

The audit was conducted in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards issued by the Comptroller General of the United States. The results of the audit were discussed with Commission officials and the OIG throughout the audit. The auditors' reported that the recommendation made during FY 2005 has yet to be satisfied as their sample testing showed that 50% of the grant progress reports were not submitted timely. This prior year finding and recommendation on compliance will remain open, pending full implementation of the corrective action plan.

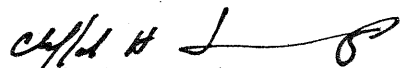
M.D. Oppenheim & Company, P.C., also identified two additional matters presenting opportunities for strengthening internal controls and operating efficiency. They are communicated in a separate letter dated November 6, 2006 for management's consideration and is attached under separate cover.

M.D. Oppenheim & Company, P.C is responsible for the attached auditors' report dated November 6, 2006 and the conclusions expressed in the report. We do not express opinions on the Appalachian Regional Commission's financial statements or internal controls.

In connection with the contract, we reviewed M.D. Oppenheim & Company's report and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with U.S. generally accepted auditing standards, was not intended to enable us to express, and we do not express, opinions on the Appalachian Regional Commission's financial statements or internal control. M.D. Oppenheim & Company, P.C is responsible for the attached auditors' report dated November 6, 2006 and the conclusions expressed in the report. However, our review disclosed no instances where M.D. Oppenheim & Company, P.C did not comply, in all material respects, with auditing standards generally accepted in the United States of America and Government Auditing Standards issued by the Comptroller General of the United States.

As noted in the letter, the consideration of internal controls was for the limited purpose of auditing the financial statements. My office is currently performing a more comprehensive audit of the internal controls.

I appreciate the cooperation given by the Finance and Administration Division to my office and M.D. Oppenheim & Company, P.C., during the audit.



Clifford H. Jennings
Inspector General

Attachments

cc: Director, Finance and Administration Division

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M.D. OPPENHEIM & COMPANY, P.C.

CERTIFIED PUBLIC ACCOUNTANTS

8403 Colesville Road, Suite 340 Silver Spring, Maryland 20910-3367
(301) 585-7990 FAX (301) 585-7975 www.mdcpa.com

November 6, 2006

Mr. Cliff Jennings
Inspector General
Appalachian Regional Commission
1666 Connecticut Ave.
Suite 215
Washington, DC 20009

Dear Mr. Jennings:

We have been asked to furnish the following information to you because our firm has been engaged to perform the audit of the financial statements of the Appalachian Regional Commission as of and for the year ended September 30, 2006:

Independence

We are familiar with the independence requirements in the U.S. Government Accountability Office (GAO) *Government Auditing Standards*, the American Institute of Certified Public Accountants professional standards, the applicable state boards of accountancy regulations, and the applicable state societies of CPAs regulations.

As far as the Appalachian Regional Commission is concerned, our firm and the individuals that have worked on the above engagement(s) have been, for the period covered by the financial statements under report and thereafter to date, independent as contemplated in the GAO *Government Auditing Standards*, American Institute of Certified Public Accountants professional standards, the applicable state boards of accountancy regulations, and the applicable state societies of CPAs regulations.

We have not provided any nonaudit services to the above-mentioned organizations.

Peer Review Report

We have attached a copy of our external peer review report in accordance with the GAO *Government Auditing Standards* and the American Institute of Certified Public Accountants professional standards.

Continuing Professional Education

The professional staff that have worked on the above engagements meet the continuing professional education requirements prescribed in the GAO *Government Auditing Standards* and the American Institute of Certified Public Accountants professional standards, the applicable state boards of accountancy regulations, and the applicable state societies of CPAs regulations.

Nancy E. Davis
Name

Partner
Title

Nancy E. Davis
Signature



Affiliated Offices Worldwide



Lilling & Company LLP

Certified Public Accountants

October 7, 2004

To the Owners
M. D. Oppenheim & Company, P.C.

We have reviewed the system of quality control for the accounting and auditing practice of M. D. Oppenheim & Company, P.C. (the firm) in effect for the year ended June 30, 2004. A system of quality control encompasses the firm's organizational structure and the policies adopted and procedures established to provide it with reasonable assurance of conforming with professional standards. The elements of quality control are described in the Statements on Quality Control Standards issued by the American Institute of Certified Public Accountants (AICPA). The design of the system and compliance with it are the responsibility of the firm. Our responsibility is to express an opinion on the design of the system, and the firm's compliance with the system based on our review.

