

INDEPENDENT AUDITOR'S REPORT
AUD-FM-IB-17-14

To the Board of Governors and the Inspector General of the Broadcasting Board of Governors

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of the Broadcasting Board of Governors (BBG), which comprise the consolidated balance sheets as of September 30, 2016 and 2015, the related consolidated statements of net cost and changes in net position, and the combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements (hereinafter referred to as the "consolidated financial statements").

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, "Audit Requirements for Federal Financial Statements." Those standards and OMB Bulletin No. 15-02 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate under the circumstances but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



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

Opinion on the Consolidated Financial Statements

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of BBG as of September 30, 2016 and 2015, and its net cost of operations, changes in net position, and budgetary resources for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Deferred Maintenance sections (hereinafter referred to as "required supplementary information") be presented to supplement the consolidated financial statements. Such information, although not a part of the consolidated financial statements, is required by OMB Circular A-136, "Financial Reporting Requirements," and the Federal Accounting Standards Advisory Board, which consider the information to be an essential part of financial reporting for placing the consolidated financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing it for consistency with management's responses to our inquiries, the consolidated financial statements, and other knowledge we obtained during our audits of the consolidated financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The information in the Message from the BBG Chairman and CEO, the Introduction, the Performance Information, and the Other Information sections, as listed in the Table of Contents of BBG's Performance and Accountability Report, is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards* and OMB Bulletin No. 15-02, we have also issued reports, dated November 13, 2016, on our consideration of BBG's internal control over

financial reporting and on our tests of BBG's compliance with provisions of applicable laws, regulations, contracts, and grant agreements for the year ended September 30, 2016. The purpose of those reports 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 internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Bulletin No. 15-02, and should be considered in assessing the results of our audit.



Alexandria, Virginia
November 13, 2016

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING**

To the Board of Governors and the Inspector General of the Broadcasting Board of Governors

We have audited the consolidated financial statements of the Broadcasting Board of Governors (BBG) as of and for the year ended September 30, 2016, and have issued our report thereon dated November 13, 2016. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, "Audit Requirements for Federal Financial Statements."

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered BBG's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate under the circumstances for the purpose of expressing our opinion on the consolidated financial statements but not for the purpose of expressing an opinion on the effectiveness of BBG's internal control. Accordingly, we do not express an opinion on the effectiveness of BBG's internal control. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 15-02. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies; therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the following sections, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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

Material Weakness

I. Validity and Accuracy of Unliquidated Obligations

Unliquidated obligations (ULOs) represent the cumulative amount of orders, contracts, and other binding agreements for which the goods and services ordered have not been received or the goods and services have been received but payment has not yet been made. BBG should record an obligation in its financial management system when it enters into an agreement, such as a contract or a purchase order, to purchase goods and services. Once recorded, the obligation remains open until it is fully reduced by disbursements, is deobligated, or the appropriation funding the obligation is canceled. BBG reported more than \$178 million in ULOs as of September 30, 2016.

Of a sample of 91 ULOs tested, we found 27 (30 percent) invalid ULOs. During FY 2016, BBG's Office of Chief Financial Officer (OCFO) assigned an analyst to focus on ULO reduction efforts in accordance with its draft Unliquidated Obligations Review Standard Operating Procedures (SOP). The analyst reviewed current and prior year ULOs and deobligated those that were determined to be invalid. The analyst's efforts reduced the amount of invalid ULOs in BBG's accounting records in FY 2016. However, we found that invalid obligations continued to exist because allotment holders outside OCFO were not always effectively monitoring the validity of obligations.¹ Although OCFO distributes monthly reports listing potentially invalid obligations, allotment holders are not always responsive in reviewing obligations and deobligating obligations found to be invalid. We also found that some allotment holders were unaware of their responsibility to deobligate invalid obligations that have been identified.

Although the draft SOP includes guidance for allotment holders to identify and deobligate invalid ULOs, the draft SOP has not been approved by BBG and distributed across the agency. Further, the draft SOP does not include a process for OCFO to confirm the receipt of responses from all allotment holders or to confirm that invalid ULOs identified by allotment holders were deobligated. In addition, BBG does not review overseas ULOs for validity and the draft SOP does not contain any guidance on reviewing ULOs for overseas program officers. As a result of invalid ULOs identified by our audit, BBG adjusted its financial statements. These funds could have been used for other purposes but remained in unnecessary obligations. Weaknesses in controls over ULOs were initially reported in our audit of BBG's FY 2013 financial statements.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance. We consider the following deficiencies in BBG's internal control to be significant deficiencies.

¹ Allotment holders include Contracting Officer's Representatives and other officials who are responsible for managing obligations relating to contracts, interagency agreements and other miscellaneous obligations, such as utility payments and travel.

