U.S. Department of Energy

Office of Inspector General

Office of Audits and Inspections

AUDIT REPORT

Federal Energy Regulatory Commission's Fiscal Year 2014 Financial Statement Audit

OAS-FS-15-05

December 2014

Department of Energy
Washington, DC 20585

December 17, 2014

MEMORANDUM FOR THE CHAIRMAN, FEDERAL ENERGY REGULATORY COMMISSION

FROM: Rickey R. Hass
Deputy Inspector General
for Audits and Inspections
Office of Inspector General

SUBJECT: INFORMATION: Audit Report on "Federal Energy Regulatory Commission's Fiscal Year 2014 Financial Statement Audit"

The attached report presents the results of the independent certified public accountants' audit of the Federal Energy Regulatory Commission's (Commission) balance sheets, as of September 30, 2014 and 2013, and the related statements of net cost, changes in net position, budgetary resources and custodial activity for the years then ended.

To fulfill the Office of Inspector General's audit responsibilities, we contracted with the independent public accounting firm of KPMG, LLP (KPMG) to conduct the audit, subject to our review. KPMG is responsible for expressing an opinion on the Commission's financial statements and reporting on applicable internal controls and compliance with laws and regulations. The Office of Inspector General monitored audit progress and reviewed the audit report and related documentation. This review disclosed no instances where KPMG did not comply, in all material respects, with generally accepted Government auditing standards. The Office of Inspector General did not express an independent opinion on the Commission's financial statements.

KPMG concluded that the financial statements present fairly, in all material respects, the financial position of the Commission as of September 30, 2014 and 2013, and its net costs, changes in net position, budgetary resources and custodial activities for the years then ended, in accordance with United States generally accepted accounting principles.

As part of this review, auditors also considered the Commission's internal controls over financial reporting and tested for compliance with certain provisions of laws, regulations, contracts and grant agreements that could have a direct and material effect on the determination of financial statement amounts. The audit identified one deficiency in internal control over financial reporting that is considered a material weakness:

> **Financial Reporting:** A material weakness over Accounting for Appropriations was identified where management's review and knowledge of the financial statements preparation and presentation related to Appropriations were not adequately designed to prevent, or detect and correct, material misstatements.

In addition to the material weakness in internal control, the deficiency resulted in instances of noncompliance with United States generally accepted accounting principles, and consequently, noncompliance with the *Federal Financial Management Improvement Act of 1996*, in which financial management systems did not substantially comply with the applicable Federal accounting standards.

Commission management concurred with the findings and recommendations and agreed to take the necessary corrective actions.

Report Number: OAS-FS-15-05

Attachment

cc: Executive Director, Federal Energy Regulatory Commission
Chief Financial Officer, Federal Energy Regulatory Commission
Deputy Chief Financial Officer, CF-2
Director, Internal Controls and Evaluation Division, Federal Energy Regulatory Commission
Director, Office of Financial Risk, Policy and Controls, CF-50
Deputy Director, Office of Finance and Accounting, CF-10
Assistant Director, Office of Financial Risk, Policy and Controls, CF-50
Assistant Director for Internal Review, CF-50
Audit Resolution Specialist, Office of Financial Risk, Policy and Controls, CF-50
Team Leader, Office of Financial Risk, Policy and Controls, CF-50
Audit Coordinator, Federal Energy Regulatory Commission

http://www.ferc.gov/about/strat-docs/perf-rev.asp

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Independent Auditors' Report

The Federal Energy Regulatory Commission and the
Inspector General, United States Department of Energy

Report on the Financial Statements

We have audited the accompanying financial statements of the Federal Energy Regulatory Commission (the Commission), which comprise the balance sheets as of September 30, 2014 and 2013, and the related statements of net cost, changes in net position, budgetary resources, and custodial activity for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 Office of Management and Budget (OMB) Bulletin No. 14-02, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 14-02 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Commission's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

KPMG

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Federal Energy Regulatory Commission as of September 30, 2014 and 2013, and its net costs, changes in net position, budgetary resources, and custodial activity for the years then ended in accordance with U.S. generally accepted accounting principles.

Emphasis of Matter

As discussed in Note 18 to the financial statements, the 2013 financial statements have been restated to correct a misstatement. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis section be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audits of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Letter from the Chairman, Message from the Chief Financial Officer, Other Information - Schedule of Spending, Performance Report section, and the Appendices of the Performance and Accountability Report 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 audits of the financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Government Auditing Standards*

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended September 30, 2014, we considered the Commission's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described in Exhibit I, we identified a deficiency in internal control that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in Exhibit I to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commission's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contract agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 14-02. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 14-02.

We also performed tests of its compliance with certain provisions referred to in Section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). Providing an opinion on compliance with FFMIA was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of FFMIA disclosed instances, described in the accompanying Exhibit I, in which the Commission's financial management systems did not substantially comply with the applicable Federal accounting standards. The results of our tests of FFMIA disclosed no instances in which the Commission's financial management systems did not substantially comply with the Federal financial management systems requirements and United States Government Standard General Ledger at the transaction level.

