



OFFICE OF INSPECTOR GENERAL

MEMORANDUM

DATE: November 14, 2014

TO: Chairman

FROM: Inspector General 

SUBJECT: Audit of the Federal Communications Commission's Financial Statements for Fiscal Year 2014

As required by the Accountability of Tax Dollars Act of 2002, (Pub. L. 107-289), the Office of Inspector General (OIG) engaged the independent certified public accounting firm of KPMG LLP to audit the fiscal year 2014 financial statements of the Federal Communications Commission (FCC) in accordance-with generally accepted government auditing standards.

KPMG LLP's reports include an opinion on FCC's financial statements, report on internal control over financial reporting, and report on compliance and other matters. In summary, K.PMG LLP found that:

- The financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles.
- There was one material weaknesses in internal control related to USF's Budgetary Accounting.
- There was one repeat significant deficiency related to FCC's information technology controls.
- There was one repeat instance of noncompliance with laws and regulations related to requirements of the Debt Collection Improvement Act.

While management has made improvements as it relates to the repeated internal control significant deficiency noted above, this issue has been reported by financial statement auditors since FY 2005.

The OIG reviewed KPMG LLP's reports and related documentation and made necessary inquires of KPMG's representatives . Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards was not intended to enable us to express an opinion and we do not express an opinion on the FCC's financial statements, conclusions about the effectiveness of internal controls, or conclusions on compliance with laws and regulations. KPMG LLP is wholly responsible for the attached report dated November 14, 2014 and the conclusions expressed therein.

Our review, while still ongoing, disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

cc: Jon Wilkins, Managing Director
Ruth Milkman, Chief of Staff
Mark Stephens, Chief Financial Officer
Dr. David Bray, Chief Information Officer

AUDIT OF THE FEDERAL COMMUNICATIONS COMMISSION's



Financial Statements for
Fiscal Year 2014

(OCTOBER 1, 2013 – SEPTEMBER 30, 2014)

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KPMG LLP
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Independent Auditors' Report

Managing Director
Federal Communications Commission

Inspector General
Federal Communications Commission

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated 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 entity'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 consolidated financial statements.



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

Opinion on the Financial Statements

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Federal Communications 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.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis and Required Supplementary Information sections be presented to supplement the basic consolidated financial statements. Such information, although not a part of the basic consolidated 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 basic consolidated 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 basic consolidated financial statements, and other knowledge we obtained during our audits of the basic consolidated 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 basic consolidated financial statements as a whole. The information in the *Message from the Chairman* and the *Other Information* sections are presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.



Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2014, on our consideration of the FCC's internal control over financial reporting and our report dated November 14, 2014, on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering FCC's internal control over financial reporting and compliance.

KPMG LLP

November 14, 2014



KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

Managing Director
Federal Communications Commission

Inspector General
Federal Communications Commission

We have audited, 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*, the consolidated financial statements of the Federal Communications Commission (FCC), which comprise the consolidated balance sheets as of September 30, 2014 and 2013, and the related consolidated statements of net cost, changes in net position, and custodial activity, and combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated November 14, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements as of and for the year ended September 30, 2014, we considered the FCC'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 consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the FCC's internal control. Accordingly, we do not express an opinion on the effectiveness of the FCC'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 Exhibits I and II, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiency.

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. We consider the deficiency described in Exhibit I to be a material weakness.

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 II to be a significant deficiency.



FCC's Responses to Findings

The FCC's response to the significant deficiency and material weakness identified in our audit is included in the memorandum from management titled "Management's Response to Independent Auditors' Reports on Internal Control over Financial Reporting and Compliance and Other Matters for Fiscal Year 2014." The FCC's response was not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and the result of that testing, and not to provide an opinion on the effectiveness of the FCC's internal control. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the FCC's internal control. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

November 14, 2014

EXHIBIT I

MATERIAL WEAKNESS

Universal Service Fund (USF) Budgetary Accounting

During our fiscal year (FY) 2014 audit, we noted improvements were needed in internal controls and processes related to USF budgetary accounting. Our audit identified errors in non-routine, manual journal entries related to the implementation of new programs, as well as errors caused by a lack of formal communication between certain Universal Service Administrative Company (USAC) accounting department and the Schools and Libraries (SLD) program managers.

Specifically, we noted the following:

- USAC management did not initially follow an FCC approved administrative change issued in February 2013 extending the invoice deadline and obligation expiration date for \$581 million in SLD obligations. As a result, the obligations were incorrectly deobligated in November 2013. USAC management subsequently identified and corrected the error, but not until February 2014. The related control, as well as the compensating controls, were not adequate to detect and correct the error in a timely manner.
- An unusual transaction of \$62 million existed in the population of new commitments provided by USAC for the High Cost Connect America Fund (CAF). This transaction was related to the deobligation of unclaimed CAF Phase 1 amounts. This transaction was the result of USAC incorrectly debiting the Exempt Undelivered Orders – Obligations, Unpaid (account 4801) instead of Downward Adjustments of Prior-Year Unpaid Undelivered Orders - Obligations, Recoveries (account 4871). This error was subsequently corrected as of September 30, 2014.
- USAC incorrectly recorded an obligation for the full amount of a High Cost Mobility fund winning bid, for which a portion in the amount of \$48,400 was in default as of September 2013. The error was discovered during an informal review of transactions by USAC in September 2014 and reversed.

USAC management did not have formal lines of communication in place between the USAC accounting department and the SLD program managers regarding relevant FCC approved administrative changes in order to ensure the appropriate budgetary accounting treatment was applied to the affected transactions. SLD program managers updated their records to reflect the granted extension in their database but did not coordinate with the USAC accounting team to update their records for financial reporting purposes. As a result, the deobligation was recorded based on Data Insight reports using an outdated data table.

In addition, USAC management did not have sufficient controls in place to review the non-routine, manual journal entries recorded for the Connect America Fund or the Mobility Fund to ensure compliance with USSGL budgetary accounting guidance and that only valid obligations were recorded.

Without adequate internal controls in place, there is an increased risk that material errors could occur in the financial statements and not be detected and corrected in a timely manner.

Recommendations:

1. Develop more formal lines of communication between the USAC accounting department and the SLD program managers regarding relevant FCC approved administrative changes in order to implement the proper accounting treatment for the related transactions. **(New)**
2. Enhance the controls over the review of non-routine budgetary journal entries to ensure transactions are properly recorded. **(New)**

EXHIBIT II

SIGNIFICANT DEFICIENCY

Information Technology (IT) Controls

Since fiscal year (FY) 2009, we have reported that the FCC needed to improve its entity-wide security program. An effective security program embodies the organization's internal control responsibilities with respect to securing its Information Technology (IT) infrastructure and services. The Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Internal Control*, provides guidance to assist agencies complying with the standards related to control environment, risk assessment, control activities, monitoring, and information and communication. For purposes of financial reporting, management is responsible for developing and maintaining internal control activities that comply with OMB circular No. A-123 to ensure the reliability of financial reporting.

In FY 2014, the FCC continued to progress in maintaining an entity-wide security program that provided for an internal control environment that included the components of continuous monitoring, risk assessment, control activities, and information and communication in order to prevent and detect unauthorized access to agency information resources. Although the FCC performed certain monitoring activities and initiatives, and made moderate improvements from the prior year, the FCC IT infrastructure still did not fully comply with certain requirements prescribed in National Institute of Standards and Technology (NIST) Special Publication (SP) 800-53, Revision 4, *Recommended Security Controls for Federal Information Systems*, and OMB Circular No. A-123. In the current year, we identified additional deficiencies in the FCC's control environment, risk assessment process, control activities, and monitoring process related to securing FCC's IT infrastructure. The FCC's consolidated financial statements are comprised of three reporting components: FCC headquarters and field offices, the Universal Service Fund (USF), and the North American Numbering Plan (NANP). However, the current year IT deficiencies described below relate primarily to the FCC, which represents approximately \$464.9 million of \$9.3 billion of consolidated total program costs. We have previously reported these deficiencies to FCC management, including identified causes and recommendations, and provided further detail in the sections below on the reported deficiencies.

Control Environment Findings

OMB Circular A-123 requires management to clearly identify areas of authority and responsibility, and appropriately delegate the authority and responsibility throughout the agency. We noted the FCC had not documented policies and procedures for actively directing and overseeing external third parties. In addition, the FCC's FY14 inventory of information systems did not include interfaces between certain information systems and subsystems, or contractor-operated systems.

While a procedure was in place for the periodic inventory and tracking of information systems, the FCC had not developed policies and procedures for actively directing and overseeing external third parties.

The FCC excluded existing contractor-operated systems and related interfaces from the FCC's inventory of information systems, which led to an incomplete inventory. An incomplete inventory may result in FCC management: a) not being aware of the existence of all relevant contractor systems; b) not being aware when

significant changes occur that could impact the effectiveness of contractors' security controls; or c) not requiring a re-assessment and re-authorization of a relevant contractor system.

Control Environment Recommendation

Strengthen the control environment by:

1. Developing and implementing policies and procedures for actively directing and overseeing external third parties, and distributing them to contractor management. Additionally, a complete inventory should be maintained and updated at least annually to include information systems, subsystems, contractor-operated systems, and all related interfaces. **(Updated)**

Risk Assessment Findings

OMB Circular A-123 requires management to identify internal and external risks that may prevent the organization from meeting its objectives. We noted that the FCC performed procedures to assess the effectiveness of its IT security controls and to assess related risks. However, the FCC's assessment procedures were incomplete and did not comply with relevant requirements in NIST SP 800-53, Revision 4 and NIST SP 800-37, Revision 1, *Guide for Applying the Risk Management Framework to Federal Information Systems*. The FCC's failure to meet the relevant requirements noted above led to the deficiencies discussed below.

The FCC's risk management activities were not fully implemented. Specifically, we noted that the Authorizations to Operate (ATOs) had expired for the two systems reviewed on July 11, 2014 and August 21, 2014, respectively. By not reassessing and reauthorizing information systems at least every three years, there is an increased risk that the system security plan will no longer accurately depict the system's current controls, and the security assessment report will no longer consider the full range of significant risks to which the system is subject. This could ultimately result in security control gaps remaining undetected.

