NATIONAL SCIENCE FOUNDATION

CHIEF FINANCIAL OFFICER'S

FY1997 ANNUAL REPORT

NATIONAL SCIENCE FOUNDATION
4201 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22230

OFFICE OF THE
DIRECTOR

March 25, 1998

Dear Readers:

It is my pleasure to present the National Science Foundation's 1997 Annual Financial Report.

NSF's portfolio of investments in research and education is motivated by a clear vision of how science and technology will shape our future as a nation and drive progress, productivity, and innovation across our society. These investments aim to provide the intellectual infrastructure that helps lead and shape the information revolution, address key national priorities in such areas as global change and the environment, improve teaching and learning at all levels of education, and embrace a commitment to reaching out and raising public understanding of science and technology. Guiding all of this is the Foundation's longstanding commitment to merit-based processes and decisions that adhere to the highest standards of excellence.

NSF is always seeking new ways to increase the already high returns on the taxpayer's investment in science and engineering. For example, priority is given throughout the Foundation to activities with strong ties to industry and other potential users of NSF-supported advances. In addition, special emphasis is placed on activities that improve the productivity of research and education, particularly in the use of advanced information technology for administrative processes.

We hope you find this report to be useful, informative and engaging, and we thank you for your interest in the Foundation.

Sincerely,

Neal Lane

Neal Lane
Director

NATIONAL SCIENCE FOUNDATION
4201 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22230

FEB 27 1998

Dear Readers:

I am pleased to present to you the National Science Foundation's Chief Financial Officer's *Annual Report* for Fiscal Year 1997. This report accounts to the taxpayers for the $3.3 billion appropriated to the Foundation by the U.S. Congress. It shares our pride and excitement in what the Foundation -- in partnership and as catalyst with U.S. scientists, engineers, and educators -- has achieved with these funds. We believe our investments make a significant difference and improve the quality of life.

We seek to be leaders in excellent business practices and to further the NSF's mission to promote the progress of science so that we are effective in our program investments and efficient in our operations. Advanced technology has enabled us to make significant strides in electronic communication with our grantee community, keeping overhead costs at a minimum and, most importantly, reducing administrative burdens for our customers.

We strive to streamline and work smarter. Today, NSF conducts more than half of its business using the World Wide Web. While technology plays a prominent and vital role, we will continue to emphasize human resource development, as we transform our work environment and culture to one that will be further defined by outcomes and results.

I invite you to read this report in detail, and to visit our Home Page on the Internet (http:\\www.nsf.gov). Ask questions, and share your ideas and suggestions for how we at NSF can continue to promote the progress of science.

Sincerely,

Joseph L. Kull
Chief Financial Officer

NATIONAL SCIENCE FOUNDATION

FY 1997 CHIEF FINANCIAL OFFICER'S ANNUAL REPORT

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OVERVIEW

NATIONAL SCIENCE FOUNDATION
FY 1997 CFO ANNUAL REPORT

OVERVIEW

The latter half of the 20th century has been a period of extraordinary change in the way we live, work, and play. A mere fifty years ago it was unimaginable that without leaving home we could have instantaneous access to the greatest collection of knowledge ever assembled, electronic mail that allows immediate worldwide communication literally at your fingertips, or radio telescopes that receive detailed data from exotic objects in the distant universe. Without question, advances in science, engineering and technology have played a major role in bringing about the progress that has been made in health, prosperity and welfare.

At the end of World War II, President Franklin Delano Roosevelt asked Vannevar Bush, Director of the Office of Scientific Research and Development, to transform the successful large-scale wartime research and development effort to a peacetime effort. The result was congressional enactment of the National Science Foundation Act of 1950, which created the National Science Foundation (NSF) and authorized it to initiate and support basic scientific research, research fundamental to the engineering process and education programs at all levels, in all fields of science and engineering. The Act also authorized establishment of an information base for science and engineering appropriate for development of national and international policy.

Without question, advances in science, engineering and technology have played a major role in bringing about the progress that has been made in health, prosperity and welfare in the latter half of the 20th century.

Almost fifty years later, the National Science Foundation continues its long-standing tradition of investing in the nation's science and engineering intellectual and physical infrastructure. The Foundation holds a special responsibility for the overall health of science and engineering across all disciplines, providing leadership across the frontier of scientific and engineering knowledge.

The NSF Statutory Mission:

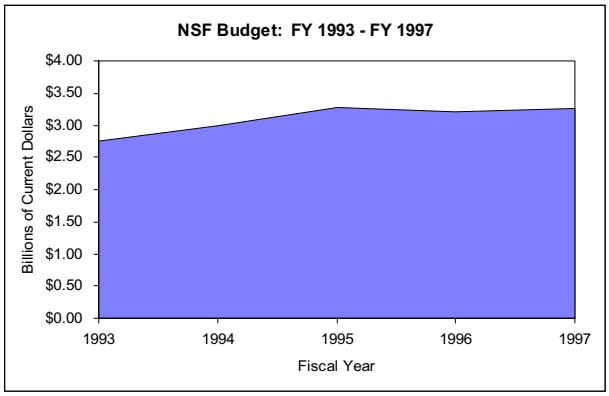
To promote the progress of science; to advance the national health, prosperity, and welfare; and to secure the national defense.

NSF also provides the stewardship necessary to strengthen and sustain the nation's science, mathematics, and engineering capabilities. By pursuing an integrative approach to research and education, the Foundation's investments ensure that America develops and maintains a premier cadre of scientists, engineers, mathematicians and science educators.

INVESTING IN THE FUTURE

Research is a high-risk enterprise that requires a long-term financial investment in which rates of return are uncertain and pay-off time frames are long. Nevertheless a commitment to frontier research is absolutely essential if the United States is to advance knowledge, continue to develop new technology, and lead the world in innovation.

NSF is analogous to a venture capital organization that provides "seed" money to fund creative opportunities in the exploration of science, mathematics, and engineering research and education. The Foundation itself does not conduct research. Rather, it provides funding to support the best ideas and most capable people in their pursuit of new knowledge, discoveries and innovation. The Foundation makes merit based grants and cooperative agreements and provides other forms of assistance to individual researchers and groups, in partnership with colleges, universities and other institutions -- public and private, state, local and federal -- throughout the United States.



THE STRATEGIC PLAN AND DESIRED OUTCOME GOALS

In the Fall of 1997, in compliance with the Government Performance and Results Act, the Foundation developed a new Strategic Plan that charts the course for NSF investment for the next three-to-five years. The desired future outcomes toward which the Foundation will be working are:

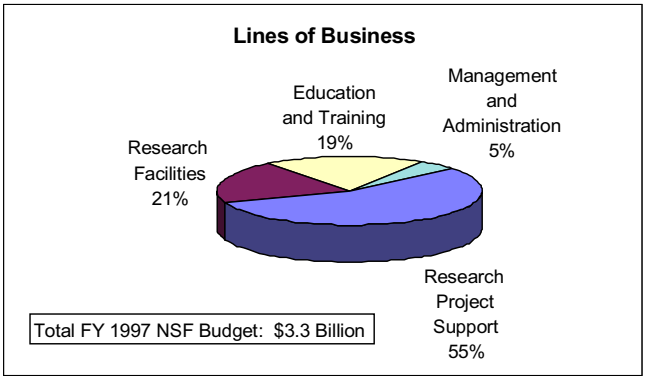
- Discoveries at and across the frontier of science and engineering;
- Connections between discoveries and their use in service to society;
- A diverse, globally-oriented workforce of scientists and engineers;
- Improved achievement in mathematics and science skills needed by all Americans; and
- Timely and relevant information on the national and international science and engineering enterprise.

These goals will be realized through the Foundation's investments in three primary lines of business -- Research Project Support, Research Facilities, and Education and Training. In addition, program support is provided by the Administration and Management function, which accounts for about five percent of the Foundation's budget.

RESEARCH PROJECT SUPPORT

In FY 1997, more than half -- 55 percent -- of NSF's $3.3 billion budget was for Research Project Support. The Foundation develops intellectual capital by funding individuals and small groups devoted to research in traditional fields as well as to those performing cross-disciplinary research and research in areas of national priority. NSF supports researchers, postdoctoral associates, undergraduate and graduate student assistants as well as provides funding for those items necessary for performing research, such as instrumentation, supplies, and related costs for travel and conference support.

Through Research Project Support, NSF also provides funding for centers, based on the premise that some scientific questions and research problems can best be addressed through the multi-disciplinary, long-term, coordinated efforts of many researchers. In FY 1997, the Foundation provided support for a wide array of research centers, including Engineering Research Centers, Science and Technology Centers, Materials Research Science and Engineering Centers, Earthquake Engineering Research Centers and Long-Term Ecological Research sites.



The support of research projects contributes directly to fulfilling NSF's strategic outcome goals of making discoveries at the frontier of science and of making connections between discoveries and their use in service to society. Moreover, the collaboration of researchers, postdoctoral fellows, and student assistants working together on a research project is a natural integration of research and education and a critical component to the development of a diverse, globally-oriented workforce of scientists and engineers, another of NSF's strategic outcome goals.

In FY 1997, NSF grantees made significant discoveries across all fields of science, mathematics and engineering. For example:

- The discovery of a molecular mechanism that provides disease resistance in plants sets the stage for developing genetically engineered disease-resistant crops in the future.

- Researchers have concluded that adding soluble iron to certain low productive tropical ocean waters resulted in uncharacteristically strong blooms of algae. Simulating plant growth in the oceans is seen as a possible weapon in combating carbon dioxide build-ups in the atmosphere.

- Polymer-based composites are finding increasing applications in diverse areas ranging from microelectronics to adhesives. Recently, this has been extended to large-scale technology. A research group at the NSF Science and Technology Center for High Performance Polymeric Adhesives and Composites at Virginia Polytechnic Institute replaced the deteriorated Tom's Creek Bridge near Blacksburg, Virginia, with one made from a polymer matrix composite reinforced by carbon/glass fibers.

- At the Science and Technology Center on Computer Graphics and Scientific Visualization, radical re-thinking of the human interface in computer-aided design led to development of the "Sketch" system, in which the computer translates simple sketches into detailed engineering models

- Radio carbon dating is reliable for organic material up to 30,000 years old, and potassium argon dating is reliable for other materials over 300,000 years old. Until recently, dating techniques were lacking for other materials/ages. NSF-supported researchers at the Carnegie Institute of Washington have established reliable indices of time-dependent changes in amino acids, and have pushed back the known date for anatomically modern human fossils to at least 125,000 years.

In the 28 years since the establishment of the Nobel Memorial Prize in Economic Sciences, all but a handful of winners have been NSF grantees. In 1997, the award was once again presented to a NSF grantee, Robert Merton of Harvard, who, with his colleagues, developed a pioneering formula for valuation of stock options. This work generated new types of financial instruments that are now the basis for a trillion-dollar market worldwide.

