

CHAPTER 1: MANAGEMENT'S DISCUSSION AND ANALYSIS

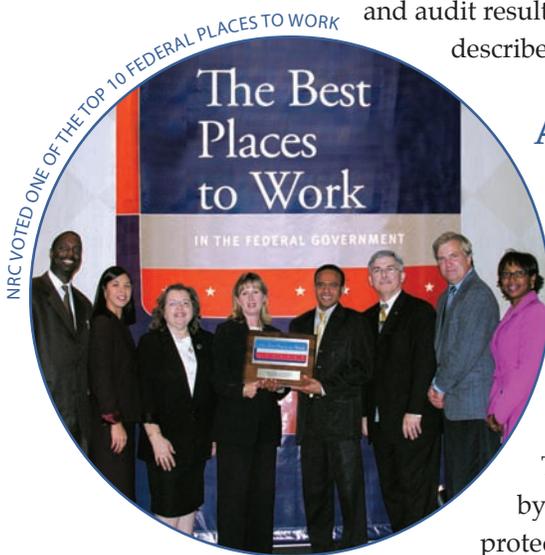


... NRC's
best asset is
its staff ...

INTRODUCTION

This *Performance and Accountability Report* represents the culmination of the U.S. Nuclear Regulatory Commission's (NRC) program and financial management processes, which began with mission and program planning, continued through the formulation and justification of NRC's budget to the President and the Congress, through budget execution, and ended with this report on our program performance and use of the resources entrusted to us. This report was prepared pursuant to the requirements of the Chief Financial Officers Act, as amended by the Reports Consolidation Act, and covers activities from October 1, 2004, to September 30, 2005. This report can be accessed on NRC's Web site at <http://www.nrc.gov>.

Chapter 1, *Management's Discussion and Analysis*, provides an overview of the NRC. It consists of six sections: *About the NRC* describes the agency's mission, organizational structure, and regulatory responsibility; *Future Challenges* includes forward-looking information; *Program Performance Overview* discusses the agency's success in achieving its strategic goals which are further described in Chapter 2; *President's Management Agenda* describes the agency's progress in "Getting to Green" for the five management initiatives; *Financial Performance Overview* provides highlights of the NRC's financial position and audit results contained in Chapter 3; and *Systems, Controls, and Legal Compliance* describes the agency's compliance with key legal and regulatory requirements.



ABOUT THE NRC

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

The NRC's mission is to regulate the Nation's civilian use of byproduct, source, and special nuclear materials to ensure adequate protection of public health and safety, to promote the common defense and security, and to protect the environment.

Organization

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

The NRC's headquarters is located in Rockville, Maryland. Four regional offices are located in King of Prussia, Pennsylvania; Atlanta, Georgia; Lisle, Illinois; and Arlington, Texas. The NRC's technical training center is located in Chattanooga, Tennessee. The NRC also has at least two resident inspectors at each of the Nation's nuclear power reactor sites. The NRC's Operations Center is the focal point for NRC communications with its licensees, State agencies, and other Federal agencies concerning operating events in the commercial nuclear sector. The Operations Center is staffed 24 hours a day by NRC operations officers. An organization chart of the NRC is contained in Appendix E.

The NRC's budget for fiscal year (FY) 2005 was \$669.3 million (see Figure 1) and 3,108 full-time equivalent staff (see Figure 2). The FY 2004 budget was \$625.6 million and 3,040 full-time equivalent staff. The NRC recovers most of its appropriations from fees paid by NRC licensees. Approximately 66 percent of the budget and 69 percent of the staff are for reactor safety.

Regulatory Responsibility

To fulfill its responsibility to protect the public health and safety, the NRC performs three principal regulatory functions (1) establish standards and regulations, (2) issue licenses for nuclear facilities and users of nuclear materials, and (3) inspect facilities and users of nuclear materials to ensure compliance with regulatory requirements. These regulatory functions relate to nuclear power plants, other nuclear facilities, and other civilian uses of nuclear materials, such as nuclear medicine programs at hospitals; academic activities at educational institutions; research work; industrial applications, such as

