



... committed
to effective
and efficient
management of
our resources ...

A MESSAGE FROM THE CHIEF FINANCIAL OFFICER

I am pleased to present the U.S. Nuclear Regulatory Commission's financial statements for FY 2005 as an integral part of the agency's *FY 2005 Performance and Accountability Report*. Our independent auditor has rendered an unqualified opinion on our financial statements, attesting to the fact that NRC's financial statements are fairly presented and demonstrate discipline and accountability in the execution of our responsibilities as stewards of the American taxpayers' dollars.



As of September 30, 2005, the financial condition of the NRC is sound with respect to having sufficient funds to meet its mission and having adequate control of these funds to ensure our budget authority is not exceeded. We successfully collected approximately 99 percent of the agency's budget that is subject to fee recovery from NRC licensees and our year-end delinquent debt was minimal, less than our goal of one-half of one percent of the fees collected. Ninety-six percent of payments to commercial vendors, subject to the Prompt Payment Act, were made on-time with less than one-half of one percent made erroneously. We have also received excellent ratings for maintaining our fund balance with Treasury and for our timely and accurate reporting.

During FY 2005, we continued our efforts to eliminate the auditor-identified material internal control weakness related to the Fee Billing System. We implemented improvements to the fee billing process but further corrective action is needed (Chapter 1, *Audit Results*). In addition, we have resolved two reportable conditions and are working to address the remaining three. We identified three systems, Fee Billing System and two systems provided under an e-Government cross-servicing arrangement (core accounting and payroll), to be in substantial noncompliance with Federal financial management system requirements. We developed a remediation plan for the Fee Billing System targeted to achieve compliance in 2007 and are monitoring the corrective actions being taken by the cross-service provider to bring their systems into compliance.

The NRC is committed to effective and efficient management of its resources. Our goals and strategies for improving financial management are centered on maintaining unqualified audit opinions, eliminating our material internal control weakness, upgrading financial systems to meet Federal requirements, meeting new reporting requirements, and implementing e-Government initiatives. We continue to be successful

CHAPTER 3
AUDITORS' REPORTS AND FINANCIAL STATEMENTS

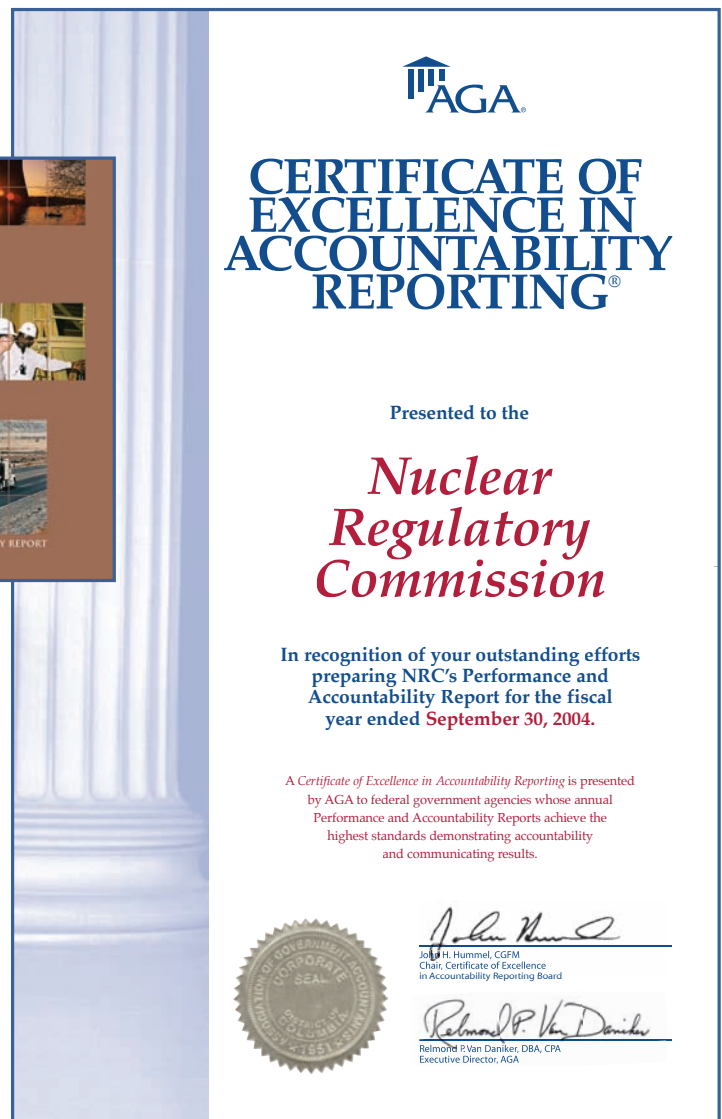
in ensuring that our operations provide timely and reliable information that is used to promote results, accountability, and efficiency. This has been possible through the efforts and teamwork of program, financial management, and audit staff.

I anticipate another productive year in FY 2006 and a continuation of the same high level of financial services that resulted in our past successes. While we make progress, we are mindful of our support role in getting an unqualified audit opinion on the *Financial Report of the United States Government*.

Jesse L. Funches



November 15, 2005



AUDITORS' REPORTS



UNITED STATES
NUCLEAR REGULATORY COMMISSION
WASHINGTON, D.C. 20555-0001

OFFICE OF THE
INSPECTOR GENERAL

November 10, 2005

MEMORANDUM TO: Chairman Diaz

FROM: Hubert T. Bell
Inspector General

A handwritten signature in black ink that reads "Hubert T. Bell".

SUBJECT: RESULTS OF THE AUDIT OF THE
UNITED STATES NUCLEAR REGULATORY COMMISSION'S
FINANCIAL STATEMENTS FOR FISCAL YEARS 2005
AND 2004 (OIG-06-A-01)

The Chief Financial Officers Act of 1990, as amended, (CFO Act) requires the Inspector General (IG) or an independent external auditor, as determined by the IG, to annually audit the United States Nuclear Regulatory Commission's (NRC) financial statements in accordance with applicable standards. In compliance with this requirement, this memorandum transmits the following R. Navarro & Associates, Inc. Auditors' Reports:

- Independent Auditors' Report on the FYs 2005 and 2004 Financial Statements,
- Report on the Effectiveness of Internal Control over Financial Reporting, and
- Report on Compliance with Laws and Regulations.

Objective of a Financial Statement Audit

The objective of a financial statement audit is to determine whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation.

R. Navarro & Associates' examination was made in accordance with generally accepted auditing standards, *Government Auditing Standards* issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. The audit included obtaining an understanding of the internal controls over financial reporting and testing and evaluating the design and operating effectiveness of the internal controls. Because of inherent limitations in any internal control, there is a risk that errors or fraud may occur and not be detected. Also, projections of any evaluation of internal control over financial reporting to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate. The risk of fraud is inherent to many of NRC's programs and operations.

Results of Audit

The results are as follows:

Financial Statements

- FYs 2005 and 2004 — Unqualified opinion

FY 2005 Internal Controls

- Qualified opinion
- Reportable Conditions:
 - Fee Billing System (Also represents a **Continuing Material Weakness**)
 - Monitoring of Accounting for Internal Use Software (Continuing Condition)
 - Information System-Wide Security Controls (New Condition)
 - Financial Controls over Disbursements (New Condition)

FY 2005 Compliance with Laws and Regulations

- Noncompliances:
 - Part 170 Hourly Rates (Continuing Noncompliance)
 - Fee Billing System (Continuing **Substantial Noncompliance**)
 - Information System-Wide Security Controls (New **Substantial Noncompliance**)

OIG Evaluation of R. Navarro and Associates, Inc., Performance

To fulfill our responsibilities under the CFO Act and related legislation for ensuring the quality of the audit work performed, we monitored R. Navarro & Associates' audit of NRC's FYs 2005 and 2004 financial statements by:

- Reviewing their approach and planning of the audit,
- Evaluating the qualifications and independence of its auditors,
- Monitoring the progress of the audit at key points,
- Examining the workpapers related to planning and performing the audit and assessing NRC's internal control, Reviewing R. Navarro & Associates' audit reports to ensure compliance with *Government Auditing Standards* and OMB Bulletin No. 01-02,
- Coordinating the issuance of the audit reports, and
- Performing other procedures that we deemed necessary.

R. Navarro & Associates, Inc., is responsible for the attached auditors' reports, dated November 4, 2005, and the conclusions expressed therein. The Office of the Inspector General (OIG) is responsible for technical and administrative oversight regarding the firm's performance under the terms of the contract. Our review, as differentiated from an audit in conformance with *Government Auditing Standards*, was not intended to enable us to express, and accordingly we do not express an opinion on NRC's financial statements, the effectiveness of its internal control over financial reporting, or NRC's compliance with laws and regulations. However, our monitoring review, as described above, disclosed no instances where R. Navarro & Associates, Inc., did not comply with applicable auditing standards.

Performance Reporting

As required by OMB Bulletin No. 01-02, with respect to internal control related to performance measures determined by management to be key and reported in the *Management's Discussion and Analysis*, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over performance measures and, accordingly, we do not provide an opinion thereon.

Meeting with the Chief Financial Officer

At the exit conference on November 7, 2005, representatives of the Office of the Chief Financial Officer, OIG, and R. Navarro & Associates, Inc., discussed the issues in the report.

Comments of the Chief Financial Officer

In his response, the CFO generally agreed with the auditors' recommendations. We will follow-up on the CFO's planned corrective actions during FY 2006. The full text of the CFO's response follows this report.

We appreciate NRC staff's cooperation and continued interest in improving financial management within NRC.

