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An Audit Report on

**The System Benefit Fund  
and the Low-Income Electric  
Discount Program at the  
Public Utility Commission**

July 2011

Report No. 11-043



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# The System Benefit Fund and the Low-Income Electric Discount Program at the Public Utility Commission

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## Overall Conclusion

The Public Utility Commission (Commission) made expenditures from the System Benefit Fund (SBF) for the Low-Income Electric Discount Program (discount program) in accordance with the Public Utility Regulatory Act (Texas Utilities Code, Title 2), the Texas Administrative Code, and General Appropriations Act requirements. The SBF cash balance was \$548,823,167 at the end of fiscal year 2009 and \$607,788,713 at the end of fiscal year 2010.

The Commission should strengthen two important aspects of its administration of the SBF. Specifically:

- The Commission should conduct analyses of the SBF fee that utility customers pay to determine whether that fee amount is appropriate. The Commission has approved and set the SBF fee at 65 cents per megawatt hour, the statutory maximum, since fiscal year 2002.
- The Commission should verify whether the total amount of SBF fees the State receives is the amount the State should have received.

The Commission also should strengthen two important aspects of its administration of the discount program. (The discount program enables eligible customers to receive discounts on their utility bills and is funded by the SBF.) Specifically:

- The Commission should monitor the contractor<sup>1</sup> that determines which customers are eligible for the discount program to ensure that the contractor correctly identifies all eligible customers.

### System Benefit Fund (SBF)

The SBF is a dedicated account in the General Revenue Fund.

The SBF is funded through a fee that retail electric providers charge on the utility bills of all electricity consumers in competitive markets in Texas. The Public Utility Commission (Commission) sets the SBF fee annually.

Transmission and distribution utilities bill the retail electric providers for the SBF fees the providers collect from customers. Transmission and distribution utilities then forward those fees to the State for deposit into the SBF.

### Low-Income Electric Discount Program (Discount Program)

The discount program enables eligible customers to receive discounts on their electricity bills from May through September. The Commission determines the discount rates.

The Commission contracts with a contractor to determine which customers are eligible for the discount program. The contractor then notifies retail electric providers about which customers are eligible for a discount on their utility bills.

Retail electric providers factor the discounts into the utility bills they send to eligible customers. The retail electric providers then request reimbursements for discounts from the Commission. The Commission uses SBF funds to reimburse the retail electric providers.

<sup>1</sup> The Commission refers to this contractor as the Low Income Discount Administrator (LIDA).

- The Commission should verify the accuracy of the amounts of reimbursements that retail electric providers request for providing discounts.

Although the Commission should make certain improvements in its administration of both the SBF and the discount program, the Commission properly accounted for its expenditures from the SBF in accordance with applicable requirements. The Commission also has a reasonable process for setting discount rates, and 97 percent of customers that auditors tested received the correct discount amount.

## Key Points

### System Benefit Fund (SBF)

**SBF Fee Analysis.** The Commission does not perform an analysis of the SBF fee that it sets. Texas Utilities Code, Section 39.903(d), requires the Commission to annually review and approve SBF accounts; projected revenue requirements; and proposed, nonbypassable fees.

Title 16, Texas Administrative Code, Section 25.451(e), states that the amount of revenue received from the SBF fee shall be an amount necessary to fund the purposes outlined in Texas Utilities Code, Section 39.903, consistent with legislative appropriations and expected fund revenue; operating costs of the discount program and other obligations of the SBF; a necessary fund reserve balance; and any other purpose required by statute or legislative appropriations. However, the Commission did not provide documentation to demonstrate its consideration of those factors during its fee-setting process.

According to Commission orders, each budget for the 2008-2009 biennium and the 2010-2011 biennium "contemplates that the system benefit fund fee remain at the maximum level authorized by law, 65 cents per [megawatt hour]." As a result, the Commission set the SBF fee at 65 cents per megawatt hour metered during fiscal years 2009 and 2010 without performing the analysis the Texas Administrative Code requires.

**Verification of SBF Fee Amounts Received.** The Commission does not verify that the amount of SBF fees the State receives from transmission and distribution utilities is accurate. The Commission receives only signed certifications from transmission and distribution utilities that the information they provide regarding the SBF fees is correct.

### Low-Income Electric Discount Program (Discount Program)

**Monitoring of the Contractor That Determines Which Customers Are Eligible for the Discount Program.** The Commission has not conducted any audits or reviews of the contractor that determines which customers are eligible for the discount program. The Commission has contracted with this contractor since September 1,

2008. The contractor appropriately processed the majority of discount program self-enrollment applications tested.

The contractor's process to determine which customers are eligible for the discount program did not identify certain eligible customers that auditors identified, but that group of customers represented only 0.5 percent of the eligible customers that the contractor had identified. However, without monitoring the contractor, the Commission is unable to ensure that the contractor continues to properly identify customers who are eligible for discounts.

**Reimbursement of Retail Electric Providers.** After retail electric providers give discounts to customers, they submit reimbursement requests to the Commission. However, the Commission does not receive adequate supporting documentation for those reimbursement requests to ensure that they are accurate. The Commission receives only summary level, self-reported information from the retail electric providers, and it does not request detailed information regarding the discounts.

In addition, the Commission performs only a limited number of audits of retail electric providers' compliance with discount program requirements each year. The Commission assigned one staff person to compliance monitoring. That individual also is responsible for conducting compliance monitoring for other programs. According to the Commission, that individual completes two to three audits of retail electric providers every two years and a limited number of desk reviews annually for the discount program. However, those desk reviews are based on high-level information that retail electric providers submit to the Commission and high-level reports that the Commission's contractor submits to the Commission.

Auditors identified less significant issues and communicated those issues to the Commission separately in writing.

## ***Summary of Management's Response***

Commission management agreed with the recommendations in this report. Management's detailed responses are presented following each set of recommendations in the Detailed Results section of this report. An overall response from management is presented in Appendix 5 on page 25.

## ***Summary of Information Technology Review***

Auditors performed a limited review of application controls for the Commission's SBF system. Those controls included password management controls, user access controls, and data integrity controls.

Auditors also reviewed the Commission's user access to the Uniform Statewide Accounting System (USAS), which the Office of the Comptroller of Public Accounts

maintains. Commission employees with access to USAS had access levels that were reasonable and consistent with their job duties.

Auditors did not perform any reviews of the information technology systems that the Commission's contractor or retail electric providers maintain.

## ***Summary of Objectives, Scope, and Methodology***

The objectives of this audit were to:

- Determine whether the Commission makes expenditures from the SBF for the discount program in accordance with applicable laws, regulations, and policies and procedures.
- Verify the accuracy of the cash balance in General Revenue Dedicated Account - System Benefit Fund 5100 at the end of fiscal years 2009 and 2010.

The scope of this audit covered SBF revenues, transfers, and expenditures from September 1, 2008, through August 31, 2010; Commission processes for analyzing, reviewing, and determining the amount of the SBF fee and discount rates for the discount program; and discount program eligibility processes.