Our review was conducted in accordance with standards established by the Peer Review Board of the AICPA. In performing our review, we obtained an understanding of the system of quality control for the firm's accounting and auditing practice. In addition, we tested compliance with the firm's quality control policies and procedures to the extent we considered appropriate. These tests covered the application of the firm's policies and procedures on selected engagements. Because our review was based on selective tests, it would not necessarily disclose all weaknesses in the system of quality control or all instances of lack of compliance with it.

Because there are inherent limitations in the effectiveness of any system of quality control, departures from the system may occur and not be detected. Also, projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the system of quality control for the accounting and auditing practice of M. D. Oppenheim & Company, P.C. in effect for the year ended June 30, 2004, has been designed to meet the requirements of the quality control standards for an accounting and auditing practice established by the AICPA and was complied with during the year then ended to provide the firm with reasonable assurance of conforming with professional standards.



LILLING & COMPANY LLP

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Appalachian Regional Commission

Financial Statements and
Independent Auditors' Report

September 30, 2006 and 2005

APPALACHIAN REGIONAL COMMISSION

September 30, 2006 and 2005

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To the Commission Members
Appalachian Regional Commission
Washington, DC

Independent Auditors' Report

We have audited the accompanying balance sheets of the Appalachian Regional Commission ("ARC") as of September 30, 2006 and 2005, and the related statements of operations and changes in net position and cash flows for the years then ended. These financial statements are the responsibility of ARC's management. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Appalachian Regional Commission as of September 30, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental information on pages 14 and 15 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements, and accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 6, 2006 on our consideration of ARC's internal controls

The Commission Members
Appalachian Regional Commission
Washington, DC

over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of the audit.

Silver Spring, Maryland
November 6, 2006

APPALACHIAN REGIONAL COMMISSION
Balance Sheets
September 30, 2006 and 2005

		2006	2005
ASSETS			
Current assets			
Fund balance with U.S. Treasury	4100.20	\$ 60,655,435 ✓	\$ 61,537,066
Cash in commercial institutions	┆	95,898 ✓	71,117
Total cash		60,751,333	61,608,183
Accounts receivable	4200.10	4,219 ✓	-
Advances to grantees	4200.40	61,828 ✓	-
Total current assets		60,817,380	61,608,183
Business development revolving loan funds	4200.20	30,235,390 ✓	28,942,787
TOTAL ASSETS		\$ 91,052,770	\$ 90,550,970
LIABILITIES AND NET POSITION			
Current liabilities			
Accounts payable	5100.30	\$ 1,148,389 ✓	\$ 1,177,477
Center for Disease Control and Prevention grants	5200.30	398,078	750,000
Accrued pension liability	5200.50	1,934,715	1,683,124
Accrued leave	5200.20	370,046	386,370
Accrued payroll and taxes payable	✓ 5100.40	249,596	241,706
Other accrued liabilities (78,361.65 + 87,322.79)	5200.40	165,684	75,754
Total current liabilities	↑	4,266,508	4,314,431
Net position	6100.20	86,786,262	86,236,539
TOTAL LIABILITIES AND NET POSITION		\$ 91,052,770	\$ 90,550,970

See accompanying notes and Independent Auditors' Report.

APPALACHIAN REGIONAL COMMISSION
Statements of Operations and Changes in Net Position
Years Ended September 30, 2006 and 2005

	2006	2005
REVENUES		
Appropriations	7100.25 \$ 64,817,280 \$	65,472,000
Less: Grant transfers to other agencies	7100.30 (25,937,110)	(26,160,682)
Appropriations (net)	38,880,170	39,311,318
Appalachian Development Highway System administrative revenue	7100.15 616,558	1,064,200
State contributions	7100.40 3,293,000	3,164,000
Other revenue	7100.13 460,447	273,833
Total revenues	43,250,175	43,813,351
EXPENSES		
Area development grants	7500.11 33,038,339	32,170,267
Office of the Federal Co-Chair and Inspector General	1,776,601	1,724,265
Commission management and administration	7,885,512	7,501,639
Total expenses	42,700,452	41,396,171
NET INCOME	549,723	2,417,180
Net position, beginning of period	86,236,539	83,819,359
NET POSITION, END OF PERIOD	\$ 86,786,262 \$	86,236,539

See accompanying notes and Independent Auditors' Report.

