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Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to testify at your request on the work of the Office of Inspector General regarding the Department of Energy's (Department) Loan Programs Office (Program).
The Program was originally created to accelerate the domestic commercial deployment of innovative and advanced clean energy technologies at a scale sufficient to contribute to the achievement of national clean energy objectives. In fulfilling its mission, the Program guarantees loans to eligible clean energy projects and provides direct loans to eligible manufacturers of advanced technology vehicles and components. As of May 2014, the Program had approximately $43 billion in remaining loan and loan guarantee authority and was monitoring about a $30 billion loan portfolio.

Because of the significant taxpayer funds involved, the Office of Inspector General has, over the years, performed a series of reviews on various aspects of the Department's Loan Programs Office. These reviews have identified needed improvements in both the origination and monitoring of loans. In April 2014, the Office of Inspector General published a report on a loan guarantee to Abound Solar Manufacturing, LLC (Abound), an entity that declared bankruptcy after failing to satisfy the terms of its loan agreement with the Department.[1] Further, in May 2014, we reported on the Department's progress in implementing recommendations for improvement that resulted from an Administration requested review by an independent consultant.[2]

[1] *Audit Report on the Department of Energy's Loan Guarantee to Abound Solar Manufacturing, LLC.* (DOE/IG-0907, April 2014)
[2] *Audit Report on Implementation of Recommendations from the January 2012 Independent Consultant's Review of the Department of Energy Loan and Loan Guarantee Portfolio* (DOE/IG-0909, May 2014)

My testimony today will focus on our findings regarding the Department's implementation of the independent consultant's recommendations. Prior to this, I will outline our findings regarding the Abound loan guarantee to provide a benchmark for understanding the Department's progress and actions yet to be completed to fully implement the consultant's recommendations.

Office of Inspector General Oversight

Abound Solar

The purpose of our April 2014 audit was to examine the circumstances surrounding the Program's approval and administration of a loan guarantee to Abound. The Program issued the loan guarantee to Abound for up to $400 million in December 2010, to construct and commission thin-film photovoltaic solar panel manufacturing facilities. In September 2011, Abound failed to meet certain milestones; therefore, the Program suspended funding to the project. Subsequently, Abound filed for bankruptcy in July 2012.

Our audit revealed that Abound's failure to meet its project milestones and its subsequent bankruptcy occurred as a result of a combination of market conditions and technical issues that negatively impacted its operations. These issues included dramatic changes in the solar panel market that resulted in downward price pressures and performance shortfalls in Abound's solar panels, which negatively affected its sales and delayed its expansion plans. The Program had identified and evaluated these types of market and technical risks prior to the loan approval and issuance. The program concluded that, despite these risks, there remained a reasonable prospect of repayment of the loan. Additionally, the Program established mitigation measures prior to issuing the loan to address these risks, such as instituting technical and financial performance metrics prior to allowing the recipient to drawdown loan funds. However, subsequent to loan closure, market conditions further deteriorated and technical issues continued, resulting in Abound's failure to meet requirements of the loan and its ultimate bankruptcy.

Although the Department had identified, considered and taken steps to mitigate the market and technical risks, and had reduced the financial exposure to the project by suspending funding when Abound did not meet its project milestones, our audit identified several weaknesses in the Department's administration of the Abound loan. Specifically, we found the Program had not:

- Consulted with the Department's Credit Review Board concerning a material change in the credit subsidy used to cover potential losses subsequent to the Board's recommendation to approve the loan. Specifically, the Program lowered its recovery rating estimate, the potential recovery in the event of default, from 38 percent to 8.3 percent prior to loan closing. This change increased the credit subsidy from $71 million to $96 million, an increase of $25 million in taxpayer funds appropriated under the American Recovery and Reinvestment Act of 2009. In our opinion, the change in potential recovery should have been made known to board members so they could determine if such information would have altered their decision to recommend approval of the loan to the Secretary.

- Resolved conflicting opinions of its advisors regarding Abound's ability to overcome technical issues. While the Program's Independent Engineer believed that Abound's plans to address the technical issues were achievable and the project funding should continue, the Program's internal solar expert recommended that the Program not approve additional disbursements based on the number, severity, and frequency of Abound's product and quality control issues. Despite the technical shortfalls and the solar expert's concerns regarding Abound's quality control, the Program allowed the project to continue without reconciling the conflicting opinions of the Independent Engineer and the solar expert.

- Adequately documented the assumptions in the financial modeling used to support loan approval and monitoring. Program officials stated that assumptions used in the models fully considered deteriorating market conditions, overcapacity in the solar panel industry and Abound's technical performance issues. However, we were unable to verify the Program's assertion because the results of key/critical discussions were not formally documented and thus were not available for our examination.

- Conducted ongoing, formal financial and market analyses as part of its monitoring activities as required by the Program's policy manual. Specifically, we found no evidence that these types of analyses were regularly performed during Abound's disbursement period. Although Abound supplied financial data, we were unable to establish that the Program used such information to determine whether financial requirements of the loan were being satisfied.

We concluded that the issues we identified occurred because the Program had not established comprehensive policies, procedures and guidance for awarding, monitoring and administering loans. Specifically, we noted a lack of guidance in the areas of the Board's reconsideration of loans, the processes for resolving differences in professional opinions among the Program's technical experts, the nature and timing of financial and market analysis, and the management of distressed loans.