The audit methodology included reviewing a sample of discount program self-enrollment applications and associated supporting documentation from the Commission's contractor; verifying the contractor's discount program eligible customer lists for a sample of retail electric providers for selected months; reviewing a sample of customer billing statements from a sample of retail electric providers; reviewing a sample of retail electric providers' reimbursement requests; reviewing a sample of expenditures, revenues, transfers, and associated supporting documentation for the SBF for fiscal years 2009 and 2010; reviewing and recalculating the amount of the SBF fee charged to customers; reviewing the Commission's processes for analyzing and determining the SBF fee and discount rates for the discount program; and interviewing Commission management and staff.

To assess the reliability of (1) the discount program self-enrollment application data the Commission's contractor provided and (2) reimbursement request data from the Commission's SBF system, auditors:

- Reviewed the data for accuracy and completeness by reviewing database schemata, verifying record counts, and performing a high-level review of data fields and contents for appropriateness.
- Interviewed Commission and contractor staff with knowledge about the data.
- Traced a sample of data to source documents.

Auditors also relied on prior audit work the State Auditor's Office conducted to assess the reliability of USAS data. Auditors determined that USAS data was sufficiently reliable for the purposes of this audit.

Auditors did not determine the reliability of (1) data received from retail electric providers and (2) eligible customer lists for the discount program from the Commission's contractor. However, that data was not the primary focus of this audit. Auditors used that data only to substantiate information the Commission maintained.

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# Detailed Results

Chapter 1

## ***The Commission Should Analyze the SBF Fee That Utility Customers Pay, and It Should Ensure That the State Receives the Correct Amount of SBF Fees from Transmission and Distribution Utilities***

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The Public Utility Commission (Commission) has an annual approval process for the System Benefit Fund (SBF) fee that utility customers pay on their electricity bills, but that process does not include a detailed analysis of the amount of the SBF fee. Additionally, there are inconsistencies between the Texas Utilities Code and the Commission's rules in the Texas Administrative Code regarding the amount of the SBF fee.

### **The System Benefit Fund (SBF)**

The primary source of revenue for the SBF is a nonbypassable fee (the SBF fee) that retail electric providers charge on the utility bills of all electricity customers in deregulated markets in Texas. The Public Utility Commission (Commission) sets the SBF fee annually.

The primary purpose of the SBF is to fund the Low-Income Electric Discount Program (discount program). Chapter 2 of this report contains details regarding the discount program.

The Commission ensures that transmission and distribution utilities deposit SBF fees into the State Treasury; however, it does not verify the accuracy of the amount of SBF fees remitted to the State.

The Commission properly accounted for its expenditures from the SBF in accordance with the Texas Utilities Code, the Texas Administrative Code, and General Appropriations Act requirements.

As of August 31, 2010, the SBF cash balance was \$607,788,713.

Chapter 1-A

## **The Commission Should Perform a Detailed Analysis of the SBF Fee That Utility Customers Pay and Ensure That the Amount of the SBF Fee Complies with Statute**

### **Fee Analysis**

The Commission reviews and projects SBF revenues and considers legislative appropriations for future fiscal years, but it does not use that information to set the amount of the SBF fee charged to customers on their utility bills.

Texas Utilities Code, Section 39.903(d), requires the Commission to annually review and approve SBF accounts; projected revenue requirements; and proposed, nonbypassable fees. In addition, Title 16, Texas Administrative Code, Section 25.451(e), states that the amount of revenue from the SBF fee shall be an amount necessary to fund the purposes outlined in Texas Utilities Code, Section 39.903, consistent with:

- Legislative appropriations and expected fund revenue.

- Operating costs of the Low-Income Electric Discount Program (discount program) and other obligations of the SBF.
- A necessary fund reserve balance.
- Any other purpose required by statute or legislative appropriations.

The Commission did not provide documentation to demonstrate its consideration of the factors listed above during its annual SBF fee approval process.

According to Commission orders, each budget for the 2008-2009 biennium and the 2010-2011 biennium “contemplates that the system benefit fund fee remain at the maximum level authorized by law, 65 cents per [megawatt hour].” As a result, the Commission approved and set the SBF fee at 65 cents per megawatt hour during fiscal years 2009 and 2010 without performing the analysis that the Texas Administrative Code requires. The Commission has approved and set the SBF fee at 65 cents per megawatt hour, the statutory maximum, since fiscal year 2002.

#### Inconsistency between Statute and the Texas Administrative Code

##### Texas Utilities Code

The Legislature enacted Texas Utilities Code, Section 39.903(b), effective September 1, 1999.

##### Texas Administrative Code

The Texas Administrative Code is a compilation of all Texas state agency rules.

Rules are more limited in scope and power than statutes and are generally a state agency's statement of general applicability that implements, interprets, or prescribes law or policy or describes the procedure or practice requirements of the agency.

Requirements regarding the amount of the SBF fee in statute differ from requirements in the Texas Administrative Code. Specifically:

- Texas Utilities Code, Section 39.903(b), specifies that the SBF fee cannot exceed 65 cents per megawatt hour and is allocated to customers based on the amount of kilowatt hours used.
- Title 16, Texas Administrative Code, Section 25.451(d)(3), specifies that the average SBF fee may not exceed 65 cents per megawatt hour. Title 16, Texas Administrative Code, Section 25.451(c)(3), further specifies that the SBF fee shall be charged to electric retail customers based on the amount of kilowatt hours of electric energy used, as measured at the meter and adjusted for voltage level losses.

Through Commission orders, the Commission approved and set the SBF fee amount for fiscal years 2009 and 2010 at a rate of 65 cents per megawatt hour, rather than an average of 65 cents per megawatt hour as stated in the Texas Administrative Code. However, through the rate-setting process, the Commission allows transmission and distribution utilities to charge a range of SBF fees to different customer classes to adjust for voltage level losses. As a result, some customer classes are charged an SBF fee that exceeds the statutory maximum of 65 cents per megawatt hour established in the Texas Utilities Code. For example, the SBF fees that customers were charged during fiscal years 2009 and 2010 ranged from 64 cents per megawatt hour metered to 66 cents per megawatt hour metered. This was in compliance with Texas

Administrative Code requirements; however, it did not comply with the Texas Utilities Code requirement that fees cannot exceed 65 cents per megawatt hour and be allocated based on the amount of kilowatt hours used.

## Recommendations

The Commission should:

- Develop and implement policies and procedures to perform an analysis of the amount of the SBF fee during its annual fee approval process as required by the Texas Administrative Code. The members of the Public Utility Commission should consider that analysis when reviewing and approving the amount of the SBF fee during open meetings. The analysis should consider the requirements in Title 16, Texas Administrative Code, Section 25.451(e), which state that the amount of revenue from the SBF fee shall be an amount necessary to fund the purposes outlined in Texas Utilities Code, Section 39.903, consistent with:
  - ♦ Legislative appropriations and expected fund revenue.
  - ♦ Operating costs of the discount program and other obligations of the SBF.
  - ♦ A necessary fund reserve balance.
  - ♦ Any other purpose required by statute or legislative appropriations.
- Work to achieve consistency between Texas Administrative Code requirements regarding the SBF fee and Texas Utilities Code, Section 39.903(b). This could include updating Texas Administrative Code requirements, seeking clarification on statutory requirements, or both.