APPALACHIAN REGIONAL COMMISSION
Statements of Cash Flows
Years Ended September 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Net income	\$ 549,723	\$ 2,417,180
Adjustments to reconcile income to net cash provided by operating activities:		
Depreciation	-	13,394
Changes in assets and liabilities:		
Accounts receivable	(4,219)	-
Advances to grantees	(61,828)	864,383
Business development revolving loan funds	(1,292,603)	(2,400,996)
Accounts payable	(29,088)	(771,943)
Center for Disease Control and Prevention grants	(351,922)	750,000
Accrued pension liability	251,591	697,557
Accrued leave	(16,324)	32,781
Accrued payroll and taxes payable	7,890	30,351
Other accrued liabilities	89,930	(16,715)
Net cash provided by operating activities	(856,850)	1,615,992
Net (decrease)/increase in cash	(856,850)	1,615,992
Cash at beginning of year	61,608,183	59,992,191
CASH AT END OF YEAR	\$ 60,751,333	\$ 61,608,183

Supplemental disclosures:

No amounts were paid for Interest and Taxes in 2006 or 2005.

See accompanying notes and Independent Auditors' Report.

APPALACHIAN REGIONAL COMMISSION

Notes to Financial Statements

Years Ended September 30, 2006 and 2005

Note A – Organization and Mission

The Appalachian Regional Commission (“ARC”) was established under the Appalachian Regional Development Act of 1965, as amended, the Appalachian Regional Development Reform Act of 1998 and the Appalachian Regional Development Act Amendments of 2002. ARC is a regional development agency designed to function as a Federal, state, and local partnership. ARC is not a Federal executive branch agency (as defined in Title 5 and 31 of the United States Code and by the Department of Justice).

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

ARC supports economic and social development in the Appalachian Region. The Appalachian Region is a 200,000 square mile region from the Appalachian Mountains in Southern New York to Northern Mississippi. The ARC programs affect approximately 410 counties located in thirteen states including all of West Virginia and parts of Alabama, Georgia, Kentucky, Maryland, Mississippi, New York, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, and Virginia.

Note B – Summary of Significant Accounting Policies

1. **Major Programs** – ARC is authorized to fund area and other development programs including education, workforce training, water and sewer construction, housing, leadership development, small business start-ups and expansions and development of health care resources. In executing its programs, local communities and Federal agencies provide administrative and technical services. ARC utilizes approximately 10 Federal departments and agencies to administer, disburse funds, and account for its infrastructure and other programs. ARC is responsible for allocating funds to the projects and for the management and administration of all projects.

2. **Basis of Accounting** – The accompanying financial statements have been prepared using the accrual method of accounting. Under the accrual method, revenues are recognized when earned and expenses are recognized when incurred. Appropriations are recognized as revenue when appropriated and available.

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note B – Summary of Significant Accounting Policies (continued)

3. **Financing Sources** – ARC receives annual no-year Federal appropriations to provide grants to the entities within the Appalachian Region and to fund its operations. The state members also contribute funds to ARC operations. Funds are allocated to thirteen states and are available until expended. States can generally decide how their allocations will be used for ARC programs.
4. **Fund Balance with U.S. Treasury** – Cash receipts and disbursements for operations and the area development programs are processed by the U.S. Department of Treasury. Funds held by the Department of Treasury represent funds available for operations.
5. **Cash in Commercial Institutions** – ARC uses commercial bank accounts to accommodate collections and payments that cannot be processed by the U.S. Department of Treasury.
6. **Advances to Grantees** – Unexpended grant funds in the hands of grantees at the end of the fiscal year are reclassified as advances.
7. **Equipment and Software** – Capital assets are stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets of three to five years. All assets are fully depreciated as of September 30, 2006. Depreciation expense for the years ended September 30, 2006 and 2005 is \$0 and \$13,394, respectively. *4600.20*
8. **Retirement Plans** – ARC Federal employees participate in Federal retirement plans. ARC non-Federal employees participate in the ARC Pension and 401(k) plan.
9. **Accrued Pension Liability** – ARC recognizes and records a liability for post-retirement benefits other than pension in accordance with the Statement of Financial Accounting Standards (SFAS) No. 106, *Employer's Accounting for Post-retirement Benefits Other Than Pensions*.
10. **Accrued 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 accrual at current pay rates.
11. **Use of Estimates** – The preparation of the accompanying financial statements requires management to make estimates and assumptions about certain estimates included in the financial statements. Actual results will invariably differ from those estimates.

