

Office of the
Inspector General
Commonwealth of Massachusetts

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Advisory for the
Procurement of Energy
Management/Conservation
Services

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Massachusetts Office of the Inspector General

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Office of the Inspector General

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January 28, 2009

Dear School Business Official:

The Office of the Inspector General is issuing this advisory to assist school districts in procuring energy efficiency and conservation consultants. These consultants assist in reducing energy costs through education, training, or other methods that do not involve the purchase or retrofit of equipment, fixtures, or other assets.

This advisory is based on a review of nearly 20 contracts that school districts have had with Energy Education Inc., (EEI) an energy consulting firm that claims to achieve energy cost savings through education and behavior modification.

In June 2008, because of concerns about energy consultant services, this office wrote to the Department of Energy Resources (DOER) as it proceeds with the statewide "green communities" initiative that: "municipalities lack the resources to fully evaluate the services being offered by private sector entities" and that "promises of savings made to cities and towns...[should be] verifiable." After consultation with DOER, this office advises municipalities to procure consulting services, such as those provided by Energy Education Inc., under M.G.L. c.25A, §11I.

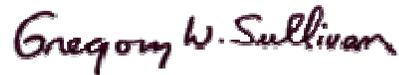
This review is not an evaluation of EEI's services. This is intended only to clarify procurement issues and to point out energy saving options. This advisory contains the following energy consultant procurement recommendations for school districts and other public entities:

- Perform due diligence before conducting the procurement. Public utility companies, state agencies and others may offer free energy consulting services. Take advantage of free services before entering into costly consulting contracts. Remember, contracts paid for through energy savings are not "free" or "no cost" services.

- When procuring these services you must use either M.G.L. c.25A or 30B. This office and DOER recommend c.25A, §11I for energy consulting services. We further recommend that you do not use vendor supplied language for your bid document. Using vendor supplied language could have legal and policy implications.
- Do not enter into a contract unless you: 1) understand how you will be charged for services; 2) will be able to verify these charges; 3) will be able to verify any vendor savings estimates; and 4) understand all contract related costs.

Please do not hesitate to contact this office if you have any questions, concerns, or require assistance regarding this or any other issue.

Sincerely,

A handwritten signature in dark ink that reads "Gregory W. Sullivan". The signature is written in a cursive, slightly slanted style.

Gregory W. Sullivan
Inspector General

Introduction

The Office of the Inspector General received a complaint regarding the contract practices of Energy Education Inc. (EEI). During the past year, the Office of the Inspector General has reviewed 19 contracts between Massachusetts school districts and EEI and the procurement of those contracts. EEI is an energy management company offering “people driven energy conservation programs” to school districts. EEI claims to generate substantial energy savings for clients through education and behavior modification. According to school districts we spoke with, EEI has helped them generate utility cost savings.

Findings

1. School districts should perform due diligence before procuring energy education or management services.

Recommendation: Before paying a vendor hundreds of thousands of dollars, this Office strongly recommends that school districts determine if some energy savings can be achieved through other forms of education or energy conservation measures.

Financially strapped school districts find the EEI program option appealing because it precludes capital investment in equipment, retrofits or upgrades and offers the potential for immediate, large dollar savings. In its sales pitch, EEI explains that it derives its fee from a percentage of what the district saves in energy costs and it guarantees that savings will exceed costs or EEI will make up the difference.

School districts should perform due diligence in researching alternatives before signing on with EEI or any energy conservation program based on behavior modification such as EEI. Although EEI claims that its program is unique, energy conservation and management service options exist in abundance and the Green Communities Act (Chapter 169 of the Acts of 2008) is spurring the creation of more. In many of the districts we reviewed, procurement officials had not investigated whether other free or less costly options existed for energy management and savings before committing to EEI contracts.

This Office has not reviewed and makes no claims as to the application or effectiveness of any other programs. However, alternative energy savings programs do exist, many at no cost. Although it is sometimes easier to let a vendor identify the cost savings, especially when it pitches a risk free program funded from a portion of savings, it is incumbent on school districts to investigate all options before committing to fee-based contracts.

During the course of our review, this Office became aware of many new programs and opportunities for school districts to reduce energy costs. Also, public utilities are required by law to offer energy conservation services at no cost. One school district

informed us that it received lighting retrofits from its local utility at no cost. EEI itself has estimated that school districts can save 5-7% off their utility costs through a do-it-yourself approach.

