

### **III. FINANCIALS**





## A MESSAGE FROM THE CHIEF FINANCIAL OFFICER

I am delighted to join NSF Director Dr. Rita Colwell in presenting the National Science Foundation's *FY 2003 Performance and Accountability Report*. This report provides a combined reporting of the Foundation's programmatic performance, financial and management information for the past year.

I am pleased to report that the agency received an unqualified audit opinion for the sixth consecutive year. However, the Independent Auditor's Report included one reportable condition related to post-award monitoring. This reportable condition focuses on the need to ensure that adequate resources are devoted to achieving our post-award monitoring program goals. In the coming year, we will be working to realign staff and dedicate additional resources to further strengthen our post-award monitoring program. To an extent our ability to carry out this activity is reliant upon the outcome of the agency's annual Salaries and Expenses appropriations.

Over the past year, significant effort was devoted to enhancing NSF's information security program. In addition, NSF made significant efforts to enhance the monitoring of NSF-owned property in the custody of awardees, as part of more rigorous post-award monitoring. Both are no longer reportable conditions in the FY 2003 Audit Report.

With respect to overall management, doing business more efficiently and effectively is a long-standing priority for the Foundation. NSF's commitment to leading edge technology and management information systems is an important element in the infrastructure that supports our continued achievements. Whether it is making transactions with our stakeholders more user friendly, increasing the efficiency of our internal operations, or providing real time financial and management information and reporting for decision making purposes, our systems provide the framework for our success.

- Today, NSF is the only federal agency to process all its full and complete proposals electronically.
- Despite a 14 percent increase in the number of proposal received this year, nearly 80 percent of award decisions – over 40,000 FY 2003 – were made within six months of receipt.
- Nearly 90 percent of the Foundation's funds support projects reviewed by external peers and selected through a merit-based competition.
- The re-engineered business practices implemented in recent years continue to yield cost efficiencies for the agency in FY 2003.

Accountability reporting also remains a high priority for the agency. For the second consecutive year, our Highlights report on performance and management was rated as among the top 10 in a national competition of 900 annual reports, many from Fortune 500 companies. In addition, we are proud to have again received two "green" ratings from the Office of Management and Budget, for successful achievement in the financial management and electronic government initiatives of

the President's Management Agenda (PMA). We continue to make progress in all the PMA initiatives, and indeed, advanced from a "red" to "yellow" status for the Budget Performance and Integration Initiative in FY 2003.

NSF continues to face the future in a position of operational strength thanks to our sound financial management, our commitment to continuous improvement in business practices and, most importantly, the extraordinary talent and commitment of our staff. More than reacting to change, we are committed to leading change and setting new standards of excellence for the federal financial community. We look forward to achieving many more milestones in the years ahead.

Thomas N. Cooley

November 7, 2003

# **National Science Foundation**

Financial Statements  
as of and for the years ended  
September 30, 2003 and 2002

**National Science Foundation  
Balance Sheet  
As of September 30, 2003 and 2002  
(Amounts in Thousands)**

**ASSETS**

	<u>2003</u>	<u>2002</u>
Intragovernmental		
Fund Balance With Treasury (Note 2)	\$ 7,083,797	\$ 6,419,700
Accounts Receivable (Note 3)	18,247	185
Advances (Note 4)	18,557	8,309
Total Intragovernmental Assets	<u>7,120,601</u>	<u>6,428,194</u>
Cash	6,729	7,766
Accounts Receivable, Net (Note 3)	202	571
Advances (Note 4)	66,610	52,479
General Property, Plant and Equipment, Net (Note 5)	<u>230,777</u>	<u>224,141</u>
<b>Total Assets</b>	<b>\$ <u>7,424,919</u></b>	<b>\$ <u>6,713,151</u></b>

**LIABILITIES**

Intragovernmental Liabilities		
Advances From Others	\$ 41,933	\$ 100,531
Other Intragovernmental Liabilities (Note 7)	396	321
FECA Employee Benefits (Notes 8 and 9)	264	254
Total Intragovernmental Liabilities	<u>42,593</u>	<u>101,106</u>
Accounts Payable	68,420	38,370
Other Liabilities (Note 7)	255,923	214,266
FECA Employee Benefits (Notes 8 and 9)	1,649	1,637
Lease Liabilities	-	60
Accrued Annual Leave (Note 8)	<u>11,120</u>	<u>10,567</u>
<b>Total Liabilities</b>	<b><u>379,705</u></b>	<b><u>366,006</u></b>

**NET POSITION**

Unexpended Appropriations	6,771,590	6,089,118
Cumulative Results of Operations	<u>273,624</u>	<u>258,027</u>
<b>Total Net Position</b>	<b><u>7,045,214</u></b>	<b><u>6,347,145</u></b>
<b>Total Liabilities and Net Position</b>	<b>\$ <u>7,424,919</u></b>	<b>\$ <u>6,713,151</u></b>

The accompanying notes are an integral part of these statements.

**National Science Foundation**  
**Statements of Net Cost**  
**For the Years Ended September 30, 2003 and 2002**  
(Amounts in Thousands)

**Program Costs**

	<u>2003</u>	<u>2002</u>
<b>People</b>		
Intragovernmental		
Program Cost	\$ 2,363	\$ 1,714
Salary & Expense, National Science Board (NSB) and Inspector General Cost	699	678
<b>Total Intragovernmental Cost</b>	<u>3,062</u>	<u>2,392</u>
With the Public		
Program Cost	865,126	766,020
Salary & Expense, NSB and Inspector General Cost	30,975	28,732
<b>Total Public Cost</b>	<u>896,101</u>	<u>794,752</u>
Total People Program Cost	899,163	797,144
Less: Intragovernmental Earned Revenues	22,880	17,903
<b>Net People Program Cost</b>	<u>876,283</u>	<u>779,241</u>
<b>Ideas</b>		
Intragovernmental		
Program Cost	3,188	13,293
Salary & Expense, NSB and Inspector General Cost	3,414	5,305
<b>Total Intragovernmental Cost</b>	<u>6,602</u>	<u>18,598</u>
With the Public		
Program Cost	2,464,532	2,166,046
Salary & Expense, NSB and Inspector General Cost	84,806	79,095
<b>Total Public Cost</b>	<u>2,549,338</u>	<u>2,245,141</u>
Total Ideas Program Cost	2,555,940	2,263,739
Less: Intragovernmental Earned Revenues	42,003	60,979
<b>Net Ideas Program Cost</b>	<u>2,513,937</u>	<u>2,202,760</u>
<b>Tools</b>		
Intragovernmental		
Program Cost	113,396	63,131
Salary & Expense, NSB and Inspector General Cost	34,295	30,860
<b>Total Intragovernmental Cost</b>	<u>147,691</u>	<u>93,991</u>
With the Public		
Program Cost	1,156,195	1,043,378
Salary & Expense, NSB and Inspector General Cost	42,174	39,216
<b>Total Public Cost</b>	<u>1,198,369</u>	<u>1,082,594</u>
Total Tools Program Cost	1,346,060	1,176,585
Less: Intragovernmental Earned Revenues	28,509	26,320
<b>Net Tools Program Cost</b>	<u>1,317,551</u>	<u>1,150,265</u>
<b>Net Cost of Operations</b> (Note 10)	<u>\$ 4,707,771</u>	<u>\$ 4,132,266</u>

The accompanying notes are an integral part of these statements.

**National Science Foundation**  
**Statement of Changes in Net Position**  
**For the Year Ended September 30, 2003**  
(Amounts in Thousands)

	<u>Cumulative Results of Operations</u>	<u>Unexpended Appropriations</u>
<b>Beginning Balances</b>	\$ 258,027	\$ 6,089,118
<b>Budgetary Financing Sources</b>		
Appropriations Received (Net of Offsetting Receipts)	-	5,410,035
Appropriations Transferred In/(Out)	-	13,143
Other Adjustments	-	(67,254)
Appropriations Used	4,673,452	(4,673,452)
Nonexchange Revenue	49	-
Donations and Forfeitures of Cash	42,113	-
<b>Other Financing Sources</b>		
Transfers-in/out Without Reimbursement	54	-
Imputed Financing from Costs Absorbed by Others	7,700	-
<b>Total Financing Sources</b>	<u>4,723,368</u>	<u>682,472</u>
Net Cost of Operations (Note 10)	<u>4,707,771</u>	<u>-</u>
<b>Ending Balances</b>	<u>\$ 273,624</u>	<u>\$ 6,771,590</u>

The accompanying notes are an integral part of these statements.

**National Science Foundation**  
**Statement of Changes in Net Position**  
**For the Year Ended September 30, 2002**  
(Amounts in Thousands)

	<u>Cumulative Results of Operations</u>	<u>Unexpended Appropriations</u>
<b>Beginning Balances</b>	\$ 243,312	\$ 5,343,547
<b>Budgetary Financing Sources</b>		
Appropriations Received (Net of Offsetting Receipts)	-	4,869,579
Appropriations Transferred In/(Out)	-	14,000
Other Adjustments	-	(30,086)
Appropriations Used	4,107,922	(4,107,922)
Nonexchange Revenue	87	-
Donations and Forfeitures of Cash	32,606	-
<b>Other Financing Sources</b>		
Imputed Financing from Costs Absorbed by Others	<u>6,366</u>	<u>-</u>
<b>Total Financing Sources</b>	4,146,981	745,571
Net Cost of Operations (Note 10)	<u>4,132,266</u>	<u>-</u>
<b>Ending Balances</b>	<u>\$ 258,027</u>	<u>\$ 6,089,118</u>

The accompanying notes are an integral part of these statements.



**National Science Foundation**  
**Statement of Budgetary Resources**  
**For the Year Ended September 30, 2003 and 2002**  
(Amounts in Thousands)

**Budgetary Resources**

	<u>2003</u>	<u>2002</u>
<b>Budgetary Authority: (Note 11)</b>		
Appropriations Received	\$ 5,452,197	\$ 4,902,272
Net Transfers	13,143	14,000
<b>Unobligated Balance – Beginning of Period</b>	304,817	239,272
<b>Spending Authority from Offsetting Collections:</b>		
Earned:		
Collected	\$ 75,568	\$ 111,198
Receivable from Federal Sources	18,062	(5,403)
Change in Unfilled Customer Orders:		
Advance Received	(58,598)	(14,594)
Without Advance from Federal Sources	73,755	(5,309)
Subtotal	<u>108,787</u>	<u>85,892</u>
<b>Recoveries of Prior Year Obligations</b>	65,399	47,092
<b>Permanently Not Available</b>	(67,271)	(30,076)
<b>Total Budgetary Resources</b>	<u>\$ 5,877,072</u>	<u>\$ 5,258,452</u>

**Status of Budgetary Resources**

<b>Obligations Incurred:</b>		
Direct	\$ 5,469,724	\$ 4,868,335
Reimbursable	108,920	85,300
Subtotal	<u>\$ 5,578,644</u>	<u>\$ 4,953,635</u>
<b>Unobligated Balance:</b>		
Apportioned	202,221	213,344
<b>Unobligated Balance Not Available</b>	96,207	91,473
<b>Total Status of Budgetary Resources</b>	<u>\$ 5,877,072</u>	<u>\$ 5,258,452</u>

**Relationship of Obligations to Outlays**

<b>Net Obligated Balance – Beginning of Period</b>	\$ 6,114,623	\$ 5,480,812
<b>Net Obligated Balance – End of Period</b>		
Accounts Receivable	(18,247)	(185)
Unfilled Customer Orders from Federal Sources	(76,261)	(2,505)
Undelivered Orders	6,561,867	5,872,382
Accounts Payable	317,088	244,931
<b>Total Net Obligated Balance – End of Period</b>	<u>\$ 6,784,447</u>	<u>\$ 6,114,623</u>
<b>Outlays:</b>		
Disbursements	\$ 4,751,604	\$ 4,283,444
Collections	(16,970)	(96,604)
Subtotal	<u>4,734,634</u>	<u>4,186,840</u>
<b>Less: Offsetting Receipts</b>	42,162	32,693
<b>Net Outlays</b>	<u>\$ 4,692,472</u>	<u>\$ 4,154,147</u>

The accompanying notes are an integral part of these statements.

