Office of Inspector General

OFFICE OF CYBER ASSESSMENTS AND DATA ANALYTICS

AUDIT REPORT

THE SOUTHWESTERN FEDERAL POWER SYSTEM'S FISCAL YEAR 2023 FINANCIAL STATEMENTS AUDIT

DOE-OIG-24-24
JULY 2024

Department of Energy
Washington, DC 20585

July 25, 2024

MEMORANDUM FOR THE ADMINISTRATOR, SOUTHWESTERN POWER ADMINISTRATION

FROM: Kshemendra Paul
Assistant Inspector General
for Cyber Assessments and Data Analytics
Office of Inspector General

SUBJECT: Audit Report on The Southwestern Federal Power System's Fiscal Year 2023 Financial Statements Audit

The attached report presents the results of the independent certified public accountants' audit of the Southwestern Federal Power System's (SWFPS) balance sheets as of September 30, 2023, and 2022, and the related consolidated statements of net costs, changes in net position, custodial activity, combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements.

To fulfill the Office of Inspector General's audit responsibilities, we contracted with the independent public accounting firm of KPMG LLP (KPMG) to conduct the audit, subject to our review. KPMG is responsible for expressing an opinion on the SWFPS's financial statements and reporting on applicable internal controls and compliance with laws and regulations. The Office of Inspector General monitored audit progress and reviewed the audit report and related documentation. This review disclosed no instances where KPMG did not comply, in all material respects, with generally accepted government auditing standards. The Office of Inspector General did not express an independent opinion on the SWFPS's financial statements.

KPMG concluded that the financial statements present fairly, in all material respects, the financial position of the SWFPS as of September 30, 2023, and 2022, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles. The results of the auditors' review disclosed no instances of noncompliance or other matters required to be reported under Government Auditing Standards.

As part of this review, auditors also considered the SWFPS's internal controls over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the combined financial statements. The audit identified a deficiency in internal control that we consider to be a significant deficiency:

- KPMG identified a significant deficiency with internal controls over property, plant, and equipment. KPMG identified that the SWFPS inappropriately depreciated land balances in the combined financial statements. In addition, KPMG found that the SWFPS had inappropriately recorded losses on the disposal of retired plant and equipment to accumulated depreciation. Lastly, the SWFPS and Army Corps of Engineers had not ensured substantially completed construction projects were transferred to property, plant, and equipment and depreciated at period end.

SWFPS management concurred with the findings and recommendations and agreed to take action to address each of our recommendations. Management's proposed corrective actions are consistent with our recommendations; therefore, a management decision is not required. However, the recommendations remain open and should be tracked in the Departmental Audit Report Tracking System until corrective actions are completed.

We appreciated the cooperation of your staff during the audit.

Attachment

cc: Chief Financial Officer, Southwestern Power Administration, SWPA

KPMG

SOUTHWESTERN FEDERAL POWER PROGRAM

Combined Financial Statements

September 30, 2023 and 2022

SOUTHWESTERN FEDERAL POWER SYSTEM

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KPMG LLP
Suite 800
1225 17th Street
Denver, CO 80202-5598

Independent Auditors' Report

The Inspector General, United States Department of Energy and
The Administrator, Southwestern Power Administration:

Report on the Audit of the Combined Financial Statements

Opinion

We have audited the combined financial statements of the Southwestern Federal Power System (SWFPS), which comprise the combined balance sheets as of September 30, 2023 and 2022, and the related combined statements of changes in capitalization, revenues and expenses, and cash flows for the years then ended, and the related notes to the combined financial statements. The combined financial statements include the Southwestern Power Administration (Southwestern), a component of the U.S. Department of Energy, and the U.S. Department of Defense, Army Corps of Engineers (the Corps) for which Southwestern markets and transmits power.

In our opinion, the accompanying combined financial statements present fairly, in all material respects, the financial position of the SWFPS as of September 30, 2023 and 2022, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Combined Financial Statements section of our report. We are required to be independent of the SWFPS and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matter

As discussed in note 1(r) to the combined financial statements, in 2023, the SWFPS adopted new accounting guidance related to leases. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Combined Financial Statements

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

In preparing the combined financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the SWFPS's ability to continue as a going concern for one year after the date that the combined financial statements are available to be issued.

Auditors' Responsibilities for the Audit of the Combined Financial Statements

Our objectives are to obtain reasonable assurance about whether the combined financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the combined financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the combined financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the combined financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the SWFPS's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the combined financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the SWFPS's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the combined financial statements as a whole. The supplementary information in schedules 1 through 4 is presented for purposes of additional analysis and is not a required part of the combined financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the combined financial statements. The information has been subjected to the auditing procedures applied in the audits of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves, and other additional procedures in accordance with GAAS. In our opinion, the information is fairly stated in all material respects in relation to the combined financial statements as a whole.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the combined financial statements as of and for the year ended September 30, 2023, we considered the SWFPS's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of the SWFPS's internal control. Accordingly, we do not express an opinion on the effectiveness of the SWFPS's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We identified a deficiency in internal control, described below, that we consider to be a significant deficiency.

1. **Controls Over General Property, Plant, and Equipment (23-SWFPS-01)**

   Condition

   Southwestern is responsible for marketing and transmitting the hydroelectric power generated by the Corps within Southwestern's marketing areas and is responsible for the preparation and presentation of the SWFPS combined financial statements. With more than $1.3 billion in net property, plant, and equipment (PP&E), including construction work in progress (CWIP), general PP&E is one of the largest balances on the SWFPS's balance sheet.

   During our testing over the SWFPS combined financial statements, we identified the following conditions:

   - Southwestern inappropriately depreciated land balances in the combined financial statements. Consequently, accumulated depreciation was overstated by $2.9 million as of September 30, 2023, and 2022, with the annual impact to depreciation expense of approximately $57,000.

   - Southwestern inappropriately recorded losses on the disposal of retired plant and equipment to accumulated depreciation. Consequently, accumulated depreciation was understated by $28.9 million and $28.8 million as of September 30, 2023, and 2022, respectively. Further, the operations and maintenance expense was understated by approximately $85,500 and $678,500 for the year ended September 30, 2023, and 2022, respectively.

   - Controls at Southwestern and the Corps were not operating effectively to ensure substantially completed construction projects are transferred to PP&E and depreciated at period end. Specifically:

     – We reviewed a sample of seven CWIP projects at Southwestern and identified one project that was substantially complete and in use as of September 30, 2023, but had not been transferred out of CWIP and into PP&E. The value of this project was $1.9 million and the total factual and projected misstatement was $2.3 million, with an inconsequential impact to depreciation expense. The known misstatement was corrected by Southwestern management.

- We reviewed a sample of 15 CWIP projects at the Corps and identified multiple project work items totaling $8.2 million that were substantially complete and in use as of September 30, 2023. In response to the misstatements, the Corps performed a review of all outstanding CWIP project balances, identifying additional completed projects that should have been transferred to PP&E for a total adjustment of $18.4 million and a related impact to depreciation expense of $2.1 million. The known misstatements were corrected by Corps management. We re-sampled the post-correction population and did not identify additional exceptions.

Criteria

- The Government Accountability Office's *Standards for Internal Control in the Federal Government* (Green Book), Principle 10, *Design Control Activities*, paragraph 10.03.
- Green Book, Principle 11, *Design Activities for the Information System*, paragraph 11.03.
- Green Book, Principle 12, *Implement Control Activities*, paragraph 12.03.
- Financial Accounting Standards Board Accounting Standards Codification (ASC) Topic 360, *Property, Plant, and Equipment*, Sections 10-35-4, 10-50-1, and 20-35-1.

Cause and Effect

The weaknesses identified occurred because Southwestern did not have the financial reporting infrastructure in place to identify all non-Generally Accepted Accounting Principles (GAAP) policies within the combined financial statements and evaluate the accounting implications of unusual arrangements within the Federal Government.

Further, we determined that the misclassification of expenditures into CWIP occurred primarily because existing controls were not operating at a precise enough level. While both Southwestern and the Corps have policies and procedures in place for periodically reviewing open CWIP balance for transfer to PP&E, the procedures were not operating at a sufficiently precise level to either identify all substantially completed projects or ensure substantially completed projects are transferred to PP&E by the balance sheet date.

Collectively, the conditions relate to insufficient risk assessment and monitoring controls at the SWFPS. Consequently, the SWFPS combined financial statements may include non-GAAP policies not previously monitored by Southwestern management or may include improper accounting treatments due to complexities in arrangement unusual within the Federal Government. While the misstatements were quantitatively large to the combined financial statements, the misstatements did not impact the power or transmission rates or the users of the financial statements.

