



November 29, 2017

Memorandum for: The Federal Co-Chair
ARC Executive Director

Subject: OIG Report 18-04
Fiscal Year 2017 Financial Statement Audit

The enclosed report presents the results of the audit of the Commission's financial statements for the fiscal year ended September 30, 2017. The report should be read in conjunction with the Commission's financial statements and notes to fully understand the context of the information contained therein.

The Appalachian Regional Commission (ARC) contracted with the independent certified public accounting firm of Key & Associates, P.C., to audit the financial statements of the Commission as of and for the fiscal year ended September 30, 2017. The contract required that the audit be conducted in accordance with U.S. generally accepted government auditing standards and OMB audit guidance. ARC's Office of Inspector General monitored audit activities to help ensure audit quality.

The following results were noted from Key's audit of ARC's financial statements for the fiscal year ended September 30, 2017.

- Key stated it was their opinion that ARC's financial statements were presented fairly in all material respects, in accordance with U.S. generally accepted accounting principles.
- Key was not contracted for and did not provide an opinion on the effectiveness of ARC's internal controls over financial reporting. However, Key did state that they did not identify any deficiencies in internal control that were considered to be material weaknesses, relative to their expressing an opinion on ARC's financial statements.
- No significant deficiencies were reported.
- Key did not express an opinion on compliance with laws and regulations, but noted no instances of non-compliance with laws or regulations required to be reported under the provisions of OMB audit guidance.

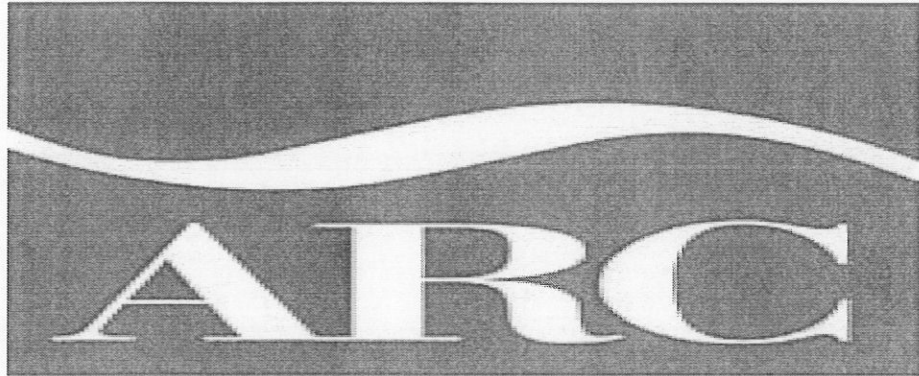
In connection with the contract, we reviewed Key's report and related documentation and inquired of its representatives. Our involvement in the audit process consisted of monitoring of

audit activities, reviewing auditor independence and qualifications, attending meetings, participating in discussions, and reviewing audit planning and conclusion workpapers and reports. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, opinions on the Appalachian Regional Commission's financial statements, conclusions about the effectiveness of internal control, or conclusions about compliance with laws and regulations. Key is responsible for the attached auditor's report dated November 17, 2016 and the conclusions expressed in the report. However, our review disclosed no instances where Key did not comply, in all material respects, with U.S. generally accepted government auditing standards.

Hubert Sparks
Inspector General

Attachment

cc: Director, Finance and Administration Division
Key & Associates, LLP



**APPALACHIAN
REGIONAL
COMMISSION**

FINANCIAL STATEMENTS

As of And For The Years Ended September 30, 2017 and 2016

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Key & Associates, P.C.

INDEPENDENT AUDITOR'S REPORT

To the Federal Co-Chair and the Executive Director
The Appalachian Regional Commission

In accordance with the Accountability of Tax Dollars Act of 2002 and at the request of the Inspector General, we are responsible for conducting the audit of the financial statements of the Appalachian Regional Commission. We have audited the accompanying balance sheets of the Appalachian Regional Commission as of September 30, 2017 and 2016 and the related statements of net cost, changes in net position, and budgetary resources for the years then ended, and the related notes to the financial statements (hereinafter referred to as "financial statements").

Management's Responsibility for the Financial Statements

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

Auditor's Responsibilities

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 17-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin 17-03 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the agency's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Appalachian Regional Commission internal control. Accordingly, we do not express such an opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion on Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Appalachian Regional Commission, as of September 30, 2017 and 2016, and its net costs, changes in net position, and budgetary resources for the years then ended, in accordance with U.S. generally accepted accounting principles.

Other Matters

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

Other Information

Our audits were conducted for the purpose of forming an opinion on the basic financial statements as a whole. The Chairperson's message, performance and other information sections of the Appalachian Regional Commission's *Agency Financial Report* are presented for purposes of additional analysis and are not a required part of the basic financial statements. We read the information included with the financial statements in order to identify material inconsistencies, if any, with the audited financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, as of and for the year ended September 30, 2017, we considered the Appalachian Regional Commission's internal control over the financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion of the effectiveness of the Appalachian Regional Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Appalachian Regional Commission's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a significant deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Appalachian Regional Commission's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB bulletin No. 17-03. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests of compliance disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 17-03.