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note B – Summary of Significant Accounting Policies (continued)

12. **Income Tax Status** – ARC is exempt from Federal income tax under § 501(c)(3) of the Internal Revenue Code and is classified as other than a private foundation.

Note C – Business Development Revolving Loan Funds

ARC established business development revolving loan funds (RLF) grants to provide pools of funds to be made available to grantees to create and retain jobs. Various entities (grantees) within the thirteen states were provided with loan capitalization funds. These funds are loaned to borrowers who qualify with program objectives. The earnings (interest and fees) net of expenses (including bad debt) are available to the grantees to make additional loans.

Grantees return the funds to ARC when they terminate the RLF. Grantees that have income in excess of expenses (net income) return the excess funds to ARC, and ARC deposits the net income funds in the U.S. Treasury general fund. Grantees that have net losses return the funds to ARC net of the losses. Grant balances that are returned are added back to the state allocation.

The following summarizes the RLF balances at September 30:

		2006		2005
RLF Funds Obligated	4200.25	\$ 34,543,851	\$	33,435,470
RLF Funds Advanced	4200.20	30,235,390		28,942,787
RLF Loans Outstanding	4200.20	24,851,106		34,261,278

Note D – Grant Transfers to Other Federal Agencies

ARC transfers funds to basic agencies to oversee economic and social development projects in the Appalachian Region. ARC records the funds transferred as contra revenue at the time the transfer is made. ARC transferred or received funds as follows:

		2006		2005
Department of Transportation	1300.25	\$ 210,000	\$	688,000
US Army Corps of Engineers		3,960,000		(493,000)
Economic Development Administration		2,538,000		2,323,298
Environmental Protection Agency		(746,710)		
Department of Agriculture		13,900,000		12,325,976
Department of Housing and Urban Development		6,075,820		11,316,408
	└─	\$ 25,937,110	\$	26,160,682

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note E – Retirement and Other Post-Employment Benefit Plans

Federal

ARC participates in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) for Federal and certain non-Federal employees. The CSRS and FERS plans are administered by the U.S. Office of Personnel Management (OPM). ARC makes contributions at rates applicable to agencies of the Federal government. The contributions do not equal the full service cost of the pension expense, which is the actuarial present value of benefits attributed to services rendered by covered employees during the accounting period. The measurement of service costs requires the use of actuarial cost methods to determine the percentage of the employees' basic compensation sufficient to fund their projected pension benefit. These percentages (cost factors) are provided by OPM.

The excess of total pension expense over the amount contributed by ARC and ARC employees represents the amount which must be financed directly by OPM. ARC does not recognize in its financial statements these excess amounts as they are deemed to be immaterial.

Contributions to these plans for FY 2006 were \$43,055 and \$72,154 for CSRS and FERS, respectively, and contributions for FY 2005 were \$44,099 and \$69,879 for CSRS and FERS, respectively.

Several employees also participate in the Federal Employees Health Benefit plan (FEHB) and the Federal Employees Group Life Insurance program (FEGLI), also administered by OPM. ARC pays the cost of current employees. Post-retirement benefits are paid by OPM. No amounts have been recognized in the financial statements for these imputed costs as they are not deemed material. Contributions to these plans for FY 2006 were \$58,846 and \$2,161 and for FY 2005 \$56,862 and \$2,234 for FEHB and FEGLI, respectively.

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

ARC also contributed \$27,236 and \$25,894 to the Federal Thrift Savings plan for all eligible employees for the years ended September 30, 2006 and 2005, respectively.