**National Science Foundation**  
**Statement of Financing**  
**For the Year Ended September 30, 2003 and 2002**  
(Amounts in Thousands)

<i>Resources Used to Finance Activities</i>	<u>2003</u>	<u>2002</u>
<b>Budgetary Resources Obligated</b>		
Obligations Incurred	\$ 5,578,644	\$ 4,953,635
Less: Spending Authority for Offsetting Collections and Recoveries	174,186	132,984
Obligations Net of Offsetting Collections and Recoveries	5,404,458	4,820,651
Less: Offsetting Receipts	42,162	32,693
<b>Net Obligations</b>	5,362,296	4,787,958
<b>Other Resources</b>		
Transfers-in	54	
Imputed Financing from Costs Absorbed by Others	7,700	6,366
<b>Net Other Resources Used to Finance Activities</b>	7,754	6,366
<b>Total Resources Used to Finance Activities</b>	5,370,050	4,794,324
<b>Resources Used to Finance Items not Part of the Net Cost of Operations</b>		
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered but not yet Provided	(698,707)	(674,451)
Resources that Fund Expenses Recognized in Prior Periods	369	93
Budgetary Offsetting Collections and Receipts that do not affect Net Cost of Operations	42,162	32,693
Resources that Finance the Acquisition of Assets	(24,029)	(35,694)
<b>Total Resources Used to Finance Items not Part of the Net Cost of Operations</b>	(680,205)	(677,359)
<b>Total Resources Used to Finance Net Cost of Operations</b>	4,689,845	4,116,965
<b>Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period</b>		
<b>Components Requiring or Generating Resources in Future Periods</b>		
Other	516	516
<b>Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods (Note 13)</b>	516	516
<b>Components not Requiring or Generating Resources</b>		
Depreciation and Amortization	17,314	14,737
Revaluation of Assets or Liabilities	17	(9)
Other	79	57
<b>Total Components of Net Cost of Operations that will not Require or Generate Resources</b>	17,410	14,785
<b>Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period</b>	17,926	15,301
<b>Net Cost of Operations (Note 10)</b>	\$ 4,707,771	\$ 4,132,266

The accompanying notes are an integral part of these statements.

## **Note 1. Summary of Significant Accounting Policies**

### **A. Reporting Entity**

The National Science Foundation (NSF or Foundation) is an independent federal agency created by the National Science Foundation Act of 1950, as amended (42 U.S.C. 1861-75). Its aim is to promote and advance scientific progress in the United States. NSF initiates and supports basic scientific research and research fundamental to the engineering process and programs to strengthen scientific and engineering research potential. NSF also supports science and engineering education programs at all levels in all fields of science and engineering. NSF funds research and education in science and engineering by awarding grants and contracts to educational and research institutions in all parts of the United States. NSF, by law, cannot operate research facilities. By award, NSF enters into relationships to fund the research operations conducted by grantees.

NSF is led by a Presidentially-appointed director and the policy-making National Science Board (NSB). The NSB, composed of 24 members, represents a cross section of American leaders in science and engineering research and education. Members are appointed by the President for six-year terms. The NSF Director is a member *ex officio* of the Board.

NSF is authorized to accept (and use) U.S. and foreign funds into the NSF Donation Account per the General Authority of the Foundation as found in 42 U.S.C. 1862 Section 3 (a)(3), to foster the interchange of scientific and engineering information among scientists and engineers in the United States and foreign countries, and also in 42 U.S.C. 1870 Section 11 (f) which allows NSF to receive and use funds donated by others. Donations are received from foreign governments, private companies, academic institutions, non-profit foundations and individuals. Donated funds are either earmarked for a specific NSF program or unrestricted, and can be used on one or more of the general purposes of the Foundation. NSF maintains three interest bearing accounts; interest earned on the bank deposits are used for the same purpose as the principal donations. When needed for program support, donations are transferred into the trust fund account at the U.S. Treasury. Funds are made available for obligations as necessary to support NSF programs.

### **B. Basis of Presentation**

These financial statements have been prepared to report the financial position and results of operations of NSF as required by the Chief Financial Officers Act of 1990; the Government Management Reform Act of 1994; the Reports Consolidation Act of 2000; and the Office of Management and Budget Bulletin No. 01-09, *Form and Content of Agency Financial Statements*. They have been prepared from the books and records of NSF in accordance with generally accepted accounting principles in the United States of America. These statements are therefore different from the financial reports, also prepared by NSF pursuant to OMB directives, that are used to monitor and control NSF's use of budgetary resources.

The *FY 2005 Budget of the United States* (also known as the President's Budget) will include actual numbers for FY 2003; the FY 2005 Budget was not published at the time these financial statements were issued. The President's Budget is expected to be published in February 2004 and will be available from the United States Government Printing Office. There are no differences in

the actual amounts for FY 2002 that have been reported in the FY 2004 Budget of the United States and the actual numbers that appear in the FY 2002 Statement of Budgetary Resources.

### **C. Basis of Accounting**

The accompanying financial statements have been prepared using the accrual method of accounting in addition to recognizing certain budgetary transactions. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls that guide the use of federal funds. NSF records grant expenses from expenditure reports submitted by the grantees.

### **D. Revenues and Other Financing Sources**

NSF receives the majority of its funding through appropriations contained in the Departments of Veterans Affairs, Housing and Urban Development, and Independent Agencies Appropriations Act. NSF receives both annual and multi-year appropriations that may be expended, within statutory limits. Additional amounts are obtained through reimbursements for services provided to other federal agencies; allocation transfers from other federal agencies; and donations to the trust fund account. Also, NSF receives interest earned on overdue receivables and excess cash advances to grantees. The interest earned on overdue receivables is returned to the Treasury. Interest earned on excess cash advances to grantees is sent directly to the Department of Health and Human Services in accordance with OMB Circular A-110, *Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Non Profit Organizations*.

Appropriations are recognized as a financing source at the time the related “funded” program or administrative expenses are incurred. Appropriations are also recognized when used to purchase property, plant and equipment. “Unfunded” liabilities result from liabilities not covered by budgetary resources and will be paid when future appropriations are made available for these purposes. Donations are recognized as revenues when funds are received. Revenues from reimbursable agreements are recognized when the services are provided and the related expenditures are incurred. Reimbursable agreements are mainly for grant administrative services provided by NSF on behalf of other federal agencies.

In FY 2002, separate funding was authorized for the National Science Board, in the National Science Foundation Authorization Act of 2002, P.L. 107-368 and was initially provided in the FY 2003 appropriation, P.L 108-7. The Board, established with the National Science Foundation in 1950, establishes policies and approves programs and budgets for the NSF. The Board is also called upon to provide advice to the President and the Congress on matters of science and engineering policy.

### **E. Fund Balance with Treasury and Cash**

Cash receipts and disbursements are processed by the Treasury. The Fund Balance with Treasury is composed primarily of appropriated funds that are available to pay current liabilities and finance authorized purchase commitments, but also includes non-appropriated funding sources

from donations and other revenue received from an NSF cooperative agreement to register Internet domain names.

NSF has also established commercial bank accounts to hold some donated funds in trust, in interest bearing accounts as permitted by the contributors. These funds are collateralized by the bank through the U.S. Treasury.

#### **F. Accounts Receivable, Net**

Accounts Receivable consists of amounts due from governmental agencies, private organizations and individuals. NSF establishes an allowance for accounts receivable from private sources that are deemed uncollectible but regards amounts due from other federal agencies as fully collectible. Due to the small number and dollar amount of the private receivables, NSF analyzes each account independently to assess collectability and the need for an offsetting allowance or write-off.

#### **G. Advances**

Advances consist of advances to grantees, contractors, and employees. Advance payments are made to grant recipients so that recipients may incur expenses related to the approved grant. Payments are only made within the amount of the recorded grant obligation and are intended to cover immediate cash needs. Total grant expenditures for the year include an estimate of fourth quarter amounts due and payable to grantees. The estimate is compiled using historical grantee expenditure data. For those grantees with advance payments exceeding expenditures, the aggregate difference is reported as an advance. Additionally, for those grantees with expenditures exceeding advance payments, the aggregate difference is reported as a grant liability. Advances to contractors are payments made in advance of incurring expenses. Advances to employees are related to travel. Advances are reduced when documentation supporting the expenditures is received.

#### **H. General Property, Plant and Equipment (PP&E)**

##### PP&E

NSF capitalizes acquisitions with costs exceeding \$25,000 and useful lives of two or more years. Acquisitions not meeting these criteria are recorded as operating expenses. NSF currently reports capitalized PP&E at original acquisition cost; assets acquired from General Services Administration's (GSA) excess property schedules are recorded at the value assigned by the donating agency; assets transferred in from other agencies are at the cost recorded by the transferring entity for the asset net of accumulated depreciation or amortization. Depreciation expense is calculated using the straight-line method. The economic life classifications for capitalized assets are as follows:

##### Equipment

- 5 years - computers and peripheral equipment, fuel storage tanks, laboratory equipment, and vehicles
- 7 years - communications equipment, office furniture and equipment,

*National Science Foundation  
Notes to the Financial Statements  
For the Years Ended September 30, 2003 and 2002*

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10 years - pumps and compressors  
generators, Department of Defense equipment

Aircraft and Satellites

7 years - aircraft, aircraft conversions, and satellites

Buildings and Structures

31.5 years - buildings and structures placed in service prior to 1993  
39 years - buildings and structures placed in service after 1993

Internal Use Software

5 years - internal use software

Leasehold Improvements

The economic life of Leasehold Improvements is amortized over the number of years remaining on the lease for the NSF headquarters building. In FY 2003, Leasehold Improvements completed during FY 2003 will be amortized over 10 years, which represents the remaining years on NSF's lease with GSA.

The PP&E balance consists of Equipment, Aircraft and Satellites, Buildings and Structures, Leasehold Improvements, and Construction in Progress. Costs are accumulated in construction in progress until such time as the project is completed and at that time capitalized and depreciated over the respective useful life of the assets. These balances are comprised of PP&E maintained "in-house" by NSF to support agency operations and PP&E under the U.S. Antarctic Program (USAP). The majority of USAP property is currently the custodial responsibility of Raytheon Technical Services Company, the NSF contractor for the program. Additionally, the U.S. Navy's Space and Naval Warfare Center and the Air National Guard 109th also have custodial responsibility for some USAP property.