## Management's Response

*The Public Utility Commission concurs with the audit recommendation to “develop and implement policies and procedures to perform an analysis of the amount of the SBF fee during its annual fee approval process as required by the Texas Administrative Code”.*

*The PUC has had an established process for calculating the amount required to fund the appropriated SBF expenditures and projected revenue requirements, but the procedures for the process was not formally documented. As noted during the audit, because the General Appropriations Act has contemplated that the State would receive revenues at the maximum statutory rate, that has essentially dictated that the PUC retain the rate at that level. The PUC's SBF Program Administrator has developed written policies*

*and procedures to perform the more detailed analysis suggested and to ensure more detailed information is being presented annually to the Commissioners. The formal policies and procedures were approved by the PUC's Director of Operations and the formal procedures will be followed by the SBF Program Administrator during the SBF fee approval process in 2012.*

*The Public Utility Commission concurs with the audit recommendation to "work to achieve consistency between Texas Administrative Code requirements regarding the SBF fee and Texas Utilities Code, Section 39.903(b)".*

*In order to implement the statutory requirement that the SBF fee be collected on the basis of kilowatt hours used, the PUC adopted rules requiring the fee to be adjusted for energy produced for consumers but not metered due to voltage line losses. This is a standard utility ratemaking principle. No party appealed the PUC rules or tariffs providing for this adjustment.*

*The SBF Program Administrator and the Rate Regulation division of the Public Utility Commission will review the Texas Administrative Code and the Texas Utilities Code to ensure the Texas Administrative code is in line with the Texas Utilities Code. In addition, the PUC intends to seek clarification of the intent of the Texas Utilities Code during the next legislative session.*

Chapter 1-B

**The Commission Should Verify the Accuracy of the Amount of SBF Fees the State Receives from Transmission and Distribution Utilities**

The Commission ensures that transmission and distribution utilities deposit SBF fees into the State Treasury; however, it does not verify the accuracy of the amount of SBF fees remitted to the State. The Commission receives only signed certifications from transmission and distribution utilities that the information regarding the SBF fees they deposit is factual and correct (see Appendix 4 for a copy of the certification.)

**SBF Revenues**

The SBF had revenues of \$149,603,723 in fiscal year 2009 and \$149,160,854 in fiscal year 2010. For those two fiscal years combined:

- 94 percent of SBF revenue came from SBF fees.
- 6 percent of SBF revenue came from interest earned.

See Appendix 2 for information related to SBF revenues.

Auditors tested SBF fee receipts for 4 months for 10 retail electric providers and determined that, on a net basis, the fee amounts the transmission and distribution utilities billed those retail electric providers may have been \$171,984 (0.6 percent) more than the fee amounts deposited into the SBF.<sup>2</sup> Auditors could not conclusively determine whether that amount was accurate due to various adjustments that may have been made prior to or after the months tested. However, the variance that auditors identified

<sup>2</sup> Transmission and distribution utilities bill retail electric providers for the SBF fees that the retail electric providers collect from utility customers. Transmission and distribution utilities then forward those fees to the State for deposit into the SBF.

between the amount billed and the amount deposited indicates that the Commission should monitor to ensure that the State receives the accurate amount of SBF fees based on the Commission-approved SBF fee. After auditors brought this matter to the Commission's attention, the Commission asserted that it has taken steps toward identifying a process that would allow it to ensure that the amount of SBF fees remitted to the State is accurate.

Auditors confirmed that the amount of SBF fees the transmission and distribution utilities certified they had sent to the SBF was deposited into the SBF.

### Recommendation

The Commission should develop and implement policies and procedures to ensure that the amount of SBF fees the State receives from the transmission and distribution utilities is accurate and based on the Commission-approved SBF fee.

### Management's Response

*The Public Utility Commission concurs with the recommendation that "The Commission should develop and implement policies and procedures to ensure that the amount of SBF fees the State receives from the transmission and distribution utilities is accurate and based on the Commission-approved SBF fee."*

*As noted in the SAO's audit report, the Public Utility Commission has taken steps toward identifying a process to help achieve the recommendation. The PUC's SBF Program Administrator will have a monitoring procedure in place to randomly verify the correct SBF fee is remitted to the State by the Transmission and Distribution Utilities by December 31, 2011.*

Chapter 1-C

### **The Commission Made Expenditures from the SBF in Accordance with Applicable Requirements**

The Commission properly accounted for its expenditures from the SBF in accordance with the Public Utility Regulatory Act (Texas Utilities Code, Title 2), the Texas Administrative Code, and General Appropriations Act requirements.

The Commission made expenditures from the SBF totaling \$103,998,769 in fiscal year 2009 and \$90,195,307 in fiscal year 2010. In fiscal year 2009, 95 percent of those expenditures were to reimburse retail electric providers for

the discounts they provided to eligible electricity customers through the discount program; in fiscal year 2010, 94 percent of expenditures were for that purpose. The majority of the remaining expenditures in fiscal years 2009 and 2010 were for professional services and fees and salaries and wages.

Table 1 summarizes the expenditures the Commission made from the SBF during fiscal years 2009 and 2010 (see Appendix 2 for additional information related to SBF expenditures).

Table 1

| Expenditures the Commission Made from the SBF |                      |                     |
|---|----------------------|---------------------|
| Category                                      | Fiscal Year 2009     | Fiscal Year 2010    |
| Discounts to Eligible Electricity Customers   | \$ 98,727,805        | \$ 84,982,060       |
| Professional Services and Fees                | 3,438,216            | 2,652,928           |
| Salaries and Wages                            | 1,473,559            | 2,108,343           |
| Employee Benefits                             | 183,383              | 198,750             |
| Interfund Transfers/Other                     | 94,004               | 115,376             |
| Printing and Reproduction                     | 0                    | 132,449             |
| Other Expenditures                            | 80,002               | 4,088               |
| Repairs and Maintenance                       | 1,800                | 0                   |
| Supplies and Materials                        | 0                    | 1,313               |
| <b>Totals</b>                                 | <b>\$103,998,769</b> | <b>\$90,195,307</b> |

Source: The Uniform Statewide Accounting System.

## The SBF Cash Balance Exceeded \$500 Million at the End of Fiscal Years 2009 and Exceeded \$600 Million at the End of Fiscal Year 2010

As discussed above, the SBF is funded by the SBF fee charged on customers' utility bills. Customers in deregulated markets pay the SBF fee, and the primary purpose of the SBF is to provide discounts on utility bills to eligible customers in those markets.