Attachment: As stated

cc: Commissioner McGaffigan
Commissioner Merrifield
Commissioner Jaczko
Commissioner Lyons



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Chairman Nils J. Diaz
U.S. Nuclear Regulatory Commission
Washington, DC

In our audits of the U.S. Nuclear Regulatory Commission (NRC), we found:

- The balance sheets of NRC as of September 30, 2005, and 2004, and the related statements of net cost, statements of changes in net position, statements of budgetary resources, and statements of financing for the fiscal years then ended are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America;
- Except for the material weakness over the Fee Billing System, the effectiveness of internal control over financial reporting was fairly stated as of September 30, 2005, in compliance with the internal control objectives in the Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*. The Bulletin requires that transactions be properly recorded, processed, and summarized to permit the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America and that assets be safeguarded against loss from unauthorized acquisition, use or disposal; and
- The NRC continues to be noncompliant with the provisions of OMB Circular A-25, *User Charges*, for Part 170 fees. Additionally, NRC continues to have a substantial noncompliance related to the Fee Billing System, and, in the current year, we are reporting an Improvement Act substantial noncompliance with the security controls over applications operating at a cross-servicing agency.

The following sections outline each of these conclusions in more detail.

INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying balance sheets of NRC as of September 30, 2005, and 2004, and the related statements of net cost, statements of changes in net position, statements of budgetary resources, and statements of financing for the fiscal years then ended. These financial statements are the responsibility of NRC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Bulletin No. 01-02. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Matters of Emphasis

Classification of Costs

OMB Circular A-136, *Financial Reporting Requirements*, provides guidance to Federal agencies for presenting program costs classified by intragovernmental and public components. The basis for classification relies on the concept of who received the benefits of the costs incurred (i.e., private sector licensees versus Federal licensees) rather than who was paid. However, following the advice of OMB, NRC classified the costs on the Statement of Net Cost using an underlying concept of who was paid. Furthermore, OMB Circular A-136 requires that the Statement of Net Cost be presented using full program costs by output. The agency presents its costs aggregated by strategic plan programs.

U.S. Department of Energy Expenses

NRC's principal statements include reimbursable expenses of the U.S. Department of Energy (DOE) National Laboratories. For the years ended September 30, 2005, and 2004, NRC's Statements of Net Cost include approximately \$68.7 and \$77.2 million, respectively, of reimbursed expenses. Our audits included testing these expenses for compliance with laws and regulations applicable to NRC. The work placed with DOE is under the auspices of a Memorandum of Understanding between NRC and DOE. The examination of DOE National Laboratories for compliance with laws and regulations is DOE's responsibility. This responsibility was further clarified by a memorandum of the Government Accountability Office's (GAO) Assistant General Counsel, dated March 6, 1995, where he opined that "...DOE's inability to assure that its contractors' costs [National Laboratories] are legal and proper...does not compel a conclusion that NRC has failed to comply with laws and regulations." DOE also has the cognizant responsibility to assure audit resolution and should provide the results of its audits to NRC.

In our opinion, the financial statements referred to above and included in NRC's performance and accountability report present fairly, in all material respects, the financial position as of September 30, 2005, and 2004, and its net cost, changes in net position, budgetary resources, and reconciliations of net cost to budgetary resources for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

Report on the Effectiveness of Internal Control Over Financial Reporting

We have examined the effectiveness of NRC's internal control over financial reporting, as of September 30, 2005, based on the criteria in OMB Bulletin No. 01-02. The Bulletin requires management to establish internal accounting and administrative controls to provide reasonable assurance that transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America and that assets be safeguarded against loss from unauthorized acquisition, use or disposal. NRC's management is responsible for maintaining effective internal control over financial reporting. Our responsibility is to express an opinion on the effectiveness of internal control based on our examination.

Our examination was conducted in accordance with the attestation standards established by the American Institute of Certified Public Accountants (AICPA); the standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin No. 01-02. Accordingly, we obtained an understanding of the internal control over financial reporting, tested and evaluated the design and operating effectiveness of internal control, and performed such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of internal control over financial reporting to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate.

We identified continuing significant deficiencies in the Fee Billing System. The system in place does not meet the requirements of sound internal control over financial reporting as provided in OMB Bulletin No. 01-02, nor is the system's design compliant with the requirements of the Joint Financial Management Improvement Program (JFMIP—Effective December 2004, JFMIP ceased to become a standalone entity). Its functions are now under the auspices of OMB and the Chief Financial Officers' Council) for Revenue Systems. We believe such a condition represents a material weakness. A material weakness is a reportable condition that precludes the NRC's internal control from providing reasonable assurance that material misstatements in the financial statements will be prevented and detected on a timely basis.

In our opinion, except for the effect of the material weakness described in the preceding paragraph, NRC has maintained, in all material respects, effective internal control over financial reporting as of September 30, 2005, based on the internal control objectives listed in OMB Bulletin No. 01-02.

Additionally, we noted certain matters involving the internal control and its operation that we consider to be reportable conditions under standards established by the AICPA and OMB Bulletin No. 01-02. A reportable condition is a matter coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the agency's ability to meet the internal control objectives described above. We identified four reportable conditions; NRC needs to

(1) improve the Fee Billing System, (2) improve monitoring of accounting for internal use software, (3) strengthen information system-wide security controls, and (4) strengthen financial controls over disbursements. The Fee Billing System condition is considered a material weakness.

A material weakness, as defined by the AICPA and OMB Bulletin No. 01-02, is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the principal financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We believe that the reportable conditions that follow, except for the Fee Billing System, are not material weaknesses as defined by the AICPA and OMB Bulletin No. 01-02.

Fee Billing System

During the assessment of internal controls in FY 2004, we identified significant deficiencies in the NRC's Fee Billing System, as described below. The agency has put forth a significant effort to address the issues reported in the prior year; however, greater emphasis and demonstrated sustainable business process improvements must be provided to remediate the material weakness.

The Omnibus Budget Reconciliation Act (OBRA-90), Public Law 101-508, as amended, requires that NRC recover, through fee billing, a percentage of its budget authority in each fiscal year, less amounts appropriated from the Nuclear Waste Fund. In FYs 2005 and 2004, the recovery percentage was 90 and 92 percent, respectively. In order to meet this requirement, the NRC assesses two types of fees to recover its budget authority. Annual fees are assessed under 10 CFR Part 171 for nuclear facilities and materials licensees, commonly known as Part 171 fees. Other fee types include license, inspection, and other services, established in 10 CFR Part 170 under the authority of the Independent Offices Appropriation Act (IOAA). The Part 170 fees are assessed to recover NRC's costs of providing individually identifiable services to specific applicants and licensees.

The conditions reported in the prior year resulted from several deficiencies, (1) inadequate acceptance testing of software modifications, (2) intensive manual processes, and (3) the lack of comprehensive quality assurance procedures over the billing process. In the current year, the agency has continued to identify underbilling problems with the Fee Billing System, indicating the need to more diligently document and design internal controls for each operating aspect of the system.

The GAO's *Standards for Internal Control in the Federal Government* state, "Internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties."

The following examples provide insights into the agency's progress and current condition in addressing (1) intensive manual processes, (2) lack of comprehensive quality assurance procedures, and (3) fee billing feeder processes.

Intensive Manual Processes

Due to the age and design of the Fee Billing System, NRC has evolved over the years into an operating style characterized by over-reliance on a small team to prepare, review, and issue billings on a monthly and quarterly basis. The License Fee Team employs various manual processes to compensate for the lack of flexibility in the legacy fee billing system. The system does not have the ability to give the agency drill down capacity to review billing questions. In particular, the system does not provide automated audit trails from the initial source of the transaction (i.e., billable hours) to the development of an invoice.

Over the last 2 fiscal years, the agency performed an assessment of the Fee Billing System and concluded, "...that the existing nine systems that collectively comprise the Fee Systems will not fully support fee billing and will not promote consistency across the agency. Streamlining, automating, and improving its fee systems and processes with modern and integrated technology and processes will be critical to the agency, its staff, and its customer going forward." The agency prepared a remediation plan describing actions designed to replace the existing system. Deployment of the replacement solution is planned for FY 2008.

The lack of system functionality coupled with the age of the system and its reliance on manual intervention continues to result in an Improvement Act substantial noncompliance.

Lack of Comprehensive Quality Assurance Procedures

During the current year, the agency developed quality assurance procedures to reconcile the completeness of Part 170 (hourly) invoices to the license fee reports produced by the Fee Billing System. The reports provide the amounts available for billing. Late in the fiscal year, an accompanying reconciliation was performed

using the new quality assurance procedures. However, the agency did not address several other reconciliation points that are essential to the internal control over fee billings.

For example, the quality assurance procedures did not address the completeness of billable contract costs as compared to contract payments made to vendors. The procedures also do not provide for a review of the reliability and completeness of data inputs from sources outside the Office of the Chief Financial Officer's (OCFO) business domain, which are integral to the reliability of invoices. Regional and technical offices such as Nuclear Materials Safety and Safeguards are the feeder source for license fee activities. This data is fundamental to the mapping of license fee rates in the billing preparation process. We commend the agency for its prompt action in developing some quality assurance procedures; however, much more needs to be done to mitigate known design and system risks of the legacy system and to assert to the completeness and reliability of the fee billing process.

Fee Billing Feeder Processes

In the current year, the agency identified several instances of underbilling, some of which date back to FY 1991. Although the net value of these unbilled accounts receivable does not have a material impact on the Balance Sheet, these instances highlight risks that are present in the Fee Billing System. The instances identified demonstrate the need to validate the feeder data from offices outside the CFO's business domain. The issues identified impact both Part 170 (hourly) and Part 171 (annual) fee billings and were identified during tasks related to data conversion, cost accounting data analysis, and policy research, as follows:

- **Data Conversion**—The agency is undergoing a conversion of the system used by the Office of Nuclear Materials Safety and Safeguards to track the licensee information by type of license. During this process, the universe of licensees was reviewed for completeness. The review identified several licensees that were inadvertently dropped from the universe of billable annual materials licensees. The information captured in this system by the program office is a key element of the data sources necessary for OCFO to identify licensees available for billing. The OCFO does not have procedures to verify the completeness of this data prior to initiating a billing cycle. The agency performed an analysis of the listing

of dropped licensees and identified approximately \$911 thousand of unbilled fees. The net effect on the Balance Sheet after providing for the allowance for doubtful accounts is approximately \$197 thousand.

