

CHAPTER 1: MANAGEMENT'S DISCUSSION AND ANALYSIS

A MESSAGE FROM THE CHAIRMAN

I am pleased to present the Nuclear Regulatory Commission's *Performance and Accountability Report for FY 2004*. Ensuring the protection of public health and safety and the environment has always been the NRC's primary goal. I am proud to report that once again the NRC has achieved all of its safety performance goals. These results have been achieved through the application of the NRC's comprehensive safety framework, including defense-in-depth principles, as well as risk-informed and, where appropriate, performance-based regulation. I am also pleased to report that the NRC is positioning its resources and infrastructure to continue its strong oversight of existing facilities, and to review applications associated with new power reactors, high-level waste repository, and license renewals for existing facilities.



Security continues to be one of NRC's highest priorities. The NRC strengthened security at commercial nuclear facilities and augmented protection of the radioactive material it regulates. In requiring upgraded physical protection, access authorization, security force training and qualification, and safeguards-design standards and, in conducting new force-on-force exercises, improved emergency preparedness exercises, and continued partnerships with authorities at the Federal, State, local and international levels, the NRC has made significant progress in bolstering homeland security and preparedness. As a result, nuclear power plants continue to be among the best protected private sector facilities in the Nation.

One of my goals is to ensure that our resources are well managed and wisely used. This report provides information which demonstrates the prudent management of the funds entrusted to us by the American public and describes our successes in implementing the President's Management Agenda to promote a more efficient and effective Government.

The Reports Consolidation Act requires an assessment of the completeness and reliability of the program and financial data contained in this report based on evaluation criteria issued by the Office of Management and Budget. I conclude that the data are complete and reliable. In addition, the NRC has evaluated its management controls and financial management systems, as required by the Federal Managers' Financial Integrity Act. On the basis of our comprehensive

MANAGEMENT'S DISCUSSION AND ANALYSIS

management control program, I certify, with reasonable assurance, that the NRC is in compliance with the provisions of this act.

The NRC is committed to carrying out its regulatory responsibilities to enable the use and management of radioactive materials and nuclear fuel for beneficial civilian purposes in a manner that protects public health and safety and the environment, promotes the security of our Nation, and provides for regulatory actions that are open, effective, efficient, realistic and timely. The Commission is proud of this past fiscal year's accomplishments and looks forward to providing high-quality service to the American public in FY 2005 and beyond.



Nils J. Diaz

November 15, 2004



INTRODUCTION

INTRODUCTION

This Performance and Accountability Report represents the culmination of the U.S. Nuclear Regulatory Commission's (NRC) program and financial management processes, which began with mission and program planning, continued through the formulation and justification of NRC's budget to the President and the Congress, through budget execution, and ended with this report on our program performance and use of the resources entrusted to us. This report was prepared pursuant to the requirements of the Chief Financial Officers Act, as amended by the Reports Consolidation Act, and covers activities from October 1, 2003, to September 30, 2004.

Chapter 1, Management's Discussion and Analysis, provides an overview of the NRC. It consists of six sections: *About the NRC* describes the agency's mission, organizational structure, and regulatory responsibility; *Future Challenges* includes forward-looking information; *Program Performance Overview* discusses the agency's success in achieving its strategic goals; *President's Management Agenda* describes the agency progress in "Getting to Green" for the five management initiatives; *Financial Performance Overview* provides highlights of the NRC's financial position and audit results; and *Systems, Controls, and Legal Compliance* describes the agency's compliance with key legal and regulatory requirements.

ABOUT THE NRC

The NRC was established on January 19, 1975, as an independent Federal agency to regulate various commercial and institutional uses of nuclear materials. The NRC's purpose is defined by the Atomic Energy Act, as amended, and the Energy Reorganization Act, as amended. These acts provide the foundation for regulating the Nation's civilian uses of nuclear materials.

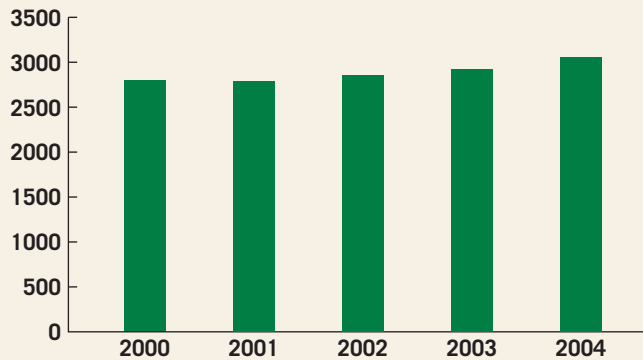
ORGANIZATION

The NRC is headed by a Commission composed of five members, with one member designated by the President to serve as Chairman. Each member is appointed by the President, with the advice and consent of the Senate, to serve 5 year terms. The Chairman serves as the principal executive officer and official spokesman for the Commission. The Executive Director for Operations carries out the program policies and decisions made by the Commission.

The NRC's headquarters is located in Rockville, Maryland. Four regional offices are located in King of Prussia, Pennsylvania; Atlanta, Georgia; Lisle, Illinois; and Arlington, Texas. The NRC's technical training center is located in Chattanooga, Tennessee. The NRC also has at least two resident inspectors at each nuclear power reactor site. The NRC's Operations Center

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NRC PERSONNEL CEILING FTE



is the focal point for NRC communications with its licensees, State agencies, and other Federal agencies concerning operating events in the commercial nuclear sector. The Operations Center is staffed 24 hours a day by NRC operations officers.

The NRC's budget for fiscal year (FY) 2004 was \$625.6 million and 3,040 full-time equivalent staff. The FY 2003 budget was \$584.6 million and 2,906 full-time equivalent staff. The NRC recovers most of its appropriations from fees paid by NRC licensees. Approximately 49 percent of the budget and 55 percent of the staff are for reactor safety.