Significant Deficiencies

I. Grantee Monitoring

BBG has three grantees that it funds through annual grant agreements: Radio Free Europe/Radio Liberty, Radio Free Asia, and the Middle East Broadcasting Networks. The grantees are responsible for developing broadcast content (radio and television news programs), which is distributed by BBG. In FY 2016, the three grantees received \$270 million, approximately one-third of BBG's total funding.

BBG is responsible for monitoring grantee use of BBG funds to ensure grantees adhere to applicable laws and regulations as well as all terms and conditions specified in the grant agreements. To aid in the monitoring process, BBG drafted a Grantee Handbook, which presents information and procedures that both BBG and its grantees will use during the life of a grant. We selected 14 control activities from the draft Grantee Handbook to test whether BBG had effectively implemented grantee monitoring. We found that 5 of the 14 controls tested were implemented during FY 2016, but the remaining 9 control activities were not implemented. For example, BBG had not performed risk assessments to finalize the scope and frequency of grantee site visits, issued site visit reports to communicate findings and needed improvements to its grantees, or obtained Performance Project Reports from its grantees. BBG officials stated that many oversight activities would not be initiated until the draft Grantee Handbook is fully approved and finalized.

Because BBG lacked effective grantee oversight, the risk of waste, fraud, and abuse of Federal funds increases. An organized and documented approach to oversight is needed to demonstrate accountability and mitigate the risk of waste, fraud, and abuse. We have identified weaknesses in controls over grantee monitoring since our audit of BBG's FY 2013 financial statements.

II. Information Technology

BBG's information systems and sensitive information rely on the confidentiality, integrity, and availability of BBG's comprehensive and interconnected infrastructure. Managing information security risk effectively throughout the organization is critical to achieving BBG's mission. BBG uses several financial management systems to compile information for financial reporting purposes. BBG's main domestic financial management and accounting system is Momentum, which is provided by an external service provider that is also responsible for maintaining a number of IT controls. However, Momentum is accessed through BBG's general IT support system, which is a component of BBG's information security program. Therefore, security weaknesses noted in BBG's information security program could potentially impact Momentum as well. For overseas accounting and budget execution, BBG uses the Regional Financial Management System (RFMS) provided by the Department of State (Department). The Department is also responsible for maintaining an adequate information security program.

The Office of Inspector General (OIG) annually audits BBG's and the Department's information security programs' compliance with IT provisions as required by the Federal Information

Security Modernization Act of 2014 (FISMA). In the FY 2016 FISMA report for BBG,² OIG reported security weaknesses that had a significant impact on BBG's information security program. Specifically, OIG reported control weaknesses in all eight key FY 2016 Inspector General FISMA metric domains, which consist of risk management, contractor systems, configuration management, identity and access management, security and privacy training, information security continuous monitoring, incident response, and contingency planning.

OIG's FY 2016 FISMA report for the Department³ identified information security program weaknesses that are similar to the weaknesses identified at BBG. OIG reported that the Department did not have an effective information security program. RFMS is hosted on the Department's general support system and is a component of the Department's information security program. Because of the security weaknesses noted with the information security program at the Department, BBG needs to implement additional controls to ensure that financial information is being processed accurately and completely by the Department.

Without an effective information security program, BBG is vulnerable to IT-centered attacks and threats. Information security program weaknesses can affect the integrity of financial applications, which increases the risk that sensitive financial information could be accessed by unauthorized individuals or that financial transactions could be altered either accidentally or intentionally. Information security program weaknesses increase the risk that BBG will be unable to report financial data accurately. We have reported weaknesses in IT security controls as a significant deficiency since our audit of BBG's FY 2013 financial statements.

During the audit, we noted certain additional matters involving internal control over financial reporting that we will report to BBG management in a separate letter.

Status of Prior Year Findings

In the Independent Auditor's Report on Internal Control Over Financial Reporting, included in the audit report on BBG's FY 2015 financial statements,⁴ we noted several issues that were related to internal control over financial reporting. The status of these issues is summarized in Table 1.

² OIG, *Audit of the Broadcasting Board of Governors Information Security Program* (AUD-IT-IB-17-18, November 2016).

³ OIG, *Audit of Department of State Information Security Program* (AUD-IT-17-17, November 2016).

⁴ OIG, *Independent Auditor's Report on the Broadcasting Board of Governors 2015 and 2014 Financial Statements* (AUD-FM-IB-16-14, November 2015).