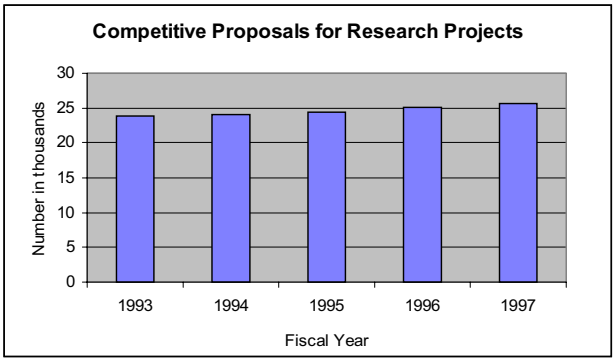
- Engineers at the Center for Emerging Cardiovascular Technologies based at Duke

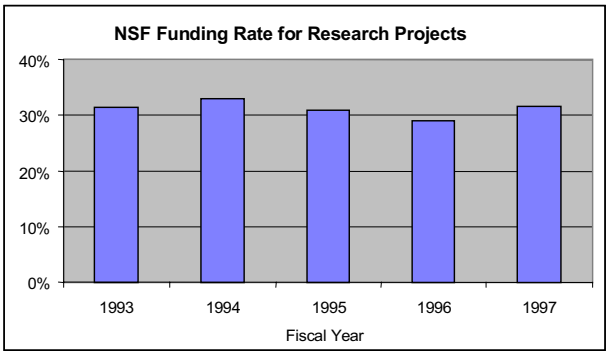
University have injected biopsied skeletal muscle cells directly into a damaged heart, and within two weeks the cells formed elongated healthy muscle fibers extending through the damaged zone. One day doctors may transplant skeletal muscle obtained from a patient's leg or arm into the heart to repair damage after a heart attack.

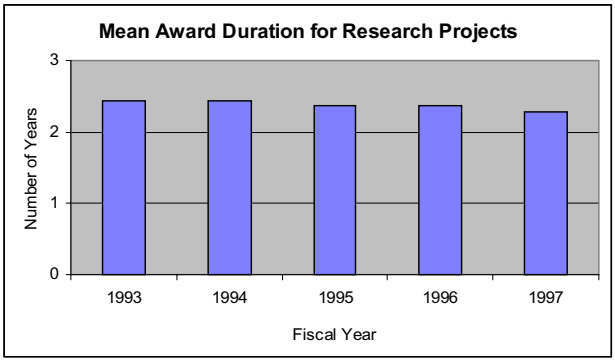
- In partnership with the National Academy of Science and the National Institutes of Health, NSF support is providing the framework for study of human genetic diversity. An award to the University of Utah resulted in a prototype laboratory for contemporary molecular biotechnology that can make DNA-type collection and preservation practicable in the third world. This is a basic step in the study of human genetic diversity worldwide, and to understanding human evolution and migration.

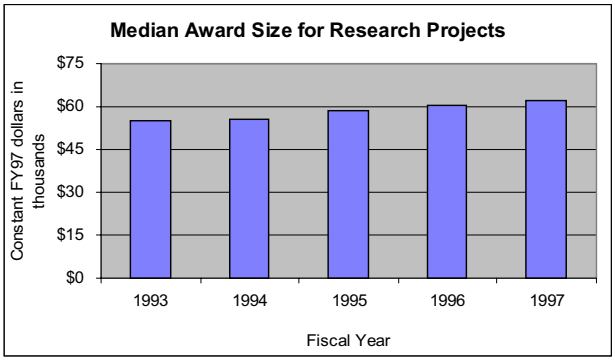
- The Classic Maya civilization, centered in the Yucatan Peninsula of Mexico and Central America, developed around 3,000 years ago and was well adapted to its tropical environment reaching population levels that far exceed modern levels. Yet this civilization suffered a sudden decline around 800 A.D. Paleoclimatologists have reconstructed the region's history of climate variability over the past 3,500 years from isotopic measurements of fossil organisms recovered in lake sediment cores. The record reveals an interval of frequent drought throughout the region, which coincides with the collapse of this civilization. Although population growth, environmental degradation and inter-city conflict may also be implicated, the paleoclimatic record provides evidence that the multi-decadal and millennial-scale change in evaporation/precipitation are closely related to cultural evolution and may be a key factor in societal history.

Performance Information for Research Project Support









- NSF-funded researchers presented the first direct evidence that increased ultraviolet light (UVB) damages the DNA of Antarctic icefish eggs and larvae. The ozone hole opens up over Antarctica every southern spring, letting more UVB from the sun penetrate to the earth's surface. The study demonstrated that icefish eggs accumulate significant levels of DNA lesions called cyclobutane pyrimidine dimers. Ozone depletion has previously been shown to harm one-celled marine plants in Antarctica but now it has been documented that significant damage is occurring higher up the food chain. The studies were done on cruises in waters around the Antarctic Peninsula. The next step is to explore whether the DNA damage actually hampers the animals' ability to survive. This study shows that key members of the Southern Ocean food web (the food base for seabirds, whales, and seals) could all be vulnerable to increased UVB.

- The thickness of annual tree growth rings is determined by climate, temperature and rainfall. NSF-supported researchers at Cornell University have established a 6,500-year sequence for tree ring patterns for the Middle East, during the period of development of agriculture and cities. Analysis of the rings themselves has allowed reconstruction of the climate, including human/ecological interactions, over the same time period.

RESEARCH FACILITIES

Research Facilities are characteristically complicated and expensive projects that require a long-term investment commitment. The Foundation supports research facilities -- including initial construction as well as ongoing operations -- principally to provide U.S. researchers access to state-of-the art capabilities, including instruments, that enable research at the cutting-edge of science and engineering.

In FY 1997, support for research facilities accounted for about 20 percent of the total NSF budget. NSF supports a wide range of research facilities in different fields, among them the National High Magnetic Field Laboratory, Antarctic research facilities, the National Center for Atmospheric Research, the Incorporated Research Institutions for Seismology, the Ocean Drilling Program, the National Astronomy Centers, and Advanced Scientific Computing facilities.

An example of working at the frontier of science at a NSF-supported facility is the major breakthrough that was made in understanding gamma ray bursts in FY 1997. Gamma ray bursts are highly energetic explosions that have been one of the biggest mysteries in astrophysics for the last 30 years. In late 1996, the newly launched Italian-Dutch satellite BeppoSAX was able to provide much more accurate information to pinpoint the bursts' location than previous spacecraft. Using this information, several observatories, including the Very Large Array (VLA) and the Very Long Baseline Array (VLBA) radio telescopes, were able to make observations that have provided unprecedented knowledge about a class of objects about which almost nothing was known.

A photograph of one of the VLBA radio telescopes, located at Los Alamos, New Mexico

The VLA is an array of 27 radio telescopes located in New Mexico, and the VLBA is an array of ten radio telescopes spread out over the full length and width of the United States, from the Virgin Islands to Hawaii. Both are instruments of the National Radio Astronomy Observatory, a NSF-supported facility.

Although the research done at the national facilities may appear remote, the implications and results of this research often have real-life impact on our daily lives. For example, many technologies depend on research in high magnetic fields or on advanced magnets, work that is currently being done at the National High Magnetic Field Laboratory. High magnetic fields continue to play an important role in semiconductor research that drives advances in computer technology, and new magnetic resonance techniques open up research opportunities in structural chemistry and biology that impact drug design and treatment. The development of new magnetic resonance techniques will also lead to advanced Magnetic Resonance Imaging (MRI) systems. Another example of fundamental importance is the study of high temperature-superconductors and ultimately the hoped-for discovery of room-temperature superconductivity. The technological and economic potential of such superconductors in such areas as magnetic levitation and propulsion, and energy storage and transportation, is likely to be significant.

Clearly, the support of research facilities contributes directly to the achievement of NSF's strategic outcome goals. National facilities provide the physical and institutional capabilities to prompt the discovery and dissemination of new knowledge in service to society. At research facilities, scientists and engineers carry out research that enables the United States to uphold world leadership across a broad spectrum of scientific and engineering fields. For graduate and undergraduate science, mathematics and engineering students, NSF-supported facilities provide opportunity for fully integrated research and education activities as students routinely work alongside senior staff to acquire the skills to perform world class research. Indeed, the students currently being trained at NSF-supported research facilities will be members of the next generation's diverse, globally oriented workforce.

This image of the Gemini construction site at Mauna Kea, Hawaii, was taken in December 1997. A camera mounted on the site takes pictures at regular intervals and posts them on the Web, providing a ready means of monitoring progress. The Hawaii telescope is one of a pair of 8-meter telescopes -- the other is located in Chile -- currently under construction. Once completed, the telescopes will be ten times more sensitive than existing telescopes and will be used to study the origins of planets and stars, chemical elements, and the universe itself. The Gemini project is supported by funding from NSF and a group of international partners. For the construction and commissioning phases it is being managed by the Association of Universities in Research in Astronomy, Inc. (AURA). For futher information, check out the Gemini website, www.gemini.edu.

Performance Information. The Foundation is committed to efficient and effective operation of its facilities as well as good management of facility construction projects. Periodic status reports of on-going facility construction projects go to both the National Science Board and the NSF Director. For example, the October 1997 Laser Interferometer Gravitational-Wave observatory (LIGO) status report to the NSF Director indicated that activities were

proceeding on the projected schedule, costs were within estimates, all large contracts had been placed and major progress had been made on implementing procedures to involve scientists outside the LIGO project in research with the facility.

In an attempt to establish performance measures of NSF-supported national facilities, a pilot study of the performance of a select group of these facilities was completed in June 1997. This information will help NSF establish GPRA performance measures for NSF-supported facilities.

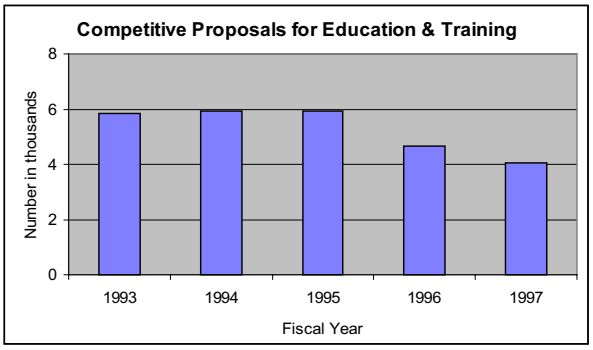
EDUCATION AND TRAINING

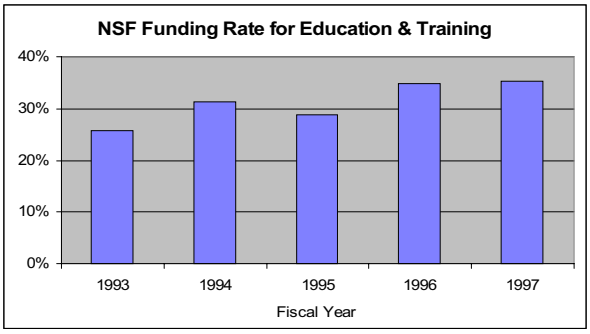
NSF's investment in Education and Training activities contribute directly to the strategic outcome goals of developing a diverse, globally oriented workforce of scientists and engineers, and improving achievement in mathematics and science skills needed by all Americans. The Foundation supports activities from pre-kindergarten through postdoctoral levels, including public science literacy aimed at enabling U.S. students to become scientifically literate citizens and well-trained members of the nation's workforce. Education and Training programs comprised about 19 percent of the total NSF FY 1997 budget.