According to the Office of the Comptroller of Public Accounts' *Annual Cash Report*, the SBF first had a cash balance in fiscal year 2002<sup>3</sup> of \$50,228,804. The cash balance has continued to grow since fiscal year 2003 (see Appendix 3 for additional details regarding the SBF cash balance).

Table 2 shows the cash balance of the SBF at the end of fiscal years 2009 and 2010, and through the third quarter of fiscal year 2011.

Table 2

| SBF Cash Balance  |               |  |
|---|---------------|--|
| As of Date  | Cash Balance  | Percent Increase from Previous Fiscal Year |
| August 31, 2009   | \$548,823,167 | 9.1%                                       |
| August 31, 2010   | \$607,788,713 | 10.7%                                      |
| May 31, 2011 <sup>a</sup>   | \$672,283,016 | 10.6%                                      |
| <sup>a</sup> Auditors did not audit the cash balance as of May 31, 2011; the amount presented in this table was the cash balance on the Commission's financial statements as of May 31, 2011. |               |  |

Source: The Uniform Statewide Accounting System.

<sup>3</sup> In fiscal years 2002 and 2003, the System Benefit Trust Fund (Fund 0852) was used to collect the SBF fee and fund the discount program. In fiscal year 2003, the System Benefit Fund (Fund 5100) was established, and that is the fund currently in use.

## ***The Commission Should Ensure That Eligible Customers Receive Electricity Discounts; However, Its Process for Reviewing and Setting Discount Rates for the Discount Program Is Reasonable***

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The Commission should improve its monitoring of the contractor<sup>4</sup> that performs customer eligibility determinations for the discount program. Without adequate monitoring of the contractor, the Commission is unable to ensure that the contractor continues to properly process applications for the discount program and determine whether customers are eligible for the discount program.

The Commission also does not receive adequate supporting documentation for the reimbursement requests that retail electric providers submit for providing discounts to customers. However, auditors determined that 97 percent of customers tested received the correct discount amount on their utility bills.

The Commission has a reasonable process for reviewing and setting the discount rates for the discount program. Based on the discount percentages approved by the members of the Public Utility Commission, Commission staff accurately calculated the discount rates for each transmission and distribution utility for fiscal years 2009 and 2010.

### Chapter 2-A

## **The Commission Should Improve Its Monitoring of the Contractor That Determines Customer Eligibility for the Discount Program**

### **Discount Program Enrollment**

Electric customers can enroll in the discount program in two ways:

- A customer whose household income is at or below 125 percent of the federal poverty guideline can self-enroll in the discount program by submitting an application. The Commission's contractor processes self-enrollment applications.
- If customers receive assistance through Medicaid and/or the Supplemental Nutrition Assistance Program, the Commission's contractor enrolls them in the discount program.

After customers are enrolled in the discount program, the Commission's contractor notifies the customers' retail electric providers that the customers are eligible for the discount program.

The Commission's contractor processes applications to receive discounts from the discount program and determines which customers of retail electric providers are eligible for the discount program (see text box for additional details). However, the Commission has not conducted any audits or reviews of the contractor since the contract began on September 1, 2008. The Commission also does not require the contractor to obtain audits of its controls related to electricity discounts. For example, the Commission does not require the contractor to obtain an examination of its internal controls by an independent auditor in accordance with American Institute of Certified Public Accountants Statement on Auditing Standards No. 70 (referred to as a SAS 70 examination) or a similar review. The Commission asserted that a review of its contractor's internal controls will be completed by the end of fiscal year 2011.

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<sup>4</sup> The Commission refers to this contractor as the Low Income Discount Administrator (LIDA).

### Self-enrollment in the Discount Program

Although the contractor appropriately processed the majority of discount program self-enrollment applications that auditors tested, the Commission should monitor the contractor to ensure that the contractor continues to process applications correctly. The contractor accurately processed 58 (97 percent) of 60 applications that auditors tested. Based on the eligibility requirements in Title 16, Texas Administrative Code, Section 25.454(f)(2), the contractor approved one application it should have rejected, and it rejected another application it should have approved; both errors occurred because the contractor incorrectly calculated the applicants' annual income.

### Determining Which Customers of Retail Electric Providers Are Eligible for the Discount Program

#### Average Number of Electric Customers Eligible for the Discount Program

An average of 481,868 electricity customers were determined to be eligible for the discount program in fiscal year 2009; an average of 555,515 electricity customers were determined to be eligible in fiscal year 2010.

The contractor's process to determine which electric customers are eligible for the discount program did not identify certain eligible customers that auditors identified, but that group of customers represented only 0.5 percent of the eligible customers that the contractor had identified. However, without sufficient monitoring of the contractor, the Commission is unable to ensure that the contractor continues to properly determine which customers are eligible for discounts.

### Recommendation

The Commission should develop and implement policies and procedures to adequately monitor its contractor to ensure that the contractor accurately determines discount program eligibility for electric customers.

### Management's Response

*The Public Utility Commission concurs with the State Auditor's Office recommendation that "The Commission should develop and implement policies and procedures to adequately monitor its contractor to ensure that the contractor accurately determines discount program eligibility for electric customers".*

*An SSAE 16 (formerly SAS 70) audit of the internal controls of the contractor's discount program was in process before the SAO audit started. The SSAE 16 audit will be completed by August 31, 2011. In addition, an SSAE 16 audit of the internal controls of the contractor's discount program will be conducted annually. The PUC's SBF Program Administrator will also develop and implement policies and procedures to ensure that the contractor accurately determines discount program eligibility for electric customers by December 31, 2011.*

## The Commission Should Improve Processes for Reimbursing the Retail Electric Providers That Give Discounts; However, 97 Percent of Customers Tested Received the Correct Discount Amount

### Reimbursements

After retail electric providers give electric discounts to customers, they submit reimbursement requests to the Commission. The Commission then reimburses the retail electric providers for the amounts they request. However, the Commission does not receive adequate supporting documentation for retail electric providers' reimbursement requests to ensure that they are accurate. The Commission receives only summary level, self-reported information from the retail electric providers, and it does not request detailed information regarding electric discounts.

Along with their reimbursement requests, retail electric providers submit a "Certification of Responsible Official" on which they certify that the information in the request is factual and correct (see Appendix 4 for that certification). The Commission relies on that certification to ensure the accuracy of the information that retail electric providers submit. However, when auditors requested summary level supporting documentation from 5 retail electric providers for a combined sample of 44 months of reimbursements, the supporting documentation they provided did not always match the reimbursement requests they had originally submitted to the Commission. Specifically:

- For 3 (7 percent) of the 44 months tested, the amounts of the reimbursements requested differed from the amounts on the supporting documentation. For two months, reimbursement amounts requested exceeded the amounts on the supporting documentation. For one month, the reimbursement amount requested was less than the amount on the supporting documentation.
- For 4 (9 percent) of the 44 months tested, the number of kilowatt hours on the reimbursement requests differed from the number of kilowatt hours on the supporting documentation. For one month, the number of kilowatt hours on the reimbursement request exceeded the number of kilowatt hours on the supporting documentation. For three months, the numbers of kilowatt hours on the reimbursement requests were less than the numbers of kilowatt hours on the supporting documentation.
- For 3 (7 percent) of the 44 months tested, the numbers of discounts given as reported on the reimbursement request differed from the numbers of discounts given in the supporting documentation. For one month, the number of discounts given on the reimbursement request exceeded the number of discounts given on the supporting documentation. For two

months, the numbers of discounts given on the reimbursement requests were less than the numbers of discounts given on the supporting documentation.