Non-Federal

ARC has a Defined Benefit Pension Plan which was open to all employees not participating in CSRS and FERS. The plan was closed in February 2000 to further entry. The Commission uses a July 1 measurement date for its plan. Plan information at September 30 consists of the following:

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note E – Retirement and Other Post-Employment Benefit Plans (continued)

	<u>2006</u>	<u>2005</u>
Benefit obligation	\$ (11,133,361)	\$ (11,415,578)
Fair value of plan assets	4,415,875	3,313,848
Funded status	<u>\$ (6,717,486)</u>	<u>\$ (8,101,730)</u>

Accrued benefit cost recognized in the balance sheet	\$ 1,934,715	\$ 1,683,124
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	<u>2006</u>	<u>2005</u>
Employer contribution	\$ 1,212,108	\$ 467,777
Participant contribution	20,565	25,815
Benefits paid	345,831	121,609
Net periodic benefit costs	1,441,506	1,165,334

The accumulated benefit obligation was \$9,783,577 and \$9,070,903 at September 30, 2006 and 2005, respectively.

Additional Information

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

	<u>2006</u>	<u>2005</u>
Discount rate	5.75%	4.75%
Rate of compensation increase	3.00	4.51

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

	<u>2006</u>	<u>2005</u>
Discount rate	4.75%	5.75%
Expected return on plan assets	7.25	7.50
Rate of compensation increase	4.51	4.08

Historical returns of multiple asset classes were analyzed to develop a risk-free real rate of return and risk premiums for each asset class. The overall rate for each asset class was developed by combining a long-term inflation component, the risk-free real rate of return, and the associated risk premium. A weighted average rate was developed based on those overall rates and the target asset allocation plan.

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note E – Retirement and Other Post-Employment Benefit Plans (continued)

Plan Assets

Pension plan weighted-average asset allocations at September 30, 2006 and 2005 are as follows:

<u>Asset Category</u>	<u>2006</u>	<u>2005</u>
Equity securities	34.00%	30.00%
Debt securities	61.00	65.00
Real estate	5.00	5.00
Total assets	<u>100.00%</u>	<u>100.00%</u>

The Commission's investment strategy is a long-term, risk-controlled approach using diversified investment options with a minimal exposure to volatile investment options like derivatives.

The Commission expects to contribute \$1,271,329 to the plan in FY2007.

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

	<u>Pension Benefits</u>
2007	\$ 3,952,404
2008	1,022,268
2009	466,351
2010	71,724
2011	1,689,832
Years 2011 – 2016	7,190,877

ARC also maintains a 401(k) plan covering substantially all non-Federal employees. ARC contributed \$152,806 and \$146,018 for the years ended September 30, 2006 and 2005, respectively.

Note F – Lease

ARC's lease for its office space provides for increases in annual base rent based on consumer price index increases, and payment of a portion of the increases in building operating expenses and real estate taxes. The old lease commenced on April 30, 1996 and extends through December 31, 2006. The new lease commences on January 1, 2007 and extends through December 31, 2016. Future minimum lease payments required under these non-cancelable leases are as follows:

APPALACHIAN REGIONAL COMMISSION
Notes to Financial Statements
Years Ended September 30, 2006 and 2005

Note F – Lease (continued)

<u>Year Ended September 30,</u>	<u>Amount</u>
2007	\$ 705,414
2008	740,154
2009	754,957
2010	770,056
2011	785,458
Thereafter	4,542,200
Total	<u>\$ 8,298,239</u>

Rent expense for the years ended September 30, 2006 and 2005 was \$598,605 and \$667,188, respectively.

Additional Information

APPALACHIAN REGIONAL COMMISSION
Additional Information (Unaudited)
Years Ended September 30, 2006 and 2005

Appalachian Development Highway System
(Appropriated Funds held by the U.S. Department of Transportation)

Congress authorized approximately \$9.7 billion for the construction of the Appalachian Development Highway System (ADHS) through fiscal year 2009. When it is complete, there will be a 3,090 mile regional system. The purpose of the ADHS is to generate economic development in previously isolated areas, supplement the national interstate system, connect Appalachia to the interstate system, and provide access to the Appalachian Region.

The U.S. Department of Transportation (DOT) funds the ADHS primarily through the Highway Trust Fund, from which Congress authorizes annual obligation ceilings for the program. Periodically, additional funds may be provided by direct appropriation to the DOT. ARC exercises policy and programmatic control over the ADHS, including the responsibility to set policy for allocating funds to the states, and DOT is accountable for the funds. The program includes flexibility for states to use some highway funds for access road development, and ARC exercises approval for such projects.

