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INSPECTOR GENERAL

September 2006

To: George Cannelos, Federal Co-Chair

FINAL REPORT

From: Mike Marsh, Inspector General

FOR PUBLIC RELEASE

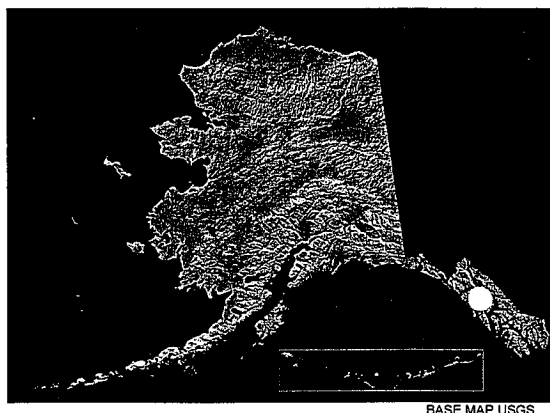
Subject: Inspection of Tenakee Springs power plant project

On August 4, 2006, I conducted a routine inspection of the power plant currently under construction at Tenakee Springs, Alaska. The purpose of this inspection was to confirm (1) activity at the project site and (2) the traceability of individual expenditures within the total reported to the Commission on OMB Form 269A.

The Denali Commission's strategic plan aspires that "[a]ll Alaska, *no matter how isolated*, will have the physical infrastructure necessary to protect health and safety and to support self-sustaining economic development."¹ The Commission uses its implementing "program partner," the Alaska Energy Authority (AEA), to address self-supporting rural electrification in some of the most isolated locations in America. Tenakee Springs (pop. $\approx$ 100) lies deep among the rain forest islands of southeast Alaska and is one of those places.²

This is one of three Denali-funded power plants that AEA was actively constructing in late summer. I have inspected all three (the other two are at Buckland and Manokotak).

During the inspection process, I received exemplary cooperation from AEA, the City of Tenakee Springs, and the staff of the Denali Commission.



¹ Denali Commission Five Year Strategic Plan (2005-2009), p. 3 (emphasis added).

² Tenakee Springs is a small (pop. $\approx$ 100), rural, incorporated settlement in the "panhandle" of southeast Alaska. It is located on a large island between Juneau and Sitka. No roads, railroads, or power grids lead to Tenakee Springs. Access is by weather-challenged floatplanes and a weekly visit by the state ferry.

Prior to this inspection, I reviewed records kept at both the Denali Commission and AEA. The project at Tenakee Springs is totally funded by the Denali Commission and anticipated to cost about \$1.3 million. As of late June 2006, AEA reported total expenditures of around \$1 million.

Conclusions

Nothing in this inspection indicated any need for the Denali Commission to change its selection of a program partner or its continued funding of this particular project.

Expenditure traceability

This power plant project was funded as part of two "lump sum" awards to AEA that cover numerous other projects around the state.³ Nevertheless, computerized accounting records at AEA readily enabled a transparent, traceable "roll-up" from individual project expenditures, to project totals, to the cumulative expenditures reported⁴ on OMB Form 269A. This form has been filed timely with the Commission. Physical records kept at both the Commission and AEA were well-organized and readily reviewable during the inspection.

Project's physical status

My inspection verified that a facility consistent with AEA's project records is now under physical construction at the expected site in Tenakee Springs. The power plant building had been brought to the site as an intact module,⁵ and I observed that all major components had been installed inside. My observations at the site were consistent with the photographs that AEA has previously submitted for public display on the Commission's online project database at www.denali.gov.

Control over purchases

In my review of AEA's accounting records, I judgmentally selected various expenditures of interest for further study. AEA provided a plausible and acceptable need for the items sampled.

Documentation (e.g., invoices) was readily available and consistently supported the purchases, with one exception. The purchase of another project's computer (\$1,478) was erroneously charged to this project.

³ Denali Commission award nos. 48-DC-2002-II, 165-05.

⁴ As of the second quarter of federal fiscal year 2006.

⁵ The preassembled module was barged all the way from Anchorage, and the ingenious transfer to its mountainside perch almost warrants one of those *Modern Marvels* episodes.

