PROSPECTIVE CONSIDERATIONS FOR THE LOAN AUTHORITY SUPPORTED UNDER THE LOAN PROGRAMS OFFICE TO IMPROVE INTERNAL CONTROLS AND PREVENT FRAUD, WASTE, AND ABUSE
MEMORANDUM FOR THE SECRETARY

SUBJECT: Special Report on Prospective Considerations for the Loan Authority Supported Under the Loan Programs Office to Improve Internal Controls and Prevent Fraud, Waste, and Abuse

When we met on February 3, 2022, I committed to sharing with Department of Energy leadership any historic reports that may serve to improve internal controls and help prevent fraud, waste, and abuse as the Department launches its many projects funded by the Infrastructure Law. Under the Infrastructure Law, the Department’s Office of Fossil Energy and Carbon Management is to receive $2.1 billion to implement the new Carbon Dioxide Transportation Infrastructure Finance and Innovation Program, which can be distributed through loans, loan guarantees, or grants. To carry out this new program, the Department entered into a Memorandum of Understanding with the Loan Programs Office (LPO) to administer the funding based on its experience in evaluating financing for large-scale energy infrastructure projects and issuing Government loans and loan guarantees. In addition to the impending Infrastructure Law funding, the LPO currently administers three distinct loan programs with more than $40 billion in loan and loan guarantee authority, as well as manages a portfolio comprising of more than $30 billion of loans, loan guarantees, and conditional commitments.

The Office of Inspector General has identified prior reports from six audits, two inspections, and numerous investigations regarding the LPO. Additionally, we identified several Government Accountability Office reports related to the LPO. Based on our review of this body of work, we identified four major risk areas that warrant immediate attention and consideration from Department leadership to prevent similar problems from recurring. Specifically:

- **Insufficient Federal Staffing**: Prior audit reports identified that insufficient Federal staffing adversely affected LPO’s ability to administer the loan approval process and perform key risk and portfolio management functions. Capable and proficient staff are essential to ensure financial and technical risks are thoroughly analyzed and mitigated and Program objectives are achieved.

- **Inadequate Policies, Procedures, and Internal Controls**: Prior audit and investigative work highlighted issues related to the LPO’s control structure. In particular, we identified a lack of comprehensive policies and procedures related to critical stages of the loan

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1 This body of work includes reviews completed from 2007 through 2015 which covered the period when the majority of loans and loan guarantees were issued by the LPO and associated with the American Recovery and Reinvestment Act. Due to a lack of activity with the LPO, no additional reviews of the program have been conducted by the Office of Inspector General or Government Accountability Office.
approval and monitoring processes including credit underwriting for applicants, assessment of financial and technical risks, and monitoring of credit and technical performance of disbursed loans. These reports also revealed inadequate controls related to the oversight of contractors and resolution of differences of professional opinion among technical experts. Additionally, investigative work demonstrated cases where companies engaged in improper conduct, however, the Office of Inspector General did not make referrals for administrative remedies to the program, and the LPO’s control structure at that time did not include consideration of such remedies. The establishment of a robust set of administrative safeguards is essential to ensure continuity and consistency in administration of the loan programs, prevent circumvention of control points, and protect the Government’s and taxpayer’s interests.

• Lack of Accountability and Transparency: In reviewing prior audit and investigation work related to the LPO, we noted that the Department had not maintained complete and accurate records summarizing the results of the due diligence and risk assessment processes or memorializing key decision points in accordance with records management requirements. Such information is vitally important to: (a) protect the legal and financial rights of the Government over the life of loans and loan guarantees; (b) assist current managers and their successors in making informed decisions; and (c) provide a reliable source for information needed to respond to inquiries from the Congress and other oversight bodies. A lack of key decision documents also leaves the Department open to criticism that it may have exposed taxpayers to unacceptable risks. Finally, in the event that a loan or loan guarantee is subject to legal action, the availability of a complete record is an invaluable tool in supporting the Government’s position.

• Potential Conflicts of Interest and Undue Influence: Issued audit, inspection, and investigation reports identified instances where LPO officials potentially violated standards of ethical conduct or engaged in irregular hiring practices and made decisions that appeared to have been influenced by internal and external parties. Such activities could call into question the integrity of the LPO and erode the public trust.