The Massachusetts Operational Services Division (OSD) recently congratulated one school district which was the recipient of the “2008 Leading by Example and Environmental Purchasing Innovation Awards” at a State House ceremony. As noted in OSD’s Procurement e-News, this district hired National Grid, a public utility, to replace lighting at an elementary school, while training staff in better management of electricity. The program resulted in a 14.3% reduction in electricity use in ten months, saving the town \$8,000 at no cost to taxpayers. The school projects a 23% savings in FY 2009. In the same district, the middle school also saved 11.5% on electricity use through automated lighting controls, and expects to save 20% or \$12,000 in the next fiscal year.

National Grid has partnered with the U.S. Environmental Protection Agency’s (EPA) ENERGY STAR (R) program to help customers improve the energy and financial performance of their buildings. This “whole building assessment program” starts with a benchmark questionnaire available online which the client fills out. An expert will provide free advice to identify and implement cost-effective and energy-efficient projects pointing out ways to reduce energy and operating costs.

Other resources available around the Commonwealth include:

- The Department of Energy Resources
- The Massachusetts School Building Authority
- The Massachusetts Technology Collaborative
- The National Energy Education Development Project (NEED)
- The Center for Ecological Technology
- The Massachusetts Energy Consumers Alliance
- The Cape Light Compact

The Federal Energy Management Program (FEMP) website provides links to a number of energy efficiency solutions including; resources, strategies, products, design, financing, and operations and maintenance.

This Office neither questions nor endorses the value of EEI's services. Our review has identified that some school districts are unaware of available, alternative programs. This report is intended to clarify procurement issues and to point out energy saving options to school districts of which they may be unaware. For those school districts that choose to contract with EEI, our review focused on certain contract and procurement issues that municipalities may encounter.

The following findings identify contract and procurement issues of concern for energy management/conservation service procurement and contracting.

2. The procurement of energy management services must be conducted under either M.G.L. c.25A or M.G.L. c.30B.

Recommendation: EEI's services and those of other energy management providers are best procured under M.G.L. 25A rather than M.G.L. c.30B.

The energy management services provided by EEI must be procured according to one of two Massachusetts statutes:

- Chapter 25A which includes; contracts for procurement of energy management services, contracts for energy management, guaranteed energy savings contracts, and qualified providers or
- The competitive bidding procedures of M.G.L. c.30B, the Uniform Procurement Act

This Office believes that M.G.L. c. 25A, §§11C or 11I are best suited for procurement of EEI's services. This statute is enforced by the Department of Energy Resources (DOER) which has opined that EEI's services comport with a key definition applicable to both 11C and 11I:

Services eligible for procurement under this provision are defined as "energy conservation measures". That term is defined as, "measures involving modifications of maintenance and operating procedures of a building." "Therefore, it is our opinion that municipalities may procure such services using either sections 11C or 11I." DOER oversees performance contracting for public buildings (other than Housing Authorities and state government buildings), cities, towns, counties, and schools.

Chapter 25A includes the following safeguards for municipalities:

- Under Chapter 25A, DOER has oversight of EEI's contracts with school districts.
- Prior to soliciting a request for qualifications, the awarding authority must notify the commissioner of DOER who will issue an acknowledgment of receipt upon successful compliance with the requirements Chapter 25A.
- The awarding authority must provide public notice of the meeting to award the contract and must provide DOER with a copy of the contract.
- In accordance with Chapter 25A, EEI's method for measurement and verification of guaranteed savings must conform to the most recent standards established by the Federal Energy Management Program (FEMP) of the U. S. Department of Energy.
- Chapter 25A includes a requirement for EEI to file with the awarding authority a performance bond equal to 100 per cent of the estimated contract value.
- Chapter 25A requires the annual submission of information to allow for regular monitoring of the costs and benefits of contracts for energy management services.

The Massachusetts school districts which have procured EEI's services to date, have done so by issuing a request for proposal (RFP) as required by M.G.L. 30B, §6 the Uniform Procurement Act.

This Office recently became aware of an instance in which EEI entered into a contract with a regional school district without the benefit of a competitive process. It is the understanding of this Office that the regional school district rescinded the contract after determining that the contract was subject to M.G.L. c.30B, and that the regional school district has since solicited proposals. Had EEI provided services under this invalid contract, M.G.L. c.30B, §17(b) would have prohibited the school district from making payment to EEI.