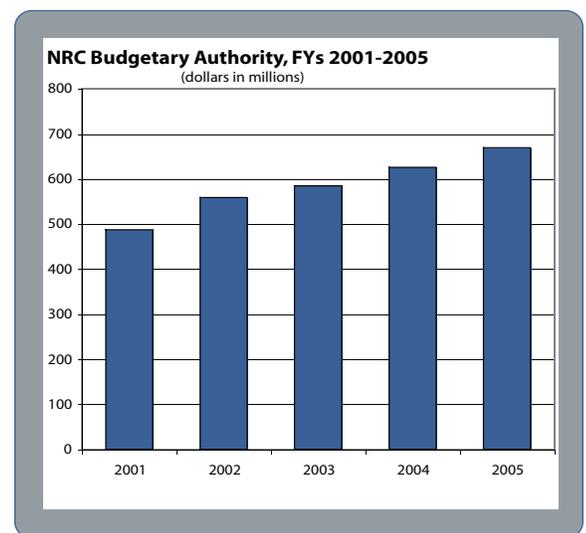


Figure 1

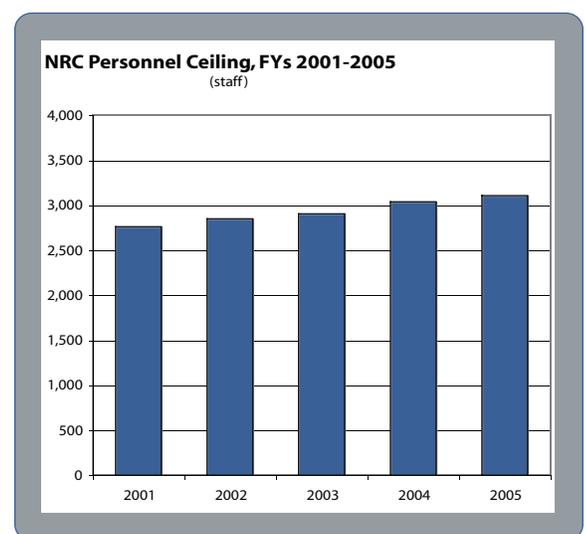


Figure 2

gauges and testing equipment; and the transport, storage, and disposal of nuclear materials and wastes. The NRC has aligned its regulatory activities into the Nuclear Reactor Safety program and the Nuclear Materials and Waste Safety program.

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

Approximately 20 percent of the Nation’s electricity is generated by 104 commercial nuclear reactors that are licensed by the NRC to operate in 31 States (see Figure 3). Since 1993, nuclear electric generation has increased by approximately 20 percent. The NRC expends over 368,500 hours of inspection effort annually at 104 operating reactors and licenses approximately 4,700 reactor operators.

The NRC oversees approximately 4,500 licenses for medical, academic, industrial, and general uses of nuclear materials. The NRC conducts between 1,150 and 1,200 health and safety inspections of its nuclear materials licensees annually. Additionally, approximately 17,300 licenses are administered by the 33 States that participate in the NRC Agreement States program, which authorizes the State to regulate the use of radioactive materials within that State (see Figure 4). The NRC, Agreement States, and their licensees share a common responsibility to protect public health and safety.

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

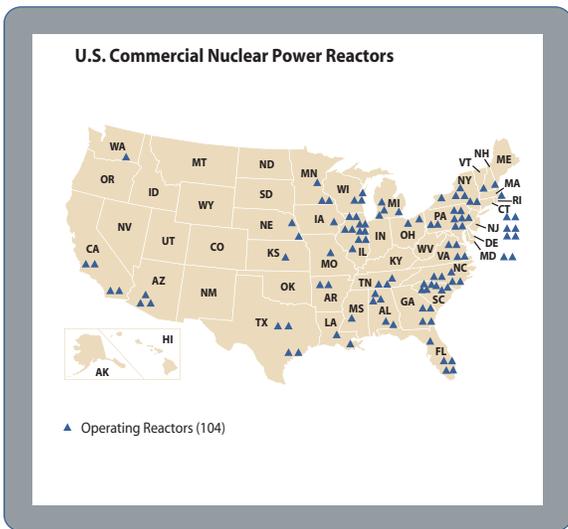


Figure 3

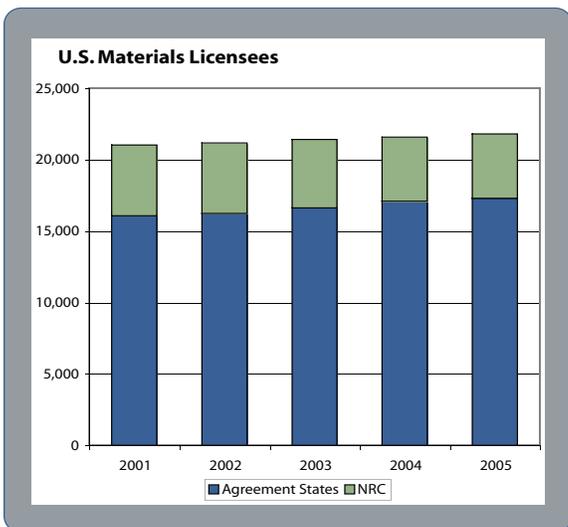


Figure 4

FUTURE CHALLENGES

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

- NRC strategic initiatives will include continued emphasis on strengthening the interrelationship between safety, security, and emergency preparedness.
- The NRC will continue to be challenged by the need to excel in the management of safety and in the area of communications. One of our greatest continuing challenges lies in the area of integrating power plant security, and its many improvements, into the fabric of day-to-day operational safety and regulation. We also need to continue to enhance integration of our security-related interfaces with other agencies, at the Federal, State, and local levels.
- The NRC must continue to foster and strengthen, internally and externally, the means of achieving safety-focused policy, programs, and practices, directed by and with the ultimate goal of benefiting the American public.
- The nuclear industry needs to continue to foster and strengthen design, operational and safety maintenance, making the right choices, and avoiding the pitfall of complacency or lack of safety focus.
- The majority of operating nuclear power plants will apply for license renewal to help meet the Nation's demand for energy production.
- The Department of Energy (DOE) is expected in the near future to submit an application to construct and operate the Nation's high-level radioactive waste repository at Yucca Mountain, Nevada.
- Increasing quantities of radioactive waste may be transported and held in interim storage or permanent disposal sites.
- The nuclear power industry will begin to submit applications to construct and operate new nuclear power plants to meet the Nation's demand for energy.

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- The NRC, Agreement States, and licensees will continue to devote increasing attention to the security of radioactive materials and facilities; in addition, the NRC will continue its nuclear non-proliferation activities.
 - The NRC will continue to see an increase in requirements for coordination with a wide array of Federal, State, and local agencies related to homeland security and emergency planning.
 - The number of Agreement States will increase, as will the numbers of medical, academic, and industrial entities using radioactive materials under the oversight of the Agreement States.
 - The regulatory climate is expected to adjust to both internal and external factors through the use of risk-informed and, as appropriate, performance-based regulations.