The following is a summary of the balances and activity related to the ADHS for FY 2006: *1300,20*

	Unexpended Authority as of 10/1/2005	FY 2006 Authorizations	FY 2006 Expenditures	Unexpended Authority as of 9/30/2006
DOT				
Appropriations	\$ 207,640,713	\$ 99,160,000	\$ (62,554,752)	\$ 244,245,961
Highway Trust Fund Obligation Ceiling	1,372,242,485	395,295,735	(661,262,398)	1,106,275,822
Total	<u>\$ 1,579,883,198</u>	<u>\$ 494,455,735</u>	<u>\$ (723,817,150)</u>	<u>\$ 1,350,521,783</u> ✓

Status of budgetary resources as of September 30, 2006:

	Obligated Balance	Unobligated Balance	Total
DOT Appropriations	\$ 136,008,694	\$ 108,237,267	\$ 244,245,961
Highway Trust Fund Obligation Ceiling	440,547,887	665,727,935	1,106,275,822
	<u>\$ 576,556,581</u>	<u>\$ 773,965,202</u>	<u>\$ 1,350,521,783</u>

APPALACHIAN REGIONAL COMMISSION
Additional Information (Unaudited)
Years Ended September 30, 2006 and 2005

Federal Budgetary Data

The following summarizes the budgetary data related to ARC's Federal appropriations for the year ended September 30:

BUDGETARY RESOURCES	<u>2006</u>	<u>2005</u>
Budget authority – appropriation	\$ 65,472,000	\$ 66,000,000
Net transfers	(25,937,110)	(26,160,682)
Unobligated balance brought forward October 1	5,891,302	8,565,932
Spending authority from offsetting collections	1,213,540	1,027,169
Recoveries of prior year obligations	4,177,838	3,189,101
Permanently not available	(654,720)	(528,000)
Total budgetary resources	<u>50,162,850</u>	<u>52,093,520</u>
 STATUS OF BUDGETARY RESOURCES		
Obligations incurred	39,725,374	46,202,218
Unobligated balance	10,437,476	5,891,302
Total budgetary resources	<u>\$ 50,162,850</u>	<u>\$ 52,093,520</u>

To the Commission Members
Appalachian Regional Commission
Washington, DC

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

We have audited the financial statements of the Appalachian Regional Commission as of and for the year ended September 30, 2006, and have issued our report thereon dated November 6, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered ARC'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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance

As part of obtaining reasonable assurance about whether ARC's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying audit finding.

The Commission Members
Appalachian Regional Commission
Washington, DC

We noted other matters involving the internal control over financial reporting, which we have reported to the management of ARC in a separate letter dated November 6, 2006.

This report is intended solely for the information and use of the Inspector General, the Commission Members, management and others within the organization and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

November 6, 2006

APPALACHIAN REGIONAL COMMISSION

Follow-up on Prior Audit Finding

Grant Reporting

Condition: During the prior year audit of ARC's grant files, we noted a lack of timely submission of grant progress and final reports. Our FY 2005 testing found that out of the 44 grant files sampled, 7 of the files where the grant period had expired, the final reports were not submitted timely which caused a delay in closing of the grants.

Recommendation: We recommended ARC develop policies and procedures to effectively monitor grantee compliance with grant reporting requirements and to promptly follow-up with any instances of non-compliance were noted.

Current Status: During our current year audit, we found that in 5 out of 10 (50%) of the files, the progress reports were not submitted timely per ARC policy. Due to the continued late filing of progress report submissions, this finding will remain open pending full implementation of the corrective action plan. 7/30/11

Summary of Qualifications

Ms. Davis is a highly experienced audit Partner and engagement manager who has concentrated her career in auditing for government agencies and the governmentally funded not-for-profit sector. She has developed particular expertise in performing audits of Federal Fiduciary Funds administered by the U.S. Department of Labor.

Ms. Davis joined M.D. Oppenheim & Company, P.C. in 1990. In 1999 she became the Partner-in-Charge of the Firm's office in Silver Spring, Maryland and in 2000 also took on Firm-wide responsibility as the Firm's Director of Federal Government Client Services. In 2004 she was elected a member of the Firm's Executive Committee.