Table 1. Status of Prior Year Findings

Control Deficiency	FY 2015 Status	FY 2016 Status
Validity and Accuracy of Unliquidated Obligations	Material Weakness	Material Weakness
Grantee Monitoring	Significant Deficiency	Significant Deficiency
Information Technology	Significant Deficiency	Significant Deficiency

BBG’s Response to Findings

BBG management has provided its response to our findings in a separate letter included in this report as Appendix A. We did not audit management’s response, and accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and the results of that testing and not to provide an opinion on the effectiveness of BBG’s internal control. This report is an integral part of an audit performed in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Bulletin No. 15-02, in considering BBG’s internal control over financial reporting. Accordingly, this report is not suitable for any other purpose.



Alexandria, Virginia
November 13, 2016

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS,
REGULATIONS, CONTRACTS, AND GRANT AGREEMENTS**

To the Board of Governors and the Inspector General of the Broadcasting Board of Governors

We have audited the consolidated financial statements of the Broadcasting Board of Governors (BBG) as of and for the year ended September 30, 2016, and have issued our report thereon dated November 13, 2016. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 15-02, "Audit Requirements for Federal Financial Statements."

Compliance

As part of obtaining reasonable assurance about whether BBG's consolidated financial statements are free from material misstatement, we performed tests of BBG's compliance with provisions of applicable laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material impact on the determination of financial statement amounts. We limited our tests of compliance to these provisions and did not test compliance with all laws, regulations, contracts, and grant agreements applicable to BBG. 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 instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 15-02 and which are summarized as follows:

- *Federal Grant Regulations.* BBG is responsible for monitoring the use of funds provided to its grantees to ensure the grantees adhere to relevant laws and regulations. Since our FY 2013 audit of BBG's financial statements, we have identified substantial noncompliance with Federal grant regulations. As noted in our Independent Auditor's Report on Internal Control Over Financial Reporting, BBG took steps to strengthen its grantee monitoring program during FY 2016. Despite these efforts, BBG has not fully implemented many of its newly designed monitoring controls. As a result, BBG continued to be in substantial noncompliance with the Code of Federal Regulations, Title 2, Subtitle A, Chapter II, Part 200 – Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, which provides guidance to agencies for grant oversight.
- *Federal Managers' Financial Integrity Act.* The Federal Managers' Financial Integrity Act requires executive branch agencies to establish and maintain effective internal control. Heads of agencies must annually evaluate and report on the effectiveness of the

internal control and financial management systems that protect the integrity of Federal programs. BBG has made progress in FY 2016 by hiring staff and contractors to oversee and implement an internal control assessment program; however, controls testing and other procedures necessary for management to make an informed judgment as to the overall adequacy and effectiveness of internal control over operations, reporting, and compliance were not performed. Further, BBG did not complete its annual evaluation in FY 2016. Noncompliance with the Federal Managers' Financial Integrity Act was initially noted in our audit of BBG's FY 2013 financial statements.

During the audit, we noted certain additional matters involving compliance that we will report to BBG management in a separate letter.

BBG's Response to Findings

BBG management has provided its response to our findings in a separate letter included in this report as Appendix A. We did not audit management's response, and accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing and not to provide an opinion on the effectiveness of BBG's compliance. This report is an integral part of an audit performed in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Bulletin No. 15-02, in considering BBG's compliance. Accordingly, this report is not suitable for any other purpose.



Alexandria, Virginia
November 13, 2016



BROADCASTING BOARD OF GOVERNORS
UNITED STATES OF AMERICA

November 14, 2016

The Honorable Steve A. Linick
Inspector General
U.S. Department of State

Dear Mr. Linick:

The BBG is committed to transparency and accountability for the taxpayer funds provided by Congress to pursue its mission to inform, engage, and connect people around the world in support of freedom and democracy. The Performance and Accountability Report (PAR) is a key part of maintaining this commitment, providing a comprehensive account of the BBG's financial activities.

I am pleased to report that the BBG has received an unmodified opinion for this fiscal year's financial audit. For the one material weakness and two significant deficiencies that the audit identified, we are committed to building on the progress achieved in the past year to address them.

In FY 2017, we will apply rigorous dedication to achieving maximum compliance, transparency, and accountability, similar to our core mission. In order to have impact with audiences, the BBG must provide quality programming and earn the trust of audiences. We are monitoring our progress through an impact model, which tracks engagement, connection, and being influential with audiences, media institutions, and governments through a range of quantitative, qualitative, digital, and anecdotal indicators. We understand that achieving such impact relies on effectively managing the resources provided by Congress.

We would be remiss if we did not thank Kearney & Company for their sustained efforts and professionalism in working through the complex issues associated with the global nature of BBG's financial processes.

Sincerely,

A handwritten signature in black ink, which appears to read "John Barkhamer", is written over a horizontal line.

John Barkhamer
Acting Chief Financial Officer