Office Space

The NSF headquarters building is leased through the GSA. NSF is billed by GSA for the leased space as rent based upon estimated lease payments made by GSA plus an administrative fee. The cost of the headquarters building is not capitalized by NSF. The cost of leasehold improvements performed by GSA is financed with NSF appropriated funds. The leasehold improvements are capitalized by NSF as they are transferred from CIP upon completion, if the leasehold improvements meet NSF's capitalization threshold. Amortization is calculated using the straight-line method over the lesser of their useful lives or the unexpired lease term.

Internal Use Software

NSF controls, values and reports purchased or developed software as tangible property assets, in accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 10, "Accounting for Internal Use Software." NSF identifies software investments as accountable

property for items that in the aggregate cost \$500,000 or more to purchase, develop, enhance or modify a new or existing NSF system. Software projects that are not completed at year end and are expected to exceed the capitalization threshold are recorded as software in development. All internal use software meeting the capitalization threshold is amortized over a five-year period using the straight-line method.

*Assets Owned by NSF in the Custody of Other Entities*

NSF awards grants, cooperative agreements and contracts to various organizations, including colleges and universities; non-profit organizations; state and local governments; Federally Funded Research and Development Centers; and private entities. The funds provided may be used in certain cases to purchase or construct Property, Plant, and Equipment to be used for operations or research on the projects or programs supported by NSF. In these instances, NSF funds the acquisition of property but transfers control to these entities. NSF's authorizing legislation specifically prohibits the Foundation from operating such property directly. In practice, NSF's ownership interest in such PP&E is similar to a reversionary interest. To address the accounting and reporting of these assets, specific guidance was sought by NSF and provided by the Federal Accounting Standards Advisory Board (FASAB). This guidance stipulated that NSF should: (i) Disclose the value of such PP&E held by others in its financial statements based on information contained in the audited financial statements of these entities (if available). Where separate audited amounts are not available for a specific entity, NSF should name the entity and note that these amounts are unavailable; and (ii) report information on costs incurred to acquire the research facilities, equipment, and platforms in the Research and Human Capital Activity costs as required by the Statement of Federal Financial Accounting Standards No. 8, *Supplementary Stewardship Reporting*.

**I. Advances from Others**

Advances from Others consist of prior year amounts obligated and advanced by other federal entities to NSF for grant administration and other services furnished under reimbursable agreements. Balances at the end of the year are adjusted by an allocated amount from the fourth quarter grantee expenditure estimate described under Note 1G, Advances. The amount to be allocated is based on a percentage of the reimbursable grant expenditures, by partner agencies to NSF, to the total grant expenditures. In FY 2003, NSF implemented OMB Memorandum M-03-01, *Business Rules for Intra-Governmental Transactions*, which establishes a set of guidelines that agencies must use in order to standardize the processing and recording of intra-governmental activity among federal entities. These new guidelines required NSF to transition from accepting advances from other agencies to billing on a reimbursable basis.

**J. Accounts Payable**

Accounts Payable consists of liabilities to commercial vendors, contractors, and disbursements in transit. Accounts payable to commercial vendors are expenses for goods and services received but not yet paid by NSF at the end of the fiscal year. At year end, NSF accrues for the amount of estimated unpaid expenses to commercial vendors. Contract liabilities are estimated expenses over and above the amount of advances given to contractors. At year end, NSF accrues the

amount of estimated expenses not covered by advances given to contractors. Intra-governmental accounts payable consists of disbursements in transit recorded by NSF but not paid by Treasury.

#### **K. Other Liabilities**

Other liabilities consist of grant accruals, accrued payroll, benefits, and income taxes withheld. Grant liabilities are estimated grantee expenses over and above the amount of advances given to grantees. At year end, NSF accrues for the amount of estimated grantee expenses not covered by advances given to grantees. Accrued payroll, benefits and income taxes withheld relate to services rendered by NSF employees but not yet paid. At year end, NSF accrues the actual amount of wages and benefits earned but not yet paid and income tax withholdings.

#### **L. Annual, Sick, and Other Leave**

Annual leave is accrued as it is earned and the accrual is reduced as leave is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect changes. To the extent current and prior-year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future Salaries and Expenses appropriations. Sick leave and other types of non-vested leave are expensed as taken.

#### **M. Employee Benefits**

A liability is recorded for estimated and actual future payments to be made for workers' compensation pursuant to the Federal Employees' Compensation Act (FECA). The liability consists of the net present value of estimated future payments calculated by the U.S. Department of Labor (DOL) and the actual unreimbursed cost paid by DOL for compensation paid to recipients under FECA. The actual costs incurred are reflected as a liability because NSF will reimburse DOL two years after the actual payment of expenses. Future NSF Salaries and Expenses Appropriations will be used for DOL's estimated reimbursement.

#### **N. Net Position**

Net position is the residual difference between assets and liabilities and is composed of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent the amount of unobligated and unexpended budget authority. Unobligated balances are the amount of appropriations or other authority remaining after deducting the cumulative obligations from the amount available for obligation. Cumulative results of operations are the net result of NSF's operations since inception.

#### **O. Retirement Plan**

In FY 2003, approximately 31 percent of NSF employees participated in the Civil Service Retirement System (CSRS), to which NSF made matching contributions equal to 7 percent of pay. The majority of NSF employees are covered by the Federal Employees Retirement System (FERS) and Social Security. A primary feature of FERS is that it offers a thrift savings plan to which NSF automatically contributes one percent of pay and matches employee contributions up to an additional four percent of pay. NSF also contributes the employer's matching share for Social Security for FERS participants.



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Although NSF funds a portion of the benefits under FERS and CSRS relating to its employees and withholds the necessary payroll deductions, the agency has no liability for future payments to employees under these plans, nor does NSF report CSRS, FERS, or Social Security assets, or accumulated plan benefits on its financial statements. Reporting such amounts is the responsibility of the Office of Personnel Management (OPM) and The Federal Retirement Thrift Investment Board. In FY 2003, NSF's contributions to CSRS and FERS were \$2,448,930, and \$7,108,098, respectively. In FY 2002, NSF's contributions to CSRS and FERS were \$2,994,127 and \$6,282,728, respectively.

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, requires employing agencies to recognize the cost of pensions and other retirement benefits during their employees' active years of service. OPM actuaries determine pension cost factors by calculating the value of pension benefits expected to be paid in the future, and communicate these factors to the agency for current period expense reporting. Information was also provided by OPM regarding the full cost of health and life insurance benefits. In FY 2003, NSF, utilizing OPM-provided cost factors, recognized \$3,835,518 of pension expenses, \$3,845,086 of post-retirement health benefits expenses, and \$19,540 of post-retirement life insurance expenses beyond amounts actually paid. NSF recognized offsetting revenue of \$7,700,144 as an imputed financing source to the extent that these intragovernmental expenses will be paid by OPM.

In FY 2002, NSF, utilizing cost factors dated September 11, 2002, recognized \$2,845,333 of pension expenses; \$3,502,521 of post-retirement health benefits expenses; and \$18,444 of post-retirement life insurance expenses beyond amounts actually paid. NSF recognized offsetting revenue of \$6,366,298 as an imputed financing source to the extent that these intragovernmental expenses will be paid by OPM.

**P. Commitments, Contingencies, and Possible Future Costs**

*Commitments*

Commitments are contractual agreements involving financial obligations. NSF is committed for goods and services that have been ordered but have not yet been delivered.

*Contingencies - Claims and Lawsuits*

NSF is a party to various legal actions and claims brought against it. In the opinion of NSF management and legal counsel, the ultimate resolution of the actions and claims will not materially affect the financial position or operations of the Foundation. NSF recognizes the contingency in the financial statements when claims are expected to result in a material loss, whether from NSF's appropriations or the "Judgment Fund" administered by the Department of Justice under Section 1304 of Title 31 of the United States Code and the payment amounts can be reasonably estimated.

Claims and lawsuits have also been made and filed against awardees of the Foundation by third parties. NSF is not a party to these actions and NSF believes there is no possibility that NSF will be legally required to satisfy such claims. Judgments or settlements of the claims against awardees that impose financial obligation on them may be claimed as costs under the applicable contract, grant, or cooperative agreement and thus may affect the allocation of program funds in

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future fiscal years. In the event that the likelihood of loss on such claims by awardees becomes probable, these amounts can be reasonably estimated and NSF management determines that it will probably pay them, NSF will recognize these potential payments as expenses.

Contingencies – Unasserted Claims

For claims and lawsuits that have not been made and filed against the Foundation, NSF management and legal counsel determine, in their opinion, whether resolution of the actions and claims it is aware of will materially affect the agency's financial position or operations. NSF recognizes a contingency in the financial statements when unasserted claims are probable of assertion, and if asserted would be probable of an unfavorable outcome and expected to result in a measurable loss, whether from NSF's appropriations or the "Judgment Fund." NSF discloses unasserted claims if materiality or measurability of a potential loss cannot be determined or the loss is more likely than not to occur rather than probable.

**Q. Use of Estimates**

The preparation of the accompanying financial statements requires management to make estimates and assumptions about certain estimates included in the financial statements. Actual results will invariably differ from those estimates.

**R. Tax Status**

NSF, as a federal agency, is not subject to federal, state, or local income taxes and, accordingly, no provision for income taxes is recorded.

**Note 2. Fund Balance with Treasury**

Fund Balance with Treasury consisted of the following components as of September 30, 2003 and 2002:

*(Amounts in Thousands)*

	<u>2003</u>			
	Appropriated Funds	Trust Funds	Other Funds	Total
	<hr/>			
Obligated	\$ 6,750,490	32,366	1,591	6,784,447
Unobligated Available	183,303	18,918	-	202,221
Unobligated Unavailable	96,109	98	922	97,129
Total Fund Balance	<u>\$ 7,029,902</u>	<u>51,382</u>	<u>2,513</u>	<u>7,083,797</u>

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(Amounts in Thousands)

	<u>2002</u>			
	Appropriated Funds	Trust Funds	Other Funds	Total
Obligated	\$ 6,092,725	\$ 11,186	\$ 10,712	\$ 6,114,623
Unobligated Available	192,762	20,582	-	213,344
Unobligated Unavailable	91,411	62	260	91,733
Total Fund Balance	<u>\$ 6,376,898</u>	<u>\$ 31,830</u>	<u>\$ 10,972</u>	<u>\$ 6,419,700</u>

\* Certain reclassifications have been made to previously reported 2002 amounts to conform to the 2003 presentation.

Appropriated funds are amounts provided by Congress for NSF operations. Included in appropriated funds are Indian rupees (Rs) in the amount of Rs13,577,123 and Rs14,063,769 converted as of September 30, 2003 and 2002, respectively, to U.S. dollars at the prevailing Treasury rate of 45.70 rupees to \$1 US, or \$297,092 and 48.38 rupees to \$1 US, or \$290,693 respectively.

The Trust Fund includes amounts donated to NSF. Other Funds and Trust Funds are restricted for intended purposes. Unavailable balances include recovered expired appropriations and other amounts related to expired authority and holdings, which are unavailable for NSF use.

"Other Funds" consists of \$1,591,019 and \$10,711,902, as of September 30, 2003 and 2002, respectively, received from a corporation that registered second level Internet domain names under NSF's cooperative agreement and nonexpenditure transfer authorizations, deposits, holdings, and miscellaneous receipt accounts. These "Other Funds" have no budgetary impact and therefore are not part of the unobligated balance per the Statement of Budgetary Resources.