Purpose of Other Reporting Required by Government Auditing Standards

The purpose of the communication provided in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the agency's internal control or on compliance. This communication is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering internal control and compliance with provisions of laws, regulations, contracts, and grant agreements noncompliance with which could have a material effect on the closing package financial statements. Accordingly, this communication is not suitable for any other purpose.

Restriction of Use of the Report on the Financial Statements

This report is intended solely for the information and use of the management and members of the Appalachian Regional Commission, U.S. Department of Treasury, the U.S. Office of Management and Budget, the U.S. Government Accountability Office, and the U.S. Congress in connection with the preparation and audit of the Financial Report of the U.S. Government and is not intended to be and should not be used by anyone other than these specified parties.

Key & Associates, PC

Silver Spring, Maryland
November 2, 2017

APPALACHIAN REGIONAL COMMISSION

BALANCE SHEET

As Of September 30, 2017 and 2016

	2017	2016
Assets:		
Intragovernmental:		
Fund Balance With Treasury	(Note 1 & 2) \$ 329,644,342.00	\$ 261,826,010.06
Accounts Receivable	(Note 1 & 3) 1,873.32	869.42
Other:		
Advances and Prepayments	(Note 1 & 4) 2,041,459.86	3,821,991.49
Total Intragovernmental	331,687,675.18	265,648,870.97
Assets With The Public:		
Cash and Other Monetary Assets	(Note 1 & 5) 1,624,223.19	1,434,740.66
Other:		
Advances and Prepayments	(Note 1 & 4) 38,955,071.00	38,807,862.28
Total Assets	\$ 372,266,969.37	\$ 305,891,473.91
Liabilities:		
Intragovernmental:		
Other:	(Note 7)	
Employer Contributions and Payroll Taxes Payable	(Note 7 & 8) \$ 24,150.13	\$ 23,744.20
Liability for Advances and Prepayments	566,190.43	803,022.59
Total Intragovernmental	590,340.56	826,766.79
Liabilities With the Public:		
Accounts Payable	(Note 1 & 7) 31,400,552.87	8,297,296.36
Other:	(Note 1, 7 & 8)	
Accrued Funded Payroll and Leave	252,420.20	255,968.34
Employer Contributions and Payroll Taxes Payable	1,756.31	1,805.94
Unfunded Leave	488,012.09	464,188.40
Liability for Advances and Prepayments	580,557.12	392,254.12
Other Liabilities Without Related Budgetary Obligations	1,711,545.98	1,522,063.45
Total Liabilities	\$ 35,025,185.13	\$ 11,760,343.40
Net Position:		
Unexpended Appropriations - All Other Funds		
(Consolidated Totals)	359,419,274.95	292,154,635.17
Cumulative Results of Operations - All Other		
Funds (Consolidated Totals)	(22,177,490.71)	1,976,495.34
Total Net Position - All Other Funds	337,241,784.24	294,131,130.51
(Consolidated Totals)	337,241,784.24	294,131,130.51
Total Net Position	337,241,784.24	294,131,130.51
Total Liabilities and Net Position	\$ 372,266,969.37	\$ 305,891,473.91

The accompanying notes are an integral part of these statements.

APPALACHIAN REGIONAL COMMISSION
STATEMENT OF NET COST

As of And For The Years Ended September 30, 2017 and 2016

	2017	2016
Gross Program Costs:		
ARC:		
Gross Costs	\$ 113,648,740.82	\$ 76,063,512.36
Less: Earned Revenue	4,561,450.72	4,461,363.00
Net Program Costs	109,087,290.10	71,602,149.36
Net Cost of Operations	\$ 109,087,290.10	\$ 71,602,149.36

(Note 11)

The accompanying notes are an integral part of these statements.

APPALACHIAN REGIONAL COMMISSION
STATEMENT OF CHANGES IN NET POSITION
As of And For The Years Ended September 30, 2017 and 2016

	<u>2017</u> <u>Consolidated Totals</u>	<u>2016</u> <u>Consolidated Totals</u>
Cumulative Results from Operations:		
Beginning Balances	\$ 1,976,495.34	\$ 2,186,463.34
Adjustments:		
Corrections of errors (Note 12)	<u>209,968.00</u>	
Beginning balance, as adjusted	<u>2,186,463.34</u>	<u>2,186,463.34</u>
Budgetary Financing Sources:		
Appropriations used	84,525,392.22	71,213,200.12
Other Financing Sources (Non-Exchange):		
Imputed financing	197,943.83	178,981.24
Total Financing Sources	<u>84,723,336.05</u>	<u>71,392,181.36</u>
Net Cost of Operations	<u>109,087,290.10</u>	<u>71,602,149.36</u>
Net Change	<u>(24,363,954.05)</u>	<u>(209,968.00)</u>
Cumulative Results of Operations	<u>(22,177,490.71)</u>	<u>1,976,495.34</u>
Unexpended Appropriations:		
Beginning Balance	292,154,635.17	217,367,835.29
Adjustments:		
Corrections of errors (Note 12)	<u>(209,968.00)</u>	
Beginning Balance, as adjusted	<u>291,944,667.17</u>	<u>217,367,835.29</u>
Budgetary Financing Sources:		
Appropriations received	152,000,000.00	146,000,000.00
Appropriations used	<u>(84,525,392.22)</u>	<u>(71,213,200.12)</u>
Total Budgetary Financing Sources	<u>67,474,607.78</u>	<u>74,786,799.88</u>
Total Unexpended Appropriations	<u>359,419,274.95</u>	<u>292,154,635.17</u>
Net Position	<u>\$ 337,241,784.24</u>	<u>\$ 294,131,130.51</u>

The accompanying notes are an integral part of these statements.