Collectively, given the quantitatively large adjustments to the combined financial statements, the potential impact of CWIP transfers to rates and the users of the financial statements, and similar CWIP conditions identified in the fiscal year 2022 audit at the Corps, we consider this deficiency to be significant deficiency.

Recommendations

We recommend that the Chief Financial Officer, Southwestern:

1. Evaluate and document all accounting policies within the combined financial statements to ensure non-GAAP policies are identified and monitored at least annually for quantitative and qualitative impacts;
2. Evaluate and document the accounting implications of all unusual arrangements within the Federal Government, including alternative financing arrangements and regulatory assets and liabilities;
3. Enhance existing Southwestern processes to ensure that all substantially completed projects are transferred from CWIP to PP&E for financial reporting purposes; and
4. Work with the Corps to enhance existing CWIP monitoring processes to ensure the timely transfer of CWIP to PP&E.

Management's Response to Recommendations

Southwestern and the Corps concurs with the above recommendations and will:

1. Annually evaluate and document accounting policies within the combined financial statements to ensure non-GAAP policies are identified and monitored at least annually for quantitative and qualitative impacts.
2. Annually evaluate and document the accounting implications of all unusual arrangements within the Federal Government, including alternative financing arrangements and regulatory assets and liabilities.
3. Enhance existing Southwestern processes to ensure that all substantially completed projects are transferred from CWIP to PP&E for financial reporting purposes. Southwestern will review CWIP project balances quarterly and will transfer completed projects and material project balances based on percentage of project completion to PP&E.
4. Enhance existing CWIP monitoring processes to ensure the timely transfer of CWIP to PP&E.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the SWFPS's combined financial statements as of and for the year ended September 30, 2023 are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the combined financial statements. 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

SWFPS's Responses to the Findings

Government Auditing Standards requires the auditor to perform limited procedures on the SWFPS's responses to the findings identified in our audit and described previously. The SWFPS's responses were not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

KPMG

Purpose of the Reporting Required by *Government Auditing Standards*

The purpose of the communication described in the Report on Internal Control Over Financial Reporting and the Report on Compliance and Other Matters sections is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the SWFPS's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Denver, Colorado
July 19, 2024

SOUTHWESTERN FEDERAL POWER SYSTEM

Combined Balance Sheets

September 30, 2023 and 2022

Assets	**2023**	**2022**
Plant in service	$ 2,274,270,527	2,201,545,973
Accumulated depreciation	(1,046,163,370)	(1,003,859,401)
Construction work in progress	125,519,676	136,758,336
Net utility plant	1,353,626,833	1,334,444,908
Cash	807,645,159	693,644,537
Funds held in escrow (note 1(d))	170,372,212	180,133,726
Cash and funds held in escrow	978,017,371	873,778,263
Accounts receivable	16,479,824	24,485,158
Materials and supplies, at average cost	3,776,816	3,957,038
Banking exchange receivables	75,642	4,233,882
Deferred workers' compensation (note 4)	7,926,721	11,969,419
Other assets	68,973	924,275
Total assets	$ 2,359,972,180	2,253,792,943
Liabilities and Capitalization		
Liabilities:		
Accounts payable and accrued liabilities	$ 18,712,598	24,742,472
Advances for construction	4,408,257	2,471,234
Accrued workers' compensation	8,319,594	12,746,372
Purchased power and banking exchange deferral (note 4)	40,369,954	63,129,246
Hydropower water storage reallocation deferral (note 4)	58,209,942	58,576,945
Total liabilities	130,020,345	161,666,269
Capitalization:		
Payable to U.S. Treasury	1,477,645,158	1,355,728,673
Accumulated net revenues	752,306,677	736,398,001
Total capitalization	2,229,951,835	2,092,126,674
Commitments and contingencies (notes 6 and 7)		
Total liabilities and capitalization	$ 2,359,972,180	2,253,792,943

See accompanying notes to combined financial statements.

SOUTHWESTERN FEDERAL POWER SYSTEM

Combined Statements of Changes in Capitalization

Years ended September 30, 2023 and 2022

	Payable to U.S. Treasury	Accumulated net revenues	Total capitalization
Total capitalization as of September 30, 2021	$ 1,274,544,522	714,295,920	1,988,840,442
Additions:			
Congressional appropriations	109,503,347	—	109,503,347
Interest on payable to U.S. Treasury and other	10,795,681	—	10,795,681
Transfers of property and services, net	3,501,880	—	3,501,880
Total additions to capitalization	123,800,908	—	123,800,908
Deductions:			
Payments to U.S. Treasury	(42,616,757)	—	(42,616,757)
Total deductions to capitalization	(42,616,757)	—	(42,616,757)
Net revenues for the year ended September 30, 2022		22,102,081	22,102,081
Total capitalization as of September 30, 2022	1,355,728,673	736,398,001	2,092,126,674
Additions:			
Congressional appropriations	143,747,928	4,000,000	147,747,928
Interest on payable to U.S. Treasury and other	7,446,743	—	7,446,743
Transfers of property and services, net	6,933,943	—	6,933,943
Total additions to capitalization	158,128,614	4,000,000	162,128,614
Deductions:			
Payments to U.S. Treasury	(36,212,129)	—	(36,212,129)
Total deductions to capitalization	(36,212,129)	—	(36,212,129)
Net revenues for the year ended September 30, 2023		11,908,676	11,908,676
Total capitalization as of September 30, 2023	$ 1,477,645,158	752,306,677	2,229,951,835

See accompanying notes to combined financial statements.

SOUTHWESTERN FEDERAL POWER SYSTEM

Combined Statements of Revenues and Expenses

Years ended September 30, 2023 and 2022

	2023	2022
Operating revenues:		
Sales of electric power	$ 172,957,712	176,992,735
Transmission and other operating revenues	34,313,642	37,430,630
Total operating revenues before deferrals	207,271,354	214,423,365
Net purchased power and banking exchange deferral	19,709,994	8,556,940
Total operating revenues	226,981,348	222,980,305
Non-reimbursable revenues	9,361,098	2,170,048
Total revenues	236,342,446	225,150,353
Operating expenses:		
Operation and maintenance	127,661,129	113,562,616
Purchased power and banking exchange	35,788,165	24,869,181
Depreciation and amortization	44,175,156	54,090,847
Transmission service charges by others	—	32,913
Non-reimbursable expenses	9,266,343	3,915,978
Total operating expenses	216,890,793	196,471,535
Net operating revenues	19,451,653	28,678,818
Interest expense:		
Interest on payable to U.S. Treasury and other	10,371,813	13,048,608
Allowance for funds used during construction	(2,828,836)	(6,471,871)
Net interest expense	7,542,977	6,576,737
Net revenues	$ 11,908,676	22,102,081

See accompanying notes to combined financial statements.

SOUTHWESTERN FEDERAL POWER SYSTEM

Combined Statements of Cash Flows

Years ended September 30, 2023 and 2022

	2023	2022
Cash flows from operating activities:		
Net revenues	$ 11,908,676	22,102,081
Adjustments to reconcile net revenues to net cash provided by operating activities:		
Depreciation and amortization	44,175,156	54,090,847
Loss on retirement of plant in service	930,865	678,547
Benefit expense paid by other Federal agencies	13,532,433	8,369,135
Interest on payable to U.S. Treasury and other	7,542,977	6,576,737
Deferred workers' compensation	4,042,698	(3,957,870)
(Increase) decrease in assets:		
Accounts receivable	8,005,334	3,553,198
Materials and supplies	180,222	(555,598)
Banking exchange receivables	4,158,240	(451)
Other assets	855,302	(327,790)
Increase (decrease) in liabilities:		
Accounts payable and accrued liabilities	(6,029,874)	2,295,289
Accrued workers' compensation	(4,426,778)	4,012,341
Purchased power and banking exchange deferral	(24,100,367)	(8,503,254)
Advances for construction	1,937,023	949,249
Net cash provided by operating activities	62,711,907	89,282,461
Cash flows used in investing activities:		
Additions to utility plant	(61,459,111)	(74,036,248)
Cash flows from financing activities:		
Congressional appropriations	147,747,928	109,503,347
Payments to U.S. Treasury	(36,212,129)	(42,616,757)
Transfers of property and services, net	(6,598,490)	(4,867,255)
Hydropower water storage reallocation deferral	(1,950,997)	(1,914,166)
Net cash provided by financing activities	102,986,312	60,105,169
Net increase in cash and funds held in escrow	104,239,108	75,351,382
Cash and funds held in escrow, beginning of year	873,778,263	798,426,881
Cash and funds held in escrow, end of year	$ 978,017,371	873,778,263
Supplemental cash flow information:		
Interest charged to construction	$ 2,828,836	6,471,871
Interest deferred on regulatory liabilities	2,925,068	2,252,928
Transfer of construction work in progress to plant in service	54,240,900	171,445,118

See accompanying notes to combined financial statements.