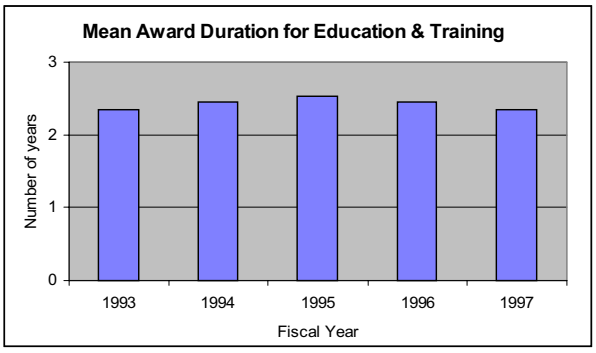
In addition, the Foundation supports the collection of data and the conducting of surveys that provide quantitative information about domestic and international resources devoted to science, engineering and technology. This information is crucial for policy formulation by NSF as well as other Federal agencies.

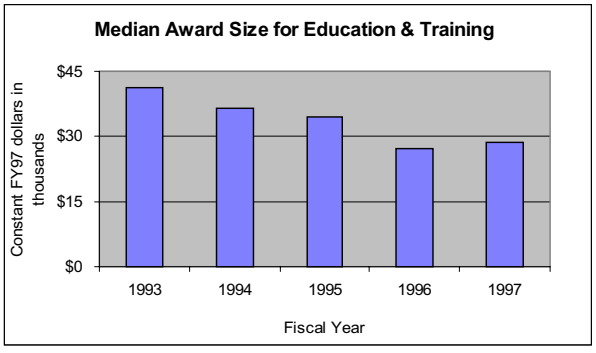
In 1991, NSF initiated its strategy for the systemic reform of science and mathematics education. With implementation now in states, urban and rural school districts, systemic reform is widely accepted as an effective means for increasing impact and sustaining improvements.

Performance Information for Education & Training









- Under the State Systemic Initiative (SSI), 17 states and Puerto Rico provide intellectual leadership for reform, impacting to date over 795,000 teachers and six million students. From 1991 to 1997, NSF has invested over $266 million in the SSI program; in 1997 alone, the NSF investment was matched by over $391 million from other sources that align their activities or resources with NSF sites to meet this common goal of national reform.

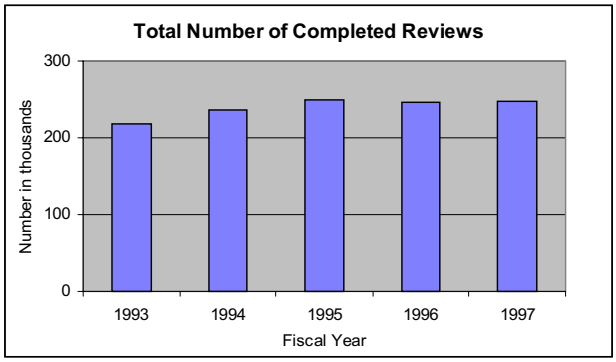
One way to increase scientific literacy is to bring science to unexpected places. With support from the Directorate for Education and Human Resources' Informal Science Education program, Scholastic's **The Magic School Bus** ***television and book series have done just that.*** **The Magic School Bus** ***can be seen on PBS stations nationwide, and stations showing this program work with schools and libraries to coordinate*** **Magic School Bus** ***activities.***

- In 1993, the Urban System Initiatives (USI) program began to catalyze science and mathematics education reform in urban areas with the largest number of school-age children in poverty. Through 1996, USI has impacted more than 145,000 teachers and 1.4 million students in 20 cities. In Chicago, for example, student achievement in grades three and six in USI schools have increased for two consecutive years, outpacing non-participating schools; significantly more students are completing algebra before high school; and several hundred teachers are receiving training to improve their credentials.

Graduate Research Fellowships have been awarded by the Foundation since 1952. A Minority Graduate Fellowship component was initiated in 1978. A Women in Engineering component was added to both in 1990, and a Women in Computer and Information Science component in 1994. Since its inception, over 33,000 U.S. students have received such awards. Many have contributed significantly to basic research, to academe, and to industry.

MERIT REVIEW: SELECTING FOR EXCELLENCE

Each year, the Foundation receives thousands of proposals, each of which is evaluated by experts in the fields of science, engineering, mathematics and education, through a merit review process. The merit review process is critical to NSF's efforts to foster the highest standards of excellence and accountability. NSF program officers rely on the recommendations of expert reviewers to help make often difficult decisions on how to best allocate limited resources and to target those proposals that promise to produce the most significant contributions.



Merit review is successful because of the thousands of experts from various fields who volunteer their time to evaluate and determine which proposals deserve consideration for funding. In FY 1997, nearly 248,000 reviews

were provided by experts as part of this merit review process.

NSF continuously assesses the effectiveness and fairness of the merit review process to ensure equal access to funds and to maintain a fresh perspective on research ideas worth pursuing. In 1997, the National Science Board approved new criteria for evaluating funding proposals, following discussions with the research and education community and analysis by a special NSF task force. Under the new criteria, reviewers are asked to consider both the intellectual merit and quality of the proposed activity, and the broader impacts of the proposed activity.

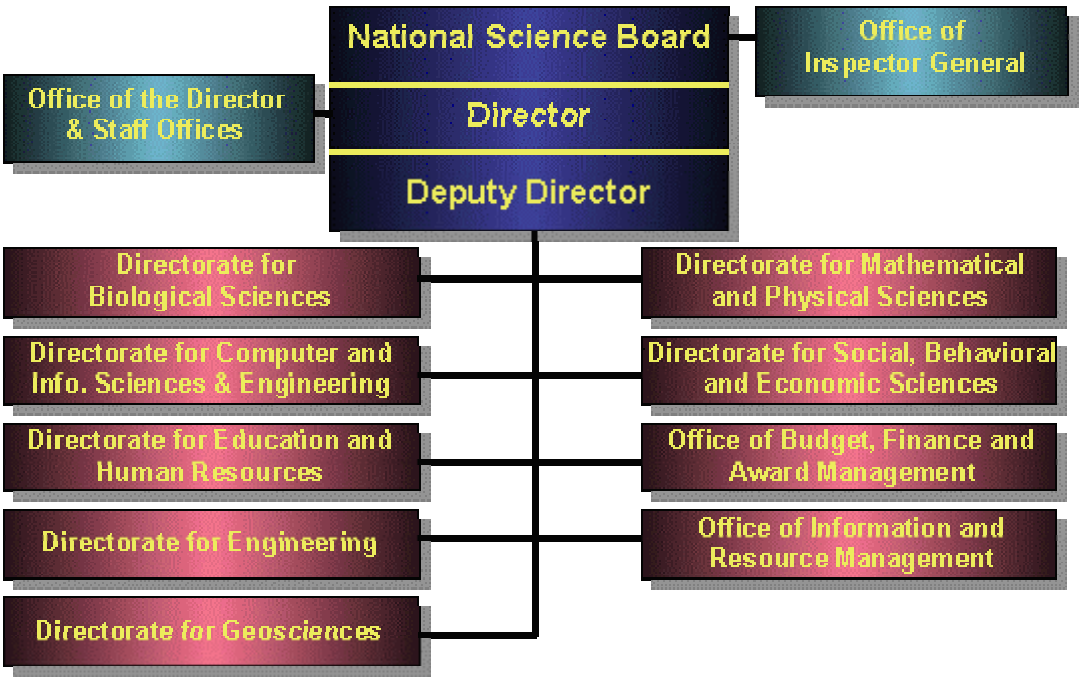
ADMINISTRATION AND MANAGEMENT

Organizational Structure. NSF is headed by a Director who is appointed by the President and confirmed by the United States Senate to serve a six-year term. The Foundation is governed by a National Science Board consisting of 24 part-time members, each appointed by the President with the advice and consent of the U.S. Senate. Each serves a six-year term, with one-third appointed every two years, selected solely on the basis of established records of distinguished accomplishments. The Director is a member *ex officio* of the board. The Board also serves the President and the Congress as an independent advisory body on policies affecting the health of U.S. science and engineering and on education in science and engineering

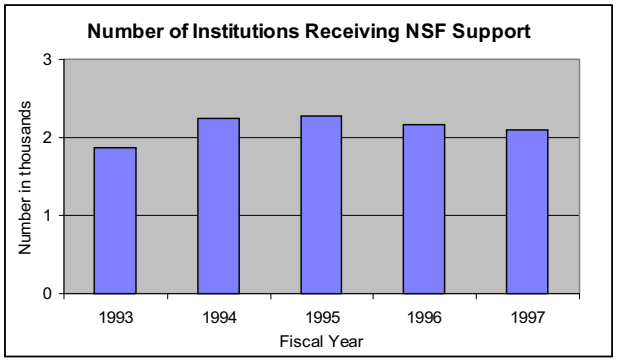
NSF is structured much like its academic clientele, with divisions delineated by various disciplines and fields of science and engineering, and for science, math, engineering and technology education. The Foundation has seven operating directorates and two management offices. (See organization chart.)

Workload and Staff. Since FY 1988, the Foundation's budget and the volume and complexity of its workload have increased dramatically, yet its staff has remained relatively stable. In FY 1988, the Foundation's budget was $1.7 billion, and staffing was about 1,200 FTEs (full-time equivalents). In FY 1997,

National Science Foundation Organization Chart



NSF's budget had nearly doubled to $3.3 billion, accompanied by significant increases in the number of competitive proposals received and in the number of active awards. In addition, the number of institutions to which NSF awards grants and makes agreements has also increased substantially. Staffing, however, has increased only about ten percent.