- **Cost Accounting Data Analysis**—During the third quarter billing cycle, the Cost Accounting Team identified transactions that were assigned to suspended activity codes. Subsequently, the license fee staff researched these transactions and found that billable time (Part 170–hourly fees) had not been billed. Program activity codes are used to capture agency costs within NRC’s established budgetary program framework. The program activity codes were suspended because the general ledger tables containing viable billable codes had not been properly synchronized. At the start of each fiscal year, program activity codes are set up for all anticipated activities; however, as the year progresses new activity codes may be assigned, thereby triggering table maintenance issues. The unbilled amount was approximately \$20 thousand. The agency has indicated it will develop a process to verify that all tables are properly synchronized prior to starting a billing cycle.
- **Policy Research**—During research of a policy question on billing of project managers’ time (Part 170–hourly fees), the license fee staff found that billable time assigned by Nuclear Materials Safety and Safeguards managers was not included in billed amounts. Although the proper program activity codes were established at the beginning of the year, the contractor who supports the billing process was not advised of the code for general and administrative activities. As a result, \$50 thousand was not billed.

Although not material to these financial statements, the unbilled amounts illustrate the need for improved quality assurance procedures over the billing preparation process. The agency has indicated it will pursue billing and collection of each amount described in these examples.

Recommendations

1. The CFO should direct an assessment of all aspects of the Fee Billing System to ensure that the remediation plan is updated as necessary and implemented in a timely manner to enhance the controls over fee billing processes.
2. The CFO should define, design, and implement compensating controls over the fee billing system, while the system is being considered for redesign.

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3. As the CFO identifies needed improvement of internal controls outside OCFO's business domain, there should be coordination and collaboration with the Executive Director for Operations as to how, when and to what extent the internal controls should be strengthened in operational program feeder systems, relied upon by OCFO for billing preparation purposes.

Monitoring of Accounting for Internal Use Software

Although the OCFO has made strides with policy development and training, we continue to identify costs incurred and not recorded by OCFO for internal use software. OCFO's management control structure is designed to rely heavily on project managers to inform OCFO of time and costs expended in the software development phase. OCFO has not been fully successful in identifying projects through their monitoring procedures in order to ensure the completeness or reasonableness of the project manager's information.

Federal Accounting Standards Advisory Board issued Statements of Federal Financial Accounting Standards (SFFAS) No. 10, *Accounting for Internal Use Software*, effective October 1, 2000. SFFAS No. 10 defines three software life-cycle phases, planning, development, and operations. Paragraph 16 requires, "For internally developed software, capitalized cost should include the full cost (direct and indirect cost) incurred during the development phase." The Statement defines full cost to include salaries of programmers, project managers, administrative personnel, and associated employee benefits and outside consultants' fees.

Our review of the agency's practices for accounting for internal use software projects continues to identify the following inconsistencies:

- Contractor cost incurred on projects for work performed, but for which NRC has not been billed, were not being captured and capitalized;
- Project managers, in some instances, were not coding their time appropriately during the development phase of their projects; and
- Labor certifications, in some instances, were not being completed, signed and/or were being completed late.

For example, in the current year our audit procedures identified several projects where the costs were not properly recorded. At September 30, 2004, several projects were capitalized at \$480 thousand; however, we noted that the actual cost of the projects was in excess of \$700 thousand. The OCFO did not have a business process to collect invoices from contractors involved in the development process in order to more accurately capture project costs. The June 30, 2005, quarterly financial statements reflected the correction of these asset values.

Recommendation

4. The CFO should continue to promote strengthening internal use software practices, in order to encourage project managers to comply with procedures in effect governing the completeness of new and existing development initiatives.

Information System-wide Security Controls

A recent report issued by the Office of Inspector General (OIG) (Report No. OIG-05-A-21) identified risks in the agency's information security environment. The report identifies various conditions placing the agency in an "at risk" position. The following is a partial list of the issues reported:

- A majority of the information systems (19 of 27) are under an interim authorization to operate and, therefore are not considered certified;
- Agency information system security self-assessments were not performed timely;
- Annual contingency planning is not being performed; and
- Oversight of other contractor systems is lacking.

The OIG's report states, "NRC's general support systems have not had a complete certification and accreditation performed in the past 3 years. Therefore, the agency does not know whether the security controls for these general support systems are adequate, creating unknown potential risk. As a result, all NRC information systems that depend on the security controls provided by these general support systems inherit that unknown potential risk."

The primary agency financial reporting systems include cost accounting, human resources management system, fees and two systems outsourced with Department of Interior's National Business Center (DOI-NBC). The two outsourced systems are the Federal Financial System (i.e., the general ledger application) and Federal Personnel and Payroll System (i.e., the payroll application). These systems operate or have access protocols on the NRC's general support system, which has been identified as vulnerable,

since the general support system had a lapsed authorization to operate. OCFO, as the business sponsor for its systems, performed the assessment procedures necessary to adequately maintain their systems. However, their applications would be at risk since they rely on the top tier controls of the general support system.

For the systems that are outsourced to DOI-NBC, OCFO does not have processes to monitor the adequacy of security controls maintained by the service provider. In the current year, the agency did not know that the service provider had information security issues until they were provided a reasonable assurance letter, dated October 5, 2005. DOI-NBC reported a serious weakness in complying with OMB Circular A-130, *Management of Federal Information Resources*. DOI-NBC also characterized the weakness as an Improvement Act substantial noncompliance. The risks associated with (1) the lack of timely certification and accreditation, (2) delays in self- assessments, (3) the lack of annual contingency planning, and (4) the outsourced systems' substantial noncompliance, introduce an elevated risk to the NRC's information security system.

NRC management discussed these issues during the annual meeting on management controls as considerations for the agency's Integrity Act reportable items. NRC management is reporting the security risks associated with DOI-NBC as a substantial noncompliance with the Improvement Act.

Recommendations

5. The CFO should coordinate with the Office of Information Services and the Executive Director for Operations to keep abreast of progress in implementing the recommendations made in the OIG's report. This awareness will enable the CFO to better plan his information system security needs.
6. The CFO should establish procedures to monitor and participate in customer advisory work groups on information security issues with the service bureau. At a minimum, the CFO should devise a communication process to stay informed about information security testing and the related results.

Financial Controls Over Disbursements

The OCFO's Division of Financial Services develops and administers policies, standards, and procedures for all financial operation activities of the NRC. The Division is comprised of teams which devote their full attention to time and payroll processing, development of payment policy, processing of obligations, authorizing the payment of nonpayroll transactions, and managing approximately 60 percent of the agency's budget through the Central Allowance Team.

The GAO's *Standards for Internal Control in the Federal Government*, state "Internal control should generally be designed to assure that ongoing monitoring occurs in the normal course of operations. . . . It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties." The Standards also state, "Management's philosophy and operating style also affect the environment. This fact determines the degree of risk the agency is willing to take and management's philosophy toward performance-based management. Further the attitude and philosophy of management toward information systems, accounting, personnel functions, monitoring, and audits and evaluations can have a profound effect on the internal control."

In the current year, we found that the agency made one improper payment in excess of \$1 million. The NRC became aware of the error because the rightful vendor, who was not initially paid, contacted the agency to inquire about the status of its payment. An error of this nature could have been prevented by the controls described below:

- The agency has controls to verify the existence of vendors prior to payment. However, the agency does not have verification controls to review the propriety of edits made to the vendor tables. In the present case, two vendors requested changes to their vendor profiles. Items such as vendor name, address, tax identification number, and bank routing numbers are maintained in the vendor profiles.
- In the prior year, the agency indicated that it was adopting OMB's guidelines for drawing on the Central Contractor Registration (CCR) information to verify electronic funds transfer (EFT) information. The agency's system was planned to verify the propriety of payment information between the NRC's vendor tables and the CCR database prior to payment. We understand that the CCR business rules were implemented relying on internal NRC vendor table maintenance controls, rather than CCR validations. NRC has not implemented the secondary review of vendor table changes.

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- The agency does not have controls in place for review and approval of high value payments to non-Federal entities. NRC's high value payments range from amounts in excess of \$250 thousand to \$300 thousand. Payments in the high value category are not reviewed any differently than payments of nominal value. An independent or secondary validation of these amounts would most likely have detected the payment error.

Additional concerns with this improper payment are (1) the OCFO's lack of disclosure and (2) the lack of understanding of the impact of interest owed on the late invoice to the liabilities included on the Balance Sheet. This condition imposes unnecessary risk in the control environment.

Recommendations

7. The CFO should direct an assessment of financial controls over disbursement activities. At a minimum, the assessment should provide for the development and implementation of second party reviews of the propriety and accuracy of edits to vendor tables.
8. The CFO should periodically assess whether CCR data can be used to provide an electronic validation of EFT information against NRC's payment system prior to certifying the payment.
9. The CFO should establish a secondary review of high value payments. The secondary review should be performed by parties that are not involved directly in payment processing.
10. The CFO should reiterate to all agency managers the importance of having full and open discussion about internal control impacting the reliability and completeness of the agency's financial statements. This discussion could be incorporated during the upcoming implementation of OMB Circular A-123.

Status of Prior Year Comments

In the prior year, we included conditions related to User Organization Compensating Controls and Inadequate Acceptance Testing (included in the Fee Billing System condition) in our report. Corrective actions were implemented during the year to close these two conditions. However, conditions related to the fee billing system and monitoring of accounting for internal use software continued in the current fiscal year.

Report on Compliance with Laws and Regulations

We conducted our audit for the year ended September 30, 2005, in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and OMB Bulletin No. 01-02.

NRC management is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether the agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of applicable regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts and certain other laws and regulations specified in OMB Bulletin No. 01-02, including the requirements in the Improvement Act. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to NRC. The results of our tests of compliance disclosed noncompliances with laws and regulations that are required to be reported under *Government Auditing Standards*, OMB Bulletin No. 01-02 or under the Improvement Act.

U.S. Department of Energy Expenses

NRC's principal statements include reimbursable expenses of DOE National Laboratories. For the years ended September 30, 2005, and 2004, NRC's Statements of Net Cost include approximately \$68.7 and \$77.2 million, respectively, of reimbursed expenses. Our audits included testing these expenses for compliance with laws and regulations applicable to NRC. The work placed with DOE is under the auspices of a Memorandum of Understanding between NRC and DOE. The examination of DOE National Laboratories for compliance with laws and regulations is DOE's responsibility. This responsibility was further clarified by a memorandum of the GAO's Assistant General Counsel, dated March 6, 1995, where he opined that "...DOE's inability to assure that its contractors' costs [National Laboratories] are legal and proper...does not compel a conclusion that NRC has failed to comply with laws and regulations." DOE also has the cognizant responsibility to assure audit resolution and should provide the results of its audits to NRC.

The objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions of laws and regulations and, accordingly, we do not express such an opinion.

Our report contains three noncompliances. There is one noncompliance with OMB Circular A-25, relating to the development of Part 170 hourly rates, which was initially reported in 1998. The other two items are substantial noncompliances with the Improvement Act. The Fee Billing System condition reported in FY 2004 continues to exist. In the current year there is an information system security substantial noncompliance related to the Department of Interior's cross-servicing of the agency's general ledger and payroll service applications. The following discussion addresses the noncompliances.

Part 170 Hourly Rates

As previously reported from FYs 1998 through 2004, the Omnibus Budget Reconciliation Act of 1990 (OBRA-90) requires the NRC to recover approximately 100 percent of its budget authority by assessing fees. (In recent years, the recovery percentage has been reduced by 2 percent each year. During FY 2005, the recovery percentage was 90 percent.) Accordingly, NRC assesses two types of fees to its licensees and applicants. One type, specified in 10 CFR Part 171, consists of annual fees assessed to power reactors, materials and other licensees. The other type, specified in 10 CFR Part 170, and authorized by the Independent Offices Appropriation Act of 1952, is assessed for specific licensing actions, inspections, and other services provided to NRC's licensees and applicants.

Each year, the OCFO computes the hourly rates used to charge for Part 170 services. Consistent with OBRA-90, the rates are based on budgetary data and are used to price individually identifiable Part 170 services. NRC developed the FY 1998 and subsequent years' rates using the budgetary basis without validating the fee amounts to the full cost of providing Part 170 services.

During FYs 2004 and 2005, the agency continued to make progress and is presently refining a strategy to address this noncompliance. At year-end the CFO initiated a dialogue with us on their strategy. Initially the agency was pursuing the development of a validation model to compare budget versus cost-based fee calculations. More recently, the agency has devised a proposed cost-based calculation strategy to develop rates in compliance with OMB Circular A-25, *User Charges*. Once the OCFO completes the implementation of this proposed calculation strategy, we will review the resulting calculations or model and the underlying documented assumptions and data sources used in order to verify the reliability and completeness of the results. The audit assessment will also evaluate the adequacy of fee rule changes, if any. We commend the CFO for their continuing efforts to close this comment.

Recommendation

11. The CFO should continue to pursue the proposed calculation strategy and develop rates in compliance with OMB Circular A-25. OCFO management should inform the Office of Inspector General of the progress and actions taken to correct this condition.

Fee Billing System

In our *Report on the Effectiveness of Internal Control Over Financial Reporting*, we identified Fee Billing System as both a material weakness and an Improvement Act substantial noncompliance. Refer to that report for a detailed discussion of the condition.

Information System-wide Security Controls

In our *Report on the Effectiveness of Internal Control Over Financial Reporting*, we identified the information system-wide security controls as an Improvement Act substantial noncompliance. Refer to that report for a detailed discussion of the condition.

Status of Prior Year Comments

In the prior year, we included a condition related to Fee Recovery From Licensees in our report. Corrective actions were implemented during the year to close this condition. However, the condition related to Part 170 fees and the Improvement Act substantial noncompliance of the Fee Billing System continued in the current fiscal year.

Internal Control Related to Performance Measures

With respect to internal controls related to performance measures described in Chapter 2 of the *FY 2005 Performance and Accountability Report*, the OIG performed those procedures and will address this issue separately. Our procedures were not designed to provide assurance over reported performance measures and, accordingly, we do not provide an opinion on such information.

Consistency of Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements of NRC taken as a whole. The required supplementary information referred to in the *Management Discussion and Analysis*, Chapter 1 of this *Performance and Accountability Report*, is not a required part of the financial statements but is supplementary information required by OMB Circular A-136. We have applied certain limited procedures which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

The other accompanying information included in Chapter 2 and the appendices to the *Performance and Accountability Report* are required by OMB Circular A-136 and are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements of NRC taken as a whole. The required supplementary information, Schedule of Intragovernmental Assets and Liabilities, and the Schedule of Budgetary Resources, included on pages 150 through 151 of this *Performance and Accountability Report*, is not a required part of the financial statements but is supplementary information required by OMB Circular A-136. This information is also presented for purposes of additional analysis of the financial statements rather than to present the budgetary resources of NRC programs. This information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

This report is intended solely for the information and use of NRC management, the Inspector General, OMB, GAO, and the Congress and is not intended to be and should not be used by anyone other than these specified parties.

November 4, 2005

R. Navano & Associates, Inc.


MANAGEMENT'S RESPONSE TO AUDITORS' REPORTS



UNITED STATES
NUCLEAR REGULATORY COMMISSION
WASHINGTON, D.C. 20555-001

November 9, 2005

MEMORANDUM TO: Stephen D. Dingbaum
Assistant Inspector General for Audits

FROM: Jesse L. Funches
Chief Financial Officer 

SUBJECT: AUDIT OF THE FY 2005 FINANCIAL STATEMENTS

I have reviewed the audit report of the agency's FY 2005 financial statements.
Our responses to the recommendations follow.

Recommendation 1

The CFO should direct an assessment of all aspects of the Fee Billing System to ensure that the remediation plan is updated as necessary and implemented in a timely manner to enhance the controls over fee billing processes.

Response

Agree. By March 2006, the OCFO will assess the operating aspects of the Fee Billing System that are essential to the internal control over fee billings, including the processes related to data obtained from feeder systems, to identify cost-effective controls that will strengthen the completeness and reliability of the fee billing processes. The remediation plan will be updated as necessary based on the results of the assessment.

Recommendation 2

The CFO should define, design, and implement compensating controls over the Fee Billing System, while the system is being considered for redesign.

Response

Agree. By July 2006, the OCFO will use the results of the assessment performed in the response to Recommendation 1, and the experience gained implementing improved controls and quality assurance procedures, to establish additional cost-effective compensating controls in the existing fee billing processes.

Recommendation 3

As the OCFO identifies needed improvement of internal controls outside OCFO's business domain, there should be coordination and collaboration with the Executive Director for Operations as to how, when and to what extent the internal controls should be strengthened in operational program feeder systems, relied upon by OCFO for billing preparation purposes.

Response

Agree.

Recommendation 4

The CFO should continue to promote strengthening internal use software practices, in order to encourage project managers to comply with procedures in effect governing the completeness of new and existing development initiatives.

Response

Agree. The OIG has acknowledged that a significant amount of work has been done by the OCFO over the years to promote and strengthen internal use software practices. However, the OCFO will seek to identify further measures that can be taken and will develop a plan of additional actions by January 2006.

Recommendation 5

The CFO should coordinate with the Office of Information Services and the Executive Director for Operations to keep abreast of progress in implementing the recommendations made in the OIG's report. This awareness will enable the CFO to better plan his information system security needs.

Response

Agree.

Recommendation 6

The CFO should establish procedures to monitor and participate in customer advisory work groups on information security issues with the service bureau. At a minimum, the CFO should devise a communication process to stay informed about information security testing and the related results.

Response

Agree. As a followup to his verbal communications with the service bureau, I will write to the Director and CFO of the Department of Interior National Business Center (DOI-NBC) to document concerns about the security of DOI-NBC's network and mainframe, and to establish an agreement to be informed timely of information security issues and documented completion of corrective actions. The letter will be sent by December 2005.

Recommendation 7

The CFO should direct an assessment of financial controls over disbursement activities. At a minimum, the assessment should provide for the development and implementation of second party reviews of the propriety and accuracy of edits to vendor tables.

Response

Agree. The OCFO will perform an assessment of the financial controls over disbursement activities and make necessary revisions to our existing procedures. This will be completed by June 30, 2006. Additionally, by December 15, 2005, secondary reviews of revisions to the vendor tables in the core financial system will be implemented.

Recommendation 8

The CFO should periodically assess whether, CCR data can be used to provide an electronic validation of EFT information against NRC's payment system prior to certifying the payment.

Response

Agree. The CCR data will be made available in the NRC's core financial system by the end of February 2006, for validation of payments. OCFO will semiannually assess whether CCR data can be used to provide an electronic validation of EFT information for payments. We will perform the next assessment by March 30, 2006.

Recommendation 9

The CFO should establish a secondary review of high value payments. The secondary review should be performed by parties that are not involved directly in payment processing.

Response

Agree. By December 15, 2005, the OCFO will implement secondary reviews of high value payments. These reviews will be performed by staff not involved directly in payment processing.

Recommendation 10

The CFO should reiterate to all agency managers the importance of having full and open discussion about internal control impacting the reliability and completeness of the agency's financial statements. This discussion could be incorporated during the upcoming implementation of OMB Circular A-123.

Response

Agree. I am committed to ensuring that integrity and ethical values are not compromised and will continue to emphasize the importance of having full and open discussion relating to internal controls impacting the reliability and completeness of NRC's financial statements. By December 15, 2005, I will issue a memorandum to all agency managers emphasizing the importance of a full and open discussion relating to internal controls impacting the reliability and completeness of NRC's financial statements.

Recommendation 11

The CFO should continue to pursue the proposed calculation strategy and develop rates in compliance with OMB Circular A-25. OCFO management should inform the Office of Inspector General of the progress and actions taken to correct this condition.

Response

Agree. We will continue with plans to calculate 10 CFR Part 170 hourly rates using actual cost data from the Cost Accounting System. We may use these rates to recover the costs of activities under 10 CFR Part 170 beginning with the FY 2006 fee rule. We will continue to keep the Office of the Inspector General informed of progress and actions.