APPALACHIAN REGIONAL COMMISSION
STATEMENT OF BUDGETARY RESOURCES

As of And For The Years Ended September 30, 2017 and 2016

	<u>2017</u> <u>Budgetary</u>	<u>2016</u> <u>Budgetary</u>
BUDGETARY RESOURCES		
Unobligated balance brought forward, Oct 1	\$ 63,790,086.44	\$ 25,478,161.75
Unobligated balance brought forward, Oct 1, as adjusted	63,790,086.44	25,478,161.75
Recoveries of prior year unpaid obligations	6,204,656.55	9,074,669.76
Other changes in unobligated balance (+ or -)	846,802.39	1,410,103.82
Unobligated balance from prior year budget authority, net	70,841,545.38	35,962,935.33
Appropriations (discretionary and mandatory)	152,000,000.00	146,000,000.00
Spending authority from offsetting collections (discretionary and mandatory)	4,061,350.35	5,023,654.86
Total budgetary resources	<u>\$ 226,902,895.73</u>	<u>\$ 186,986,590.19</u>
 STATUS OF BUDGETARY RESOURCES		
New obligations and upward adjustments (total)	(Note 13) \$ 162,702,576.92	\$ 123,196,503.75
Unobligated balance, end of year:		
Apportioned, unexpired account	61,267,758.61	54,972,214.18
Unapportioned, unexpired accounts	2,932,560.20	8,817,872.26
Unexpired unobligated balance, end of year	64,200,318.81	63,790,086.44
Unobligated balance, end of year (total)	64,200,318.81	63,790,086.44
Total budgetary resources	<u>\$ 226,902,895.73</u>	<u>\$ 186,986,590.19</u>
 CHANGE IN OBLIGATED BALANCE		
Unpaid obligations:		
Unpaid obligations, brought forward, Oct 1	\$ 197,542,483.04	\$ 153,208,915.56
New obligations and upward adjustments	162,702,576.92	123,196,503.75
Outlays (gross) (-)	(89,554,239.39)	(69,788,266.51)
Recoveries of prior year unpaid obligations (-)	(6,204,656.55)	(9,074,669.76)
Unpaid obligations, end of year	264,486,164.02	197,542,483.04
Uncollected payments:		
Uncollected pymts, Fed sources, brought forward, Oct 1 (-)	(200,869.42)	
Change in uncollected pymts, Fed sources (+ or -)	176,895.59	(200,869.42)
Uncollected pymts, Fed sources, end of year (-)	(23,973.83)	(200,869.42)
Obligated balance, start of year (+ or -)	197,341,613.62	153,208,915.56
Obligated balance, end of year (+ or -)	<u>\$ 264,462,190.19</u>	<u>\$ 197,341,613.62</u>
 BUDGET AUTHORITY AND OUTLAYS, NET		
Budget authority, gross (discretionary and mandatory)	\$ 156,061,350.35	\$ 151,023,654.86
Actual offsetting collections (discretionary and mandatory) (-)	(5,372,571.33)	(6,232,889.26)
Change in uncollected pymts, Fed sources (discretionary and mandatory) (+ or -)	176,895.59	(200,869.42)
Recoveries of prior year paid obligations (discretionary and mandatory)	846,802.39	1,410,103.82
Budget authority, net (total) (discretionary and mandatory)	151,712,477.00	146,000,000.00
Outlays, gross (discretionary and mandatory)	89,554,239.39	69,788,266.51
Actual offsetting collections (discretionary and mandatory) (-)	(5,372,571.33)	(6,232,889.26)
Outlays, net (total) (discretionary and mandatory)	<u>\$ 84,181,668.06</u>	<u>\$ 63,555,377.25</u>
Agency outlays, net (discretionary and mandatory)	<u>\$ 84,181,668.06</u>	<u>\$ 63,555,377.25</u>

The accompanying notes are an integral part of these statements.

Note 1 – Summary of Significant Accounting Policies

Reporting Entity

The Appalachian Regional Commission (ARC) was established under the Appalachian Regional Development Act of 1965, as amended. ARC is a regional development agency designed to function as a federal, state, and local partnership. ARC is not a federal executive branch agency (as defined in Title 5 and 31 of the United States Code and by the Department of Justice).

Commission members are comprised of a federal member (Federal Co-Chair), who is appointed by the President of the United States, and the governors of each of the 13 states in the Appalachian Region. The state members elect a State Co-Chair from their members. ARC has an Executive Director and Program and Administrative Offices that implement the policies and procedures established by the Federal and State Co-Chairs. ARC personnel are comprised of both federal and non-federal employees.

