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"This Accountability Report demonstrates the Department of the Treasury's commitment to strong program and financial management."

A Message from the Secretary of the Treasury

March 1999

I am pleased to present the Department of the Treasury's Accountability Report for fiscal year 1998 -- the fourth annual Accountability Report we have issued. The report describes the Department's missions, goals and accomplishments, and demonstrates the way in which our diverse functions are tied to the Department's broad economic, financial, and law enforcement missions. The report also includes the Department's financial statements and other key management information.

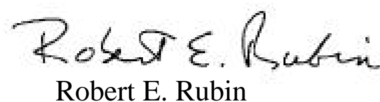
The Department of the Treasury plays a key role in the core functions of government, including tax policy and administration, revenue collection, law enforcement, financial management, banking policy, and international and domestic economic policy. Among other activities, we fight narcotics trafficking and money laundering through our law enforcement agencies, and manage the federal government's debt structure. We manufacture and protect the nation's currency, process the benefit payments for millions of Americans, protect our nations's leaders, and help develop policies on the budget, the nation's tax structure, international economic matters, and inner city economic development.

The Department of the Treasury continues to strive for greater efficiencies and improved customer service. This report demonstrates how we are using our key performance measures to maintain focus on our most critical objectives. We have worked hard to make the Government Performance and Results Act a dynamic and integral part of our efforts to improve how we fulfill our many missions. For fiscal year 1998, the Department met or exceeded 69 percent of its key performance targets, and expects to report even better results for future years.

For fiscal year 1998, the Department again received a qualified opinion on its financial statements. The qualification was primarily due to the well-publicized problems experienced by the Internal Revenue Service in its efforts to produce the newly required financial reports on its administrative activities. The Department is working with the Service to correct these problems and meet the Administration's goal of achieving an unqualified audit opinion on fiscal year 1999's financial statements.

The American public deserves a government that is accountable for how it spends taxpayers' money. This Accountability Report demonstrates the Department of the Treasury's commitment to strong program and financial management. Next year, with the help of all of the senior program and financial managers in the Department, I plan to report even better results.

Sincerely,



Robert E. Rubin

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A Message From the Assistant Secretary for Management and Chief Financial Officer

March 1999

Fiscal Year 1998 presented a significant challenge for the Department of the Treasury, as well as for all of the Executive agencies. The Office of Management and Budget's financial statement guidance not only revised reporting formats for various financial statements, but also required new financial statements, such as the Statement of Net Cost, Statement of Budgetary Resources, and Statement of Financing.

Treasury's responsibilities for complete, timely and accurate reporting of its financial resources are huge. At September 30, 1998, the Department's total assets were $5.7 trillion, and total liabilities were $5.6 trillion. $5.5 trillion of these liabilities, most of which is Federal debt managed by the Department on behalf of the Federal Government, is not covered by budgetary resources. Net cost of operations for fiscal year 1998 was $384 billion, which includes interest on the Federal debt of $363 billion. Total net revenue collected on behalf of the Federal Government was $1.7 trillion.

"Treasury focuses its resources on helping the Nation achieve a number of important public policy goals, including a healthy economy, voluntary compliance with the tax laws, and streets that are safe from illegal drugs and violent crime."

While we were able to successfully address the problems that resulted in a qualified audit opinion on the Department's fiscal year 1997 financial statements, the Department received a qualified opinion on its fiscal year 1998 financial statements. The qualification was primarily due to the inability of IRS' administrative systems to produce timely, auditable data to support the new financial statements described above.

We are disappointed in these results and actions are underway to address the problems for more favorable results in fiscal year 1999. However, on a positive note, as in fiscal year 1997, the Department received unqualified opinions on its fiscal year 1998 revenue collection ($1.7 trillion) and debt management ($5.5 trillion) activity.

Treasury focuses its resources on helping the Nation achieve a number of important public policy goals, including a healthy economy, voluntary compliance with the tax laws, and streets that are safe from illegal drugs and violent crime.

Treasury had many positive results that were in programs of particular importance to this Administration. From among the roughly 300 measures in the Treasury Performance Plan, 90 were selected to be highlighted in the FY 1998 budget. These 90 targets were selected by the senior managers within each bureau and their respective Treasury Policy Official. For fiscal year 1998, the Department met or exceeded 69 percent of these key performance targets.

Finally, the report identifies several issues that remain a high priority within the Department. These include: Year 2000 compliance; data and EDP security; IRS modernization and restructuring; financial management weaknesses; debt collection; government-wide audited financial statements; and IRS accounts receivable. In future Accountability Reports, I expect to report that we have appropriately addressed all of these issues.

Sincerely,

Nancy Killefer

EXECUTIVE SUMMARY

INTRODUCTION

The Secretary of the Treasury has primary responsibility within the Administration for economic, tax, and fiscal policies. The Secretary also oversees the Department's other diverse functions, including law enforcement and financial operations.

The Department of the Treasury has been preparing an Accountability Report since Fiscal Year 1995, under the pilot program authorized by the Government Management Reform Act of 1994, and endorsed by the Office of Management and Budget.

ORGANIZATION

The Departmental Offices functions as the "headquarters" for Treasury, and also carries out many domestic and international responsibilities. There are eleven bureaus which report to the Department: the Bureau of Alcohol, Tobacco and Firearms; Office of the Comptroller of the Currency; U. S. Customs Service; Bureau of Engraving and Printing; Federal Law Enforcement Training Center; Financial Management Service; Internal Revenue Service; U.S. Mint; Bureau of the Public Debt; U.S. Secret Service; and the Office of Thrift Supervision.

The Department's FY98 operating budget for salaries and expenses was $11.5 billion, with 141,727 employees.

MISSION

The Department's strategic plan identifies three programmatic missions covering its ***economic, financial, and law enforcement*** responsibilities, and a fourth ***management*** mission area. Performance measures were developed for various goals and objectives in accordance with the Government Performance and Results Act to evaluate the Department's programs.

FINANCIAL STATEMENT HIGHLIGHTS

Fiscal Year 1998 presented a significant challenge for Treasury, as well as for all of the Executive agencies. The Office of Management and Budget's (OMB) financial statement guidance not only revised reporting formats for various financial statements, but also required new financial statements, such as the Statement of Net Cost, Statement of Budgetary Resources, and Statement of Financing.

The Department has prepared its financial statements in accordance with the accounting standards codified in the Statements of Federal Financial Accounting Standards and the form and content requirements issued by OMB. The Department received a qualified opinion on its FY97 financial statements. The Office of Inspector General issued a qualified opinion on the Department's FY 1998 financial statements.

As in FY 97, the Department received unqualified opinions on its FY 98 revenue collection and debt management activities. However, among other problems in the administrative area, the administrative systems at the IRS were unable to produce timely, auditable data to support the new financial statements described above. Actions are underway to address these problems in FY99.

At September 30, 1998, the Department's total assets were $5.7 trillion, and total liabilities were $5.6 trillion. $5.5 trillion of these liabilities, most of which is Federal debt managed by the Department on behalf of the Federal Government, is not covered by budgetary resources. Net cost of operations for FY98 was $384 billion, which includes interest on the Federal debt of $363 billion. Total net revenue collected on behalf of the Federal Government was $1.7 trillion.

PROGRAM HIGHLIGHTS

The following presents key Treasury initiatives and activities during FY 1998 which contributed to success in achieving the Department's various missions.

ECONOMIC MISSION: Promote Prosperous and Stable American and World Economies

The Department of the Treasury has primary responsibility for formulating and recommending domestic and international economic, financial, and fiscal policies that affect growth and stability.