This barged module approach is reminiscent of the power plant barges that the *Wall Street Journal* reported innovative companies were trying a decade ago in developing nations. (See William M. Bulkeley, "More Power Plants Are Floating Off Developing Nations," *Wall Street Journal*, May 22, 1996, p. B1.) However, the latter facilities, unlike the one at Tenakee, were meant to be readily removed if conditions deteriorated. Fortunately, the power plant at Tenakee Springs has a bigger issue with brown bears than the stability of its national government.

The electrification of Alaska definitely has its unique challenges. In the week following my inspection at Tenakee Springs, a seven-foot bear had a 5000-volt line as its last meal in the far more urban setting of Anchorage. (See Megan Holland, "Grizzlies bite off too much," *Anchorage Daily News*, August 11, 2006, p. B-1.)

I was able to confirm the existence of the selected items, with the exception of the OptiPlex computer (\$1,179) that will be used to control the equipment. AEA indicated that this computer was in transit to the job site. Occasional unobserved items are of less concern in the “inspection” of an ongoing construction project, the case here, than they would be in a full “audit” of a completed project.

Public complaints

An unsuccessful bidder filed an administrative protest over AEA’s procurement of a major component for the project. The procurement manager ruled in favor of AEA and the bidder did not appeal further.

Ancillary reports

This is the first inspection of this project by the Denali Commission’s inspector general.

This project has not been the subject of any audit reports issued by Congress’ Government Accountability Office (GAO) or the state’s Division of Legislative Audit. AEA does not have an internal auditor.

Program partner AEA is a state agency and annually obtains a single audit for itself from a CPA firm. Neither the latest audit report (for the state’s FY05) nor the associated management letter signal any matters of concern to the Denali Commission. The CPA firm considered AEA to be a low-risk auditee for purposes of federal OMB Circular A-133.

Concept, design, and business plans were prepared for AEA as part of the routine preparation of this project. However, I have not discovered any other reports, reviews, audits, studies, or evaluations of this facility.

Inspection process

My inspection was conducted in accordance with section 2 of the Commission’s standard grant assurances, the project’s business operating plan (p. 14), sections 4(a) and 6(a) of the Inspector General Act, and the *Quality Standards for Inspections* issued by the federal Executive Council on Integrity and Efficiency.⁶ An “inspection” is narrower in scope and procedures than the classic financial “audit.”

Tenakee Spring’s new power plant was the subject of my August 4 inspection but, to understand the local context of this project, I also visited the tank farm and fuel dock that have been funded by the Denali Commission. A member of the city council met with me during my visit.

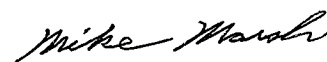
⁶ Per standard B(1), I have disclosed a prior contact with this project in which I verified the program manager’s completion of a planning checklist required at the time. The federal co-chair and I concur that this task did not impair my ability to later conduct the procedures involved here.

In my "bush" floatplane flights between tiny Tenakee Springs and regional hub Juneau, I appreciated the reassurance of flying with an air service that participates in Alaska's Capstone and Medallion Foundation safety programs.

Response by Denali Commission's management

The Federal Co-Chair was provided a draft of this report and invited to comment on my proposed conclusions. He was encouraged to consult his staff, AEA,⁷ and any other parties as desired in the preparation of his response.

The Federal Co-Chair's response is attached as an appendix. The response indicates the general concurrence of the Commission's management with my conclusions.



Mike Marsh
Inspector General

⁷ On August 24, I discussed pertinent conclusions with AEA's deputy director for rural energy.

Appendix

Federal Co-Chair's Response



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September 11, 2006

Mike Marsh
Inspector General
Denali Commission
510 L Street, Suite 410
Anchorage, Alaska 99501

Re: Response to draft inspection reports on power plant projects in Buckland,
Manokotak and Tenakee Springs

Dear Inspector General:

Thank you for the recent inspection reports on Denali Commission power plant projects in the communities of Buckland, Manokotak, and Tenakee Springs. Thank you for the insightful review of these important projects. With this letter I am providing a response to several recommendations that were presented in the draft reports for your consideration in drafting of the final public reports on these three projects.