Furthermore, we noted the security assessment testing and the assessment of risks for all tested major applications were incomplete. Specifically, we noted the security assessment testing did not include management and operational controls, as required by NIST 800-53, Revision 4. Additionally, testing did not include all technical controls because security assessment testing was limited to technical vulnerability scans of relevant servers. The security assessment and authorization process, as required by NIST 800-53 Revision 4, is intended to drive the adoption of necessary IT security controls designed to achieve more secure information systems at federal agencies. However, for the three FCC systems tested, the security assessment report was incomplete as the vulnerabilities identified were largely limited to technical vulnerabilities as management and operational vulnerabilities were not included. Limiting the assessment of risks to vulnerabilities identified by incomplete security assessment testing may result in significant risks not being considered in the risk assessment. Further, utilizing incomplete risk assessments to assist in tailoring and scoping a system security plan (SSP) may result in an incomplete risk assessment and SSP's not documenting all appropriate controls and enhancements.

In addition, the FCC's Cyber Security Policy directed that security assessment testing be performed but did not reference to the applicable standards (e.g. NIST SP 800-53A, Revision 1) to prescribe the appropriate rigor and breadth of testing.

The FCC did not perform system security planning and assessments for the majority of its systems, and did not reassess and reauthorize its information systems in the last three years. As a result, two FCC systems had an expired ATO, as described above, and the majority of FCC systems had temporary ATOs issued by the FCC Chief Information Officer (CIO).

We also noted that risk assessments for three applications that authenticate users outside of the FCC did not map to the assurance levels in OMB Memorandum 04-04, *E-Authentication Guidance for Federal Agencies*, and the e-authentication controls in NIST SP 800-63, *Electronic Authentication Guideline*.

Incomplete system security plans increase the risk that security assessment testing may not include all required IT security controls for each system. Further, if security assessment testing of all required IT security controls, including management and operational controls, is not performed, there is an increased risk that control deficiencies will not be identified and corrected, or mitigated with effective compensating controls in a timely manner.

Risk Assessment Recommendations

Strengthen risk assessments by:

2. Assessing the risks of identified vulnerabilities (by considering both vulnerabilities and related threats), and adding mitigating controls to the system security plans. **(Reissued)**
3. Performing security assessment testing for applicable management, operational and technical controls in accordance with evaluation criteria from NIST SP 800-53a Revision 4 at least once every three years for FCC information systems. **(Reissued)**
4. Authorizing all FCC information systems to operate subsequent to planning and successfully testing the necessary IT security controls. Information systems considered to be major applications should be prioritized. **(Updated)**
5. Performing E-authentication risk assessments and updating system security plans to define the relevant authentication level and the required level of e-authentication controls to implement for each e-government application. **(Reissued)**

Control Activities Findings

OMB Circular A-123 requires internal control to be in place over information systems in the form of both general and application controls. General controls apply to all information systems such as servers, the FCC network and end-user environments, and also includes agency-wide security program planning, management, control over data center operations, and system software acquisition and maintenance. Control activities include policies, procedures, and mechanisms in place to help ensure that agency objectives are met.

Examples of such mechanisms include: proper segregation of duties (separate personnel with authority to authorize a transaction, process the transaction, and review the transaction); physical controls over assets; proper authorization; and appropriate documentation and access to that documentation.

Due to the rapid changes in information technology, controls must adjust to remain effective. Based on our procedures performed, we noted deficiencies in FCC's general control activities related specifically to the FCC security program, access controls, and change controls. The deficiencies are discussed in more detail below.

Security Program

The FCC did not update its system security plans to document controls that mapped to NIST SP 800-53 Revision 4, which are recommended minimum baseline controls. Additionally, security assessments of controls to support the FCC's information systems' ATOs were incomplete.

Access Controls

During our review, we found that access controls were not consistently implemented throughout the FCC environment, including documentation of access approvals, removal of access for terminated or inactive users; as well as periodically reviewing user access privileges. Specifically, we identified the following control weaknesses:

- Procedures for user account management functions were not consistently implemented for major applications. Inconsistent implementation of documented procedures led to instances where access was granted without documented authorization.
- User account management controls were not operating effectively to prevent logical or physical access from being granted to users who should not have access or to remove access from users who no longer needed it. The FCC also did not perform periodic reviews and recertification of network and infrastructure users.
- Accounts were not removed in a timely manner for separated users. As a result, there was an increased risk that data and resources were subject to unauthorized use, loss, or disclosure.
- Controls to limit privileged access were not operating effectively. In addition, the resolution of identified vulnerabilities was not documented and the FCC did not consistently use audit logs to monitor user actions. Further, the FCC's password policies were not clearly defined.
- FCC policies and procedures have not been implemented for vulnerability scanning of all FCC information systems and assets.
- Incidents were not accurately classified in the appropriate categories due to lack of training in the Network Security Operations Center (NSOC) group. Therefore, all required incidents were not being

reported to United States Computer Emergency Readiness Team (US-CERT) to meet Federal requirements.

- There was not a documented process for FCC's contractor system application to perform periodic reviews of the database suspicious activity.

Change Controls

The FCC could not provide documentation to evidence that system configurations were monitored for unauthorized changes. Furthermore, the FCC did not periodically review configurations for server operating systems, server software, network devices and database management systems for compliance with baseline configurations.

Control Activities Recommendations

Security Program

Strengthen security program oversight and planning by:

6. Documenting system security plans across all components to clearly define system security controls for information systems that are equivalent to the NIST SP 800-53, Revision 4, minimum baseline controls (including required enhancements), that categorize controls as common, hybrid or system-specific, and that describe controls in sufficient detail to identify the system components to which they are applicable. **(Updated)**
7. Ensuring that contractor deliverables (including the security authorization and assessment packages) are consistent with the NIST SP 800-53, Revision 4 and NIST SP 800-37, Revision 1. **(Reissued)**

Access Controls

Strengthen access controls by:

8. Consolidating all existing procedures related to adding users into one comprehensive document, and including a standardized process that specifies the appropriate access request form to be used for each information system. **(Updated)**
9. Establishing a process for retaining access authorization forms for new users to the FCC network domain, remote access and FCC applications. **(Reissued)**
10. Updating the applicable applications to possess the capability of having individual user access accounts for each external user. **(Reissued)**
11. Updating and implementing USAC procedures for adding users, removing users, and reviewing and recertifying users. **(Updated)**

12. Implementing the Cyber Security Policy and Application User Account Management Procedures by performing quarterly reviews of the FCC Network and FCC applications to ensure that user access is reviewed and recertified by management. Access should be promptly revoked for users found to no longer need access or whose access is not recertified. **(Reissued)**
13. Ensuring individuals are not granted computer room access without approval from the Chief of Network Operations and a signed Computer Room Access Acknowledgment of Responsibilities form. **(Updated)**
14. Ensuring network access is revoked within the two weeks-of the required deadline for any employees and contractors that fail to take annual security awareness training, in accordance with the FCC Cyber Security Policy. **(New)**
15. Revoking access of separated employees or contractors by using the monthly list of separated contractors distributed by the Security Operations Center, and the bi-weekly list of separated employees distributed by Human Resources. **(Updated)**
16. Defining agency-wide password strength and account lockout requirements, including the scope and applicability. Further, FCC should implement password strength and account lockout settings for FCC applications to be consistent with its policies. Any exceptions to the policies should be documented. **(Reissued)**
17. Configuring the Security Information and Event Management (SIEM) solution to encompass all platforms for monitoring and reporting purposes. Further, documenting and implementing procedures for security audit logging and review of UNIX platforms, remote connections, network domain controllers, intrusion detection systems, backend infrastructure, and FCC major applications to ensure users accessing FCC information systems are uniquely identified and their actions are auditable. **(Updated)**
18. Revising current vulnerability assessment program to include information and/or procedures, which at a minimum contain the following: the tools currently utilized configuration and licensing specifications, a list of all FCC devices and assets subject to periodic vulnerability scanning, reporting requirements, and how to document exceptions. **(Updated)**
19. Following US-CERT Federal Incident Reporting Guidelines for categorizing and documenting all security incidents from initial occurrence to resolution, and reporting all necessary security incidents to US-CERT in accordance with US-CERT Concept of Operations (CONOPS). **(Updated)**
20. Documenting a process to perform periodic reviews of the database audit log activity and implementing the documented process to periodically perform reviews on audit logs database as defined by NIST 800-53, Revision 4 criteria. **(Reissued)**

Change Control

Strengthen change and configuration management controls by:

21. Implementing configuration management procedures for server operating systems, server software, network devices and database management systems. **(Reissued)**
22. Establishing baseline configurations for applicable systems supporting information technology (IT) infrastructures. **(Reissued)**
23. Establishing and documenting baseline configurations for applicable systems across all components for applicable systems and supporting information technology (IT) infrastructure environments across all components. **(Updated)**
24. Periodically reviewing configurations for applicable systems across all components against baselines to ensure that the applicable IT infrastructures are securely configured. **(Updated)**

Monitoring Findings

OMB Circular A-123 requires that monitoring of the effectiveness of internal control should occur in the normal course of business. Periodic assessments should be integrated as part of management's continuous monitoring of internal control, which should be ingrained in the agency's operations. We noted the FCC had not fully implemented a process to test a subset of technical, operational, and management controls annually across FCC information systems. The FCC IT Continuous Monitoring and Enforcement Plan documented this requirement; however, the process was not fully implemented.

If annual security assessment testing is not performed to monitor the controls' effectiveness, there is an increased risk that ineffective controls or outdated security authorization packages may go undetected. OMB also requires that deficiencies found in internal control be reported to the appropriate personnel and management responsible for that area. Deficiencies identified through either internal review or by an external audit should be evaluated and corrected and a systematic process should be in place for addressing deficiencies. We noted Plan of Action & Milestones (POAM) tracking procedures had not been established for contractor systems operated on behalf of the FCC. In addition, the FCC agency-wide POA&M listing did not incorporate weaknesses discovered during reviews, including GAO audits, other audits, and critical infrastructure vulnerability assessments. Some weaknesses identified at the FCC did not include milestone or completion dates. Lastly, system-level POA&Ms were not updated for any FCC major systems tested in the current fiscal year.