ARC supports economic and social development in the Appalachian Region. The Appalachian Region is a 205,000 square mile region from Southern New York to Northern Mississippi. The ARC programs affect 420 counties located in 13 states including all of West Virginia and parts of Alabama, Georgia, Kentucky, Maryland, Mississippi, New York, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, and Virginia.

Fund Accounting Structure

ARC's financial activities are accounted for by utilizing individual funds and fund accounts in reporting to the U.S. Treasury and the Office of Management and Budget (OMB). For financial statement purposes, these funds are classified all other funds, which consist of area development program funds and funding for the Office of the Federal Co-Chair and the Office of Inspector General.

Budgets and Budgetary Accounting

ARC programs and activities are funded through no-year appropriations and contributions from the 13 states in the Appalachian Region. Federal funds are available without fiscal year limitation and remain available until expended. Because of the no-year status of the funds, unobligated amounts are not returned to the U.S. Treasury.

Basis of Accounting and Presentation

These financial statements present the financial position, net cost of operations, changes in net position, and budgetary resources of ARC in accordance with U.S. generally accepted accounting principles (GAAP) and form and content requirements of OMB

Circular A-136 Financial Reporting Requirements. GAAP for federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which is the official standard-setting body for the federal government. The financial statements have been prepared from the books and records of ARC, and include the accounts of all funds under the control of the ARC reporting entity.

U.S. generally accepted accounting principles encompass both accrual and budgetary transactions. Under accrual accounting, revenues are recognized when earned, and expenses are recognized when incurred. Budgetary accounting facilitates compliance with legal constraints on, and controls over, the use of federal funds. These financial statements are prepared by ARC pursuant to OMB directives and used to monitor ARC's use of budgetary resources.

Fund Balance with U.S. Treasury

ARC's cash receipts and disbursements are processed by the U.S. Treasury. Funds with U.S. Treasury represent obligated and unobligated no-year funds available to finance allowable current and future expenditures.

Cash in Commercial Institutions

ARC uses commercial bank accounts to accommodate collections and payments that cannot be processed by the U.S. Treasury. Cash in commercial institutions totaled \$1,624,223.19 and \$1,434,740.20 at September 30, 2017 and 2016, respectively.

Advances

ARC advances funds to federal agencies for work performed on its behalf under various reimbursable agreements. These intra-governmental advances are recorded as an asset, which is reduced when actual expenditures or the accrual of unreported expenditures are recorded.

ARC also has advances made to grantees. These primarily include revolving loan fund/equity fund payments to provide pools of funds to be made available to grantees to create and retain jobs. These advance payments are recorded by ARC as an asset, which is reduced if the revolving fund is terminated.

Equipment

ARC's equipment is recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The capitalization threshold is \$35,000. All equipment was fully depreciated at September 30, 2017 and 2016.

Liabilities

Liabilities represent probable amounts to be paid by ARC as a result of past transactions. Liabilities covered by budgetary or other resources are those for which Congress has appropriated funds or funding is otherwise available to pay amounts due.

Liabilities not covered by budgetary or other resources represent amounts owed in excess of available congressionally appropriated funds or other amounts. The liquidation of liabilities not covered by budgetary or other resources is dependent on future Congressional appropriations or other funding.

Accounts Payable

Accounts payable consists of amounts owed to grantees and amounts owed to federal and nonfederal entities for goods and services received by ARC.

Benefits Due and Payable:

Unfunded Annual 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 leave account is adjusted to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of non-vested leave are expensed as taken.

Retirement Benefits

ARC's federal and certain non-federal employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). FERS was established by the enactment of Public Law 99-335. Pursuant to this law, FERS and the Social Security and the Thrift Savings Plan program automatically cover most employees hired after December 31, 1983. Employees hired before January 1, 1984 elected to participate in the FERS and Social Security or to remain in CSRS.

All federal and certain non-federal employees are eligible to contribute to the Thrift Savings Plan (TSP). For those employees participating in the FERS, a TSP account is automatically established and ARC makes a mandatory one percent contribution to this account. In addition, ARC makes matching contributions, ranging from one to four percent, for FERS eligible employees who contribute to their TSP accounts. Matching contributions are not made to the TSP accounts established by CSRS employees. FERS employees and certain CSRS reinstatement employees are eligible to participate in the Social Security program after retirement. In these instances, ARC remits the employer's share of the required contribution.

The Office of Personnel Management (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 ARC. OPM also provides information regarding the full cost of health and life insurance benefits. Reporting amounts such as plan assets, accumulated plan benefits, and related unfunded liabilities, if any, is the responsibility of OPM.

ARC also has a Defined Benefit Pension Plan which was open to all employees not participating in CSRS and FERS. ARC uses an October 1 measurement date for its plan.

In February 2000 ARC established a 401(k) retirement plan that mirrors FERS. The plan covers substantially all non-federal employees. Employees are eligible to participate in and are fully vested in the plan upon employment. ARC's funding policy is to make a 3% contribution of total salary and a matching 3% of the first 50% of the participants' contributions to the plan up to 6% of total salary.

