OFFICE OF INSPECTOR GENERAL

U.S. Department of Energy

INSPECTION REPORT

DOE-OIG-18-38

July 2018

WESTERN AREA POWER ADMINISTRATION'S UNOBLIGATED BALANCES FROM VARIOUS FUNDING SOURCES

Department of Energy
Washington, DC 20585

July 10, 2018

MEMORANDUM FOR THE ADMINISTRATOR, WESTERN AREA POWER ADMINISTRATION

Michelle Anderson

FROM: Michelle Anderson
Deputy Inspector General
for Audits and Inspections
Office of Inspector General

SUBJECT: INFORMATION: Inspection Report on "Western Area Power Administration's Unobligated Balances from Various Funding Sources"

BACKGROUND

Western Area Power Administration (Western) is one of the four power marketing administrations within the Department of Energy that markets and transmits wholesale electricity from multi-use water projects. In fiscal year (FY) 2017, Western's operations exceeded $1 billion, more than 90 percent of which was financed through customer funding. The remaining annual requirements were provided by appropriations. To ensure financial sustainability, including continued operations during a lapse in appropriation or severe weather conditions that affect Western's ability to meet its contractual commitments, Western maintains balances in its Treasury accounts from year to year, referred to as "unobligated balances." An unobligated balance is funding that has not been obligated and is legally available to carry forward from one year to another. Western's unobligated balances are made up of various funding sources including appropriations, the authority to use receipts from the sale of power, as well as alternative financing, which includes customer advances. Most recently, in FY 2017, Western's year-end unobligated balances were $707 million, over $569 million of which resided in its Construction, Rehabilitation, Operation and Maintenance (CROM) account. Western's CROM account funds a majority of Western's operations.

During FY 2017, the House of Representatives' Committee on Oversight and Government Reform referred concerns raised by a Western employee regarding potential improprieties in the management of Western's unobligated balances, including whether Western appropriately retained, used, and disclosed those balances. Due to the sensitivity surrounding this issue, we initiated an inspection on Western's unobligated balances from various funding sources. The objectives of the inspection were to determine whether Western (1) properly retained unobligated balances in its CROM account, (2) implemented a strategy for managing unobligated balances, and (3) adequately disclosed unobligated balances.

RESULTS OF INSPECTION

Nothing came to our attention to indicate that Western had mismanaged its unobligated balances. Specifically, we found that Western had appropriately:

- Retained and carried forward unobligated balances in its CROM account from year to year;

- Developed and implemented a strategy for managing its unobligated balances in FY 2017, as well as established a mechanism to monitor and report the balances; and

- Disclosed its unobligated balances to the Department's Office of the Chief Financial Officer, the Office of Management and Budget (OMB), and Congress as part of the President's Budget Request.

Although Western monitored and reported its unobligated balances during FY 2017, we found that the year-end reporting mechanism may not have provided sufficient transparency of management decisions towards achieving its unobligated balance strategy. Based on recent concerns from Congress and Western's customers regarding the transparency of Western's financial decisions, we determined a more detailed report would be beneficial. As a result of discussions with Western officials, they addressed our concern and prepared a detailed report that summarized Western's FY 2017 actions planned and taken to implement its strategy for managing unobligated balances.

Retention of Unobligated Balances

We found that Western had appropriately retained and carried forward unobligated balances in its CROM account. Specifically, we found that, per requirements in the annual appropriation language, Western was allowed to accumulate and carry forward unobligated balances in its CROM account from year to year until the funds were expended. To operate, Western primarily relied on an annual budget authority from Congress that included an appropriation and the authority to use customer receipts from the sale of power. This annual budget authority remains available until the funding is spent, as Western's budget authority from FYs 2012 to 2017 included the phrase "to remain available until expended." Federal Appropriation Law defines this phrase to mean that the appropriation and the authority to use customer receipts is available for an indefinite period. Additionally, we found no law or regulation limiting the amount of unobligated balances an eligible agency can maintain.

We also noted that the Government Accountability Office (GAO) did not take exception to Western maintaining unobligated balances. In October 2015, GAO issued a report entitled, *2013 SEQUESTRATION AND SHUTDOWN: Selected Agencies Generally Managed Unobligated Balances in Reviewed Accounts, but Balances Exceeded Target Levels in Two Accounts* (GAO-16-26, October 2015). While GAO did not take issue with Western's retention of unobligated balances, the report noted that for FY 2014, Western had exceeded one of its target levels of unobligated balances that had been identified in a draft strategy developed by Western management. In an effort to ensure effective use of Federal funds and management of unobligated balances, GAO recommended that the Secretary of Energy direct Western's Administrator and Chief Executive Officer to finalize and implement a strategy to reduce excess unobligated balances.