Domestically: The Administration's sound fiscal policy has encouraged sustained economic expansion, which resulted in the Federal budget surplus of $70 billion for FY98 (0.8% of GDP). Treasury played a primary role in the formulation and review of Administration budget and economic policies, and contributed to the country's economic well-being by:

- Developing a consumer financial education initiative to help consumers get the information they need to make smart choices and protect their savings;
- Introducing inflation-indexed Savings Bonds, making inflation protection available, on a tax-advantaged basis, for as little as $50; and
- Improving the economies of distressed communities (through the Community Development Financial Institutions Fund) by awarding $46 million in financial assistance to community development organizations, and making 79 Bank Enterprise Awards totaling almost $28 million to insured depository institutions.

Internationally: Overall, the world economy grew by 2 percent. Unfortunately, the overall growth of countries in transition from central planning to market-based economies fell by 0.2 percent, caused primarily by the economic downturn in Russia and its severe financial crisis that resulted in devaluation and default. Treasury played a key role in the international economic arena by:

- Working to secure approval of $18 billion for the U.S. share of the International Monetary Fund (IMF) quota increase and the U.S. contribution to the IMF's New Arrangement to Borrow;
- Successfully negotiating a World Trade Organization financial services agreement in which 102 member countries committed to open their markets for banking and securities; and
- Reducing multilateral development bank payments in arrears from $862 million in FY 1997 to $310 million in FY98.

FINANCIAL MISSION: Manage the Government's Finances

As the primary fiscal agent for the Federal Government, Treasury manages the nation's finances through collecting money due the United States, making its payments, managing its borrowing, performing central accounting functions, and producing coins and currency sufficient to meet demand. Key accomplishments for the year were:

- Providing critical tax code analyses and playing a vital role in drafting the IRS Restructuring and Reform Act of 1998;
- Collecting 95 percent of total Federal receipts in FY98. Net revenues collected were $1.7 trillion.

- Collecting nearly $14 million of delinquent debt owed the government, negotiating $45 million in repayment agreements with debtors, and collecting an additional $4 million through adminitrative offsets of payments to debtors;

- Collecting in excess of $17.5 billion in Customs duties via electronic means, which was 79.6 percent of total Customs revenue collected;

- Continuing expansion of electronic collection mechanisms for collecting the government's $1.9 trillion in total revenue. In FY98, 68.5 percent of total collections were made electronically, up from 52 percent in FY 97;

- Making approximately 862 million payments in FY 1998, with sixty-three percent of these payments made electronically, compared to 58 percent in 1997, resulting in an estimated saving of $13.1 million in 1998;

- Making 99.9% of combined check and electronic payments on time;

- Completing ninety percent of Treasury marketable securities auction results within one hour, and completing 98.9% of marketable Treasury Direct Securities customer service transactions within three weeks;

- Issuing on time the first ever Consolidated Financial Statements (CFS) of the United States government that were subjected to audit. While the General Accounting Office disclaimed an opinion on the CFS, this was a critical first step towards the issuance of audited, reliable financial statements that will be useful to a wide variety of interested audiences;

- Successfully introducing the newly-designed $20 Federal Reserve Note, incorporating new advanced counterfeit deterrent features. 9.2 billion notes were delivered to the Federal Reserve System, and 19.7 billion stamps were delivered to the U.S. Postal Service.

- Meeting coin demand by providing 16.6 billion circulating coins to the Federal Reserve for distribution, while reducing average coin production costs by almost 70% over FY 1997 costs.

LAW ENFORCEMENT MISSION: Protect Our Financial Systems and Our Nation's Leaders, and Foster a Safe and Drug-Free America

Treasury's effort in the law enforcement area represents a significant amount of the total Federal Government's law enforcement activities. Treasury's accomplishments are:

- Operation Casablanca resulted in the seizure of over $100 million in drug trafficking proceeds, 2 tons of cocaine, 4 tons of marijuana, over 160 arrests, and the disruption of two notorious international financial crime enterprises. The operation also resulted in the indictment of 26 foreign bank officials and three foreign banks;

- Operation "Brass Ring" resulted in the seizure of 45 percent more narcotics than had been seized during the same time period in FY 1997;

- Outbound currency seizures increased from $55.2 million in FY97 to $68.4 million in FY98;

- During FY 1998, $80.5 million in counterfeit U.S. currency was seized abroad prior to circulation, a 32 percent increase over FY 1997. In addition, 29 counterfeit plant operations in foreign countries were suppressed; and

- For FY 1998, equitable sharing with state and local law enforcement agencies from the Treasury Forfeiture Fund was nearly $72 million, as compared to just over $42 million in FY 1997. In addition, the number of payments for equitable sharing was at an all time-high of 4,883.

MANAGEMENT MISSION: Continue to Build a Strong Institution

Treasury continued to emphasize the need for a strong and efficient organization in order to effectively accomplish our programmatic goals. Performance improvement initiatives were implemented in several areas, including financial, information, and human resource management, as well as customer service.

- Treasury's Year 2000 process met critical milestones during FY 1998 and is on schedule for successful conversion of all mission-critical systems.

- In the area of strategic management, Treasury significantly increased its compliance with the Results Act ahead of schedule in order to improve program performance and management.

- The Department also undertook a major effort to transform human resources management and improve service delivery of human resources processes through a department-wide integrated human resources system.

- In response to Executive Order #12862 and direction in the Treasury Strategic Plan, the bureaus established a total of 105 customer service standards for FY 1998, and met these standards 72 percent of the time.

- Significant progress was made in reorganizing and restructuring the Internal Revenue Service, shifting from a focus on revenue collection and enforcement to a taxpayer-service oriented organization. IRS continues to implement fundamental changes in the way it conducts its business.

- The Treasury Franchise Fund completed a very successful second year of operation. Revenues increased 109 percent, from $38.5 million to $80.4 million. Cumulative results of operations increased 110 percent, from $3.2 million to $3.3 million.

SIGNIFICANT ISSUES AND CHALLENGES

Overall Priorities

Secretary Rubin and senior management officials have developed a comprehensive list of priorities for the coming year which covers a broad range of activities, from tax and budget issues to drug interdiction and gun control, from dealing with the global financial crisis to addressing inner city poverty, from the management of the government's debt to the reform of the regulatory structure of the U.S. financial system, and the promotion of economic growth both at home and abroad.

Year 2000 Compliance

This is one of the highest and time-sensitive priorities facing Treasury. Treasury's information systems, especially those related to revenue collection and disbursement of funds, are crucial to the financial operations of the Federal Government. Further, Treasury's systems have a direct influence on many facets of the U.S. and world economies. The rapid approach of the new millennium and its impact on Treasury's information systems require the most cost-effective approach to plan and manage the century date conversion effort. Senior management at the Treasury bureaus and the Department are strongly committed to this resource-intensive effort.

Data and EDP Security

Financial statement audits at Treasury bureaus identified weaknesses relating to internal controls over the data in the automated systems. Major computer systems at several bureaus are still vulnerable to unauthorized access. This challenge is receiving senior management attention throughout the Department in order to prevent unauthorized access to the Department's program and financial systems and to protect sensitive data related to Treasury's missions.

Internal Revenue Service Modernization and Restructuring

Serious management and technical weaknesses were identified which jeopardize IRS' capability to successfully complete this modernization program. In addition, the IRS Restructuring and Reform Act of 1998 requires significant changes in IRS' organization structure and business processes. The Act also provides many important taxpayer protections which link the Commissioner's modernization plan with IRS' new mission statement: ***"Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all."***

Financial Management Weaknesses

Management reviews and audits conducted by GAO and Treasury's Office of Inspector General have identified financial management weaknesses which hinder Treasury's ability to achieve its program objectives. These weaknesses have also prevented the Department from obtaining an unqualified audit opinion on its financial statements. Action plans are in place or are being developed to correct these weaknesses.