During the last five years she has served as Partner-in-Charge of the Firm's participation in auditing the consolidated financial statements of the U.S. Department of Labor. In FY2003/5 Ms. Davis was responsible for the audit of the Federal Employees' Compensation Act Special Benefit Fund, Longshore and Harbor Workers' Compensation Act Special Fund, District of Columbia Workmen's Compensation Act Special Fund and the Energy Employees' Occupational Illness Compensation Program. In recent years other U.S. Department of Labor audit projects included the Departmental Budget, Funds with U.S. Treasury, Grants, Procurement, Departmental Property, and Non-Payroll Salaries and Expenses. In FY2003/5 she served as the Partner-in-Charge of the Firm's audits of U.S. Department of Labor Job Corp Centers.

Ms. Davis began her professional career with an international not-for-profit educational organization. During her eleven years of employment there she held numerous financial and managerial positions. Her service culminated in two and a half years as the Director of State Operations for the State of Ohio. The State Director's position involved responsibility for a multi-million dollar annual budget, planning, directing and analyzing the educational and programmatic activities of the organization, and responsibility for supervising a large staff. During those eleven years, Ms. Davis gained extensive expertise at the grantee/contractor level in handling funding provided by various levels of government. Subsequently, she made a career change and completed additional courses to qualify for the Certified Public Accountant examination.

Since entering public accounting she has experienced a wide range of government audits and special projects. Government agency assignments she has supervised include audits for the U.S. Department of Labor, Peace Corps (in Africa and Kazakhstan), National Science Foundation, Securities and Exchange Commission and the Appalachian Regional Commission, among many others.

Education | Certifications | Qualifications | Affiliations

- Bachelor of Science - University of California at Davis (Psychology and Child Development); Additional Post Graduate Courses in Accounting
- Certified Public Accountant – Maryland, District of Columbia, Virginia and West Virginia
- Certified Government Financial Manager
- American Institute of Certified Public Accountants
- Maryland Association of Certified Public Accountants
- Association of Government Accountants

Relevant Experience

Name of Client

U.S. Department of Labor:

CFO Act Financial Statement Audit:

- Federal Employees' Compensation Act
Special Benefit

Fund (including AUP)

- Energy Employees' Occupational Illness
Compensation
Program

Federal Fiduciary Activities Audits

- Longshore and Harbor Workers'
Compensation Act
Special Fund
- District of Columbia Workmen's Compensation
Act
Special Fund

- Funds with U.S. Treasury
- Non-Payroll Salaries and Expenses
- Departmental Property
- Working Capital Fund
- Procurement
- Departmental Budget
- Grants
- Debt Management

U.S. Department of Labor:

Performance and agreed-upon procedures audits
of
Job Corps Centers, review of working papers and
reports in 2003, 2004 and 2005

Appalachian Regional Commission:

Audit of governmental commission

Legal Services Corporation:

Audit of governmental corporation

Denali Commission (Alaska):

Audit of government commission

U.S. Equal Employment Opportunity Commission:

Performance audit of the Education, Technical
Assistance and Training Revolving Fund

National Labor Relations Board:

Performance audit – evaluation of board
casehandling reports

Denali Commission:

Agreed-upon-procedures - financial management
and reporting assessment

Appalachian Regional Commission:

Performance audit of the Appalachian
Development Highway System

Summary of Qualifications

Mr. Karakashian joined M.D. Oppenheim & Company, P.C. upon his graduation from college and has progressed to a highly responsible Manager's position. Throughout the past ten years, he has utilized the bulk of his time performing audits and special projects for Federal departments and agencies. Additionally, he has also performed audits of numerous firm not-for-profit clients, many of which require A-133 "Single Audits".

Most recently he has been responsible for the overall management of all the firm's responsibilities under the consolidated financial statement audit of the U.S. Department of Labor, including the audits of the Federal Employees' Compensation Act Special Benefit Fund (including AUP), Energy Employees' Occupational Illness Compensation Program, Procurement, Budget, Fund Balances with U.S. Treasury, and Non-payroll salaries and expenses. He conducted the FFMIA review of the PRISM system and planned and supervised the imprest fund audit. His other responsibilities at DOL have involved the audit of grant funding and debt management activity related to disallowed grant costs.