If school districts contracting for energy management services choose to undertake a request for proposals (RFP) process, it is important for both the districts and EEI to understand what is required to conduct a valid RFP process pursuant to M.G.L. c.30B, §6:

- Only those school districts with a chief procurement officer (CPO) may utilize the RFP process and only a CPO or a person with delegated authority from the CPO may conduct the RFP process.
- The CPO, or a person with delegated authority, must put his or her reason in writing why the procurement requires the use of the RFP, that is, why the selection of the most advantageous proposal requires comparative judgments in addition to price.
- The RFP must include the time, date and location for the receipt of proposals, the purchase description and all evaluation criteria that will be utilized, and all contractual terms and conditions applicable to the procurement.
- The RFP must be advertised.
- Responses to the RFP must be submitted in two separate envelopes (price and non-price or technical proposals). The price envelope is opened only after the technical proposals have been fully evaluated. Neither envelope can be opened publicly, but must be opened in front of one or more witnesses.
- The proposals must remain confidential until the time for acceptance has passed or the evaluation process is complete, whichever occurs earlier.
- Only a vendor that is responsive to the specifications, that is, a vendor that submits a proposal that conforms in all respects to the RFP, may be eligible to receive a contract. If a school district requires that the selected vendor provide evidence of the ability to obtain a performance bond to guarantee the savings a vendor must submit said evidence in accordance with the terms specified in the RFP in order to be considered responsive.

Additionally, contracts that exceed one year in length, including any options to renew or extend, must meet additional requirements found in M.G.L. c.30B, §12, including but not limited to:

- The RFP must include a statement that the procurement officer shall cancel the contract if funds are not appropriated or otherwise made available to support continuation of performance in any fiscal year succeeding the first (this includes funds for early termination penalties, EEI contracts include significant dollar penalties for early termination).
- If the contract will exceed three years in length, the contract cannot be entered into without majority vote approval.

Because it is reasonable to interpret EEI's activities as falling well within the meaning of such "measures involving modifications of maintenance and operating procedures", it is the opinion of this Office that MGL 25A is a more suitable statute for the procurement of EEI's services by municipalities.

3. Vendor supplied specifications in the Request for Proposal (RFP) process can undermine fair and open competition.

Recommendation: This Office recommends against relying on vendor supplied specifications, RFP language, and contract provisions.

This Office is aware that it is EEI's practice to provide specifications and contract documents to school districts for use when procuring energy management services. We have found in several instances, that the specifications EEI provides are proprietary in nature, that is, that specifications are written so restrictively that only EEI can provide the needed services, and that the contract terms strongly protect EEI, perhaps to the detriment of the school districts. This Office recommends against the use of vendor supplied specifications as they often tend to severely limit competition while at the same time increasing the cost to the school districts. M.G.L. c.30B, §14 requires the school district, through its procurement officer, document in writing the reason why no other manner of description will suffice, that is, why the proprietary services provided by EEI are the only services that meet the school district's needs.

Additionally, a recent Massachusetts Attorney General opinion explains that while vendor or industry assisted specifications may not be a violation of competitive bidding laws, "it does lead to unacceptable situations" in the absence of the prudent and judicious use of this vendor supplied information.

The DOER provides similar procurement advice stating: "Do not rely on a contractor to develop your Request for Responses (RFR) either for the document itself or for audit services if the contractor may bid on the RFR". [Note: RFRs are used by state agencies while RFPs are used by municipal entities. Under Chapter 25A, §11I the awarding authority may also use a Request for Qualifications (RFQ).]

In one case, a potential proposer told the awarding authority that it could help the district achieve equivalent savings for less money but that it could not bid based on the RFP as written. Other vendors have stated that they do not bother to compete with EEI because of the inherent bias in this particular RFP process. Districts are cautioned that the use of vendor supplied specifications can lead to a biased process and result in a pre-determined outcome.

The following link provided by the Department of Energy Resources for a sample bid solicitation document may be beneficial for municipalities to review:

<http://www.mass.gov/Eoeea/docs/doer/ems/ems-model-rfr.pdf>

4. Awarding authorities must fully understand the vendor's projection, fee and guarantee.

Recommendation: This Office recommends that awarding authorities not execute contracts until they fully understand the basis of the service fee being charged and should be able to tie the fee to a measurable product deliverable.

EEl explains to prospective clients, that its fee can be recouped from a percentage of what the district will save in energy costs. Provided that the district energy manager performs to EEl's satisfaction, EEl guarantees that savings will exceed costs or EEl will make up the difference. This is marketed as a risk free program with no added cost. In the proposal, EEl provides the district with a long term, estimated, cost savings projection. According to EEl, this projection is based on "information provided by and specific to the potential client (primarily utility bills, age and number of buildings) and on EEl's prior experience with other "similar districts" around the United States. EEl explained to this office that their projections exist as estimates of future savings potential, and that actual savings are a function of the client's implementation of their program.