Consolidated Financial Statements (CFS) for the Federal Government

The Department of the Treasury is responsible for preparing auditable Consolidated Financial Statements (CFS) for the Federal Government. A number of problems were identified in the first ever audit of the FY97 CFS which resulted in a disclaimer of audit opinion from the GAO. Significant deficiencies in the agencies' financial systems seriously hampered Treasury's ability to obtain timely and reliable information for the Government-wide financial statements. In addition, new Federal accounting standards and new reporting requirements continue to be a major challenge for the entire Federal Government.

IRS Accounts Receivable

Effective management of IRS receivables continues to be an IRS and Departmental management priority. IRS continues to balance collection efforts with efforts to

promote voluntary compliance, and is also continuing efforts to develop systems that will enhance collection efforts.

Debt Collection

The Department has the lead role in implementing the Debt Collection Improvement Act of 1996. Progress has been made: participants in the debt offset program have increased from 17 to 37 agencies, and debts referred to Treasury for collection have increased from $9.4 billion in FY97 to nearly $17 billion in FY98. Continued efforts are required to put a complete infrastructure in place to maximize the collection of delinquent debts.

MANAGEMENT CONTROLS

Utilizing management evaluations and independent audits, the Department assessed its level of compliance with the internal control and financial systems standards of the Federal Managers' Financial Integrity Act and the Federal Financial Management Improvement Act (FFMIA). While acknowledging material weaknesses, the Department provides reasonable assurance that the internal control objectives are being achieved. However, the Department does not provide reasonable assurance that the financial systems standards are being achieved due to the number and magnitude of identified financial systems weaknesses. For the same reason, the Department is not in substantial compliance with the FFMIA. Actions are underway to address all identified internal control and financial systems weaknesses.

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This report is similar in many respects to last year's report, but also reflects many changes which we believe will enhance its usefulness to readers. Our goal is to continue building on past experiences and make each successive year's report more readable and useful for our many customers. Your comments are welcomed and appreciated, and can be sent to any of the e-mail addresses listed at our Internet site at:
http://www.ustreas.gov/tcfo/dcfo.html

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

As a major policy advisor to the President, the Secretary of the Treasury has primary responsibility for formulating and recommending domestic and international financial, economic, and tax policy; participating in the formulation of broad fiscal policies that have general significance for the economy; identifying and collecting taxes and duties; and managing the public debt. The Secretary also oversees the activities of the Department in carrying out its major law enforcement responsibilities; in serving as the financial agent for the U.S. Government; and in manufacturing coins, currency, and other products for customer agencies.

This Management's Discussion and Analysis (MD&A) section of the Accountability Report provides readers with the FY 1998 highlights of Treasury's many diverse programs by each of the four mission areas as articulated in the Treasury-wide Strategic Plan. The Government Performance and Results Act (Results Act) establishes formal requirements for strategic planning and performance measurement in the Federal government. Because of the complex nature of several Treasury bureaus, a bureau's activities may impact one or more strategic mission area and its related goals.

This MD&A also presents highlights of Treasury's financial position and the auditor's opinion on our FY 1998 financial statements. Selected program initiatives and activities for each of the four missions are presented by their goals as they relate to the Department's Strategic Plan. Key performance results from the Performance Plan for FY 1998 are compared with the targets planned in our budget.

This report not only describes various accomplishments achieved by the Department during the FY 1998, but also addresses the significant challenges facing the Department in the next fiscal year and future years. Some of these challenges have been identified by the General Accounting Office (GAO) as being high risks to the efficiency of Treasury management and the effectiveness of its programs. Plans for corrective actions to address these issues have been developed and progress is being made.

TREASURY'S ORGANIZATION

In addition to the Departmental Offices, the Office of Inspector General, the Exchange Stabilization Fund, the Federal Financing Bank, the Community Development Financial Institutions (CDFI) Fund, and various other funds which together comprise Treasury "headquarters" operations, the Department also includes eleven bureaus: Bureau of Alcohol, Tobacco and Firearms; Office of the Comptroller of the Currency; U.S. Customs Service; Bureau of Engraving and Printing; Federal Law Enforcement Training Center; Financial Management Service; Internal Revenue Service; U.S. Mint; Bureau of the Public Debt; U.S. Secret Service; and the Office of Thrift Supervision.

MISSION

Because Treasury's responsibilities and activities are broad in scope and touch the lives of all Americans, we have developed a four-part mission statement which describes the purposes of our diverse functions. It includes three programmatic missions covering our ***economic, financial, and law enforcement*** responsibilities, and a fourth ***management*** mission area, because only a strong and efficient organization can succeed in accomplishing our programmatic goals.

The table on the following page describes the specific goals and objectives for each of these mission areas.

FINANCIAL STATEMENT HIGHLIGHTS

The Department has prepared its financial statements in accordance with the accounting standards codified in the Statements of Federal Financial Accounting Standards, and the form and content requirements contained in the Office of Management and Budget (OMB) Bulletin No. 97-01.

Fiscal Year 1998 presented significant challenges for Treasury, as well as for all of the Executive agencies, in preparing its financial statements. The challenges included new reporting formats for the statements and the requirement for new financial statements (Statement of Changes in Net Position, Statement of Net Cost, Statement of Budgetary Resources and Statement of Financing). As an option offered by OMB Bulletin No. 97-01, Treasury prepared **combined** statements for the Statement of Budgetary Resources and the Statement of Financing.

The Office of Inspector General (OIG) issued a *qualified* opinion on the Department's FY 1998 financial statements. This qualification is primarily due to the Internal Revenue Service (IRS) inability to provide quality and timely accounting data to support its financial statements, and the Department's reporting of certain investments in Federal debt securities. As described in the Department's response to the OIG audit report, the Department believes its reporting of such investments is proper. (See Part IV of this report)

The OIG audit identified material weaknesses in:

- Financial management and reporting at the IRS; and,
- Electronic data processing (EDP) general controls over financial systems.

In addition, the OIG also disclosed three reportable instances of non-compliance with laws, regulations, and government-wide policies:

- IRS' installment agreements are not in compliance with the Internal Revenue Code;
- The U.S. Customs Service did not conduct a biennial review of fees and charges for its reimbursable projects; and,
- The Department's financial management systems do not substantially comply with the requirements of the Federal Financial Management Improve-ment Act of 1996.

The Department of the Treasury's financial statements reflect the entity activities of the Treasury, and certain non-entity functions it performs on behalf of the Federal government and others. Entity activities include appropriations and revenue Treasury received to conduct its operations. Entity related functions also include activities of Treasury's Exchange Stabilization Fund and the Department's Federal Financing Bank. Non-entity activities include the collection of Federal revenue, managing the Federal Debt, disbursing Federal funds, and maintaining certain assets and liabilities for the Federal government as well as for others.

Assets

Treasury's total assets as of September 30, 1998 were $5.696 trillion, which included $158 billion entity assets and $5.538 trillion non-entity assets. Non-entity assets included $5.247 trillion due to Treasury from the General Fund of the Federal Government to pay the principal on the public debt, as well as tax refunds.

Liabilities

Total liabilities as of September 30, 1998 were $5.617 trillion, which included $131 billion of liabilities covered by budgetary resources and $5.486 trillion not covered by budgetary resources.

Intra-governmental liabilities not covered by budgetary resources totaled $1.785 trillion, including interest payable, in borrowing from various Federal agencies. However, they do not include debt issued by other governmental agencies, such as the Tennessee Valley Authority or the Department of Housing and Urban Development. Liabilities not covered by budgetary resources also include Federal debt held by the public

totaled $3.695 trillion; the majority of these are Treasury marketable Notes and Bonds.

Net Cost of Treasury Operations

The net cost of Treasury operations totaled $13 billion for the year ended September 30, 1998. The majority of the costs are in the *Financial* mission, as Treasury is the primary fiscal agent for the Federal government in managing the Nation's finances by collecting revenue, making Federal payments, managing Federal borrowing, performing central accounting functions, and producing coins and currency sufficient to meet demand.