As part of this effort, we discussed the risk areas highlighted above with LPO officials. According to LPO officials, actions have been taken or were underway to address the risk areas. For example, officials asserted that the number of staff has significantly increased in recent years and additional positions are being actively pursued to ensure sufficient staffing exists to meet program needs. In addition, officials indicated that enhanced policies and procedures are in place that address previously identified weaknesses. These policies include more stringent documentation requirements and require the LPO to conduct an annual assessment of internal controls to validate their effectiveness. Further, LPO officials noted that administrative remedies would be considered and pursued as necessary as the program moves forward with new loans and loan guarantees.

While LPO officials asserted that actions have been taken or were underway to address the risk areas, we did not perform test work to determine whether the actions will be fully effective to correct previously identified weaknesses. As such, we have identified several prospective considerations to help prevent fraud, waste, and abuse as the Department moves forward with
financing projects funded through the Infrastructure Law and existing loan authorities. As a top priority, we suggest that the LPO undertake proper staffing, and develop comprehensive policies, procedures, and internal controls to ensure the Government and taxpayers are adequately protected.

Teri L. Donaldson
Inspector General

cc: Deputy Secretary
Chief of Staff
SUMMARY OF ISSUES ON LOAN AUTHORITY UNDER LOAN PROGRAMS OFFICE

After reviewing prior reports and casework related to the Department of Energy’s Loan Programs Office (LPO), the Office of Inspector General (OIG) identified four risk areas that warrant additional attention and consideration from senior Department leadership for loan authority supported under the LPO and the Infrastructure Law. These areas include:

- Insufficient Federal Staffing
- Inadequate Policies, Procedures, and Internal Controls
- Lack of Accountability and Transparency
- Potential Conflicts of Interest and Undue Influence

As a result of the previous OIG and Government Accountability Office (GAO) efforts, we have identified prospective considerations that Department leadership should consider to enhance internal controls and prevent fraud, waste, and abuse.

INSUFFICIENT FEDERAL STAFFING

Prior audit reports related to the LPO identified that insufficient Federal staffing adversely affected LPO’s ability to administer the loan approval process and perform key risk and portfolio management functions. These reports demonstrate that capable and proficient staff are essential to ensure financial and technical risks are thoroughly analyzed and mitigated. For instance:

- In our February 2009 report on the Department’s Loan Guarantee Program (LGP), we found that the Department had not fully staffed the LGP Office and experienced competing demands for its limited staff and resources. The number of onboard staff was not adequate to, among other things, establish program controls, complete due diligence and credit underwriting for applicants, and monitor disbursed loans.

- Our April 2014 report on the Department’s loan guarantee to a solar panel manufacturer found that monitoring of the manufacturer’s loan was adversely affected by inadequate staffing of the LPO’s Portfolio Management function. In particular, the individual assigned to monitor the loan had no prior loan management experience and a limited background in project finance and financial statement analysis yet was assigned to manage a number of loans totaling over $2 billion. Since this individual did not have the skill set needed to effectively monitor financial and technical performance, credit reports were not completed for loans under the individual’s purview.

- The GAO’s May 2014 report on the LPO’s loan monitoring function found that the Department adhered to policies inconsistently or not at all because of staff vacancies. In

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particular, the LPO had not adhered to its policy requiring it to evaluate the effectiveness of its loan monitoring because of continuing staff vacancies. Without conducting these evaluations, the Department could not assess the adequacy of its monitoring efforts; thus, it could not be reasonably assured that it was effectively managing risks associated with its loan programs.

- In its February 2011 report\(^5\) on the LPO’s Advanced Technology Vehicles Manufacturing loan program, the GAO found that the LPO had not engaged outside engineering expertise needed for technical oversight. Instead, the LPO was using Federal staff to monitor the technical progress of the projects which was concerning because the staff’s expertise was largely financial and not technical. The GAO concluded that Federal staff lacked the engineering expertise called for in the LPO’s procedures, which cited the need for independent engineering expertise to validate project progress. Without qualified oversight to analyze the information submitted by the borrowers and to provide technical monitoring, the LPO could not ensure that the borrowers were delivering the vehicle and component projects as required by the loan agreements.