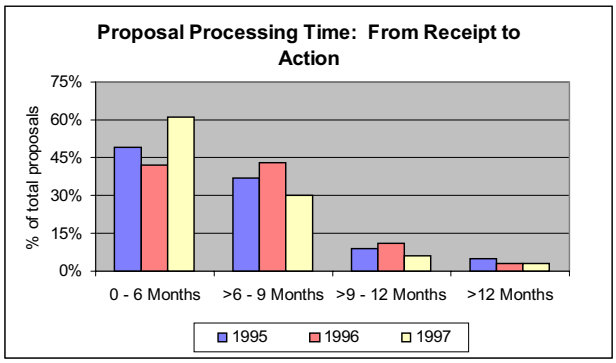
Streamlining Administrative Processes. To meet this growing workload, the Foundation has actively pursued the use of advanced information technology to redesign the way NSF does business and reduce the administrative burden on NSF staff as well as NSF customers. In an attempt to move towards more streamlined, paperless electronic administrative activities, the Foundation initiated the FastLane project in 1994.

FastLane was developed to enable the NSF and its customer community to conduct and facilitate business transactions and exchange information electronically using the World Wide Web. Since its inception, FastLane has been tremendously successful, and experienced explosive growth in all areas in FY 1997. The system that began as an experiment with 16 university partners currently has 600 registered institutions. Today, NSF conducts nearly $2 billion worth of business on FastLane. Among the enhancements added in FY 1997 were post-award notifications and requests, institutional reports spreadsheet download, postdoctoral fellowship applications, reviewer profile information, new proposal cover sheet and other proposal forms, and expansion of cash request.

Year 2000 Issue. The Year 2000 problem is a result of computer programs written using two digits rather than four to identify an applicable year. Computer programs that have time-sensitive software may recognize a date using "00" as the year 1900 rather than 2000, thus resulting in miscalculations or even system failure. NSF has conducted a comprehensive review of its computer systems to identify those that could be affected by the Year 2000 issue and has developed an implementation plan to resolve the issue. NSF is currently on schedule for completing the Year 2000 transition and fully expects to meet OMB's target date of March 1999 for agency compliance. The Foundation is also working with the grantee community to ensure NSF-related activities will not be adversely impacted by the Year 2000 problem.

Customer Service Standards. Grantees and potential grantees are the Foundation's primary customers. Thus NSF has chosen to focus on the proposal review process to set customer service standards. In FY 1997, NSF made significant progress towards achieving its customer service standard of providing notice of a decision to 95 percent of applicants within six months.

In FY 1997, 61 percent of grant applications were processed within six months, and 30 percent within six to nine months. This is a marked improvement from the prior year, when 42 percent of grant applications were processed within six months and 43 percent within six to nine months. The Foundation will continue to work towards meeting its customer service standards.



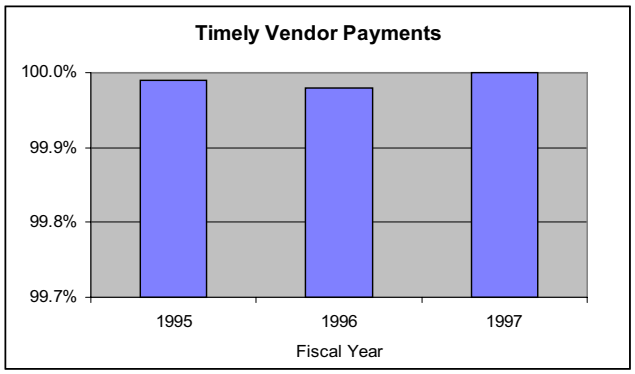
FinanceNet. As part of the Administration's efforts to create a government that "works smarter and costs less," FinanceNet was established to provide an efficient means to disseminate information on Federal financial management. NSF is the innovator, developer, and custodian for FinanceNet *(www.financenet.gov),* the government's Internet "home page" for financial management improvement initiatives.

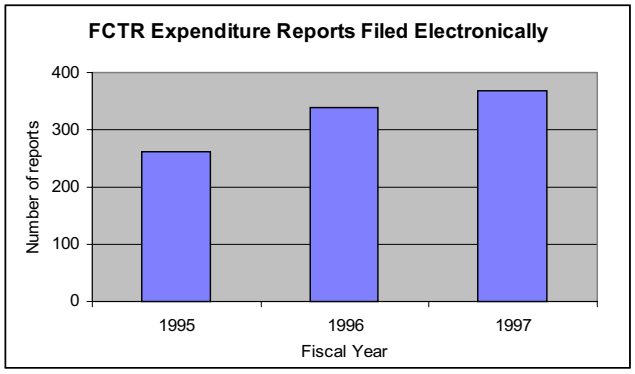
Open and accessible to everyone, FinanceNet provides an electronic forum for federal, state and local and international government financial managers, and other interested members of the general public, to exchange ideas and information on topical issues. FinanceNet also serves as a repository or access point to volumes of Federal financial management laws and regulations and other reference materials which would normally take significant time and energy to locate, compile and receive.

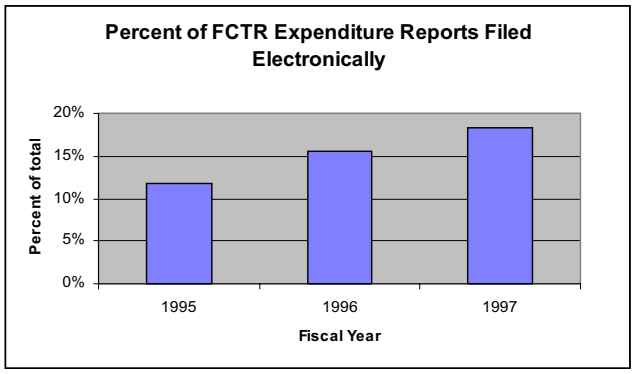
In FY 1997, FinanceNet World Wide Web visits increased to approximately 13 million "hits" per year with subscriptions to its more than 50 topical Internet mailing lists increasing to over 30,000. The Foundation also further broadened FinanceNet's outreach. In FY 1997, NSF, through FinanceNet, completed the worldwide release of the International GovNews project (IGP) which provides electronic access *(www.govnews.org)* to a wealth of public government information to citizens worldwide. The Foundation chairs the IGP Coordinating Committee.

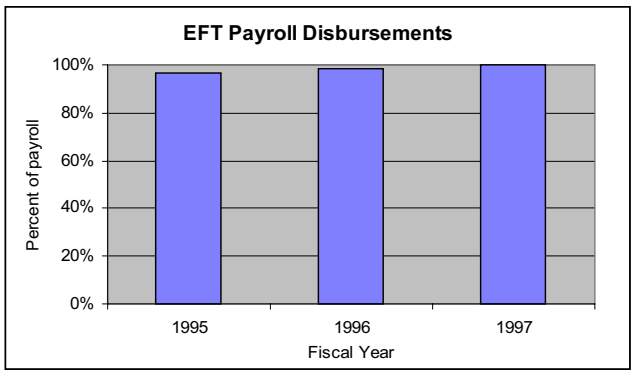
Financial Performance Measures. In the area of financial management, in FY 1997, the Foundation continued to meet or exceed virtually every Federal goal for performance. As evidence*:*

- NSF paid virtually no interest penalties due to late payment to vendors.









- All NSF employees were paid through electronic funds transfers.

- All required OMB reporting and reconciliations were completed on time.

- Delinquent accounts receivable were held to a minimal amount and write-offs, as necessary, promptly occurred.

- There was an increase in the number of electronic transactions with grantees and vendors.

Each of these helps the Foundation maintain its leadership role in Federal financial management practices.

PREPARING FINANCIAL STATEMENTS

The financial statements, included as part of this Report, present the financial position and results of operations and changes in net position of the National Science Foundation for the year ending September 30, 1997, pursuant to the requirements of 31 USC 3515(b), the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. The Foundation was granted a waiver by the Office of Management and Budget (OMB) from preparing statements of cash flows, budgetary resources and actual expense. Consequently, these statements are not included in this NSF FY 1997 report.

NSF prepared the attached financial statements from its books and records in accordance with the formats prescribed by OMB Bulletins No. 94-01 and No. 97-01, "Form and Content of Agency Financial Statements." These statements are, however, different from the financial reports used to monitor budgetary resources that are prepared from the same books and records and reported in Federal budget documents. Therefore, direct comparisons are not possible between figures found in this report and similar financial concepts found in the Fiscal Year 1997 budget of the United States Government.

Additionally, readers should realize that the financial statements are for a component unit of the United States Government, that liabilities not covered by budgetary resources reported in the financial statements cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

These are maturing* Arabidopsis thaliana *plants. NSF supports an international partnership to sequence the entire genome of this higher order flowering plant, which when completed will provide new knowledge with broad implications for agriculture, energy, environment and health.

PRINCIPAL FINANCIAL STATEMENTS
and
RELATED NOTES

National Science Foundation
Statement of Financial Position
As of September 30, 1997

(Amounts in Thousands)

Assets

Entity Assets:	
Intragovernmental Assets:	
Fund Balance With Treasury (Note 2)	$ 3,701,031
Accounts Receivable (Note 3)	889
Governmental Assets:	
Accounts Receivable, Net (Note 3)	436
Advances (Note 4)	41,352
Cash	15,265
Property and Equipment, Net (Note 5)	77,835
Total Assets	$ 3,836,808

Liabilities

Liabilities Covered by Budgetary Resources	
Intragovernmental Liabilities:	
Advances from Others (Note 6)	$ 75,080
Other Liabilities	496
Governmental Liabilities:	
Accounts Payable	30,661
Accrued Liabilities	109,977
Other Governmental Liabilities (Note 7)	4,484
Total Liabilities covered by Budgetary Resources	220,698
Liabilities Not Covered by Budgetary Resources	
Governmental Liabilities:	
Lease Liabilities (Note 8)	67
Accrued Unfunded Annual Leave	9,936
Accrued Workers' Compensation Benefits (Note 9)	1,061
Total Liabilities Not Covered by Budgetary Resources	11,064
Total Liabilities	231,762

Net Position

Balances:	
Unexpended Appropriations	3,495,449
Invested Capital	77,835
Cumulative Results of Operations	42,826
Future Funding Requirements	(11,064)
Total Net Position (Note 10)	3,605,046
Total Liabilities and Net Position	$ 3,836,808

National Science Foundation
Statement of Operations and Changes in Net Position
For The Year Ended September 30, 1997

(Amounts in Thousands)

Revenues and Financing Sources

Appropriated Capital Used	$ 3,065,055
Revenues from Sales of Goods and Services	
Intragovernmental	125,666
Other Revenues and Financing Sources	36,859
Imputed Financing - Post-Retirement Benefits Expense	6,360
Interest	973
Less: Receipts Transferred to the Treasury or Other Government Agencies	(540)
Total Revenues and Financing Sources	3,234,373