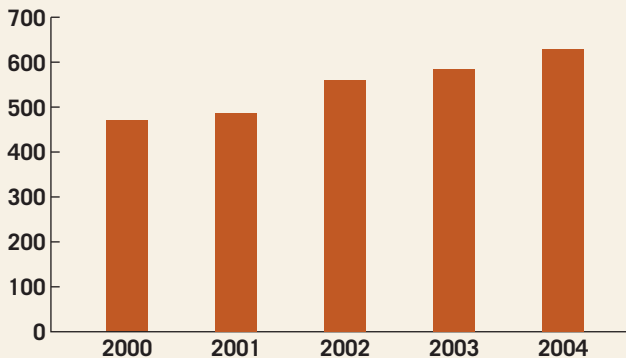
REGULATORY RESPONSIBILITY

To fulfill its responsibility to protect the public health and safety, the NRC performs three principal regulatory functions: (1) establish standards and regulations, (2) issue licenses for nuclear facilities and users of nuclear materials, and (3) inspect facilities and users of nuclear materials to ensure compliance with regulatory requirements. These regulatory functions relate to nuclear power plants, other nuclear facilities, and other civilian uses of nuclear materials, such as nuclear medicine programs at hospitals; academic activities at educational institutions; research work; industrial applications, such as gauges and testing equipment; and the transport, storage, and disposal of nuclear materials and wastes. The NRC has aligned its regulatory programs into the following four strategic arenas.

Nuclear Reactor Safety encompasses all NRC efforts to ensure that civilian nuclear power reactor facilities, as well as test and research reactors, are operated in a manner that adequately protects public health and safety and the environment, and that safeguards special nuclear materials used in reactors.

Nuclear Materials Safety encompasses NRC efforts to ensure that nuclear fuel cycle facilities; and academic, industrial, and medical uses of nuclear materials are handled in a manner that adequately protects public health and safety and the environment, and protects against radiological sabotage and theft or diversion of special nuclear materials.

NRC NEW BUDGET AUTHORITY Dollars in Millions





ABOUT THE NRC

Nuclear Waste Safety encompasses NRC efforts to ensure that the decommissioning of nuclear reactors and other facilities, storage of spent nuclear fuel, transportation of radioactive materials, and disposal of radioactive wastes are handled in a manner that adequately protects public health and safety and the environment, and protects against radiological sabotage and theft or diversion of special nuclear materials.

International Nuclear Safety Support encompasses international nuclear safety and regulatory policy formulation, import-export licensing for nuclear materials and equipment, treaty implementation, and international information exchange.

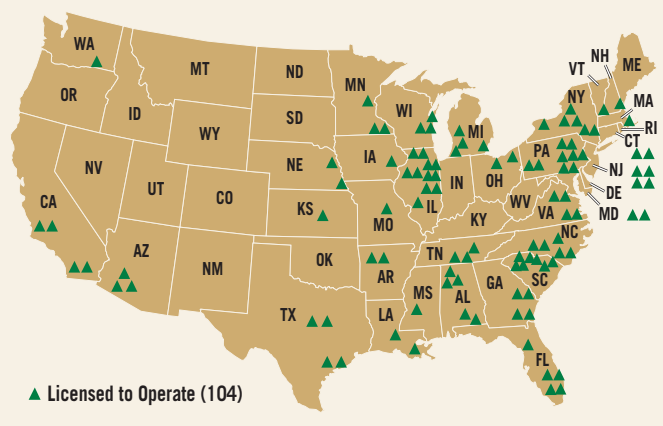
The NRC also carries out a **corporate management and support** function for information technology, financial management, human resources, and other support functions. Efforts in this area are aligned with the President's Management Agenda and focus on the five Governmentwide initiatives aimed at improving agency management.

Approximately 20 percent of the Nation's electricity is generated by 104 commercial nuclear reactors which are licensed by the NRC to operate in 31 States. Since 1992, nuclear electric generation has increased by approximately 21 percent. The NRC expends over 355,000 hours of inspection effort annually at 104 operating reactors and licenses approximately 4,500 reactor operators.

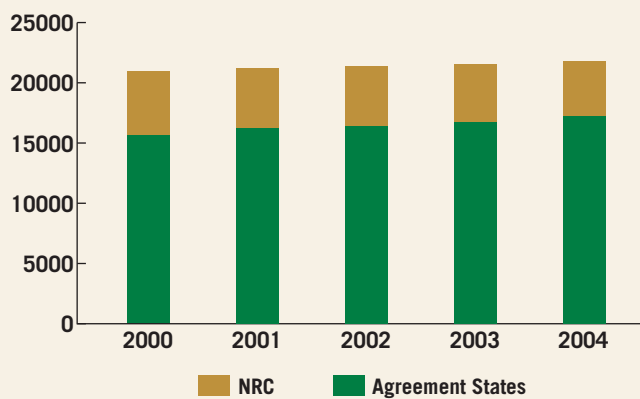
The NRC oversees approximately 4,500 licenses for medical, academic, industrial, and general uses of nuclear materials. The NRC conducts approximately 1,200 health and safety inspections of its nuclear materials licensees annually. Additionally, approximately 17,100 licenses are administered by the 33 States that participate in the NRC Agreement States Program, which authorizes the State to regulate the use of radioactive materials within that State. The NRC, Agreement States, and their licensees share a common responsibility to protect public health and safety.

The NRC places a high priority on keeping the public informed of its activities. Visit our Web site at www.nrc.gov to learn more about who we are and what we do to serve the American people.