Mr. Karakashian has also performed audits surveys, performance reviews and special projects for a number of other Federal agencies and government corporations. In the commercial area he has provided firm clients with agreed-upon-procedures engagements, financial statement audits and forensic audits.

**Education | Certifications | Qualifications | Affiliations | Professional
Accomplishments**

- Bachelor of Science – The Pennsylvania State University at University Park, Pennsylvania (Accounting and Business Law)
- Certified Public Accountant – Maryland
- Certified Fraud Examiner
- Certified Information Systems Auditor
- American Institute of Certified Public Accountants
- Maryland Association of Certified Public Accountants
- Association of Government Accountants
- Association of Certified Fraud Examiners

Relevant Experience

Name of Client/

U.S. Department of Labor:

CFO Act Financial Statement Audit

- Federal Employees' Compensation Act Special Benefit

 - Fund (including AUP)

- Energy Employees' Occupational Illness Compensation Program

- Longshore and Harbor Workers' Compensation Act

 - Special Fund

- District of Columbia Workmen's Compensation Act

 - Special Fund

 - Funds with U.S. Treasury
 - Non-Payroll Salaries and Expenses
 - Departmental Property
 - Working Capital Fund
 - Procurement
 - Departmental Budget
 - Grants
 - Debt Management

Legal Services Corporation:

Audit of governmental corporation

National Science Foundation:

Indirect and direct cost audits of not-for-profit organizations including:

- North Carolina Museum of Science
- Carnegie Institution of Washington
- Mathematical Association of America
- American Chemical Society

U.S. Equal Employment Opportunity Commission:

Performance audit of the education, technical assistance and training revolving fund

KRA Corporation:

Subcontract audit of USDOL funds

Summary of Qualifications

Ms. Wagner has had a varied and extensive public accounting career with an emphasis on performing audits of the financial statements of government agencies and of grants and contracts awarded for such agencies. She has also developed expertise in auditing not-for-profit organizations, including those receiving government funding and requiring OMB A-133 "Single Audits".

Ms. Wagner has performed at a Supervisory Auditor level for several years during the M.D. Oppenheim & Company, P.C. audits of the U.S. Department of Labor FY 2005, 2004, 2003 and 2002 consolidated financial statements. She is currently involved during FY 2005 in auditing the Federal Employees' Compensation Act Special Benefit Fund, Longshore and Harbor Workers' Compensation Act Special Fund, and the District of Columbia Workers' Compensation Act Special Fund.

She has significant experience with the National Science Foundation where she has participated in both indirect and direct cost audits of not-for-profit agencies. She has also had a supervisory role in the financial and administrative evaluations the Firm is performing of "Small Business Innovation Research" (SBIR) Phase II Awards, under a separate Firm contract with NSF.

After graduating from college, Ms. Wagner was initially employed by the U.S. Department of Defense in Stuttgart, Germany as a Protocol Assistant at Headquarters USEUCOM for several years. She then returned to the United States where she was employed by the Department of the Army as an Administrative Assistant based at Fort Sam Houston in San Antonio, Texas. Ms. Wagner subsequently relocated to the Washington area and commenced her career in public accounting with M.D. Oppenheim & Company, P.C.

Education | Certifications | Qualifications | Affiliations

- Bachelor of Science – Weber State University, (Accounting)
- Candidate for Certified Public Accountant – Maryland – has passed three parts of the examination and holds partial credit; final parts in process.
- Association of Government Accountants

Relevant Experience

Name of Client

U.S. Department of Labor:

CFO Act Financial Statement Audit

- Federal Employees' Compensation Act Special Benefit Fund (including AUP)

Federal Fiduciary Activities Audits

- Longshore and Harbor Workers' Compensation Act Special Fund
- District of Columbia Workmen's Compensation Act Special Fund
- Funds with U.S. Treasury
- Non-Payroll Salaries and Expenses
- Departmental Property

Legal Services Corporation:

Audit of government corporation

National Science Foundation:

SBIR financial and administrative reviews

National Science Foundation:

Indirect and direct cost audits of not-for-profit organizations including:

North Carolina Museum of Science
Carnegie Institution of Washington
Mathematical Association of America
American Chemical Society