Expenses

Operating/Program Expenses (Note 11)	3,211,742
Depreciation Expense	7,869
Total Expenses	3,219,611
Excess of Revenues and Financing Sources Over Total Expenses	14,762
Net Position, Beginning Balance as Previously Stated	4,273,838
Prior Period Adjustments (Note 12)	(84,119)
Cumulative Effect of Change in Accounting Principles (Note 13)	(763,292)
Net Position, Beginning Balance as Restated	3,426,427
Excess of Revenues and Financing Sources Over Total Expenses	14,762
Plus Non Operating Changes (Note 14)	163,857
Net Position, Ending Balance	$ 3,605,046

Note 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the National Science Foundation ("NSF" or "Foundation") as required by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. They have been prepared from the books and records of NSF in accordance with the hierarchy of accounting principles and standards approved by the principals of the Federal Accounting Standards Advisory Board, Office of Management and Budget (OMB) Bulletin 94-01, Form and Content of Agency Financial Statements, and the Foundation's accounting policies which are summarized in this Note. 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 NSF applies accounting principles and standards and complies with operating policies and procedures established, issued, and implemented by the General Accounting Office (GAO), the OMB, and the Department of Treasury, as recommended by Federal Accounting Standards Advisory Board (FASAB). The accompanying financial statements have been prepared in accordance with the following hierarchy of accounting principles and standards, which constitutes another comprehensive basis of accounting:

1. Statements of Federal Financial Accounting Standards effective for 1997.
2. Form and Content requirements included in OMB Bulletins 94-01 (and 97-01, where applicable);
3. NSF accounting policies summarized in this note;
4. Accounting principles published by authoritative standard-setting bodies and other authoritative sources (1) in the absence of other guidance in the first three parts of this hierarchy, and (2) if the use of such accounting standards improve the meaningfulness of these financial statements.

NSF received a waiver from OMB for preparing the Statement of Cash Flows and the Statement of Budgetary Resources and Actual Expenses.

B. Reporting Entity

NSF is an independent federal agency created by the National Science Foundation Act of 1950 (P.L. 81-507). Its aim is to promote and advance scientific progress in the United States. The agency is responsible for the overall health of science and engineering across all disciplines. The Foundation is also committed to ensuring the

Nation's supply of scientists, engineers and science educators. 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 conduct research or operate research facilities. By award, NSF enters into a relationship to fund the research operations conducted by the grantees.

NSF is led by a presidentially - appointed director and governed by the National Science Board ("The Board"). The Board is composed of 24 members, representing a cross section of American leadership in science and engineering research and education, appointed by the President for 6-year terms. The NSF Director is a member ex officio of the Board.

C. Basis of Accounting

The accompanying financial statements have been prepared on the accrual method 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 over the use of Federal funds. NSF records its grants expenses from expenditure reports submitted by the grantees. Grantees may be on either an accrual or cash basis of accounting, and NSF records amounts as reported.

D. Revenues and Other Financing Sources

NSF receives the majority of its funding through congressional appropriations. 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 and appropriation allocations from other government agencies, as well as donations from foreign governments, private companies, academic institutions, non-profit foundations and individuals. Also, NSF receives interest earned on overdue receivables, excess cash advances to grantees and cash donation trust funds held in a commercial bank. The interest earned on overdue receivables and excess cash advances is returned to the Treasury.

Appropriations are recognized as revenues at the time the related program or administrative expenses are incurred. Revenues from reimbursable agreements are recognized when the services are provided and the related expenditures are incurred. Donations are recognized as revenues when funds are received.

During Fiscal Year 1997, a corporation that registered second-level Internet domain names under an NSF cooperative agreement deposited thirty percent of the amounts

charged for that service into a fund "for the preservation and enhancement of the 'Intellectual Infrastructure' of the Internet." In October 1997, $23 million dollars from that fund was credited to the Foundation's Research and Related Activities appropriation to assist with Next Generation Internet activities in Fiscal Year 1998. A preliminary injunction has been issued against the Foundation, however, regarding the use of the $23 million obtained by NSF during FY 1998 from registration fees collected by an NSF awardee. Until this interlocutory decision is reversed or the legal issues are resolved in NSF's favor, the Foundation will not obligate these monies.

E. Fund Balance with the U.S. Treasury and Cash

Cash receipts and disbursements are processed by the U.S. Treasury. The balances with Treasury are comprised primarily of appropriated funds that are available to pay current liabilities and finance authorized purchase commitments, but also include some trust funds. NSF has 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. All other donated funds represent the trust fund and are held by the U.S. Treasury.

F. Accounts Receivable

Accounts Receivable consists of amounts due from governmental agencies, private organizations and individuals. NSF establishes an allowance for uncollectible accounts receivable from private sources, but regards amounts due from other Federal agencies as 100% 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.

G. Advances

Advances are composed of advances to grantees, contractors and employees. The advances are recorded as assets until the grantee submits a Federal Cash Transaction Report (FCTR). At that time, the used portions of the payments are reclassified as an expense. At year end, NSF posts an accrual for the amount of unfunded expenses and adjusts the advance account by the portion of the expenses that have already been funded through grant advances. NSF makes a few advances to employees for travel expenses.

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

NSF capitalizes acquisitions with costs exceeding $25,000 and a useful life exceeding 2 years. Acquisitions not meeting these criteria are recorded as operating expenses. NSF currently reports capitalized PP&E at original acquisition cost; assets acquired from GSA's excess property schedules are recorded at the value assigned by the donating agency. Depreciation expense is calculated using the straight-line method. The economic life classifications for capitalized assets are as follows:

5 years	-	copiers, computers and peripheral equipment, fuel storage tanks, laboratory equipment, vehicles
7 years	-	aircraft, communications equipment, office furniture and equipment, pumps and compressors
10 years	-	generators
31.5 years	-	Buildings and structures placed in service prior to 1993
39 years	-	Buildings and structures placed in service after 1993

NSF occupies and pays rent for a building leased by GSA. GSA is the party to the lease with the building owners.

Nearly all of the PP&E reported on the FY 1996 Statement of Financial Position was maintained and operated by NSF grantees and contractors. In FY 1997, however, only PP&E over which NSF has operational responsibility is reported on the Statement. The FY 1997 balance consists of real and personal property, as well as construction in progress, used in the United States Antarctic Program (USAP) by NSF's contractor, Antarctic Support Associates (ASA), and the Department of Defense (DoD) , plus "in-house" PP&E maintained by NSF to support agency operations. This change reflects agency specific guidance from FASAB that PP&E used by awardees for research and development activities, which NSF is prohibited by statute from operating, should not be included in NSF asset balances. Although NSF retains title to the property to facilitate transfer to subsequent awardees, operations and control of this PP&E are transferred to awardees responsible for coordinating, directing and conducting research utilizing the PP&E resources. Current standards do not fully address this situation. Until standards are developed to more fully address this issue, FASAB has issued interim guidance that considers NSF's ownership interest in this PP&E to be "limited in practice to an interest similar to a reversionary interest", and directed the agency to exclude these items from the Statement of Financial Position. Rather, costs incurred to acquire such PP&E are treated as agency investments in research and development. This information is presented as Annual Stewardship information in the Research and Human Capital Statement reported in the attached Supplemental Financial and Management Information.

I. Advances from Others

Advances from Others are composed of amounts obligated and advanced by other federal entities for services to be furnished under reimbursable agreements.

J. Accrued Liabilities

Accrued Liabilities are composed of grant liabilities. Grant liabilities are grantee expenses not yet funded or reimbursed by NSF. At year end, NSF posts an accrual for the amount of unfunded grant expenses and adjusts the advance account by the portion of the expenses that have already been funded through grant advances.

K. 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 current pay rates. 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 nonvested leave are expensed as taken.

L. Accrued Workers' Compensation

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 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 Salaries and Expenses Appropriations will be used for DOL's estimated reimbursement.

M. Cumulative Results of Operations

A net income or loss can result from the operation for a period to the extent that donated revenues are received in excess or shortage of expenses incurred. The net effect of these excesses and shortages over time are presented in Cumulative Results of Operations.

N. Retirement Plan

In fiscal year 1997, approximately 47% of NSF employees participated in the Civil Service Retirement System (CSRS), to which NSF made matching contributions equal to 7 percent of pay. On January 1, 1987, the Federal Employees Retirement System (FERS) went into effect pursuant to the Federal Employees' Retirement System Act of 1986 (5 U.S.C. 8401-79). Most employees hired after December 31, 1983 are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984 can elect to either join FERS and Social Security or remain in CSRS. A primary feature of FERS is that it offers a savings plan to which NSF automatically contributes 1 percent of pay and matches employee contributions up to an additional 4 percent of pay. NSF also contributes the employer's matching share for Social Security for FERS participants.

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 and FERS. In 1997, NSF paid for the agency's contributions to CSRS and FERS of $2,717,678 and 4,106,811.

Beginning in fiscal year 1997, SFFAS No.5 requires employing agencies to recognize the cost of pensions and other retirement benefits during their employees' active years of service. 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 the agency for current period expense reporting. Information was also provided by OPM regarding the full cost of health and life insurance benefits. In fiscal year 1997, NSF recognized an additional $3,830,781 of pension expenses, $2,517,307 of post-retirement health benefits expenses and $ 12,147 of post-retirement life insurance expenses related to life insurance, beyond amounts actually paid. NSF recognized an offsetting revenue of $6,360,235 as imputed financing sources for the extent of these expenses that will be paid by OPM.

O. Contingencies

NSF has claims and lawsuits pending against it. In the opinion of management and legal counsel, none of these will materially affect the financial position or operations of the Foundation. When claims are expected to result in material payment whether from the Foundation'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, NSF discloses and recognizes them in the financial statements.

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

NSF engages organizations in cooperative agreements to manage, operate, and maintain research facilities for the benefit of the scientific community. Under the terms of four of these agreements, NSF has included clauses that, in the event of termination or non-renewal of the cooperative agreement, provide for NSF to pay accrued annual leave and/or certain post retirement benefit liabilities incurred by the awardee, subject to the availability of appropriated funds from which NSF may legally use for such purposes.

Upon termination or non-renewal of an agreement, NSF, at the sole discretion of its Director, has offered to use its best efforts to obtain these additional funds, including efforts to obtain such funds from Congress. However, nothing in the cooperative agreements can be construed as implying that the Congress will appropriate funds sufficient to meet the terms of these provisions.

As of September 30, 1997, the awardees reported in their financial statements approximately $31,540,500 in unfunded accrued annual leave and post-retirement benefits. One organization (Cornell) did not provide information on this item in their audited financial statements. The Cornell amount is not material to the NSF financial statements. There is inconsistency in the treatment of these amounts on the audited financial statements of the awardees. Two of the awardees have recorded accounts receivable totaling $12,090,000 on their audited financial statements.