Parent Child Reporting

ARC is a party to allocation transfers with federal agencies as both a transferring (parent) entity and receiving (child) entity. Allocation transfers are legal delegations by one entity of its authority to obligate budget authority and outlay funds to another entity. A separate fund account (allocation account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent entity. Generally, all financial activity related to these allocation transfers (e.g., budget authority, obligations, outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations and budget apportionments are derived. ARC allocates funds, as the parent agency, to the U.S. Department of Transportation, Housing and Urban Development, the Rural Development Agency, U.S. Army Corps of Engineers and the Economic Development Agency. Additionally, ARC receives allocation transfers, as the child agency from the U.S. Department of Transportation to cover Appalachian Development Highway System administrative costs.

Net Position

Net position is the residual difference between assets and liabilities and is comprised of unexpended appropriations and cumulative results of operations. Unexpended appropriations 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. The cumulative results of operations are the net results of ARC's operations since inception.

Net Cost of Operations

Earned revenues arise from the collection of state contributions and other inter-agency agreements are deducted from the full cost of ARC's major programs to arrive at net

program cost. Earned revenues are recognized by ARC to the extent reimbursements are payable from the public, as a result of costs incurred or services performed on the public's behalf.

Budgetary Financing Sources

Budgetary financing sources other than earned revenues provide funding for ARC's net cost of operations and are reported on the Statement of Changes in Net Position. These financing sources include amounts received from Congressional appropriations to support its operations. A financing source is recognized for these appropriated funds received.

Use of Estimates

Management has made certain estimates when reporting assets, liabilities, revenue, and expenses, and in the note disclosures. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Tax Exempt Status

As an instrumentality of the federal government, ARC is exempt from income taxes imposed by any governing body whether it is a federal, state, commonwealth, local, or foreign government and exempt from sales and use taxes of the District of Columbia.

Note 2 – Fund Balance With Treasury

ARC's fund balance with treasury at September 30 consisted of the following:

A. Fund Balances	2017	2016
General Funds	\$ 329,230,936.00	\$ 261,412,604.06
Trust Fund	413,406.00	413,406.00
Total Fund Balance with Treasury	<u>329,644,342.00</u>	<u>261,826,010.06</u>
B. Status of Fund Balance with Treasury		
1) Unobligated Balance		
a) Available	61,267,758.61	54,972,214.18
b) Unavailable	2,932,560.20	8,817,872.26
2) Obligated Balance not yet Disbursed	264,462,190.19	197,341,613.62
3) Temporary Sequestration	981,833.00	694,310.00
Total	<u>\$ 329,644,342.00</u>	<u>\$ 261,826,010.06</u>

A trust fund was once established to receive, hold, and disburse monies collected to cover

Appalachian Regional Commission
Notes to Financial Statements
September 30, 2017 and 2016

the administrative expenses of ARC. This fund has not been used since FY 2014. The balance in the trust fund is the amount sequestered in prior years.

Note 3 – Accounts Receivable, net

This line item represents the gross amount of monies owed to the ARC for expenses incurred for the Office of the States' Washington Representative. ARC has historically collected any receivables due and thus has not established an allowance for uncollectible accounts.

	2017	2016
Accounts Receivable	\$1,873.32	\$ 869.42

Note 4 – Other Assets

Advances at September 30 consist of the following:

Advances to the Tennessee Valley Authority	\$ 1,916,670.22	\$ 3,490,307.62
Advances to the Environmental Protection Agency	49,789.64	256,683.87
Advances to the Corps of Engineers	75,000.00	75,000.00
	<u>2,041,459.86</u>	<u>3,821,991.49</u>
2. Other		
Advances to grantees to finance future program expenditures		
-Revolving Loan Fund	27,345,467.31	27,861,432.49
-Other	8,159,351.69	7,373,497.79
Prepaid Pension Expense	3,450,252.00	3,572,932.00
	<u>38,955,071.00</u>	<u>38,807,862.28</u>
Total	<u>\$ 40,996,530.86</u>	<u>\$ 42,629,853.77</u>

Intragovernmental: ARC advances funds to federal agencies for work performed on its behalf under various reimbursable agreements for construction projects. These intra-governmental advances are recorded as an asset, which is reduced when actual expenditures or the accrual of unreported expenditures are recorded.

Other: ARC also has advances made to grantees that are not federal entities. The majority of these advances are disbursed to grantees operating revolving loan funds, the remaining amounts are to all other grantees.

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- Revolving Loan Fund Grantees - ARC provides grants to revolving loan funds operating in its region for the purpose of saving and creating private-sector jobs. Because of the revolving nature of the funds, the grants have no fixed end date. Grant funds provided to revolving loan funds retain their federal identity and are subject to the Cash Management Improvement Act of 1990 (Public Law 101-453), for which the Appalachian Regional Commission has established a policy on excess cash. Accounting treatment of RLF transactions is that cash outlays are recorded as increases to SGL 1410 Advances and Prepayments and refunds of excess cash are recorded as decreases to SGL 1410 Advances and Prepayments.
- Other – ARC advances funds to non-federal grantees for work performed on its behalf under various grant agreements. It includes funding capital for Loan and Investment Funds. These advances are recorded as an asset, which is reduced when actual expenditures or the accrual of unreported expenditures are recorded.