General response to review of Alaska Energy Authority

I was pleased to see from your review that the traceability of expenditures, quarterly programmatic reporting, financial reporting, annual auditing, and photographic documentation provided by Alaska Energy Authority (AEA) to the Commission were all found to be consistent with the Commission's policies and procedures. The Commission is proud to have AEA as a partner to deliver our largest programs and has had a strong and positive relationship with the AEA since our inception. We intend to continue working with AEA into the future in order to complete the Commission's Bulk Fuel and Power Plant Programs and explore other areas to develop Alaska's energy infrastructure. Your reviews provide the Commission many recommendations that will further strengthen this partnership for the future.

Control over purchases

In your selected review of Alaska Energy Authority's expenditures on materials and equipment for the three projects you found several items that had either been delivered to another project or erroneously charged to a project. This equipment was all computers, web cam or other related technology for remotely managed power plants. The Commission understands that AEA is managing multiple projects and purchases equipment for several projects at one time which can lead to difficulty in accounting for equipment by project. In addition the amount and dollar value of items is small comparative to the overall scope of the projects. With this said, Commission management is concerned with this finding and will be working with AEA to ensure future technology equipment is more carefully tracked and accounted for accurately by project.

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Federal Co-Chair's Response

Response to Draft Inspection Reports (Buckland, Manokotak & Tenakee Springs) - 9/11/2006
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Disposition of surplus material

Your recommendation on clear grant conditions that anticipate excess material that may be left on site is not an issue the Commission has explicitly addressed in the past. Beginning in FY 07 the Commission will work to develop standard financial assistance award language that addresses this issue for all recipients and partners, if monetary effects to the projects can be suitably controlled. Minimizing excess material without increasing project costs is a laudable goal.

Monitoring and expenses of litigation

Although a rare occurrence in the short history of the Commission, litigation and challenges to procurement are an inevitable part of managing the construction of public infrastructure projects. The Commission has not explicitly provided direction to partner agencies or recipients on notification and allowable expenses. Beginning in FY 07 the Commission will develop standard financial assistance award language that addresses this issue for all recipients and partners. We will also pursue your recommendation to assess the use of grant funds in dealing with litigation and claims, since this could lead to an unfunded liability.

Feasibility of continuing audit requirements

The Commission has developed requirements to ensure the useful life of a facility is achieved and projects constructed with Commission funds are generally sustainable into the future. As your review discovered the use of the business plan by AEA is a cornerstone of this requirement. The Commission and AEA are continuously reviewing the standard business plan language for improvement toward this goal. The feasibility of requiring annual audits by communities will be reviewed by the Commission.

Potential for community contributions

The Commission's funding for bulk fuel and power plants in rural communities does not have a specific statutory requirement for cost share funding by recipients like the Commission's health facilities program. The Commission strongly encourages local contribution and funding for these projects while balancing the threat to public safety and the environment by allowing non-code compliant bulk fuel storage facilities and inadequate power infrastructure to remain. It should be noted that both Manokotak and Buckland were required to sign up with an outside electrical utility in a management/mentoring arrangement in order to qualify for the power plant upgrades in their communities. Buckland pays the entire cost of this agreement, while Manokotak pays about half the cost overall (graduated over time). This represents a small, but significant monetary contribution from both communities. The Commission and AEA have received local contributions on several other projects in the past, that were not part of your review, in the form of land donations, labor, materials and direct funding. It is an area that is important to review further. The Commission will be working with Alaska Energy Authority and other program partners to develop strategies for further cost participation by local communities.

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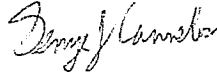
Complaints from Kotzebue Electric Association (KEA) on Buckland Power Plant

The Commission is aware of the concerns of KEA in regards to design of the power plant. This unique model of a regional entity providing operations support for a community power plant designed and constructed by the State was a first for the Commission and

AEA. The Commission will further consider how to approach similar projects in the future with information learned from this project and believes that AEA has adequately addressed the concerns raised at this time for this project.

Please let me know if you have any questions, or need additional information. Thank you again for completing these inspections and for the detailed reviews.

Sincerely,



George J. Cannelos
Federal Co-Chair