SOUTHWESTERN FEDERAL POWER SYSTEM

Notes to Combined Financial Statements

September 30, 2023 and 2022

(1) Summary of Significant Accounting Policies

(a) General Information and Basis of Preparation of Combined Financial Statements

The Southwestern Federal Power System (SWFPS) financial statements combine all of the activities associated with the generation, transmission, and disposition of all Federal power marketed under Section 5 of the Flood Control Act of 1944 (the Flood Control Act) by the Southwestern Power Administration (Southwestern), an agency of the U.S. Department of Energy (DOE). The accompanying combined financial statements include the accounts of Southwestern and the related hydroelectric generating facilities and power operations of the U.S. Army Corps of Engineers (Corps), a component of the U.S. Department of Defense (DOD), for which Southwestern markets and transmits the power. Southwestern and the Corps are separately managed and financed, and each maintains their own accounting records. For purposes of financial and operational reporting, the facilities and related operations of Southwestern and the Corps (power purpose) are combined as SWFPS.

The Corps has constructed and operates hydroelectric generating facilities in the states of Arkansas, Missouri, Oklahoma, and Texas. Operating expenses and net assets of multipurpose Corps projects are allocated to power and non-power purposes (primarily recreation and flood control). Only the portion of such project costs and net assets allocated to power are included in the combined financial statements. Southwestern, as designated by the Secretary of Energy, transmits and markets power generated from these hydroelectric generating facilities.

SWFPS is subject to the accounting regulations of the Federal Energy Regulatory Commission (FERC). Accounts are maintained in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) as established by the Financial Accounting Standards Board (FASB), the uniform system of accounts prescribed for electric utilities by the FERC, the accounting practices and standards established by the DOE and DOD, and the requirements of specific legislation and executive directives issued by government agencies. All material intra-entity balances and transactions are eliminated. SWFPS's combined financial statements follow the accounting and reporting guidance contained in FASB Accounting Standards Codification (ASC) Topic 980, *Regulated Operations*. Allocation of costs and revenues to accounting periods for rate-making and regulatory purposes may differ from bases generally applied by non-regulated companies. Such allocations to meet regulatory accounting requirements are considered to be U.S. GAAP for regulated utilities, provided that there is a demonstrable ability to recover any deferred costs in future rates and such costs or revenues are accounted for as regulatory assets or liabilities.

(b) Confirmation and Approval of New Rates

SWFPS is not a public utility within the jurisdiction of the FERC under the Federal Power Act. Under a Delegation Order issued by the Secretary of Energy, the Administrator of Southwestern has the authority to develop power and transmission rates for SWFPS and place the rates into effect on an interim basis. The FERC has the exclusive authority to confirm, approve, and place into effect on a final basis, to remand, or to disapprove rates developed by the Administrator.

The FERC's review is limited to (1) whether the rates are the lowest possible consistent with sound business principles, (2) whether the revenue levels generated are sufficient to recover the costs of producing and transmitting electric energy, including repayment within the period permitted by law, and (3) the assumptions and projections used in developing the rates component. The FERC shall reject decisions of the Administrator only if it finds them to be arbitrary, capricious, or in violation of the law.

As of September 30, 2023 and 2022, there were no revenues subject to a refund.

The rates in effect as of September 30, 2023 are summarized as follows:

The Integrated System rate schedules were placed into effect October 1, 2013 and were confirmed and approved by the FERC on January 9, 2014. These rate schedules incorporated a 4.7% revenue increase for the period October 1, 2013 through September 30 2017, or until superseded by a new rate schedule. These rate schedules have been subsequently extended through September 30, 2019 by the Deputy Secretary of Energy, through September 30, 2021 by the Assistant Secretary, Office of Electricity, through September 30, 2023 by the Administrator, Southwestern, and most recently temporarily extended by the Administrator to remain in effect through September 30, 2024.

The Sam Rayburn Dam project rate was placed into effect January 1, 2016 and was confirmed and approved by the FERC on June 30, 2016. This rate increase incorporated a 7.9% revenue increase for the period January 1, 2016 through September 30, 2019, or until superseded by a new rate schedule. This rate schedule was extended through September 30, 2021 by the Assistant Secretary, Office of Electricity, through September 30, 2023 by the Administrator, Southwestern, and most recently temporarily extended by the Administrator to remain in effect through September 30, 2024.

The Robert Douglas Willis (RD Willis) project rate was placed into effect January 1, 2016 and was confirmed and approved by the FERC on June 15, 2016. The rate increase incorporated an 8.6% revenue increase for the period January 1, 2016 through September 30, 2019, or until superseded by a new rate schedule. This rate schedule was extended through September 30, 2021 by the Assistant Secretary, Office of Electricity, through September 30, 2023 by the Administrator, Southwestern, and most recently temporarily extended by the Administrator to remain in effect through September 30, 2024.

(c) Utility Plant and Depreciation

Utility plant includes items such as dams, spillways, generators, turbines, substations and related components (generating facilities), and transmission lines and related components. Utility plant is stated at original cost, net of contributions by external entities. Property transferred from other government agencies is transferred at net book value. Cost includes direct labor and material, payments to contractors, indirect charges for engineering, supervision and similar overhead items, and an allowance for funds used during construction. The costs of additions and betterments are capitalized. Repairs and minor replacements are charged to operation and maintenance expense. The net cost of utility plant retired, together with removal costs less salvage, is recorded to accumulated depreciation when the property is removed from service.

The policy of Southwestern and the Corps is to move capitalized costs into completed utility plant at the time a project or feature of a project is deemed to be substantially complete. A project is substantially complete when it is providing benefits and services for the intended purpose and is generating project purpose revenue, where applicable.

Depreciation on utility plant is computed on a straight-line basis over the estimated service lives of the various classes of property. Depreciation on utility plant assets is depreciated using the straight-line method over the estimated service lives ranging from 5 to 50 years for transmission assets and 5 to 100 years for generation assets.

Most completed utility plant is recovered through the rates regardless of whether an asset is abandoned, loses value, is disposed of significantly before the end of its estimated useful life or is destroyed. Consequently, the cash flow is not impaired regardless of the condition of the asset.

(d) Cash and Funds Held in Escrow

Cash represents the unexpended balance of funds authorized by Congress, customer advances, and spectrum relocation funds, held at the U.S. Department of the Treasury (U.S. Treasury), and allocations of the amount of funds required to satisfy current hydroelectric power obligations.

Funds held in escrow represents the unexpended balance of cash and cash equivalents held in a bank trust escrow account under alternative financing agreements (note 5 (b)) with certain customers and are restricted specifically to fund operation, maintenance, rehabilitation, and modernization activities at hydroelectric generating facilities of the Corps in SWFPS's marketing region. Under the agreements, funds deposited to the escrow account by customers are credited by Southwestern against accounts receivable for power, energy, and other services sold to the customer. The escrowed funds are transferred to the Corps as agreed to between Southwestern, the Corps, the Southwestern Power Resources Association, and the customers.

(e) Congressional Appropriations

Southwestern and the Corps receive congressional appropriations through the DOE and the DOD, respectively, to finance their operations. A portion of Southwestern's appropriations is offset by the use of receipts collected from the sale of Federal hydroelectric power, resulting in a net zero appropriation. The Corps also receives appropriations to finance construction of its hydroelectric projects. In accordance with the Flood Control Act, Southwestern is responsible for repayment to the Federal government, with interest, of its appropriations, and the portion of congressional appropriations allocated to the Corps for construction and operations of the power projects.

Congressional appropriations received by the Corps are authorized and allocated to individual projects. It is the intent of the Corps' project management to distribute congressional appropriations in amounts approximating estimated current year expenses and to adjust the distribution as necessary within the limits of the transfer authority residing at the district level. Project costs that are not specific to a project purpose are distributed between power and non-power purposes based on project cost allocation.

(f) Operating Revenues

The SWFPS recognizes operating revenues in accordance with ASU No. 2014-09, *Revenue from Contracts with Customers (ASC Topic 606)*, which requires a company to recognize revenue when the company transfers of control of promised goods or services to the customer.

Under the provisions of Topic 606, the SWFPS has elected the following practical expedients:

- Recognize revenue in the amount SWFPS has the right to invoice a customer.
- Apply the standard to a portfolio of contracts with similar characteristics, as the effects of applying the guidance to the portfolio would not differ materially from applying this guidance to the individual contracts.