Note 5 – Cash and Other Monetary Assets

ARC uses commercial bank accounts to accommodate collections and payments that cannot be processed by the U.S. Treasury.

	2017	2016
Commercial Bank Balance	\$ 1,624,223.19	\$ 1,434,740.66

Note 6 – General Property, Plant and Equipment, Net

Assets are recorded at cost. The depreciation calculation method used is Straight Line with an estimated useful life of the asset. A \$35,000 threshold is used as the capitalized threshold.

2017	Equipment	Internal Use Software	Total
Cost	\$ 69,194.00	\$ 48,422.40	\$ 117,616.40
Accumulated Depreciation	(69,194.00)	(48,422.40)	(117,616.40)
Net Book Value	\$ -	\$ -	\$ -

2016	Equipment	Internal Use Software	Total
Cost	\$ 69,194.00	\$ 48,422.40	\$ 117,616.40
Accumulated Depreciation	(69,194.00)	(48,422.40)	(117,616.40)
Net Book Value	\$ -	\$ -	\$ -

Note 7 – Liabilities Not Covered by Budgetary Resources

The accrued liabilities of ARC are comprised of program expense accruals, payroll accruals and unfunded annual leave earned by employees. Program expense accruals represent expenses that were incurred prior to year-end but were not paid. Similarly, payroll accruals represent payroll expenses that were incurred prior to year-end but were not paid.

Liabilities at September 30, 2017 and 2016 consist of the following:

	<u>2017</u>	<u>2016</u>
With the Public		
Unfunded annual leave	\$488,012.09	\$464,188.40
Total liabilities not covered by budgetary resources	<u>488,012.09</u>	<u>464,188.40</u>
<u>Advances</u>		
Advances from Centers for Disease Control	536,190.43	773,022.59
Advances from the National Endowment for the Arts	30,000.00	30,000.00
Advances from Non Federal Vendors	580,557.12	392,254.12
Total Advances	<u>1,146,747.55</u>	<u>1,195,276.71</u>
<u>Benefits Due</u>		
Accrued health and flexible spending benefits	87,322.79	87,322.79
Accrued salaries and benefits	278,326.64	281,518.48
Total benefits due	<u>365,649.43</u>	<u>368,841.27</u>
Payments Due to grantees to finance program expenditures	31,400,552.87	8,297,296.36
Commercial Bank Balance	1,624,223.19	1,434,740.66
Total liabilities covered by budgetary resources	<u>34,537,173.04</u>	<u>11,296,155.00</u>
Total Liabilities	<u><u>\$35,025,185.13</u></u>	<u><u>\$11,760,343.40</u></u>

Note 8 – Other Liabilities

As of September 30, 2017 and 2016, other liabilities with the public consist of Accrued Funded Payroll and Leave, Employer Contributions and Payroll Taxes Payable, Unfunded Leave, Liability for Advances from Non Federal Sources, Accrued Health and Flexible Spending Benefits and Commercial Bank Balance. Other Liabilities Federal consists of Liability for Advances from Federal Sources and Employer Contributions and Payroll Taxes Payable.

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	FY 2017		
	Non-Current	Current	Total
Intragovernmental			
Employer Contributions and Payroll Taxes Payable	-	24,150.13	24,150.13
Liability for Advances from Federal Sources	-	566,190.43	566,190.43
Total Intragovernmental	-	590,340.56	590,340.56
Liabilities with the Public			
Accrued Funded Payroll and Leave	-	252,420.20	252,420.20
Employer Contributions and Payroll Taxes Payable	-	1,756.31	1,756.31
Unfunded Leave	488,012.09	-	488,012.09
Liability for Advances from Non Federal Sources	-	580,557.12	580,557.12
Accrued Health and Flexible Spending Benefits	87,322.79	-	87,322.79
Commercial Bank Balance	1,624,223.19	-	1,624,223.19
Total Liabilities with the Public	2,199,558.07	834,733.63	3,034,291.70
Total Other Liabilities	2,199,558.07	1,425,074.19	3,624,632.26

	FY 2016		
	Non-Current	Current	Total
Intragovernmental			
Employer Contributions and Payroll Taxes Payable	-	23,744.20	23,744.20
Liability for Advances from Federal Sources	-	803,022.59	803,022.59
Total Intragovernmental	-	826,766.79	826,766.79
Liabilities with the Public			
Accrued Funded Payroll and Leave	-	255,968.34	255,968.34
Employer Contributions and Payroll Taxes Payable	-	1,805.94	1,805.94
Unfunded Leave	464,188.40	-	464,188.40
Liability for Advances from Non Federal Sources	-	392,254.12	392,254.12
Accrued Health and Flexible Spending Benefits	87,322.79	-	87,322.79
Commercial Bank Balance	1,434,740.66	-	1,434,740.66
Total Liabilities with the Public	1,986,251.85	650,028.40	2,636,280.25
Total Other Liabilities	1,986,251.85	1,476,795.19	3,463,047.04

Note 9 – Retirement Plans

Federal

ARC participates in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) for federal and certain non-federal employees. The CSRS and FERS plans are administered by the OPM. ARC's contributions to these plans for FY 2017 were \$5,887 and \$147,497 for CSRS and FERS, respectively and contributions for FY 2016 were \$5,472 and \$136,313 for CSRS and FERS, respectively.