It is possible that the supporting documentation differed from the reimbursement requests because of adjustments that retail electric providers are allowed to make; but without performing some type of verification, the Commission cannot ensure that retail electric providers are requesting correct reimbursement amounts.

The Commission performs only a limited number of audits each year of retail electric providers' compliance with discount program requirements and has assigned one staff person to compliance monitoring for the discount program. That individual also is responsible for conducting compliance monitoring for other programs. According to the Commission, that individual completes two to three audits of retail electric providers every two years and a limited number of desk reviews annually for the discount program. However, those desk reviews are based on high-level information that retail electric providers submit to the Commission and high-level reports that the Commission's contractor submits to the Commission. A total of 54 retail electric providers participated in the discount program during fiscal years 2009 and 2010.

#### Accuracy of Discounts

Customers who are eligible for the discount program receive a discount on their utility bills based on Commission-approved rates. That discount applies to the rate the customers pay for the number of kilowatt hours used during the billing cycle. The discount program operates from May through September during years when the discount program is funded (see Appendix 3 for additional details regarding the funding of the discount program).

#### Discount Statistics

For the 150 customers that auditors tested:

- The average kilowatts used per billing cycle was 1,324 kilowatts.
- The average rate paid per kilowatt hour was 12 cents.
- The average discount amount per billing statement was \$35.08.
- The average discount as a percentage of the total billing statement was 20 percent.

Auditors reviewed a sample of billing statements from five retail electric providers. For the 150 customers eligible for the discount program that auditors tested:

- 146 (97.3 percent) received the correct discount amount on their utility bills.
- 3 (2.0 percent) did not receive a discount when they were eligible.
- 1 (0.7 percent) received only a portion of the discount for which the customer was eligible.

## Recommendation

The Commission should develop and implement policies and procedures to adequately verify that reimbursement requests the retail electric providers submit are accurate.

## Management's Response

*The PUC already has detailed written policies and procedures to verify that reimbursement requests the retail electric providers submit are accurate. The PUC sent audit notification letters to four retail electric providers in June 2011. As noted in the SAO's audit report, the strategy of conducting a limited number of audits of retail electric provider's compliance with the discount program requirements was necessitated by having only one staff assigned to compliance monitoring for both the SBF and other programs.*

*The PUC has a strategy to substantially increase the number (and frequency) of audits of retail electric providers by soliciting assistance from the program administrator to assist the PUC in conducting some of the audits on an annual basis. This should provide a larger population of review and assist the PUC in verifying reimbursement request submitted by retail electric providers.*

Chapter 2-C

## The Commission Has a Reasonable Process for Reviewing and Setting Discount Rates for the Discount Program

The Commission sets discount rates for the discount program in accordance with Title 16, Texas Administrative Code, Section 25.454(e)(1). Specifically:

- The Commission estimates the number of discount customers, the expected kilowatt usage, and the weighted average of the “provider of last resort” rates (see text box for information on provider of last resort). Based on those factors, it determines the discount percentage that can be given within the amount appropriated for the discounts.

### Provider of Last Resort

The provider of last resort serves as a back-up electric service provider in the competitive retail electric market if a retail electric provider leaves the market.

Provider of last resort service is a safety net for customers whose chosen retail electric provider discontinues providing service. Customers can also request provider of last resort service.

For fiscal year 2009, the members of the Public Utility Commission set the discount percentage at 20 percent for September 2008, 15.5 percent for May 2009 through July 2009, and 17 percent for August 2009. For fiscal year 2010, the discount percentage remained at 17 percent (fiscal year 2010 program months included September 2009 and May 2010 through August 2010). (See

Appendix 3 for additional details regarding the discount percentages the Commission sets.)

- Commission staff then use the discount percentage to calculate the discount rates applicable to each transmission and distribution utility. Those discount rates determine the amount of the discount an individual customer will receive.

Based on the applicable discount percentages and provider of last resort rates, the Commission calculated the discount rates for each transmission and distribution utility correctly for fiscal years 2009 and 2010.

# Appendices

Appendix 1

## **Objectives, Scope, and Methodology**

---

### **Objectives**

The objectives of this audit were to:

- Determine whether the Public Utility Commission (Commission) makes expenditures from the System Benefit Fund (SBF) for the Low-Income Electric Discount Program (discount program) in accordance with applicable laws, regulations, and policies and procedures.
- Verify the accuracy of the cash balance in General Revenue Dedicated Account – System Benefit Fund 5100 at the end of fiscal years 2009 and 2010.

### **Scope**

The scope of this audit covered SBF revenues, transfers, and expenditures from September 1, 2008, through August 31, 2010; Commission processes for analyzing, reviewing, and determining the amount of the SBF fee and discount rates for the discount program; and discount program eligibility processes.

### **Methodology**

The audit methodology included reviewing a sample of discount program self-enrollment applications and associated supporting documentation from the Commission's contractor; verifying the contractor's discount program eligible customer lists for a sample of retail electric providers for selected months; reviewing a sample of customer billing statements from a sample of retail electric providers; reviewing a sample of retail electric providers' reimbursement requests; reviewing a sample of expenditures, revenues, transfers, and associated supporting documentation for the SBF for fiscal years 2009 and 2010; reviewing and recalculating the amount of the SBF fee charged to customers; reviewing the Commission's processes for analyzing and determining the SBF fee and discount rates for the discount program; and interviewing Commission management and staff.

To assess the reliability of (1) the discount program self-enrollment application data the Commission's contractor provided and (2) reimbursement request data from the Commission's SBF system, auditors:

- Reviewed the data for accuracy and completeness by reviewing database schemata, verifying record counts, and performing a high-level review of data fields and contents for appropriateness.
- Interviewed Commission and contractor staff with knowledge about the data.
- Traced a sample of data to source documents.

Auditors also relied on prior audit work the State Auditor’s Office conducted to assess the reliability of Uniform Statewide Accounting System (USAS) data. Auditors determined that USAS data was sufficiently reliable for the purposes of this audit.

Auditors did not determine the reliability of (1) data received from retail electric providers and (2) eligible customer lists for the discount program from the Commission’s contractor. However, that data was not the primary focus of this audit. Auditors used that data only to substantiate information the Commission maintained.

