

Los Angeles  Department of Water & Power

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General Manager

April 20, 2015

The Honorable City Council
c/o Office of the City Clerk
Room 395, City Hall
Mail Stop 160

Honorable Members:

Subject: Audit of the Loan Program for the Calendar Year Ended
December 31, 2014

Los Angeles Administrative Code (LAAC) Section 23.141 requires that audits be conducted to validate the number of the loan agreements that the Los Angeles Department of Water and Power (LADWP) entered into, to analyze and summarize delinquency and default rates by borrowers, to determine administrative costs and expenses, and to verify whether the requirements stipulated in LAAC Section 23.141 have been met. Section 23.141 also requires that the General Manager report the audit findings to the City Council on at least an annual basis.

Enclosed, please find the report on the Audit of Compliance with the Loan Program Requirements under LAAC Section 23.141 for the Calendar Year Ended December 31, 2014, completed by the Internal Audit Division of the LADWP.

There were 80 loans totaling \$81.4 million awarded from 2002 to 2014, of which nine loans totaling \$6.8 million were outstanding as of December 31, 2014. Two outstanding loans were made to other City Departments, totaling \$5.6 million and the remaining seven loans, totaling \$1.2 million, were made to other qualified LADWP customers.

The audit concludes that the Loan Program is in compliance with the requirements stipulated in LAAC Section 23.141 and no loans defaulted during 2014.




Los Angeles Aqueduct Centennial Celebrating 100 Years of Water 1913-2013

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The Honorable City Council

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If you have any questions, please call me at (213) 367-1338, or have a member of your staff contact Ms. Winifred J. Yancy, Director of Intergovernmental Affairs and Community Relations, at (213) 367-0025.

Sincerely,

A handwritten signature in blue ink, appearing to read 'MLE', with a long horizontal flourish extending to the right.

Marcie L. Edwards
General Manager

JT:jt

Enclosure

c/enc: The Honorable Councilmembers
Mr. Miguel A. Santana, City Administrative Officer
Ms. Sharon M. Tso, Chief Legislative Analyst
Ms. Winifred J. Yancy

**FINANCIAL SERVICES ORGANIZATION
INTERNAL AUDIT DIVISION**

March 24, 2015

**AUDIT OF COMPLIANCE
WITH THE LOAN PROGRAM REQUIREMENTS
UNDER LOS ANGELES ADMINISTRATIVE CODE SECTION 23.141
FOR THE CALENDAR YEAR ENDED DECEMBER 31, 2014**

BACKGROUND

As required by Los Angeles Administrative Code (LAAC) Section 23.141(i), we have completed an audit of compliance with the Loan Program Requirements under LAAC Section 23.141, for the calendar year ended December 31, 2014.

The Loan Program was originally authorized by Ordinance Number 172606 and Los Angeles Department of Water and Power (LADWP) Board Resolution 002-170. It was later amended by Ordinance Number 182721. The ordinances are codified under LAAC Section 23.141.

LAAC Section 23.141 allows the LADWP to enter into loan agreements with its customers for solar energy, utility infrastructure, water conservation, and energy efficiency projects.

LAAC Section 23.141 Subsection (i) requires that audits be conducted to validate the number of loan agreements entered into, to analyze and summarize delinquency and default rates by customers, to determine the amount of administrative costs and expenses, and to verify whether the conditions described in LAAC Section 23.141 have been satisfied. The General Manager and Chief Financial Officer shall report the audit findings to the Board of Water and Power Commissioners and to the City Council on at least an annual basis.

The prior audit of the loan program was published on February 28, 2014.

The Energy Efficiency Division administers the energy efficiency and water conservation loans to various Los Angeles City Departments (City Departments).

The Economic Development Division administers the utility infrastructure loans to new and existing commercial and industrial LADWP customers, and Los Angeles Convention Center.

PURPOSE

Our objectives were to validate the number of loans awarded, to analyze and summarize delinquency and default rates by customers, to determine the amount of administrative costs and expenses, and to verify whether the requirements described in the LAAC Section 23.141 (b) through (h), relating to the qualification of borrowers, interest rates charged, loan amount limits, credit checking and other requirements, have been met.

SCOPE

The audit covered nine outstanding loans with a total amount of \$6,783,481 as of December 31, 2014. We reviewed the requirements under LAAC Section 23.141, analyzed the population of outstanding loans for compliance with general requirements and stratified the loans according to types. The nine outstanding loans were comprised of one energy efficiency loan and one water conservation retrofit loan to two City Departments, and seven utility infrastructure loans granted to other qualified LADWP commercial customers.

Of the nine outstanding loans, six of them were reviewed in the prior audits. The remaining three loans issued in CY2014 were tested during the current audit, totaling \$6,005,836 and representing 89 percent of the total outstanding loan amount, or 33 percent of the total number of outstanding loans.

CONCLUSION

Under the Loan Program, 80 loans totaling \$81.4 million were awarded from 2002 to 2014. As of December 31, 2014, of the nine outstanding loans totaling \$6.8 million, two were made to various City Departments, totaling \$5.6 million. The remaining seven loans, totaling \$1.2 million, were made to other qualified LADWP customers.