Operating revenues are recorded on the basis of service rendered. Rates are established under requirements of the Flood Control Act, related legislation and executive departmental directives, and are to provide sufficient revenues to meet all required repayment of system costs, including operation and maintenance expenses less depreciation, interest, and payment to the U.S. Treasury for the Payable to U.S. Treasury in utility plant. Rates are intended to provide for recovery of the investment in transmission and generating facilities not to exceed 50 years from the date placed in service, while operation and maintenance costs and interest on Payable to U.S. Treasury are intended to be recovered annually.

As set forth in note 1(c), assets are being depreciated for financial reporting purposes using the straight-line method over their estimated service lives. Accordingly, annual depreciation charges are not matched with the recovery of the related capital costs and will, in the case of generating facilities, continue beyond the period within which such costs will have been recovered through rates.

While energy and transmission rates are established to recover the costs of operating the power projects, rates are also required to be at the lowest possible level, consistent with sound business principles. Over the life of the power system, accumulated net revenues represent differences between the timing of the recognition of expenses and related revenues, resulting primarily from the difference between the recognition of depreciation and the related recovery of the U.S. Treasury's investment in utility plant. SWFPS is, in effect, a Federal entity, thus at any given time the accumulated net revenues, to the extent available, are committed to the repayment of the Payable to U.S. Treasury.

The practices followed by Southwestern and the Corps are in conformity with the accounting practices and standards established by DOE and DOD and the requirements of specific legislation and executive directives issued by government agencies. Based upon guidelines established in DOE Order RA 6120.2, revenues distributed to the Corps cover annual operating expenses, including interest, with the remainder applied to the unpaid generation and transmission investment.

In addition to providing electric power and energy, Southwestern provides scheduling, billing, and other ancillary services. Southwestern may provide multiple services to any one customer. Services qualify as separate performance obligations under ASU No. 2014-09 with distinguishable rates, terms, and delivery schedules. Services are provided to meet customer load requirements and revenues are recognized when services are provided.

(g) Regulatory Assets and Liabilities (Note 4)

Regulatory assets and liabilities result from rate actions of Southwestern's Administrator and other regulatory agencies. These assets and liabilities arise from specific costs and revenues that would have been included in the determination of net revenue in one period but are deferred until a different period for purposes of developing rates to charge for services, per the requirements of ASC Topic 980, *Regulated Operations*. SWFPS defers transactions as regulatory assets and liabilities so that costs will be recovered during the periods when the costs are scheduled to be paid, which ensures the matching of revenues and expenses. The assets and liabilities below are regulatory in nature:

Deferred Workers' Compensation

Workers' compensation consists of two elements: actuarial liability associated with workers' compensation cases incurred for which additional claims may still be made in the future (future claims) and a liability for expenses associated with actual claims incurred and paid by the Department of Labor (DOL), the program administrator, whom SWFPS must reimburse. DOL, DOE, and DOD determined Southwestern and the Corps' actuarial liability associated with workers' compensation cases. The actuarial liability for future claims is determined using historical benefit payment patterns and the U.S. Treasury discount rates.

The recovery of these future claims is deferred for purposes of the rate-making process until such time as the future claims are actually submitted and paid by the DOL. Therefore, the recognition of the expenses associated with this actuarially determined liability has been recorded as deferred workers' compensation in the combined balance sheets in accordance with ASC Topic 980 to reflect the effects of the rate-making process. SWFPS does not earn a rate of return on the deferred workers' compensation regulatory asset.

Denison Hydropower Water Storage Reallocation

Section 838 of P.L. 99-662 (Section 838) authorized the Corps to reallocate hydropower storage to water supply storage at Lake Texoma, in increments as needed, up to 150,000 acre-feet for users in the State of Texas and up to 150,000 acre-feet for users in the State of Oklahoma. Section 838 directed that the Corps would provide credits to Southwestern equal to the replacement cost of the hydropower lost as a result of the reallocations, and Southwestern would reimburse the preference customers (Denison allottees) for an amount equal to the customers' replacement cost of the hydropower lost as a result of the reallocations.

In fiscal year 2010, the Corps executed water supply contracts for the 150,000 acre-feet of storage authorized for customers in the State of Texas by Section 838. According to a June 2010 agreement between Southwestern and the Corps, the Corps agreed to deposit all cost of storage payments for storage reallocated under Section 838 into the U.S. Treasury and to provide credits in the same amount to the hydropower income account. The total amount received of $58,786,011 was deferred by Southwestern for the provision of the reimbursement to the Denison allottees and Southwestern for future hydropower storage revenues foregone. The reallocation deferral accrued interest at 2.75% and 1.88% of the outstanding balance for the years ended September 30, 2023 and 2022, respectively, based on law, administrative order, or administrative policy. Cumulative interest deferred totaled $21,916,630 and $20,332,635 and the unpaid principal balance deferred totaled $36,293,312 and $38,244,310 for the years ended September 30, 2023 and 2022, respectively.

A September 2010 agreement between Southwestern and the Denison allottees provided the initial hydropower replacement cost as determined by Southwestern and the methodology for providing the reimbursement to the Denison allottees as authorized under Section 838. Beginning with the invoice for the October 2010 service month, reimbursement pursuant to Section 838 began as a credit on the Denison allottees' monthly invoices. Reimbursement to the Denison allottees and distribution of revenue foregone to Southwestern's integrated system will continue as long as there is a reallocation deferred balance of funds, subject to provisions established in the aforementioned agreements between Southwestern and the Corps and between Southwestern and the Denison allottees.

Purchased Power and Banking Exchange Deferral

SWFPS utilizes a separate rate component (purchased power adder) to recover the estimated cost of purchased power based upon the average purchased power costs expected to occur in the future. If the actual expenses of purchased power exceed the revenue generated from this adder, the cost is deferred for future recovery through the rates. Likewise, if the expense is less than the adder, the excess revenue is deferred. From time to time, SWFPS may utilize a separate rate component (adder adjustment) to manage additional purchased power expenses or excess revenues, respectively. The net purchased power deferral accrued interest at 2.75% and 1.88% of the outstanding balance for the years ended September 30, 2023 and 2022, respectively, based on law, administrative order, or administrative policy. Interest expense deferred on the outstanding balance totaled $1,341,075 and $1,157,210 for the years ended September 30, 2023 and 2022, respectively.

SWFPS has arrangements with certain customers in which excess power available on the power system is banked with the customer until needed by the power system and the customer has power available. The power system records a receivable for the power banked at the cost specified in the marketing arrangement, under the provisions of ASC Topic 845, *Nonmonetary Transactions*. The net revenue or expense associated with banking activity is deferred until the power is returned or delivered.

(h) Accounts Receivable

SWFPS's accounts receivable consist generally of receivables for power and energy sold to its customers who are primarily public bodies and cooperatives. SWFPS maintains an allowance for credit losses for estimated losses inherent in its accounts receivables portfolio. SWFPS reviews its allowance for credit losses monthly. Uncollectible balances are fully reserved. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. As of September 30, 2023 and 2022, there is no allowance for uncollectible accounts.

Southwestern's billing methods include net billing. Net billing is an agreement between Southwestern and a customer, whereby the customer's power invoice is credited and the funds received from the sale of power are used to fund transmission and generation activities. Net billing is discussed more fully in note 5(b). Under Southwestern billing methods, purchase and sale transactions are reported "gross" in the combined financial statements.

(i) Concentration of Credit Risk

Financial instruments, which potentially subject SWFPS to credit risk, include accounts receivable for customer purchases of power, transmission, or other products and services. These receivables are primarily with a group of diverse customers that are generally stable and established organizations and do not represent a significant credit risk. Although SWFPS is affected by the business environment of the utility industry, management does not believe a significant risk of loss from a concentration of credit exists.

(j) Interest on Payable to U.S. Treasury

Interest on payable to U.S. Treasury is a cost mandated by the Secretary of Energy and by the FERC. SWFPS computes interest in accordance with DOE Order RA 6120.2, which provides that interest be computed on the remaining investment after revenues have been applied to recovery of costs during the year, any prior year unpaid costs, and also to unpaid Federal investment at the applicable interest rate.

(k) Allowance for Funds Used During Construction

The FERC Uniform System of Accounts defines Allowance for Funds Used During Construction as the net costs for the period of borrowed funds used for construction purposes and a reasonable rate on other funds when so used. While cash is not realized currently from this allowance, it is realized under the rate-making process over the repayment life of the related property through increased revenues resulting from a higher recoverable investment. The interest rates used were 2.75% and 1.88% for the years ended September 30, 2023 and 2022, respectively, based on law, administrative order, or administrative policy.

