authorized expenditures are within the approved program administration budget.

The audit recommendation for finding 6 is that the CPUC provide guidance to the types of administrative activities required of the administrators so the administrative funding budget is sufficient to cover all required activities. The CEC supports a collaborative discussion with the CPUC and IOUs on this topic, but further requests that the CPUC strongly consider the information provided by the CEC to the on-going EPIC proceeding that clearly shows the need for an increase in the administrative cap for CEC as well as the disproportionately low allocation of administrative funding to this research program in comparison to other similar research programs.

Further, the audit noted "CEC indicated that not all administrative costs incurred are charged to their EPIC program due to the ten percent cap placed on the program and different funding sources may be used to pay administrative expenses to ensure the maximum cap is not exceeded. Even still, CEC acknowledges that it is possible that the administrative funds for its EPIC projects may run out before all projects are complete and, in that case, CEC would request an increased administrative cap or would investigate utilizing additional alternative funding sources to complete the projects." The audit recommends requiring the CEC to report on the utilization of its actual expenses rather than budgetary expenditures or adjustments.

State budgeting and accounting practice is to report encumbrances as expenditures. The CEC follows the reporting requirements provided in CPUC Decisions, which only requires we report EPIC fund-related expenditures.

Thank you for the opportunity to respond to the audit findings. We appreciate the chance to share the corrections the CEC has already made in response to the report recommendations. We look forward to working with the CPUC and fellow administrators on the recommendations that require collaboration. We are proud of the EPIC program and all it is doing to foster innovation and we are committed to making any administrative enhancements that will improve our execution of the program.

Sincerely,

Drew Bohan
Executive Director