The aggregate outstanding loans made to LADWP customers other than the City of Los Angeles did not exceed the \$15 million limit, as stipulated under LAAC Section 23.141 (g).

The recovery periods of all the loans issued before October 30, 2013 did not exceed the 10-year limit set by the previous version of LAAC Section 23.141 (e). The three new loans issued in 2014 did not exceed the 20-year limit as set by the amended recovery period requirement, which became effective October 30, 2013.

Credit checks were performed on all loans, except for the loans made to other City Departments, as required under LAAC Section 23.141 (h).

The prior audit report dated March 25, 2008 noted two loans in default with a combined outstanding balance of \$190,725. Through litigation, the borrower agreed to pay \$160,000 plus interest at an annual rate of 5.4 percent in three

installments. The City Attorney's Office has successfully collected \$113,333 and is in the process of collecting the remaining balance. No additional loan delinquencies have occurred since 2008.

Administrative costs for the Loan Program include costs for loan application, loan processing and loan servicing. The loan application and processing costs increased by 69 percent from calendar year 2013 because extra hours were spent on processing the application by the Department of General Services for a Water Conservation Retrofits loan, and a loan Memorandum of Understanding (MOU) amendment to Department of Public Works. Additionally, more time was spent on credit check and financial review of a loan application from a commercial customer. The loan servicing costs increased by two percent mainly due to the changes of labor distribution rates.

Calendar Year:	<u>CY 2013</u>	<u>CY 2014</u>	<u>Difference</u>	<u>Percentage</u>
Loan Application & Processing Costs:	\$12,402	\$21,007	\$8,605	69%
Loan Service Costs:	\$8,758	\$8,937	\$179	2%
	<u>\$21,160</u>	<u>\$29,944</u>	<u>\$8,784</u>	<u>42%</u>

The total LADWP percentage cost of processing and servicing the loans for the last three calendar years were significantly below the average interest rates charged by the LADWP, as illustrated below:

	<u>CY 2012</u>	<u>CY 2013</u>	<u>CY 2014</u>	<u>Average</u>
Total Loan Processing and Servicing Costs	\$19,690	\$21,160	\$29,944	\$23,598
Amounts of the Total Outstanding Loans	\$43,869,848	\$1,022,870	\$6,783,481	\$17,225,400
Percentage Cost of Processing and Servicing the Loans	<u>0.04%</u>	<u>2.07% *</u>	<u>0.44%</u>	<u>0.14%</u>
Average Interest Rate Charged :	<u>5.29%</u>	<u>5.23%</u>	<u>4.92%</u>	<u>5.15%</u>

* The percentage was higher than CY 2012 and CY 2014 as a result of lower amount of outstanding loans primarily due to 10 City loans paid-off in full during CY 2013, totalling \$48.9 million.

For a detailed analysis of administrative costs, please see Attachment 1.

To conclude, the Loan Program was in compliance with the requirements stipulated in LAAC Section 23.141.


 Florence Kong
 Internal Auditor


 Lucy Chou, CPA, CFE
 Senior Internal Auditor

Calendar Year 2014 Administrative Cost Analysis

Administrative costs for the Loan Program include costs for loan application, loan processing and loan servicing. The total administrative costs, percentage, and average interest rates charged for the last three calendar years are as follows:

	<u>CY 2012</u>	<u>CY 2013</u>	<u>CY 2014</u>	<u>Average</u>
Loan Application & Processing Costs:	\$7,468	\$12,402	\$21,007	\$13,626
Loan Service Costs:	\$12,222	\$8,758	\$8,937	\$9,972
Total Administrative Cost:	<u>\$19,690</u>	<u>\$21,160</u>	<u>\$29,944</u>	<u>\$23,598</u>

Loan application and processing costs include labor costs for review of technical specifications, credit evaluation, financial analysis, and the preparation, review and approval of the loan package. The application and processing costs per loan application for the last three calendar years are as follows:

	<u>CY 2012</u>	<u>CY 2013</u>	<u>CY 2014</u>	<u>Average</u>
Loan Application & Processing Costs:	\$7,468	\$12,402	\$21,007	\$13,626
Loans Processed:	4	12	4	7
Processing Cost per loan:	<u>\$1,867</u>	<u>\$1,034</u>	<u>\$5,252</u>	<u>\$2,044</u>

Loan servicing costs include the preparation and approval of invoices sent to loan recipients and other administrative tasks. The service costs per outstanding loan for the last three calendar years are as follows:

	<u>CY 2012</u>	<u>CY 2013</u>	<u>CY 2014</u>	<u>Average</u>
Loan Service Costs:	\$12,222	\$8,758	\$8,937	\$9,972
Loans Outstanding:	17	7	9	11
Annual Invoicing Cost per loan:	<u>\$719</u>	<u>\$1,251</u>	<u>\$993</u>	<u>\$907</u>