The following awardees reported unfunded annual leave and post-retirement benefits on their financial statements:

Awardee		FY 1997 Awardee Financial Statement Information
Associated Universities, Inc. (AUI)		
	Vacation	$ 1,984,700
	Retirement	14,964,800
	Total AUI	16,949,500
Association of Universities for Research in Astronomy (AURA)		
	Vacation	2,653,000
	Retirement	2,501,000
	Total AURA	5,154,000
University Corporation of Atmospheric Research (UCAR)		
	Vacation	2,282,000
	Retirement	7,155,000
	Total UCAR	9,437,000
Cornell		-
Total		$ 31,540,500

Note 2. Fund Balances with Treasury

Fund balance with Treasury consisted of the following components as of September 30, 1997:

(Amounts in Thousands)

	Appropriated Fund	Trust Fund	Other Funds	Total
Obligated	$ 3,606,405	$ 17,427	$ -	$ 3,623,832
Unobligated Available	8,567	13,827	872	23,266
Unobligated Unavailable	53,366	-	567	53,933
Total Fund Balance	$ 3,668,338	$ 31,254	$ 1,439	$ 3,701,031

"Other Funds" consists of nonexpenditure transfer authorizations, deposits, holdings, and miscellaneous receipt accounts. The nonexpenditure transfer authorizations are appropriation allocations from other government agencies and include 31,523,005 Indian rupees converted at September 30, 1997 to U.S. Dollars at the prevailing Treasury rate of 36.13 rupees to US$1. Unavailable balances include recovered expired appropriations, other amounts related to expired authority and holdings which are unavailable for NSF use.

Note 3. Accounts Receivable

The Intragovernmental Accounts Receivable consists of reimbursements and repayments due from other government agencies. The repayments represent amounts due for salaries and other expenses incurred by NSF employees on behalf of those agencies. As of September 30, 1997, NSF recorded $889,047 in Intragovernmental Accounts Receivable.

As of September 30, 1997, NSF recorded $436,021 in Governmental Accounts Receivable. This account represents amounts due from public sources net of allowances. For fiscal year 1997, NSF has recorded an allowance of $113,000 for Governmental Accounts Receivable that are anticipated to be uncollectible.

Note 4. Advances

As of September 30, 1997 and 1996, Advances consisted of the following components:

(Amounts in Thousands)

Advances to Grantees	$	39,245
Advances to Contractors		2,103
Advances to Employees		4
Total Advances	$	41,352

Note 5. Property, Plant and Equipment

NSF PP&E consists of equipment, buildings, other structures and facilities, and construction in progress for which NSF is operationally responsible and retains title. This PP&E is maintained and operated by Antarctic Support Associates (ASA), an NSF contractor, and the Department of Defense (DoD) for the United States Antarctic

Program (USAP) and by the Foundation for agency operations. Structures and Facilities consist of research and development structures and site improvements.

The components of Property, Plant and Equipment as of September 30, 1997 were:

(Amounts in Thousands)

	Acquisition Cost	Accumulated Depreciation	Net Book Value
Buildings	$ 29,072	$ 10,348	$ 18,724
Other Structures and Facilities	34,064	7,595	26,469
Construction in Progress	1,755	-	1,755
Grantee and Contractor Equipment	122,486	92,840	29,646
Furniture and Equipment	9,518	8,386	1,132
Assets Under Lease	109	-	109
Total Plant, Property and Equipment	$ 197,004	$ 119,169	$ 77,835

In FY 1997, NSF began reporting depreciation of capitalized PP&E. USAP and in house PP&E is depreciated over the economic life of the asset using the straight-line method. However, non-aircraft USAP PP&E maintained by DoD totaling $2,142,920 was not depreciated, as acquisition dates are not available.

Note 6. Advances from Others

Advances from Others consisted of the following components as of September 30, 1997:

(Amounts in Thousands)

Reimbursable Agreements	$ 75,080
Nonexpenditure Transfer Authorization	-
Total Advances from Others	$ 75,080

To comply with new requirements issued by the Department of Treasury, in FY 1997, NSF no longer records funds transferred from other government agencies, other than

reimbursable agreements, in "Advances From Others." The balances which were formerly in Advances From Others were also moved to "Unexpended Appropriations."

Note 7. Other Governmental Liabilities

Other Governmental Liabilities represents accrued payroll and benefits and various employee related liabilities for payroll and benefit deductions. As of September 30, 1997, Other Governmental Liabilities consisted of:

(Amounts in Thousands)

Accrued Payroll and Benefits	$	4,246
State and Other Income Taxes Withheld		230
Employee Deductions for U.S. Savings Bonds		8
Total Other Governmental Liabilities	$	4,484

Note 8. Lease Liabilities

On July 1, 1996 NSF acquired four copiers under a Lease to Ownership Plan for a three year period. Future payments due under this lease for fiscal year 1997 are

(Amounts in Thousands)

Future Lease Payments:			
	Year 1		42
	Year 2		31
	Year 3		-
Future Lease Payments			73
Less: Imputed Interest			(6)
Total Capital Lease Liability		$	67

Note 9. Accrued Workers' Compensation Benefit

Accrued Workers' Compensation Benefit consisted of the following components as of September 30, 1997:

(Amounts in Thousands)

Estimated Actuarial Liability		805
Unreimbursed Actual Costs		256
Total Workers' Compensation Benefits	$	1,061

These amounts represented the estimated actuarial liability for future workers' compensation benefit of $805,000, and the unreimbursed actual cost of $255,552 and for total benefits and other payments made from employees compensation funds during expense periods July 1, 1996 through June 30, 1997 and July 1, 1995 through June 30, 1996 respectively. Of the $255,552, $140,341 will be paid 30 days after FY 98 funds are available, and $115,211 will be paid 30 days after FY 99 funds are available.

Note 10. Net Position

Net Position consisted of the following components at September 30, 1997:

(Amounts in Thousands)

	Appropriated & Other Funds	Trust Fund	Totals
Unexpended Appropriations			
Unobligated:			
Available	$ 9,303	$ -	$ 9,303
Unavailable	53,933	-	53,933
Undelivered Orders	3,432,213	-	3,432,213
Total Unexpended Appropriations	3,495,449	-	3,495,449
Invested Capital	77,835	-	77,835
Cumulative Results of Operations	-	42,826	42,826
Future Funding Requirements	(11,064)	-	(11,064)
	$ 3,562,220	$ 42,826	$ 3,605,046

Note 11 . Operating /Program Expenses

Operating/Program Expenses by object classification consisted of the following amounts for the year ended September 30, 1997:

(Amounts in Thousands)

Grants, Subsidies and Contributions		2,813,254
Personnel Services and Benefits		101,512
Contractual Services		255,644
Rental, Communication and Utilities		18,710
Travel and Transportation		9,574
Supplies and Materials		3,321
Printing and Reproduction		1,609
Equipment not Capitalized		8,118
Total Expenses	$	3,211,742

Note 12. Prior Period Adjustments

The prior period adjustment presented on the FY 97 Statement of Operations reflects the correction of errors identified in the USAP and in house PP&E balances reported in FY 1996, and accumulated depreciation. The cumulative effect of these items resulted in following:

(Amounts in Thousands)

Accumulated Depreciation	$	(111,300)
Errors		27,181
Total	$	(84,119)

Note 13. Cumulative Effect of Change in Accounting Principles

NSF made several changes in their accounting for and reporting of PP&E that resulted in a $763,292,326 decrease in NSF PP&E balances. The net PP&E adjustment consists of the following:

- *FASAB Interim Guidance.* As a result of FASAB's interim guidance for reporting PP&E held by others, NSF removed $748,116,464 of assets in reported FY 1996 from the FY 1997 Statement of Financial Position. This guidance is explained in detail in Note 1, H.

- *Change in the NSF Capitalization Threshold*. In FY 1996, NSF capitalized assets with values of $5,000 or more and useful lives in excess of 2 years. During FY 1997, NSF increased the PP&E capitalization threshold to $25,000. This change resulted in a reduction of the FY 1996 USAP and in house asset balances by $15,175,912.

Note 14. Non-Operating Changes

Non-operating changes consisted of the following amounts for the year ended September 30, 1997:

(Amounts in Thousands)

Increases:		
New Appropriations	$	3,270,000
Total Increases		3,270,000
Decreases:		
Appropriated Capital Used		(3,065,055)
Funds Returned to Treasury		(15,895)
Other Decreases Due to Adjustments		(25,193)
Total Decreases		(3,106,143)
Total Non-Operating Changes	$	163,857

SUPPLEMENTAL FINANCIAL and MANAGEMENT INFORMATION

National Science Foundation
Balance Sheet
As of September 30, 1997
(Amounts in Thousands)
Unaudited

ASSETS	
Entity Assets:	
Intragovernmental	
Fund Balance With Treasury	$ 3,669,777
Accounts Receivable, Net	889
Governmental	
Fund Balance With Treasury	31,254
Accounts Receivable, Net	436
Other Assets	41,352
Cash and Other Monetary Assets	15,265
General Property, Plant and Equipment, Net	77,835
Total Assets	$ 3,836,808
LIABILITIES	
Liabilities Covered by Budgetary Resources:	
Intragovernmental Liabilities:	
Advances From Others	$ 75,080
Other Intragovernmental Liabilities	496
Governmental Liabilities:	
Accounts Payable	140,638
Other Governmental Liabilities	4,484
Total Liabilities Covered by Budgetary Resources	220,698
Liabilities Not Covered by Budgetary Resources:	
Governmental Liabilities:	
Lease Liabilities	67
Other Governmental Liabilities	10,997
Total Liabilities Not covered by Budgetary Resources	11,064
Total Liabilities	231,762
NET POSITION	
Unexpended Appropriations	3,562,220
Cumulative Results of Operations	42,826
Total Net Position	3,605,046
Total Liabilities and Net Position	$ 3,836,808

National Science Foundation
Statement of Net Costs
For The Year Ended September 30, 1997
Unaudited
(Amounts in Thousands)

Program Costs	
Research and Education Programs	
Intragovernmental	$ 88,132
With the Public	3,131,479
Less: Earned Revenues	
Intragovernmental	(125,666)
Net Program Costs	3,093,945
Net Cost of Operations	$ 3,093,945

National Science Foundation
Statement of Changes in Net Position
For The Year Ended September 30, 1997
Unaudited
(Amounts in Thousands)

Net Costs of Operations	$ 3,093,945
Financing Sources:	
Appropriations Used	3,065,055
Donations	36,859
Interest and Penalties	973
Imputed Financing	6,360
Transfers-Out	(540)
Total Financing Sources	3,108,707
Net Results of Operations	14,762
Prior Period Adjustments	(84,119)
Cumulative Effect of Change in Accounting Principles	(763,292)
Net Change in Cumulative Results of Operations	(832,649)
Increase (Decrease) in Unexpended Appropriations	163,857
Change in Net Position	(668,792)
Net Position-Beginning of Period	4,273,838
Net Position-End of Period	$ 3,605,046