**Note 3. Accounts Receivable, Net**

Intragovernmental

The Intragovernmental Accounts Receivable consists of reimbursements and repayments due from other government agencies. As of September 30, 2003 and 2002, the amount of intragovernmental accounts receivable was \$18,246,756 and \$184,572, respectively. The increase in our Intragovernmental Receivable balance is due to the implementation of OMB's Memorandum M-03-01: *Business Rules for Intragovernmental Transactions*. These rules required NSF to transition to bill agencies on a reimbursable basis after we have incurred costs. Previously, NSF billed most agencies on an advanced basis.

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Public

As of September 30, 2003 and 2002, Accounts Receivable (net) due from private organizations and individuals consisted of:

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
Accounts Receivable	\$ 8,384	\$ 8,753
Allowance for Uncollectible Accounts	<u>(8,182)</u>	<u>(8,182)</u>
Net Amount Due	<u>\$ 202</u>	<u>\$ 571</u>

As of September 30, 2003 and 2002, the reconciliation of the allowance for uncollectible accounts is as follows:

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
Beginning Allowance	\$ 8,182	\$ 8,183
Additions	-	-
Reduction (write-offs)	<u>-</u>	<u>(1)</u>
Ending Allowance	<u>\$ 8,182</u>	<u>\$ 8,182</u>

An allowance was set up in FY 2000 for \$7,929,465, which represents the allowance for a receivable from a grantee that filed for dissolution. The receivable has been forwarded to the Department of Justice, as required by OMB Circular A-129, *Policies for Federal Credit Programs and Non-Tax Receivables*, and U.S.C. 31 Section 3711, for concurrence on the termination of debt.

**Note 4. Advances**

As of September 30, 2003 and 2002, Advances consisted of the following components:

Intragovernmental

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
Advances to Others	\$ 18,557	\$ 8,309

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Public

(Amounts in Thousands)

		<u>2003</u>		<u>2002</u>
Advances to Grantees	\$	66,601	\$	52,472
Advances to Contractors		<u>9</u>		<u>7</u>
Total Advances with the Public	\$	<u>66,610</u>	\$	<u>52,479</u>

**Note 5. Property, Plant and Equipment in the Custody of NSF**

The components of Property, Plant and Equipment as of September 30, 2003 and 2002 were:

(Amounts in Thousands)

	Acquisition		<u>2003</u>		Net
	Cost		Accumulated		Book Value
			Depreciation		
Equipment	\$ 67,066	\$	47,179	\$	19,887
Aircraft and Satellites	138,109		103,321		34,788
Buildings and Structures	89,537		41,169		48,368
Construction in Progress	122,700		-		122,700
Internal Use Software	4,714		1,087		3,627
Software in Development	1,407		-		1,407
Total PP&E	<u>\$ 423,533</u>	\$	<u>192,756</u>	\$	<u>230,777</u>

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(Amounts in Thousands)

	<u>2002</u>		
	Acquisition Cost	Accumulated Depreciation	Net Book Value
Equipment	\$ 62,565	\$ 44,805	\$ 17,760
Aircraft and Satellites	135,865	94,842	41,023
Buildings and Structures	85,034	39,078	45,956
Construction in Progress	116,313	-	116,313
Internal Use Software	2,175	652	1,523
Software in Development	1,566	-	1,566
Total PP&E	<u>\$ 403,518</u>	<u>\$ 179,377</u>	<u>\$ 224,141</u>

**Note 6. Property, Plant and Equipment in the Custody of Other Entities**

NSF received a ruling from FASAB on accounting for PP&E owned by NSF but in the custody of and used by others. The FASAB guidance requires that PP&E in the custody of others be excluded from NSF PP&E as defined in the Statement of Federal Financial Accounting Standards No. 6 *Accounting for Property, Plant and Equipment*, and instead based on information contained in the audited financial statements of the organizations holding the assets disclose the dollar amount of NSF PP&E held by others in the footnotes.

The amount of PP&E owned by NSF but in the custody of other entities identified in the following table was obtained from the respective entities' audited financial statements. If the audited financial statements were not published or released by September 1, or if NSF PP&E is not separately stated on the entities' audited financial statements, then the amounts relating to such entities are annotated as "NA" (Not Available) in the table.

The amounts reported by entities in their audited financial statements submitted as of September 1 are as follows:

(Amounts in Thousands)

Federally Funded Research and Development Centers

	<u>2003</u>	<u>2002</u>	<u>Year End</u>
National Astronomy and Ionosphere Center - Cornell	\$ N/A	\$ N/A	06/30
National Center for Atmospheric Research - UCAR	N/A	137,476	09/30
National Optical Astronomy Observatories - AURA	N/A	384,455	09/30
National Radio Astronomy Observatories - AUI	N/A	295,844	09/30
The Science and Technology Policy Institute - RAND	N/A	N/A	09/30

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Colleges and Universities

	<u>2003</u>		<u>2002</u>	<u>Year End</u>
California Institute of Technology	\$ N/A	\$	N/A	9/30
Columbia University	N/A		N/A	9/30
Cornell University – Endowed	N/A		N/A	9/30
Duke University	N/A		N/A	9/30
Oregon State University	N/A		N/A	9/30
San Jose State University Foundation	N/A		N/A	9/30
University of Alaska Fairbanks Campus	N/A		N/A	9/30
University of California-San Diego	N/A		N/A	9/30
University of Hawaii	N/A		N/A	9/30
University of Miami Rosenstiel School of Marine & Atmospheric Science	N/A		N/A	5/31
University of Rhode Island	N/A		N/A	6/30
University of Texas at Austin	N/A		N/A	8/31
University of Washington	N/A		N/A	6/30
University of Wisconsin	N/A		N/A	6/30

Other Entities

	<u>2003</u>		<u>2002</u>	<u>Year End</u>
Aerodyne Research Inc	\$ N/A	\$	N/A	9/30
Brighton Technologies Group, Inc.	N/A		N/A	Not Audited
Fourth Wave Imaging Corporation	N/A		N/A	12/31
Imago Scientific Instruments Corp	N/A		N/A	9/30
Incorporated Research Institutions for Seismology	N/A		N/A	9/30
Information Systems Laboratories Inc	N/A		N/A	12/31
Joint Oceanographic Institutions Inc	N/A		N/A	9/30
Lucigen Corporation (formerly Microgen - a WI Corp)	N/A		N/A	Not Audited
Lynntech, Inc	N/A		N/A	Not Audited
Physical Optics Corporation	N/A		N/A	12/31
SRI International	N/A		N/A	12/31
T/J Technologies, Inc	N/A		N/A	Not Audited
UNVACO, Inc.	N/A		N/A	12/31
Veco Rocky Mountain Inc.	N/A		N/A	3/31
Weidlinger Associates Inc	N/A		N/A	12/31
Woods Hole Oceanographic Institution	N/A		N/A	12/31
Xencor	N/A		N/A	12/31

**Note 7. Other Liabilities**

Other Liabilities represent current accrued liabilities, which consist of grant and contract accruals, accrued employer contributions for payroll and benefits, disbursements in transit, accrued payroll and benefits, and various employee related liabilities for payroll and benefit deductions. As of September 30, 2003 and 2002, Other Liabilities consisted of the following:

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
<u>Intragovernmental</u>		
Employer Contributions for Payroll Benefits	\$ 396	\$ 321
Total Intragovernmental	<u>\$ 396</u>	<u>\$ 321</u>
<u>Other Liabilities</u>		
Accrued Liabilities	\$ 251,107	\$ 210,738
Accrued Payroll and Benefits	3,893	3,269
State and Other Income Taxes Withheld	915	248
Employee Deductions for U.S. Savings Bonds	8	11
Total Other Liabilities	<u>\$ 255,923</u>	<u>\$ 214,266</u>

**Note 8. Liabilities Not Covered by Budgetary Resources**

Certain liabilities are not funded by current budgetary resources. As of September 30, 2003 and 2002, Liabilities Not Covered by Budgetary Resources consisted of the following:

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
Intragovernmental: FECA Employee Benefits	\$ 264	\$ 254
Public: FECA Employee Benefits	1,649	1,637
Accrued Annual Leave	11,120	10,567
Liabilities Not Covered by Budgetary Resources to Fund		
Cost of Operations	\$ 13,033	\$ 12,458
Lease Liabilities	-	60
Total Liabilities Not Covered By Budgetary Resources	<u>\$ 13,033</u>	<u>\$ 12,518</u>



**Note 9. FECA Employee Benefits**

FECA Employee Benefits consisted of the following components as of September 30, 2003 and 2002:

*(Amounts in Thousands)*

	<u>2003</u>	<u>2002</u>
Intragovernmental: Unreimbursed Actual Costs	\$ 264	\$ 254
Public: Estimated Liability	1,649	1,637
Total Workers' Compensation Benefits	<u>\$ 1,913</u>	<u>\$ 1,891</u>

For Fiscal Years 2003 and 2002, these amounts represent \$264,278 and \$253,872 respectively, of unreimbursed cost to the DOL for actual compensation paid to recipients under FECA. FECA provides income and medical cost protection to cover federal employees injured on the job or who have a work-related injury or occupational disease, and beneficiaries of employees whose death is attributable to a job related injury or occupational disease. The DOL initially pays valid claims and then bills the employing federal agency.

As of September 30, 2003 and 2002, the estimated liability of \$1,649,000 and \$1,637,000, respectively, are for future worker compensation claims calculated by DOL and includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period and annual benefit payments discounted to present value using OMB's economic assumptions for 10-year Treasury notes and bonds. To account for the effects of inflation on the liability, wage and medical inflation factors are applied to the calculation of future benefits.

**Note 10. Statements of Net Cost**

*Major Program Descriptions*

NSF's primary business is to make merit-based grants and cooperative agreements to individual researchers and groups, in partnership with colleges, universities, and other public, private, state, local, and federal institutions, throughout the U.S. By providing these resources, NSF contributes to the health and vitality of the U.S. research and education enterprise, which enables and enhances the Nation's capacity to sustain growth and prosperity. These grants are managed through eight programmatic organizations within NSF that review and evaluate competitive proposals submitted by the science and engineering community for its consideration.

NSF is a single entity for net cost reporting purposes. The NSF programmatic organizations are the Directorates for the Biological Sciences; Computer and Information Science and Engineering; Education and Human Resources; Engineering; Geosciences; Mathematical and Physical Sciences; Social, Behavioral and Economic Sciences; and the Office of Polar Programs.

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The Statement of Net Cost is a general overall presentation of NSF wide expenses incurred by the agency. The presentation of the statement of Net Cost is aligned with NSF's strategic goals of People (P), Ideas (I), and Tools (T). These goals are outlined in NSF's FY 2003 GPRA Performance Plan ([www.nsf.gov/od/gpra/perfplan/fy2003/fy2003revisedfinalplan](http://www.nsf.gov/od/gpra/perfplan/fy2003/fy2003revisedfinalplan)) and in NSF's FY 2003 Budget Request ([www.nsf.gov/bfa](http://www.nsf.gov/bfa)).