Strategy Implementation

We found that Western had developed and taken steps to implement a strategy for managing unobligated balances and had established a mechanism to continuously monitor the balances. In December 2016, Western finalized *WAPA's Unobligated Balance Strategy FY 2016-2020* (FY 2016-2020 Strategy), which focused on maintaining reasonable and appropriate funding to ensure sustainability for the following primary purposes:

- <u>Annual Operations and Maintenance (O&M)</u> - maintain sufficient unobligated balances to allow Western to continue operation for at least one quarter and to cover the potential for a lapse in appropriations of up to 21 days.

- <u>Capital Investments</u> - maintain sufficient balances to ensure that the level of planned capital investments that rely on non-Federal financing for the upcoming 3-year period is sustainable.

- <u>Purchase Power and Wheeling</u> - maintain sufficient balances to acquire purchase power and wheeling services on the open market in order to mitigate the increased expenses associated with a long-term drought scenario. The strategy ensures contractual energy obligations are met when weather conditions impede Western's ability to generate/transmit required energy.

We found that Western had taken actions to implement its FY 2016-2020 Strategy. For example, although Western's annual O&M unobligated balance had exceeded its targets for FY 2016 and FY 2017, Western had initiated actions to gradually lower the balance. To align with its strategy target of $79 million for annual O&M, Western reduced its unobligated balance from $151 million at the end of FY 2016 to $129 million at the end of FY 2017. Specifically, to reduce the balance in FY 2017, Western requested and received less annual Program Direction (workforce compensation and related expenses) and O&M funding than needed and instead used $34 million of its unobligated balances. To continue lowering the balance towards its target, Western took similar action in FY 2018 by proposing the use of $44 million in unobligated balances.

We also found Western had monitored and reported its unobligated balances during FY 2017. Western had developed a financial tool that provided monthly updates on the unobligated balances and forecasted the end-of-year balances. Western financial managers stated that the balances and any actions were discussed at monthly meetings between regional and headquarters' financial managers, as well as at senior leadership meetings. Additionally, Western planned to use the financial tool to report year-end unobligated balances and assess those balances against the strategy targets. An annual report detailing the results of implementing the FY 2016-2020 Strategy was required in a memorandum from the Acting Chief Financial Officer that accompanied Western's FY 2016-2020 Strategy.

However, in our opinion, using Western's financial tool as a year-end report may not have provided sufficient transparency of management decisions towards achieving its unobligated balance strategy. Specifically, the financial tool report only included data and corresponding graphics and did not detail Western's actions planned and taken. With continued concerns over transparency of Western's financial decisions from Western's customers and Congress alike, we determined a more comprehensive report would be beneficial. When we brought this concern to Western's attention, budget officials agreed to prepare a detailed report. In January 2018, Western officials finalized a report that included proposed action plans, actual steps taken during the year to better align with the strategy, and the actual year-end unobligated balances. We determined that this report adequately described actions taken by Western to better align with its unobligated balance strategy and believe it prudent for Western to publish these reports annually on its website to further ensure transparency.

Disclosure of Unobligated Balances

We found that Western's unobligated balances had been adequately disclosed and the cash account, where the majority of the balances reside, was audited by an independent public accounting firm. Specifically, Western was transparent with its unobligated balances, as the balances were disclosed to the:

- Department's Office of the Chief Financial Officer;
- OMB; and
- Congress in the President's Annual Budget Request.

The Department's Office of the Chief Financial Officer, whose mission is to assure the effective management and financial integrity of Department activities, had the ability to monitor Western's unobligated balances. Specifically, Western uploaded financial information to the Department's accounting system on a monthly basis. From this information, the Department's Office of the Chief Financial Officer was able to generate a monthly spending report that included information regarding Western's unobligated balances. In addition, on an annual basis, Western's Chief Financial Officer certified a report detailing Western's fiscal year-end unobligated balances and provided this report to the Department's Office of the Chief Financial Officer.

We found that OMB was aware of Western's unobligated balances and its strategy to manage those balances. Specifically, an OMB official told us that OMB typically received information on Western's unobligated balances from the Department's Office of Chief Financial Officer annually through Western's initial apportionment. The official stated that OMB was briefed on Western's strategy in October 2016; and although OMB had not formed an opinion on the strategy, it understood that Western sought to hold contingency balances for annual expenses, capital funding, and purchase power and wheeling needs. Additionally, we noted that Western's unobligated balances are presented to Congress each year in the President's Congressional Budget Request.

Furthermore, according to the audit team from the independent public accounting firm that performs Western's annual financial statement audit, the majority of Western's unobligated balances resided in its cash account. The audit team also told us that although it did not test the validity of management decisions regarding the size of the unobligated balances, Western's cash account was tested annually as part of the financial statement audit. In the *Western Federal Power System's Fiscal Year 2017 Financial Statement Audit* (DOE-OIG-18-21, February 2018) report, the public accounting firm concluded that the combined financial statements presented fairly, in all material respects, the respective financial position of the Western Federal Power System, and that the results of its operations and its cash flow for the year was in conformity with United States generally accepted accounting principles.