National Science Foundation
Statement of Budgetary Resources
For The Year Ended September 30, 1997
Unaudited
(Amounts in Thousands)

Budgetary Resources	
Budget Authority	$ 3,308,593
Unobligated Balances - Beginning of Period	90,767
Spending Authority from Offsetting Collections	83,879
Adjustments	12,396
Total Budgetary Resources	$ 3,495,635
Status of Budgetary Resources:	
Obligations Incurred	$ 3,419,480
Unobligated Balances - End of Period	22,782
Unobligated Balances - Not Available	53,373
Total, Status of Budgetary Resources	$ 3,495,635
Outlays	
Obligations Incurred	$ 3,419,480
Less: Spending Authority from offsetting Collections and Adjustments	112,170
Obligated Balance, Net - Beginning of Period	3,449,447
Less: Obligated Balance, Net - End of Period	3,594,427
Total, Outlays	$ 3,162,330

National Science Foundation
Statement of Financing
For the Period Ended September 30, 1996
Unaudited
(Amounts in Thousands)

Obligations and Nonbudgetary Resources	
Obligations Incurred	$ 3,419,480
Less: Spending Authority for Offsetting Collections and Adjustments	(112,170)
Financing Imputed for Cost Subsidies	6,360
Exchange Revenue not in the Budget	(2)
Other	1,220
Total Obligations and Nonbudgetary Resources	3,314,888
Resources That Do Not Fund Net Cost of Operations	
Changes in Amount of Goods, Services, and Benefits Ordered but not yet Received or Provided	(269,871)
Cost Capitalized on the Balance Sheet	(852,421)
Financing Sources that fund Costs of Prior Periods	118
Other	45,919
Total Resources That Do Not Fund Net Cost of Operations	(1,076,255)
Costs That Do Not Require Resources	
Depreciation and Amortization	7,869
Revaluation of Assets and Liabilities	847,411
Other	32
Total Costs that Do Not require Resources	855,312
Net Costs of Operations	$ 3,093,945

National Science Foundation
Research and Human Capital
Annual Stewardship Information
For the Fiscal Year Ended September 30, 1997
Unaudited
(Dollars in Thousands)

	1993	1994	1995	1996	1997
Research and Human Capital Activities					
Basic Research	$ 1,743,770	$ 1,870,669	$ 1,973,264	$ 2,002,895	$ 2,056,713
Applied Research	138,119	169,689	176,013	185,418	191,807
Facilities	130,436	171,866	289,581	187,192	203,826
Education and Training	407,610	458,520	511,204	501,636	519,308
Non-Investment Activities (Note)	329,791	316,470	320,212	329,184	327,154
Total Research and Human Capital Activities	$ 2,749,726	$ 2,987,214	$ 3,270,274	$ 3,206,325	$ 3,298,808

Outputs and/or Outcomes

Research and Human Capital Activities					
Dollar Distribution to Universities	1,882,129	2,054,619	2,267,798	2,177,060	2,255,700
Dollar Distribution to Industry	162,387	198,144	236,705	235,340	265,012
Dollar Distribution to Federal Agencies	148,610	104,852	88,481	97,599	89,647
Dollar Distribution to Others	556,600	629,599	677,290	696,326	688,449
Dollar of Scientist Support	275,943	303,567	325,436	317,410	330,778
Dollar of Postdoctoral Support	84,981	91,834	98,767	109,295	106,783
Dollar of Graduate Student Support	275,030	269,287	285,371	288,889	290,430
Number of awards	18,216	19,346	19,393	18,699	18,582
Number of Scientists Supported	23,038	24,315	25,259	24,386	23,885
Number of Years of Scientist support	5,701	5,381	5,456	5,192	5,409
Number of Postdoctorals Supported	4,281	4,258	4,134	4,490	4,817
Number of Graduate Students Supported	19,558	21,639	20,071	20,280	19,355

Note: "Non-Investment Activities" includes NSF's Administrative and Management costs, a portion of awardee administrative costs, and some Polar Program costs.

Source:

Justification of Estimates of Appropriations to the Congress.

National Science Foundation
Research and Human Capital
Annual Stewardship Information
For the Fiscal Year Ended September 30, 1997
Unaudited
(Dollars in Thousands)

Organization Summary	Real Property	Construction in Progress	Capitalized Equipment (>= $25,000)	Total
Total	**249,054**	**220,171**	**220,796**	**690,021**
Associated Universities Inc.(Brookhaven)	0	0	639	639
AUI-NRAO	146,870	77,563	56,106	280,539
AURA-NOAO	65,150	8,773	17,974	91,897
California Institute of Technology	0	109,255	0	109,255
Columbia University	86	0	13,439	13,525
Cornell University End.	18,833	23,212	3,133	45,178
Duke University	0	0	3,561	3,561
Incorporated Research Institutions for Seismology	0	0	13,873	13,873
Indiana University	0	0	134	134
Joint Oceanographic Institutions, Inc.	0	0	4,409	4,409
Oregon State University	0	0	6,976	6,976
San Jose State University Foundation	0	0	3,730	3,730
SRI International	620	0	3,189	3,809
University Corporation for Atmospheric Research	17,495	1,368	71,501	90,364
University of Alaska, Fairbanks	0	0	1,843	1,843
University of California - San Diego	0	0	472	472
University of Hawaii - Manoa	0	0	477	477
University of Michigan	0	0	704	704
University of Nebraska, Lincoln	0	0	2,638	2,638
University of Rhode Island	0	0	6,159	6,159
University of Washington	0	0	863	863
William Rice University	0	0	176	176
Woods Hole Oceanographic Institution	0	0	8,800	8,800

These balances represent NSF's stewardship investments in property used to support scientific and engineering research. Although NSF retains title to this property, awardees are responsible for the control and operation of these items. These numbers have been provided by Awardees and have not been subject to independent audit.

INSPECTOR GENERAL'S REPORT

NATIONAL SCIENCE FOUNDATION
4201 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22230

OFFICE OF
INSPECTOR GENERAL

FEB 26 1998

Memorandum for: Richard N. Zare
Chairman, National Science Foundation

Neal Lane
Director, National Science Foundation

From: Linda Sundro
Inspector General

Subject: Transmittal of Auditors' Reports on NSF's Fiscal Year 1997 Financial Statements

Attached are the Independent Auditors' Reports on the Foundation's financial statements for the fiscal year ending September 30, 1997. As you know, this is the second year that the Foundation's Chief Financial Officer (CFO) was required to prepare financial statements for all the agency's accounts and my office was required to conduct an audit of these statements in accordance with the CFO and Government Management Reform Acts.

Attached are the three reports we are required to prepare: (1) the Report on the Financial Statements, (2) the Report on Internal Control Over Financial Reporting, and (3) the Report on Compliance with Laws and Regulations. In our 1997 Report on Financial Statements, we qualified our opinion on NSF's financial statements, because we were not able to plan and perform audit procedures and determine if NSF's property, plant, and equipment (PP&E) balance, as of September 30, 1997, was fairly presented.

On December 5, 1997, NSF received interim guidance from the Financial Accounting Standards Advisory Board and the Office of Management and Budget that only PP&E used in the U.S. Antarctic Program (USAP) and used within NSF headquarters should be reported in NSF's Statement of Financial Position.

In December 1997, we were able to survey the contractor's site in Colorado, where the majority of the records for the USAP PP&E are held, in order to estimate the cost to perform a complete audit of the USAP PP&E.

However, we were unable to return to Colorado and travel to New Zealand and the Antarctic to perform the complete audit in time to affect our opinion on the FY 1997 financial statements. We plan to perform the audit of the USAP PP&E in 1998 and are committed to work with NSF management in an effort to arrive at unqualified "clean" opinions on future financial statements.

We made four recommendations in our Report on Internal Control Over Financial Reporting. These recommendations are classified as "reportable conditions" because, in our opinion, they are significant deficiencies in the design or operation of the internal controls that, in our judgment, could adversely affect NSF's ability to ensure that the objectives of the internal controls are being achieved. First, we recommend that NSF prepare formal written procedures for accumulating and recording the accounts payable balance at year-end. Second, NSF should continue to refine its performance measures by linking them to NSF's desired outcome goals. Third, NSF should devise and implement a mechanism for identifying the existence of all liabilities arising from grant and contract provisions. Finally, the agency should review and evaluate liability termination clauses that provide for accrued employee benefits in some of its larger awards. NSF should also clarify to each awardee, the costs included in its definition of accrued employee benefits and provide specific and consistent guidance to the awardee, regarding the treatment of these benefits on the awardee's financial statements.

We wish to acknowledge NSF's Chief Operating Officer, CFO, Deputy CFO, and their staff for the cooperation we received during this audit.

Attachment

INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENTS

KPMG Peat Marwick LLP
2001 M Street, N.W.
Washington, DC 20036

NATIONAL SCIENCE FOUNDATION

OFFICE OF
INSPECTOR GENERAL

Independent Auditors' Report on Financial Statements

Dr. Richard N. Zare
Chairman, National Science Board:

Dr. Neal Lane
Director, National Science Foundation:

We have audited the accompanying statement of financial position of the National Science Foundation (NSF) as of September 30, 1997 and the related statement of operations and changes in net position for the year then ended. These financial statements are the responsibility of NSF's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as described in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards; 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. 93-06, *Audit Requirements for Federal Financial Statements,* as amended. Those standards require that we plan and perform the audit 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

We were unable to plan and perform audit procedures to satisfy ourselves regarding the fairness of presentation of NSF's recorded balance of property, plant, and equipment, net (PP&E) of $76,594,000 (of the total PP&E balance of $77,835,000) at September 30, 1997 of the U.S. Antarctic Program (USAP), which is located in Antarctica and under the custodial care of NSF's contractor, as well as the related balance of depreciation expense for the year then ended.

As described in Note 1, these financial statements were prepared in conformity with the hierarchy of accounting principles and standards recommended by the Federal Accounting Standards Advisory Board (FASAB). This hierarchy is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, except for the effects on the 1997 financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to apply adequate procedures to test NSF's USAP PP&E balance at September 30, 1997, as discussed in the second

paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the National Science Foundation as of September 30, 1997, and the results of its operations and changes in net position for the year then ended, in conformity with the basis of accounting described in Note 1.

As discussed in Note 1-N to the financial statements, NSF implemented Statement of Federal Financial Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government*, effective October 1, 1996. Also, as discussed in Note 1-H to the financial statements, NSF changed its method of accounting for PP&E effective October 1, 1996, based on agency-specific guidance received from FASAB.