A backdrop to these industry-specific changes is one of elevated security and heightened public concern about safety. This has resulted in increased public dialogue about the uses of radioactive materials, varying from the potential for terrorist activities, to public concern about the adequacy of emergency preparedness plans for areas surrounding nuclear facilities. In this regard, the NRC is committed to sharing openly with the public its information and decision-making processes consistent with the law and is committed to implementing regulatory processes that facilitate stakeholder involvement. While the NRC will continue to make as much information as possible available to the public, the agency will withhold information that could assist potential terrorists. The manner in which the NRC regulates is also evolving. As the NRC continues to learn from operational experience and develops more effective ways of assessing risks and using risk-informed and performance-based approaches founded in ‘realistic conservatism,’ the agency is better able to make appropriate safety decisions and to better allocate resources to areas where they will have the greatest positive effect. In addition, the NRC continues to seek improvement in effectiveness and efficiency.

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

Ensuring the protection of public health, safety, and the environment has always been, and continues to be, the NRC’s primary goal. Accordingly, safety is the most important consideration in evaluating license applications, licensee performance, and proposed

changes to the regulatory framework. Because security is essential to the NRC's mission and linked to safety, it also is an important consideration in the agency's actions. The agency continuously works to improve its effectiveness and efficiency without conflicting with or undermining its safety and security mission.

PROGRAM PERFORMANCE OVERVIEW

Federal agencies provide an annual performance budget to Congress with measurable target levels of performance. The NRC evaluates its program performance within a structured planning, budgeting, and performance management process.

Strategic Plan

The NRC's FY 2004–FY 2009 Strategic Plan describes the strategies and means by which the agency intends to accomplish its mission. The Strategic Plan provides a foundation to guide the development of the NRC's annual performance plan and subsequent resource requirement determination. The Strategic Plan focuses on the agency's strategic objective to "enable the use and management of radioactive materials and nuclear fuels for beneficial civilian purposes in a manner that protects public health and safety and the environment, promotes the security of our Nation, and provides for regulatory actions that are open, effective, efficient, realistic, and timely." The Strategic Plan also contains the agency's five goals of safety, security, openness, effectiveness, and management. Safety and security are the agency's highest priorities and are supported by the goals of openness, effectiveness, and management. The agency's success in achieving each goal is defined by strategic outcome(s) that are associated with each goal, which is described below. A further description of each goal and their associated performance measures are provided in Chapter 2, *Program Performance*, which describes the agency's overall program performance.

Goals

Safety goal—*Ensure protection of public health and safety and the environment.*

Strategic Outcomes

- No nuclear reactor accidents.¹
- No inadvertent criticality events.
- No acute radiation exposures resulting in fatalities.

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- No releases of radioactive materials that result in significant radiation exposures.
 - No releases of radioactive materials that cause significant adverse environmental impacts.

The NRC's primary goal is to regulate the safe uses of radioactive materials for civilian purposes to ensure the protection of public health and safety and the environment. The NRC achieves its safety goal by licensing individuals and organizations to use radioactive materials for beneficial civilian purposes and then ensuring that the performance of these licensees is at or above acceptable safety levels. In particular, we maintain vigilance over safety performance through ongoing licensing reviews and inspections and expanded oversight. We also use enforcement actions for significant deficiencies, including issuing orders for corrective action, issuing shutdown orders, imposing civil penalties and/or criminal prosecution, or, when appropriate, suspending or revoking a license.

Security goal—*Ensure the secure use and management of radioactive materials.*

Strategic Outcome

- No instances where licensed radioactive materials are used domestically in a manner hostile to the security of the United States.

The security goal has been explicitly identified to reflect changes in the threat environment and the agency's response to the events of September 11, 2001. The primary challenge facing the NRC in the coming years is to emerge from the period of uncertainty in post-September 11 security requirements; determine what long-term security provisions are necessary; and revise its regulations, orders, and internal procedures as necessary to ensure public health and safety and the common defense and security in an elevated threat environment. In particular, the NRC will focus its efforts on the following activities:

- Assure the continuing validity of the NRC design-basis threats.
- Complete the identification of vulnerabilities and mitigating strategies at licensed facilities.
- Revise requirements to provide additional protection where needed. Develop improved methods of communicating sensitive information to licensees.
- Enhance controls on high-risk radiation sources.
- Develop more formal, long-term relationships with Federal, State, and local organizations with shared responsibilities for protecting nuclear facilities and activities and responding to incidents.

Openness goal—*Ensure openness in our regulatory process.*

Strategic Outcome

- Stakeholders are informed and involved in NRC processes as appropriate.

The goal on openness recognizes that stakeholders be informed about, and have an opportunity to participate in the NRC's regulatory process. The NRC views nuclear regulation as the public's business; as such, it should be transacted openly and candidly in order to maintain the public's confidence. The agency is committed to keeping the public informed and believes that a responsible and effective regulatory process includes an involved public that is well informed.

Effectiveness goal—*Ensure that NRC actions are effective, efficient, realistic, and timely.*

Strategic Outcome

- No significant licensing or regulatory impediments to the safe and beneficial uses of radioactive materials.

Over the next several years, the NRC anticipates a significant increase in agency workload. In particular, the workload is likely to include licensing requests of unprecedented technical complexity, including the Department of Energy's application to license the Yucca Mountain high-level radioactive waste repository and requests to license the next generation of nuclear reactors. Security demands are becoming more complex, requiring diverse professional expertise and close coordination with other Federal, State, and local agencies. Increases in both the frequency and the extent of stakeholder involvement in the NRC's regulatory processes are expected as the agency works to improve openness.

