ATTACHMENT A

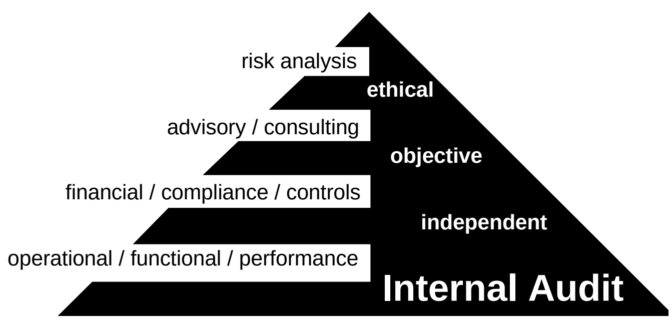
ORANGE COUNTY TRANSPORTATION AUTHORITY
INTERNAL AUDIT DEPARTMENT

OCTA

Agreement with Element Markets Renewable Energy, LLC, for Purchase of Natural Gas and Monetization of Federal and State Credits

Internal Audit Report No. 19-511

July 16, 2019



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Conclusion

The Internal Audit Department (Internal Audit) has completed an audit of Agreement No. C-5-3636 with Element Markets Renewable Energy, LLC (Element Markets), for the purchase of renewable natural gas and monetization of credits under the state Low Carbon Fuel Standard (LCFS) Program and the federal Renewable Fuel Standard (RFS) Program. Based on the audit, program oversight controls are adequate, consultant selection complied with procurement policy, credit revenues are properly monitored, reconciled, and recorded, and invoices are properly reviewed and authorized.

Background

Programs

On March 14, 2016, the Orange County Transportation Authority (OCTA) Board of Directors selected Element Markets to provide renewable natural gas for OCTA operations, and to assist OCTA in managing two programs; the LCFS Program generating LCFS credits at the state level and the RFS Program, generating Renewable Identification Number (RIN) credits at the federal level. As a consumer of natural gas for its bus operation, OCTA is able to sell credits generated and obtain revenues under these programs.

California's LCFS Program was enacted to support the California Global Warming Solutions Act of 2006. The LCFS Program was designed to lower greenhouse gas emissions by requiring producers of petroleum-based fuels to reduce the carbon intensity of their transportation fuels. One of the ways that producers of petroleum-based fuels can meet this requirement is to buy credits from entities who use low carbon fuels, such as OCTA.

The RFS program was authorized under the Energy Policy Act of 2005 and expanded under the Energy Independence and Security Act of 2007. Congress created the RFS program to ensure that transportation fuel in the United States contains a minimum volume of renewable fuel. The RFS program requires entities that refine, import, or blend fossil fuels to meet certain individual RFS quotas based on the volume of fuel they introduce to the market. In order to meet their quotas, these entities must submit RINs to the Environmental Protection Agency (EPA) to demonstrate compliance.

As of March 31, 2019, OCTA has purchased approximately $11 million in renewable natural gas and has received credit revenues of approximately $14 million from the sale of credits sold by Element Markets. It is anticipated that revenues generated from these programs will continue to fully fund the cost of renewable natural gas required to fuel the OCTA fleet.

Regulatory Compliance

Both the state LCFS Program and the federal RFS Program maintain compliance guidelines for generating, selling, and reporting of credits. OCTA delegated its regulatory obligations to Element Markets to sell the credits and assume all responsibilities associated with program management, including regulatory and compliance issues. The California Air Resources Board regulates the LCFS program and the EPA regulates the RFS program.

Objectives, Scope, and Methodology

The objectives were to determine the adequacy of program oversight controls and to assess compliance with procurement, invoice review, and reconciliation policies and procedures.

According to Generally Accepted Government Auditing Standards (GAGAS), internal control, in the broadest sense, encompasses the plans, policies, procedures, methods, and processes adopted by management to meet its mission, goals, and objectives. Internal controls significant within the context of the audit objectives were evaluated as part of this audit.

The scope was limited to the Renewable Natural Gas Credit Program from July 1, 2016 to March 1, 2019.

The methodology included review of the procurement file to determine compliance with Contracts Administration and Materials Management policy and procedures, review and testing of controls over the cash receipts, reconciliation and recording processes, and review and testing of the invoice review process. A judgmental sample of ten wire transfers during the scope period was selected for testing of the cash receipt, reconciliation, and recording process for revenues received from the sale of natural gas credits. A judgmental sample of ten invoices during the scope period was selected for testing to determine compliance with invoice review procedures. Both judgmental samples were selected to provide an even distribution of coverage during the scope period. Since the samples were non-statistical, any conclusions are limited to the sample items tested.

We conducted this performance audit in accordance with GAGAS. 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. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.