U.S. COMMERCIAL NUCLEAR POWER REACTORS



U.S. MATERIALS LICENSES



MANAGEMENT'S DISCUSSION AND ANALYSIS

FUTURE CHALLENGES

The Commission is focused on addressing a number of significant challenges that will have a long-term impact in accomplishing its mission. The many industries that utilize radioactive materials are experiencing change, particularly in the areas of nuclear safety, security and emergency preparedness, risk-informed and performance based regulations, energy production, and waste management. In the next 5 years, the Nation is likely to see the following changes occur:

- NRC strategic initiatives will include continued emphasis on strengthening the interrelationship between safety, security, and emergency preparedness.
- The majority of operating nuclear power plants will have applied for license renewal to help meet the Nation's demand for energy production.
- The Department of Energy is expected to submit an application to construct and operate the Nation's high-level radioactive waste repository.
- Increasing quantities of radioactive waste may be transported and held in interim storage or permanent disposal sites.
- The nuclear power industry will show a growing interest in licensing and constructing new nuclear power plants and fuel cycle facilities (*e.g.*, gas centrifuge facilities and a mixed oxide fuel facility) to meet the Nation's demand for energy production.
- The NRC, Agreement States, and licensees will continue to devote increasing attention to the security of radioactive materials and facilities; in addition, the NRC will continue its nuclear non-proliferation activities.
- The NRC will continue to see an increase in requirements for coordination with a wide array of Federal, State, and local agencies related to homeland security and emergency planning.
- The number of Agreement States will increase, as will the numbers of medical, academic and industrial entities using radioactive materials under the oversight of the Agreement States.
- The regulatory climate is expected to adjust to both internal and external factors through the use of risk-informed and, as appropriate, performance-based regulations.



PROGRAM PERFORMANCE OVERVIEW

A backdrop to these industry-specific changes is one of elevated security and heightened public concern about safety. This has resulted in increased public dialogue about the uses of radioactive materials, varying from the potential for terrorist activities, to public concern about the adequacy of emergency preparedness plans for areas surrounding nuclear facilities. In this regard the NRC is committed to sharing openly with the public its information and decision-making processes consistent with the law and is committed to implementing regulatory processes that facilitate stakeholder involvement. While the NRC will continue to make as much information as possible available to the public, the agency will withhold information that could assist potential terrorists.

The manner in which the NRC regulates is also evolving. As the NRC continues to learn from operational experience and develops more effective ways of assessing risks and using risk-informed and performance based approaches founded in ‘realistic conservatism,’ the agency is better able to make appropriate safety decisions and to better allocate resources to areas where they will have the greatest positive effect. In addition, the NRC continues to seek improvement in effectiveness and efficiency. Toward that end, the agency is taking on specific management challenges that have been identified through ongoing program evaluations.

With respect to all facilities licensed by the NRC and Agreement States, the NRC is increasingly approaching safety, security, and emergency preparedness in an integrated manner. Safety requirements for structures, systems, components, programs, and people all contribute to both safety and security by making accidents unlikely and by making mitigation capability strong. In addition, safety and security requirements work together to make these facilities uninviting targets.

Ensuring the protection of public health and safety and the environment has always been, and continues to be, the NRC’s primary goal. Accordingly, safety is the most important consideration in evaluating license applications, licensee performance, and proposed changes to the regulatory framework. Because security is essential to the NRC’s mission and linked to safety, it also is an important consideration in the Agency’s actions. The Agency continuously works to improve its effectiveness and efficiency without conflicting with or undermining its safety and security mission.

PROGRAM PERFORMANCE OVERVIEW

Federal agencies provide an annual performance plan to Congress, setting goals with measurable target levels of performance based on the Government Performance and Results Act. The NRC evaluates its program performance within a structured planning, budgeting, and performance management process. As such, NRC has organized its strategic goals, performance goals, and strategies for achieving its mission into four strategic arenas. Our highest priority

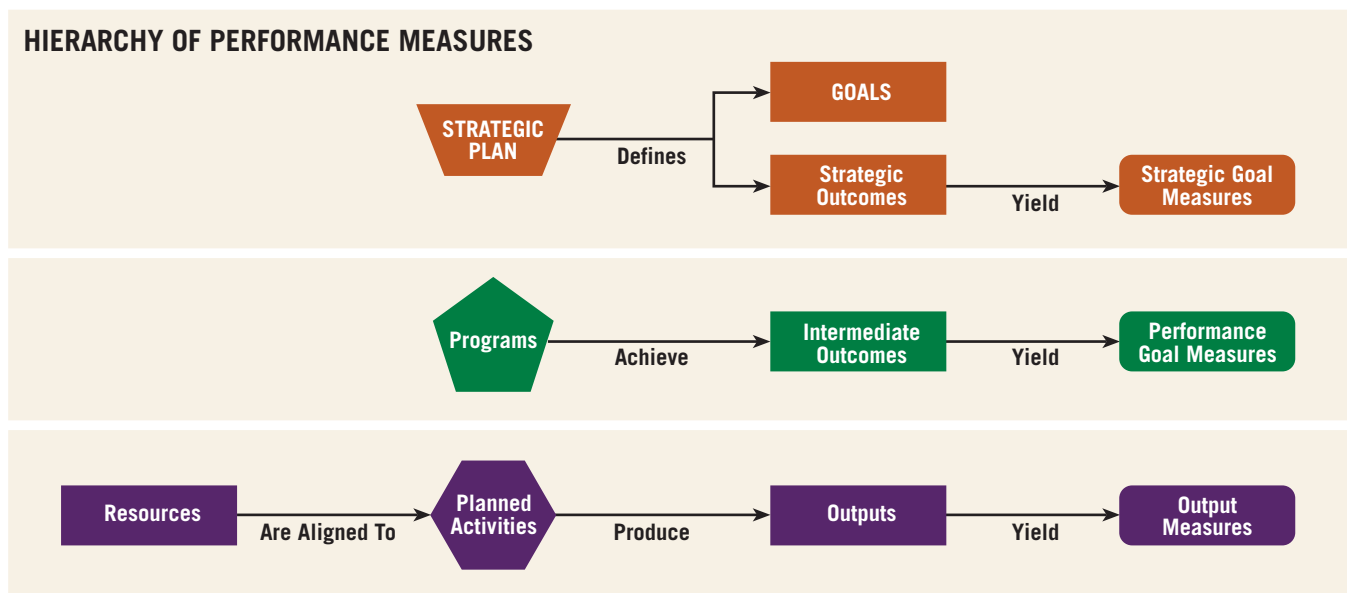
MANAGEMENT'S DISCUSSION AND ANALYSIS

is safety, and our strategic goals focus on the achievement of this priority. The NRC's FY 2000-FY 2005 Strategic Plan is available on the Web site <http://www.nrc.gov/reading-rm/doc-collections/nuregs/staff/sr1614/v2/part1/>. The complete FY 2004 Performance Report is contained in Chapter 2: Program Performance.