**INADEQUATE POLICIES, PROCEDURES, AND INTERNAL CONTROLS**

Prior audit and investigative work highlighted issues related to the LPO’s control structure. In particular, prior audits and investigative work revealed a lack of comprehensive policies and procedures covering all aspects of the loan process. Investigative work also demonstrated cases where companies engaged in improper conduct, however, the OIG did not make referrals for administrative remedies to the program, and the LPO’s control structure at that time did not include consideration of remedies such as suspension and debarment.\(^6\) The establishment of a robust set of administrative safeguards is essential to ensure continuity and consistency in the administration of the loan programs, prevent circumvention of control points, and protect the Government’s and taxpayer’s interests.

**LPO Policies and Procedures**

Prior audit reports identified a lack of comprehensive policies, procedures, and guidance related to critical stages of the loan approval and monitoring processes including credit underwriting for applicants, assessment of financial and technical risks, and monitoring of credit and technical performance of disbursed loans. These reports also revealed inadequate controls related to the oversight of contractors and resolution of differences of professional opinion among technical experts. For example:


\(^6\) Suspensions and debarments are administrative remedies used to prevent the Government from working with parties who are not “presently responsible” – i.e., those that have engaged in criminal or other improper conduct of such a compelling and serious nature that it would lead one to question their honesty, ethics, or competence. Government agencies use these remedies to prevent non-responsible parties from obtaining new Federal contracts and certain subcontracts or discretionary assistance, lease, loan, or benefit program awards.
• In our February 2009 report\textsuperscript{7} on the Department’s LGP, we found that the Department had not completed and implemented a control structure necessary to award and monitor associated projects. Specifically, the LPO had not fully developed and implemented controls in a number of critically important areas including evaluating loan applications, approving loan guarantees, monitoring project and loan guarantee performance, and qualifying potential lenders and monitoring participating lenders. In addition, we found that the LPO had drafted but not finalized procedures for, among other things, evaluating project financing and cash flow and estimating potential recoveries in the event of default.

• Our March 2011 report\textsuperscript{8} on the Department’s LGP found that the LPO had not updated policies and procedures to include improvements in loan processing to provide for the consistent use of lessons learned. Additionally, we noted that policies and procedures related to financial oversight of independent advisor costs were lacking, and roles and responsibilities for reviewing costs were not clearly defined. Improving reviews of billings in this area could help prevent reimbursements of several examples of inappropriate charges for items such as task order overruns and unauthorized first-class air travel that we observed during our testing.

• In our April 2014 report\textsuperscript{9} on the Department’s loan guarantee to a solar panel manufacturer, we found that the LPO had not established comprehensive policies, procedures, and guidance for awarding, monitoring, and administering loans. Specifically, the LPO had not established any guidance for determining the materiality of events occurring subsequent to conditional approval warranting reconsideration of a loan by the Credit Review Board, the entity responsible for recommending whether loans should be made and determining the terms and conditions needed to protect the Government’s interest. The LPO also had not developed formal processes for resolving differences of professional opinion among internal and external experts regarding technical performance and quality control issues. Furthermore, detailed guidance related to distressed loan management, loan restructuring, and bankruptcy monitoring had not been developed.

• The GAO’s May 2014 report\textsuperscript{10} on the LPO’s loan monitoring function found that the Department had not fully developed or consistently adhered to loan monitoring policies for its loan programs. The GAO noted that loan monitoring policies for evaluating and mitigating program-wide risk were incomplete or outdated. In addition, the GAO determined that the LPO inconsistently adhered to its policies for monitoring and reporting on credit risk, particularly for preparing credit reports, periodic reviews of project progress, and factors that may affect the borrower’s ability to meet the terms of the loan, and policies for managing troubled loans that required preparing and approving plans for handling loans to borrowers in danger of defaulting on their loan repayments.