(l) Retirement Benefits

SWFPS employees participate in one of the following contributory defined benefit plans: the Civil Service Retirement System (CSRS) or Federal Employees Retirement System (FERS). Agency contributions are based on eligible employee compensation and are submitted to benefit program trust funds administered by the Office of Personnel Management (OPM). Based on statutory contribution rates, the fiscal years 2023 and 2022 cost factors under CSRS were 50.4% and 46.2%, respectively, of basic pay. The cost factors under FERS for fiscal years 2023 and 2022 were 22.4% and 19.7%, respectively, of basic pay. The contribution levels, however, are legislatively mandated and do not reflect the current full cost requirements to fund the plans. Costs incurred by OPM on behalf of SWFPS are included as transfers of property and services, net, within the Payable to U.S. Treasury on the combined balance sheets.

Other retirement benefits administered by OPM include the Federal Employees Health Benefits Program (FEHB) and the Federal Employees Group Life Insurance Program (FEGLI). FEHB is calculated at $9,640 and $8,775 per enrolled employee, for fiscal years 2023 and 2022, respectively, and FEGLI is based on 0.02% of basic pay for each employee enrolled in these programs.

In addition to the amounts contributed to the CSRS and FERS as stated previously, SWFPS recorded an expense and related liability for the pension and other postretirement benefits in the combined financial statements of $13,532,433 and $8,369,135 for the years ended September 30, 2023 and 2022, respectively. These amounts reflect the contributions made on behalf of SWFPS by OPM to the benefit program trust funds.

As a Federal agency, all post-retirement activity is managed by OPM, therefore, neither the assets of the plans nor the actuarial data with respect to the accumulated plan benefits relative to Southwestern and the Corps employees are included in this report.

(m) Transfers of Property and Services, Net

Transfers of property and services, net, is a component of total capitalization that represents the cumulative receipt of transfers of assets or costs offset by the cumulative disbursement of revenue transfers. Transfers are recognized upon physical delivery of the asset or performance of the service. Transfers occur between projects, project types, and other Federal entities. Transfers between Southwestern and the Corps eliminate upon combination.

SOUTHWESTERN FEDERAL POWER SYSTEM

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(n) Income Taxes

As agencies of the U.S. Government, Southwestern and the Corps are exempt from all income taxes imposed by any governing body, whether it is a Federal, state, or commonwealth of the United States.

(o) Use of Estimates

The preparation of the combined financial statements in conformity with U.S. GAAP requires management of SWFPS to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Due to uncertainties inherent in the estimation process, actual results could differ from those estimates.

(p) Non-Reimbursable Activities

Non-reimbursable activities for the years ended September 30, 2023 and 2022 consist of the following:

		2023	2022
Non-reimbursable revenues:			
Non-Federal project revenue	$	91,254	47,807
Federal project revenue		449,604	92,266
Escrow interest revenue		8,820,240	2,029,975
Total non-reimbursable revenues	$	9,361,098	2,170,048
Non-reimbursable expenses:			
Non-Federal project expense	$	91,254	47,807
Federal project expense		449,604	92,266
White River Minimum Flows Project expense		4,226,796	3,016,926
Spectrum Relocation Fund expense		4,498,689	758,979
Total non-reimbursable expenses	$	9,266,343	3,915,978

Federal and Non-Federal Projects

Southwestern has agreements with Federal and non-Federal entities to provide services on a cost basis. Non-Federal entities are required to provide advance payment for Southwestern's services. The operating revenues and expenses related to these services are excluded from the rate-making process. A portion of cash and advances for construction in the accompanying combined financial statements relate to these activities.

Escrow Interest Revenue

Interest revenue represents the interest earned on funds held in escrow. These funds due from escrow are authorized specifically to fund operation, maintenance, rehabilitation, and modernization activities at hydroelectric generating facilities of the Corps in SWFPS's marketing region.

White River Minimum Flows Project

In accordance with Section 132 of P.L. 109-103, Southwestern implemented the offset to the minimum flows project in fiscal year 2010. Section 132 provided that losses to Federal hydropower shall be offset by a reduction in the costs allocated to the Federal hydropower purpose. Southwestern determined the Federal hydropower impacts to include lost on-peak energy and capacity, lost off-peak energy, increased costs due to dissolved oxygen impacts, and increased maintenance costs at Bull Shoals. This activity is non-reimbursable through the rate-making process.

Spectrum Relocation Fund

In December 2004, the U.S. Congress passed and the President signed the Commercial Spectrum Enhancement Act (CSEA, Title II of P.L. 108-494), creating the Spectrum Relocation Fund to streamline the relocation of Federal systems from existing spectrum bands to accommodate commercial use by facilitating reimbursement to affected agencies of relocation costs. In fiscal years 2023, 2012, 2009, and 2007, Southwestern received $4,000,000, $17,000,000, $17,730,000, and $8,091,360, respectively, in spectrum relocation funds, as approved by the Office of Management and Budget, and as reported to the Congress. Expenses incurred represent labor, construction contracts, travel, and other administrative costs. This activity is non-reimbursable through the rate-making process and is recorded as congressional appropriations directly to accumulated net revenues within the combined statements of changes in capitalization.

(q) Derivative and Hedging Activities

Southwestern analyzes derivative financial instruments under ASC Topic 815, *Derivatives and Hedging*. This standard requires that all derivative instruments, as defined by ASC Topic 815, be recorded on the combined balance sheets at fair value, unless exempted. Changes in a derivative instrument's fair value must be recognized currently in the combined statement of revenues and expenses, unless the derivative has been designated in a qualifying hedging relationship. The application of hedge accounting allows a derivative instrument's gains and losses to offset related results of the hedged item in the combined statements of revenues and expenses to the extent effective. ASC Topic 815 requires that the hedging relationship be highly effective and that an organization formally designate a hedging relationship at the inception of the contract to apply hedge accounting.

Southwestern enters into contracts for the sale of electricity for use in its business operations. ASC Topic 815 requires Southwestern to evaluate these contracts to determine whether the contracts are derivatives. Certain contracts that literally meet the definition of a derivative may be exempted from ASC Topic 815 as normal purchases or normal sales. Normal purchases and sales are contracts that provide for the purchase or sale of something other than a financial instrument or derivative instrument that will be delivered in quantities expected to be used or sold over a reasonable period of time in the normal course of business. Contracts that meet the requirements of normal purchases or sales are documented and exempted from the accounting and reporting requirements of ASC Topic 815.

Southwestern's policy is to fulfill all derivative and hedging contracts by providing power to a third party as provided for in each contract. Southwestern's policy does not authorize the use of derivative or hedging instruments for speculative purposes such as hedging electricity pricing fluctuations beyond Southwestern's estimated capability to deliver power. Accordingly, Southwestern evaluates all of its contracts to determine if they are derivatives and, if applicable, to ensure that they qualify and meet the normal purchases and normal sales designation requirements under ASC Topic 815. Normal purchases and normal sales contracts are accounted for as executory contracts as required under U.S.

GAAP. As of September 30, 2023 and 2022, Southwestern has no contracts accounted for at fair value as all derivatives qualify as normal purchases and normal sales.

(r) Recent Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, *Leases* (Topic 842), which requires the recognition of lease assets and lease and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. SWFPS adopted Topic 842 as of October 1, 2022, using the non-comparative transition option pursuant to ASU 2018-11.

SWFPS elected the package of practical expedients permitted under the transition guidance within the new standard which, among other things, (i) allowed SWFPS to carry forward the historical lease classification; (ii) did not require SWFPS to reassess whether any expired or existing contracts are or contain leases under the new definition of a lease; and (iii) did not require SWFPS to reassess whether previously capitalized initial direct costs for any existing leases would qualify for capitalization under Topic 842. SWFPS also elected the practical expedients related to (i) use of risk-free discount rate for the entire population of their leases when an incremental borrowing rate is not readily available; (ii) short-term lease exemption, which allows SWFPS to not recognize leases with the total lease term of 12 months or less on the balance sheet; and (iii) non-separation of lease and non-lease components (such as common area maintenance) and treating them as a single lease component.

Adoption of Topic 842 did not result in the recording of operating lease right-of-use assets or operating lease liabilities, or finance lease assets and finance lease liabilities, as of October 1, 2022. Further, no cumulative adjustment to accumulated net revenues was required as of October 1, 2022, for the impact of the new accounting standard. SWFPS's financial position for reporting periods beginning on or after October 1, 2022, is presented under the new guidance, as discussed above. The standards did not materially impact the combined balance sheets, statements of revenues and expenses, or cash flows as of and for the year ended September 30, 2023.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments*, which requires a financial asset (or a group of financial assets) measured at amortized cost to be presented at the net amount expected to be collected. The ASU is intended to improve financial reporting by requiring earlier recognition of credit losses on certain financial assets including trade and financing receivables. The ASU replaces the current incurred loss impairment model that recognizes losses when a probable threshold is met with a requirement to recognize lifetime expected credit losses immediately when a financial asset is originated or purchased. Additionally, from 2016 through 2023, the FASB issued additional related ASUs that provide further guidance and clarification and become effective for the Company upon the adoption of ASU 2016-13.