ACHIEVING STRATEGIC GOAL RESULTS

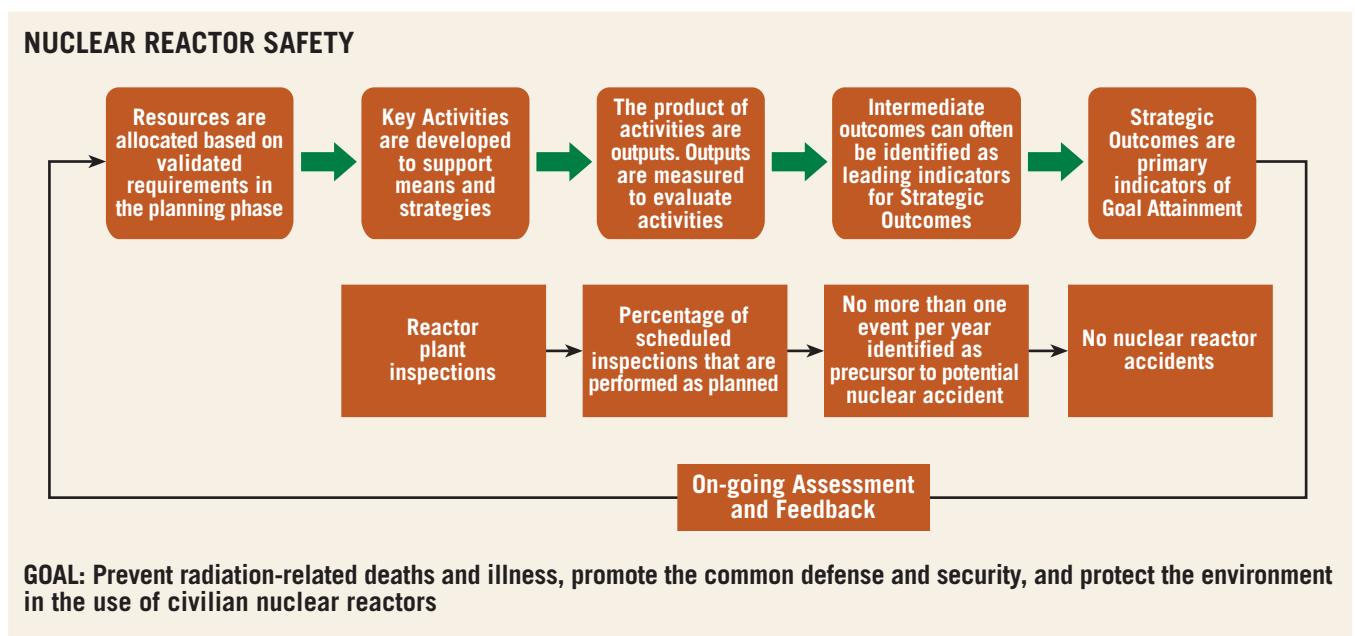
The NRC's performance management process approaches performance measurement as a layered process. As depicted in the diagram below, NRC's outputs are used to measure planned activities, intermediate outcomes are used to measure performance goals and strategic outcomes are used to measure achievement of the NRC's strategic goals. In the Performance and Accountability Report, the NRC reports mainly the results of strategic and performance goal measures. Selected output measures are used to identify significant accomplishments. However, output measures are most often reported in the NRC's annual performance budget.

The NRC's layered performance management approach links resources to planned activities, planned activities to programs, and programs to strategic goals. The associated measures inform management as to the efficiency of activities at the tactical level, the effectiveness of programs at the operational level and the attainment of goals at the strategic level.



PROGRAM PERFORMANCE OVERVIEW

The following example shows the relationship between NRC's reactor inspection activities and its strategic goal for nuclear reactor safety — Prevent radiation-related deaths and illness, promote the common defense and security, and protect the environment in the use of civilian nuclear reactors. In this example, resources are allocated to the planned activity, 'reactor plant inspections.' Key outputs from this planned activity support multiple intermediate outcomes (one is shown here as an example) and eventually the strategic outcome, 'no nuclear accidents.'



The NRC reports the output measures associated with the planned activity 'reactor plant inspections' in the annual performance budget. This level of reporting is focused on efficiencies at the working levels of the agency. The NRC reports the performance goal measures associated with the 'reactor inspection program,' and the strategic goal measures associated with the safety strategic outcome "no nuclear reactor accidents" in the NRC's annual Performance and Accountability Report.

During FY 2004, The NRC successfully met all strategic and performance goal targets for the four safety arenas. A brief summary of performance measurement follows here, with details contained in Chapter 2: Program Performance.

MANAGEMENT'S DISCUSSION AND ANALYSIS

NUCLEAR REACTOR SAFETY

Strategic Goal: Prevent radiation-related deaths and illnesses, promote the common defense and security, and protect the environment in the use of civilian nuclear reactors.

The NRC regulates 104 nuclear power reactors and 35 test and research reactors that are currently licensed to operate. Of these licensed reactors, the nuclear power plants generate approximately 20 percent of the Nation's electricity, while test and research reactors are used to safely conduct research and development. During FY 2004, the NRC met all five of the strategic goal measures for this arena. NRC completed 1,741 licensing actions during FY 2004 in support of the Nuclear Reactor Safety Goal.

NUCLEAR MATERIALS SAFETY

Strategic Goal: Prevent radiation-related deaths and illnesses, promote the common defense and security, and protect the environment in the use of source, byproduct, and special nuclear material.

The Nuclear Materials Safety program encompasses NRC-regulated aspects of nuclear fuel cycle facilities and nuclear materials activities. The NRC and 33 Agreement States regulate more than 20,000 specific and 150,000 general licensees. The Materials Users License and Inspection Program currently regulates and inspects approximately 4,500 specific licensees for the use of nuclear byproduct and other radioactive materials. For FY 2004, the NRC met all four of its strategic goal measures for this arena.