Federal Debt Interest Costs

Treasury's Consolidated Statement of Net Cost includes $363.3 billion for interest on the Federal debt and other Federal costs, such as payments made to or by the Judgment Fund, the Resolution Funding Corporation, and the District of Columbia.

Custodial Revenue

Total net revenue collected by Treasury on behalf of the Federal Government for FY 1998 was $1.7 trillion. This includes various taxes, tariff duties, user fees, fines and penalties, and other revenue.

Other Financial Highlights

The following table provides additional information for the Department of the Treasury and its bureaus.

Fiscal Year 1998

Treasury Bureau	Appropriations Enacted (in Millions)	Full Time Equivalent Employees	Total Budget Resources (in Millions)	Total Outlays (in Millions)
Alcohol, Tobacco and Firearms (ATF)	$ 563	3,872	$ 668	$ 495
Office of the Comptroller of the Currency (OCC)	*	2,785	430	(32)
U. S. Customs Service (Customs)	1,683	18,989	3,366	1,929
Departmental Offices (DO) **	397	2,134	56,257	4,925
Bureau of Engraving and Printing (BEP)	*	2,532	652	47
Federal Law Enforcement Training Center (FLETC)	98	511	180	83
Financial Management Service (FMS)	208	2,029	8,903	8,111
Internal Revenue Service (IRS)	7,775	99,089	8,421	7,338
U. S. Mint	*	2,010	1,281	(95)
Bureau of the Public Debt (BPD) Resources/Outlays include interest on the public debt)	169	1,749	364,161	364,093
U. S. Secret Service (SS)	590	4,758	761	655
Office of Thrift Supervision (OTS)	*	1,269	156	(1)
TOTAL	**$ 11,483**	**141,727**	**$445,236**	**$387,548**

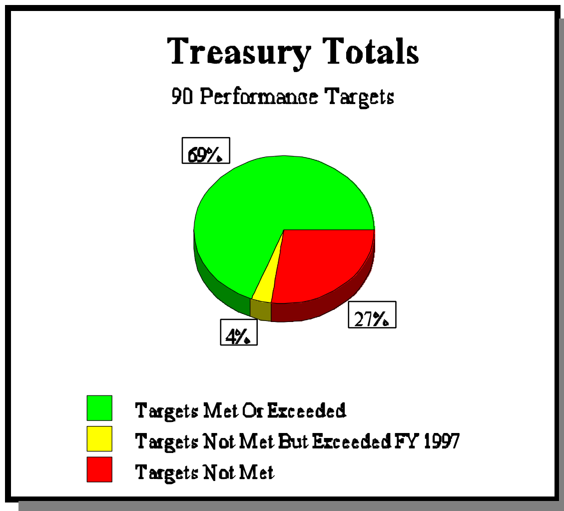
* These entities operate on self-supporting revolving funds, and do not receive appropriations.

** Departmental Offices includes the Office of Inspector General, Working Capital Fund, Exchange Stabilization Fund, Federal Financing Bank, Treasury Forfeiture Fund, Community Development Financial Institutions Fund, Financial Crimes Enforcement Network, and DC Pension.

PROGRAM HIGHLIGHTS

Treasury focuses its resources on helping the Nation achieve a number of important public policy goals, including a healthy economy, voluntary compliance with the tax laws, and streets that are safe from illegal drugs and violent crime.

Treasury had many positive results that were in programs of particular importance to this Administration. In summary, from among the roughly 300 measures in the Treasury Performance Plan, 90 were selected to be highlighted in the FY 1998 budget. These 90 targets were selected by the senior managers within each bureau and their respective Treasury Policy Official.



Overall, the Department met or exceeded 69 percent of these key performance targets. In some cases, the targets were unmet due to a management decision to shift emphasis from one program to another. Other targets were not achieved due to unplanned events or bureaus being overly optimistic when setting their targets.

Treasury continues to refine its performance measures, striving to present measures of program *results* rather than the traditional output-oriented or workload measures. Consequently, many of the performance measures presented in this report are different from those presented in the FY 1997 report. As this iterative process continues, we expect to make further improvements for future years. In doing so, it recognizes that many factors come into play in these areas, and that there are many other key contributors to success or failure. Treasury is in a position to influence, but not control, the final outcomes in many instances.

The amount of control that Treasury has over meeting its broad outcome goals should be proportional to its accountability for those goals. Since it is difficult to quantify the extent to which any one event or effort influences an outcome goal -- such as reducing illegal drug usage -- Treasury believes it is appropriate to report on major outcomes, but, generally, will take no direct credit for results.

Note: Due to timing difference between the budget submission and issuance of the Accountability Report, the results for some performance measures may differ from the Management's Discussion and Analysis (MD&A) section. The MD&A contains updated performance results from the bureaus' financial statement audits.

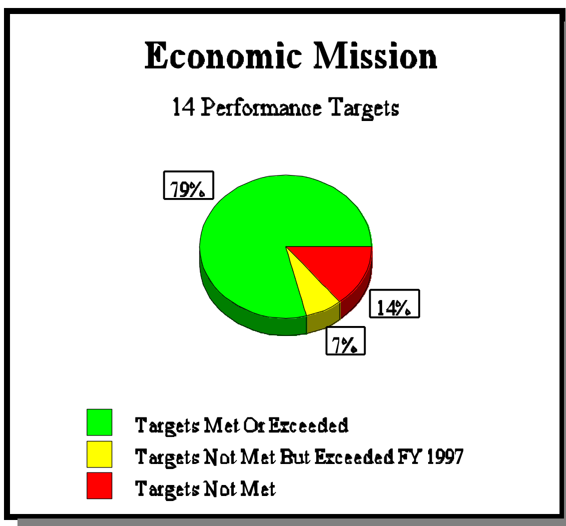
ECONOMIC MISSION: PROMOTE PROSPEROUS AND STABLE AMERICAN AND WORLD ECONOMIES

Treasury seeks to maximize the potential of the U.S. and world economies for growth and stability. In pursuit of this, the Secretary of the Treasury is the principal economic advisor to the President and plays a critical role in policy-making by bringing an economic and government financial policy perspective to issues facing the government.

In the domestic area, Treasury develops policy and guidance affecting fiscal policy, financial institutions, financial regulation, and capital markets. In the international arena, Treasury is the principal Cabinet agency charged with developing policies and guidance affecting international monetary affairs, trade and investment policy, international debt strategy, and U.S. participation in international financial institutions.

This mission area is supported by programs managed by many of the Departmental Offices policy offices,

Office of the Comptroller of the Currency, Office of Thrift Supervision, Community Development Financial Institutions Fund, Bureau of the Public Debt, U.S. Customs Service's trade programs, and ATF's compliance program.



Goal: Promote Domestic Economic Growth

Treasury provides advice and assistance to the President in the areas of domestic finance, banking, and other related economic matters, including issues relating to financial institutions, federal debt finance, federal cash management, financial regulation, capital markets, and U.S. government accounts and payments. The Administration's sound fiscal policy has encour-aged the sustained economic expansion, which resulted in the Federal budget surplus of $70 billion for FY 1998 (0.8% of GDP). Treasury played a primary role in the formulation and review of Administration budget and economic policies, and contributed to the country's economic well-being.

The mission of the **Office of the Comptroller of the Currency (OCC)** is to charter, regulate and supervise all national banks, national trust companies, data service providers, and Federal branches and agencies of foreign banks in the United States to ensure a safe, sound, and competitive national banking system.

At September 30, 1998, there were 2,519 Federally chartered national banks, representing about 29 percent of the 8,910 commercial banks in the United States. The national banking system had approximately $3.05 trillion in assets, accounting for about 58 percent of the commercial banking system assets. During the past several years, national bank asset have increased significantly, unlike earlier years that had periods of slow growth. Between 1994 and 1998, national bank asset growth averaged 8.5 percent on a fiscal year basis, in part through the conversion, merger, and acquisition of state and thrift institutions into the national banking system.