Monitoring Recommendations

Strengthen monitoring controls by:

25. Ensuring that the FCC performs annual security assessment testing of a subset of controls to monitor the controls' effectiveness and such testing includes use of the NIST SP 800-53a assessment cases as well as assessing the controls at least once during the three-year authorization cycle. **(Updated)**

26. Developing and implementing procedures for tracking identified contractor system vulnerabilities into a POA&M. **(New)**
27. Implementing the Cyber Security Agency-Wide POA&M Management Plan, including that POA&Ms: include all security weaknesses found during any other review done by, for, or on behalf of the agency, including GAO audits, financial system audits, and critical infrastructure vulnerability assessments; include milestone and completion dates so weaknesses can be appropriately budgeted and remediated in a timely manner; and are updated at the system-level at least quarterly. **(New)**



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Independent Auditors' Report on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

Managing Director
Federal Communications Commission

Inspector General
Federal Communications Commission

We have audited, 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*, the consolidated financial statements of Federal Communications Commission (FCC), which comprise the consolidated balance sheets as of September 30, 2014 and 2013, and the related consolidated statements of net cost, changes in net position, and custodial activity, and combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated November 14, 2014.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the FCC's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant 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 disclosed an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 14-02, which is described in Exhibit I.

Management is reviewing two matters regarding potential violations of the Anti-Deficiency Act. As of the date of this report, the outcome of these matters, and any resulting ramifications, is not known.

FCC's Response to Findings

The FCC's response to the finding identified in our audit is included in the memorandum titled "Management's Response to Independent Auditors' Reports on Internal Control Over Financial Reporting and Compliance and Other Matters for Fiscal Year 2014." The FCC's response was not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on the response.



Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of compliance and the result of that testing, and not to provide an opinion on the FCC's compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the FCC's compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

November 14, 2014

EXHIBIT I

Debt Collection Improvement Act of 1996 (DCIA)

FCC management informed us that the FCC had not transferred all eligible debt outstanding for more than 180 days to the U.S. Department of the Treasury (Treasury) in accordance with the DCIA during fiscal year 2014. FCC was in the process of transferring the eligible delinquent debt to Treasury or writing it off; however, as of September 30, 2014, this had not yet been completed. It was not completed because of the backlog related to prior year issues remitting debt, and current year issues with the overdue fee calculations performed in Genesis, the FCC's financial system.

The DCIA, as cited at 31 U.S.C. 3711 (g)(1), states that: "If a nontax debt or claim owed to the United States has been delinquent for a period of 180 days – (A) the head of the executive, judicial, or legislative agency that administers the program that gave rise to the debt or claim shall transfer the debt or claim to the Secretary of the Treasury."

Recommendations:

1. Continue to write-off or transfer to Treasury the remaining debt over 180 days past due, as appropriate; and
2. Work with the Genesis vendor to correct the Genesis system issues related to overdue fee calculations in order to timely facilitate the transfer of eligible debt to Treasury.



Office of the Managing Director

MEMORANDUM

DATE: November 14, 2014

TO: David L. Hunt, Inspector General

FROM: Jon Wilkins, Managing Director
Mark Stephens, Chief Financial Officer

SUBJECT: Management's Response to Independent Auditors' Reports on Internal Control Over Financial Reporting and Compliance and Other Matters for Fiscal Year 2014

Thank you for the opportunity to review and comment on the audit reports entitled *Independent Auditors' Report on Internal Control Over Financial Reporting* and *Independent Auditors' Report on Compliance and Other Matters*. We appreciate the efforts of your team and the independent auditor, KPMG LLP, to work with the Federal Communications Commission (Commission) throughout the fiscal year (FY) 2014 audit process. This year's audit opinion was the result of the commitment and professionalism that both of our offices as well as the independent auditors demonstrated during the FY 2014 audit process. During the entire audit process, the Commission worked closely with your office and the independent auditors' team to provide necessary and timely information to facilitate an efficient audit process.

We are pleased that, for the ninth straight year, the independent auditor provided an unmodified opinion and found that the Commission's consolidated financial statements for FY 2014 present fairly, in all material respects, the financial position of the Commission as of September 30, 2014. Nine straight years of clean audit opinions is an unprecedented accomplishment for the Commission. We have worked very hard to continue strengthening the Commission's internal controls and improving its financial management.

Despite these successes, work remains here at the Commission. The FY 2014 audit report points out one material weakness, one significant deficiency, and one instance of non-compliance with laws and regulations. The auditor's primary areas of concern relate to Universal Service Fund (USF) budgetary accounting, information technology controls, and non-compliance with the Debt Collection Improvement Act (DCIA). We concur with the recommendations made by the independent auditors in their reports.

First, we would like to address the material weakness. For the first time since FY 2008, the independent auditor identified a material weakness in the control environment over financial and accounting operations. The independent auditors identified errors in non-routine, manual journal entries related to the implementation of new programs, as well as errors caused by a lack of formal communication

between the Universal Service Administrative Company (USAC) accounting department and the Schools and Libraries (SLD) program managers.

The errors that the auditors noted were corrected by USAC during the course of the fiscal year and did not impact the Commission's FY 2014 financial statements. The Commission and USAC have already discussed this issue and have started to implement appropriate corrective action to ensure that this or similar breakdowns do not occur in the future. The Commission will work to close out this audit finding during FY 2015 and will continue to monitor USAC's processes in this area in the future.

Second, the Commission is committed to remediating information technology control deficiencies. The Commission's information technology team worked diligently throughout FY 2014 to make improvements and to resolve audit findings from previous year audits. For example, the FCC's information technology team focused on addressing the investment planning and configuration management issues identified in prior year reports and successfully closed out audit findings in these areas. During the FY 2015, the information technology team plans to keep up their efforts from FY 2014 and will be focused on achieving additional successes in strengthening controls and closing audit findings.

Furthermore, at the end of FY 2014, the Commission transferred 95.6%, of all eligible debt to the Department of the Treasury in its ongoing efforts to comply with DCIA. The Commission has a plan in place to complete the transfer of the remaining 4.4% of eligible debt to the Treasury by the end of the first quarter in FY 2015. With these corrective actions already in motion, the FCC hopes that it will be able to have this non-compliance issue closed during the FY 2015 financial audit cycle.

Finally, we are committed to continually strengthening the internal controls of the Commission and its reporting components. This commitment includes developing timely, accurate, and useful performance and financial information to ensure the most effective stewardship of both the funds that the Commission oversees and the funds that the Commission uses to finance its operations. We look forward to working in FY 2015 to resolve the FY 2014 audit findings and to enhance the culture of integrity, accountability, and excellence that exists here at the Commission.



Jon Wilkins, Managing Director
Office of Managing Director



Mark Stephens, Chief Financial Officer
Office of Managing Director

PRINCIPAL STATEMENTS

FEDERAL COMMUNICATIONS COMMISSION CONSOLIDATED BALANCE SHEET

As of September 30, 2014 and 2013
(Dollars in thousands)

	FY 2014	FY 2013
Assets (Note 2):		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 537,984	\$ 279,163
Investments (Note 5)	7,685,783	7,200,600
Accounts receivable (Note 6)	711	1,235
Other	1,063	-
Total intragovernmental	8,225,541	7,480,998
Cash and other monetary assets (Note 4)	181,519	173,084
Accounts receivable, net (Note 6)	842,736	852,026
Direct loans receivable, net	-	3,502
General property, plant, and equipment, net	34,443	47,590
Other	13,024	13,024
Total assets	\$ 9,297,263	\$ 8,570,224
Liabilities (Note 7):		
Intragovernmental:		
Accounts payable	\$ 1,575	\$ 2,522
Debt	-	353
Other (Note 8)		
Custodial	325,448	81,444
Other	4,831	8,114
Total other	330,279	89,558
Total intragovernmental	331,854	92,433
Accounts payable	115,845	134,727
Other (Note 8)		
Deferred revenue	56,520	59,920
Prepaid contributions	47,625	110,057
Accrued liabilities for Universal Service	670,755	1,088,415
Other	33,338	35,036
Total other	808,238	1,293,428
Total liabilities	\$ 1,255,937	\$ 1,520,588
Commitments and contingencies (Note 9)		
Net position:		
Unexpended appropriations - All Other Funds	\$ 3,059	\$ 3,394
Cumulative results of operations - Funds from Dedicated Collections (Note 10)	7,880,477	6,884,853
Cumulative results of operations - All Other Funds	157,790	161,389
Total net position	\$ 8,041,326	\$ 7,049,636
Total liabilities and net position	\$ 9,297,263	\$ 8,570,224

The accompanying notes are an integral part of these statements.

FEDERAL COMMUNICATIONS COMMISSION
CONSOLIDATED STATEMENT OF NET COST
For the Years Ended September 30, 2014 and 2013
(Dollars in thousands)

	<u>FY 2014</u>	<u>FY 2013</u>
Program costs (Note 11):		
Connect America:		
Total Gross Cost	\$ 46,380	\$ 47,037
Maximize Benefits of Spectrum:		
Total Gross Cost	110,562	79,655
Protect and Empower Consumers:		
Total Gross Cost	49,259	52,155
Promote Innovation, Investment, and America's Global Competitiveness:		
Total Gross Cost	10,341	9,697
Promote Competition:		
Total Gross Cost	8,884,501	9,580,394
Public Safety and Homeland Security:		
Total Gross Cost	43,101	47,359
Advance Key National Purposes:		
Total Gross Cost	78,101	10,000
Operational Excellence:		
Total Gross Cost	74,932	92,807
Total Program Costs	<u>\$ 9,297,177</u>	<u>\$ 9,919,104</u>
Less: earned revenues not attributed to programs	<u>(473,168)</u>	<u>(486,596)</u>
Net cost of operations	<u>\$ 8,824,009</u>	<u>\$ 9,432,508</u>

The accompanying notes are an integral part of these statements.

FEDERAL COMMUNICATIONS COMMISSION
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the Years Ended September 30, 2014 and 2013
(Dollars in thousands)

	Funds from Dedicated Collections (Note 10)			Funds from Dedicated Collections (Note 10)		
		All Other Funds	Total		All Other Funds	Total
Cumulative Results of Operations:						
Beginning Balances	\$ 6,884,853	\$ 161,389	\$ 7,046,242	\$ 6,622,985	\$ 148,527	\$ 6,771,512
Budgetary Financing Sources:						
Appropriations used	-	661	661	-	661	661
Non-exchange revenue	9,821,685	-	9,821,685	9,722,967	-	9,722,967
Other	1	-	1	67	(1)	66
Other Financing Sources (Non Exchange):						
Imputed financing	-	16,195	16,195	-	15,146	15,146
Other	-	(22,508)	(22,508)	-	(31,602)	(31,602)
Total Financing Sources	9,821,686	(5,652)	9,816,034	9,723,034	(15,796)	9,707,238
Net Cost of Operations	8,826,062	(2,053)	8,824,009	9,461,166	(28,658)	9,432,508
Net Change	995,624	(3,599)	992,025	261,868	12,862	274,730
Cumulative Results of Operations	7,880,477	157,790	8,038,267	6,884,853	161,389	7,046,242
Unexpended Appropriations:						
Beginning Balances	-	3,394	3,394	-	4,251	4,251
Budgetary Financing Sources:						
Appropriations received	-	351	351	-	-	-
Other adjustments	-	(25)	(25)	-	(196)	(196)
Appropriations used	-	(661)	(661)	-	(661)	(661)
Total Budgetary Financing Sources	-	(335)	(335)	-	(857)	(857)
Total Unexpended Appropriations	-	3,059	3,059	-	3,394	3,394
Net Position	\$ 7,880,477	\$ 160,849	\$ 8,041,326	\$ 6,884,853	\$ 164,783	\$ 7,049,636

The accompanying notes are an integral part of these statements.