NUCLEAR WASTE SAFETY

Strategic Goal: Prevent significant adverse impacts from radioactive waste to the current and future public health and safety and the environment, and promote the common defense and security.

Nuclear Waste Safety encompasses regulatory activities associated with the decommissioning of nuclear reactors and other facilities, storage of spent nuclear fuel, transportation of radioactive materials, and disposal of radioactive waste. For FY 2004, the NRC met all four of its strategic goal measures for this arena. The NRC continued to build and refine the regulatory framework for evaluating the license application for the proposed Yucca Mountain Repository. This included certifying the NRC's documentary material for the purposes of the Licensing Support Network.



PRESIDENT'S MANAGEMENT AGENDA

INTERNATIONAL NUCLEAR SAFETY SUPPORT

Strategic Goal: Support U.S. interests in the safe and secure use of nuclear materials and in nuclear nonproliferation.

International Nuclear Safety Support encompasses international nuclear policy formulation, export-import licensing for nuclear materials and equipment, treaty implementation, nuclear proliferation deterrence, international safety assistance, and safeguards support and assistance. For FY 2004, the NRC met all three measures established for this arena. During FY 2004, the NRC furnished its extensive regulatory experience to other nations' nuclear safety and security efforts. This included collaborating in the finalization of the International Atomic Energy Agency (IAEA) Code of Conduct for the Safety and Security of Radioactive Sources. NRC also contributed to development of the international guidance document for the import/export of high-risk radioactive sources.

PRESIDENT'S MANAGEMENT AGENDA

The Governmentwide initiatives of the President's Management Agenda are intended to make Government more citizen-centered, results-oriented, and market-based and to actively promote competition. The five Governmentwide initiatives are: (1) Strategic Management of Human Capital, (2) Competitive Sourcing, (3) Improved Financial Management, (4) Expanded E-Government, and (5) Budget and Performance Integration. The NRC is actively implementing the agenda to improve the management and performance of the Federal Government. Chapter 2 of this report discusses our accomplishments in these important areas.

FINANCIAL PERFORMANCE OVERVIEW

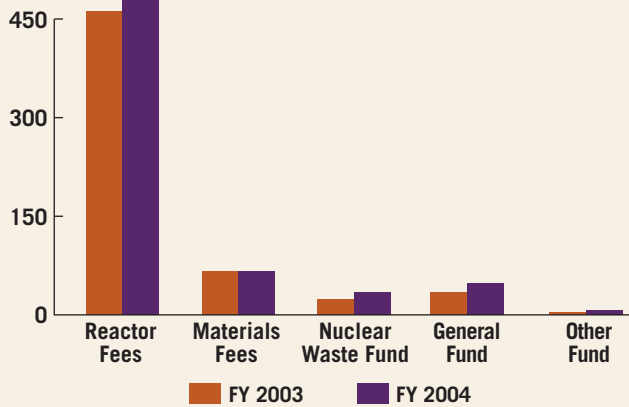
As of September 30, 2004, and 2003, the financial condition of the NRC was sound with respect to having sufficient funds to meet program needs and adequate control of these funds in place to ensure obligations did not exceed budget authority. The NRC prepared its financial statements in accordance with the accounting standards codified in the Statements of Federal Financial Accounting Standards (SFFAS) and Office of Management and Budget (OMB) Bulletin No. 01-09, *Form and Content of Agency Financial Statements*.

SOURCES OF FUNDS

The NRC has two appropriations, Salaries and Expenses and Office of the Inspector General (OIG), and funds for both appropriations are available until expended. The NRC's total new

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SOURCES OF FUNDS in millions

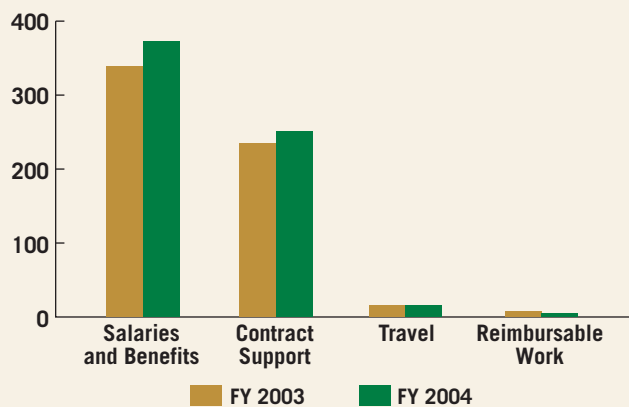


FY 2004 budget authority was \$625.6 million. Of this amount, \$618.3 million is for the Salaries and Expenses appropriation and \$7.3 million is for the Office of the Inspector General appropriation. This represents an increase in new budget authority of \$41.0 million over FY 2003 (\$40.5 million for the Salaries and Expenses appropriation and \$0.5 million for the Office of the Inspector General appropriation). In addition, \$43.5 million from prior year appropriations, \$3.7 million from prior year reimbursable work, and \$8.8 million for new reimbursable work to be performed for others was available to obligate in FY 2004. The sum of all funds available to obligate for FY 2004 was \$681.6 million, which is a \$44.2 million increase over the FY 2003 amount of \$637.4 million.

The Omnibus Budget Reconciliation Act of 1990 (OBRA-90), as amended, required the NRC to collect fees to offset approximately 92 percent of its new budget authority, less the amount appropriated to the NRC from the Nuclear Waste Fund for FY 2004. The NRC collected \$547.3 million in FY 2004. This is 100 percent of the recovery requirement. For FY 2003, OBRA-90 required NRC to collect approximately 94 percent of its new budget authority, excluding appropriations from the Nuclear Waste Fund.