Many factors could contribute to licensing and regulatory impediments, such as an inadequate regulatory framework, an ineffective program, or an inefficient process that results in an untimely regulatory decision. The NRC is committed to addressing such issues through initiatives related to this goal, and it will also monitor the regulated community for instances where agency actions may have unnecessarily impeded licensees and applicants. In conducting this monitoring, the NRC may consider the results of self-assessments and external assessments, feedback from stakeholders, congressional direction, and other sources.

Management goal—*Ensure excellence in agency management to carry out the NRC's strategic objective.*

Strategic Outcomes

- Continuous improvement in NRC's leadership and management effectiveness in delivering the mission.
- A diverse, skilled workforce and an infrastructure that fully support the agency's mission and goals.

The NRC strives for management excellence in carrying out all of its regulatory responsibilities. The agency believes that management excellence should be achieved while fostering the successful conduct of priority activities. In setting this goal, the NRC considered the management and support needed to achieve the agency's mission, preexisting management challenges, and other initiatives identified by central organizations such as the Government Accountability Office (GAO), Office of Management and Budget (OMB), and Office of Personnel Management (OPM). This goal includes strategies for the management of human capital, infrastructure management, improved financial performance, expanded electronic Government, budget and performance integration, and internal communications.

The NRC's FY 2004–FY 2009 Strategic Plan is available on the Web site at <http://www.nrc.gov/reading-rm/doc-collections/nuregs/staff/sr1614/v3/index.html>.

Performance Budget

The FY 2004–FY 2009 Strategic Plan led to a re-alignment of the agency's performance budget structure. Beginning with the FY 2006 Performance Budget, budget requests have been structured by two major programs—Nuclear Reactor Safety and Nuclear Materials and Waste Safety.

Nuclear Reactor Safety

The Nuclear Reactor Safety program encompasses all NRC efforts to ensure that civilian nuclear power reactor facilities and research and test reactors are licensed and operated in a manner that adequately protects the public health and safety and the environment and protects against radiological sabotage and theft or diversion of special nuclear materials. The Atomic Energy Act of 1954, as amended, and the Energy Reorganization

Act of 1974, as amended, are the foundation for regulating the Nation's civilian nuclear power industry. The Nuclear Reactor Safety program contains two activities—Nuclear Reactor Licensing and Nuclear Reactor Inspection.

Nuclear Materials and Waste Safety

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

The NRC's FY 2006 Performance Budget is available on the Web site at <http://www.nrc.gov/reading-rm/doc-collections/nuregs/staff/sr1100/v21/>.

Program Performance Report

The *FY 2005 Performance and Accountability Report* is reporting on the agency's performance measures by each of the five goals contained in the agency's FY 2004–FY 2009 Strategic Plan. The *FY 2005 Performance and Accountability Report* also describes the achievements and challenges faced by each of the seven activities under the agency's major programs of Nuclear Reactor Safety and Nuclear Materials and Waste Safety. The NRC is reporting FY 2005 performance measures contained in both the FY 2005 and FY 2006 Performance Budgets.

Program Assessment Rating Tool

Over the past several years, the Office of Management and Budget has conducted Program Assessment Rating Tool reviews of the NRC's Nuclear Reactor Safety and the Nuclear Materials and Waste Safety program activities. All the program activities reviewed have been rated as either "effective" or "moderately effective." For the program activities reviewed in FY 2003 and FY 2004, the Office of Management and Budget recommended that the agency include better linkages of budget requests to the NRC's annual and long-term goals, as well as the linkage of performance measures in the organization's operating plan to support the safety performance measures in the agency's FY 2004–FY 2009 Strategic Plan. A further recommendation was for more transparency in how allocation decisions are made and how the activity contributes to achievement of the agency's long-term goals. In addition, the Office of Management and Budget recommended a complete review of operating plan format and content

to improve their effectiveness as management tools. The NRC has been addressing the recommendations from the Office of Management and Budget to improve the effectiveness of these program activities.

PRESIDENT'S MANAGEMENT AGENDA

The President's Management Agenda prescribes Governmentwide initiatives to reform the U.S. Government to be more citizen-centered, results-oriented, and market-based, and to actively promote competition rather than stifling innovation. To achieve this goal, the Administration has identified five initiatives to improve Government performance in the areas of (1) strategic management of human capital, (2) budget and performance integration, (3) competitive sourcing, (4) expanded electronic Government, and (5) improved financial management. The NRC is actively implementing the agenda to improve the management and performance of the Federal Government. Chapter 2 of this report discusses our accomplishments in these important areas.

FINANCIAL PERFORMANCE OVERVIEW

As of September 30, 2005, and 2004, the financial condition of the NRC was sound with respect to having sufficient funds to meet program needs and adequate control of these funds in place to ensure obligations did not exceed budget authority. The NRC prepared its financial statements in accordance with the accounting standards codified in the Statements of Federal Financial Accounting Standards (SFFAS) and Office of Management and Budget Circular A-136, *Financial Reporting Requirements*.