Commission's Response to Findings

The Commission's response to the findings identified in our audit is described in Exhibit I. The Commission's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

***Purpose of the Other Reporting Required by* Government Auditing Standards**

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Commission's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Washington, D.C.
November 24, 2014

Independent Auditors' Report
Exhibit I – Material Weakness

Financial Reporting

Management's review and knowledge of the financial statements preparation and presentation, as well as the journal entries supporting the underlying transactions related to Appropriations, were not adequately designed at a sufficient level of detail to include a review to prevent, or detect and correct, material misstatements in FY 2014 related to proper accounting/reporting in accordance with Federal accounting standards. Similarly, this ineffective control environment existed in FY2013, which allowed a material error to occur and not be detected and corrected in the prior year financial statements.

During our review of the fiscal year 2014 draft financial statements, we identified a material change in amounts between the fiscal years 2014 and 2013 presentation of the comparative balance sheets and statements of changes in net position. Furthermore, the draft financial statements and related notes did not include a disclosure or explanation that there had been a change in how the Commission was accounting for the unexpended appropriation. We identified this as a material weakness in the Commission's internal controls over financial reporting related to the accounting for appropriations.

The Commission receives and uses an annual appropriation from Congress for "necessary expenses … to carry out the provisions of the Department of Energy Organization Act." The 2014 appropriation law (Public Law 113-76) further provides that the sum appropriated from the general fund "shall be reduced as revenues are received during fiscal year 2014 so as to result in a final fiscal year appropriation from the general fund estimated at not more than $-0-." The United States Treasury, based on this appropriation, issues a warrant to the Commission to pay its expenses. This same provision to receive and repay an appropriation was also included in previous years' authorizing legislation.

The Commission receives and uses the appropriation during the year to operate (i.e., to pay for salaries and expenses). Consistent with the requirements of the Omnibus Budget Reconciliation Act of 1986, the Commission also collects revenues for fees, annual charges and other services during the year to offset 100% of its budget authority (i.e., offsetting collections). At year end, the Commission repays the Treasury the full amount of the appropriation by using offsetting collections for the appropriations used throughout the year, plus returning any unused portion of the appropriation, resulting in no remaining unexpended appropriations. The Commission also transfers to Treasury the amount of offsetting collections in excess of the appropriations. The remaining unused offsetting collections become a financing source to replace the unused portion of the appropriation.

During review of its authorizing legislation in FY 2014, the Commission determined it had been incorrectly accounting for the appropriations in the current fiscal year by carrying over from one year to the next the residual "unexpended appropriations" instead of reflecting "unexpended appropriations" at the end of the year at $-0-. The Commission initially believed the accounting for and presentation of the appropriations and offsetting collections only affected FY 2014 and prepared journal entries at year end to reflect the change in FY 2014 balances. However, based upon our review of the draft FY 2014 statement of changes in net position and audit testing performed on the underlying FY 2014 accounting transactions related to appropriations we identified errors that resulted in incorrect amounts reported in the FY 2014 and FY 2013 balance sheets and statements of changes in net position. Management reviewed the identified errors and corrected FY 2014 accounting transactions to properly present the Unexpended Appropriations in FY 2014 and also agreed the FY 2013 balance sheet and statement of changes in net position were in error and that a restatement of that year was required.

The effect of the restatement is described in more detail in Footnote 18 to the Commission's FY 2014 and 2013 financial statements. In summary, the September 30, 2013 Unexpended Appropriations reported of

$49,840,825 should have been reported at $-0- and the Cumulative Results of Operations reported of $(7,280,772) should have been reported at $42,560,053.

In addition to the material weakness in internal control, the deficiency resulted in instances of noncompliance with U.S. generally accepted accounting principles, and consequently, noncompliance with *Federal Financial Management Improvement Act of 1996* (FFMIA) in which financial management systems did not substantially comply with the applicable Federal accounting standards.

Recommendation: Develop training to improve the knowledge of technical matters related to financial reporting of budgetary resources for those who are preparing and reviewing journal entries, as well as preparing and reviewing the financial statements and increase the level of detail in the review of appropriations, related journal entries, and the financial statements.

Management's response:

We concur with this finding. The Commission's Chief Financial Officer will ensure appropriate Commission staff is adequately trained to enhance their knowledge of technical accounting matters related to the accounting and reporting of budgetary resources. Furthermore, as part of the enhanced training, the Chief Financial Officer will document the procedures necessary for specific accounting transactions to be used in accounting for the Commission's complex and/or unique financial transactions related to both budgetary and proprietary accounting in addition to an increased level of detail review of accounting for and presentation of budgetary resources.

FEEDBACK

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