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April 11, 2014

Michele Weaver, Superintendent
Members of the Board of Education
Middleburgh Central School District
245 Main Street
Middleburgh, NY 12122

Report Number: P4-13-5

Dear Superintendent Weaver and Members of the Board of Education:

The Office of the State Comptroller works to help school district officials manage their resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support district operations. The Comptroller oversees the fiscal affairs of districts statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Education governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard district assets.

In accordance with these goals, we conducted an audit of eight school districts in Broome, Delaware, Schoharie, Sullivan and Tompkins Counties. The objective of our audit was to determine whether energy performance contracts (EPCs) entered into by school districts achieved the cost and/or energy savings projected by the vendor who executed the contract. We included the Middleburgh Central School District (District) in this audit. Within the scope of this audit, we examined the District's EPC, including the Energy Service Company's (ESCO) projections, and reviewed energy consumption and costs for the period July 1, 1999 through August 6, 2013.

This report of examination letter contains our findings and recommendations specific to the District. We discussed the findings and recommendations with District officials and considered their comments, which appear in Appendix A, in preparing this report. District officials generally agreed with our recommendations and indicated they planned to take correction action. At the completion of our audit of the eight school districts, we prepared a global report that summarizes the significant issues we identified at all of the school districts audited.

Summary of Findings

The District will likely achieve the cost savings projected by the ESCO that executed the EPC. However, these cost savings are achieved only when State aid and grants are factored into the calculation. Although the energy and operational cost savings are projected to total approximately \$1.5 million over the life of the EPC, the total expenditures are approximately \$2.14 million, netting to a loss of \$624,800. When the grants and State aid are included, the District is projected to save a total of \$500,600.

Background and Methodology

Article 9 of the Energy Law establishes procedures to be used by school districts in initiating and administering EPCs. An EPC is an agreement by an ESCO for the provision of energy services in which energy systems are installed, maintained or managed to improve the energy efficiency of, or produce energy for, a facility in exchange for a portion of the energy savings or revenues. EPCs are not subject to voter approval or competitive bidding requirements and the length of the contract must not exceed the useful life of the building (which the New York State Education Department has established at 18 years). In addition, school districts should establish procedures to monitor these EPCs. The ESCO may agree to guarantee that the improvements will generate cost savings sufficient to pay for the project over the term of the EPC; however, cost savings are not a requirement for a successful contract. After the EPC ends, the school districts may continue to realize additional cost savings as a result of the improvements.

The District is located in Albany and Schoharie Counties and has two buildings in operation. It has approximately 900 students and general fund budgeted appropriations of \$20.2 million for the 2013-14 fiscal year. The District is governed by a five-member Board of Education (Board). The Board is responsible for conducting the business of the District within the laws of the State and regulations of the New York State Commissioner of Education.

In February 2002, the Board entered into an EPC with an 18-year contract term from August 2003 through July 2021. The related project work was completed in July 2003 and included several upgrades to the District's lighting, heating, ventilation and air controls. The ESCO guaranteed energy savings from these upgrades, but did not guarantee corresponding cost savings. The ESCO also guaranteed annual operational cost savings of \$11,300, totaling \$203,400 over the life of the EPC. The total capital project cost totaled \$1.06 million. During the capital work of the EPC, the District also had an EXCEL¹ capital project that added an additional 8,356 square feet to the elementary school building.

To accomplish our objective, we interviewed District officials and a representative from the ESCO. We also reviewed the EPC to obtain the scope of the work, the cost of the project, the length of the contract, the contracted ongoing maintenance and verification costs, the guaranteed energy savings, and the projected energy cost savings and operational savings over the life of the project. We obtained utility data, including consumption, cost and rates for the base year of July 1999 through June 2000, and verified the reasonableness of the ESCO's base-year calculations. We also verified the ESCO's projected increase in utility rates based on utility costs for New

¹ Expanding our Children's Education and Learning (EXCEL) is a New York State Education Department grant/aid program.

York State from the U.S. Energy Information Administration from 1992 through 2002 and verified an average increase in utilities of zero percent was reasonable. We verified the reasonableness of the ESCO’s annual measurement and verification reports for August 2003 through July 2012 by subtracting the annual consumption for August 2011 through July 2012 from the base year’s consumption and comparing it to the ESCO’s energy savings in its report. We then used the ESCO’s reported energy savings for August 2003 through July 2012 and the ESCO’s guaranteed energy savings for August 2012 through July 2021 and multiplied it by the base-year utility rates to calculate the annual actual and projected energy cost savings. We also documented the lease payments over the life of the contract using the payment schedule. We then subtracted the expenditures related to the EPC from the total cost savings calculated to identify any potential savings. We also considered any grants or State aid received or expected to be received relating to the EPC.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). 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 objective.