PRINCIPAL STATEMENTS

BALANCE SHEET

(Dollars in Thousands)

| As of September 30, | 2005 | 2004 |
|---|-------------------|-------------------|
| Assets | | |
| Intragovernmental | | |
| Fund balances with Treasury (Note 2) | \$ 220,695 | \$ 200,277 |
| Accounts receivable (Note 3) | 3,227 | 3,357 |
| Other | 1,961 | 2,295 |
| <i>Total intragovernmental</i> | 225,883 | 205,929 |
| Accounts receivable, net (Note 3) | 60,757 | 50,648 |
| Property and equipment, net (Note 4) | 26,983 | 26,800 |
| Other | 66 | 29 |
| Total Assets | \$ 313,689 | \$ 283,406 |
| Liabilities | | |
| Intragovernmental | | |
| Accounts payable | \$ 7,730 | \$ 8,564 |
| Other (Note 5) | 69,495 | 61,568 |
| <i>Total intragovernmental</i> | 77,225 | 70,132 |
| Accounts payable | 21,296 | 19,367 |
| Federal employees' benefits (Note 6) | 8,417 | 8,114 |
| Other liabilities (Note 5) | 49,268 | 48,317 |
| Total Liabilities | 156,206 | 145,930 |
| Net Position | | |
| Unexpended appropriations | 170,836 | 149,901 |
| Cumulative results of operations (Note 8) | (13,353) | (12,425) |
| Total Net Position | 157,483 | 137,476 |
| Total Liabilities and Net Position | \$ 313,689 | \$ 283,406 |

The accompanying notes to the principal statements are an integral part of this statement.

STATEMENT OF NET COST*(Dollars in Thousands)*

For the years ended September 30, (Note 9)

2005

2004

Nuclear Reactor Safety

| | | |
|---|------------|-----------------|
| Gross costs | \$ 476,481 | \$ 466,440 |
| Less: Earned revenue | (476,020) | (478,488) |
| Total Net Cost of Nuclear Reactor Safety | 461 | (12,048) |

Nuclear Materials and Waste Safety

| | | |
|---|----------------|----------------|
| Gross costs | 206,518 | 196,078 |
| Less: Earned revenue | (73,972) | (73,679) |
| Total Net Cost of Nuclear Materials and Waste Safety | 132,546 | 122,399 |

Net Cost of Operations**\$ 133,007** **\$ 110,351**

The accompanying notes to the principal statements are an integral part of this statement.

CHAPTER 3
AUDITORS' REPORTS AND FINANCIAL STATEMENTS

STATEMENT OF CHANGES IN NET POSITION
(Dollars in Thousands)

| For the years ended September 30, | 2005 | | 2004 | |
|---|--|------------------------------|--|------------------------------|
| | Cumulative Results of Operations | Unexpended Appropriations | Cumulative Results of Operations | Unexpended Appropriations |
| Beginning Balances | \$ (12,425) | \$ 149,901 | \$ (8,089) | \$ 149,719 |
| Budgetary Financing Sources | | | | |
| Appropriations received | - | 601,245 | - | 593,000 |
| Appropriations transferred-in/out | - | (463,729) | - | (510,439) |
| Other adjustments | - | (481) | - | (280) |
| Appropriations used | 116,100 | (116,100) | 82,099 | (82,099) |
| Non-exchange revenue | 7,344 | - | 725 | - |
| Transfers-in/out without reimbursement | (7,344) | - | (725) | - |
| Other Financing Sources | | | | |
| Imputed financing from costs absorbed by others | 25,904 | - | 25,129 | - |
| Other | (9,925) | - | (1,213) | - |
| Total Financing Sources | 132,079 | 20,935 | 106,015 | 182 |
| Net Cost of Operations | (133,007) | - | (110,351) | - |
| Ending Balances | \$ (13,353) | \$ 170,836 | \$ (12,425) | \$ 149,901 |

The accompanying notes to the principal statements are an integral part of this statement.

STATEMENT OF BUDGETARY RESOURCES

(Dollars in Thousands)

| For the years ended September 30, | 2005 | 2004 |
|---|-------------------|-------------------|
| <i>Budgetary Resources</i> | | |
| Budget authority | | |
| Appropriations received | \$ 601,245 | \$ 593,000 |
| Net transfers | 68,498 | 32,905 |
| Unobligated balances | | |
| Beginning of period | 36,328 | 40,572 |
| Spending authority from offsetting collections | | |
| Reimbursements earned | 5,836 | 5,491 |
| Change in unfilled customer orders | 431 | 1,298 |
| <i>Total Spending Authority from Offsetting Collections</i> | 6,267 | 6,789 |
| Recoveries of prior-year obligations | 11,019 | 8,618 |
| Permanently not available | (481) | (280) |
| <i>Total Budgetary Resources</i> | \$ 722,876 | \$ 681,604 |
| <i>Status of Budgetary Resources</i> | | |
| Obligations incurred (Note 13) | | |
| Direct | \$ 659,530 | \$ 639,322 |
| Reimbursable | 6,002 | 5,953 |
| Unobligated balance | | |
| Apportioned | 33,620 | 35,282 |
| Exempt from apportionment | 23,724 | 1,047 |
| <i>Total Status of Budgetary Resources</i> | \$ 722,876 | \$ 681,604 |
| <i>Relationship of Obligations to Outlays</i> | | |
| Obligated balance, net, beginning of period | \$ 157,218 | \$ 143,934 |
| Obligated balance, net, end of period | | |
| Accounts receivable | (322) | (275) |
| Unfilled customer orders from Federal sources | (3,885) | (3,882) |
| Undelivered orders | 118,580 | 117,150 |
| Accounts payable | 45,919 | 44,225 |
| <i>Obligated balance, net, end of period</i> | \$ 160,292 | \$ 157,218 |
| Outlays | | |
| Disbursements | \$ 651,389 | \$ 623,131 |
| Collections | (6,216) | (6,546) |
| <i>Subtotal</i> | 645,173 | 616,585 |
| Less: Offsetting Receipts | (534,119) | (545,302) |
| <i>Net Outlays</i> | \$ 111,054 | \$ 71,283 |

The accompanying notes to the principal statements are an integral part of this statement.

CHAPTER 3
AUDITORS' REPORTS AND FINANCIAL STATEMENTS

STATEMENT OF FINANCING

(Dollars in Thousands)

| For the years ended September 30, | 2005 | 2004 |
|---|-------------------|------------|
| Resources Used to Finance Activities | | |
| Budgetary Resources Obligated | | |
| Obligations incurred (Note 13) | \$ 665,532 | \$ 645,275 |
| Less: Spending authority from offsetting collections and recoveries | (17,286) | (15,407) |
| <i>Obligations Net of Offsetting Collections and Recoveries</i> | 648,246 | 629,868 |
| Less: Offsetting receipts | (534,119) | (545,302) |
| <i>Net Obligations</i> | 114,127 | 84,566 |
| Other Resources | | |
| Imputed financing from costs absorbed by others | 25,904 | 25,129 |
| Allocation transfer | 2,124 | 3,206 |
| Other | (9,925) | (1,213) |
| <i>Net Other Resources Used to Finance Activities</i> | 18,103 | 27,122 |
| Total Resources Used to Finance Activities | 132,230 | 111,688 |
| Resources Used to Finance Items not Part of the Net Cost of Operations | | |
| Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | (151) | (5,074) |
| Resources that finance the acquisition of assets | (7,393) | (5,796) |
| Other | (46) | (217) |
| <i>Total Resources Used to Finance Items not Part of the Net Cost of Operations</i> | (7,590) | (11,087) |
| Total Resources Used to Finance the Net Cost of Operations | 124,640 | 100,601 |
| Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period | | |
| Components Requiring or Generating Resources in the Future Periods | | |
| Increase in annual leave liability | 755 | 2,170 |
| Increase (Decrease) Actuarial Workers' Compensation | 303 | (959) |
| Increase (Decrease) in Unfunded Workers' Compensation | 228 | 10 |
| Increase in Unfunded Unemployment | (12) | (5) |
| <i>Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods</i> | 1,274 | 1,216 |
| Components not Requiring or Generating Resources: | | |
| Depreciation and amortization | 7,093 | 8,534 |
| <i>Total Components not Requiring or Generating Resources</i> | 7,093 | 8,534 |
| Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period | 8,367 | 9,750 |
| Net Costs of Operations | \$ 133,007 | \$ 110,351 |

The accompanying notes to the principal statements are an integral part of this statement.

NOTES TO PRINCIPAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. *Reporting Entity*

The NRC is an independent regulatory agency of the Federal Government that was created by the U.S. Congress to regulate the Nation's civilian use of byproduct, source, and special nuclear materials to ensure adequate protection of the public health and safety, to promote the common defense and security, and to protect the environment. Its purposes are defined by the Energy Reorganization Act of 1974, as amended, along with the Atomic Energy Act of 1954, as amended, which provide the foundation for regulating the Nation's civilian use of nuclear materials.

The NRC operates through the execution of its congressionally approved appropriations for salaries and expenses and the Inspector General, including funds derived from the Nuclear Waste Fund. In addition, transfer appropriations are provided by the U.S. Agency for International Development for the development of nuclear safety and regulatory authorities in Russia, Ukraine, Kazakhstan, and Armenia for the independent oversight of nuclear reactors in these countries.

B. *Basis of Presentation*

These principal statements were prepared to report the financial position and results of operations of the NRC as required by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. These financial statements were prepared from the books and records of the NRC in conformity with accounting principles generally accepted in the United States of America, the requirements of OMB Circular A-136, *Financial Reporting Requirements*, and NRC accounting policies. These statements are, therefore, different from the financial reports, also prepared by the NRC pursuant to OMB directives, which are used to monitor and control NRC's use of budgetary resources.

NRC has not presented a Statement of Custodial Activity because the amounts involved are immaterial and incidental to its operations and mission.

NRC reclassified the FY 2004 Statement of Net Cost to reflect a change from four strategic arenas to two programs. The two programs are Nuclear Reactor Safety and the Nuclear Materials and Waste Safety. The Nuclear Reactor Safety program is the combination of the FY 2004 Nuclear Reactor Safety and the International Nuclear Safety Support. The Nuclear Materials and Waste Safety program is the combination of FY 2004 Nuclear Materials Safety and Nuclear Waste Safety.