FEDERAL COMMUNICATIONS COMMISSION

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2014 and 2013

(Dollars in thousands)

	FY 2014	FY 2013
Budgetary Resources:		
Unobligated balance brought forward, October 1	\$ 3,367,269	\$ 3,206,967
Recoveries of prior year unpaid obligations	461,521	927,684
Other changes in unobligated balance (+ or -)	(3,618)	(1)
Unobligated balance from prior year budget authority, net	3,825,172	4,134,650
Appropriations (discretionary and mandatory)	9,808,739	9,786,362
Borrowing authority (discretionary and mandatory)	3,616	1,496
Spending authority from offsetting collections (discretionary and mandatory)	450,637	450,669
Total budgetary resources	\$ 14,088,164	\$ 14,373,177
Status of Budgetary Resources:		
Obligations incurred (Note 12)	\$ 10,790,933	\$ 11,005,908
Unobligated balance, end of year:		
Apportioned	22,325	11,073
Exempt from apportionment	3,074,850	3,173,822
Unapportioned	200,056	182,374
Total unobligated balance, end of year	3,297,231	3,367,269
Total status of budgetary resources	\$ 14,088,164	\$ 14,373,177
Change in Obligated Balance:		
Unpaid obligations:		
Unpaid obligations, brought forward, Oct 1	\$ 4,052,196	\$ 3,581,685
Obligations incurred	10,790,933	11,005,908
Outlays (gross) (-)	(9,746,042)	(9,607,713)
Recoveries of prior year unpaid obligations (-)	(461,521)	(927,684)
Unpaid obligations, end of year	4,635,566	4,052,196
Uncollected payments:		
Uncollected payments, Fed sources, brought forward, Oct 1 (-)	(4,418)	(5,616)
Change in uncollected payments, Fed sources (+ or -)	148	1,198
Uncollected payments, Fed sources, end of year (-)	(4,270)	(4,418)
Memorandum (non-add) entries		
Obligated balance, start of year (+ or -)	\$ 4,047,778	\$ 3,576,069
Obligated balance, end of year (net)	\$ 4,631,296	\$ 4,047,778
Budget Authority and Outlays, Net:		
Budget authority, gross (discretionary and mandatory)	\$ 10,262,992	\$ 10,238,527
Actual offsetting collections (discretionary and mandatory) (-)	(459,857)	(481,038)
Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -)	148	1,198
Budget Authority, net (discretionary and mandatory)	\$ 9,803,283	\$ 9,758,687
Outlays, gross (discretionary and mandatory)	\$ 9,746,042	\$ 9,607,713
Actual offsetting collections (discretionary and mandatory) (-)	(459,857)	(481,038)
Outlays, net (discretionary and mandatory)	9,286,185	9,126,675
Distributed offsetting receipts (-)	(67,396)	(13,356)
Agency outlays, net (discretionary and mandatory)	\$ 9,218,789	\$ 9,113,319

The accompanying notes are an integral part of these statements.

FEDERAL COMMUNICATIONS COMMISSION
CONSOLIDATED STATEMENT OF CUSTODIAL ACTIVITY
For the Years Ended September 30, 2014 and 2013
(Dollars in thousands)

	<u>FY 2014</u>	<u>FY 2013</u>
Revenue Activity:		
Sources of Cash Collections:		
Spectrum Auctions	\$ 1,568,559	\$ 15,183
Fines and Penalties	42,099	25,287
Loan Payments	-	62
Total Cash Collections	<u>1,610,658</u>	<u>40,532</u>
Accrual Adjustments (+/-)		
Spectrum Auctions	-	(1,564)
Fines and Penalties	(4,855)	3,907
Total Accrual Adjustments	<u>(4,855)</u>	<u>2,343</u>
Total Custodial Revenue	1,605,803	42,875
Disposition of Collections:		
Transferred to Others:		
U.S. Treasury	(42,099)	(25,349)
Public Safety Trust Fund	(1,221,000)	-
(Increase)/Decrease in Amounts Yet to be Transferred (+/-)	(244,004)	81,213
Retained by the Reporting Entity	<u>(98,700)</u>	<u>(98,739)</u>
Total Disposition of Collections	(1,605,803)	(42,875)
Net Custodial Activity	<u>\$ -</u>	<u>\$ -</u>

The accompanying notes are an integral part of these statements.

NOTES TO THE PRINCIPAL FINANCIAL STATEMENTS

FOR THE YEARS ENDED SEPTEMBER 30, 2014 AND 2013

(Dollars in thousands unless otherwise stated)

Note 1 - Summary of Significant Accounting Policies

A. Reporting Entity

The Federal Communications Commission (Commission) is an independent United States Government agency, established by the Communications Act of 1934 (Act), as amended. The Commission is charged with regulating interstate and international communications by radio, television, wire, satellite, and cable. The Commission's jurisdiction spans the 50 states, the District of Columbia, and the U.S. possessions. Five commissioners direct the Commission; they are appointed by the President of the United States and confirmed by the Senate for five-year terms, except when filling an unexpired term or serving in holdover status.

The Commission is comprised of three reporting components. The primary component consists of Commission headquarters and field offices. The two additional components are the Universal Service Fund (USF) and the North American Numbering Plan (NANP). The USF reports the results of the four Universal Service support mechanisms (established pursuant to section 254 of the Act, as amended) and the results of the Telecommunications Relay Service (TRS) Fund (established by the Americans with Disabilities Act of 1990, Title IV). The NANP reports the results of billing and collection activities conducted to support the NANP (47 U.S.C. § 251(e); 47 C.F.R. § 52.16, 52.17, 52.32, and 52.33).

B. Basis of Accounting and Presentation

The consolidated and combined financial statements (financial statements) have been prepared from the accounting records of the Commission in conformity with U.S. generally accepted accounting principles (GAAP) and the form and content for Federal entity financial statements specified by the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*. Custodial activity reported on the Statement of Custodial Activity is prepared on the modified cash basis.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results may differ from those estimates.

C. Fund Balance with Treasury

Funds with the U.S. Department of the Treasury (Treasury) primarily represent general, revolving, and deposit funds. The Commission may use the general and revolving funds to finance expenses, depending on budgetary availability. The deposit accounts are used to hold funds temporarily until they can be properly disbursed or distributed.

Note 1 - Summary of Significant Accounting Policies (continued)

D. Cash and Other Monetary Assets

Cash and Other Monetary Assets represent third party deposits and demand deposits at several commercial banks which are maintained by Universal Service Administrative Company (USAC), Rolka Loube Saltzer Associates, LLC (RLSA), and Welch LLP, serving as administrators and/or billing and collection agents. Demand deposits bear the names of those entities, as well as the Commission or the fund for which they serve as administrator and/or billing and collection agent. Cash on deposit is collateralized by the Federal Reserve.

E. Investments

Investments are reported at their acquisition cost, adjusted for amortization of premiums or discounts using the Effective Interest Method. All investments are in Treasury securities.

F. Accounts Receivable, Net

Accounts Receivable consists of claims made for payment from the public and other Federal entities. Gross receivables are reduced to net realizable value by an allowance for doubtful accounts. The Commission's portion of the allowance for doubtful accounts is determined by applying predetermined percentages against the respective date the receivable was established. An additional analysis of higher dollar value receivables is also performed on individual account balances.

The following chart summarizes the formula for the allowance with related outstanding days:

<u>Accounts Receivable Age</u>	<u>Allowance</u>
90 Days and Less	0%
91 - 180 Days	25%
181 - 365 Days	75%
Over 365 Days	100%

The USF portion of the allowance is determined by calculating an estimated general allowance for doubtful accounts receivable. The general allowance is calculated by multiplying the receivable amounts by the percentage of the estimated uncollectible amount as determined by a review of historical collection rates by type of receivable.

G. Property, Plant and Equipment

The basis for recording purchased general Property, Plant, and Equipment (PP&E) is full cost, including all costs incurred to bring the PP&E to and from a location suitable for its intended use. The capitalization threshold is \$100 for PP&E and \$200 for internally developed software with an estimated useful life of two years or more. There is no capitalization of bulk purchases of similar items. PP&E are depreciated on a straight-line basis over the estimated useful lives of the items.

Note 1 - Summary of Significant Accounting Policies (continued)

G. Property, Plant and Equipment (continued)

The following chart summarizes the PP&E classifications with related estimated useful lives:

<u>PP&E Classification</u>	<u>Estimated Useful Lives (years)</u>
Building	40
Non-Computer Equipment	7
Computer & Vehicle Equipment	5
Software	3

Land, including permanent improvements, and software in development are not depreciated. Normal maintenance and repair costs are expensed as incurred.

Leasehold improvement, which includes all cost incurred during the design and construction phase of the improvement, are either amortized over the remaining life of the lease or the useful life of the improvement, whichever is shorter.

H. Other Assets

Other Assets with agencies represent advance payments for intragovernmental agreements. Other Assets with the public represent the balance of transfers less expenses made by the USF to USAC to fund administrative costs in advance. Advances are drawn down as expenses are incurred.

I. Accounts Payable and Accrued Liabilities

Accounts Payable and Accrued Liabilities represent a probable future outflow or other sacrifice of resources as a result of past transactions or events. Liabilities are recognized when they are incurred, regardless of whether they are covered by available budgetary resources. Liabilities cannot be liquidated without legislation that provides resources to do so. As a component of the U.S. Government, a sovereign entity, payments of all liabilities other than contracts can be abrogated by the sovereign entity. Accrued Liabilities for Universal Service mostly represent liabilities recorded by the USF for anticipated subsidies in the High Cost, Lifeline (formerly known as Low Income), and TRS programs. The obligation for these subsidies is not recognized until payment files are approved in the subsequent month.