Sources of Funds

The NRC has two appropriations, Salaries and Expenses and Office of the Inspector General, and funds for both appropriations are available until expended. The NRC's total new FY 2005 budget authority was \$669.3 million. Of this amount, \$661.8 million was for the Salaries and Expenses appropriation and \$7.5 million was for the Office of the Inspector General appropriation. This represents an increase in new budget authority of \$43.6 million over FY 2004 (\$43.4 million for the Salaries and Expenses appropriation and \$0.2 million for the Office of the Inspector General appropriation). In addition, \$40.9 million from prior-year appropriations, \$6.1 million from prior-year reimbursable work, and \$6.6 million for new reimbursable work to be performed for

others was available to obligate in FY 2005. The sum of all funds available to obligate for FY 2005 was \$722.9 million, which is a \$41.3 million increase over the FY 2004 amount of \$681.6 million.

The Omnibus Budget Reconciliation Act of 1990 (OBRA-90), as amended, required the NRC to collect fees to offset approximately 90 percent of its new budget authority, less the amount appropriated to the NRC from the Nuclear Waste Fund for FY 2005 (see Figure 5). The NRC collected \$534.1 million in FY 2005. This is 98.8 percent of the recovery requirement. For FY 2004, OBRA-90 required NRC to collect approximately 92 percent of its new budget authority, excluding appropriations from the Nuclear Waste Fund.

Uses of Funds by Function

The NRC incurred obligations of \$665.5 million, which was an increase of \$20.3 million over FY 2004. Approximately 60 percent of obligations were used for salaries and benefits. The remaining 40 percent was used to obtain technical assistance for the NRC's principal regulatory programs, to conduct confirmatory safety research, to cover operating expenses, (e.g., building rentals, transportation, printing, security services, supplies, office automation, training), staff travel, and reimbursable work (see Figure 6). The unobligated budget authority available at the end of FY 2005 was \$57.3 million, which is an increase compared to the FY 2004 amount of \$36.3 million. This increase in year-end unobligated budget authority is primarily the result of the delay in the Department of Energy's submission of a license application for a high-level waste repository for NRC review. Of this \$57.3 million, \$6.7 million is for reimbursable work and \$50.6 million is available to fund critical NRC needs in FY 2006.

Audit Results

The NRC received an unqualified audit opinion on its FY 2005 financial statements. The auditors identified two new reportable conditions concerning information system security and financial controls over disbursements. In FY 2004, the auditors identified one reportable condition, which was classified as a material internal control weakness concerning the Fee Billing System. This weakness was also identified as a substantial noncompliance with the Federal

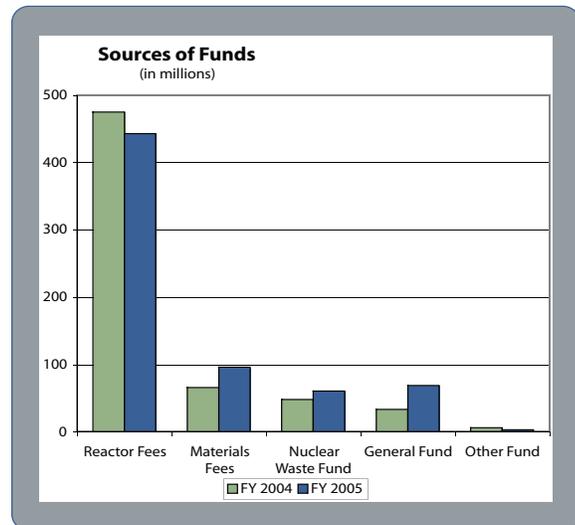


Figure 5

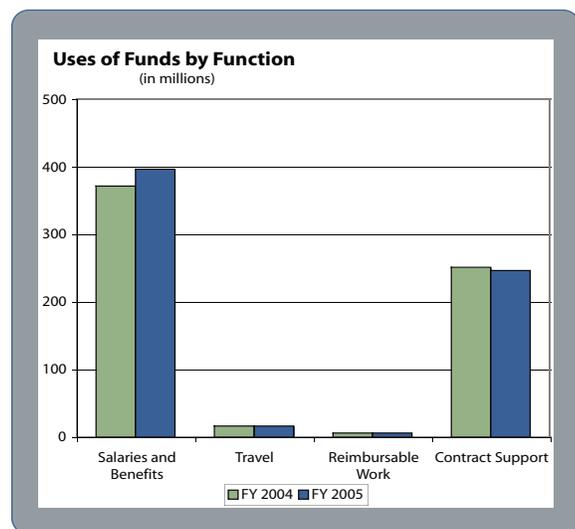


Figure 6

Financial Management Improvement Act (Improvement Act). The agency's core accounting and payroll systems, cross-serviced by the Department of the Interior's National Business Center (DOI-NBC) as part of the e-Government initiative, were also found to be in substantial noncompliance with the Improvement Act for lack of compliance with Federal financial management system requirements. The agency will continue to implement corrective actions in FY 2006 for the material weakness and substantial noncompliances.

The auditors closed two of the remaining four prior-year reportable conditions concerning user organization compensating controls for the payroll system and fee recovery from licensees. The remaining two reportable conditions concern the development of the hourly rate for license fees and accounting for internal use software. During FY 2006, the agency expects to implement corrective action for the hourly rate development for license fees and will continue to promote strengthening its internal use software practices.

Limitations of the Financial Statements

The principal statements have been prepared to report the financial position and results of operations of the NRC, pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management and Reform Act of 1994. These statements have been prepared for the books and records of the NRC in accordance with the formats prescribed by the Office of Management and Budget. However, these statements differ from the financial reports used to monitor and control budgetary resources that are prepared from the same books and records. The principal statements should be read with the realization that they are for a sovereign entity, liabilities not covered by budgetary resources cannot be liquidated without enactment of an appropriation, and the payment of all liabilities other than for contracts can be abrogated by the sovereign entity. Other limitations are included in the footnotes to the principal statements.