Over the last year, the OCC revised its supervisory strategy for the near term and directed a significant portion of its supervisory resources to Year 2000 supervision activities. As a result, only 80 percent of "safety and soundness" examinations were started on schedule in fiscal year 1998, falling short of the performance plan goal of one hundred percent. However, nearly 78 percent of the late "safety and soundness" examinations were related to resource constraints. The remaining 22 percent were late due to circumstances at the banks, such as mergers or conversions. These activities made the examinations impractical to perform at the time. The exams were rescheduled as appropriate.

The mission of the **Office of Thrift Supervision (OTS)** is to effectively and efficiently supervise thrift institutions to maintain their safety and soundness in a manner that encourages a competitive industry to meet America's housing, community credit and financial service needs and to provide access to financial services for all Americans.

As of September 30, 1998, the OTS had oversight over 1,170 institutions with assets of approximately $795.4 billion. While the overall number of OTS-regulated institutions has declined steadily since 1990 (there were 2,359 private sector institutions as of year-end 1990 with assets of $1,129 billion), the OTS is experiencing an increase in applications to form new thrifts. While these applications remain relatively few in number (18 in 1996, 51 in 1997, and 90 in 1998) interest in the Federal thrift charter is growing, and some of these applications pose new supervisory issues requiring policy development.

Thrift industry earnings for the first nine months of 1998 totaled $6.2 billion, setting a new record,

while aggregate industry return on assets (ROA) was 106 basis points during the first nine months. Equity capital reached a record high of 8.58 percent in the third quarter, and troubled assets totaled only 0.8 percent of total assets as of September 30, 1998.

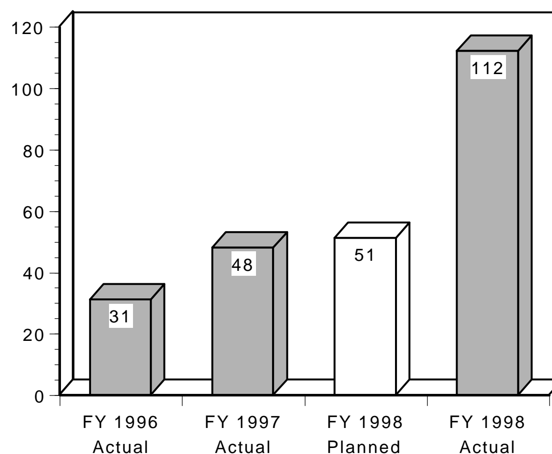
The OTS exceeded most of its performance goals for FY 1998 in performing various types of examinations on thrifts, except the information systems (IS) examinations; IS examiners were diverted to examinations dealing with Year 2000 issues.

The mission of the **Community Development Financial Institutions (CDFI) Fund** is to promote access to capital and local economic growth by directly investing in and supporting community development financial institutions (CDFIs), and expanding financial service organizations' lending, investment, and services within under-served markets, such as poor urban, rural and Native American communities. Access to capital is an essential ingredient for creating and retaining jobs, developing affordable housing, revitalizing neighborhoods, and building local economies.

The number of certified CDFIs increased from 196 in 1997 to 262 in 1998, and from 42 states to 44 states, the District of Columbia and Puerto Rico. The total volume of new activity within distressed communities by insured depository institutions increased from $82.8 million in 1997 to $194.4 million in FY 1998. The total number of CDFIs receiving financial assistance increased significantly during FY 1998, and the Fund increased the amount awarded to CDFIs from $41 million in 1997 to $46 million in 1998. The number of Bank Enterprise Awards increased from 55 in 1997 to 79 in FY 1998, and the total amount increased from $16 million in 1998 to $28 million.

**** The number of CDFIs receiving financial assistance for FY 1997 round has increased to 50. Two more awards were made in FY 1998 for the FY 1997 round.***

Number of CDFIs Receiving Financial Assistance



The **Bureau of the Public Debt (BPD)** concentrated on a number of customer-oriented initiatives during FY 1998 to attract small or self-employed investors, and to encourage investments through new products and enhanced services.

BPD continued its commitment in providing investor services via the Internet by enhancing its web site for information as well as a resource for downloading forms, making inquiries, and transacting business.

Perhaps the most exciting online activity at BPD in FY 1998 centered on the new *TreasuryDirect* Electronic Service. Investors now can buy and reinvest securities, check account balances, and order Statements of Account and duplicate interest income statements by visiting BPD's web site.

In September 1998, BPD debuted inflation-indexed securities, *Series I bonds*, which earn interest at a rate that is a combination of a fixed rate and a variable inflation rate. These bonds are designed to appeal to individuals who wish to maximize protection on their investments from the effects of any future increases in the inflation rate.

The **Bureau of Alcohol, Tobacco and Firearms (ATF)** is the nation's expert on such legal consumer products as alcohol, tobacco, firearms and explosives. These products require special attention due to the important social consequences of misuse. One of ATF's goals is to protect the public and prevent

consumer deception in these regulated commodities. This goal is accomplished through the following three programs:

- To assure the integrity of the products, so that people and companies in the marketplace know that these commodities meet safety and product identity standards. ATF is responsible for regulating fully the alcohol beverages industry and to provide protection to consumers from contaminated or adulterated products. ATF also conducts inspections of applicants for firearms and explosives licenses and permits to ensure ineligible or prohibited persons are kept out of these regulated industries;

- To ensure compliance with laws and regulations through education, inspection and investigation of firearms and explosives licensees, and to ensure alcohol and tobacco industries are compliant with product and trade practice provisions; and

- To inform the public on ATF policies and regulations, product safety and theft prevention using the Internet, trade publications, seminars, and industry meetings.

Goal: Maintain U.S. Leadership on Global Economic Issues

The activity within the Department's Office of International Affairs includes formulating and executing U.S. international economic and financial policies regarding a wide range of international development and analysis functions. FY 1998 accomplishments include:

- The promotion of sound economic policies in developing and emerging market economies. Overall, the economy for developing countries grew by two percent. Unfortunately, the overall growth of countries in transition from central planning to market-based economy fell by 0.2%, caused primarily by the economic downturn in Russia and its severe financial crisis that resulted in devaluation and default. Because of the Asian financial crisis and low oil prices, growth rates for both developing and transitional economies were less than those achieved in 1997;

- The successful achievement of several critical agreements related to the funding of the International Financial Institutions (IFIs), which strengthened their financing capacity and effectiveness. Of particular importance were ongoing U.S. efforts during FY 1998 to secure Congressional funding for the International Monetary Fund (IMF) quota increase and the New Arrangements to Borrow (NAB). Final Congressional approval was obtained in October 1998 for a quota increase valued at $14.8 billion and NAB funding valued at $3.5 billion. Many of the agreements that are entered into with the multilateral development banks (MDB) state that the contribution or investment will be paid over several years. As stipulated in agreements with the MDBs, these payments are contingent upon congressional approval. In FY 1997, future payments subject to congressional approval, due to the MDBs, were $862 million. Major progress was made in obtaining approval for these payments, the balance of which now stands at $310 million. Multilateral negotiations were completed on a capital increase for the African Development Bank and the Multilateral Investment Guarantee Agency (MIGA), and a replenishment for the Global Environment Facility (GEF), accomplished by significant policy reforms;

- The successful conclusion of the World Trade Organization (WTO) financial services agreement in which 102 member countries, accounting for 95 percent of world revenues, committed to open their markets for banking and securities. This culminated fifteen years of negotiations. The Office also reduced export financing subsidies and assorted trade distortions and secured renewal of a soft ban to avoid tied aid in Central and Eastern Europe, including the former Soviet Union;

- The direct investment abroad totaling $861 billion in CY 1997, up 8% over prior year level of $797 billion. International Affairs negotiated bilateral investment treaties with Bolivia and Mozambique; and reviewed 60 proposed foreign acquisitions of U.S. businesses. However, negotiations on a multilateral agreement on investment have been temporarily suspended; and

- The active pursuit of exchange rate policies to promote world economic growth (up 2%) and financial stability in 1998. Significant fluctuations in the value of the U.S. dollar with major foreign currencies were avoided (except for the Russian ruble). International Affairs used sales proceeds of the Exchange Stabilization Fund to purchase $417 million of Japanese yen in mid-June. Global market stability was adversely affected by Russia's devaluation in mid-August. The Russian ruble was devalued by over 170% against the U.S. dollar during FY 1998.