Several employees also participate in the Federal Employees Health Benefit plan (FEHB) and the Federal Employees Group Life Insurance program (FEGLI), also administered by OPM. ARC pays a portion of the cost of current employees. Post-retirement benefits are

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paid by OPM. ARC's contributions to these plans for FY 2017 were \$52,174 and \$897 and for FY 2016 were \$43,757 and \$783 for FEHB and FEGLI, respectively.

ARC does not report in its financial statements CSRS, FERS, FEHB or FEGLI assets, accumulated plan benefits or unfunded liabilities, if any, applicable to its employees.

ARC also contributed \$35,255 and \$32,601 to the Federal Thrift Savings plan for all eligible employees for the years ended September 30, 2017 and 2016, respectively.

Non-Federal

The following table presents the pension benefit expense for the defined benefit pension plan by component for fiscal years 2017 and 2016:

	2017	2016
Service cost	\$713,746.00	\$701,404.00
Interest cost	945,917.00	1,004,440.00
Expected return	(1,638,972.00)	(1,509,109.00)
Amortization of prior service cost	415,646.00	415,646.00
Recognized loss	501,343.00	307,643.00
Net periodic benefit cost	<u>\$ 937,680.00</u>	<u>\$ 920,024.00</u>

The following table presents the pension liability or prepayment by component for fiscal years 2017 and 2016:

	2017	2016
Pension liability at October 1	(\$3,572,932.00)	(\$3,647,496.00)
Net periodic benefit expense	937,680.00	920,024.00
Contributions	(815,000.00)	(845,460.00)
Pension Prepayment at September 30	<u>\$ (3,450,252.00)</u>	<u>\$ (3,572,932.00)</u>

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	2017	2016
<u>Additional Information</u>		
Benefit obligation	(29,356,138.00)	(28,205,947.00)
Fair value of plan assets	25,160,836.00	23,076,946.00
Funded status	\$ (4,195,302.00)	\$ (5,129,001.00)
Employer contribution	\$ 815,000.00	\$ 845,460.00
Participant contribution	0.00	0.00
<u>Benefits paid</u>	469,813.00	355,737.00
Net periodic benefit expense	\$ 25,160,836.00	\$ 23,076,946.00

The accumulated benefit obligation was \$25,160,836 and \$23,076,946 at September 30, 2017 and 2016, respectively.

Weighted-average of economic assumptions used to determine benefit obligations at September 30:

	2017	2016
Discount rate	3.65%	3.40%
Rate of compensation increase	3.00%	3.00%

Weighted-average of economic assumptions used to determine net periodic benefit cost for the years ended September 30:

	2017	2016
Discount rate	3.40%	4.15%
Expected return on plan assets	7.25%	7.25%
Rate of compensation increase	3.00%	3.00%

Plan Assets

Pension plan weighted-average asset allocations at September 30 are as follows:

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<u>Asset Category</u>	<u>2017</u>	<u>2016</u>
Equity securities	38.77%	34.00%
Debt securities	56.66%	61.07%
Real Estate	4.57%	4.93%
Other	0.00%	0.00%
Total assets	<u>100.00%</u>	<u>100.00%</u>

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

<u>Fiscal Year</u>	<u>Amount</u>
2018	1,138,695
2019	1,243,330
2020	1,251,513
2021	1,408,557
2022	1,418,118
Years 2023-2027	7,547,131

ARC contributed \$285,118 and \$265,820 to the 401(k) plan for the years ended September 30, 2017 and 2016, respectively.

Note 10 – Leases

ARC's lease for its office commenced on April 30, 2013 and extends through March 31, 2025. The future minimum lease payments required under this lease are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2018	946,841
2019	968,148
2020	989,911
2021	1,012,129
2022	1,051,894
Thereafter	<u>2,774,553</u>
Total	<u>\$ 7,743,476</u>

Rent expense for the years ended September 30, 2017 and 2016 was \$969,455 and \$953,397.86 respectively.

Note 11 –Costs and Exchange Revenue

Intragovernmental costs are those of goods/services purchased from a federal entity.

	Total 2017	Total 2016
ARC		
Intragovernmental costs	\$ 3,074,514.95	\$ 5,949,560.64
Public costs	110,574,225.87	70,113,951.72
Total ARC Program costs	113,648,740.82	76,063,512.36
Intragovernmental earned revenue	431,884.27	481,965.32
Public earned revenue	4,129,566.45	3,979,397.68
Total ARC Program earned revenue	4,561,450.72	4,461,363.00
Total ARC Program Net Costs	\$ 109,087,290.10	\$ 71,602,149.36

Public earned revenue represents state contributions for half of ARC non-federal administrative expenses, and other minor items unrelated to state contributions.