(2) Disaggregated Revenue

Disaggregated revenues as of September 30, 2023 and 2022 consists of the following:

		2023	2022
Disaggregated revenues:			
Sale of Federal electric power	$	172,399,322	176,302,039
Non-Federal transmission services		17,718,033	16,349,394
Ancillary services		680,394	685,639
Other revenues		16,473,605	21,086,293
Total operating revenue before deferrals	$	207,271,354	214,423,365

Revenue from Contracts with Customers

Southwestern provides wholesale Federal electric power (energy and capacity) to preference power customers under long-term firm and non-firm contracts. Southwestern establishes power rates for these contracts in a formal rate setting process. Excess energy is sold at established power rates. Federal electric power revenues are recognized over time as the customer receives and consumes the benefits. Federal electric power revenues are billed monthly based on meter readings and contracted allocations and estimated unbilled electric power revenues are accrued at the end of each reporting period. Revenues can vary from period to period due to hydropower plant availability, hydrological conditions, and customer usage requirements.

Non-Federal transmission service revenues consist primarily of revenue for transmission of non-Federal power on Southwestern's transmission system. Transmission rates are established through a formal rate setting process and revenues are recognized over time as capacity and electric transmission is made available. Transmission services are billed monthly and estimated unbilled transmission services are accrued at the end of each reporting period.

Ancillary services ensure transmission grid reliability and include items such as scheduling, system control, dispatch, balancing reserves and other services. Ancillary revenue is recognized over time as services are provided. Ancillary services are billed monthly and estimated unbilled ancillary services are accrued at the end of the reporting period.

Other revenues consist of headwater benefits, hydropower benefits foregone revenues and miscellaneous revenues from the Corps attributable to the power function, as well as market participant agreement revenues for the sale of power from Blakely Mountain and DeGray into the Midcontinent Independent System Operator (MISO) market plus miscellaneous revenues for Southwestern. These revenues are recognized upon receipt.

SOUTHWESTERN FEDERAL POWER SYSTEM

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(3) Utility Plant

Utility plant as of September 30, 2023 and 2022 consists of the following:

Generating facilities	$ 1,747,874,120	1,681,729,858
Transmission facilities	526,396,407	519,816,115
	2,274,270,527	2,201,545,973
Less accumulated depreciation	(1,046,163,370)	(1,003,859,401)
Construction work in progress:		
Generating facilities	85,942,613	100,026,139
Transmission facilities	39,577,063	36,732,197
	125,519,676	136,758,336
Net utility plant	$ 1,353,626,833	1,334,444,908

In accordance with FERC guidelines, SWFPS excludes contributed plant within the combined balance sheets to eliminate the impact on power rates. As of September 30, 2023 and 2022, contributed plant, net, used in SWFPS's operations totaled $23,003,072.

(4) Regulatory Assets and Liabilities

Regulatory assets and liabilities as of September 30, 2023 and 2022 consist of the following:

	2023	2022
Regulatory assets:		
Deferred workers' compensation	$ 7,926,721	11,969,419
Regulatory liabilities:		
Purchased power and banking exchange deferral	$ 40,369,954	63,129,246
Hydropower water storage reallocation deferral	58,209,942	58,576,945
Total	$ 98,579,896	121,706,191

Southwestern's purchased power and banking exchange deferral account represents the deferral of net revenues or expenses associated with net purchased power and banking exchange activities as follows:

		Purchased power and banking exchange deferral
September 30, 2021	$	(70,475,290)
Purchased power adder revenue		(14,378,884)
Purchased power expense		22,952,969
Net banking exchange		(17,145)
Net purchased power and banking exchange deferral		8,556,940
Interest on deferred activities and other		(1,210,896)
September 30, 2022		(63,129,246)
Purchased power adder revenue		(14,380,347)
Purchased power expense		33,914,654
Value energy banking agreement		4,362,669
Net banking exchange		168,533
Net purchased power and banking exchange deferral		24,065,509
Interest on deferred activities and other		(1,306,217)
September 30, 2023	$	(40,369,954)

(5) Financing Sources

SWFPS's financing sources include annual appropriations, Federal power receipts, and alternative financing arrangements to fund its operations.

(a) Payable to U.S. Treasury

Construction and operation of Southwestern's transmission system and the Corps' generating facilities and operations are financed through congressional appropriations. The exceptions are capital assets and maintenance activities funded through the alternative financing arrangements and the funding by non-Federal parties of the construction of the RD Willis project. The U.S. Government's investment in each generating project and each year's investment in the transmission system are to be repaid to the U.S. Treasury over a period not to exceed 50 years from the time the facility is placed in service. There is no requirement for repayment of a specific amount on an annual basis.

Annual revenues are first applied to the current year operating expenses (less depreciation) and interest expense. All annual amounts for such expenses have been paid through fiscal year 2023. Remaining revenues are to be first applied to repayment of operating deficits (which include all expenses except depreciation), if any, and then to repayment of the Payable to U.S. Treasury. To the extent possible, while still complying with the repayment period established for each increment of investment and unless otherwise required by legislation, repayment of the investment is to be accomplished by a repayment of the highest interest-bearing investment first. Interest rates applied to the unamortized investment of the U.S. Government in Southwestern's transmission system and the Corps' hydroelectric generating facilities range from 1.63% to 3.13% for unpaid facilities in service prior to and including fiscal year 2023 (2.75%). The rates have been set by law, by administrative order pursuant to law, or by administrative policies using the U.S. Senate Document No. 97 formula for the fiscal year during which the appropriations were requested.

(b) Alternative Financing

Due to fluctuations in the amount of annual appropriations received to fund operations, maintenance, rehabilitation, and modernization of SWFPS facilities, SWFPS has established an alternative financing program under reimbursable authority regulations. Under agreements with customers to finance projects, which benefit SWFPS, funds received from the sale of power are net billed, allowing a portion of the funds to be utilized to finance agreed-upon projects. Under the agreements with certain customers, alternative financing restricted specifically to fund operation, maintenance, rehabilitation, and modernization activities at the hydroelectric generating facilities is held in escrow (note 1(d)).

(6) Commitments and Contingencies

(a) General

Southwestern sells its marketable power to customers under long-term power sales contracts of 15 years, the majority of which require Southwestern to provide 1,200 kilowatt hours per kilowatt of peaking contract demand per year, subject to scheduling constraints outlined in each customer's contract. If sufficient power is unavailable to Southwestern from Corps' hydroelectric facilities to meet these commitments, Southwestern may be required to purchase power from other sources to meet these commitments. The cost to purchase such power is recovered through the purchased power adder discussed more fully in note 1(g).

(b) Legal

SWFPS has exposure to certain claims and legal actions arising in the ordinary course of business. In February 2023, Southwestern received notification from the Sam Rayburn Municipal Power Agency (SRMPA) of its intentions to terminate its power sales contract effective April 2023 relating to the RD Willis powerhouse. In fiscal year 2023, SWFPS reached an agreement with SRMPA whereupon SRMPA's participation in the RD Willis power sales contract was terminated and SRMPA agreed to continue to provide station service power to the RD Willis powerhouse for a period of time. As part of the agreement, the U.S. Treasury Judgment Fund remitted payment of approximately $1 million to SRMPA; the SWFPS is not required to reimburse the U.S. Treasury for this payment. However, the termination of SRMPA's participation in the RD Willis power sales contract impacts payments to the U.S. Treasury as reimbursement for outstanding project costs until RD Willis is again marketed to a power sales customer.

As of September 30, 2022, SWFPS accrued legal liabilities of $3,474,420 where additional capital costs were determined to be probable based on a settlement reached as a subsequent event in March 2023. In fiscal year 2023, the Corps remitted payment on the settlement and the remaining liability is $0 as of September 30, 2023.

(7) Leases

Southwestern has a 191-month Occupancy Agreement for office space with the General Services Administration (GSA), which commenced January 19, 2018 and is scheduled to terminate December 31, 2033. The lease agreement between the GSA and the building owner is for a 20-year term, 10-year firm term for the first 10 years and the option to terminate during the second 10-year-term, which commenced on January 1, 2014 and ends on December 31, 2033.

In August 2019, Southwestern purchased a new headquarters building in Tulsa, Oklahoma, with a fiscal year 2024 target move-in date. In accordance with the Occupancy Agreement, Southwestern may relinquish space upon four months' notice to GSA and will not be obligated to make any additional payments.

As of September 30, 2023, expected future minimum lease payments, given the termination of the Occupancy Agreement by October 31, 2024, total $379,500 and $32,600 for fiscal years 2024 and 2025, respectively.