USES OF FUNDS BY FUNCTION

USES OF FUNDS BY FUNCTION in millions



The NRC incurred obligations of \$645.3 million, which was an increase of \$48.3 million over FY 2003. Approximately 58 percent of obligations were used for salaries and benefits. The remaining 42 percent was used to obtain technical assistance for the NRC's principal regulatory programs, to conduct confirmatory safety research, to cover operating expenses, (e.g., building rentals, transportation, printing, security services, supplies, office automation, training), staff travel, and reimbursable work. The unobligated budget authority available at the end of FY 2004 was \$36.3 million, which is a decrease compared to the FY 2003 amount of \$40.4 million. Of this \$36.3 million, \$6.5 million is for reimbursable work and \$29.8 million is available to fund critical NRC needs in FY 2005.



FINANCIAL PERFORMANCE OVERVIEW

AUDIT RESULTS

The NRC received an unqualified audit opinion on its FY 2004 financial statements and a qualified opinion on its restated FY 2003 financial statements. The auditors identified one material internal control weakness concerning the Fee Billing System. This weakness was also identified as a substantial noncompliance with the Federal Financial Management Improvement Act (Improvement Act). The agency is developing its corrective action and remediation plans to address the auditor's identified material weakness and the substantial noncompliance.

In addition to the material weakness, the auditors identified two new reportable conditions concerning user organization compensating controls and fee recovery from licensees. The auditors closed three of the five prior-year reportable conditions concerning contract close-out processing procedures, information systems security access, and sustaining management controls over cost accounting. The remaining two reportable conditions concern the development of the hourly rate for license fees and accounting for internal use software. The agency expects to fully implement corrective action during FY 2005 for the internal use software condition and to complete corrective action for the hourly rate for license fees during FY 2006.

FINANCIAL STATEMENT HIGHLIGHTS

The NRC's financial statements summarize the financial activity and financial position of the agency. The NRC's FY 2003 financial statements have been restated to reflect an under statement of accounts receivable and revenue of approximately \$3 million from license fee billings and \$777 thousand in FY 2002 capital leases not previously recorded, and a reclassification of unfilled customer orders of \$4.7 million. The financial statements, footnotes, and the balance of the required supplementary information, appear in Chapter 3: Auditors' Report and Financial Statements. Analysis of the principal statements follows.

ANALYSIS OF THE BALANCE SHEET

The NRC's assets were approximately \$283.3 million as of September 30, 2004. This is an increase of \$3.5 million from the end of FY 2003. The assets reported in NRC's Balance Sheet are summarized in the accompanying table.

The Fund Balance with Treasury represents the NRC's largest asset of \$200.3 million as of September 30, 2004, an increase of \$6.9 million from the FY 2003 year-end balance. This balance accounts for approximately 71 percent of total assets

ASSET SUMMARY (in millions)		
	FY 2004	FY 2003 Restated
Fund Balance with Treasury	\$200.3	\$193.4
Accounts Receivable, Net	54.0	53.2
Property, Plant, & Equipment, Net	26.7	30.2
Other	2.3	3.0
Total Assets	\$283.3	\$279.8

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and represents appropriated funds, collected license fees, and other funds maintained at the U.S. Treasury to pay current liabilities.

Accounts Receivable, Net, as of September 30, 2004, was \$54.0 million and includes an offsetting allowance for doubtful accounts of \$2.1 million. This is a 2 percent increase from the FY 2003 year-end Accounts Receivable, Net, balance of \$53.2 million. Accounts Receivable Due from the Public was \$50.6 million, representing 18 percent of total assets.

The value of Property, Plant, and Equipment, Net, was \$26.7 million, representing 9 percent of total assets. The majority of the balance is comprised of nuclear reactor simulators, leasehold improvements, and computer hardware and software.

LIABILITIES SUMMARY (in millions)		
	FY 2004	FY 2003 Restated
Accounts Payable	\$27.9	\$27.3
Federal Employee Benefits	8.1	9.1
Other Liabilities	109.9	101.8
Total Liabilities	\$145.9	\$138.2

The NRC's liabilities were \$145.9 million as of September 30, 2004. The accompanying table shows an increase in Total Liabilities of \$7.7 million from the FY 2003 year-end balance of \$138.2 million. Other Liabilities include \$53.7 million for recoveries from unbilled accounts receivable, \$13.0 million for accrued salaries to employees, and \$32.2 million for accrued annual leave. Of the agency's liabilities, \$42.0 million were not covered by budgetary resources, which is a slight increase over the balance as of September 30, 2003. Liabilities not covered by budgetary resources are unfunded pension expenses, accrued annual leave, and future

workers' compensation. The Federal budget process does not recognize the cost of future benefits for today's employees. Instead, the Federal budget process recognizes those costs in future years when they are actually paid.

NET POSITION SUMMARY (in millions)		
	FY 2004	FY 2003 Restated
Unexpended Appropriations	\$149.9	\$149.7
Cumulative Results of Operations	(12.5)	(8.1)
Total Net Position	\$137.4	\$141.6

The difference between total assets and total liabilities, net position, was \$137.4 million as of September 30, 2004. This is a decrease of \$4.2 million from the FY 2003 year-end balance. Unexpended Appropriations is the amount of authority granted by Congress that has not been expended. Cumulative Results of Operations represent net results of operations since the NRC's inception. The decrease is primarily the result of a \$3.5 million decrease in Property, Plant, and Equipment, Net.



FINANCIAL PERFORMANCE OVERVIEW

ANALYSIS OF THE STATEMENT OF NET COST

The Statement of Net Cost presents the net cost of NRC's four strategic arenas as identified in the NRC Annual Performance Plan. The purpose of this statement is to link program performance to the cost of programs. The NRC's net cost of operations for the year ended September 30, 2004, was \$110.5 million, which is an increase of \$49.8 million over the restated FY 2003 net cost of \$60.7 million. The greater percentage of this increase is due to an increase in gross costs in the Nuclear Reactor Safety arena pertaining to an increase in salaries, benefits, and contract costs. Net costs by strategic arena are shown in the accompanying table.