\textsuperscript{7} See \textit{supra} note 2.
\textsuperscript{8} Audit Report on \textit{The Department of Energy’s Loan Guarantee Program for Clean Energy Technologies} (DOE/IG-0849, March 2011).
\textsuperscript{9} See \textit{supra} note 3.
\textsuperscript{10} See \textit{supra} note 4.
In addition, our review of prior investigative casework related to the LPO also demonstrated the need for more rigorous controls during the due diligence process. For instance, our August 2015 investigation report\textsuperscript{11} on a loan guarantee to a solar panel manufacturer found that at various points during the loan guarantee process, company officials provided updated information to LPO contractors and consultants, however, the information was not always shared with LPO staff and there was no evidence that the updated information was thoroughly analyzed. As a result, the investigation identified the need for Federal officials to provide quality assurance checks on contractors and expert consultants retained to assist in the Department’s loan guarantee application due diligence process, noting that consultants must be held accountable for the quality of their work. In addition, the report concluded that more intrusive validation techniques were needed to deter and identify information misrepresentations and omissions.

**Use of Administrative Remedies**

The OIG examined completed investigations that resulted in judicial outcomes, as well as several cases that resulted in administrative recommendations to the Department. Among other positive outcomes, OIG investigations helped recover $29 million in Federal loan funds and made Department managers aware of cases where companies engaged in improper conduct. Although the cases highlighted below demonstrated improper conduct, the OIG did not make referrals for administrative remedies to the program, and the LPO’s control structure at that time did not include consideration of remedies such as suspension and debarment.\textsuperscript{12}

- In California, an electric vehicle manufacturer received $529 million in loans from the Department under the Advanced Technology Vehicles Manufacturing loan program. The company subsequently declared bankruptcy, defaulted on the loan, and was forced to auction the value of the loan at a proceeding managed by LPO. The OIG conducted four investigations involving this recipient. Three of these cases were related to the auction process itself; the first involved an alleged leak of proprietary information regarding the valuation of the company’s assets by a Department contractor assisting in the auction process, and the second and third involved potential bid rigging and collusion between multiple bidders in the auction itself.

- Also in California, a solar technology company received a $535 million loan guarantee from LPO to manufacture photovoltaic technology in California. The OIG proactively determined, through review of publicly available information, that statements made by that company to the U.S. Securities and Exchange Commission contradicted statements made on the loan application to the Department. After a 4-year investigation with the U.S. Department of Justice, the OIG determined that the company provided the Department with statements, assertions, and certifications that were inaccurate and misleading, misrepresented known facts, and in some instances, omitted information that was highly relevant to key decisions in the loan guarantee process.

\textsuperscript{11} Special Report on *The Department of Energy’s Loan Guarantee to Solyndra, Inc.* (11-0078-I, August 2015).

\textsuperscript{12} In recent years, the OIG has enhanced its capability to develop and refer matters for administrative remedies by creating a new division focused, in part, on making appropriate remedial referrals. We have also developed a policy support framework to ensure evidence, once identified, goes to proper Federal officials so the Government has an opportunity to protect its interests. The Department’s processing time for suspension and debarment referrals has decreased in the last fiscal year.
The LPO must ensure its forms related to the submission of information sufficiently establish the reliance the Government is placing on the information and require an individual submitting the information to certify to the accuracy of that information. Where the information is part of the Government’s decision, the forms must identify that reliance in a manner sufficient to meet the materiality standard of criminal statues related to the submission of false information to the Government and the False Claims Act. Where an applicant submits inconsistent information, the LPO must resolve that conflict prior to reliance on that information. Likewise, the Department must ensure it takes programmatic and remedial actions consistent with the seriousness of the matter when it determines an applicant has submitted false, inconsistent, or incomplete information. Programmatic actions may include, but are not limited to, bonding, enhanced underwriting procedures, and expanded reporting.

To compliment program actions the Department must also maintain a functional remedial capacity. Pursuing remedies can help establish materiality in situations where programmatic concerns or other obligations might limit the Department’s ability to halt transactions. That capacity should include, as a minimum, the ability to act quickly in suspending or debarring individuals or entities when acceptable evidence demonstrates a program risk. The Department should also have the practical capability to pursue Program Fraud Civil Remedies Act cases in addition to supporting U.S. Department of Justice enforcement. These remedies constitute a necessary part of ensuring program integrity. An effective remedial approach would consider all means to protect, punish, and restore taxpayer funds.