In pursuit of its mission, NSF makes investments in People, Ideas, and Tools. These goals reflect outcomes at the heart of the research enterprise: a world-class science and engineering workforce (People); the generation of new knowledge across the frontiers of science and engineering (Ideas); and the Tools to get the job done efficiently and effectively. People produce the Ideas that are the currency of the new knowledge-based economy. The need for more sophisticated Tools has paralleled recent advances in science and engineering, creating a growing demand for access to them. NSF's overall strategy is to invest in state-of-the-art tools that add unique value to research and are accessible and widely shared among researchers across the nation.

Approximately 96 percent of NSF's investments are directly related to the People, Ideas, and Tools (PIT) strategic areas of focus. About four percent of NSF's investments are for support of management and administrative activities. All investment costs are assigned to the three strategic PIT areas.

In FYs 2002 and 2003, management and administration activities include Salary & Expenses, NSB and Office of Inspector General (OIG) expenses which provide for salaries and benefits of persons employed at the NSF; general operating expenses, including key activities to advance the NSF information systems technology and to enhance staff training, audit and OIG activities, and OPM and DOL benefits costs paid on behalf of NSF. These indirect costs are allocated to NSF programs based on each program's direct costs.

In accordance with OMB Bulletin 01-09, *Form and Content of Agency Financial Statements*, costs incurred for services provided by other federal entities are reported in the full costs of NSF programs and are identified as "intragovernmental." All earned revenues are funding sources provided through reimbursable agreements with other federal entities and are retained by NSF. Earned revenues are recognized when the related program or administrative expenses are incurred and are deducted from the full cost of the programs to arrive at the net cost of operating NSF's programs.

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Gross Cost and Earned Revenue by Budget Functional Classification

Total Gross Cost and Earned Revenue by Budget Functional Classification for FYs 2003 and 2002 were as follows:

*(Amounts in Thousands)*

<u>Budget Functional Classification</u>		
NSF – General Science, Space and Technology (Code 250)		
	<u>2003</u>	<u>2002</u>
Gross Cost	\$ 4,801,163	\$ 4,237,468
Earned Revenue	<u>93,392</u>	<u>105,202</u>
Net Cost	<u>\$ 4,707,771</u>	<u>\$ 4,132,266</u>

Intragovernmental Gross Cost and Earned Revenue by Budget Functional Classification

Intragovernmental Gross Cost and Earned Revenue by Budget Functional Classification for FYs 2003 and 2002 were as follows:

*(Amounts in Thousands)*

<u>Budget Functional Classification</u>		
NSF – General Science, Space and Technology (Code 250)		
	<u>2003</u>	<u>2002</u>
Gross Cost	\$ 157,356	\$ 114,981
Earned Revenue	<u>93,392</u>	<u>105,202</u>
Net Cost	<u>\$ 63,964</u>	<u>\$ 9,779</u>

**Note 11. Budget Authority**

Budget Authority includes \$42,161,490 and \$32,693,473 of donations and interest as of September 30, 2003 and 2002, respectively. Budget Authority was increased for non-expenditure transfers from the U.S. Agency for International Development for \$13,143,175 in 2003, and \$14,000,000 in 2002. Budget Authority as of September 30, 2003 and 2002 was also adjusted for Congressional initiated rescissions contained in P.L. 108-7 totaling \$34,740,498 and P.L. 107-206 totaling \$314,000, respectively.

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NSF maintains permanent indefinite appropriations for Research and Related Activities - 49x0100, Major Research Equipment - 49x0551, H-1B Nonimmigrant Petitioner fees - 49x5176, and Trust Fund donations - 49x8960.

The status of Budgetary Resources as of September 30, 2003, consisted of Budgetary Resources obligated of \$5,578,644,000 available authority of \$202,220,949 and unavailable authority of \$96,207,143. The status of Budgetary Resources as of September 30, 2002, included Budgetary Resources obligated of \$4,953,634,607, available authority of \$213,343,532 and unavailable authority of \$91,473,438.

**Note 12. Commitments and Contingencies**

*Unasserted Claims*

NSF has been informed of potential contractor claims for additional compensation under a contract, awarded by the United States Air Force, for reconfiguration of three NSF-owned aircraft. NSF will work with the Air Force to determine the validity of the potential contractor's claims. It is NSF's opinion that payment of some additional compensation is probable. Since the claims have not been formally presented, documented and assessed, the amount of additional compensation has not been determined.

*Environmental Costs*

NSF manages the U.S. Antarctic Program. The Antarctic Conservation Act and its implementing regulations identify the requirements for environmental cleanup in Antarctica. NSF continually monitors the U.S. Antarctic Program in regards to environmental issues.

A project that NSF is currently undertaking is limited clean-up of a former research station at Cape Hallett, in cooperation with the New Zealand Antarctic Program. The station was jointly operated by the U.S. and New Zealand from 1957 to 1973. In the past year, progress has been made in determining the scope of the effort that will need to be undertaken to assess clean-up activities. This assessment effort is being planned over the next two years. Approximately \$85,000 will be spent in fiscal year 2004 for the initial assessment and equipment. At present, the full extent of the clean-up activities required at Cape Hallett has yet to be determined.

**Note 13. Statement of Financing Disclosures**

*Explanation of the Relationship Between Liabilities Not Covered by Budgetary Resources on the Balance Sheet and the Change in Components Requiring or Generating Resources in Future Periods.*

Liabilities Not Covered by Budgetary Resources of \$13,032,863 and \$12,517,321 for FY 2003 and 2002, respectively, represent NSF's FECA liability to DOL and employees, leave earned but not taken and lease liabilities. The amount reported on the Statement of Financing as Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods of \$515,543 for FY 2003 and \$516,689 for FY 2002, represents the change in NSF's expenses for unfunded liabilities for FECA, leave earned but not taken and lease liabilities.

**Required Supplementary Information**  
Budgetary Resources by Major Budgetary Accounts

In the following table, NSF budgetary information for the fiscal years ended September 30, 2003 and 2002, as presented in the Statement of Budgetary Resources, is disaggregated for each of NSF's major budgetary accounts.

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**2003**  
(Amounts in Thousands)

	<u>Research and Related</u>	<u>Education</u>	<u>Major Research Equipment</u>	<u>OIG, S&amp;E, and NSB</u>	<u>Trust Fund</u>	<u>Total</u>
<b>Budgetary Resources</b>						
<b>Budget Authority:</b>						
Appropriations Received	\$ 4,083,000	974,423	149,510	203,102	42,162	\$ 5,452,197
Net Transfers	12,828	-	-	315	-	13,143
<b>Unobligated Balances – Beginning of Period</b>	<b>56,677</b>	<b>128,172</b>	<b>96,551</b>	<b>2,773</b>	<b>20,644</b>	<b>304,817</b>
<b>Spending Authority from Offsetting Collections:</b>						
Earned:						
Collected	62,487	8,261	-	4,819	1	75,568
Receivable from Federal Sources	17,067	621	-	374	-	18,062
Change in Unfilled Customer Orders:						
Advance Received	(50,871)	(7,724)	-	(3)	-	(58,598)
Without Advance from Federal Sources	70,396	3,359	-	-	-	73,755
Anticipated for Rest of Year, Without Advance	-	-	-	-	-	-
Spending Authority Subtotal	<u>99,079</u>	<u>4,517</u>	<u>-</u>	<u>5,190</u>	<u>1</u>	<u>108,787</u>
<b>Recoveries of Prior Year Obligations</b>	<b>38,858</b>	<b>24,418</b>	<b>48</b>	<b>1,962</b>	<b>113</b>	<b>65,399</b>
<b>Permanently Not Available</b>	<b>(45,794)</b>	<b>(18,012)</b>	<b>(972)</b>	<b>(2,493)</b>	<b>-</b>	<b>(67,271)</b>
<b>Total Budgetary Resources</b>	<b>\$ 4,244,648</b>	<b>1,113,518</b>	<b>245,137</b>	<b>210,849</b>	<b>62,920</b>	<b>\$ 5,877,072</b>
<b>Status of Budgetary Resources</b>						
<b>Obligations Incurred:</b>						
Direct	\$ 4,062,220	983,131	179,029	201,440	43,904	\$ 5,469,724
Reimbursable	99,384	4,508	-	5,028	-	108,920
Total Obligations Incurred	<u>4,161,604</u>	<u>987,639</u>	<u>179,029</u>	<u>206,468</u>	<u>43,904</u>	<u>5,578,644</u>
<b>Unobligated Balances:</b>						
Apportioned	28,075	87,914	66,060	1,254	18,918	202,221
<b>Unobligated Balances Not Available</b>	<b>54,969</b>	<b>37,965</b>	<b>48</b>	<b>3,127</b>	<b>98</b>	<b>96,207</b>
<b>Total Status of Budgetary Resources</b>	<b>\$ 4,244,648</b>	<b>1,113,518</b>	<b>245,137</b>	<b>210,849</b>	<b>62,920</b>	<b>\$ 5,877,072</b>
<b>Relationship of Obligations to Outlays</b>						
<b>Net Obligated Balance – Beginning of Period</b>	<b>\$ 4,441,353</b>	<b>1,499,264</b>	<b>137,418</b>	<b>25,402</b>	<b>11,186</b>	<b>\$ 6,114,623</b>
<b>Net Obligated Balance – End of Period</b>						
Accounts Receivable	(17,134)	(621)	-	(492)	-	(18,247)
Unfilled Customer Orders from Federal Sources	(72,895)	(3,359)	-	(7)	-	(76,261)
Undelivered Orders	4,699,456	1,616,122	191,010	20,083	35,196	6,561,867
Accounts Payable	246,434	49,247	7,472	16,765	(2,830)	317,088
<b>Total Net Obligated Balance – End of Period</b>	<b>\$ 4,855,861</b>	<b>1,661,389</b>	<b>198,482</b>	<b>36,349</b>	<b>32,366</b>	<b>\$ 6,784,447</b>
<b>Outlays</b>						
Disbursements	\$ 3,620,775	797,117	117,916	193,186	22,610	\$ 4,751,604
Collections	(11,616)	(537)	-	(4,816)	(1)	(16,970)
Subtotal	<u>3,609,159</u>	<u>796,580</u>	<u>117,916</u>	<u>188,370</u>	<u>22,609</u>	<u>4,734,634</u>
Less: Offsetting Receipts	-	-	-	-	42,162	42,162
<b>Net Outlays</b>	<b>\$ 3,609,159</b>	<b>796,580</b>	<b>117,916</b>	<b>188,370</b>	<b>(19,553)</b>	<b>\$ 4,692,472</b>