In the proposals that this Office reviewed, the savings projections provided to Massachusetts districts ranged from a low of \$897,000 for 7 years to a high of \$4,027,527 for 10 years. EEl stated that its fee is based on the resources that EEl projects it must commit to help the district achieve their 10-year estimated savings. Although the projection may be adjusted over time, EEl stated that, "the fee is a set amount established in advance by agreement with each client and does not vary according to actual savings". In other words, the fee, based on a 10 year estimate, is established up front, is contractually locked in and cannot be re-negotiated if actual savings do not match the projected savings.

Once established, the fee is broken out into 48 equal monthly payments made over four years. (Contracts of three years have also been used in some prior agreements). These four years are the “performance years” of the contract. The average total cost of the EEI contract to the districts we reviewed was \$390,875. In addition to EEI’s fee, the district’s costs include the energy manager’s salary, benefits, and travel expenses, a one time \$12,000 purchase price for the software and an annual two thousand dollar fee for renewal of the proprietary, software license. EEI guarantees that for each of the four performance years, the district will not spend more than it saves or EEI will make up the difference. If savings do not exceed costs, EEI promises to reimburse the amount of the difference to the district at the end of each performance year. This guarantee ends at the conclusion of the final performance year.

Awarding authorities should be very clear on the following points:

- The ten year projection used to market and sell the program is not guaranteed and the district is contractually obligated to pay EEI’s fee regardless of whether the district ever achieves the projected savings.
- EEI’s savings guarantee applies only to the four year term of the contract, not the ten year projection. EEI guarantees only that savings will exceed costs, not that savings will equal EEI’s projected savings. A contract based on projected savings that does not tie the vendor’s fee to actual savings may eliminate the possibility for adequate performance measurement and is weighted in the vendor’s favor.
- EEI’s guarantee applies only if EEI is satisfied that the energy manager devotes enough time and effort to the program and that the district “substantially implements” the program.
- Cost savings achieved in any given year are considered to be recurring savings. Therefore removal of a light fixture in year one is counted as a cost savings in each year of the ten year projection.
- Our analysis confirms that, as projected by EEI, districts must continue the program for a number of years after the four year contract term in order to approach the ten year cost savings projected by EEI.
- Districts should be aware that EEI’s contracts include significant dollar penalties for early termination. The penalty amount must be appropriated each year if the awarding authority chooses to use a Chapter 30B process.

5. The “third party software” required by the vendor is not entirely independent of EEI.

Recommendation: The awarding authority should conduct due diligence and ask for details about the software it is purchasing in order to understand how cost savings are calculated, measured and interpreted.

In order to receive EEI’s guarantee, EEI clients are required to purchase software, to measure energy savings. The version of the software that EEI recommends, EnergyCAP Professional, is provided by Good Steward Software, LLC, costs \$12,000 and requires an annual \$2,000 renewal fee. According to some school districts, EEI informed the district that it had to use the EnergyCAP Professional software and that using other software could compromise the program and EEI’s savings guarantee.

EEI has a business relationship with the software provider which should be disclosed to clients prior to the signing of a contract. The founder and owner of EEI, established a company, American Energy Intelligence, for the sole purpose of purchasing the software from Enron Corporation, and assigned the rights to Good Steward, LLC. Although Good Steward offers other software packages, the EnergyCAP Professional version is only available to clients of EEI and is not sold to others. Reports from this software are used to identify school district cost savings and are the means by which EEI tracks its savings guarantee.

When this office contacted Good Steward with specific questions about how the software calculates savings, we were referred to EEI. When we asked EEI how clients could get answers about calculations made by the software, EEI stated that they should communicate directly with Good Steward, the software vendor.

Any third party vendor should be prepared to explain its product to prospective clients. The reporting of cost savings is not a simple comparison of costs over time. Because the software must take into account factors like weather, utility rate structures, building occupancy, mechanical systems, behavior modification, grounds care, data analysis, etc., the statement of cost avoidance is not a statement of actual energy savings, it is more of a statistical model that interprets, with a certain degree of confidence, the amount of money that the district saved. Although Good Steward includes on its web

page a list of functions that the software performs and user testimonials, not knowing how the savings are calculated makes it impossible for this office to attest to the validity of the savings claims.