**LACK OF ACCOUNTABILITY AND TRANSPARENCY**

In reviewing prior audit and investigation work related to the LPO, we noted that the Department had not maintained complete and accurate records summarizing the results of the due diligence and risk assessment processes or memorializing key decision points in accordance with records management requirements. These reports demonstrate a need for more rigorous internal controls over records management. For instance:

- In our March 2011 report on the Department’s LGP, it was noted that the LPO could not always readily demonstrate, through systematically organized records, how it resolved or mitigated relevant risks prior to granting loan guarantees. Specifically, decision documents summarizing the results of the due diligence and risk assessment processes did not always describe actions taken by Federal officials to address, mitigate, and resolve risks. Additionally, the LPO had not taken action to ensure that records created by consultants and independent advisors were delivered to the Department. These records are critical elements in the loan decision-making process since they describe actions taken to review and analyze the technical, financial, and marketing conditions of applicants’ projects.

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14 See, e.g., United States v. Luce, 873 F.3d 999 (7th Cir. 2017).
15 Pub. L. 99-509, Title VI, § 6103
16 See *supra* note 8.
• Our August 2012 report\textsuperscript{17} on the procurement and management of law firm services found that in a number of cases available records lacked sufficient information to permit an independent reviewer to understand the reasons for granting waivers of conflicts of interest. Prior to granting requested waivers, the LPO had not always memorialized key decision points and, therefore, could not demonstrate that its justifications for granting waivers for actual or potential conflicts of interest were appropriate.

• In our April 2014 report\textsuperscript{18} on the Department’s loan guarantee to a solar panel manufacturer, it was noted that the LPO had not adequately documented the assumptions in the financial modeling used to support loan approval and monitoring. Specifically, the LPO could not provide evidence demonstrating how assumptions used in financial models addressed a deteriorating market and overcapacity conditions in the solar panel industry and how problems with technical performance were resolved between conditional commitment and loan closing. The LPO also could not provide evidence that it had conducted ongoing, formal financial and industrial analysis during the loan disbursement period.

According to Federal records management requirements,\textsuperscript{19} complete and accurate records are vitally important to: (a) protect the legal and financial rights of the Government over the life of loans and loan guarantees; (b) assist current managers and their successors in making informed decisions; and (c) provide a reliable source for information needed to respond to inquiries from Congress and other oversight bodies. A lack of key decision documents also leaves the Department open to criticism that it may have exposed taxpayers to unacceptable risks. Finally, in the event that a loan or loan guarantee is subject to legal action, the availability of a complete record is an invaluable tool in supporting the Government’s position.

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\textbf{POTENTIAL CONFLICTS OF INTEREST AND UNDUE INFLUENCE}
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Issued audit, inspection, and investigation reports identified instances where LPO officials potentially violated the standards of ethical conduct or engaged in irregular hiring practices and made decisions that appeared to have been influenced by internal and external parties. For instance:

• In our August 2013 report\textsuperscript{20} on irregular hiring practices and preferential treatment in the LPO, we identified actions taken by a senior LPO official that could have caused others to perceive a misuse of position. Specifically, we found that a senior LPO official hired a “friend” for a Federal position and referred 10 individuals with whom the official was affiliated to a support service contractor for hiring consideration. The appearance of favoritism in the Federal hiring process and improper involvement in the contractor

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\textsuperscript{17} Special Report on \textit{Inquiry into the Procurement of Law Firm Services and Management of Law Firm- Disclosed Organizational Conflicts of Interest by the Department of Energy’s Loan Programs Office} (OAS-RA-12-14, August 2012).
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\textsuperscript{18} See supra note 3.
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\textsuperscript{19} 44 U.S. Code Chapter 31, Records Management by Federal Agencies.
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\textsuperscript{20} Inspection Report on \textit{Allegations of Irregular Hiring Practices and Preferential Treatment in the Loan Programs Office} (INS-L-13-06, August 2013).
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staffing process could erode the public trust in the hiring process. Referring affiliates to a contractor for hiring consideration can also erode public trust by creating the perception that a Federal official is using private office for the gain of affiliated individuals.