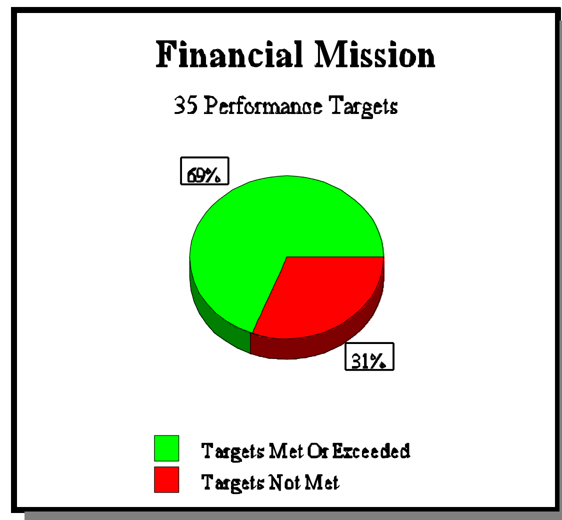
One of the **U.S. Customs Service's (Customs)** missions is to support the Administration's trade policies by participating in a number of international trade meetings with the World Trade Organization, the Asian Pacific Economic Cooperation initiatives, the North American Free Trade Agreement (NAFTA) and the Free Trade of the Americas. Customs achieved substantial progress in its goal of securing increased international cooperation on trade. Mutual Assistance Agreements were concluded with four countries, and Customs also provided 16 International Commer-cial Training programs in 29 countries for 315 officers. Efforts to improve international trade continue with Customs involvement in various international organiza-tions.

The NAFTA Enforcement Working Group trade fraud initiative started to promote compliance and to pursue NAFTA case development. In FY 1998, NAFTA investigations resulted in approximately $7 million of revenue in pre-penalties, penalties and collections.

FINANCIAL MISSION: MANAGE THE GOVERN-MENT'S FINANCES

This mission area covers Treasury's role as the primary fiscal agent for the Federal government in managing the Nation's finances by collecting taxes, tariffs and other debts, making Federal payments, managing Federal borrowing, performing central accounting functions, and producing coins and currency sufficient to meet demand. The bulk of the Department's resources are devoted to collecting taxes and customs duties, since Treasury collected roughly 95 percent of total Federal receipts in FY 1998.

The Internal Revenue Service is the primary tax collecting agent; the U.S. Customs Service and the Bureau of Alcohol, Tobacco and Firearms also collect billions of dollars in revenue each year. The Financial Management Service oversees, accounts for, and reports on government collections and expenditures, and is responsible for collecting delinquent Federal debt government-wide. The Bureau of the Public Debt borrows what is necessary to meet the monetary needs of the Federal government at the lowest possible cost over the long-term. United States coins and currency are produced by the U.S. Mint and the Bureau of Engraving and Printing.



Goal: Collect revenue due to the Federal government

To ensure Treasury collects maximum revenue that is due to the Federal government, efforts are focused on improving and simplifying tax law and administra-tive guidance, encouraging tax and trade law compli-ance, and improving collections.

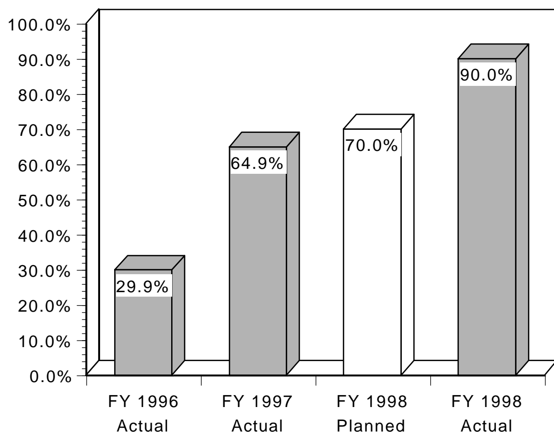
An important goal for the **Department's Office of Tax Policy** is to clarify or simplify tax rules and reduce taxpayer burden, and thereby improve taxpayer compliance and efficiency of tax administration. The Office provided critical advice and analysis regarding improvement and simplification of the tax code, which included developing 118 revenue

proposals as a part of the FY 1999 Budget. The Office also played a key role in drafting the IRS Restructuring and Reform Act of 1998 to ensure that the tax administration reforms contained therein reflected sound tax policies.

In FY 1998, **Internal Revenue Service (IRS)** collected $1.8 trillion in gross tax revenue and issued $151 billion in refunds for the Federal Government. To ensure an effective tax administration system that results in each taxpayer paying the proper amount of taxes, the IRS continues to encourage and assist taxpayers to voluntarily file accurate returns and pay timely, and appropriately enforced the law if they do not comply. Efforts to make it easier for taxpayers to file their tax returns include providing easier tax forms and alternative means of filing, such as by computer or phone and by electronic access to authoritative guidance from the IRS' award winning Internet site. In FY 1998, over 24.5 million returns were filed electronically, an increase of over 20 percent from FY 1997.

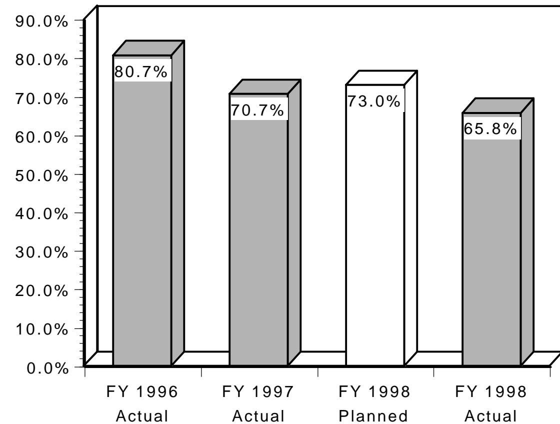
The Toll-Free Telephone Level of Access for FY 1998 significantly surpassed target planned and the FY 1997 level. This dramatic change primarily resulted from Customer Service initiatives designed to respond to the Fall of 1997 Congressional hearings on taxpayer rights, as well as the IRS Restructuring and Reform Act of 1998. Customer Service was asked to provide a greater Level of Access than in prior years. Consequently, a large population of employees were trained in a very short time frame, resulting in more taxpayers being answered on the first call.
However, this initiative affected the Initial Contact

Telephone Access by Taxpayers

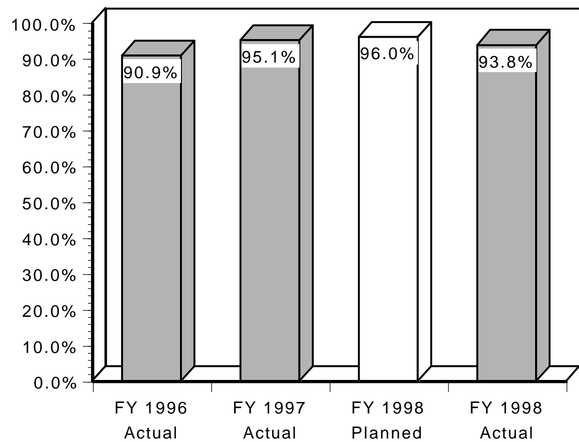


Resolution rate targeted for FY 1998 because questions sometimes were referred to subject matter experts for resolution in a subsequent callback.
The modest decline in the Tax Law Accuracy for FY 1998 also resulted from a shift in the programmatic emphasis to Level of Access.