Rent expense for operating leases during the years ended September 30, 2023 and 2022 was $369,754 and $522,218, respectively.

(8) Related Parties

As components of the DOE and the DOD, these departments are considered related parties to Southwestern and the Corps. Southwestern has certain agreements with DOD components to provide electric power, transmission services, and other services. As of September 30, 2023 and 2022, amounts outstanding in accounts receivable relating to DOD components totaled $280,467 and $277,948, respectively. For the years ended September 30, 2023 and 2022, total operating revenues earned from DOD components totaled $3,721,932 and $3,957,335, respectively.

(9) Corrections Related to Plant in Service Retirement Losses and Land Depreciation

As disclosed in note 1(c), the net cost of utility plant retired, together with removal costs less salvage value, is recognized as an expense on the statements of revenues and expenses. In addition, depreciation on utility plant is computed on a straight-line basis over the estimated service lives of the various classes of property.

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During fiscal year 2023, the SWFPS corrected these amounts by expensing $28,778,685 in retirement losses previously recorded on the combined balance sheets and reversing $2,889,147 in depreciation expense previously recognized against land. The following table presents the effects of the immaterial corrections to the combined balance sheet, capitalization, statement of revenues and expenses, and cash flows as of and for the year ended September 30, 2022:

		As previously reported	Adjustments	As adjusted
Balance sheet:				
Accumulated depreciation	$	(977,696,863)	(25,889,538)	(1,003,586,401)
Net utility plant		1,360,334,446	(25,889,538)	1,334,444,908
Total assets		2,279,682,481	(25,889,538)	2,253,792,943
Accumulated net revenues		762,287,539	(25,889,538)	736,398,001
Total capitalization		2,118,016,212	(25,889,538)	2,092,126,674
Total liabilities and capitalization		2,279,682,481	(25,889,538)	2,253,792,943
Statement of changes in capitalization:				
Total capitalization as of September 30, 2021	$	2,014,108,497	(25,268,055)	1,988,840,442
Net revenues for the year ended September 30, 2022		22,723,564	(621,483)	22,102,081
Total capitalization as of September 30, 2022		2,118,016,212	(25,889,538)	2,092,126,674
Statement of revenues and expenses:				
Operation and maintenance	$	112,884,069	678,547	113,562,616
Depreciation and amortization		54,147,911	(57,064)	54,090,847
Total operating expenses		195,850,052	621,483	196,471,535
Net operating revenues		29,300,301	(621,483)	28,678,818
Net revenues		22,723,564	(621,483)	22,102,081
Statement of cash flows:				
Net revenues	$	22,723,564	(621,483)	22,102,081
Depreciation and amortization		54,147,911	(57,064)	54,090,847
Loss on retirement of plant in service		—	678,547	678,547

Corrections impacting the supplementary information in schedules 1 through 4 have also been revised accordingly.

(10) Subsequent Events

SWFPS has evaluated subsequent events from the balance sheet date through July 19, 2024 the date the combined financial statements were available to be issued, and no subsequent events were identified.

Schedule 1

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Balance Sheet Data

September 30, 2023

Assets		Southwestern	Corps	Total
Plant in service	$	526,396,407	1,747,874,120	2,274,270,527
Accumulated depreciation		(315,206,126)	(730,957,244)	(1,046,163,370)
Construction work in progress		39,577,063	85,942,613	125,519,676
Net utility plant		250,767,344	1,102,859,489	1,353,626,833
Cash		342,656,277	464,988,882	807,645,159
Funds held in escrow		126,136,461	44,235,751	170,372,212
Accounts receivable		15,980,900	498,924	16,479,824
Materials and supplies, at average cost		3,707,904	68,912	3,776,816
Banking exchange receivables		75,642	—	75,642
Deferred workers' compensation		938,883	6,987,838	7,926,721
Other assets		68,973	—	68,973
Total assets	$	740,332,384	1,619,639,796	2,359,972,180
Liabilities and Capitalization				
Liabilities:				
Accounts payable and accrued liabilities	$	10,552,765	8,159,833	18,712,598
Advances for construction		4,408,257	—	4,408,257
Accrued workers' compensation		1,138,133	7,181,461	8,319,594
Purchased power and banking exchange deferral		40,369,954	—	40,369,954
Hydropower water storage reallocation deferral		58,209,942	—	58,209,942
Total liabilities		114,679,051	15,341,294	130,020,345
Capitalization:				
Payable to U.S. Treasury		501,540,347	976,104,811	1,477,645,158
Accumulated net revenues		124,112,986	628,193,691	752,306,677
Total capitalization		625,653,333	1,604,298,502	2,229,951,835
Total liabilities and capitalization	$	740,332,384	1,619,639,796	2,359,972,180

See accompanying independent auditors' report.

Schedule 1

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Balance Sheet Data

September 30, 2022

Assets		Southwestern	Corps	Total
Plant in service	$	519,816,115	1,681,729,858	2,201,545,973
Accumulated depreciation		(302,269,425)	(701,589,976)	(1,003,859,401)
Construction work in progress		36,732,197	100,026,139	136,758,336
Net utility plant		254,278,887	1,080,166,021	1,334,444,908
Cash		322,771,439	370,873,098	693,644,537
Funds held in escrow		125,064,224	55,069,502	180,133,726
Accounts receivable		24,035,288	449,870	24,485,158
Materials and supplies, at average cost		3,888,126	68,912	3,957,038
Banking exchange receivables		4,233,882	—	4,233,882
Deferred workers' compensation		2,908,637	9,060,782	11,969,419
Other assets		924,275	—	924,275
Total assets	$	738,104,758	1,515,688,185	2,253,792,943
Liabilities and Capitalization				
Liabilities:				
Accounts payable and accrued liabilities	$	10,619,576	14,122,896	24,742,472
Advances for construction		2,471,234	—	2,471,234
Accrued workers' compensation		3,451,423	9,294,949	12,746,372
Purchased power and banking exchange deferral		63,129,246	—	63,129,246
Hydropower water storage reallocation deferral		58,576,945	—	58,576,945
Total liabilities		138,248,424	23,417,845	161,666,269
Capitalization:				
Payable to U.S. Treasury		472,005,614	883,723,059	1,355,728,673
Accumulated net revenues		127,850,720	608,547,281	736,398,001
Total capitalization		599,856,334	1,492,270,340	2,092,126,674
Total liabilities and capitalization	$	738,104,758	1,515,688,185	2,253,792,943

See accompanying independent auditors' report.

Schedule 2

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Changes in Capitalization Data

Years ended September 30, 2023 and 2022

	Southwestern payable to U.S. Treasury	Southwestern accumulated net revenues (deficit)	Southwestern total capitalization	Corps payable to U.S. Treasury	Corps accumulated net revenues (deficit)	Corps total capitalization	Total capitalization
Total capitalization as of September 30, 2021	$ 474,975,372	99,720,531	574,695,903	799,569,150	614,575,389	1,414,144,539	1,988,840,442
Additions:							
Congressional appropriations	10,400,000	—	10,400,000	99,103,347	—	99,103,347	109,503,347
Interest on payable to U.S. Treasury and other	572,827	—	572,827	10,222,854	—	10,222,854	10,795,681
Transfers of property and services, net	(88,321,531)	—	(88,321,531)	91,823,411	—	91,823,411	3,501,880
Total additions to capitalization	(77,348,704)	—	(77,348,704)	201,149,612	—	201,149,612	123,800,908
Deductions:							
Payments to U.S. Treasury	74,378,946	—	74,378,946	(116,995,703)	—	(116,995,703)	(42,616,757)
Total deductions to capitalization	74,378,946	—	74,378,946	(116,995,703)	—	(116,995,703)	(42,616,757)
Net revenues for the year ended September 30, 2022	—	28,130,189	28,130,189	—	(6,028,108)	(6,028,108)	22,102,081
Total capitalization as of September 30, 2022	472,005,614	127,850,720	599,856,334	883,723,059	608,547,281	1,492,270,340	2,092,126,674
Additions:							
Congressional appropriations	10,608,000	4,000,000	14,608,000	133,139,928	—	133,139,928	147,747,928
Interest on payable to U.S. Treasury and other	(744,168)	—	(744,168)	8,190,911	—	8,190,911	7,446,743
Transfers of property and services, net	(88,058,246)	—	(88,058,246)	94,992,189	—	94,992,189	6,933,943
Total additions to capitalization	(78,194,414)	4,000,000	(74,194,414)	236,323,028	—	236,323,028	162,128,614
Deductions:							
Payments to U.S. Treasury	107,729,147	—	107,729,147	(143,941,276)	—	(143,941,276)	(36,212,129)
Total deductions to capitalization	107,729,147	—	107,729,147	(143,941,276)	—	(143,941,276)	(36,212,129)
Net revenues for the year ended September 30, 2023		(7,737,734)	(7,737,734)		19,646,410	19,646,410	11,908,676
Total capitalization as of September 30, 2023	$ 501,540,347	124,112,986	625,653,333	976,104,811	628,193,691	1,604,298,502	2,229,951,835

See accompanying independent auditors' report.