The programs as presented on the Statement of Net Cost are based on the strategic plans and are described as follows:

Nuclear Reactor Safety encompasses all NRC efforts to ensure that civilian nuclear power reactor facilities and research and test reactors are licensed and operated in a manner that adequately protects the public health and safety, and the environment and protects against radiological sabotage and theft or diversion of special nuclear materials. The Nuclear Reactor Safety program contains two activities—Nuclear Reactor Licensing and Nuclear Reactor Inspection.

Nuclear Materials and Waste Safety encompasses all NRC efforts to protect the public health and safety and the environment and ensures the secure use and management of radioactive materials. The Nuclear Materials and Waste Safety program contains five activities—Fuel Facilities Licensing and Inspection, Nuclear Materials Users Licensing and Inspection, High-Level Waste Repository, Decommissioning and Low-Level Waste, and Spent Fuel Storage and Transportation Licensing and Inspection.

C. Budgets and Budgetary Accounting

Budgetary accounting measures appropriation and consumption of budget/spending authority or other budgetary resources and facilitates compliance with legal constraints and controls over the use of Federal funds. Under budgetary reporting principles, budgetary resources are consumed at the time of purchase. Assets and liabilities, which do not consume current budgetary resources, are not reported, and only those liabilities for which valid obligations have been established are considered to consume budgetary resources.

For the past 31 years, Congress has enacted no-year appropriations, which are available for obligation by NRC until expended. The Energy and Water Development Appropriations Act, 2005, requires the NRC to recover approximately 90 percent of its new budget authority of \$669.3 million

by assessing fees less amounts derived from the Nuclear Waste Fund of \$68.5 million. The \$669.3 million includes rescissions of \$481 thousand to NRC's appropriation from P.L. 108-447 and \$552 thousand to the Nuclear Waste Fund appropriation. The \$669.3 million does not include any amounts transferred from the U.S. Agency for International Development.

For FY 2004, NRC recovered approximately 92 percent of its new budget authority of \$625.6 million less amounts derived from the Nuclear Waste Funds of \$32.9 million.

D. Basis of Accounting

Transactions are recorded on an accrual accounting basis. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Interest on borrowings of the U.S. Treasury is not included as a cost to NRC's programs and is not included in the accompanying financial statements.

E. Revenues and Other Financing Sources

The NRC is required to offset its appropriations by the amount of revenues received during the fiscal year by assessing fees. The NRC assesses two types of fees to recover its budget authority: (1) fees assessed under 10 CFR Part 170 for licensing, inspection, and other services under the authority of the Independent Offices Appropriation Act of 1952 to recover the NRC's costs of providing individually identifiable services to specific applicants and licensees; and (2) annual fees assessed for nuclear facilities and materials licensees under 10 CFR Part 171. All fees, with the exception of civil penalties, are exchange revenues in accordance with Statement of Federal Financial Accounting Standards No. 7, Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting.

For accounting purposes, appropriations are recognized as financing sources (appropriations used) at the time expenses are accrued. At the end of the fiscal year, appropriations recognized are reduced by the amount of assessed fees collected during the fiscal year to the extent of new budget authority for the year. Collections which exceed the new budget authority are held to offset subsequent years' appropriations. Appropriations expended for property and equipment are recognized as expenses when the asset is consumed in operations (depreciation and amortization).

F. Fund Balances with Treasury

The NRC's cash receipts and disbursements are processed by the U.S. Treasury. The fund balances with the U.S. Treasury are primarily appropriated funds that are available to pay current liabilities and to finance authorized purchase commitments. Funds with Treasury represent NRC's right to draw on the U.S. Treasury for allowable expenditures. All amounts are available to NRC for current use.

G. Accounts Receivable

Accounts receivable consist of amounts owed to the NRC by other Federal agencies and the public. Amounts due from the public are presented net of an allowance for uncollectible accounts. The allowance is based on an analysis of the outstanding balances. Receivables from Federal agencies are expected to be collected; therefore, there is no allowance for uncollectible accounts.

H. Non-Entity Assets

Accounts receivable include nonentity assets of \$5 thousand and \$7 thousand at September 30, 2005, and 2004, respectively, and consist of miscellaneous penalties and interest due from the public, which, when collected, must be transferred to the U.S. Treasury.

I. Property and Equipment

Property and equipment consist primarily of typical office furnishings, nuclear reactor simulators, and computer hardware and software. The costs of internal use software include the full cost of salaries and benefits from agency personnel involved in software development. The agency has no real property. The land and buildings in which NRC operates are provided by the General Services Administration (GSA), which charges NRC rent that approximates the commercial rental rates for similar properties.

Property with a cost of \$50 thousand or more per unit and a useful life of 2 years or more is capitalized at cost and depreciated using the straight-line method over the useful life. Other property items are expensed when purchased. Normal repairs and maintenance are charged to expense as incurred.

J. *Accounts Payable*

Accounts payable represent vendor invoices for services received by NRC that will be paid at a later date.

K. *Liabilities Not Covered by Budgetary Resources*

Liabilities represent the amount of monies or other resources that are likely to be paid by NRC as the result of a transaction or event that has already occurred. No liability can be paid by NRC absent an appropriation. Liabilities for which an appropriation has not been enacted and for which there is no certainty that an appropriation will be enacted are classified as Liabilities Not Covered by Budgetary Resources. Also, NRC liabilities arising from sources other than contracts can be abrogated by the Government acting in its sovereign capacity.

Intragovernmental

The U.S. Department of Labor (DOL) paid Federal Employees Compensation Act (FECA) benefits on behalf of NRC which had not been billed or paid by NRC as of September 30, 2005, and 2004, respectively.

Federal Employee Benefits

Federal employee benefits represent the actuarial liability for estimated future FECA disability benefits. The future workers' compensation estimate was generated by DOL from an application of actuarial procedures developed to estimate the liability for FECA, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability was calculated using historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. These projected annual benefit payments were discounted to present value. The interest rate assumptions utilized for discounting benefits were 4.53 percent for FY 2005 and 4.88 percent for FY 2004.

Other

Accrued annual leave represents the amount of annual leave earned by NRC employees but not yet taken.

L. Contingencies

Contingent liabilities are those where the existence or amount of the liability cannot be determined with certainty pending the outcome of future events. The NRC is a party to various administrative proceedings, legal actions, environmental suits, and claims brought by or against it. The NRC is a party to a case where an adverse outcome is reasonably possible and may exceed \$1.3 million. Based on the advice of legal counsel concerning contingencies, it is the opinion of management that the ultimate resolution of these proceedings, actions, suits, and claims will not materially affect the agency's financial statements.

M. Annual, Sick, and Other Leave

Annual leave is accrued as it is earned and the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave liability account is adjusted to reflect current pay rates. To the extent that current or prior year funding is not available to cover annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of nonvested leave are expensed as taken.

N. Retirement Plans

NRC employees belong to either the Federal Employees Retirement System (FERS) or the Civil Service Retirement System (CSRS). For FY 2005 and FY 2004, employees belonging to FERS, the NRC withheld 0.8 percent of base pay earnings, in addition to Federal Insurance Contribution Act (FICA) withholdings, and matched the withholdings with an 11.2 percent contribution in FY 2005 and a 10.7 percent contribution in FY 2004. The sum is transferred to the Federal Employees Retirement Fund. For employees covered by CSRS, NRC withholds 7 percent of base pay earnings. The NRC matched this withholding with a 7 percent contribution in FY 2005 and FY 2004.

The Thrift Savings Plan (TSP) is a retirement savings and investment plan for employees belonging to either FERS or CSRS. For employees belonging to FERS, NRC automatically contributes 1 percent of base pay to their account and matches contributions up to an additional 4 percent. The maximum percentage of base pay that an employee participating in FERS may contribute is 15 percent in calendar year 2005, and 14 percent in 2004. Employees belonging to CSRS may contribute up to 10 percent of their salary in calendar year 2005, and 9 percent in 2004, but there is no NRC matching of the contribution. The maximum amount

that either FERS or CSRS employees may contribute to the plan is \$14 thousand in 2005 and \$13 thousand in 2004. The sum of the employees' and NRC's contributions are transferred to the Federal Retirement Thrift Investment Board.

The NRC does not report on its financial statements FERS and CSRS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to its employees. Reporting such amounts is the responsibility of the U.S. Office of Personnel Management. The portion of the current and estimated future outlays for CSRS not paid by NRC is, in accordance with Statement of Federal Financial Accounting Standards No. 5, Accounting for Liabilities of the Federal Government, included in NRC's financial statements as an imputed financing source.

O. Leases

The total capital lease liability is funded on an annual basis and included in NRC's annual budget. The NRC's capital leases are for personal property consisting of reproduction equipment which is installed at NRC headquarters. For FY 2005 and FY 2004, there were two capital leases with terms of 5 years each and the interest rate was 4.38 percent for both leases. During FY 2004, a capital lease for a term of 3 years at an interest rate of 6.59 percent was completed. The reproduction equipment is depreciated over 5 years using the straight-line method with no salvage value.

Operating leases consist of real property leases with GSA. The leases are for NRC's headquarters and regional offices. The GSA charges NRC lease rates which approximate commercial rates for comparable space.

P. U.S. Department of Energy Charges

Financial transactions between the DOE and NRC are fully automated through the U.S. Treasury's Intragovernmental Payment and Collection (IPAC) System. The IPAC System allows DOE to collect amounts due from NRC directly from NRC's account at the U.S. Treasury for goods and/or services rendered. Project manager verification of goods and/or services received is subsequently accomplished through a system-generated voucher approval process. The vouchers are returned to the Office of the Chief Financial Officer documenting that the charges have been accepted.

Q. *Pricing Policy*

The NRC provides goods and services to the public and other Government entities. In accordance with OMB Circular No. A-25, User Charges, and the Independent Offices Appropriation Act of 1952, NRC assesses fees under 10 CFR Part 170 for licensing and inspection activities to recover the full cost of providing individually identifiable services.

The NRC's policy is to recover the full cost of goods and services provided to other Government entities where (1) the services performed are not part of its statutory mission and (2) NRC has not received appropriations for those services. Fees for reimbursable work are assessed at the 10 CFR Part 170 rate with minor exceptions for programs that are nominal activities of the NRC.

