



Audit Report



OIG-12-063

RECOVERY ACT: Audit of Grand Ridge Energy II LLC Payment Under 1603 Program

August 2, 2012

Office of
Inspector General

Department of the Treasury

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Abbreviations

MW	megawatt
NREL	National Renewable Energy Laboratory
OFAS	Office of the Fiscal Assistant Secretary
OIG	Office of Inspector General
Treas. Reg.	Treasury Regulation

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*The Department of the Treasury
Office of Inspector General*

August 2, 2012

Richard L. Gregg
Fiscal Assistant Secretary

As part of our ongoing oversight of the Department of the Treasury's (Treasury) 1603 Program – Payments for Specified Energy Property in Lieu of Tax Credits (1603 Program)¹ authorized by the American Recovery and Reinvestment Act of 2009 (Recovery Act),² we are conducting audits of selected award recipients. In this regard, we have audited the award made to Grand Ridge Energy II, LLC (Grand Ridge II) for a wind energy property in LaSalle County, Illinois. Grand Ridge II submitted its claim for payment in lieu of tax credit in the amount of \$32,571,599 and was awarded \$32,300,165 by Treasury on February 19, 2010. Our audit objectives were to assess the eligibility and accuracy of that award by determining whether (1) the property existed, (2) the property was placed into service during the eligible timeframe, and (3) the award amount was appropriate.

Results in Brief

We verified that the subject property described by Grand Ridge II in its 1603 Program application does exist and was placed in service on November 25, 2009, which was within the eligible timeframe. We also concluded that the award amount was appropriate. Overall, Grand Ridge II complied with the eligibility requirements set forth in Section 1603 of the Recovery Act and Treasury's 1603

¹ Treasury's Office of the Fiscal Assistant Secretary administers this program.

² Pub. L. No. 111-5, 123 Stat. 364-366 (Feb. 17, 2009). Under section 1603 of the Recovery Act, Treasury makes grants (payments) to eligible persons who place in service specified energy property and apply for such payments. The payments reimburse eligible applicants for a portion of the expense of such property and are made in lieu of tax credits that could potentially be claimed by the awardees.

Program guidance.³ Subsequent to our site visit, we reviewed Grand Ridge II's annual performance reports submitted to Treasury for 2010 and 2011, certifying that the subject property was not disposed of and that it continued to qualify as a specified energy property. It should be noted that in accordance with the terms and conditions of the award, Grand Ridge II must continue to certify that (1) the property has not been sold, transferred, or disposed of to a disqualified person and (2) the property continues to qualify as a specified energy property.

As part of our reporting process over 1603 Program awardees, we provided Grand Ridge II an opportunity to comment on a draft of this report. Grand Ridge II agreed with the results of our audit; its response can be found in appendix 1. After incorporating Grand Ridge II's response into this report, we provided it to Treasury management for comment. Treasury management concurred with our audit results; its response is provided in appendix 2.

Background

Eligibility Under the 1603 Program

Applicants are eligible for a 1603 Program award if a specified energy property is placed in service during calendar years 2009, 2010, or 2011⁴ and the amount awarded is in accordance with provisions of the Internal Revenue Code of 1986 for determining the appropriate cost basis. Under the 1603 Program, applicants submit an application to Treasury that reports the total eligible cost basis of a specified energy property placed in service. If approved, award amounts are based on a percent of the eligible cost basis. For the type of property claimed by Grand Ridge II, the percentage

³ Office of the Fiscal Assistant Secretary, "Payments for Specified Energy Property in Lieu of Tax Credits under the American Recovery and Reinvestment Act of 2009 Program Guidance," (July 2009/ Revised March 2010/ Revised April 2011)
(<http://www.treasury.gov/initiatives/recovery/Pages/1603.aspx>)

⁴ Section 707 of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (Pub. L. 111-312, 124 Stat. 3312 (Dec 17, 2010)), extended Treasury's 1603 Program for 1 year. To be eligible, a property must be placed in service in 2009, 2010, or 2011 or placed in service after 2011 but only if construction of the property began during 2009, 2010, or 2011 and the credit termination date of the property has not expired. The application deadline was also extended to September 30, 2012.

of the cost basis eligible for award is 30 percent. According to Treasury's 1603 Program guidance, the cost basis of the subject property is ascertained in accordance with the general rules for determining the cost basis of property for federal income tax purposes.

Specifically, for this type of property, applicants follow the capitalization procedures found in Treas. Reg. §1.263A-1, "Uniform Capitalization of Costs."⁵

The terms and conditions of award require applicants to certify annually for a period of 5 years following the property's in-service date that the claimed property (1) has not been sold, transferred, or disposed of to a disqualified person and (2) continues to qualify as a specified energy property. Otherwise, the 1603 Program payment will be subject to full or prorated recapture.

Grand Ridge II

Invenergy Wind, LLC (Invenergy) developed the Grand Ridge Energy II wind farm property located in LaSalle County, Illinois, approximately 80 miles southwest of Chicago, Illinois. The subject



OIG Photograph (April 5, 2010)

property is a 51 megawatt (MW) wind farm which utilizes 34 General Electric wind turbines capable of generating about 141 gigawatt hours of electrical output annually. Grand Ridge II sells its output to Appalachian Power

Company under a 20 year Renewable Energy Purchase Agreement.

Invenergy and its subsidiary companies have developed and placed into service 44 wind generation properties worldwide representing

⁵Treas. Reg. § 1.263A-1(a)(3) (ii), Property produced: "Taxpayers that produce real property and tangible personal property (producers) must capitalize all the direct costs of producing the property and the property's properly allocable share of indirect costs (described in paragraphs (e)(2)(i) and (3) of this section), regardless of whether the property is sold or used in the taxpayer's trade or business.

an aggregate generation capacity of over 3,752 MW. Invenergy is currently the fifth largest wind generation company in the U.S. To date, Invenergy and its affiliates have received \$199 million in 1603 Program awards for five specified energy properties — Grand Ridge Energy II, Grand Ridge Energy III, Grand Ridge Energy IV, Beech Ridge Energy, and Vantage Wind Energy.