Initial Contact Resolution Rate



Tax Law Accuracy Rate



**** The FY 1997 results for the three performance measures above are different from the attached Performance Report for FY 1998 submitted with Treasury's Budget for FY 1999. This is due to the timing difference in the issuance of the Accountability Report and the Budget. The charts reflect the numbers submitted for the financial statement audit.***

Walk-In service was added on six Saturdays at 178 nationwide sites during the filing season to provide assistance to taxpayers. The Volunteer Income Tax Assistance (VITA) and the Tax Counseling for the Elderly (TCE) programs resulted in an increase in electronic filing by 24 percent from FY 1997. Other

programs such as Problem Solving/Resolution Days, Walk-in Assistance and Taxpayer Education continued to help increase voluntary compliance by taxpayers.

As of July 1998, Examination audits resulted in recommendations for collections of over $19.5 billion. In addition to the traditional audits, new approaches stress early resolution of issues which save time and money for taxpayers and the Federal government. With programs like the Accelerated Issues Resolution (AIR), the IRS resolves taxpayers' issues quickly and completely, while improving collectability of taxes owed.

Collection activities also resulted in $5.3 billion in annual receipts. With the passage of the IRS Restructuring and Reform Act of 1998, IRS also implemented several procedural changes to enhance support for customer service, certain collection actions, and the review of levy actions. The IRS also is actively identifying and investigating new and emerging areas of financial fraud, such as: pensions, domestic and foreign trusts, subsidies and entitlements, and Earned Income Tax Credit Claims.

The IRS continues its effort in modernizing informa-tion technology to increase timeliness and accuracy of processing tax payments and tax returns, and on those activities initiated in FY 1997 from the strategic modernization plan. The Congress created the Information Technology Investment Account (ITIA) for FY 1998 to fund contracted services to design and build the Modernization Blueprint. As a part of the Modernization Blueprint, the Systems Life Cycle (SLC) Overview outlines the management practices and development processes to be employed by the IRS to manage the modernization.

In response to General Accounting Office and congressional recommendations, the IRS is working to obtain a world class organization to replace the existing Federally Funded Research and Development Center (FFRDC) to work in partnership with IRS and Treasury to address critical issues of Modernization and management of information technology resources.

During FY 1998, the **U.S. Customs Service (Customs)** collected $22.1 billion in tariff duty, user fees, excise taxes, and other assessments on imported and exported goods and services. Customs provided the majority of its collections ($21.9 billion) to Treasury to fund other agency programs. Of the remaining $187 million, Customs provided $73 million to the Puerto Rico and Virgin Islands governments, transferred $63 million directly to other Federal agencies, and retained $51 million to offset various program costs allowed by law and regulation.

Steady progress has been made in using electronic commerce to expedite transactions. Total collections received via electronic means in FY 1998 exceeded $17.5 billion which was 79.6 percent of total revenue collected. This is an increase from the 77.0 percent in FY 1997, and also exceeded Customs' goal of 75 percent for FY 1998. The number of importers participating in the Automated Clearing House (ACH) payments increased from 5,467 to 6,430, and the total amount collected via ACH increased from $15.7 billion to $16.4 billion. Customs cumulative results of operations increased by $35 million in FY 1998, from $981 million reported in FY 1997 to just over $1 billion, principally as a result of user fee collections relating to merchandise and passenger processing. User fees comprise approximately $900 million of the $1 billion balance.

Customs also continued to make progress in improving overall trade compliance by providing more and clearer information. For FY 1998, Customs aggres-sively worked to raise compliance through programs, such as MARC 2000 (Multiport Approach to Raise Compliance) and through targeted interventions by the five Strategic Trade Centers. The overall trade compliance rate for FY 1998 was 81 percent for all commodities, slightly under the target of 84 percent.

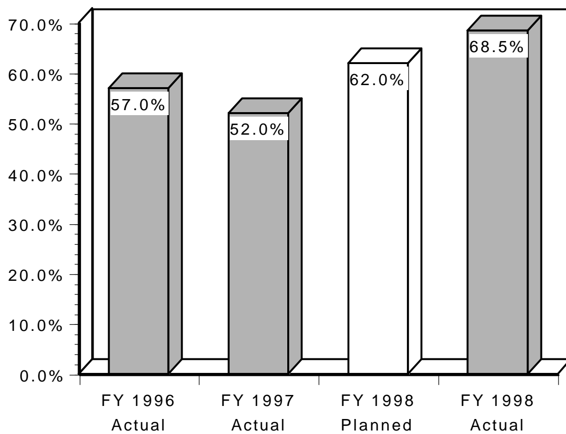
In the outbound (export) arena, Customs continued its aggressive outreach efforts to heighten the trade community's knowledge of export laws, rules and regulations, and port procedures for all methods of transportation. As a result of these and other outreach efforts, there has been an increase over FY 1997 for the compliance rates of 26 percent in the filing of bills of lading and a increase of 14 percent in the timely filing of Shippers' Export Declarations for vessel exports. Surveys will be conducted for all modes of transportation to establish compliance baselines.

The **Bureau of Alcohol, Tobacco and Firearms (ATF)** collected $12.4 billion versus $12.7 billion

in FY 1997, before refunds, in revenue generated from interests, penalties, Federal taxes and fees imposed on alcohol, tobacco, firearms, and ammunition products. Excise taxes for alcohol and tobacco comprised 97 percent of total collections. ATF's National Revenue Center and the two technical service offices continued to monitor tax collections by auditing tax returns and assessments, initiating enforced collection action, analyzing required reports; and accounting for tax payments, licensing fees, and related refunds.

The **Financial Management Service (FMS)** also managed the deposit mechanisms for FY 1998 revenue collection of approximately $1.9 trillion for the Federal government. Efforts taken by FMS in working with other Federal agencies and the private sector resulted in a significant increase in collections through electronic means.

Percentage of Revenue Collected Electronically



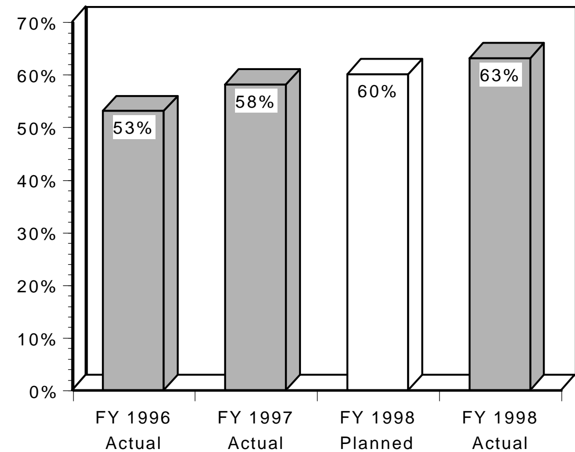
Goal: Manage the Federal government's accounts

The **Financial Management Service's (FMS)** mission is to improve the quality of Federal government's financial management by linking program and financial management objectives and by providing financial services, information, advice, and assistance to customers. FMS's major business lines are payments, collections, debt collection, and government-wide accounting and reporting. FMS continued to improve and modernize the systems and hardware platforms through which the Federal government makes payments, offsets delinquent debts, collects revenue, and issues financial reports on Government operations.

During FY 1998, FMS issued approximately 862 million payments, totaling more than one trillion dollars, for all executive agencies except the Department of Defense, the U.S. Postal Service, the U.S. Marshals Service, as well as certain Government corporations. 99.99 percent of paper check payments released to the U.S. Postal Service, and electronic payments released to the Federal Reserve Bank were made for timely delivery.