J. Deferred Revenue

The Commission collects proceeds from the sale of communications spectrum on behalf of the U.S. Government. All proceeds collected up to the amount of the net winning bid are recognized as deferred revenue until a “prepared to grant” or “grant” public notice is issued. In addition, the Commission collects multi-year regulatory fees for five and ten-year periods that are recorded as deferred revenue and amortized over the period of the fee.

Note 1 - Summary of Significant Accounting Policies (continued)

J. Deferred Revenue (continued)

The USF and NANP collect contributions from U.S., Canadian, and Caribbean carriers to cover the costs of the programs. Some carriers have the option of paying monthly or annually. The unearned portion of annual contributions is recognized as deferred revenue.

K. Debt

Debt represents amounts due to the U.S. Treasury's Bureau of the Fiscal Service (BFS) to support the spectrum auction loan program. Borrowings from BFS are determined based on subsidy estimates and reestimates in accordance with the Federal Credit Reform Act (FCRA) of 1990, as amended, and OMB guidance. Interest payments on debt are calculated annually and remitted to BFS at the end of the fiscal year. These payments are recorded in a receipt account maintained by the Commission. The spectrum auction loan program has been discontinued.

L. Retirement Plans and Other Benefits

Federal employee benefits consist of the actuarial portion of future benefits earned by Federal employees, including pensions, other retirement benefits, and other post-employment benefits. The Office of Personnel Management (OPM) administers these benefits. The Commission does not recognize any liability on the Balance Sheet for pensions, other retirement benefits, and other post-employment benefits.

The Commission recognizes and allocates the imputed costs on the Statement of Net Cost and recognizes imputed financing related to these costs on the Statement of Changes in Net Position.

Pensions provide benefits upon retirement and may also provide benefits for death, disability, or other separations from employment before retirement. Pension plans may also include benefits to survivors and dependents, and they may contain early retirement or other special features. Most Commission employees participate in the Civil Service Retirement System (CSRS), the Federal Employee Retirement System (FERS), the FERS-Revised Annuity Employee (RAE), or the FERS-Further Revised Annuity Employee (FRAE). Under CSRS, the Commission makes matching contributions equal to seven percent of basic pay. Under all FERS plans, the Commission contributes the employer's matching share for Social Security. All employees are eligible to contribute to the Thrift Saving Plan (TSP) which is a defined contribution retirement savings and investment plan. For those employees covered by the FERS plans, a TSP account is automatically established to which the commission is required to contribute 1% of gross pay and match dollar-for-dollar on the first 3% of pay contributed each pay period and 50 cents on the dollar for the next 2% of pay contributed. No government contributions are made to the TSP accounts established by CSRS employees. Most employees hired after December 31, 1983, are covered by the FERS plans.

Note 1 - Summary of Significant Accounting Policies (continued)

L. Retirement Plans and Other Benefits (continued)

The OPM reports on CSRS, FERS, FERS-RAE, and FERS-FRAE assets, accumulated plan benefits, and unfunded liabilities, if any, applicable to Federal employees.

The actuarial liability for future workers' compensation benefits payable includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, as well as a component for incurred but not reported claims. The liability is determined using historical benefit payment patterns related to injury years to predict the ultimate payment. The Department of Labor (DOL) determines no actuarial liability for the Commission due to the immateriality to the Federal Government as a whole.

The unfunded Federal Employees' Compensation Act (FECA) liability covers compensation and medical benefits for work related injury. The calculation takes the amount of benefit payments over the last nine to twelve quarters and then calculates the annual average of payments. The compensation and medical payments can be found in the chargeback reports that are issued by DOL.

M. Leave

Annual leave is accrued as earned, and the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current leave balances and pay rates. Annual leave is reflected as a liability not covered by current budgetary resources. Sick leave and other types of non-vested leave are expensed as taken.

N. Revenue and Other Financing Sources

Regulatory Fee Offsetting Collections (Exchange) – The Omnibus Budget Reconciliation Act of 1993 directed the Commission to assess and collect regulatory fees to recover the costs incurred in carrying out certain provisions of its mission. Section 9(a) of the Act, as amended, authorizes the Commission to assess and collect annual regulatory fees to recover the costs, as determined annually by Congress, incurred in carrying out its strategic goals: Connect America; Maximize Benefits of Spectrum; Protect and Empower Consumers; Promote Innovation, Investment, and America's Global Competitiveness; Promote Competition; Public Safety and Homeland Security; Advance Key National Purposes; and Operational Excellence. These fees were established by congressional authority, and consistent with OMB Circular No. A-25 revised, *User Charges*, the Commission did not determine the full costs associated with its regulatory activity in establishing regulatory fees. Since 1993, Congress has annually reviewed the regulatory fee collection requirements of the Commission and established the total fee levels to be collected. Fees collected up to the level established by Congress are applied against the Commission's appropriation at the close of each fiscal year. The regulatory fee levels of \$339,844 for FY 2014 and FY 2013 were achieved. The Commission collected \$8,720 above the required regulatory level in FY 2014 and \$10,933 in FY 2013. The cumulative amount collected above the required annual regulatory level is \$90,697 at September 30, 2014. In addition, the

Note 1 – Summary of Significant Accounting Policies (continued)

N. Revenue and Other Financing Sources (continued)

cumulative amount collected above the required annual regulatory level has been temporarily precluded from obligation since FY 2008.

Competitive Bidding System Offsetting Collections (Exchange) – One of the Commission’s primary functions is managing the spectrum auction program. Proceeds from the auctions are initially remitted to the Commission and are later transferred to either the U.S. Treasury or the appropriate agency required by Public Law, net of anticipated auction related costs (under 47 U.S.C. § 309, the Commission may retain a portion of the spectrum auction proceeds to offset the cost of performing the auction function). Collections used to offset the cost of performing auctions-related activity were appropriated at \$98,700 in FY 2014 and \$98,739 in FY 2013.

Radio Spectrum Auction Proceeds (Exchange) – In accordance with the provisions of Statement of Federal Financial Accounting Standards (SFFAS) 7, *Accounting for Revenue and Other Financing Sources*, the Commission accounts for this exchange revenue as a custodial activity. Revenue from spectrum auctions is recognized when a “prepared to grant” or “grant” public notice is issued. The value of available spectrum is determined in the market place at the time of auction. The Commission recognized total custodial revenue related to spectrum auctions, net of accrual adjustments, of \$1,568,559 in FY 2014 and \$13,619 in FY 2013. In FY 2014, the Commission transferred recognized custodial revenue of \$1,221,000 to the Public Safety Trust Fund that is managed by the National Telecommunications and Information Administration.

Application Fees (Exchange) – Congress authorized the Commission (47 U.S.C. § 8) to collect application processing fees and directed the Commission to prescribe charges for certain types of application processing or authorization services over which the Commission has jurisdiction. Section 8(b) of the Act, as amended, requires the Commission to review and amend its application fees every two years. The amended fees (Schedule of Application Fees 14 U.S.C. § 1.1102 *et seq.*) reflect the net change in the Consumer Price Index for all Urban Consumers calculated over a specific period of time, and the Commission’s cost of processing applications and associated filings. Application fees are deposited in the Treasury and are not available for the Commission’s use. Application fee revenue totaled \$22,509 in FY 2014 and \$27,985 in FY 2013.

Reimbursable Work Agreements (Exchange) – The Commission recognizes reimbursable work agreement revenue when earned, i.e., goods that have been delivered or services rendered. The Commission executed agreements totaling \$2,782 in FY 2014 and \$4,168 in FY 2013.

Allocation of Exchange Revenues

The Commission reports the entire balance of exchange revenue on line "Less: earned revenues not attributed to programs" since there is no direct relationship between earned revenues and specific programs.

Note 1 – Summary of Significant Accounting Policies (continued)

N. Revenue and Other Financing Sources (continued)

USF (Nonexchange) – Carriers conducting interstate telecommunications are required to contribute a portion of their revenues to fund the cost of providing universal service. These contributions represent dedicated collections and are accounted for as a budgetary financing source. Total contributions of \$9,783,416 and \$9,676,818 were received in FY 2014 and FY 2013, respectively.

Appropriations (Financing Source) – The Commission receives a Salaries and Expense appropriation from Congress. These funds are used to pay for operations during the fiscal year and are repaid to the Treasury once regulatory fees are collected. In FY 2014, Congress authorized the Commission to retain its appropriation as available until expended. The no-year appropriation for FY 2014 is \$339,844 and the annual appropriation for FY 2013 was \$339,844, which included a temporary reduction of \$17,096 due to the sequestration order implemented on March 1, 2013 and required by the Budget Control Act of 2011. Regulatory fee collections fully fund the no-year appropriation for FY 2014 and the annual appropriation for FY 2013.

Subsidy Estimates and Reestimates (Financing Source) – The FCRA of 1990, as amended, governs the reporting requirements for direct loan obligations made after FY 1991. As required, the Commission coordinates with OMB in developing estimation guidelines, regulations, and the criteria used in calculating the subsidy estimates and reestimates. In FY 2014 the Commission received an appropriation of \$351, of which \$25 was permanently sequestered and the remainder was available until used. In FY 2013, the Commission did not receive an appropriation since there was no upward reestimate component. The last active loan matured in April 2007 and the Commission wrote off all remaining loans in FY 2013. As result, there was no material activity related to direct loans in FY 2014, and the Commission is working with OMB to close-out the Credit Reform Program.

O. Reprogramming

In FY 2014, the Commission did not reprogram any funds. In FY 2013, the Commission received approval to reprogram \$8,433 of prior year de-obligations to fund a number of projects. The projects include settlements of legal claims, compensation and benefits, capital improvements, and information technology investments.

P. Transactions with Related Parties

The Commission has a direct oversight relationship with the administrators and Billing and Collection agents (B&C agents) of funds that are components under the overall Commission entity. These organizations are USAC, which is both the administrator and B&C agent for the four USF support mechanisms; RLSA, which is both the administrator and B&C agent for TRS; Neustar which is the administrator for NANP; and Welch LLP which is the B&C agent for NANP.