R. *Net Position*

The NRC's net position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent appropriated spending authority that is unobligated and has not been withdrawn by the U.S. Treasury, and obligations that have not been paid. Cumulative results of operations represent the excess of financing sources over expenses since inception.

S. *Use of Management Estimates*

The preparation of the accompanying financial statements in accordance with generally accepted accounting principles requires management to make certain estimates and assumptions that directly affect the results of reported assets, liabilities, revenues, and expenses. Actual results could differ from these estimates.

NOTE 2. FUND BALANCES WITH TREASURY

| (In thousands) | <u>2005</u> | <u>2004</u> |
|----------------------|-------------------|-------------------|
| Fund Balances | | |
| Appropriated funds | \$ 217,637 | \$ 193,547 |
| Allocation transfers | 3,047 | 3,839 |
| Other fund types | <u>11</u> | <u>2,891</u> |
| Total | <u>\$ 220,695</u> | <u>\$ 200,277</u> |

Status of Fund Balance with Treasury

| | | |
|-------------------------------------|-------------------|-------------------|
| Unobligated Balance | | |
| Available | | |
| Appropriated funds | \$ 57,344 | \$ 36,329 |
| Allocation transfers | 1,638 | 1,857 |
| Unavailable | <u>155</u> | <u>3,046</u> |
| Obligated balance not yet disbursed | <u>161,558</u> | <u>159,045</u> |
| Total | <u>\$ 220,695</u> | <u>\$ 200,277</u> |

The Fund Balance with Treasury consists of Unobligated and Obligated Balances budgetary accounts. It includes Nuclear Waste Fund activity. The Nuclear Waste Fund Unobligated balance is \$23.7 million as of September 30, 2005, and \$1.0 million as of September 30, 2004.

NOTE 3. ACCOUNTS RECEIVABLE

| | | |
|--|------------------|------------------|
| (In thousands) | <u>2005</u> | <u>2004</u> |
| Intragovernmental | | |
| Receivables and reimbursements | <u>\$ 3,227</u> | <u>\$ 3,357</u> |
| Receivables with the Public | | |
| Materials and facilities fees - billed | \$ 2,124 | \$ 3,060 |
| Materials and facilities fees - unbilled | 61,482 | 49,684 |
| Other | <u>38</u> | <u>37</u> |
| Total Accounts Receivable | <u>63,644</u> | 52,781 |
| Less: Allowance for uncollectible accounts | <u>(2,887)</u> | <u>(2,133)</u> |
| Accounts Receivable, Net | <u>\$ 60,757</u> | <u>\$ 50,648</u> |

NOTE 4. PROPERTY AND EQUIPMENT, NET

| | | | | | |
|------------------------------------|--------------------------|------------------------------|--|------------------------------------|------------------------------------|
| (In thousands) | | | | | |
| | | | Accumulated Depreciation and Amortization | 2005 Net Book Value | 2004 Net Book Value |
| Fixed Assets Class | Service Years | Acquisition Value | | | |
| Equipment | 5-8 | \$ 15,297 | \$ (13,931) | \$ 1,366 | \$ 1,824 |
| IT software | 5 | 41,238 | (35,420) | 5,818 | 10,288 |
| IT software under development | - | 8,303 | - | 8,303 | 4,014 |
| Leasehold improvements | 20 | 21,857 | (12,439) | 9,418 | 10,617 |
| Leasehold improvements in progress | - | 2,078 | - | 2,078 | 57 |
| | | <u>\$ 88,773</u> | <u>\$ (61,790)</u> | <u>\$ 26,983</u> | <u>\$ 26,800</u> |

NOTE 5. OTHER LIABILITIES

| (In thousands) | <u>2005</u> | <u>2004</u> |
|---|------------------|------------------|
| Intragovernmental | | |
| Liability to offset net accounts receivable for fees assessed | \$ 63,627 | \$ 53,704 |
| Liability from fees collected which will offset current year's appropriations | 6 | 2,857 |
| Liability to offset miscellaneous accounts receivable | 3 | 7 |
| Liability for advances from other agencies | 2,090 | 1,778 |
| Accrued workers' compensation | 1,883 | 1,655 |
| Accrued unemployment compensation | 12 | 24 |
| Employee benefit contributions | <u>1,874</u> | <u>1,543</u> |
| Total Intragovernmental Other Liabilities | <u>\$ 69,495</u> | <u>\$ 61,568</u> |

The liability to offset the net accounts receivable for fees assessed represents amounts which, when collected, will be transferred to the U.S. Treasury to offset NRC's appropriations in the year collected.

| (In thousands) | <u>2005</u> | <u>2004</u> |
|---|------------------|------------------|
| Accrued annual leave | \$ 32,960 | \$ 32,205 |
| Accrued salaries | 12,986 | 13,001 |
| Contract holdbacks, advances, and other | <u>3,322</u> | <u>3,111</u> |
| Total Other Liabilities | <u>\$ 49,268</u> | <u>\$ 48,317</u> |

Other liabilities, except accrued annual leave, contract holdbacks, and advances from others, are current.

NOTE 6. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

| | | |
|--|------------------|------------------|
| (In thousands) | <u>2005</u> | <u>2004</u> |
| Intragovernmental | | |
| FECA paid by DOL | \$ 1,883 | \$ 1,655 |
| Accrued unemployment compensation | 12 | 24 |
| Federal Employee Benefits | | |
| Future FECA | 8,417 | 8,114 |
| Other | | |
| Accrued annual leave | <u>32,960</u> | <u>32,205</u> |
| Total Liabilities not Covered by Budgetary Resources | <u>\$ 43,272</u> | <u>\$ 41,998</u> |

Balance Sheet amounts represent ending balances of worker's compensation and annual leave. The Statement of Financing amount represents the change in activity in worker's compensation and annual leave balance.

NOTE 7. LEASES

| | | | | |
|-----------------------------|---------------------|----------------|-------------------|-------------------|
| (In thousands) | | | <u>2005</u> | <u>2004</u> |
| Future Lease Payments Due: | | | | |
| | Fiscal Year | Capital | Operating | |
| | 2005 | \$ - | \$ - | \$ 22,980 |
| | 2006 | 164 | 22,538 | 22,218 |
| | 2007 | 128 | 22,627 | 22,271 |
| | 2008 | - | 21,496 | 21,013 |
| | 2009 | - | 19,347 | 18,864 |
| | 2010 and thereafter | - | 89,288 | 88,167 |
| | Total | <u>292</u> | <u>175,296</u> | <u>195,513</u> |
| Add: imputed interest | | 12 | - | 28 |
| Total Future Lease Payments | | <u>\$ 304</u> | <u>\$ 175,296</u> | <u>\$ 195,541</u> |

NOTE 8. CUMULATIVE RESULTS OF OPERATIONS

| (In thousands) | <u>2005</u> | <u>2004</u> |
|--|--------------------|--------------------|
| Future funding requirements | \$ (43,272) | \$ (41,998) |
| Investment in property and equipment, net | 26,983 | 26,800 |
| Contributions from foreign cooperative research agreements | 2,867 | 2,739 |
| Other | 69 | 34 |
| Cumulative Results of Operations | <u>\$ (13,353)</u> | <u>\$ (12,425)</u> |

Future funding requirements represent the amount of future funding needed to pay the accrued unfunded expenses as of September 30, 2005, and 2004. These accruals are not funded from current or prior-year appropriations and assessments, but rather should be funded from future appropriations and assessments. Accordingly, future funding requirements have been recognized for the expenses that will be paid from future appropriations.

NOTE 9. STATEMENT OF NET COST

(In thousands)

| For the years ended September 30, | <u>2005</u> | <u>2004</u> |
|---|-------------------|--------------------|
| <i>Nuclear Reactor Safety</i> | | |
| Intragovernmental gross costs | \$ 143,035 | \$ 145,494 |
| Less: Intragovernmental earned revenue | (29,299) | (28,829) |
| <i>Intragovernmental net costs</i> | <u>113,736</u> | <u>116,665</u> |
| Gross costs with the public | 333,446 | 320,946 |
| Less: Earned revenue from the public | (446,721) | (449,659) |
| <i>Net costs with the public</i> | <u>(113,275)</u> | <u>(128,713)</u> |
| Total Net Cost of Nuclear Reactor Safety | \$ 461 | \$ (12,048) |
| <i>Nuclear Materials and Waste Safety</i> | | |
| Intragovernmental gross costs | \$ 48,551 | \$ 51,832 |
| Less: Intragovernmental earned revenue | (5,113) | (5,085) |
| <i>Intragovernmental net costs</i> | <u>43,438</u> | <u>46,747</u> |
| Gross costs with the public | 157,967 | 144,246 |
| Less: Earned revenue from the public | (68,859) | (68,594) |
| <i>Net costs with the public</i> | <u>89,108</u> | <u>75,652</u> |
| Total Net Cost of Nuclear Materials and Waste Safety | \$ 132,546 | \$ 122,399 |

For "Intragovernmental gross costs," the buyers and sellers are both Federal entities. For "Earned revenues from the public," the buyers of the goods or services are non-Federal entities.

NOTE 10. EXCHANGE REVENUES

| | | |
|--|-------------------|------------|
| (In thousands) | 2005 | 2004 |
| Fees for licensing, inspection, and other services | \$ 544,044 | \$ 546,515 |
| Revenue from reimbursable work | 5,948 | 5,652 |
| Total Exchange Revenues | \$ 549,992 | \$ 552,167 |

NOTE 11. BUDGET FUNCTIONAL CLASSIFICATION

| | | | |
|--|-------------------|-----------------------|-------------------|
| (In thousands) | 2005 | | 2004 |
| Functional Classification | Gross Cost | Earned Revenue | Net Cost |
| 276 - Energy Information, Policy, & Regulation | \$ 680,350 | \$ 549,992 | \$ 130,358 |
| 150 - AID International Affairs | 2,649 | - | 2,649 |
| Total | \$ 682,999 | \$ 549,992 | \$ 133,007 |

Intragovernmental

| | | | |
|--|-------------------|-----------------------|-------------------|
| | 2005 | | 2004 |
| Functional Classification | Gross Cost | Earned Revenue | Net Cost |
| 276 - Energy Information, Policy, & Regulation | \$ 188,937 | \$ 34,412 | \$ 154,525 |
| 150 - AID International Affairs | 2,649 | - | 2,649 |
| Total | \$ 191,586 | \$ 34,412 | \$ 157,174 |

NOTE 12. FINANCING SOURCES OTHER THAN EXCHANGE REVENUE

(In thousands)

Appropriated Funds Used

Collections were used to reduce the fiscal year's appropriations recognized:

| | <u>2005</u> | <u>2004</u> |
|-------------------------------------|-------------------|------------------|
| Funds consumed | \$ 650,219 | \$ 627,401 |
| Less: collection from fees assessed | <u>(534,119)</u> | <u>(545,302)</u> |
| Appropriated funds used | <u>\$ 116,100</u> | <u>\$ 82,099</u> |

Funds consumed include \$38.3 million and \$43.8 million through September 30, 2005, and 2004, respectively, of available funds from prior years.