The NRC's FY 2005 financial statements were audited by R. Navarro and Associates, Inc., under contract to the NRC Office of the Inspector General.

Financial Statement Highlights

The NRC's financial statements summarize the financial activity and financial position of the agency. The financial statements, footnotes, and required supplementary information, appear in Chapter 3, *Auditors' Reports and Financial Statements*. Analysis of the principal statements follows.

Analysis of the Balance Sheet

The NRC's assets were approximately \$313.7 million as of September 30, 2005. This is an increase of \$30.3 million from the end of FY 2004. The assets reported in NRC's Balance Sheet are summarized in the accompanying table.

The Fund Balance with Treasury represents the NRC's largest asset of \$220.7 million as of September 30, 2005, an increase of \$20.4 million from the FY 2004 year-end balance. This balance accounts for approximately 70 percent of total assets and represents appropriated funds, collected license fees, and other funds maintained at the U.S. Department of the Treasury to pay current liabilities. The increase in Fund Balance with the U.S. Treasury is primarily because NRC did not expend \$23.0 million of the transfer from the DOE for Nuclear Waste Fund activities. Expenditures in the Nuclear Waste Fund were lower than anticipated due to delays in receipt of DOE's license application for a high-level waste repository and in procurement for the Package Performance Study. At the time the FY 2005 budget was formulated, NRC expected to receive DOE's license application in December 2004 and budgeted for increased resource needs for license review and hearings.

Accounts Receivable, Net, as of September 30, 2005, was \$64.0 million and includes an offsetting allowance for doubtful accounts of \$2.9 million. This is an 18 percent increase from the FY 2004 year-end Accounts Receivable, Net, balance of \$54.0 million. This increase is due to an improved accounts receivable accrual methodology used in FY 2005. Accounts Receivable Due from the Public was \$60.8 million, representing 19 percent of total assets. The value of Property and Equipment, Net, was \$27.0 million, representing 8 percent of total assets. The majority of the balance is comprised of nuclear reactor simulators, leasehold improvements, and computer hardware and software.

ASSET SUMMARY (in millions)		
	FY 2005	FY 2004
Fund Balance with Treasury	\$220.7	\$200.3
Accounts Receivable, Net	64.0	54.0
Property & Equipment, Net	27.0	26.8
Other	2.0	2.3
Total Assets	\$313.7	\$283.4

The NRC's liabilities were \$156.2 million as of September 30, 2005. The accompanying table shows an increase in Total Liabilities of \$10.3 million from the FY 2004 year-end

balance of \$145.9 million. This increase is primarily in the liability to offset the increase in the unbilled accounts receivable which will be paid to the U.S. Treasury when collected. This liability increased as a result of improved estimation of accounts receivable accrual. Other Liabilities include \$63.6 million for recoveries from unbilled accounts receivable, \$13.0 million for accrued salaries to employees, and \$33 million for accrued annual leave. Of the agency's

liabilities, \$43.3 million were not covered by budgetary resources, which is a slight increase over the balance as of September 30, 2004. Liabilities not covered by budgetary resources are unfunded pension expenses, accrued annual leave, and future workers' compensation. The Federal budget process does not recognize the cost of future benefits for today's employees. Instead, the Federal budget process recognizes those costs in future years when they are actually paid.

The difference between total assets and total liabilities, Net Position, was \$157.5 million as of September 30, 2005. This is an increase of \$20.0 million from the FY 2004 year-end balance. Unexpended Appropriations is the amount of authority granted by Congress that has not been expended. The increase of Unexpended Appropriations of \$20.9 million is because of

the increase in Fund Balance with Treasury due to the lower expenditures from the delays in the receipt of DOE's license application for a high-level repository (see above explanation). Cumulative Results of Operations represent net results of operations since the NRC's inception. The decrease is primarily the result of a \$1.3 million increase in future funding requirements related to increase in Federal Employees Compensation Act (FECA) paid by the U.S. Department of Labor.

LIABILITIES SUMMARY (in millions)

	FY 2005	FY 2004
Accounts Payable	\$29.0	\$27.9
Federal Employee Benefits	8.4	8.1
Other Liabilities	118.8	109.9
Total Liabilities	\$156.2	\$145.9

NET POSITION SUMMARY (in millions)

	FY 2005	FY 2004
Unexpended Appropriations	\$170.8	\$149.9
Cumulative Results of Operations	(13.3)	(12.4)
Total Net Position	\$157.5	\$137.5

Analysis of the Statement of Net Cost

The Statement of Net Cost presents the net cost of NRC’s two programs as identified in the NRC Annual Performance Plan. The purpose of this statement is to link program performance to the cost of programs. The NRC’s net cost of operations for the year ended September 30, 2005, was \$133.0 million, which is an increase of \$22.6 million over the FY 2004 net cost of \$110.4 million. Net costs by program are shown in the accompanying table. Gross costs increased primarily because of Federal pay raises and other nondiscretionary compensation and benefits increases.

NET COST OF OPERATIONS (in millions)		
	FY 2005	FY 2004
Nuclear Reactor Safety	\$0.5	\$(12.0)
Nuclear Materials & Waste Safety	132.5	122.4
Net Cost of Operations	\$133.0	\$110.4

Total exchange revenue for the year ended September 30, 2005, was \$550.0 million, which is a decrease of \$2.2 million from the exchange revenue of \$552.2 million for the year ended September 30, 2004. Exchange revenue is derived from fees for licensing, inspections, other services, and annual fees assessed in accordance with 10 CFR Parts 170 and 171 and decreased due to the 2 percent reduction in the amount the agency was required to recover under OBRA-90.