Note 1 – Summary of Significant Accounting Policies (continued)

P. Transactions with Related Parties (continued)

The Commission approves the administrative costs paid to these entities from the respective funds that they manage. The administrative costs cover expenses such as the salaries and benefits for the employees dedicated to managing the funds; rent and utilities for office space used; accounting and other financial reporting related services; and other management activities. All related party balances for the fiscal years ended September 30, 2014 and 2013 are listed below:

Administrative Fees:

	<u>USF</u>	<u>TRS</u>	<u>NANP</u>	<u>Total</u>
FY 2014	\$ 116,771	\$ 1,302	\$ 6,205	\$ 124,278
FY 2013	\$ 111,112	\$ 1,107	\$ 5,762	\$ 117,981

Q. Net Position

Net Position is the residual difference between assets and liabilities, and is comprised of Unexpended Appropriations and Cumulative Results of Operations. Unexpended Appropriations represents the amount of unobligated and unexpended budget authority. Unobligated Balance is the amount of appropriations or other authority remaining after deducting the cumulative obligations from the amount available for obligation. Cumulative Results of Operations is the net difference since the inception of the Commission of (1) expenses and losses and (2) financing sources including appropriations used, revenues, and gains.

R. Comparability of the Financial Statements

Consolidated Statement of Net Cost – In FY 2014, with significant reforms made in USF programs, the Commission developed a more comprehensive methodology that better aligns USF program costs with the strategic goals of the Commission. In FY 2013 and prior, all USF program costs were allocated to the strategic goal - Promote Competition. Allocation of TRS program costs to the strategic goal - Promote Competition did not change.

Accounts Receivable, Net (Note 6) – Prior to FY2014, Notice of Apparent Liabilities (NAL) receivables were included in the second table in Note 6 - Accounts Receivable, Net, under the Forfeiture category. The ability to collect these receivables was not determinable until a final judgment was issued. As such, a 100% allowance was established for all NAL receivables. In FY 2014, the Commission implemented a new policy to exclude NAL receivables from the Accounts Receivable balance until their collectability is determined by one of the following events: a final judgment is issued and the NAL becomes either a Forfeiture Order or a Consent Decree, the violator has made either a partial or full payment on the NAL, or the violator has signed an installment plan for the NAL. All new and existing NAL receivables will continue to be tracked by the Commission. For comparability purposes, the FY 2013 amount excludes NAL

Note 1 – Summary of Significant Accounting Policies (continued)

R. Comparability of the Financial Statements (continued)

receivables. Because NAL receivables were presented with a 100% allowance, the net effect on the balance sheet from this change is \$0.

Note 2 - Non-entity Assets

The following summarizes Non-entity Assets as of September 30, 2014 and 2013:

	<u>FY 2014</u>	<u>FY 2013</u>
Intragovernmental:		
Fund Balance with Treasury	\$ 322,815	\$ 78,415
Accounts Receivable	377	433
Total Intragovernmental	<u>323,192</u>	<u>78,848</u>
Cash and Other Monetary Assets	17	-
Accounts Receivable, Net	<u>14,914</u>	<u>25,620</u>
Total Non-entity Assets	338,123	104,468
Total Entity Assets	8,959,140	8,465,756
Total Assets	<u>\$ 9,297,263</u>	<u>\$ 8,570,224</u>

Non-entity Fund Balance with Treasury primarily represents deposits made towards spectrum auction winning bids. These deposits accounted for \$321,851 in FY 2014 and \$76,432 in FY 2013. Receivables considered non-entity are for regulatory fees, application fees, fines and forfeitures, spectrum auction receivables, and International Telecommunications Settlement (ITS) charges.

Note 3 - Fund Balance with Treasury

The following summarizes Fund Balance with Treasury (FBWT) as of September 30, 2014 and 2013:

FY 2014

<u>FY 2014</u>	Revolving				
	General Funds	Funds	Deposit Funds	Total	
Unobligated Balance					
Available	\$ 23,116	\$ 3,230	\$ -	\$ 26,346	
Unavailable	109,934	-	-	109,934	
Obligated Balance not yet Disbursed	78,889	-	-	78,889	
Non-Budgetary FBWT	-	-	322,815	322,815	
Total	\$ 211,939	\$ 3,230	\$ 322,815	\$ 537,984	

FY 2013

Unobligated Balance					
Available	\$	19,378	\$	6,833	\$ - \$ 26,211
Unavailable		103,329		-	- 103,329
Obligated Balance not yet Disbursed		71,208		-	- 71,208
Non-Budgetary FBWT		-		-	78,415 78,415
Total	\$	193,915	\$	6,833	\$ 78,415 \$ 279,163

General Funds – Includes the salaries and expense appropriation used to fund agency operations, the auction and reimbursable accounts, the credit reform program account, and the no-year accounts used to carry over spectrum auction funds, offsetting collections, excess regulatory fees, and the Office of Inspector General USF funds.

Revolving Funds – Includes the credit reform financing account used to record cash flows associated with the Commission's spectrum auction loan program.

Deposit Funds – Includes monies being held for spectrum auctions, ITS, and regulatory fees. Deposit funds are non-budgetary and are not available for use by the Commission unless they are properly identified or reclassified as Commission funds. Otherwise, these funds are returned to the depositor or transferred to the U.S. Treasury.

Note 4 – Cash and Other Monetary Assets

The following summarizes Cash and Other Monetary Assets as of September 30, 2014 and 2013:

	FY 2014	FY 2013
Cash and Other Monetary Assets	<u>\$ 181,519</u>	<u>\$ 173,084</u>

Note 4 – Cash and Other Monetary Assets (continued)

USF and NANP contributions and third party deposits made pursuant to spectrum auction activities are the sources of funds for these balances. Third-party deposits, unless refunded, are held until 45 days after the close of a given auction and then transferred to the Commission's Treasury account. Interest earned on USF and NANP contribution is reinvested. Interest earned on third-party deposits is transferred to the Treasury's General Fund.

In FY 2014, Cash and Other Monetary Assets included \$17 in upfront spectrum auctions payments, \$177,834 in USF contributions and related accrued interest being held for distribution, and \$3,668 in NANP deposits and related accrued interest. In FY 2013, Cash and Other Monetary Assets included \$170,085 in USF contributions and related accrued interest being held for distribution, and \$2,999 in NANP deposits and related accrued interest.

Note 5 - Investments

The following summarizes Investments as of September 30, 2014 and 2013:

	Purchase Cost	Amortization Method	Amortized (Premium) Discount	Interest Receivable	Investments, Net	Market Value Disclosures
<u>FY 2014</u>						
Intragovernmental Securities:						
Marketable Securities						
Treasury Bills	\$ 728,577	EI	\$ 12	\$ -	\$ 728,589	\$ 728,586
Treasury Notes	6,974,719	EI	(26,155)	8,630	6,957,194	6,951,496
Total	<u>\$ 7,703,296</u>		<u>\$ (26,143)</u>	<u>\$ 8,630</u>	<u>\$ 7,685,783</u>	<u>\$ 7,680,082</u>
<u>FY 2013</u>						
Intragovernmental Securities:						
Marketable Securities						
Treasury Bills	\$ 1,287,513	EI	\$ 29	\$ -	\$ 1,287,542	\$ 1,287,533
Treasury Notes	5,913,637	EI	(7,179)	6,600	5,913,058	5,901,937
Total	<u>\$ 7,201,150</u>		<u>\$ (7,150)</u>	<u>\$ 6,600</u>	<u>\$ 7,200,600</u>	<u>\$ 7,189,470</u>

EI - Effective Interest Method

All Treasury securities, regardless of the maturity date, are reported as investments. The Commission expects to hold all investments to maturity; therefore, no adjustments have been made to present market values. All investments are held by USF and are also recognized as part of Funds from Dedicated Collections in Note 10.

The cash receipts collected from the public for the USF are used to purchase federal securities. Treasury securities are an asset to the USF and a liability to the Treasury. Because the USF and the Treasury are both part of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Government-wide financial statements.

Note 5 – Investments (continued)

Treasury securities provide the USF with authority to draw upon the Treasury to make future benefit payments or other expenditures. When the USF requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the Government finances all other expenditures.

Note 6 - Accounts Receivable, Net

The following summarizes Accounts Receivable, Net as of September 30, 2014 and 2013:

	Intragovernmental	Public	Total
FY 2014			
Gross Accounts Receivable	\$ 711	\$ 1,445,662	\$ 1,446,373
Allowance for Doubtful Accounts	-	(602,926)	(602,926)
Accounts Receivable, Net	<u>\$ 711</u>	<u>\$ 842,736</u>	<u>\$ 843,447</u>
FY 2013			
Gross Accounts Receivable	\$ 1,235	\$ 1,531,446	\$ 1,532,681
Allowance for Doubtful Accounts	-	(679,420)	(679,420)
Accounts Receivable, Net	<u>\$ 1,235</u>	<u>\$ 852,026</u>	<u>\$ 853,261</u>

The Commitment Adjustment (COMAD) for Schools and Libraries audit receivables are subject to appeal and are not considered final until the appeals period has lapsed or a final determination has been issued. The COMAD audit receivables for Schools and Libraries have a 91% allowance in FY 2014 and 95% allowance in FY 2013.

The following summarizes accounts receivable by type as of September 30, 2014 and 2013:

	FY 2014			FY 2013		
	Accounts Receivable	Allowance	Net	Accounts Receivable	Allowance	Net
USF	\$ 1,219,144	\$ (403,950)	\$ 815,194	\$ 1,303,849	\$ (483,749)	\$ 820,100
COMAD - Schools and Libraries	133,391	(121,119)	12,272	123,145	(117,357)	5,788
Regulatory Fees	35,644	(28,901)	6,743	40,708	(28,771)	11,937
Spectrum Auction	21,081	(21,081)	-	21,568	(21,568)	-
Civil Monetary Penalties	26,247	(19,106)	7,141	27,861	(18,512)	9,349
Other	10,866	(8,769)	2,097	15,550	(9,463)	6,087
Total	<u>\$ 1,446,373</u>	<u>\$ (602,926)</u>	<u>\$ 843,447</u>	<u>\$ 1,532,681</u>	<u>\$ (679,420)</u>	<u>\$ 853,261</u>

Note 7 - Liabilities Not Covered by Budgetary Resources

The following summarizes Liabilities Not Covered by Budgetary Resources as of September 30, 2014 and 2013:

	<u>FY 2014</u>	<u>FY 2013</u>
Intragovernmental:		
FECA Liability	\$ 521	\$ 441
Unemployment Liability	42	-
GSA Real Estate Taxes	2,184	2,357
Other:		
Unfunded Leave	20,427	20,734
Accrued Liabilities for Universal Service	<u>670,755</u>	<u>1,088,415</u>
Total liabilities not covered by budgetary resources	693,929	1,111,947
Total liabilities covered by budgetary resources	<u>562,008</u>	<u>408,641</u>
Total Liabilities	<u>\$ 1,255,937</u>	<u>\$ 1,520,588</u>

Liabilities not covered by budgetary resources are liabilities incurred that are not covered by realized budgetary resources as of the Balance Sheet date.