Schedule 3

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Revenues and Expenses Data

Year ended September 30, 2023

	Southwestern	Corps	Total
Operating revenues:			
Sales of electric power	$ 172,957,712	—	172,957,712
Transmission and other operating revenues	31,468,066	2,845,576	34,313,642
Total operating revenues before deferrals	204,425,778	2,845,576	207,271,354
Net purchased power and banking exchange deferral	19,709,994	—	19,709,994
Revenue distributed to Corps	(136,309,036)	136,309,036	—
Total operating revenues	87,826,736	139,154,612	226,981,348
Non-reimbursable revenues	7,889,848	1,471,250	9,361,098
Total revenues	95,716,584	140,625,862	236,342,446
Operating expenses:			
Operation and maintenance	43,212,012	84,449,117	127,661,129
Purchased power and banking exchange	35,788,165	—	35,788,165
Depreciation and amortization	13,954,966	30,220,190	44,175,156
Transmission service charges by others	—	—	—
Non-reimbursable expenses	9,266,343	—	9,266,343
Total operating expenses	102,221,486	114,669,307	216,890,793
Net operating revenues (losses)	(6,504,902)	25,956,555	19,451,653
Interest expense:			
Interest on payable to U.S. Treasury and other	2,180,901	8,190,912	10,371,813
Allowance for funds used during construction	(948,069)	(1,880,767)	(2,828,836)
Net interest expense	1,232,832	6,310,145	7,542,977
Net revenues (losses)	$ (7,737,734)	19,646,410	11,908,676

See accompanying independent auditors' report.

Schedule 3

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Revenues and Expenses Data

Year ended September 30, 2022

	Southwestern	Corps	Total
Operating revenues:			
Sales of electric power	$ 176,992,735	—	176,992,735
Transmission and other operating revenues	34,584,727	2,845,903	37,430,630
Total operating revenues before deferrals	211,577,462	2,845,903	214,423,365
Net purchased power and banking exchange deferral	8,556,940	—	8,556,940
Revenue distributed to Corps	(110,229,178)	110,229,178	—
Total operating revenues	109,905,224	113,075,081	222,980,305
Non-reimbursable revenues	1,379,321	790,727	2,170,048
Total revenues	111,284,545	113,865,808	225,150,353
Operating expenses:			
Operation and maintenance	37,935,088	75,627,528	113,562,616
Purchased power and banking exchange	24,869,181	—	24,869,181
Depreciation and amortization	14,626,457	39,464,390	54,090,847
Transmission service charges by others	32,913	—	32,913
Non-reimbursable expenses	3,915,978	—	3,915,978
Total operating expenses	81,379,617	115,091,918	196,471,535
Net operating revenues (losses)	29,904,928	(1,226,110)	28,678,818
Interest expense:			
Interest on payable to U.S. Treasury and other	2,825,754	10,222,854	13,048,608
Allowance for funds used during construction	(1,051,015)	(5,420,856)	(6,471,871)
Net interest expense	1,774,739	4,801,998	6,576,737
Net revenues (losses)	$ 28,130,189	(6,028,108)	22,102,081

See accompanying independent auditors' report.

Schedule 4

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Cash Flows Data

Year ended September 30, 2023

	Southwestern	Corps	Total
Cash flows from operating activities:			
Net revenues (losses)	$ (7,737,734)	19,646,410	11,908,676
Adjustments to reconcile net revenues to net cash provided by (used in) operating activities:			
Revenue distributed to Corps	136,309,036	(136,309,036)	—
Depreciation and amortization	13,954,966	30,220,190	44,175,156
Loss on retirement of plant in service	383,378	547,487	930,865
Benefit expense paid by other Federal agencies	2,010,445	11,521,988	13,532,433
Interest on payable to U.S. Treasury and other	1,232,832	6,310,145	7,542,977
Deferred workers' compensation	1,969,754	2,072,944	4,042,698
(Increase) decrease in assets:			
Accounts receivable	8,054,388	(49,054)	8,005,334
Materials and supplies	180,222	—	180,222
Banking exchange receivables	4,158,240	—	4,158,240
Other assets	855,302	—	855,302
Increase (decrease) in liabilities:			
Accounts payable and accrued liabilities	(66,811)	(5,963,063)	(6,029,874)
Accrued workers' compensation	(2,313,290)	(2,113,488)	(4,426,778)
Purchased power and banking exchange deferral	(24,100,367)	—	(24,100,367)
Advances for construction	1,937,023	—	1,937,023
Net cash provided by (used in) operating activities	136,827,384	(74,115,477)	62,711,907
Cash flows used in investing activities:			
Additions to utility plant	(9,878,732)	(51,580,379)	(61,459,111)
Cash flows from financing activities:			
Congressional appropriations	14,608,000	133,139,928	147,747,928
Payments to U.S. Treasury	107,729,147	(143,941,276)	(36,212,129)
Revenue distributed to Corps	(136,309,036)	136,309,036	—
Transfers of property and services, net	(90,068,691)	83,470,201	(6,598,490)
Hydropower water storage reallocation deferral	(1,950,997)	—	(1,950,997)
Net cash (used in) provided by financing activities	(105,991,577)	208,977,889	102,986,312
Net increase in cash and funds held in escrow	20,957,075	83,282,033	104,239,108
Cash and funds held in escrow, beginning of year	447,835,663	425,942,600	873,778,263
Cash and funds held in escrow, end of year	$ 468,792,738	509,224,633	978,017,371
Supplemental cash flow information:			
Interest charged to construction	$ 948,069	1,880,767	2,828,836
Interest deferred on regulatory liabilities	2,925,068	—	2,925,068
Transfer of construction work in progress to plant in service	5,827,311	48,413,589	54,240,900

See accompanying independent auditors' report.

Schedule 4

SOUTHWESTERN FEDERAL POWER SYSTEM

Combining Schedule of Cash Flows Data

Year ended September 30, 2022

		Southwestern	Corps	Total
Cash flows from operating activities:				
Net revenues (losses)	$	28,130,189	(6,028,108)	22,102,081
Adjustments to reconcile net revenues to net cash provided by (used in) operating activities:				
Revenue distributed to Corps		110,229,178	(110,229,178)	—
Depreciation and amortization		14,626,457	39,464,390	54,090,847
Loss on retirement of plant in service		678,547	—	678,547
Benefit expense paid by other Federal agencies		1,416,864	6,952,271	8,369,135
Interest on payable to U.S. Treasury and other		1,774,739	4,801,998	6,576,737
Deferred workers' compensation		(510,470)	(3,447,400)	(3,957,870)
(Increase) decrease in assets:				
Accounts receivable		3,326,559	226,639	3,553,198
Materials and supplies		(647,701)	92,103	(555,598)
Banking exchange receivables		(451)	—	(451)
Other assets		(327,790)	—	(327,790)
Increase (decrease) in liabilities:				
Accounts payable and accrued liabilities		855,965	1,439,324	2,295,289
Accrued workers' compensation		558,165	3,454,176	4,012,341
Purchased power and banking exchange deferral		(8,503,254)	—	(8,503,254)
Advances for construction		949,249	—	949,249
Net cash provided by (used in) operating activities		152,556,246	(63,273,785)	89,282,461
Cash flows used in investing activities:				
Additions to utility plant		(19,476,233)	(54,560,015)	(74,036,248)
Cash flows from financing activities:				
Congressional appropriations		10,400,000	99,103,347	109,503,347
Payments to U.S. Treasury		74,378,946	(116,995,703)	(42,616,757)
Revenue distributed to Corps		(110,229,178)	110,229,178	—
Transfers of property and services, net		(89,738,395)	84,871,140	(4,867,255)
Hydropower water storage reallocation deferral		(1,914,166)	—	(1,914,166)
Net cash (used in) provided by financing activities		(117,102,793)	177,207,962	60,105,169
Net increase in cash and funds held in escrow		15,977,220	59,374,162	75,351,382
Cash and funds held in escrow, beginning of year		431,858,443	366,568,438	798,426,881
Cash and funds held in escrow, end of year	$	447,835,663	425,942,600	873,778,263
Supplemental cash flow information:				
Interest charged to construction	$	1,051,015	5,420,856	6,471,871
Interest deferred on regulatory liabilities		2,252,928	—	2,252,928
Transfer of construction work in progress to plant in service		12,659,380	158,785,738	171,445,118

See accompanying independent auditors' report.

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