Financial Highlights

Pursuant to the requirements of 31 U.S.C. 3515(b), VA's principal financial statements have been prepared to report the financial position and results of operations of the Department. Deloitte & Touche, LLP, performed the audit of the statements under the direction of the Office of Inspector General. While the statements have been prepared from the books and records of the Department in accordance with generally accepted accounting principles for federal entities and the formats prescribed by the Office of Management and Budget, they are, in addition to the financial reports, used to monitor and control budgetary resources that are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

VA received an unqualified opinion on the Department's financial statements for 2006 and 2005 from the external auditors, Deloitte & Touche, LLP, continuing the tradition of financial management excellence first achieved in 1999. As a result of its audit work, Deloitte & Touche, LLP reported three reportable conditions, all of which are also material weaknesses. VA continues to make significant progress remediating these material weaknesses.

VA programs operated at a net cost of $101.5 billion in 2006 compared with $263.4 billion in 2005. The calculation of the actuarial liability for future years' veterans' compensation, which increased by $31.2 billion during 2006 and increased by $197.8 billion during 2005, heavily impacts each year's cost. The actuarial liability for future years' veterans' compensation increased in 2006 due to an increase in the rate of the new compensation awards and an increase in the average disability rating for veterans receiving compensation benefits. Excluding the change in this actuarial liability from the net cost would result in an adjusted net cost for VA's programs of $70.3 billion and $65.6 billion for 2006 and 2005, respectively. The majority of the change applies to three programs--medical care increased $0.7 billion, compensation increased $2.3 billion, and loan guarantee increased $0.6 billion.

An examination of assets and liabilities reported on VA's balance sheets reveals two lines with changes greater than $1 billion. This change is an increase in the Federal Employee and Veterans Benefits Liabilities, which is related to the decrease in the actuarial liability for future compensation payments. It should be noted that the future cash flows to liquidate the Federal Employee and Veterans Benefits Liability are not supported by any identifiable assets, as they are anticipated to be funded from the future general revenues of the U.S. Government. The change in the compensation liabilities is the most significant component of the change in Cumulative Results of Operations. The other change is a decrease of $1.2 billion in Federal debt.

Medical Care collections continue to improve. In 2006, collections totaled nearly $2 billion, which builds on the $1.8 billion collected in 2005, and is a significant increase over the 2004 total of $1.7 billion. VA plans to continue to increase these collections, reaching $2.2 billion in 2007.

In the area of debt management, VA exceeded the goals established with the Department of the Treasury (Treasury) for the Treasury Offset Program (TOP) and the cross-servicing program. VA referred $331.7 million (99 percent) of eligible debt to Treasury for offset under TOP. Under the cross-servicing program, VA referred $168.4 million (97 percent) of eligible debt to Treasury for collection.

During 2006 the Department aggressively used the governmentwide commercial purchase card program. Nearly 4 million transactions were processed, representing $2.1 billion in purchases. The electronic billing and payment process for centrally billed accounts earned VA over $37 million in refunds, compared to $35 million during 2005. These refunds are returned to VA entities for use in veterans programs. The increase in refunds is attributed to expanded use of the card and normal increases in the cost of products purchased.

Throughout 2006 VA continued to make operational enhancements, which resulted in improvements in interest paid, discounts earned, and audit recoveries. Interest improvements occurred largely because the Department centralized VHA-certified payments at the Financial Services Center (FSC), while the percentage of discounts earned increased because of operational improvements implemented at the FSC and VA's National Acquisition Center. Interest paid as a percentage of principal remained virtually unchanged from 2005 levels and the percentage of discounts earned improved by 2.3 percent compared to 2005.

In 2006 the FSC's audit recovery program recovered improper payments and unapplied vendor credits totaling nearly $5.1 million. Since the program's inception in 2001, VA has recovered $18.3 million in improper payments and cancelled another $21.1 million in improper payments before making payment. VA awarded a recovery audit contract in December 2000 to review past payments by VA's Health Administration Center (HAC) for hospital care. In 2006, the National Audit Recovery Program recovered $9.8 million. The HAC Collections Program collected an additional $8.3 million.

Additional focus on operational oversight continued in 2006 due to the elevation of this reportable condition to a material weakness. During 2006, VHA formed a task force to perform a root cause analysis of issues that contributed to the material weakness. Seven areas were identified: Leadership Accountability and Alignment; Ethical Issues; Internal Control Monitoring Process; Directive, Policies and Procedures; Human Resource Issues; Medical Care Collections Fund Receivables; and Non-MCCF Receivables. Work groups are now in place to address the issues. A new VHA National Leadership Board committee, the Business Process Improvement Committee, has been established to track not only the issues raised by the root cause analysis task force and work groups, but also all business operations, to ensure that best business practices, ethical decisions, and internal controls are in place at all VHA facilities. Additionally, in December 2006, VHA is conducting a national training conference targeted to VHA field accounting and fiscal staff to address issues contributing to the material weakness and corrective actions.

VHA also continues to monitor and improve reports, such as the Financial Indicators Report, that monitor facility operations on a monthly basis. In 2006 a Desk Guide for Management Oversight of Financial Operations, designed for senior medical center management, was released. The first two sections addressed reconciliations and follow-up of aging accounts. In early FY 2007, additional sections on purchase card and agent cashier activities will be released.

Finally, in August 2006 at the Senior Management Conference, VHA held multiple sessions on financial management to give all attendees an opportunity to attend one of the sessions. VHA is actively engaged in addressing financial management at all levels of management and in all activities that have direct or indirect impact on financial records.

VBA is continuing its effort to centralize or consolidate finance functions, with a direct line to VBA's CFO. In 2006, VBA completed centralization of all regional office administrative accounting functions to one location. VBA also completed centralization/consolidation studies for the Committee on Waivers & Compromises (COWC) and Chapter 31 payment process. Consolidation of the COWC function will begin in early 2007 and for the Chapter 31 payment process in late 2007 or early 2008. A joint VHA/VBA team is developing a plan to transfer finance functions related to automobile adaptive equipment to VHA.

NCA implemented its plans to establish one site for each of the primary activities -- finance, acquisition, and asset management. Currently, the greatest proportion of contracting, finance, and accounting support for national cemeteries is provided by a VA medical center or regional office. In 2005, NCA created its own finance division, collocated with its procurement office in Quantico, Virginia.