Note 8 - Other Liabilities

The following summarizes Other Liabilities as of September 30, 2014 and 2013:

<u>FY 2014</u>	<u>Non-Current</u>	<u>Current</u>	<u>Total</u>
Intragovernmental			
Custodial Liability	\$ -	\$ 325,448	\$ 325,448
Other	-	4,831	4,831
Total Intragovernmental	<u>\$ -</u>	<u>\$ 330,279</u>	<u>\$ 330,279</u>
Deferred Revenue	\$ 35,763	\$ 20,757	\$ 56,520
Prepaid Contributions	-	47,625	47,625
Accrued Liabilities for Universal Service	-	670,755	670,755
Other	-	33,338	33,338
Total Other	<u>\$ 35,763</u>	<u>\$ 772,475</u>	<u>\$ 808,238</u>
<u>FY 2013</u>	<u>Non-Current</u>	<u>Current</u>	<u>Total</u>
Intragovernmental			
Custodial Liability	\$ -	\$ 81,444	\$ 81,444
Other	-	8,114	8,114
Total Intragovernmental	<u>\$ -</u>	<u>\$ 89,558</u>	<u>\$ 89,558</u>
Deferred Revenue	\$ 35,400	\$ 24,520	\$ 59,920
Prepaid Contributions	-	110,057	110,057
Accrued Liabilities for Universal Service	-	1,088,415	1,088,415
Other	-	35,036	35,036
Total Other	<u>\$ 35,400</u>	<u>\$ 1,258,028</u>	<u>\$ 1,293,428</u>

The Custodial Liability includes both cash collected and receivables being held for transfer to the Treasury's General Fund. The Commission collects the following types of custodial revenue: spectrum auction revenue, fines and forfeitures revenue, penalty revenue on regulatory fees, ITS processing fees, and interest revenue on auction deposits. Deferred revenue represents regulatory fees, spectrum auction revenue, or contributor payments that have been received but not earned by the Commission.

Prepaid Contributions include USF and NANP contribution overpayments that may be refunded or used to offset future payments. Accrued Liabilities for Universal Service mostly represent liabilities recorded by the USF for anticipated subsidies in the High Cost, Lifeline (formerly known as Low Income), and TRS programs. The obligation for these subsidies is not recognized until payment files are approved in the subsequent month. Remaining Other Liabilities primarily represent anticipated payments related to payroll and other services, and upfront deposits made by auction bidders as well as funds received that are being held until proper application is determined.

Note 9 - Commitments and Contingencies

The Commission, USAC, and the Department of Justice are investigating several cases and prosecuting others related to disbursements of USF funds from the Schools and Libraries, High Cost, and Lifeline programs, which might result in future proceedings or actions. Similarly the Commission, RLSA, and the Department of Justice are investigating several cases related to the TRS funds. The complexity of these future actions precludes management from estimating the total amount of recovery that may result.

The Commission is a party in various administrative proceedings, legal actions, and claims brought by or against the agency. In the opinion of Commission management, the ultimate resolution of proceedings, actions and claims will not materially affect the Commission's financial position or results of operations.

The Commission has examined its obligations related to cancelled authority and believes it has no outstanding commitments requiring future resources other than those as disclosed in Note 7. In addition, there are certain operating leases that may contain provisions regarding contract termination costs upon early contract termination. In the opinion of Commission management, early contract termination will not materially affect the Commission's financial statements.

As of September 30, 2014, there exist contingent liabilities against the Commission with a reasonable possibility of an unfavorable outcome. The amount that will ultimately be paid, if any, totals less than \$4,000. We have determined that the resolution of these reportable contingent liabilities should not have a material effect on the financial statements.

In September 2007, a grievance was filed with the Commission under the Federal Labor Standards Act alleging that certain Commission bargaining unit employees were not sufficiently compensated for overtime work. In FY 2013, the Commission entered into an agreement with the National Treasury Employee Union (NTEU) to settle the overtime claims. Based on the raw data provided by the NTEU, the Commission determined the total back pay and liquidated damage to be \$1,170. In FY 2014, a total amount of \$1,103 was paid to the employees. There are several employees who are contesting the accuracy of their back pay calculations. Any resulting amount should not have a material effect on the financial statements.

Note 10 – Funds from Dedicated Collections

U.S. telecommunications companies are obligated to make contributions to the USF and the TRS. These contributions are accounted for in the Budget of the U.S. Government as the "Universal Service Fund." The Commission currently recognizes the contributions collected under the USF Program as non-exchange revenue on its Statement of Changes in Net Position, and the related disbursements as program expenses on the Statement of Net Cost.

Note 10 – Funds from Dedicated Collections (continued)

The following summarizes the significant assets, liabilities, and related costs incurred with managing the USF Program as of September 30, 2014 and 2013:

Balance Sheet	FY 2014	FY 2013
Assets:		
Investments	\$ 7,685,783	\$ 7,200,600
Cash and other monetary assets	177,834	170,085
Accounts receivable, net	828,493	827,903
General property, plant, and equipment, net	4,988	3,999
Other assets	13,024	13,024
Total assets	<u>\$ 8,710,122</u>	<u>\$ 8,215,611</u>
Liabilities:		
Accounts payable	\$ 105,080	\$ 125,046
Deferred revenue	6,224	7,262
Prepaid contributions	47,586	110,035
Accrued liabilities	670,755	1,088,415
Total liabilities	<u>\$ 829,645</u>	<u>\$ 1,330,758</u>
Cumulative results of operations	<u>\$ 7,880,477</u>	<u>\$ 6,884,853</u>
Total liabilities and net position	<u>\$ 8,710,122</u>	<u>\$ 8,215,611</u>
Statement of Net Cost		
Net cost of operations	<u>\$ 8,826,062</u>	<u>\$ 9,461,166</u>
Statement of Changes in Net Position		
Net position beginning of period	\$ 6,884,853	\$ 6,622,985
Non-exchange revenue	9,821,685	9,722,967
Other financing sources	1	67
Net cost of operations	8,826,062	9,461,166
Change in net position	<u>995,624</u>	<u>261,868</u>
Net position end of period	<u>\$ 7,880,477</u>	<u>\$ 6,884,853</u>

Note 11 – Intragovernmental Costs and Exchange Revenue

Intragovernmental costs primarily represent goods and services purchased by the Commission from other Federal agencies.

FY 2014

Program Costs	Intragovernmental	Public	Total
Connect America	\$ 10,990	\$ 35,390	\$ 46,380
Maximize Benefits of Spectrum	28,356	82,206	110,562
Protect and Empower Consumers	12,634	36,625	49,259
Promote Innovation, Investment, and America's Global Competitiveness	2,652	7,689	10,341
Promote Competition	26,819	8,857,682	8,884,501
Public Safety and Homeland Security	11,054	32,047	43,101
Advance Key National Purposes	7,505	70,596	78,101
Operational Excellence	19,218	55,714	74,932
Total	<u>\$ 119,228</u>	<u>\$ 9,177,949</u>	<u>\$ 9,297,177</u>
Total Earned Revenue	<u>\$ 2,964</u>	<u>\$ 470,204</u>	<u>\$ 473,168</u>

FY 2013

Program Costs	Intragovernmental	Public	Total
Connect America	\$ 12,563	\$ 34,474	\$ 47,037
Maximize Benefits of Spectrum	21,275	58,380	79,655
Protect and Empower Consumers	13,930	38,225	52,155
Promote Innovation, Investment, and America's Global Competitiveness	2,590	7,107	9,697
Promote Competition	30,288	9,550,106	9,580,394
Public Safety and Homeland Security	12,649	34,710	47,359
Advance Key National Purposes	2,671	7,329	10,000
Operational Excellence	24,789	68,018	92,807
Total	<u>\$ 120,755</u>	<u>\$ 9,798,349</u>	<u>\$ 9,919,104</u>
Total Earned Revenue	<u>\$ 4,491</u>	<u>\$ 482,105</u>	<u>\$ 486,596</u>

Note 12 - Apportionment Categories of Obligations Incurred: Direct vs. Reimbursable Obligations

The following summarizes Apportionment Categories of Obligations Incurred for the years ended September 30, 2014 and 2013:

	FY 2014	FY 2013
Direct:		
Category A	\$ -	\$ 422,882
Category B	1,370,430	741,530
Exempt from Apportionment	9,417,463	9,838,207
Total Direct	10,787,893	11,002,619
Reimbursable:		
Category A	-	3,289
Category B	3,040	-
Total Obligations Incurred	\$ 10,790,933	\$ 11,005,908

Category A - Apportioned by Quarter

Category B - Apportioned by Purpose

Note 13 – Undelivered Orders at the End of the Period

The amount of budgetary resources obligated for undelivered orders totaled \$4,518,678 as of September 30, 2014 and \$3,917,916 as of September 30, 2013.

Note 14 – Permanent Indefinite Appropriations

Pursuant to 47 U.S.C §§ 254 and 225 the FCC has a permanent indefinite appropriation to fund its universal service programs, including Telecommunications Relay Service Fund. These programs operate by collecting mandatory contributions from telecommunications carriers providing interstate telecommunications services, and from other providers of interstate telecommunications required to contribute if the public interest so requires. These contributions are accounted for federal budgetary purposes as a special fund known as the Universal Service Fund.

Note 15 – Legal Arrangements Affecting Use of Unobligated Balances

Pursuant to Public Laws, offsetting collections received in excess of \$339,844 in FY 2014 and in FY 2013 are temporarily precluded from obligation. In addition, the cumulative amount collected above the required annual regulatory level has been temporarily precluded from obligation since FY 2008. For more information, refer to Note 1-N.

Note 16 - Explanation of Differences Between the Statement of Budgetary Resources (SBR) and the Budget of the U.S. Government

There were no material differences between the Combined Statement of Budgetary Resources (SBR) for FY 2013 and the amounts presented in the 2015 President's Budget. The FY 2016 *Budget of the United States Government* (President's Budget) with actual numbers for FY 2014 has not been published. Pursuant to 31 USC § 1105, the *Budget of the United States Government* will be released the first Monday in February, and will be available at the following website: <http://www.whitehouse.gov/omb>.