Analysis of Statement of Changes in Net Position

The Statement of Changes in Net Position reports the change in net position during the reporting period. Net position is affected by changes in its two components—Cumulative Results of Operations and Unexpended Appropriations. The increase in Net Position of \$20.0 million from FY 2004 to FY 2005 is due primarily from the net change in Unexpended Appropriations. The increase of Unexpended Appropriations of \$20.9 million is because of the increase in Fund Balance with Treasury due to the lower expenditures from the delays in the receipt of DOE’s license application for a high-level repository.

Analysis of the Statement of Budgetary Resources

The Statement of Budgetary Resources shows the sources of budgetary resources available and the status at the end of the period. It presents the relationship between budget authority and budget outlays, and reconciles obligations to total outlays. For FY 2005, NRC had Total Budgetary Resources available of \$722.9 million, the majority of which was derived from new budget authority. This represents a 6 percent increase over FY 2004 budgetary resources available of \$681.6 million. This 6 percent increase consists of an increase to fund Federal pay raises and other nondiscretionary compensation and benefits, from the Nuclear Waste Fund to initiate the review of the anticipated DOE application to construct a high-level waste repository at Yucca Mountain, and to support the Package Performance Study addressing the safety of spent nuclear fuel shipping containers in rail and highway accidents.

For FY 2005, the Status of Budgetary Resources showed the NRC incurred obligations of \$665.5 million, or 92 percent of funds available. This is comparable to FY 2004 obligations of \$645.3 million, or 94 percent of funds available. The decrease from 94 percent of funds available to 92 percent is because NRC did not expend \$23 million of the transfer from DOE for Nuclear Waste Fund activities. Total Outlays for FY 2005 were \$645.2 million, which represents a \$28.6 million increase from FY 2004 total Outlays of \$616.6 million.

Analysis of the Statement of Financing

The Statement of Financing is designed to provide the bridge between accrual-based (financial accounting) information in the Statement of Net Cost and obligation-based (budgetary accounting) information in the Statement of Budgetary Resources by reporting the differences and reconciling the two statements. This reconciliation ensures that the proprietary and budgetary accounts in the financial management system are in balance. The Statement of Financing takes budgetary obligations of \$665.5 million and reconciles to the net cost of operations of \$133.0 million by deducting non-budgetary resources, costs not requiring resources, and financing sources yet to be provided.

SYSTEMS, CONTROLS, AND LEGAL COMPLIANCE

This section provides information on NRC's compliance with the Federal Managers' Financial Integrity Act, Federal Financial Management Improvement Act, Prompt Payment Act, Debt Collection Improvement Act, Biennial Review of User Fees, Inspector General Act, and other key legal and regulatory requirements.

Federal Managers' Financial Integrity Act

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

Management Control Review Program

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

- Management knowledge gained from the daily operation of agency programs and reviews.
- Management reviews.
- Program evaluations.
- Audits of financial statements.
- Reviews of financial systems.



INTEGRITY ACT STATEMENT

The U.S. Nuclear Regulatory Commission evaluated its management controls and financial management systems for FY 2005, as required by the Federal Managers' Financial Integrity Act. On the basis of the NRC's comprehensive management control program, I certify, with reasonable assurance, that the agency is in compliance with the provisions of this act.

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

Nils J. Diaz
Chairman
November 15, 2005

-
- Annual performance plans.
 - Inspector General and Government Accountability Office reports.
 - Reports and other information provided by the congressional committees of jurisdiction.

The NRC's Executive Committee on Management Controls is comprised of senior executives from offices of the Chief Financial Officer and the Executive Director of Operations, with the General Counsel and the Inspector General participating as advisors. The committee met and reviewed these individual assurance statements. The committee then advised the Chairman whether the NRC had any management control deficiencies serious enough to be reported as a material weakness or material noncompliance.

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

FY 2005 Integrity Act Results

The NRC evaluated its management control systems for the fiscal year ending September 30, 2005. This evaluation provided reasonable assurance that the agency's management controls achieved their intended objectives. As a result, management concluded that the NRC did not have any material weaknesses, as defined by the Integrity Act, in its programmatic or administrative activities. The Fee Billing System was identified as a significant management control weakness and was of sufficient importance to merit the close attention of senior management.

Federal Financial Management Improvement Act

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

FY 2005 Improvement Act Results

As of September 30, 2005, the NRC evaluated its financial systems to determine if they complied with applicable Federal requirements and accounting standards required by the Improvement Act. The following eight systems were evaluated, the Federal Financial System, Federal Personnel and Payroll System, Human Resources Management System, Cost Accounting System, Advice of Allotments/Financial Plan, Capitalized Property System, Fee Billing System, and Controller Resource Database System.

The Chairman of the NRC determined that as of September 30, 2005, NRC financial management systems were in substantial compliance with the Improvement Act, except for the Fee Billing System and the Federal Financial System and Federal Personnel and Payroll System cross-serviced by the Department of the Interior's National Business Center which are in substantial noncompliance with Federal financial management system requirements. In making his determination, the Chairman considered all the information available to him, including the NRC Executive Committee on Management Control's report on the effectiveness of internal controls, Office of the Inspector General audit reports, and the results of the financial management systems reviews conducted by the agency. He also relied upon the National Business Center's annual reasonable assurance statement in which they concluded that the financial systems NRC cross-services with them, as part of the e-Government initiative, are in substantial noncompliance with Federal financial management systems requirements.