Our audit was conducted for the purpose of forming an opinion on NSF's financial statements, taken as a whole. The information in the *Overview* section is not a required part of the financial statements but is supplementary information required by OMB Bulletin Nos. 94-01 and 97-01, *Form and Content of Agency Financial Statements*. We have considered whether this information is materially inconsistent with the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we express no opinion on it. The performance information included in the *Overview* is addressed in our auditors' report on internal control in accordance with OMB Bulletin No. 93-06, as amended.

The information included in the *Supplemental Financial and Management Information* section is presented for purposes of additional analysis and is not a required part of the financial statements. It has not been subjected to the auditing procedures applied in the audit of NSF's principal financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued reports dated January 30, 1998 on our consideration of NSF's internal controls and on its compliance with laws and regulations.

This report is intended for the information of the National Science Board, the NSF Office of Inspector General, and NSF's management. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

January 30, 1998

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

KPMG Peat Marwick LLP
2001 M Street, N.W.
Washington, DC 20036

NATIONAL SCIENCE FOUNDATION

OFFICE OF
INSPECTOR GENERAL

Independent Auditors' Report on Internal Control over Financial Reporting

Dr. Richard N. Zare
Chairman, National Science Board:

Dr. Neal Lane
Director, National Science Foundation:

We have audited the financial statements of the National Science Foundation (NSF) as of and for the year ended September 30, 1997, and have issued our report thereon dated January 30, 1998, which was qualified because of our inability to audit NSF's U.S. Antarctic Program property, plant, and equipment balance. In addition, our report referred to NSF's changes in accounting principles for liabilities and property, plant, and equipment.

Except as discussed in the third paragraph of our Independent Auditors' Report on Financial Statements, we conducted our audit in accordance with generally accepted auditing standards; 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. 93-06, *Audit Requirements for Federal Financial Statements,* as amended.

The management of NSF is responsible for establishing and maintaining internal controls. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of internal controls are to provide management with reasonable, but not absolute, assurance that:

- transactions, including those relating to obligations and costs, are executed in compliance with applicable laws and regulations that could have a direct and material effect on the financial statements, and any other laws and regulations that OMB, NSF's Office of Inspector General, or NSF's management have identified as being significant and for which compliance can be objectively measured and evaluated;

- funds, property, and other assets are safeguarded against loss from unauthorized use or disposition;

- transactions are executed in accordance with management's authorization and are properly recorded and accounted for to permit the preparation of reliable financial reports in conformity with applicable accounting principles described in Note 1 to the financial statements, and to maintain accountability over the assets; and

- data that support reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.

Because of inherent limitations in internal controls, fraud may nevertheless occur and not be detected. Also, projection of any evaluation of internal controls to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit, we considered NSF's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements, and not to provide an opinion on the internal control over financial reporting. Accordingly, we do not express such an opinion. With respect to internal controls, we obtained an understanding of the design of relevant policies and procedures, determined if they had been placed in operation, assessed control risk, and performed tests of internal controls.

Our evaluation of the controls for performance information was limited to those controls designed to ensure the existence and completeness of the information. With respect to the performance measures control objective, we obtained an understanding of relevant internal control policies and procedures designed to permit the preparation of reliable and complete performance information, and we assessed control risk.

We noted certain matters involving internal controls and their operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and OMB Bulletin No. 93-06, as amended. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal controls that, in our judgment, could adversely affect NSF's ability to ensure that the objectives of the internal controls, as previously defined, are being achieved. The conditions that we consider to be reportable conditions are described in Exhibit I of this report.

A material weakness is a condition 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, or material to a performance measure or aggregation of related performance measures, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal controls would not necessarily disclose all internal control matters that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered material weaknesses as defined above. However, we believe that none of the reportable conditions described in Exhibit I are material weaknesses.

These conditions were considered in determining the nature, timing, and extent of procedures to be performed in our audit of NSF's financial statements as of September 30, 1997.

Due to time constraints, management's responses have not been included herein, but will be available under separate cover.

We also noted other matters involving internal controls and their operation that we have reported to the management of NSF in a separate letter dated January 30, 1998.

This report is intended for the information of the National Science Board, NSF's Office of Inspector General and NSF's management. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

January 30, 1998

Exhibit I

Reportable Conditions

Determining Liabilities

Liabilities Arising from Grant and Contract Provisions

NSF has not developed formal procedures for identifying liabilities arising from grant and contract provisions for the purpose of determining the need for either an accrual of a liability or a footnote disclosure in the financial statements. The need to identify liabilities is required by Statement of Federal Financial Accounting Standards (SFFAS) No. 5, *Accounting for Liabilities of the Federal Government*. A variation of this condition was also noted in fiscal year 1996.

During the audit, NSF's initial procedures did not include steps to obtain information about liability matters arising from grant and contract provisions for which NSF's Office of General Counsel is not substantially involved.

Recommendation

We recommend that NSF devise and implement a mechanism (i.e., a systematic process and formal procedures) for identifying the existence of all liabilities arising from grant and contract provisions. These procedures should initially include analyzing all NSF grants and contracts for provisions which may cause NSF liability.

Accounts Payable

As reported in the statement of financial position as of September 30, 1997, NSF recorded a liability for its accounts payable of approximately $31 million.

As a result of our audit testwork, we determined that the accounts payable balance was understated by approximately $14 million (prior to recording our recommended audit adjustment). Also, the accounts payable balance included items which did not relate to fiscal year 1997 of approximately $4 million (prior to adjustment by NSF). These errors suggest that procedures should be in writing; the procedures should include technician research to determine the period of service if not stated on the invoice; the technicians performing the analyses should be trained; and a secondary or supervisory review of all payables should be performed.

Recommendation

We recommend that NSF prepare formal written procedures (and revise as necessary) for accumulating and recording the accounts payable balance at year-end. These procedures should include instructions on identifying the period of service if no information is provided on the invoice, as well as secondary or supervisory review procedures. Also, NSF should ensure that the technicians performing these procedures receive adequate training so that the procedures are properly understood and implemented.

We are aware that NSF is developing accounts payable procedures and has plans for implementing an accounts payable subsidiary module in its current accounting system. This will assist in identifying processed items which are payable at any point during the fiscal year. However, sufficient control procedures must still be in place to ensure that the year end accounts payable balance is fairly stated.

Linking NSF Goals to Performance Measures

OMB Bulletin 97-01, *Form and Content of Agency Financial Statements,* requires that agencies include information on their mission and organizational structure, performance goals and results, and limitations on the financial statements in their *Overview* sections.

In its fiscal year 1997 Chief Financial Officer's Annual Report - *Overview* section, NSF discusses its mission, strategic plan and goals, as well as its four primary program areas. NSF presents accomplishments and statistical data, charts and graphs. However, there is little, if any, linkage between NSF's desired outcome goals and the performance information. This condition was also noted in fiscal year 1996.

We recognize that in September 1997, in compliance with the Government Performance and Results Act (GPRA), NSF developed a new strategic plan that provides five desired outcome goals, the key investment strategies that NSF will use to work toward meeting these goals, and NSF's action plan for fiscal year 1997 to fiscal year 2003, which will provide a link between the outcome goals and the development of budgets and performance plans. It also describes four critical factors that are essential for NSF to excel in managing its processes.

Recommendation

We recommend that NSF continue to refine its performance information data in the *Overview* so that it is linked to the desired outcome goals of NSF and provides a clear indication of performance against those goals.

Providing Guidance to Awardees

NSF has relationships with a number of grantees that operate large research facilities. The provisions of some of these awards provide that NSF pay certain accrued employee benefit costs incurred by the awardee, upon termination or non-renewal of the award. As a result of our audit procedures, we noted that there appears to be ambiguity among NSF and these awardees regarding NSF's liability for these accrued employee benefit costs. Some of these provisions are vague regarding the components of these accrued employee benefit costs. Also, we noted that the accounting treatment among the awardees for these costs is inconsistent.

Recommendation

We recommend that NSF review and evaluate the appropriate grant and contract provisions and clarify to each of the awardees NSF's specific understanding of the types of costs referred to as accrued employee benefits. Also, we recommend that NSF provide specific and consistent guidance to the awardees regarding the treatment of accrued employee benefit costs on the books and records of the awardee.

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

KPMG Peat Marwick LLP
2001 M Street, N.W.
Washington, DC 20036

NATIONAL SCIENCE FOUNDATION

OFFICE OF INSPECTOR GENERAL

Independent Auditors' Report on Compliance with Laws and Regulations

Dr. Richard N. Zare
Chairman, National Science Board:

Dr. Neal Lane
Director, National Science Foundation:

We have audited the financial statements of the National Science Foundation (NSF) as of and for the year ended September 30, 1997, and have issued our report thereon dated January 30, 1998, which was qualified because of our inability to audit NSF's U.S. Antarctic Program property, plant, and equipment balance. In addition, our report referred to NSF's changes in accounting principles for liabilities and property, plant, and equipment.

Except as discussed in the third paragraph of our Independent Auditors' Report on Financial Statements, we conducted our audit in accordance with generally accepted auditing standards; 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. 93-06, *Audit Requirements for Federal Financial Statements,* as amended.

The management of NSF is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether NSF's financial statements are free of material misstatement, we performed tests of NSF's compliance with (1) certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and (2) certain other laws and regulations specified in OMB Bulletin No. 93-06, as amended, including the requirements referred to in the Federal Financial Management Improvement Act of 1996. However, providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit. Accordingly, we do not express such an opinion.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 93-06, as amended.

Federal Financial Management Improvement Act (FFMIA)

With respect to FFMIA compliance, OMB Bulletin No. 93-06, as amended, requires the agency's independent auditors to report whether the agency's financial management systems substantially comply with (1) the Federal financial management systems requirements, (2) applicable

accounting standards, and (3) the United States Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance using the implementation guidance for FFMIA issued by OMB on September 9, 1997.

Our audit of NSF's financial statements was designed to be conducted in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin 93-06, as amended. Our audit was not designed to detect whether NSF's systems are Year 2000 compliant. Further, we have no responsibility with regard to NSF's efforts to make its systems, or any other systems, such as those of NSF's vendors, service providers, or other third parties, Year 2000 compliant or provide assurance on whether NSF has addressed or will be able to address all of the affected systems on a timely basis. These are responsibilities of NSF's management.

The results of our tests disclosed no instances where NSF's financial management systems did not substantially comply with the three requirements discussed in the second preceding paragraph.

* * * * *

We noted other immaterial instances of noncompliance that we have reported to the management of NSF in a separate letter dated January 30, 1998.

This report is intended for the information of the National Science Board, NSF's Office of Inspector General and NSF's management. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

January 30, 1998

NATIONAL SCIENCE FOUNDATION
ARLINGTON, VA 22230

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