Note 17 – Reconciliation of Net Cost of Operations (Proprietary) to Budget (Formerly the Statement of Financing)

As of September 30, 2014 and 2013:

	FY 2014	FY 2013
Budgetary Resources Obligated:		
Obligations incurred	\$ 10,790,933	\$ 11,005,908
Less: spending authority from offsetting collections and recoveries	921,230	1,407,524
Obligations net of offsetting collections and recoveries	9,869,703	9,598,384
Less: offsetting receipts	67,396	13,356
Net obligations	9,802,307	9,585,028
Other Resources	(6,312)	(16,389)
Resources Used to Finance Items not Part of the Net Cost of Operations:		
Change in Undelivered Orders	(600,762)	(454,726)
Budgetary offsetting collections and receipts that do not affect net cost of operations	67,899	17,014
Resources that finance the acquisition of assets	(6,170)	(9,822)
Other	(38,975)	(30,067)
Components of the Net Cost of Operations That Will Not Require or Generate Resources in the Current Period:		
Increase in annual leave liability	(265)	282
Upward/Downward reestimates of credit subsidy (+/-)	-	(3,265)
Increase in exchange revenue receivable from the public	5,945	758
Depreciation and amortization	20,029	19,064
Other (+/-)	(419,687)	324,631
Net Cost of Operations	\$ 8,824,009	\$ 9,432,508

REQUIRED SUPPLEMENTARY INFORMATION

REQUIRED SUPPLEMENTARY INFORMATION – SCHEDULE OF BUDGETARY RESOURCES BY MAJOR ACCOUNT

For the Years Ended September 30, 2014 and 2013
(Dollars in thousands)

OMB Circular No. A-136, *Financial Reporting Requirements*, requires additional disclosure of an entity's budgetary information by major budgetary accounts if the information was aggregated for presentation purposes on the Statement of Budgetary Resources. Major budgetary accounts of the Commission include Salaries and Expenses (S&E), Auctions, and USF. S&E represents general salaries and expenses of the Commission. Auctions include salaries and expenses of the spectrum auction program. USF includes Universal Service Fund and Telecommunications Relay Service Funds.

In FY 2014, there is minimal activity related to the Credit Reform account. As a result, it is no longer considered a major budgetary account of the Commission. Non-major budgetary accounts are aggregated under Other.

Reflected in the charts on the next two pages are the major budgetary accounts of the Commission that are aggregated and presented in the September 30, 2014 and 2013 Combined Statement of Budgetary Resources.

SCHEDULE OF BUDGETARY RESOURCES BY MAJOR ACCOUNT

FY 2014

	S&E	Auctions	USF	Other	Total
Budgetary Resources:					
Unobligated balance brought forward, October 1	\$ 17,942	\$ 737	\$ 3,338,493	\$ 10,097	\$ 3,367,269
Recoveries of prior year unpaid obligations	2,956	4,951	453,600	14	461,521
Other changes in unobligated balance (+ or -)	3,852	(3,852)	-	(3,618)	(3,618)
Unobligated balance from prior year budget authority, net	24,750	1,836	3,792,093	6,493	3,825,172
Appropriations (discretionary and mandatory)	-	-	9,808,413	326	9,808,739
Borrowing authority (discretionary and mandatory)	-	-	-	3,616	3,616
Spending authority from offsetting collections (discretionary and mandatory)	343,237	98,788	8,458	154	450,637
Total budgetary resources	\$ 367,987	\$ 100,624	\$ 13,608,964	\$ 10,589	\$ 14,088,164
Status of Budgetary Resources:					
Obligations incurred	\$ 346,340	\$ 97,139	\$ 10,343,006	\$ 4,448	\$ 10,790,933
Unobligated balance, end of year:					
Apportioned	17,784	1,761	-	2,780	22,325
Exempt from apportionment	-	-	3,074,850	-	3,074,850
Unapportioned	3,863	1,724	191,108	3,361	200,056
Total unobligated balance, end of year	21,647	3,485	3,265,958	6,141	3,297,231
Total status of budgetary resources	\$ 367,987	\$ 100,624	\$ 13,608,964	\$ 10,589	\$ 14,088,164
Change in Obligated Balance:					
Unpaid obligations:					
Unpaid obligations, brought forward, Oct 1	\$ 43,377	\$ 33,834	\$ 3,974,879	\$ 106	\$ 4,052,196
Obligations incurred	346,340	97,139	10,343,006	4,448	10,790,933
Outlays (gross) (-)	(339,706)	(92,833)	(9,309,091)	(4,412)	(9,746,042)
Recoveries of prior year unpaid obligations (-)	(2,956)	(4,951)	(453,600)	(14)	(461,521)
Unpaid obligations, end of year	47,055	33,189	4,555,194	128	4,635,566
Uncollected payments:					
Uncollected pymts, Fed sources, brought forward, Oct 1 (-)	(4,418)	-	-	-	(4,418)
Change in uncollected pymts, Fed sources (+ or -)	148	-	-	-	148
Uncollected pymts, Fed sources, end of year (-)	(4,270)	-	-	-	(4,270)
Memorandum (non-add) entries					
Obligated balance, start of year (+ or -)	\$ 38,959	\$ 33,834	\$ 3,974,879	\$ 106	\$ 4,047,778
Obligated balance, end of year (net)	\$ 42,785	\$ 33,189	\$ 4,555,194	\$ 128	\$ 4,631,296
Budget Authority and Outlays, Net:					
Budget authority, gross (discretionary and mandatory)	\$ 343,237	\$ 98,788	\$ 9,816,871	\$ 4,096	\$ 10,262,992
Actual offsetting collections (discretionary and mandatory) (-)	(352,105)	(98,789)	(8,458)	(505)	(459,857)
Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -)	148	-	-	-	148
Budget Authority, net (discretionary and mandatory)	\$ (8,720)	\$ (1)	\$ 9,808,413	\$ 3,591	\$ 9,803,283
Outlays, gross (discretionary and mandatory)	\$ 339,707	\$ 92,832	\$ 9,309,091	\$ 4,412	\$ 9,746,042
Actual offsetting collections (discretionary and mandatory) (-)	(352,105)	(98,789)	(8,458)	(505)	(459,857)
Outlays, net (discretionary and mandatory)	(12,398)	(5,957)	9,803,283	3,907	\$ 9,286,185
Distributed offsetting receipts (-)	(28,342)	-	(39,054)	-	(67,396)
Agency outlays, net (discretionary and mandatory)	\$ (40,740)	\$ (5,957)	\$ 9,261,579	\$ 3,907	\$ 9,218,789

SCHEDULE OF BUDGETARY RESOURCES BY MAJOR ACCOUNT

FY 2013

Budgetary Resources:

	S&E	Auctions	USF	Other	Total
Unobligated balance brought forward, October 1	\$ 18,418	\$ 479	\$ 3,179,789	\$ 8,281	\$ 3,206,967
Recoveries of prior year unpaid obligations	3,897	710	923,071	6	927,684
Other changes in unobligated balance (+ or -)	381	(382)	-	-	(1)
Unobligated balance from prior year budget authority, net	22,696	807	4,102,860	8,287	4,134,650
Appropriations (discretionary and mandatory)	-	-	9,786,558	(196)	9,786,362
Borrowing authority (discretionary and mandatory)	-	-	-	1,496	1,496
Spending authority from offsetting collections (discretionary and mandatory)	327,819	99,109	21,225	2,516	450,669
Total budgetary resources	\$ 350,515	\$ 99,916	\$ 13,910,643	\$ 12,103	\$ 14,373,177

Status of Budgetary Resources:

Obligations incurred	\$ 332,574	\$ 99,179	\$ 10,572,149	\$ 2,006	\$ 11,005,908
Unobligated balance, end of year:					
Apportioned	10,644	90	-	339	11,073
Exempt from apportionment	-	-	3,173,822	-	3,173,822
Unapportioned	7,297	647	164,672	9,758	182,374
Total unobligated balance, end of year	17,941	737	3,338,494	10,097	3,367,269
Total status of budgetary resources	\$ 350,515	\$ 99,916	\$ 13,910,643	\$ 12,103	\$ 14,373,177

Change in Obligated Balance:

Unpaid obligations:					
Unpaid obligations, brought forward, Oct 1	\$ 66,584	\$ 23,273	\$ 3,491,560	\$ 268	\$ 3,581,685
Obligations incurred	332,574	99,179	10,572,149		
Outlays (gross) (-)	(351,884)	(87,907)	(9,165,759)		
Recoveries of prior year unpaid obligations (-)	(3,897)	(710)	(923,071)	(6)	(927,684)
Unpaid obligations, end of year	43,377	33,835	3,974,879	105	4,052,196
Uncollected payments:					
Uncollected pymts, Fed sources, brought forward, Oct 1 (-)	(5,616)	-	-	-	(5,616)
Change in uncollected pymts, Fed sources (+ or -)	1,198	-	-	-	1,198
Uncollected pymts, Fed sources, end of year (-)	(4,418)	-	-	-	(4,418)
Memorandum (non-add) entries					
Obligated balance, start of year (+ or -)	\$ 60,968	\$ 23,273	\$ 3,491,560	\$ 268	\$ 3,576,069
Obligated balance, end of year (net)	\$ 38,959	\$ 33,835	\$ 3,974,879	\$ 105	\$ 4,047,778

Budget Authority and Outlays, Net:

Budget authority, gross (discretionary and mandatory)	\$ 327,819	\$ 99,109	\$ 9,807,783	\$ 3,816	\$ 10,238,527
Actual offsetting collections (discretionary and mandatory) (-)	(357,046)	(99,109)	(21,225)	(3,658)	(481,038)
Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -)	1,198	-	-	-	1,198
Budget Authority, net (discretionary and mandatory)	\$ (28,029)	\$ -	\$ 9,786,558	\$ 158	\$ 9,758,687
Outlays, gross (discretionary and mandatory)	\$ 351,884	\$ 87,907	\$ 9,165,759	\$ 2,163	\$ 9,607,713
Actual offsetting collections (discretionary and mandatory) (-)	(357,046)	(99,109)	(21,225)	(3,658)	(481,038)
Outlays, net (discretionary and mandatory)	(5,162)	(11,202)	9,144,534	(1,495)	9,126,675
Distributed offsetting receipts (-)	(35,403)	-	22,047	-	(13,356)
Agency outlays, net (discretionary and mandatory)	\$ (40,565)	\$ (11,202)	\$ 9,166,581	\$ (1,495)	\$ 9,113,319