*National Science Foundation  
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	<b>2002</b> (Amounts in Thousands)						
	<b>* Research and Related</b>	<b>Education</b>	<b>Major Research Equipment</b>	<b>** OIG and Salary Expense</b>	<b>Trust Fund</b>		<b>Total</b>
<b>Budgetary Resources</b>							
<b>Budget Authority:</b>							
Appropriations Received	\$ 3,598,639	955,339	138,800	176,800	32,694	\$	4,902,272
Net Transfers	13,664	-	-	336	-		14,000
<b>Unobligated Balances – Beginning of Period</b>	<b>51,126</b>	<b>95,184</b>	<b>73,093</b>	<b>2,194</b>	<b>17,675</b>		<b>239,272</b>
<b>Spending Authority from Offsetting Collections:</b>							
Earned:							
Collected	96,321	10,214	-	4,662	1		111,198
Receivable from Federal Sources	(4,976)	-	-	(427)	-		(5,403)
Change in Unfilled Customer Orders:							
Advance Received	(5,807)	(8,785)	-	(2)	-		(14,594)
Without Advance from Federal Sources	(5,316)	-	-	7	-		(5,309)
Subtotal	80,222	1,429	-	4,240	1		85,892
<b>Recoveries of Prior Year Obligations</b>	<b>31,408</b>	<b>14,115</b>	<b>10</b>	<b>1,475</b>	<b>84</b>		<b>47,092</b>
<b>Permanently Not Available</b>	<b>(19,102)</b>	<b>(9,596)</b>	<b>-</b>	<b>(1,378)</b>	<b>-</b>		<b>(30,076)</b>
<b>Total Budgetary Resources</b>	<b>\$ 3,755,957</b>	<b>1,056,471</b>	<b>211,903</b>	<b>183,667</b>	<b>50,454</b>	<b>\$</b>	<b>5,258,452</b>
<b>Status of Budgetary Resources</b>							
<b>Obligations Incurred:</b>							
Direct	\$ 3,619,230	927,135	115,352	176,809	29,809	\$	4,868,335
Reimbursable	80,051	1,164	-	4,085	-		85,300
Subtotal	3,699,281	928,299	115,352	180,894	29,809		4,953,635
<b>Unobligated Balances:</b>							
Apportioned	2,897	92,982	96,541	342	20,582		213,344
<b>Unobligated Balances Not Available</b>	<b>53,779</b>	<b>35,190</b>	<b>10</b>	<b>2,431</b>	<b>63</b>		<b>91,473</b>
<b>Total Status of Budgetary Resources</b>	<b>\$ 3,755,957</b>	<b>1,056,471</b>	<b>211,903</b>	<b>183,667</b>	<b>50,454</b>	<b>\$</b>	<b>5,258,452</b>
<b>Relationship of Obligations to Outlays</b>							
<b>Net Obligated Balance – Beginning of Period</b>	<b>\$ 3,984,208</b>	<b>1,300,605</b>	<b>158,613</b>	<b>24,957</b>	<b>12,429</b>	<b>\$</b>	<b>5,480,812</b>
<b>Net Obligated Balance – End of Period</b>							
Accounts Receivable	(66)	-	-	(119)	-		(185)
Unfilled Customer Orders from Federal Sources	(2,499)	-	-	(6)	-		(2,505)
Undelivered Orders	4,258,391	1,457,364	131,030	10,689	14,908		5,872,382
Accounts Payable	185,527	41,900	6,388	14,838	(3,722)		244,931
<b>Total Net Obligated Balance – End of Period</b>	<b>\$ 4,441,353</b>	<b>1,499,264</b>	<b>137,418</b>	<b>25,402</b>	<b>11,186</b>	<b>\$</b>	<b>6,114,623</b>
<b>Outlays</b>							
Disbursements	\$ 3,221,019	715,526	136,538	179,393	30,968	\$	4,283,444
Collections	(90,514)	(1,430)	-	(4,659)	(1)		(96,604)
Subtotal	3,130,505	714,096	136,538	174,734	30,967		4,186,840
<b>Less: Offsetting Receipts</b>		-	-	-	32,693		32,693
<b>Net Outlays</b>	<b>\$ 3,130,505</b>	<b>714,096</b>	<b>136,538</b>	<b>174,734</b>	<b>(1,726)</b>	<b>\$</b>	<b>4,154,147</b>

\* Certain reclassifications have been made to previously reported 2002 amounts to conform to the 2003 presentation.

\*\* Funding for the National Science Board became effective October 1, 2002 and was established by the National Science Foundation Act of 1950.

**Required Supplementary Information**  
Intragovernmental Balances and Deferred Maintenance



*National Science Foundation  
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**Intragovernmental Assets by Partner Agency (Unaudited)**

Intragovernmental assets on this schedule support the intragovernmental asset line items on NSF's Balance Sheets as of September 30, 2003 and 2002. Intragovernmental balances included in Fund Balance with Treasury as of September 30, 2003 and 2002, consisted of the following:

*(Amounts in Thousands)*

<u>Agency</u>	<u>2003</u>	<u>2002</u>
Department of State	\$ 297	\$ 291
Department of the Treasury	7,083,500	6,419,409
Total	<u>\$ 7,083,797</u>	<u>\$ 6,419,700</u>

*National Science Foundation  
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 For the Years Ended September 30, 2003 and 2002*

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Intragovernmental Accounts Receivable balances as of September 30, 2003 and 2002, consisted of the following:

*(Amounts in Thousands)*

<u>Agency</u>	<u>2003</u>	<u>2002</u>
Central Intelligence Agency	\$ 3,374	\$ 96
Department of Agriculture	66	-
Department of the Air Force	547	
Department of the Army	819	
Department of Commerce	886	-
Department of Defense	2,486	89
Department of Education	166	
Department of Energy	1,276	-
Department of Health and Human Services	4,796	-
Department of Homeland Security	117	
Department of Housing and Urban Development	135	
Department of the Interior	58	-
Department of Justice	7	
Department of Labor	44	
Department of the Navy	303	-
Department of State	70	
Department of Transportation	108	-
Department of Treasury	4	
Environmental Protection Agency	120	-
Federal Emergency Management Agency	1	
General Services Administration	4	
National Aeronautics and Space Administration	2,723	-
National Foundation on the Arts and Humanity	12	-
Office of the President	4	-
Smithsonian Institution	2	-
Social Security Administration	12	
U.S. Army Corp. Of Engineers	107	-
Total	<u>\$ 18,247</u>	<u>\$ 185</u>

*National Science Foundation  
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Intragovernmental Advances balances as of September 30, 2003 and 2002 consisted of the following:

*(Amounts in Thousands)*

<u>Agency</u>	<u>2003</u>	<u>2002</u>
Department of the Navy	\$ <u>18,557</u>	\$ <u>8,309</u>

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**Intragovernmental Liabilities by Partner Agency (Unaudited)**  
(Amounts In Thousands)

Agency	2003			2002		
	Advances From Others	Other Liabilities	Employee Benefits	Advances From Others	Other Liabilities	Employee Benefits
Central Intelligence Agency	\$ 1,833	\$ -	\$ -	\$ 2,840	\$ -	\$ -
Department of Agriculture	194	-	-	773	-	-
Department of the Air Force	2,264	-	-	4,193	-	-
Department of the Army	259	-	-	853	-	-
Department of Commerce	1,647	-	-	5,890	-	-
Department of Defense	-	-	-	-	-	-
Department of Education	19,107	-	-	26,323	-	-
Department of Energy	2,205	-	-	9,920	-	-
Department of Health and Human Services	5,218	-	-	17,080	-	-
Department of Housing and Urban Development	973	-	-	1,675	-	-
Department of the Interior	28	-	-	432	-	-
Department of Justice	112	-	-	369	-	-
Department of Labor	237	-	264	395	-	254
Department of the Navy	702	-	-	2,805	-	-
Department of State	441	-	-	718	-	-
Department of Transportation	606	-	-	1,320	-	-
Department of the Treasury	111	-	-	180	-	-
Environmental Protection Agency	59	-	-	1,015	-	-
Federal Emergency Management Agency	-	-	-	258	-	-
General Services Administration	73	-	-	358	-	-
National Aeronautics and Space Administration	3,032	-	-	15,181	-	-
National Archives and Records Administration	-	-	-	744	-	-
National Foundation on the Arts and Humanities	2	-	-	107	-	-
Office of Personnel Management	-	396	-	-	321	-
Office of the President	6	-	-	-	-	-
Office of the Secretary – Defense Agencies	2,604	-	-	6,059	-	-
Smithsonian Institute	8	-	-	-	-	-
Social Security Administration	19	-	-	-	-	-
U.S. Army Corp of Engineers	193	-	-	-	-	-
Other	-	-	-	1,043	-	-
<b>Total</b>	<b>\$ 41,933</b>	<b>\$ 396</b>	<b>\$ 264</b>	<b>\$ 100,531</b>	<b>\$ 321</b>	<b>\$ 254</b>

**Deferred Maintenance (Unaudited)**

NSF performs condition assessment surveys in accordance with FASAB standards for capitalized property, plant and equipment to determine if any maintenance is needed to keep an asset in an acceptable condition or restore an asset to a specific level of performance. NSF considers deferred maintenance to be any maintenance that is not performed on schedule, unless it is determined from the condition of the asset that scheduled maintenance does not have to be performed. Also, deferred maintenance includes any other type of maintenance that, if not performed, would render the PP&E non-operational. Circumstances such as non-availability of parts or funding are considered reasons for deferring maintenance.

NSF considered whether any scheduled maintenance necessary to keep fixed assets of the agency in an acceptable condition was deferred at the end of FYs 2003 and 2002. Assets deemed to be in excellent or good condition are considered to be in acceptable condition. Assets in fair or poor condition are in unacceptable condition and the deferred maintenance required to get them to an acceptable condition are reported. NSF determines the condition of an asset in accordance with standards comparable to those used in the private industry. Due to the environment and remote location of Antarctica, all deferred maintenance on assets in fair or poor condition is considered critical in order to maintain operational status.

In FY 2002, NSF completed the maintenance deferred from FY 2001. In addition, NSF determined that scheduled maintenance on 99 items of Antarctic equipment was not completed and was deferred or delayed for a future period. The largest dollar amount of deferred maintenance for any single item approximated \$5,000. The items included light and heavy mobile equipment with a few items of power distribution and shop equipment. 81 items were rated to be in fair condition and 18 were rated to be in poor condition. All of the equipment is considered critical to NSF operations and estimated to require \$60,470 in maintenance.

During FY 2003, NSF determined that scheduled maintenance on 194 items of Antarctic equipment was not completed and was deferred or delayed for a future period. The largest dollar amount of deferred maintenance for any single item approximated \$16,000. The items included light and heavy mobile equipment requiring \$134,083 of maintenance and a few power distribution and shop equipment items requiring \$3,167. There are 176 items rated to be in fair condition and 18 rated to be in poor condition. All of the equipment are considered critical to NSF operations and estimated to require \$137,250 in total maintenance.