Non-Exchange Revenue

| | <u>2005</u> | <u>2004</u> |
|----------------------------|-----------------|---------------|
| Civil penalties | \$ 5,807 | \$ 622 |
| Miscellaneous receipts | <u>1,537</u> | <u>103</u> |
| Total Non-Exchange Revenue | <u>\$ 7,344</u> | <u>\$ 725</u> |

Imputed Financing

| | <u>2005</u> | <u>2004</u> |
|---------------------------------------|------------------|------------------|
| Civil Service Retirement System | \$ 11,993 | \$ 13,073 |
| Federal Employee Health Benefit | <u>13,735</u> | <u>11,924</u> |
| Federal Employee Group Life Insurance | 62 | 57 |
| Judgements Awards | <u>114</u> | <u>75</u> |
| Total Imputed Financing | <u>\$ 25,904</u> | <u>\$ 25,129</u> |

Transfers In/Out

| | <u>2005</u> | <u>2004</u> |
|---------------------------------|-------------------|-------------------|
| Transfers out to Treasury | | |
| License fees | \$ 534,119 | \$ 545,302 |
| Non-exchange revenue | <u>7,344</u> | <u>725</u> |
| Total Transfers-Out to Treasury | <u>\$ 541,463</u> | <u>\$ 546,027</u> |

NOTE 13. TOTAL OBLIGATIONS INCURRED

(In thousands)

| | <u>2005</u> | <u>2004</u> |
|----------------------------|-------------------|-------------------|
| Direct Obligations | | |
| Category A | \$ 613,502 | \$ 606,764 |
| Exempt from Apportionment | 46,028 | 32,558 |
| Total Direct Obligations | 659,530 | 639,322 |
| Reimbursable Obligations | 6,002 | 5,953 |
| Total Obligations Incurred | <u>\$ 665,532</u> | <u>\$ 645,275</u> |

Obligations exempt from apportionment are the result of funds derived from the Nuclear Waste Fund. Category A Obligations consist of NRC appropriations only.

NOTE 14. NUCLEAR WASTE FUND

Included in NRC's budget for FY 2005 and 2004 are \$68.5 million and \$32.9 million, respectively, provided from the Nuclear Waste Fund. In accordance with Statement of Federal Financial Accounting Standards No. 27, Identifying and Reporting Earmarked Funds, NRC has determined that funding from the Nuclear Waste Fund does not fully meet the definition as an earmarked fund. However, in order to provide additional information to the users of these financial statements, enhanced disclosure of the fund is presented below.

The Nuclear Waste Fund was authorized by the Nuclear Waste Policy Act of 1982 (PL 97-425). The funding provided to NRC in FY 2005 and 2004 for the purpose of performing activities associated with the DOE's application for a high-level waste repository at Yucca Mountain, Nevada. These activities included assistance to DOE with the application, review of the application, the conduct of thorough safety and security evaluations, preparation of the safety evaluation report, initiation of the inspection program, ensuring that the regulation process was made available to stakeholders and the general public, and to provide legal advice and representation for staff reviews and Commission actions.

The Nuclear Waste Fund amounts received, expended, obligated, and unobligated balances as of September 30, 2005, and 2004, are shown in the following:

| (In thousands) | 2005 | 2004 |
|-------------------------|-------------|-------------|
| Appropriations Received | \$ 68,498 | \$ 32,905 |
| Expended Appropriations | 41,976 | 29,985 |
| Obligations Incurred | 46,028 | 32,558 |
| Unobligated Balances | 23,724 | 1,047 |

NOTE 15. RECLASSIFICATIONS

Costs incurred in FY 2004 for an IT software project under development have been reclassified in the FY 2004 amounts. Costs of \$117 thousand have increased the Property and Equipment, Net, in the Balance Sheet and reduced the gross costs in the Nuclear Reactor Safety program in the Statement of Net Cost. Thus FY 2005 Beginning Cumulative Results of Operations has been adjusted.

The four strategic arenas for the year ended September 30, 2004, were reclassified into the two programs used for the year ended September 30, 2005, presentation. The Net Cost of Operations below shows the reclassification of the 2004 strategic arenas into programs:

| Strategic Arenas | 2004 | Program Reclassification | |
|---------------------------------|-------------------|-----------------------------------|---|
| | | Nuclear Reactor Safety | Nuclear Materials and Waste Safety |
| Nuclear Reactor Safety | \$ (26,457) | \$ (26,457) | \$ - |
| Nuclear Materials Safety | 40,215 | - | 40,215 |
| Nuclear Waste Safety | 82,184 | - | 82,184 |
| International | 14,409 | 14,409 | - |
| Total Cost of Operations | \$ 110,351 | \$ (12,048) | \$ 122,399 |

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Intragovernmental Assets and Liabilities

| (Dollars in thousands) As of September 30, | 2005 | 2004 |
|---|------------|------------|
| Intragovernmental Assets | | |
| Fund Balance with Treasury | | |
| Department of the Treasury | \$ 220,695 | \$ 200,277 |
| Accounts Receivable | | |
| Tennessee Valley Authority | 2,778 | 2,952 |
| Department of Energy | 271 | 171 |
| Other Agencies | 178 | 234 |
| <i>Total Accounts Receivable</i> | \$ 3,227 | \$ 3,357 |
| Other Assets | | |
| General Services Administration | 254 | - |
| Department of Commerce | 472 | 778 |
| Department of Interior | 509 | 588 |
| Department of the Navy | 606 | 634 |
| Department of Labor | 42 | 42 |
| Department of Energy | 20 | - |
| Office of Personnel Management | 12 | - |
| Other Agencies | 46 | 253 |
| <i>Total Other Assets</i> | 1,961 | 2,295 |
| Total Intragovernmental Assets | \$ 225,883 | \$ 205,929 |
| Intragovernmental Liabilities | | |
| Accounts Payable | | |
| General Services Administration | \$ 950 | \$ 1,223 |
| Department of Energy | 5,667 | 6,330 |
| Office of Personnel Management | 180 | - |
| Other Agencies | 933 | 1,011 |
| <i>Total Accounts Payable</i> | 7,730 | 8,564 |
| Other Liabilities | | |
| Department of the Treasury - General Fund | 63,633 | 56,561 |
| Department of Labor | 1,895 | 1,679 |
| Office of Personnel Management | 1,874 | 1,543 |
| Other Agencies | 2,093 | 1,785 |
| <i>Total Other Liabilities</i> | 69,495 | 61,568 |
| Total Intragovernmental Liabilities | \$ 77,225 | \$ 70,132 |

Schedule of Budgetary Resources

(Dollars in thousands)

For the years ended September 30, 2005

| | X0200 | X0300 | Total |
|---|-------------------|-----------------|-------------------|
| Budgetary Resources | | | |
| Budget authority | | | |
| Appropriations received | \$ 593,727 | \$ 7,518 | \$ 601,245 |
| Net transfers | 68,498 | - | 68,498 |
| Unobligated balances | | | |
| Beginning of period | 35,032 | 1,296 | 36,328 |
| Spending authority from offsetting collections | | | |
| Reimbursements earned | 5,836 | - | 5,836 |
| Change in unfilled customer orders | 431 | - | 431 |
| <i>Total Spending Authority from Offsetting Collections</i> | 6,267 | - | 6,267 |
| Recoveries of prior year obligations | 10,799 | 220 | 11,019 |
| Permanently not available | (475) | (6) | (481) |
| Total Budgetary Resources | \$ 713,848 | \$ 9,028 | \$ 722,876 |

Status of Budgetary Resources:

| | | | |
|--|-------------------|-----------------|-------------------|
| Status of Budgetary Resources: | | | |
| Obligations incurred | | | |
| Direct | \$ 651,583 | \$ 7,947 | \$ 659,530 |
| Reimbursable | 6,002 | - | 6,002 |
| Unobligated balance | | | |
| Apportioned | 32,539 | 1,081 | 33,620 |
| Exempt from apportionment | 23,724 | - | 23,724 |
| Total Status of Budgetary Resources | \$ 713,848 | \$ 9,028 | \$ 722,876 |

Relationship of Obligations to Outlays:

| | | | |
|--|-------------------|-----------------|-------------------|
| Relationship of Obligations to Outlays: | | | |
| Obligated balance, net, beginning of period | \$ 155,918 | \$ 1,300 | \$ 157,218 |
| Obligated balance, net, end of period: | | | |
| Accounts receivable | (322) | - | (322) |
| Unfilled customer orders from Federal sources | (3,885) | - | (3,885) |
| Undelivered orders | 117,443 | 1,137 | 118,580 |
| Accounts payable | 45,580 | 339 | 45,919 |
| <i>Obligated balance, net, end of period</i> | <i>\$ 158,816</i> | <i>\$ 1,476</i> | <i>\$ 160,292</i> |
| Outlays: | | | |
| Disbursements | \$ 643,837 | \$ 7,552 | \$ 651,389 |
| Collections | (6,216) | - | (6,216) |
| <i>Subtotal</i> | <i>637,621</i> | <i>7,552</i> | <i>645,173</i> |
| Less: Offsetting receipts | (527,358) | (6,761) | (534,119) |
| Net Outlays | \$ 110,263 | \$ 791 | \$ 111,054 |