Information collected and reviewed included the following:

- Contract between the Commission and the contractor that performs customer eligibility determinations for the discount program.
- Commission policies and procedures.
- Commission orders approving the SBF fee and discount percentages.
- Discount program self-enrollment applications and supporting documentation that the Commission’s contractor provided.
- Retail electric provider customer lists that the Commission’s contractor provided.
- List of customers eligible for the discount program that the Commission’s contractor provided.
- Customer billing statements that retail electric providers provided.
- Provider of last resort rates for fiscal years 2009 and 2010.
- Commission-calculated discount rates for fiscal years 2009 and 2010.
- Retail electric provider discount reimbursement requests and associated supporting documentation for fiscal years 2009 and 2010.
- Financial transactions from USAS and associated supporting documentation.

- SBF fee billing statements that retail electric providers provided.
- Transmission and distribution utility SBF fee remittance reports that the Commission provided.

Procedures and tests conducted included the following:

- Interviewed Commission management and staff.
- Tested a sample of discount program self-enrollment applications and supporting documentation.
- Verified the list of eligible customers for the discount program and compared it to the list created by the Commission's contractor.
- Tested a sample of retail electric providers' customer billing statements to determine whether customers who were eligible for the discount program received accurate discounts.
- Compared the number of discounts offered to the number of approved customers who were eligible for the discount program for selected retail electric providers.
- Traced a sample of retail electric providers' discount program reimbursement requests to supporting documentation, payment vouchers, and USAS expenditure data.
- Tested a sample of SBF expenditures, transfers, and revenues for fiscal years 2009 and 2010.
- Traced a sample of SBF fee billing statements that retail electric providers provided to associated remittance reports submitted during fiscal years 2009 and 2010.
- Recalculated the SBF fee for the remittance reports that transmission and distribution utilities submitted during fiscal years 2009 and 2010, and compared that information to the Commission-approved fee amount.
- Reviewed Commission orders and processes for approving the SBF fee and discount percentages for fiscal years 2009 and 2010.

Criteria used included the following:

- Texas Utilities Code, Chapter 39.
- General Appropriations Acts (80th and 81st Legislatures).
- Title 16, Texas Administrative Code, Chapter 25.

- Contract between the Commission and the contractor that performs customer eligibility determinations for the discount program.
- Commission orders.

### **Project Information**

Audit fieldwork was conducted from April 2011 through June 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. While auditors did not determine the reliability of certain data received from retail electric providers and the Department's contractor as discussed above, we believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Hillary Eckford, CIA (Project Manager)
- Robert Pagenkopf (Assistant Project Manager)
- Barbette Mays
- Tamara Shepherd, CGAP
- Steven M. Summers, CPA, CISA
- Leslie Ashton, CPA (Quality Control Reviewer)
- Michelle Ann Duncan Feller, CPA, CIA (Quality Control Reviewer)
- James Timberlake, CIA (Audit Manager)

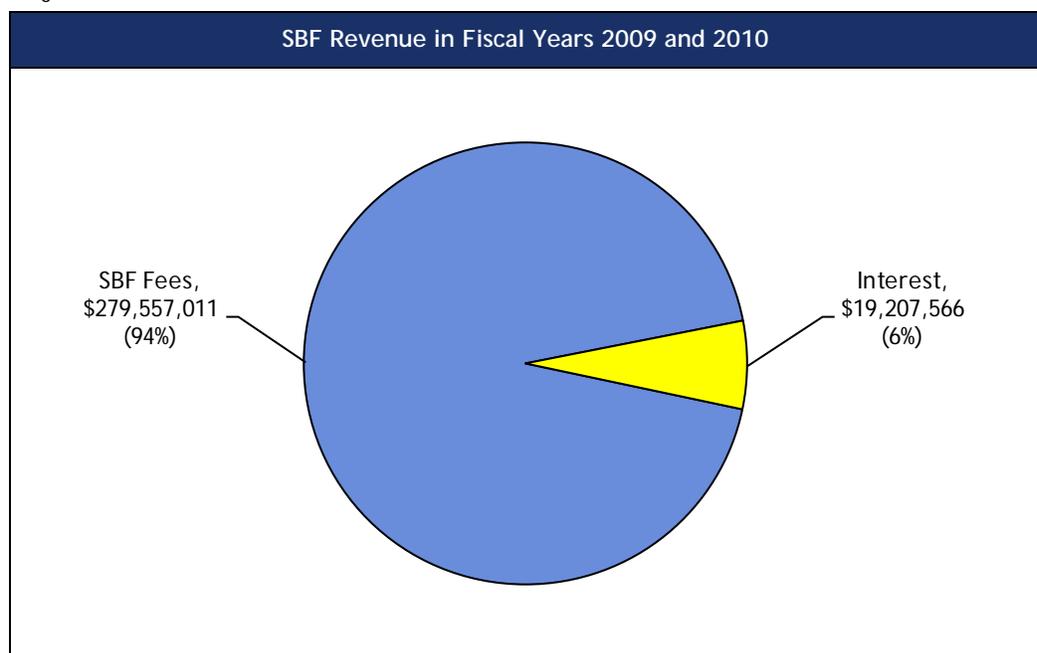
## Summary of SBF Revenue and Expenditures in Fiscal Years 2009 and 2010

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The System Benefit Fund (SBF) receives the majority of its revenue from the nonbypassable SBF fee that business and residential customers in competitive energy markets are charged on their electric bills. The Public Utility Commission (Commission) approved and set the SBF fee at 65 cents per megawatt hour, the statutory maximum, during fiscal years 2009 and 2010. Other SBF revenue comes from interest earned on the SBF.

Figure 1 shows the sources of SBF revenue in fiscal years 2009 and 2010.

Figure 1

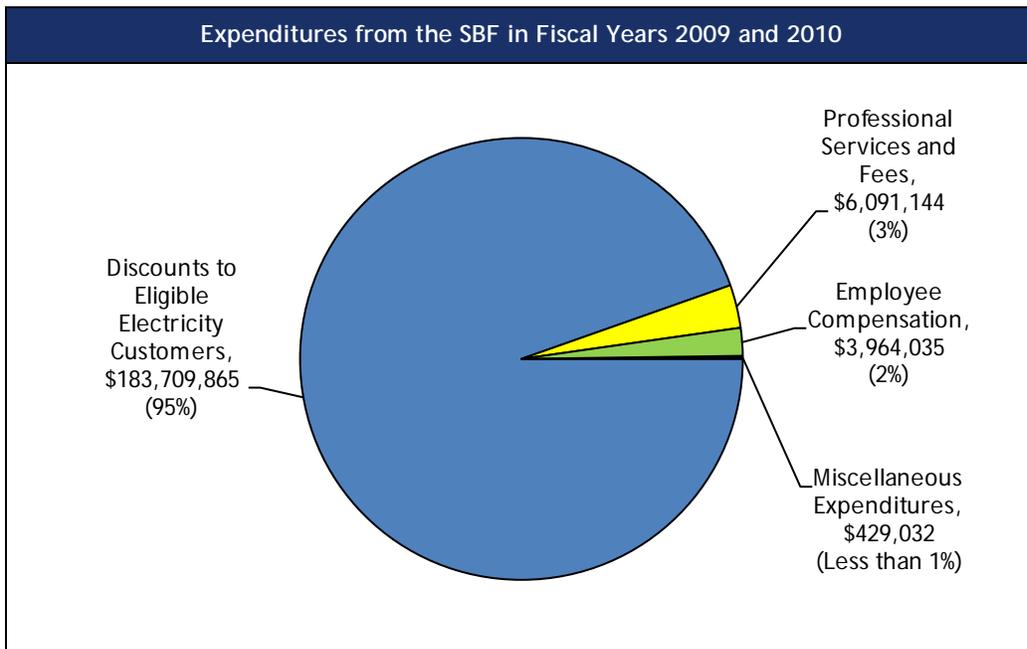


Source: The Uniform Statewide Accounting System.