Total exchange revenue for the year ended September 30, 2004, was \$552.2 million, which is an increase of \$11.7 million over the exchange revenue of \$540.5 million for the year ended September 30, 2003. Exchange revenue is derived from fees for licensing inspections, other services, and annual fees assessed in accordance with 10 CFR Parts 170 and 171. The greater percentage of the increase occurred in the Nuclear Reactor Safety arena pertaining to Part 170 inspections.

NET COST OF OPERATIONS (in millions)		
	FY 2004	FY 2003 Restated
Nuclear Reactor Safety	\$(26.3)	\$(64.4)
Nuclear Materials Safety	40.2	33.5
Nuclear Waste Safety	82.2	77.6
International Nuclear Safety Support	14.4	14.0
Net Cost of Operations	\$110.5	\$60.7

ANALYSIS OF STATEMENT OF CHANGES IN NET POSITION

The Statement of Changes in Net Position reports the change in net position during the reporting period. Net position is affected by changes in its two components—Cumulative Results of Operations and Unexpended Appropriations. The decrease in Net Position of \$4.2 million from FY 2003 to FY 2004 is due primarily from the net change in Cumulative Results of Operations of \$4.4 million due to increase in investment in Property, Plant, and Equipment.

Analysis of the Statement of Budgetary Resources

The Statement of Budgetary Resources shows the sources of budgetary resources available and the status at the end of the period. It presents the relationship between budget authority and budget outlays, and reconciles obligations to total outlays. For FY 2004, NRC had Total Budgetary Resources available of \$681.3 million, the majority of which was derived from new budget authority. This represents a 7 percent increase over FY 2003 budgetary resources available of \$637.4 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For FY 2004, the Status of Budgetary Resources showed the NRC incurred obligations of \$645.3 million, or 95 percent of funds available. This is comparable to FY 2003 obligations of \$597 million, at 94 percent of funds available. Total Outlays for FY 2004 were \$616.6 million, which represents a \$42.2 million increase from FY 2003 total Outlays of \$574.3 million.

Analysis of the Statement of Financing

The Statement of Financing is designed to provide the bridge between accrual-based (financial accounting) information in the Statement of Net Cost and obligation-based (budgetary accounting) information in the Statement of Budgetary Resources by reporting the differences and reconciling the two statements. This reconciliation ensures that the proprietary and budgetary accounts in the financial management system are in balance. The Statement of Financing takes Budgetary Obligations of \$645.3 million and reconciles to the Net Cost of Operations of \$110.5 million by deducting non-budgetary resources, costs not requiring resources, and financing sources yet to be provided.

SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

This section provides information on NRC's compliance with the:

- Federal Managers' Financial Integrity Act
- Federal Financial Management Improvement Act
- Prompt Payment Act
- Debt Collection Improvement Act
- Biennial Review of User Fees
- Inspector General Act
- Other key legal and regulatory requirements



SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

The Federal Managers' Financial Integrity Act (Integrity Act) mandates that agencies establish controls that reasonably ensure that: (i) obligations and costs comply with applicable law; (ii) assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and (iii) revenues and expenditures are properly recorded and accounted for. This act encompasses program, operational, and administrative areas as well as accounting and financial management. It also requires the Chairman to provide an assurance statement on the adequacy of management controls and conformance of financial systems with Governmentwide standards.

MANAGEMENT CONTROL REVIEW PROGRAM

Managers throughout the NRC are responsible for ensuring that effective controls are implemented in their areas of responsibilities. Each office director and regional administrator prepared an annual assurance statement that identified any control weaknesses that required the attention of the NRC's Executive Committee on Management Controls. These statements were based on various sources and included:

- Management knowledge gained from the daily operation of agency programs and reviews.
- Management reviews.
- Program evaluations.
- Audits of financial statements.
- Reviews of financial systems.
- Annual performance plans.
- Inspector General and Government Accountability Office reports.
- Reports and other information provided by the congressional committees of jurisdiction.

The NRC's Executive Committee on Management Controls is comprised of senior executives from offices of the Chief Financial Officer and the Executive Director of Operations, with the General Counsel and the Inspector General participating as advisors. The committee met and



INTEGRITY ACT STATEMENT

The U.S. Nuclear Regulatory Commission evaluated its management controls and financial management systems for FY 2004, as required by the Federal Managers' Financial Integrity Act. On the basis of the NRC's comprehensive management control program, I certify, with reasonable assurance, that the agency is in compliance with the provisions of this act.

A handwritten signature in black ink, appearing to read "Nils J. Diaz".

Nils J. Diaz
Chairman
U.S. Nuclear Regulatory Commission
November 15, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS

reviewed these individual assurance statements. The committee then advised the Chairman whether the NRC had any management control deficiencies serious enough to be reported as a material weakness or material noncompliance.

The NRC's ongoing management control program requires, among other things, that management control deficiencies are integrated into offices' and regions' annual operating plans. The operating plan process has provisions for periodic updates and for attention from senior managers. The management control information in these plans, combined with the individual assurance statements discussed previously, provides the framework for monitoring and improving the agency's management controls on an ongoing basis.

FY 2004 INTEGRITY ACT RESULTS

The NRC evaluated its management control systems for the fiscal year ending September 30, 2004. This evaluation provided reasonable assurance that the agency's management controls achieved their intended objectives. As a result, management concluded that the NRC did not have any material weaknesses, as defined by the Integrity Act, in its programmatic or administrative activities. The Fee Billing System was identified as a significant management control weakness and was of sufficient importance to merit the close attention of senior management.

FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT

The Improvement Act requires each agency to implement and maintain systems that comply substantially with: (i) Federal financial management system requirements, (ii) applicable Federal accounting standards, and (iii) the standard general ledger at the transaction level. The act requires the Chairman to determine whether the agency's financial management systems comply with the Improvement Act and to develop remediation plans for systems that do not comply.

FY 2004 IMPROVEMENT ACT RESULTS

As of September 30, 2004, the NRC evaluated its financial systems to determine if they complied with applicable Federal requirements and accounting standards required by the Improvement Act. The following seven systems were evaluated: the Federal Financial System, Human Resources Management System, Cost Accounting System, Advice of Allotments/Financial Plan, Capitalized Property System, Fee Billing System, and Controller Resource Database System.