There is an inherent potential for error in cost avoidance calculations that should be made clear to prospective clients. Industry experts told this office that, there is no single, dependable method to compute cost savings. According the American Society of Heating, Refrigerating and Air-Conditioning Engineers, (ASHRAE Guideline 14); “any statement of measured savings includes a degree of uncertainty.”

The industry created common standards for the measurement and verification (M&V) of savings known as, the International Performance Measurement and Verification Protocol or IPMVP. This document was written by and for technical, procurement, and financial personnel in government, commerce, and industry. It was created by the Efficiency Value Organization, (EVO), a non-profit organization dedicated solely to creating measurement and verification tools. Good Steward asserts that Energy Cap Professional, the software required by EEI, complies with the IPMVP.

EVO consultants told this office that Measurement and Verification is more of an art than a science which depends on a certain level of trust between the parties. Districts should therefore be aware that the use of costs avoided to determine a fee is subject to interpretation and negotiation. One energy management consultant advised that; “if the vendor’s paycheck is coming from savings – be careful”.

It is critical for public entities to have the most specific information possible to ensure that savings have been achieved commensurate with program costs and vendor performance. EEI and the software vendor should make every effort to assist in this process. EEI should clarify its relationship with Good Steward in the initial sales presentation to school districts. Good Steward should directly answer any questions districts have about the software rather than referring queries to EEI.

6. Awarding authorities should be aware of issues regarding the Energy Manager.

Recommendation: With regard to the “energy manager”, the awarding authority must be fully aware of all the financial and policy implications of the contract including the ramifications of early contract termination.

The EEI program requires that the district hire an “energy manager”, selected by EEI who then receives training from EEI consultants about cost-savings methods including such measures as lowering thermostats and shutting down computers, lighting and equipment when they are not being used. The district is responsible for the salary of the energy manager. EEI makes other recommendations that it claims are available only through its proprietary program. The district energy manager must ensure that these recommendations are implemented.

The energy manager must also maintain a database in the software program required by EEI. EEI staff consult with the energy manager during the life of the contract and provide technical support as needed. Support is more comprehensive in the early years of the contract. EEI also requires that the energy manager attend annual trainings at their facility in Texas. The contract requires that the energy manager must be a member of the district’s faculty or staff and that the district is responsible for the energy manager’s salary, fringe benefits, travel, communications and seminar expenses. The energy manager is required to sign a confidentiality agreement and a covenant not to compete and is then hired for a twelve month trial period.

EEI requires that the energy manager be given authority to implement the program to EEI’s satisfaction. EEI’s guarantee is contingent on their satisfaction with the performance of the energy manager and the district’s implementation of the program. Although energy managers are public employees, EEI’s contract precludes the energy manager from attending any user group meetings that are not sponsored by EEI to prevent the dissemination of EEI’s proprietary information. If the EEI contract is terminated, the district agrees to return all EEI materials, to discontinue the position of energy educator/manager and thereafter not to implement any part of the EEI program.

If the district should ever decide to terminate EEI's contract but wished to continue employing an energy manager for an in-house energy conservation program, the contract terms prevent this. Since many of EEI's "proprietary measures" are also "common sense" measures, a public entity should carefully evaluate the consequences of entering into a contract that restricts their option to employ an individual to direct common sense, cost saving and energy conservation measures. As EEI told this office, institutions that employ a do-it-yourself approach to energy saving will typically save 5-7% off their utility costs. With assistance from some of the free programs currently available, the percentage could be appreciably higher. The awarding authority may wish to consult legal counsel regarding potential pension and personnel policy issues related to EEI's energy manager requirements.

If the energy manager is selected from the district's faculty or other staff as required under the EEI contract, the additional salary paid for the energy management position may have pension implications depending on the size of the district. There may also be potential for conflict of interest issues arising from an employee serving a district in two separate capacities or if the person chosen to be energy manager has a familial relationship with anyone with authority to influence the choice of the energy manager. If such familial questions arise, we strongly suggest consulting the State Ethics Commission for specific advice.

Conclusion

It is incumbent on school districts to use due diligence in the investigation of cost free and low cost alternatives available through public utilities and government entities before procuring energy management services. For the procurement of energy management services M.G.L. c.25A offers school districts the best protections. In any case, energy management services must be procured under either M.G.L. c. 25A or M.G. L. c. 30B. As with any procurement, the school district must fully understand the service or product it is purchasing, the cost of the purchase, and the implication of the purchase. Based on this Office's review, it is unclear whether school districts fully understood the procurement and use of the energy management services offered by EEI.