The General Appropriations Act authorizes the Commission to make expenditures from the SBF. In fiscal years 2009 and 2010, the majority of the expenditures from the SBF were in the form of discounts to eligible electricity customers through the Low-Income Electric Discount Program.

Figure 2 shows expenditures from the SBF in fiscal years 2009 and 2010.

Figure 2



Source: The Uniform Statewide Accounting System.

## ***SBF and Discount Program Historical Information***

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The Public Utility Commission (Commission) has approved and set the System Benefit Fund (SBF) fee at 65 cents per megawatt hour, the statutory maximum, since fiscal year 2002.

The Commission evaluates and approves the Low-Income Electric Discount Program (discount program) discount percentage. Table 3 presents the Commission-approved discount percentages since the discount program started in fiscal year 2002.

Table 3

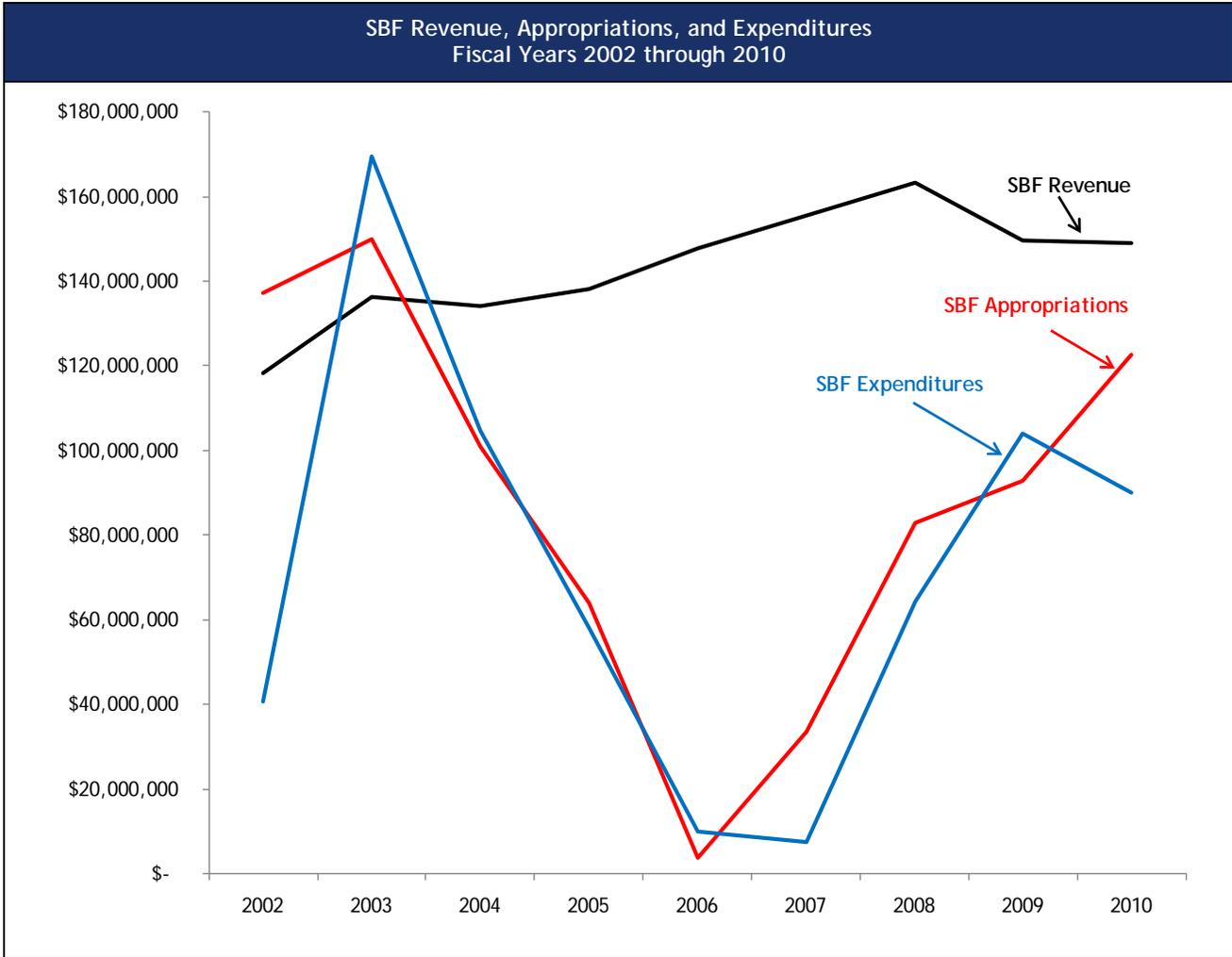
| Commission-approved Discount Percentages                                      |                     |
|---|---------------------|
| Effective Date  | Discount Percentage |
| September 1, 2001   | 10.0%               |
| June 1, 2002  | 17.0%               |
| September 1, 2003   | 10.0%               |
| July 1, 2007  | 12.0%               |
| May 1, 2008   | 20.0%               |
| July 9, 2008  | 20.0%               |
| March 12, 2009  | 15.5%               |
| August 1, 2009 <sup>a</sup>   | 17.0%               |
| <sup>a</sup> This discount percentage was in effect through fiscal year 2010. |                     |

Source: The Commission.

Customers pay the SBF fee all 12 months of the year; however, the Commission administers the discount program from May through September in years when the program has been funded.

Figure 3 presents SBF revenue, appropriations, and expenditures for fiscal years 2002 through 2010.