We also pointed out that weaknesses in the financial and market monitoring of Abound occurred during a period when the Program was just establishing its Portfolio Management Division, which limited the availability of qualified staff. In fact, the Division only had three employees overseeing loans — a newly hired Director and two support contractors who had been transferred from within the Program. Additionally, based on a review of qualifications and internal email correspondence, we confirmed that the contractor assigned as the Portfolio Manager for Abound lacked the skill-set needed to effectively monitor financial and technical performance.

The Department's experience with the Abound loan guarantee provides useful lessons learned for Program improvement that were generally encapsulated in the independent consultant's report, especially as they relate to clarifying authorities and accountabilities of managers, filling key positions with experienced professionals, and strengthening and restructuring oversight of the Program.

Independent Consultant's Recommendations

The purpose of our May 2014 report was to determine whether the Department adequately addressed findings and recommendations from the January 2012 independent consultant's report. The review, commissioned by the White House Chief of Staff in October 2011, provided an independent evaluation of the loan and loan guarantee portfolio and made recommendations for improvement. The requested review was focused on the present and future of the Program; therefore, it excluded an evaluation of loans to companies that had recently filed for bankruptcy protection, including Solyndra, Inc. The independent consultant's report identified a number of areas for improvement and included 12 overall recommendations comprised of specific actions for implementation aimed at enhancing the oversight and management of the Program.

We found that, overall, the Department appeared to have taken the consultant's recommendations seriously, and that related actions were generally responsive to the recommendations. Specifically, we concluded that the Department had completed actions to address 4 of the report's 12 recommendations and initiated actions in response to the remaining 8 recommendations. We found, however, that the Department had not always implemented actions as precisely as recommended by the independent consultant. Instead, it considered all specific recommended actions and had, based on supporting rationale, chosen alternative approaches.

Status of Recommendations

Our review found that the Department had completed actions to:

- Provide long-term funding through normal appropriations and the collection of loan fees;

- Fill a number of key positions in management with experienced professionals;
- Establish and effectively communicate clear management goals; and
- Engage in long-range strategic planning.

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

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

We noted that several of the areas for improvement recommended by the independent consultant, such as the need for a comprehensive records management system, a lessons-learned process and adequate staffing, were identified in previous reviews conducted by our Office. In particular, our March 2011 report found that the Program had not adopted a records management system or updated its policies and procedures to include improvements in its loan processing to provide for the consistent use of lessons learned.[3] In March 2013, the Program certified that all actions regarding the adoption of a records management system had been completed; however, action items to address the update of its policies and procedures were still pending at the conclusion of our most recent review. Finally, the need to ensure sufficient staffing was also identified in our September 2007 report, which identified additional opportunities for improving the management and oversight of the Program.[4]

Although we noted that the Department had made progress in addressing the independent consultant's recommendations, we identified additional areas of needed improvement that were not specified by the consultant. Specifically, we noted that the Department:

- Had not finalized changes in policies and procedures necessary to address the report's recommendations. At the time of our review, almost 2 years after the consultant's report was issued, revisions to the Program's overall policy manual were not yet finalized. In addition, our review of the Program's draft policy found that some aspects of the loan management process, such as defining what actions are "material" and establishment of clear lines of authority remained unclear.

- Had not developed a formal adjudication process for resolving differences of professional opinion. As we noted in the case of Abound, a well-defined process for resolving professional differences of opinion is essential.

[3] *Audit Report on the Department of Energy's Loan Guarantee Program for Clean Energy Technologies* (DOE/IG-0849, March 2011)
[4] *Special Report on Loan Guarantees for Innovative Energy Technologies* (DOE/IG-0777, September 2007)

- Had created a potential conflict-of-interest by appointing the Director of Portfolio Management as a member of the Program's Risk Committee. One of the committee's functions is to evaluate risks associated with individual loans monitored by the Portfolio Management Division and make recommendations for changes in risk evaluations as appropriate. We concluded that the Risk Committee, as structured at the time of our audit, had not initially allowed for a fully independent evaluation process to occur in that the Director of Portfolio Management was a voting member of the committee. After we discussed the apparent conflict with Program officials, they revised the charter for the Risk Committee and removed the Director of Portfolio Management as a committee member.

Finally, while the Department's actions show promise and substantial progress had been made in implementing recommended improvements, we were unable to make a determination as to whether these efforts will ultimately be fully effective, because, as previously noted, a number of actions, such as clarifying authorities, establishing an external advisory board, and incorporating lessons learned were still ongoing.

Path Forward

The Program issued a solicitation in December 2013, making up to $8 billion in loan guarantee authority available to support innovative advanced fossil energy projects that avoid, reduce or sequester greenhouse gases. In addition, the Program issued a draft loan guarantee solicitation in April 2014, for innovative renewable energy and energy efficiency projects located in the U.S. that avoid, reduce or sequester greenhouse gases. When finalized, the solicitation is expected to make as much as $4 billion in loan guarantees available to help commercialize technologies that may be unable to obtain full commercial financing. Given the significant amount of additional funding being made available for loan guarantees and previously identified weaknesses in the Program, we will continue to monitor its activities as part of our normal risk assessment process. In our view, the Loan Guarantee Program warrants special attention by Department officials and, therefore, has been one of our "watch list" items since 2011.[5]

Mr. Chairman, this concludes my statement and I would be pleased to answer any questions that the Subcommittee may have.

[5] *Special Report on Management Challenges at the Department of Energy - FY2012* (DOE/IG-0858, November 2011)