- Our August 2015 report on a loan guarantee to a solar panel manufacturer notes that LPO employees acknowledged that they felt tremendous pressure to process loan guarantee applications. LPO employees suggested the pressure was based on the significant interest in the LPO from Department leadership, the Administration, Congress, and applicants.

- In our April 2014 report on the Department’s loan guarantee to another solar panel manufacturer, we found that during the period the manufacturer’s loan was under consideration, the LPO operated under an environment of internal and external pressures to move the loan process along and increase the number or rate of issued loans. This finding was in line with the conclusion reached by the Congressional Committee on Oversight and Government Reform in October 2012, based on its inquiries into the LPO.

Such activities could call into question the integrity of the LPO and erode the public trust. In addition, internal and external pressures can create an environment where policies and procedures may be circumvented. As such, the LPO must ensure that a robust internal control structure is in place to mitigate the risk.

PROSPECTIVE CONSIDERATIONS

As the Department moves forward with financing projects funded through the Infrastructure Law and existing loan authorities, this report offers prospective considerations that Department leadership should consider for the LPO to improve internal controls and prevent fraud, waste, and abuse. Considerations include the following:

- Take actions necessary to ensure that the LPO is fully staffed and capable of meeting all requirements.

- Establish documentation requirements to ensure complete and accurate records summarizing the results of the due diligence and risk assessment processes are maintained and key decisions are memorialized.

- Ensure a comprehensive set of policies and procedures are in place covering all aspects of the loan process.

- Strengthen the due diligence process to include steps to validate company representations and ensure updated information provided throughout the process is properly vetted.

21 See supra note 11.
22 See supra note 3.
• Ensure any form or process eliciting material information clearly establishes the fact that the Government is relying on the information to make a funding decision.

• Consistently act in a manner that reinforces the significance of the Department’s reliance on the information submitted.

• Consistently consider and pursue administrative remedies such as suspension or debarment in instances where it has been determined that organizations provided false or misleading information to the Department.

• Provide more rigorous oversight of contractors and expert consultants to include performing quality assurance checks of their work products and thoroughly reviewing their costs.

• Confirm that LPO officials clearly understand and adhere to Federal hiring regulations and prohibited personnel practices.

• Ensure that LPO staff and contractors receive adequate training on program policies and procedures, Federal hiring regulations, and prohibited personnel practices.
Appendix 1: Related Reports

Office of Inspector General

- Allegations of Mismanagement at the Department of Energy’s Loan Programs Office (DOE-OIG-19-38, July 2019)
- The Department of Energy’s Loan Guarantee to Solyndra, Inc. (11-0078-I, August 2015)
- The Department of Energy’s Loan Guarantee to Abound Solar Manufacturing, LLC (DOE/IG-0907, April 2014)
- Allegations of Irregular Hiring Practices and Preferential Treatment in the Loan Programs Office (INS-L-13-06, August 2013)
- Inquiry into the Procurement of Law Firm Services and Management of Law Firm-Disclosed Organizational Conflicts of Interest by the Department of Energy’s Loan Programs Office (OAS-RA-12-14, August 2012)
- The Department of Energy’s Loan Guarantee Program for Clean Energy Technologies (DOE/IG-0849, March 2011)
- The Department of Energy’s Loan Guarantee Program for Innovative Energy Technologies (DOE/IG-0812, February 2009)
- Loan Guarantees for Innovative Energy Technologies (DOE/IG-0777, September 2007)

Government Accountability Office

- DOE Loan Programs: DOE Should Fully Develop Its Loan Monitoring Function and Evaluate Its Effectiveness (GAO-14-367, May 2014)
- DOE Loan Guarantees: Further Actions Are Needed to Improve Tracking and Review of Applications (GAO-12-157, March 2012)
- Department of Energy: Further Actions Are Needed to Improve DOE’s Ability to Evaluate and Implement the Loan Guarantee Program (GAO-10-627, July 2010)
- Department of Energy: New Loan Guarantee Program Should Complete Activities Necessary for Effective and Accountable Program Management (GAO-08-750, July 2008)
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