**Required Supplementary Stewardship Information**  
Stewardship Investments

*National Science Foundation  
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**Stewardship Investments  
Research and Human Capital**

*(Dollars in Thousands)  
(Unaudited)*

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
<b>Research and Human Capital Activities</b>					
Basic Research	\$ 3,519,159	\$ 3,092,060	\$ 2,692,243	\$ 2,636,518	\$ 2,507,569
Applied Research	218,152	193,788	211,421	173,670	188,742
Education and Training	867,489	767,734	704,949	596,517	599,323
Non-Investing Activities	<u>196,363</u>	<u>183,887</u>	<u>170,757</u>	<u>162,021</u>	<u>143,980</u>
<b>Total Research and Human Capital Activities</b>	<b>\$ <u>4,801,163</u></b>	<b>\$ <u>4,237,469</u></b>	<b>\$ <u>3,779,370</u></b>	<b>\$ <u>3,568,726</u></b>	<b>\$ <u>3,439,614</u></b>

**Inputs, Outputs and/or Outcomes**

**Research and Human Capital Activities**

Investments In:

Universities	\$ 3,310,365	\$ 2,919,897	\$ 2,631,405	\$ 2,470,300	\$ 2,385,492
Industry	178,000	185,062	162,176	160,573	154,555
Federal Agencies	144,792	106,458	125,823	132,790	150,959
Small Businesses	186,400	144,844	130,977	119,345	110,884
FFRDC's and Others	981,606	881,208	728,989	685,718	637,724
	<u>\$ 4,801,163</u>	<u>\$ 4,237,469</u>	<u>\$ 3,779,370</u>	<u>\$ 3,568,726</u>	<u>\$ 3,439,614</u>

Support to:

Scientists	\$ 427,304	\$ 394,144	\$ 355,261	\$ 359,228	\$ 350,841
Postdoctoral Programs	163,239	148,334	128,499	117,504	120,386
Graduate Students	475,315	402,620	362,820	315,583	323,324
	<u>\$ 1,065,858</u>	<u>\$ 945,098</u>	<u>\$ 846,580</u>	<u>\$ 792,315</u>	<u>\$ 794,551</u>

Outputs & Outcomes:

Number of:

Awards Actions	23,000	21,000	20,000	20,000	20,000
Senior Researchers	30,000	28,000	27,000	24,000	23,000
Other Professionals	12,000	11,000	10,000	8,000	9,000
Postdoctorals Associates	6,000	6,000	6,000	5,000	4,000
Graduate Students	27,000	26,000	25,000	22,000	20,000
Undergraduate Students	32,000	32,000	31,000	30,000	29,000
K – 12 Students	14,000	11,000	11,000	12,000	12,000

NSF's mission is to support basic scientific research and research fundamental to the engineering process as well as science and engineering education programs. To this end, NSF invests in the three strategic areas: People, Ideas, and Tools. Investment activities focused on "People" facilitate the creation of a diverse, internationally competitive and globally engaged workforce of scientists, engineers and well-prepared citizens. NSF supports activities to improve formal and informal science, mathematics, engineering and technology education at all levels, as well as public science literacy projects that engage people of all ages in life-long learning. Investment activities focused on "Ideas" support cutting edge research and education that yield new and

*National Science Foundation  
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important discoveries and promote the development of new knowledge and techniques within and across traditional disciplinary boundaries. Investment in “Tools” provides state-of-the-art instrumentation, equipment, computation and computing infrastructure and multi-user facilities such as digital libraries, research vessels and aircraft, for all fields of science, engineering and education.





NATIONAL SCIENCE FOUNDATION  
4201 Wilson Boulevard  
ARLINGTON, VIRGINIA 22230



November 17, 2003

To: Dr. Warren M. Washington  
Chairman, National Science Board

Dr. Rita Colwell  
Director, National Science Foundation

From: Dr. Christine C. Boesz Inspector General

Subject: Audit of the National Science Foundation's Fiscal Years 2003 and 2002 Financial Statements

This memorandum transmits KPMG LLP's financial statement audit report of the National Science Foundation (NSF) for its Fiscal Year 2003, which includes Fiscal Year 2002 comparative information.

### **Results of Independent Audit**

The Chief Financial Officer's (CFO) Act of 1990 (P.L. 101-576), as amended, requires NSF's Inspector General or an independent external auditor, as determined by the Inspector General, to audit the Foundation's financial statements. Under a contract monitored by the Office of Inspector General (OIG), KPMG, an independent public accounting firm, performed an audit of NSF's Fiscal Years 2003 and 2002 financial statements. The contract required that the audit be performed in accordance with the Government Auditing Standards issued by the Comptroller General of the United States, and Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, issued by the United States Office of Management and Budget.

KPMG issued an unqualified opinion on NSF's financial statements. In its Report on Internal Controls Over Financial Reporting, KPMG identified one reportable condition relating to NSF's post-award grant monitoring procedures. KPMG also reported that NSF's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA), and found no reportable noncompliance with laws and regulations it tested.

NSF management generally concurs with the findings regarding the reportable condition. Management's response dated November 7, 2003, follows KPMG's report.

### **Evaluation of KPMG's Audit Performance**

To fulfill our responsibilities under the CFO Act of 1990, as amended, and other related financial management legislation, the Office of Inspector General:

- Reviewed KPMG's approach and planning of the audit;
- Evaluated the qualifications and independence of the auditors;
- Monitored the progress of the audit at key points;
- Coordinated periodic meetings with NSF management to discuss audit progress, findings and recommendations;
- Reviewed KPMG's audit report to ensure compliance with Government Auditing Standards and Office of Management and Budget Bulletin No. 01-02; and
- Coordinated issuance of the audit report.

Due to the acceleration of the completion date of the NSF Fiscal Year 2003 Accountability Report, we have not yet completed our review of the working papers prepared by KPMG.

KPMG LLP is responsible for the attached auditor's report dated November 3, 2003, and the conclusions expressed in the report. We do not express any opinion on NSF's financial statements, internal control, conclusions on compliance with laws and regulations, or on whether NSF's financial management systems substantially complied with FFMIA.

The Office of Inspector General appreciates the courtesies and cooperation extended to KPMG LLP and OIG staff by NSF during the audit. If you or your staff have any questions, please contact me or Deborah H. Cureton, Associate Inspector General for Audit.

Attachment

cc: Dr. Mark S. Wrighton, Chair, Audit and Oversight Committee



2001 M Street, NW  
Washington, DC 20036

## Independent Auditors' Report

Dr. Warren M. Washington  
Chairman, National Science Board

Dr. Rita Colwell  
Director, National Science Foundation

We have audited the accompanying balance sheets of the National Science Foundation (NSF) as of September 30, 2003 and 2002, and the related statements of net cost, changes in net position, budgetary resources, and financing (hereinafter referred to as the financial statements) for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these financial statements. In connection with our audits, we also considered NSF's internal control over financial reporting and tested NSF's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on its financial statements.

### SUMMARY

As stated in our opinion on the financial statements, we concluded that NSF's financial statements as of and for the years ended September 30, 2003 and 2002 are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Our consideration of internal control over financial reporting identified one reportable condition related to NSF's post-award grant monitoring procedures. For NSF to fully implement its post-award grant monitoring procedures, adequate resources, both in terms of additional funding and staffing, are necessary before effective monitoring can take place. Further, additional policies and procedures are necessary to ensure that all post award activities are addressed comprehensively, and to improve existing policies and procedures.

However, the reportable condition identified above is not considered to be a material weakness.

The results of our tests of compliance with certain provisions of laws and regulations disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards*, issued by the Comptroller General of the United States, or Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*.

NSF management generally concurs with the findings regarding the reportable condition. Management's response dated November 7, 2003, follows our report.

The following sections discuss our opinion on NSF's financial statements, our consideration of NSF's internal control over financial reporting, our tests of NSF's compliance with certain provisions of applicable laws and regulations, and management's and our responsibilities.





## **OPINION ON THE FINANCIAL STATEMENTS**

We have audited the accompanying balance sheets of the National Science Foundation as of September 30, 2003 and 2002, and the related statements of net cost, changes in net position, budgetary resources, and financing for the years then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Science Foundation as of September 30, 2003 and 2002, and its net costs, changes in net position, budgetary resources, and reconciliation of net cost to budgetary obligations for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The information in the *Management's Discussion and Analysis, Required Supplementary Stewardship Information, and Required Supplementary Information* sections is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America or OMB Bulletin No. 01-09, *Form and Content of Agency Financial Statements*. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of this information. However, we did not audit this information, and accordingly, we express no opinion on it. Based upon our limited procedures, we determined that NSF could not complete the intragovernmental balance reconciliations with its governmental trading partners, as required by OMB Bulletin No. 01-09, because, although NSF issued confirmations to its major partners, such partners did not respond with adequate information to assist in reconciling such balances.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Detailed Performance Information (Section II) is presented for additional analysis and is not a required part of the financial statements. Accordingly, it has not been subjected to auditing procedures and therefore we express no opinion on it.

## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect NSF's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In our fiscal year 2003 audit, we noted a matter, described in Exhibit 1 involving the internal control over financial reporting and its operation that we consider to be a reportable condition. However, the reportable condition is not believed to be a material weakness.



A summary of the status of prior year reportable conditions is included as Exhibit 2.

We also noted other matters involving internal control over financial reporting and its operation that we have reported to the management of NSF in a separate letter dated November 3, 2003.

## COMPLIANCE WITH LAWS AND REGULATIONS

The results of our tests of compliance with certain provisions of laws and regulations, as described in the Auditors' Responsibilities section of this report, exclusive of Federal Financial Management Improvement Act (FFMIA), disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 01-02.

The results of our tests of compliance with FFMIA disclosed no instances in which NSF's financial management systems did not substantially comply with Federal financial management system requirements, applicable Federal accounting standards, or the United States Government Standard General Ledger at the transaction level.

We noted other matters involving compliance with laws and regulations that, under *Government Auditing Standards* and OMB Bulletin No. 01-02, were not required to be included in this report, that we have reported to the management of NSF in a separate letter dated November 3, 2003.

## RESPONSIBILITIES

**Management's Responsibilities.** The Government Management Reform Act (GMRA) of 1994 requires Federal agencies to report annually to Congress on their financial status and any other information needed to fairly present the agencies' financial position and results of operations. To meet the GMRA reporting requirements, NSF prepares annual financial statements.

Management is responsible for:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;
- Establishing and maintaining internal controls over financial reporting, and preparation of the Management's Discussion and Analysis (including the performance measures), required supplementary information, and required supplementary stewardship information; and
- Complying with laws and regulations, including FFMIA.

In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies. Because of inherent limitations in internal control, misstatements, due to error or fraud may nevertheless occur and not be detected.

**Auditors' Responsibilities.** Our responsibility is to express an opinion on the fiscal year 2003 and 2002 financial statements of NSF 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*; and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.



An audit includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2003 audit, we considered NSF's internal control over financial reporting by obtaining an understanding of NSF's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02 and *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982. The objective of our audit was not to provide assurance on NSF's internal control over financial reporting. Consequently, we do not provide an opinion on internal control over financial reporting.

As required by OMB Bulletin No. 01-02, we considered NSF's internal control over required supplementary stewardship information by obtaining an understanding of NSF's internal control, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls. Our procedures were not designed to provide assurance on internal control over required supplementary stewardship information, and, accordingly, we do not provide an opinion thereon.

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

As part of obtaining reasonable assurance about whether the NSF's fiscal year 2003 financial statements are free of material misstatement, we performed tests of NSF's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain requirements referred to in FFMIA. We limited our tests of compliance to these provisions described in the preceding sentence, and did not test compliance with all laws and regulations applicable to NSF. Providing an opinion on compliance with laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 01-02 and FFMIA, we are required to report whether NSF's financial management systems substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government



Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

**DISTRIBUTION**

This report is intended for the information and use of NSF's management, the National Science Board, the NSF Office of Inspector General, OMB, GAO, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

*KPMG LLP*

November 3, 2003



**Fiscal Year 2003 Reportable Condition****03-01 Post-award Grant Monitoring**

The National Science Foundation (NSF) was established in 1950 to promote and advance scientific and engineering progress in the United States. To carry out its mission, NSF funds research and education in science and engineering by making awards to various organizations, including colleges and universities, non-profit organizations, state and local governments, Federally Funded Research and Development Centers, and private entities. Through an award, NSF enters into a relationship to fund a particular science research or educational activity conducted by a grantee. In FY 2003, NSF had a budget of over \$5 billion and managed an estimated 30,000 awards. NSF awards are becoming larger, more cross-disciplinary and more complex. In addition, Federal requirements are increasingly calling for improved accountability for federal entities and their awardees. NSF expends approximately 90 percent of its appropriated funds on grants annually.