Audit Results

The District’s EPC is projected to achieve the guaranteed energy savings of 497,293 kilowatt hours, 1,010 kilowatts and 34,406 therms. The ESCO did not guarantee any associated energy cost savings, but did guarantee operational costs savings of \$11,300 annually. However, using the base rates, we projected energy² and operational cost savings over the life of the EPC total \$1.5 million, as shown in Table 1.

Projected Energy Cost Savings	\$1,314,418
Projected Operational Cost Savings	\$203,400
Projected Energy and Operational Cost Savings	\$1,517,818
Lease Payments Including Interest	\$1,694,984
Ongoing Maintenance and Verification ^a	\$447,602
Net Benefit Without Grants and State Aid	(\$624,768)
Grants Received	\$8,398
Projected State Building Aid	\$1,116,935
Net Benefit With Grants and State Aid	\$500,565
^a The District contacted the ESCO as a result of our audit and renegotiated the remaining projected payments, which resulted in the overall maintenance and verification costs decreasing from \$515,000 to \$447,600 for an estimated additional savings of \$67,400 over the remainder of the EPC.	

However, District expenditures to implement the terms of the EPC totaled approximately \$2.14 million, for a net cost to the District of approximately \$624,800 before any grants or State aid.

² To calculate the projected energy cost savings, we used the actual energy savings reported by the ESCO in its measurement and verification reports for August 2003 through July 2012 and multiplied it by the base-year utility rates. We then used the ESCO’s guaranteed energy savings and multiplied it by the base-year utility rates to project out the energy savings for the remaining nine years (August 2012 through July 2021) of the EPC.

With the receipt or potential receipt of grants and State aid, the total savings will amount to approximately \$500,600.

The District has no effective monitoring procedures in place. Although the District has an energy manager, the energy manager is not responsible for reviewing the ESCO's annual verification reports or ensuring that the guaranteed energy savings are being achieved. Instead, District officials are relying on the ESCO's annual verification reports that state whether they have been achieving the guaranteed savings. District officials also stated that they have not been monitoring the EPC due to District official turnover in recent years and the loss of records during the 2011 flooding.

Recommendations

1. Before considering an EPC in the future, District officials should perform a cost-benefit analysis based on the ESCO's projected energy cost savings and negotiated contractual terms to determine if the investment in energy upgrades is beneficial.
2. District officials should implement monitoring procedures, over the EPC, to include timely reviews of the District's electricity and fuel oil consumption and the related costs and compare their reviews to the ESCO's annual verification reports.

The Board has the responsibility to initiate corrective action. Pursuant to Section 35 of the General Municipal Law, Section 2116-a (3)(c) of the Education Law, and Section 170.12 of the Regulations of the Commissioner of Education, a written corrective action plan (CAP) that addresses the findings and recommendations in this report must be prepared and forwarded to our office within 90 days. To the extent practicable, implementation of the CAP must begin by the end of the next fiscal year. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. The Board should make the CAP available for public review in the District Clerk's office.

Our office is available to assist you upon request. If you have any further questions, please contact H. Todd Eames, Chief Examiner of the Binghamton Regional Office, at (607) 721-8306.

Sincerely,

Gabriel F. Deyo

APPENDIX A

RESPONSE FROM DISTRICT OFFICIALS

The District officials' response to this audit can be found on the following page.



MIDDLEBURGH CENTRAL SCHOOL DISTRICT
Office of the Superintendent
245-1 Main Street
Middleburgh, New York 12122
(518) 827-3625

[REDACTED]
Division of Local Government
and School Accountability
Office of the State Comptroller
State Office Building Room 1702
44 Hawley Street
Binghamton, New York 13901-4417

Dear [REDACTED]

This letter shall serve as the official response from the Middleburgh Central School District (“the District”) regarding the “Draft Audit Report” on the district’s Energy Performance Contract covering the period of July 1, 1999 through August 6, 2013. As discussed at the October 25, 2013 meeting, the District had concerns over the projected cost savings that will be realized by the Energy Performance Contract. The District has since provided the Comptroller’s Office with additional data to include in the final report. It is the District’s understanding that the projected cost savings to the district will increase from the original estimate of \$48,900 to a projected savings of approximately \$500,000.

The District agrees with the recommendation that the District should perform cost-benefit analysis prior to entering into an Energy Performance Contract. It is the current practice of the Middleburgh Central School District to perform cost analysis prior to entering into an agreement and/or contract of any kind.

The District currently collaborates with the Capital Area BOCES in an energy savings program. As part of the collaboration, the District reviews all electric and fuel consumption on a regular basis. As a result of the recommendation in the draft audit, the District will expand this process to include the monitoring of the ESCO’s annual verification reports. The School Business Official will compare the results on a regular basis.

We understand that following receipt of this letter a formal Report of Examination will be issued after which the district will prepare a corrective action plan within the 90 day timeframe.

Respectfully submitted,

Michele R. Weaver
Superintendent of Schools