Note 12 – Corrections of Cumulative Results from Operations

An adjustment to reflect the correct advance balance of \$209,968 for the State’s Contribution was made on the FY 2016 year-end financial statements however; the expenditure was not reclassified from reimbursable back to a direct expense. The only impact is that the expended appropriation entry of 3107/5700 should have been posted to the general ledger. This adjustment was posted as a correction in the current fiscal year as 3108/5708 for \$209,968.

Note 13 – Apportionment Categories of New Obligations and Upward Adjustments: Direct vs. Reimbursable Obligations

Apportionment is a plan, approved by the OMB, to spend resources provided by one of the annual appropriations acts, a supplemental appropriations act, a continuing resolution, or a permanent law (mandatory appropriations). OMB Circular A-11 defines apportionment categories as follows:

- Category A apportionments distribute budgetary resources by fiscal quarters.
- Category B apportionments typically distribute budgetary resources by activities, projects, objects or a combination of these categories.
- Exempt – Exempt from apportionment

Obligations incurred reported on the Statement of Budgetary Resources consist of the following:

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	<u>2017</u>	<u>2016</u>
Direct Category B Obligations		
Cat B- Non-Highway Programs	129,025,166.38	103,011,893.89
Cat B- RD (12-46X0200.020)	20,887,393.52	7,154,809.59
Cat B- EDA (13-46X0200.020)	4,861,300.83	4,922,500.00
Cat B- FHWA Non-Highway Programs(69-46X0200.05)	1,051,888.00	322,981.49
Cat B- HUD (86-46X0200)	2,322,656.00	3,226,517.00
Total direct obligations	<u>158,148,404.73</u>	<u>118,638,701.97</u>
Reimbursable Category B Obligations		
Cat B- Non-Highway Programs	4,554,172.19	4,557,801.78
Total reimbursable obligations	<u>4,554,172.19</u>	<u>4,557,801.78</u>
Total Obligations	<u>\$ 162,702,576.92</u>	<u>\$ 123,196,503.75</u>

Note 14 – Undelivered Orders at the End of the Period

Undelivered orders represent the value of goods and services ordered and obligated that have not been received. This amount includes any orders for which advance payment has been made but for which delivery or performance has not yet occurred.

	<u>2017</u>	<u>2016</u>
Unpaid Undelivered Orders	\$ 232,807,284.51	\$ 188,963,668.20
Paid Undelivered Orders	<u>\$ 40,996,530.86</u>	<u>\$ 42,629,853.77</u>
Total Undelivered Orders	<u>\$ 273,803,815.37</u>	<u>\$ 231,593,521.97</u>

Note 15 – Permanent Indefinite Appropriations

The Commission's permanent indefinite appropriation includes the trust fund. This fund has not been used since FY 2014. The balance in the trust fund is the amount sequestered in prior years.

Note 16 – Explanation of Differences between the SBR and the Budget of the U.S. Government

SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, requires an explanation of material differences between budgetary resources available, the status of those resources and outlays as presented in the Statement of Budgetary Resources to the related actual balances published in the *Budget of the United States Government* (Budget). The Budget that will include FY 2017 actual budgetary execution information is scheduled for publication in February 2018, which will be available through OMB's website at

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<http://www.whitehouse.gov/omb>. Accordingly, information required for such disclosure is not available at the time of publication of these financial statements.

Balances reported in the FY 2016 SBR and the related President's Budget reflected the following: (Dollars in Millions)

FY2016	Budgetary Resources	New Obligations & Upward Adjustments (Total)	Distributed Offsetting Receipts	Net Outlays
Statement of Budgetary Resources	187	123	0	64
<i>Budget of the U.S. Government</i>	187	123	0	64
Difference	0	0	0	0

The difference between the Statement of Budgetary Resources and the *Budget of the United States Government* for budgetary resources, obligations incurred and net outlays are primarily due to rounding.

Note 17 – Reconciliation of Net Cost of Operations to Budget

A reconciliation between budgetary resources obligated and net cost of operations (i.e. providing an explanation between budgetary and financial (proprietary) accounting) is as follows:

	2017	2016
Budgetary Resources Obligated	\$ 162,702,576.92	\$ 123,196,503.75
Spending Authority from Recoveries and Offsetting Collections	(11,400,332.29)	(15,508,428.44)
Imputed Financing from Costs Absorbed by Others	197,943.83	178,981.24
Changes in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but Not Yet Provided	(42,450,573.33)	(36,208,108.60)
Other	13,851.28	(56,798.59)
Increase in Annual Liability	23,823.69	
Net Cost of Operations	\$ 109,087,290.10	\$ 71,602,149.36

Note 18 – Subsequent Events

ARC has evaluated subsequent events occurring after the balance sheet date and through the date of November 2, 2017, the date the financial statements were available for release. Based upon this evaluation, ARC has determined that no subsequent events have occurred which require disclosure in the financial statements.