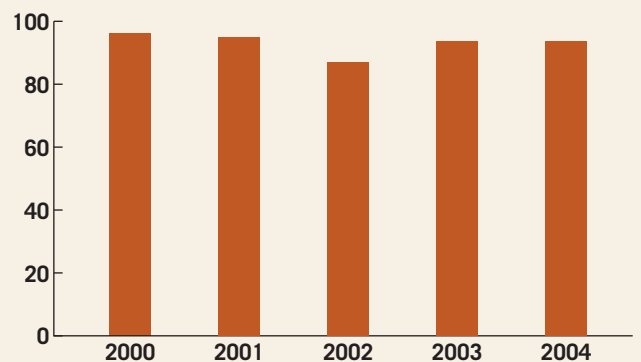
SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

The Chairman of the NRC determined that as of September 30, 2004, NRC financial management systems were in substantial compliance with the Improvement Act, except for the Fee Billing System which is in substantial noncompliance with Federal financial management system requirements. In making his determination, the Chairman considered all the information available to him, including the NRC Executive Committee on Management Control's report on the effectiveness of internal controls and OIG audit reports. He also considered the results of the financial management systems reviews conducted by the agency.

PROMPT PAYMENT

The Prompt Payment Act requires Federal agencies to make timely payments to vendors for supplies and services, to pay interest penalties when payments are made after the due date, and to take cash discounts when they are economically justified. From FY 2003 to FY 2004, the NRC had an increase of 1,042 invoices (from 8,128 to 9,170) that were paid and subject to the Prompt Payment Act. The NRC has remained at 94 percent of on-time payments subject to the Prompt Payment Act from FY 2003 to FY 2004. The amount of interest penalties incurred during FY 2004 was \$2,917, which is a slight decrease from FY 2003's amount of \$2,927. The agency continued to make over 99 percent of its vendor payments electronically.

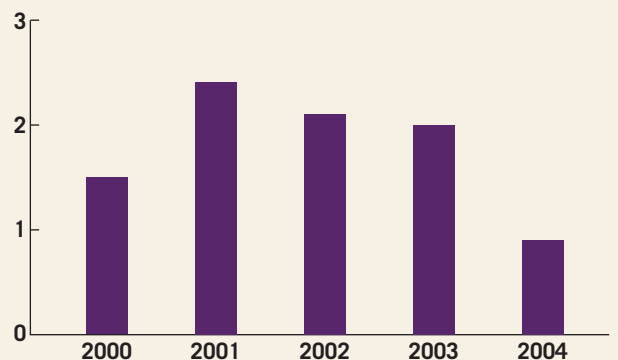
PROMPT PAYMENT Percent of On-Time Payments



DEBT COLLECTION

The Debt Collection Improvement Act is intended to enhance the ability of the Federal Government to service and collect debts. The agency's goal is to maintain the delinquent debt owed to the NRC, at year end to less than one percent of its annual billings. The NRC continues to meet this goal and has kept delinquent debt to less than one percent for the past 9 years. Delinquent debt at the end of FY 2004 was \$0.9 million. This is a decrease of \$1.1 million over FY 2003 and a decrease in the number of outstanding receivables from 233 to 154. The NRC continues to aggressively pursue the collection of delinquent debt and continues to timely refer all eligible delinquent debt over 180 days to the U.S. Treasury for collection.

DELINQUENT DEBT In Millions



MANAGEMENT'S DISCUSSION AND ANALYSIS

BIENNIAL REVIEW OF USER FEES

The Chief Financial Officers Act requires agencies to conduct a biennial review of fees, royalties, rents, and other charges imposed by agencies, and make revisions to cover program and administrative costs incurred. During FY 2004, the NRC reviewed its fees subject to the biennial review requirement. Each year, the NRC revises the hourly rates for license and inspection fees and adjusts the annual fees to meet the fee collection requirements of the Omnibus Budget Reconciliation Act of 1990, as amended.

The most recent changes to the license, inspection, and annual fees are described in the *Federal Register* (68 FR 36714, June 18, 2003). The fees and charges for the Criminal History Program were also revised to more appropriately recognize actual costs. Reviews of other types of fees were not warranted at this time.

TREASURY PERFORMANCE MEASURE SUMMARY

Treasury has five key elements for measuring how agencies complied with reporting requirements for the Federal Agencies Centralized Trial Balance Statement (FACTS I) and intragovernmental activity. Overall for FY 2003, the NRC complied with the five reporting elements for timely reporting, reconciliation of beginning and ending net position differences, reliability of FACTS I reporting, consistency of audited financial statements to FACTS I reporting, and intragovernmental activity for elimination of differences. Treasury has not issued its FY 2004 Performance Measure Summary; however, based on our self-evaluation, NRC also met the requirements for this fiscal year.

INSPECTOR GENERAL ACT

The agency has established and continues to maintain an excellent record in resolving and implementing open audit recommendations presented in Office of the Inspector General (OIG) reports. Section 5(b) of the Inspector General Act requires agencies to report on final actions taken on OIG audit recommendations. This information as well as data concerning disallowed costs determined through contract audits conducted by the Defense Contract Audit Agency can be found in Appendix C.



SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

IMPROPER PAYMENTS

Improper payments continue to be at low risk for the agency. The NRC continues to evaluate its internal controls to guard against improper payments and monitors and reports on all improper payments within its programs. At the present time, NRC's inventory of functional payment areas consists of commercial vendor, interagency, and travel payments. The Department of Interior's Federal Personnel/Payroll System became the NRC system of record for payroll disbursements effective November 2, 2003. The Department of Interior's National Business Center is responsible for monitoring and reporting on any improper payroll-related payments. The NRC will continue to perform annual risk assessments for each of these areas. Based on the FY 2004 risk assessments the reporting requirement is not applicable since each of these programs were well within the OMB guidance on what is considered to be a significant risk.

MANAGEMENT'S DISCUSSION AND ANALYSIS



CHAPTER 2: PROGRAM PERFORMANCE