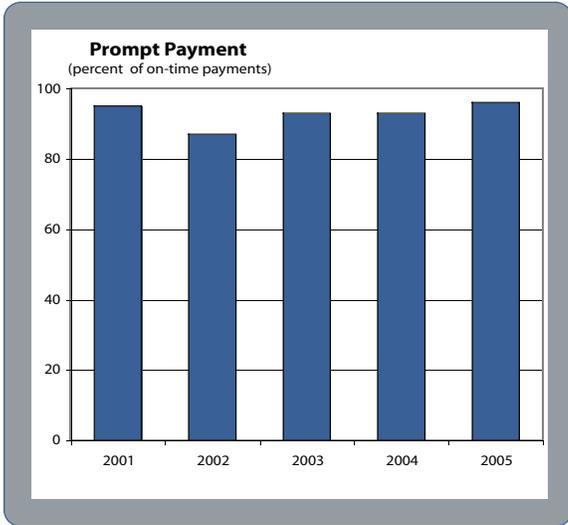


Figure 7

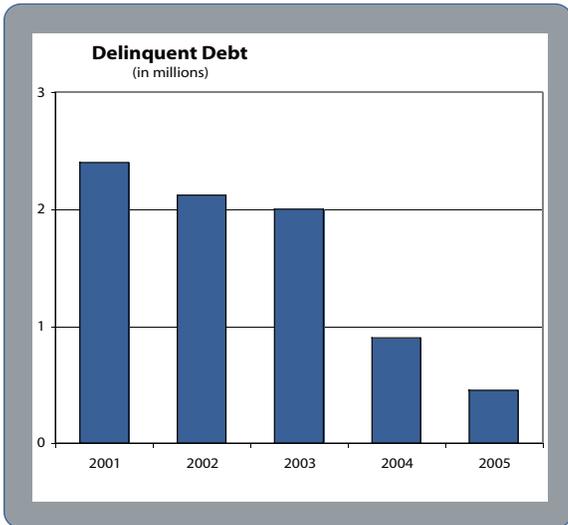


Figure 8

Prompt Payment

The Prompt Payment Act requires Federal agencies to make timely payments to vendors for supplies and services, to pay interest penalties when payments are made after the due date, and to take cash discounts when they are economically justified. During FY 2005, the NRC paid 8,629 invoices that were subject to the Prompt Payment Act. The NRC increased its percentage of on-time payments subject to the Prompt Payment Act from 94 percent in FY 2004 to 96 percent in FY 2005 (see Figure 7). The amount of interest penalties incurred during FY 2005 was \$8,850, which is an increase from FY 2004's amount of \$2,917.

Debt Collection

The Debt Collection Improvement Act is intended to enhance the ability of the Federal Government to service and collect debts. The agency's goal is to maintain the delinquent debt owed to the NRC, at year-end, to less than one percent of its annual billings. The NRC continues to meet this goal and has kept delinquent debt to less than one percent for the past 10 years. Delinquent debt at the end of FY 2005 was \$0.45 million (see Figure 8). This is a decrease of \$0.4 million over FY 2004 and a decrease in the number of outstanding receivables from 154 to 96. The NRC continues to pursue the collection of delinquent debt and continues to timely refer all eligible delinquent debt over 180 days to the U.S. Treasury for collection.

Biennial Review of User Fees

The Chief Financial Officers Act requires agencies to conduct a biennial review of fees, royalties, rents, and other charges imposed by agencies, and make revisions to cover program and administrative costs incurred. Each year, the NRC revises the hourly rates for license and inspection fees and adjusts the annual fees to meet the fee collection requirements of the Omnibus Budget Reconciliation Act of 1990, as amended. The most recent changes to the license, inspection, and annual fees are described in the *Federal Register* (70 FR 30526, May 26, 2005).

During FY 2005, the NRC reviewed its fees for criminal history licensees, public use of the auditorium, small materials licenses, international program materials licenses, and import/export licenses subject to the biennial review requirement. Reviews of other types of fees concluded that revisions were not warranted at this time.

Treasury Performance Measure Summary

Treasury has four key performance indicators for measuring how agencies complied with reporting requirements for the Governmentwide Financial Reporting System (GFRS), the Federal Agencies Centralized Trial Balance System (FACTS I), and intragovernmental activity. Overall for FY 2004, the NRC complied with the four performance indicators for timely reporting, reconciliation of unexplained differences for intragovernment activity, reliability and completeness of intragovernment reporting, and consistency and reasonableness. Treasury has not issued its FY 2005 Performance Measure Summary; however, based on our self-evaluation, NRC also met the requirements for this fiscal year.

Inspector General Act

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

Improper Payments

Improper payments continue to be at low risk for the agency. The NRC continues to evaluate its internal controls to guard against improper payments and monitors and reports on improper payments within its programs. At the present time, NRC's inventory of functional payment areas consists of commercial vendor, interagency, and travel payments. The DOI-NBC's Federal Personnel Payroll System became the NRC system of record for payroll disbursements effective November 2, 2003. The DOI-NBC is responsible for monitoring and reporting on any improper payroll-related payments. The NRC will continue to perform annual risk assessments for each of these areas. Based on the FY 2005 risk assessments, the number of and amount of improper payments fall below external reporting requirements established by Office of Management and Budget guidance on what is considered to be a significant risk.