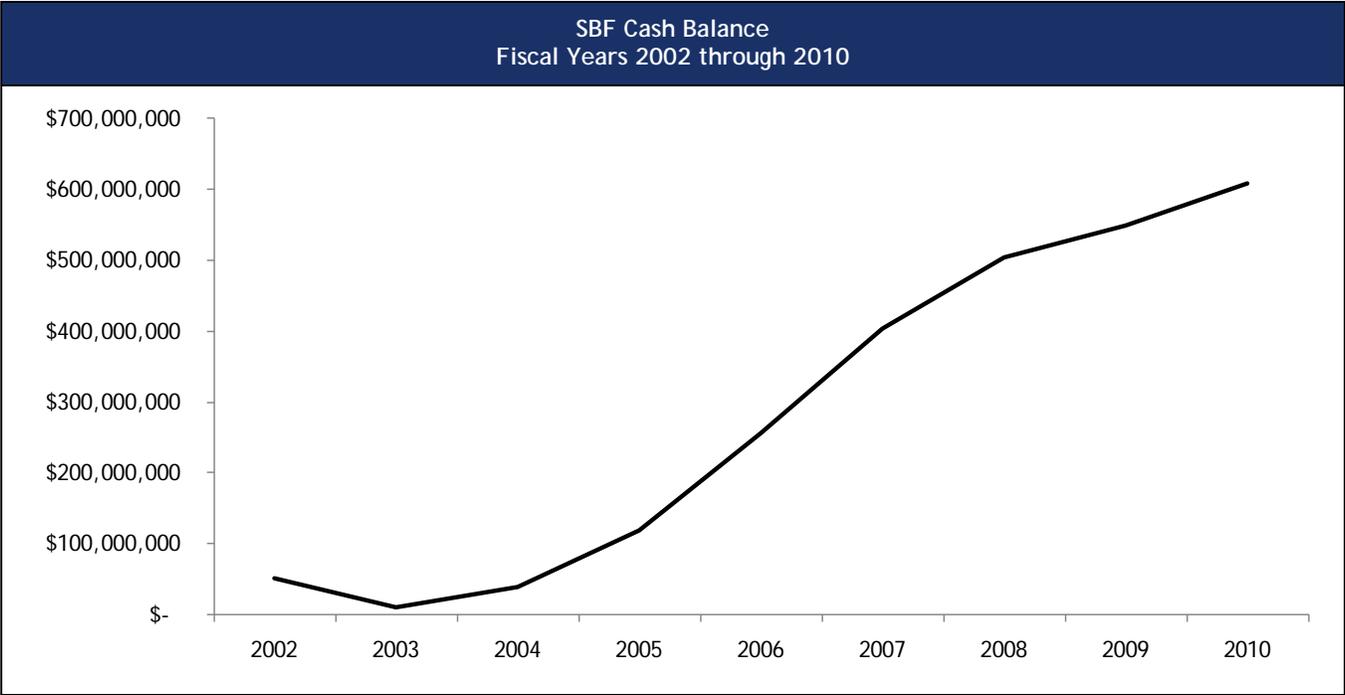
Figure 3



Sources: The Uniform Statewide Accounting System; General Appropriations Acts (77th through 81st Legislatures); House Bill 10 (79th Legislature); and House Bill 15 (80th Legislature).

Figure 4 presents the trend in the SBF cash balance from fiscal year 2002 through fiscal year 2010. The SBF cash balance was \$607,788,713 at the end of fiscal year 2010.

Figure 4



Source: The Uniform Statewide Accounting System.

## ***Certifications That Transmission and Distribution Utilities and Retail Electric Providers Submit to the Commission***

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Transmission and distribution utilities bill retail electric providers for the System Benefit Fund (SBF) fees that the retail electric providers collect. Transmission and distribution utilities then forward those fees to the State for deposit into the SBF.

Figure 5 presents the certification that transmission and distribution utilities submit to the Public Utility Commission (Commission) regarding the SBF fees collected.

Figure 5

| Transmission and Distribution Utility Certification<br>Regarding SBF Fees Collected   |                      |
|---|----------------------|
| <u>Certification of Responsible Official</u>  |                      |
| I certify that I am the responsible official of _____; that I have examined the System Benefit Fund Fee Remittance Report of said company, submitted electronically on this date; that to the best of my knowledge, information, and belief, all statements of fact contained in the said report are true and the said report is a correct statement of the business and affairs of the above-named respondent in respect to each and every matter set forth therein during the period stated. I also acknowledge that I am aware of the records retention and audit provisions of P.U.C. Substantive Rule 25.451(i). |                      |
| _____   | _____                |
| Date  | Responsible Official |
|   | _____                |
|   | Title                |

Source: The Commission.

Retail electric providers factor discounts from the Low-Income Electric Discount Program into the utility bills they send to eligible customers. The retail electric providers then request reimbursements for those discounts from the Commission. The Commission uses SBF funds to reimburse the retail electric providers.

Figure 6 presents the certification that retail electric providers submit to the Commission regarding the discounts for which the retail electric providers request reimbursement.

Figure 6

The screenshot shows a web form titled "Retail Electric Provider Certification Regarding Discounts for Which the Retail Electric Providers Request Reimbursement". The form contains a section titled "Certification of Responsible Official" with the following text: "I certify that I am the responsible official of and that to the best of my knowledge, information, and belief, all statements of fact contained in this report are true and this report is a correct statement of the business and affairs of the above-named respondent in respect to each and every matter set forth in this report during the period stated. I also acknowledge that I am aware of the records retention and audit provisions of P.U.C. Substantive Rule 25.451(i)." Below the text is a text input field with the placeholder "Type your name" and a "Submit" button.

Source: The Commission.

## Overall Response from Commission Management

**Donna L. Nelson**  
Commissioner

**Kenneth W. Anderson, Jr.**  
Commissioner

**Brian H. Lloyd**  
Executive Director



**Rick Perry**  
Governor

### *Public Utility Commission of Texas*

July 12, 2011

Ms. Hillary Eckford  
Project Manager  
State Auditor's Office  
Robert E. Johnson, Sr. Building  
1501 N. Congress Avenue  
Austin, Texas 78701

Dear Ms. Eckford:

The Public Utility Commission of Texas (PUC) appreciates the opportunity to respond to the State Auditor's Office Audit Report on the PUC's Administration of the System Benefit Fund and the Low-income Electric Discount Program. The Commission agrees with all the recommendations contained in the report, and has already begun to address the majority of the recommendations.

While we are very pleased with the success of fund and the program, we continue to devote considerable resources to improving the administration of the fund and the discount program. We will take the recommendations from the State Auditor's report and continue to refine and enhance the processes currently in place.

Thank you for the cooperative attitude you and your team extended throughout the audit. If you have any questions, please contact me at 512-936-7040.

Sincerely,

  
Brian H. Lloyd  
Executive Director

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1701 N. Congress Avenue PO Box 13326 Austin, TX 78711 512/936-7000 Fax: 512/936-7003 web site: [www.puc.state.tx.us](http://www.puc.state.tx.us)

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The Honorable Steve Ogden, Senate Finance Committee

The Honorable Thomas “Tommy” Williams, Member, Texas Senate

The Honorable Jim Pitts, House Appropriations Committee

The Honorable Harvey Hilderbran, House Ways and Means Committee

### **Office of the Governor**

The Honorable Rick Perry, Governor

### **Public Utility Commission**

Members of the Public Utility Commission

Mr. Kenneth W. Anderson, Jr.

Ms. Donna L. Nelson

Mr. Brian Lloyd, Executive Director



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