Objectives, Scope, and Methodology

To assess the eligibility and accuracy of the award made to Grand Ridge II under the 1603 Program, we determined whether (1) the property existed, (2) the property was placed into service during the eligible timeframe, and (3) the award amount was appropriate.

In performing our work, we visited Invenergy headquarters in Chicago, Illinois; interviewed key personnel of Invenergy; reviewed the application and related documents reviewed by the Department of Energy's National Renewable Energy Laboratory (NREL);⁶ reviewed documentation used to support the property's existence, its placed in service date, and the costs claimed by Grand Ridge II; and reviewed the annual performance reports submitted by the awardee for 2010 and 2011. We performed our work between April 2010 and May 2012.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform an 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.

⁶ NREL is a national laboratory of the Department of Energy. Under an interagency agreement between Treasury and the Department of Energy, NREL performs the technical review of 1603 Program applications and advises Treasury on award decisions.

Audit Results

We verified that the subject property described by Grand Ridge II in its 1603 Program application exists, was properly placed in-service within the eligible timeframe, and the award amount was appropriate.

Property Existence

We confirmed the subject property's existence through our site visit to Grand Ridge II wind farm located in LaSalle County, Illinois. As part of our site visit, we reviewed Grand Ridge II's wind turbine monitoring system and noted that there was active monitoring of its 34 wind turbines. We also concluded that the subject property included the wind turbines that had the 1.5 MW capacity each as described in the subject property's application.

Placed In-Service

We determined that the subject property was placed in service during the eligible time frame through review of documentation supporting Grand Ridge II's in-service date of November 25, 2009. Specifically, we reviewed (1) documentation detailing the completion and commission dates for each turbine, (2) correspondence from Grand Ridge II's transmission provider supporting the date Grand Ridge II commenced operation, and (3) the inter-connection agreement between Grand Ridge II and respective third parties for interconnection service.

Appropriate Award Amount

We concluded that the amount of \$32,300,165 awarded to Grand Ridge II was appropriate through our review of documentation supporting the subject property's cost basis. Prior to award, NREL technical reviewers identified \$904,778 of ineligible costs and reduced the submitted cost basis of \$108,571,996 to \$107,667,218 resulting in an adjusted award amount of \$32,300,165 (30 percent of adjusted cost basis). During our review, we obtained a schedule of all costs in the subject property's cost basis and tested supporting

documentation for cost transactions totaling \$67 million and verified that the selected costs were allowable and eligible. Accordingly, we believe the amount awarded to Grand Ridge II was appropriate.

Since our site visit to Grand Ridge II, we reviewed its "Annual Performance Report and Certification" for 2010 and 2011 to ensure compliance with Treasury's reporting requirements contained in the applicant's terms and conditions of award. As required for continued eligibility, Grand Ridge II certified that the property has not been sold, transferred, or disposed of to a disqualified person and that the property continues to qualify as a specified energy property. The next annual report is due December 15, 2012.

* * * * *

We appreciate the courtesies and cooperation provided to our staff during this audit. If you wish to discuss this report, you may contact me at (202) 927-5400 or Donna Joseph, Director, at (202) 927-5784. See appendix 3 for major contributors to this report.

/s/

Marla A. Freedman
Assistant Inspector General for Audit

Appendix 1
Grand Ridge II Response

GRAND RIDGE ENERGY II LLC
ONE SOUTH WACKER DRIVE, SUITE 1900
CHICAGO, IL 60606

June 21, 2012

Ms. Marla A. Freedman
Assistant Inspector General for Audit
Department of Treasury Office of Inspector General
740 15th Street, N.W., Suite 600
Washington, D.C. 20220

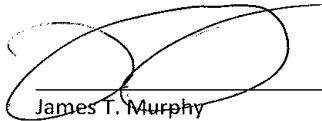
Dear Ms. Freedman,

This letter is in response to your draft audit report dated June 20, 2012 regarding the audit of Grand Ridge Energy II LLC Payment Under the 1603 Program – Payments for Specified Energy In Lieu of Tax Credits. We appreciated the opportunity to review and comment on the content of the report.

Grand Ridge Energy II LLC concurs with the findings in the draft report.

Please feel free to contact me directly with any further questions or concerns regarding this matter.

Sincerely,



James T. Murphy
Vice President
Grand Ridge Energy II LLC

Appendix 2
Management Response



ASSISTANT SECRETARY

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

July 24, 2012

Marla Freedman
Assistant Inspector General for Audit
Department of the Treasury
Office of Inspector General
740 15th Street, N.W., Suite 600
Washington, D.C. 20220

Dear Ms. Freedman:

Thank you for the opportunity to comment on the draft audit report of the Section 1603 award made to Grand Ridge Energy II, LLC. We concur with the report's findings.

Sincerely,

Richard L. Gregg
Fiscal Assistant Secretary

Appendix 3
Major Contributors To This Report

Donna Joseph, Director
Cynthia Milanez, Audit Manager
Erica Wardley, Audit Manager
James Hodge, Auditor-in-Charge
Cheryl Sroufe, Auditor
John Gauthier, Referencer

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Chief Financial Officer, and Chief Performance Officer
Fiscal Assistant Secretary
Deputy Chief Financial Officer
Director, Treasury-wide Accounting and Policy
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Deputy Director, Office of Performance Budgeting
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Office of Management and Budget

OIG Budget Examiner

Invenergy LLC

Vice President

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