An effective post award monitoring program is necessary, in order to accurately report expenditures on NSF's financial statements and ensure that the awardees are expending their grant funds in accordance with their award agreements and federal regulations. Post-award oversight consists of activities after an award has been made that are necessary to ensure that Federal funds are accounted for and are used for the purpose of the grant or cooperative agreement. This includes reviewing and approving administrative changes to grants; monitoring projects for performance and financial compliance; providing technical assistance and feedback on their progress; reviewing awardees final project outcomes and disseminating the results; and closing out expired grants in a timely manner. For these efforts to be fully effective, management must be committed to implement a comprehensive post award monitoring program, with adequate resources, in a manner that is cost effective and does not place undue burden on grantees.

In our FY 2001 and 2002 audits, we reported that even though NSF has a robust system of award management over its pre-award and award phases, NSF did not have a comprehensive and systematic risk-based internal grants management program to monitor its post-award phase. In FY 2002, we reported that NSF had made progress in improving its post award monitoring by developing a Risk Assessment and Award Monitoring Guide (Guide) that included post award monitoring policies and procedures, a systematic risk assessment process for classifying high-risk grantees and various grantee analysis techniques. However, we also reported that NSF needed to further improve its monitoring procedures and then fully implement them before effective monitoring could take place. Specifically, at that time, we found that the monitoring procedures did not identify who would conduct the review, how the reviews would be performed, what types of reviews would be done based on the risk level of the awardee, or the documentation standards for the review files. We also found that the criteria for identifying high-risk grantees was limited, analysis techniques were not fully developed to evaluate whether the grantee's internal controls were adequate, and the guide did not identify follow up procedures. Although NSF performed on-site reviews of grantees, they were not consistently conducted, documented, or reported.



In FY 2003, NSF revised its monitoring guide and conducted several on-site monitoring visits. We found that the revised guide had been improved, but still needed further revision. Specifically:

- The criteria developed for identifying high-risk grantees are not comprehensive. Additional risk characteristics such as history of poor programmatic performance, delayed or lack of submission of required financial and progress reports, financial instability, or inadequate financial management systems should also be evaluated when evaluating grantee's risk.
- The guide does not provide sufficient review procedures for medium and low-risk grantees. A lesser degree of oversight could be performed in these instances, which would greatly increase the level of oversight at minimal cost.
- The guide should include details of the types of review activities that should be conducted on each grantee depending on the type of grantee, the level of risk assessed, and the area of focus where oversight is needed.
- The guide does not provide for periodic internal monitoring of grantee financial expenditure reports. This is necessary in order to ensure grantee compliance with NSF's grant reporting guidelines, and to ensure that amounts reported are reasonable and consistent with the terms and nature of the grant.

However, more importantly, we found that NSF management did not require that the guide be followed when conducting grant monitoring reviews. Accordingly, many of the reviews were not comprehensive and did not include a review of all the core areas identified in the guide such as general management, internal controls, accounting system, procurement, property, and travel. In addition, Grant monitoring officials did not fully document their monitoring activities, which raised questions as to the extent of monitoring that was conducted. As a result, we were not able to evaluate the results of the work performed.

In addition to the quality of the reviews performed, we have concerns that the amount of resources (training, tools, staff) available to implement an effective post award grant monitoring program is not sufficient. Currently, two staff on a part time basis are primarily responsible for performing the comprehensive post award monitoring reviews. Also, as part of their annual certification of the agency's management controls, several of NSF's division directors and office heads have reported that they do not have sufficient resources to conduct effective oversight of awards.

This is the third year that post award monitoring has been identified as a reportable condition. NSF has begun to address these issues by revising its guide, performing limited reviews, and by hiring a contractor to assist in analyzing and assessing NSF's post award monitoring needs. In addition, NSF has proposed to establish a separate division within the Office of Budget, Finance and Award Management to concentrate on post award management. In order to have an effective post award monitoring program, NSF senior management must provide a clear message to both its employees and the awardee community that award administration and monitoring is essential to allow NSF to fulfill its fiscal responsibilities. Senior management needs to ensure that adequate resources including staffing, training, and funding are available to implement an effective post award monitoring program.



### ***Recommendations***

We recommend that the Chief Financial Officer:

1. Provide the staffing, training, and funding resources necessary to effectively conduct grant monitoring activities.
2. Require full implementation of post award grant monitoring policies and procedures provided in the Award Monitoring and Business Assistance Program Guide (the Guide).
3. Develop the following for inclusion in the Guide:
  - (i) Policies and procedures for the review of NSF grantees that fall into the medium and low-risk categories.
  - (ii) Additional criteria for identifying high-risk grantees.
  - (iii) Requirements for reviewers to maintain documentation in grant files on their monitoring activities in terms of what transactions and documents were reviewed, what questions were asked, what responses were received, what corrective actions resulted, etc.
  - (iv) Policies and procedures to monitor the accuracy of grantee expenditure reports submitted to the NSF.
  - (v) Policies and procedures for the types of review activities that should be conducted on each grantee depending on the type of grantee, the level of risk assessed, and the area of focus where oversight is needed.



**Status of FY 2002 Reportable Conditions**

**02-01: Post-award Management**

***A. Financial Monitoring of Grant Awards***

Although NSF has a robust system of award management over its pre-award and award phases, NSF continues to need improvement in implementing a comprehensive and systematic risk-based internal grants management program to monitor its post-award phase. Our review of NSF's corrective actions in fiscal year 2003 revealed that it needs to fully implement its post-award monitoring procedures, dedicate adequate resources both in terms of additional funding and staffing before effective monitoring can take place. As a result, this reportable condition is being repeated in fiscal year 2003.

***B. Monitoring of Assets Owned by NSF in the Custody of Other Entities***

NSF has developed and substantially implemented procedures in fiscal year 2003 to monitor NSF assets in the custody of other entities to ensure that such assets are protected from loss, misuse, or theft, and reliable and timely information is obtained on the value of these assets. As a result, this reportable condition is considered resolved.

**02-02: Information Security**

Our review of NSF's corrective actions in fiscal year 2003 revealed that NSF has made significant progress in developing, refining, and implementing its information security program, although certain improvements are still needed to strengthen NSF's security posture and to ensure compliance with the Federal Information Security Management Act. As a result, this reportable condition is considered resolved, and the remaining issues will be communicated in a management letter.



**NATIONAL SCIENCE FOUNDATION**  
4201 WILSON BOULEVARD  
ARLINGTON, VIRGINIA 22230

November 7, 2003

To: Christine C. Boesz  
Inspector General

From: Thomas N. Cooley  
Chief Financial Officer

Subject: Management's Response to Independent Auditors' Report  
Fiscal Year 2003

This memorandum and attachments transmit NSF management's response to KPMG LLP's audit report for fiscal year 2003. We have included detailed responses to the findings as Attachment 1.

**SUMMARY**

The auditors' report concluded that NSF's financial statements as of and for the years ended September 30, 2003, are presented fairly, in all material respects, and are in conformity with generally accepted accounting principles in the United States of America.

**Reportable Conditions**

The FY 2003 auditors' report identified one repeat audit finding that was deemed to be a reportable condition. The finding has moved to the next step in our post-award management program and is focusing on resources to fully implement our plans. The report also concluded that significant progress was made in part (ii) of last year's finding related to NSF owned property in awardees' custody. This part of the finding was not repeated in FY 2003.

- Post-Award Management

The auditors identified one reportable condition related to NSF's post award grant monitoring procedures. For NSF to fully implement its post award grant monitoring procedures adequate resources both in terms of additional funding and staffing are necessary before effective monitoring can take place. Further, additional policies and procedures are necessary to ensure that all post award

activities are addressed comprehensively, and to improve existing policies and procedures.

*NSF Management Response:*

NSF management generally agrees with the recommendations related to the Post Award Grant Monitoring activities, and has continued to take actions to address these concerns. We are pleased that the Office of the Inspector General (OIG) and the KPMG Audit staff have recognized our progress in this regard. We have made credible and significant improvements by establishing and implementing our Award Monitoring and Business Assistance Program. We are seeking both additional resources and the optimal organizational structure to perform effective and efficient post-award management.

I would like to thank the OIG and KPMG staff for working in such a professional and dedicated manner with my staff to accomplish our accelerated reporting goals. Together, through coordinated planning and the diligence of our staffs, we were able to complete the audit process two and half months earlier this year—an achievement we can all be proud of.

NSF management appreciates the cooperation extended by both the OIG and KPMG LLP throughout the audit process. We will continue with our collaborative efforts to maintain the high levels of internal controls and effective and efficient practices at NSF.

cc: Dr. Warren M. Washington

Attachment 1

## **Management's Responses to Auditors Report**

### Management's Response to 03-01 Post-Award Management

We have reviewed the Notification of Findings and Recommendations with regard to post-award monitoring and we are in general agreement with them. We are pleased that the Office of the Inspector General and the KPMG Audit Staff have recognized our progress and the significant effort we have put toward developing a sound program, based on pilot testing, results assessment, and continued enhancements.

We have developed a strategic program, our Award Monitoring and Business Assistance Program (AMBAP), that balances risk mitigation and cost-benefit. This program incorporates our post-award management monitoring and those complementary activities that support its effective implementation. This program includes:

- A dynamic risk assessment framework that integrates institutional and award risks. The data elements that describe our risk factors are incorporated into our database, allowing for electronic analysis.
- A site selection process that uses data from the above as a first level of identification. Our comprehensive site selection process supplements the outputs from the implementation of the risk assessment framework, with specific program office referrals and requests; institution- initiated requests; reverse site visits; and audit resolution visits.
- The AMBAP Guide that includes: core review areas, preparation protocols; site visit tools; post visit follow-up with NSF program staff and NSF grantees; and reporting and documentation requirements for which timeliness will be improved as resources increase.
- A BFA award monitoring training program that integrates a core curriculum and hands on training during on-site visits.
- For additional validation we have contracted with IBM Consultants to conduct an independent assessment of NSF's post-award management system to validate and verify the framework for assessing award risks and attendant award monitoring and management plans.



With respect to resources:

- We have increased the resources devoted to this effort over the last two years and this is demonstrated by the fact that we conducted visits to 32 awardee institutions with 1,351 active awards representing over \$700 million in assistance funding. We have continued to invest in staff training.
- We have expanded our outreach activities to include targeted business assistance to grantees by type and/or risk factor. For example, we host reverse site visits for recipients of the Math and Science Partnership awards.
- We are seeking both additional resources and the optimal organizational structure to perform effective and efficient post-award management.

We will continue to develop this activity, informed by the IBM assessment, feedback from the awardee community, and the analysis of the results of the ongoing on-site monitoring itself. A key outcome from the implementation of the FY03 post-award monitoring activity is that nowhere did we find fraud, waste, abuse, or misuse of the NSF funding we reviewed.

Ultimately, the National Science Foundation will make the determination as to the appropriate level of resources to be devoted to this activity, within the context of the accomplishment of our overall mission.