SUGGESTION

Given the importance of providing financial transparency to Congress and ratepayers alike, we suggest that the Administrator for Western Area Power Administration ensure annual reports detailing actions taken and results achieved on its unobligated balances strategy are published and made available to the public. Western agreed with the suggestion and stated that it would publish the suggested reports annually on its website "The Source." This website displays operational and financial information in one convenient location.

Attachments

cc: Deputy Secretary
Chief of Staff
Under Secretary of Energy

OBJECTIVES, SCOPE, AND METHODOLOGY

OBJECTIVES

To determine whether Western Area Power Administration (Western) (1) properly retained unobligated balances in its Construction, Rehabilitation, Operation and Maintenance account; (2) implemented a strategy for managing unobligated balances; and (3) adequately disclosed unobligated balances.

SCOPE

During fiscal year (FY) 2017, the House of Representatives' Committee on Oversight and Government Reform referred concerns raised by a Western employee regarding potential improprieties in the management of Western's unobligated balances, including whether Western appropriately retained, used, and disclosed those balances. Due to the sensitivity surrounding this issue, we initiated an inspection on Western's unobligated balances. We conducted this effort at Western's Headquarters, located in Lakewood, Colorado, and its Desert Southwest Regional Office, located in Phoenix, Arizona.

The inspection was conducted from September 2017 through July 2018 at Western's Headquarters under Office of Inspector General project number A17DN050.

METHODOLOGY

To accomplish our inspection objectives, we:

- Interviewed key Western officials and reviewed pertinent documentation to gain a general understanding of Western's funding process and unobligated balances strategy;
- Interviewed key officials from the Department of Energy's Office of the Chief Financial Officer regarding oversight responsibilities related to Western's unobligated balances;
- Obtained and reviewed written responses from the Office of Management and Budget regarding its knowledge of, and involvement with, Western's unobligated balances;
- Interviewed officials from the independent public accounting firm that performs Western's annual financial statement audit to understand work they conducted on Western's unobligated balances during the annual financial statement audit;
- Reviewed prior Government Accountability Office reports relevant to our inspection;
- Reviewed and analyzed laws and regulations pertaining to Western's funding and unobligated balances. We limited our analysis of authorities to retain unobligated balances to those associated with Western's Construction, Rehabilitation, Operation and Maintenance account, which funded 80 percent of its operations in FY 2017.

This inspection was conducted in accordance with the Council of the Inspectors General on Integrity and Efficiency's, *Quality Standards for Inspection and Evaluation*, dated January 2012. Those standards require that we plan and perform the inspection to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions and observations based on our inspection objective. We believe the evidence obtained provides a reasonable basis for our conclusions and observations based on our inspection objective. Accordingly, the inspection included tests of controls and compliance with laws and regulations to the extent necessary to satisfy the inspection objective. In particular, we assessed compliance with the *GPRA Modernization Act of 2010* and found that in its FY 2017 annual performance plan, Western had an initiative related to its unobligated balances strategy to meet one of its strategic target areas. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our inspection. Finally, we relied on computer-processed data to a limited extent to accomplish our inspection objective and performed appropriate tests to validate the results, such as verifying the reported decrease in unobligated balances with the data from Western's financial system.

Management waived an exit conference on June 5, 2018.

RELATED REPORT

Government Accountability Office

- Report on *2013 SEQUESTRATION AND SHUTDOWN: Selected Agencies Generally Managed Unobligated Balances in Reviewed Accounts, but Balances Exceeded Target Levels in Two Accounts* (GAO-16-26, October 2015). Both the 2013 sequestration and Government shutdown highlighted the importance of actively managing public funds. Effective management of unobligated balances that are carried over for use in the next fiscal year presents agencies with an opportunity to better respond to unexpected events in the future. The Government Accountability Office was asked to review how balances had changed since 2012. The report evaluated how selected agencies managed and used unobligated balances in reviewed accounts, focusing on fiscal years 2012 through 2014, which covered the 2013 sequestration and Government shutdown. Among the accounts chosen for review was Western Area Power Administration's Construction, Rehabilitation, Operation and Maintenance account. The Government Accountability Office found that the selected agencies generally managed and tracked unobligated balances to ensure the effective use of program resources in the eight reviewed accounts; however, in fiscal year 2014, the balance for one category within Western Area Power Administration's Construction, Rehabilitation, Operation and Maintenance account had exceeded the draft strategy that it had put in place. The Government Accountability Office recommended that the Secretary of Energy direct Western Area Power Administration's Administrator and Chief Executive Officer to finalize and implement a strategy to reduce excess unobligated balances.

FEEDBACK

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