The FMS continued its effort to implement the mandatory requirement for Federal payments made using Electronic Funds Transfer (EFT) in the Debt Collection Improvement Act of 1996. The FMS estimated the government's savings of $13.1 million in FY 1998 by reducing the number of check payments.

Federal Payments Made Electronically



FMS is committed to the pursuit of business related advances in technology which lead to innovative and creative approaches fostering economy and effectiveness in meeting customer needs. FMS introduced numerous new card-based mechanisms, such as the Benefit Security card, USA card, and stored value cards, to enhance the collection and payment of Federal funds.

Significant progress on Year 2000 efforts included successful implementation of compliant payment

systems, through which over 600 million payments or 80 percent of FMS's payment volume are made each year. FMS also implemented a number of systems and major enhancements to several legacy systems to strengthen the government's financial infrastructure to improve the efficiency of program management across government.

Treasury, in compliance with the Government Management and Reform Act, prepared and issued on time the first Consolidated Financial Statement (CFS) of the United States government that was subjected to audit examination by GAO, which identified a number of significant government-wide financial management issues that need corrective action. Although the GAO disclaimed an audit opinion on the CFS, it is a critical first step towards the issuance of auditable and reliable financial information that will be useful to a wide variety of interested audiences. These efforts will strengthen the govern-ment's financial infrastructure and improve govern-ment-wide implementation of accounting standards while providing accurate and timely financial information.

Goal: Cost-effectively finance the Federal government's operations

The primary mission of the **Bureau of Public Debt (BPD)** is to borrow the money needed to operate the Federal government and to account for the resulting debt. Financing the government's operations is achieved through the sale of a variety of securities: marketable securities (including bills, notes, and bonds), special purpose securities, and non-marketable U.S. Savings Bonds. The BPD continued to introduce new products and services to attract investors.

BPD developed the *EasySaver Plan* to reach approximately 120 million Americans that do not have access to a payroll savings plan. An individual can purchase savings bonds on a recurring basis by completing one application form and purchase bonds on the schedule best suited to their plans. EasySaver differs from the payroll savings plan in that the full purchase price of a bond must be paid at the time of the purchase, and the purchase price is deducted from a bank account that the employee designates.

As part of its ongoing effort to encourage Americans to save and invest, BPD put Treasury bills and two-year notes in easy reach of small investors by lowering the minimum purchase amount to $1,000. The financial press hailed the new minimums for bills and notes as a way for even small investors to take advantage of the safety and liquidity of Treasury securities. Investors quickly took advantage of the new opportunity by buying securities in the new lower amounts.

BPD implemented another important initiative in April that eliminates the risks associated with holding physical securities. BPD introduced the *Bearer Corpora Conversion System* (BECCS) to allow holders of U.S. Treasury bearer securities to convert to book-entry form. BECCS securities are maintained on the Treasury/Reserve Automated Debt Entry System. BECCS benefits investors by eliminating the costs associated with the storage and safekeeping of physical securities. Book-entry also eliminates the risk of loss or destruction of these paper securities. At the start of the open season in April, the amount of outstanding and unmatured bearer principal totaled $8.59 billion. Through the BECCS program, BPD has converted $3.84 billion (45 percent) of this amount to book-entry.

The *Savings Bond Wizard*, a program that enables bond owners to maintain an inventory of their bonds and to determine the current redemption value and earned interest, is the most popular downloadable file on BPD's web site. In addition, several savings bond pages were translated into Spanish as part of the BPD effort to build investor interest within the Hispanic market.

BPD continues to work with a number of financial institutions through the Home Banking initiative. This effort encourages financial institutions to offer Series EE and I bonds for sale as part of the electronic services they provide to customers. Payment for the bonds is obtained by debiting the bank account the customer designates.

Investors eager to buy securities over the Internet quickly took advantage of *Buy Direct,* BPD's new web-based sales option for current *TreasuryDirect* account holders. In the two days leading up to September 16, the publicized start-up date for the

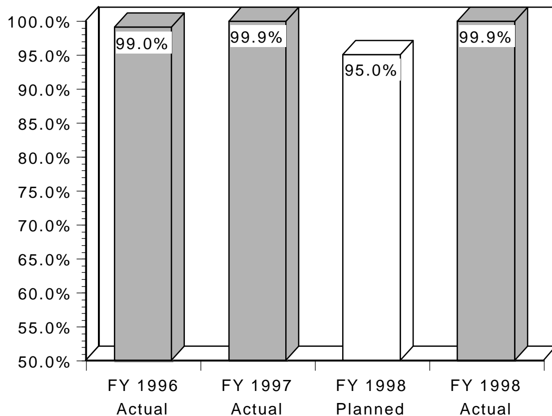
initiative, many investors logged onto the system and bought a bill, note, or bond -- including a one- million dollar purchase! All transactions are protected by Secure Sockets Layer (SSL), an Internet security protocol that prevents eavesdropping, tampering, and message forgery.

Reinvest Direct, our first electronic service, received the most use by investors in FY 1998. This program makes reinvesting more convenient than ever for investors with 24 hours a day, 7 days a week service over the phone or the Internet. Investors made more than 780,000 reinvestments, more than 44 percent of our total reinvestments, through *Reinvest Direct* last year. In addition to the convenience, investors who have opted to use the phone or Internet have saved themselves about $250,000 in postage. BPD expects to experience a significant reduction in postal costs, as well, since mail-back confirmations are not sent to investors who receive reinvestment confirmations via *Treasury-Direct* Electronic Services.

BPD must inspire confidence in investors in its savings securities and marketable securities programs for the borrowing process to work effectively. Several performance measures have been established to ensure that investors receive timely, accurate service.

BPD established a performance target to issue 95 percent of savings securities through the Regional Delivery System within 3 weeks. The Regional Delivery System is the mechanism by which bonds are sold over-the-counter at more than 40,000 locations nationwide, processed at five regional centers, and then mailed to the bond owners.

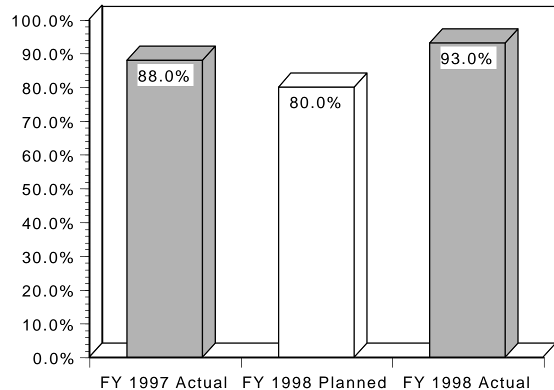
Savings Securities Issued Within 3 Weeks



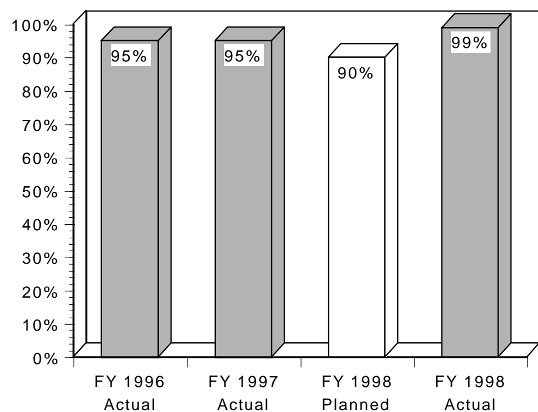
BPD maintained its commitment to good customer service by streamlining work processes, introducing new automated systems, and giving greater decision-making authority to employees. Ninety percent of Treasury marketable securities auction results were completed within one hour.

The BPD also established the following two measures to evaluate the **percentages of customer service requests completed within four weeks for savings bonds and within three weeks for marketable securities.**

Savings Bonds Requests Completed Within 4 Weeks



Marketable Securities Requests Completed Within 3 Weeks



Goal: Improve the efficiency of production operations and maintain the integrity of U.S. Legal Tender

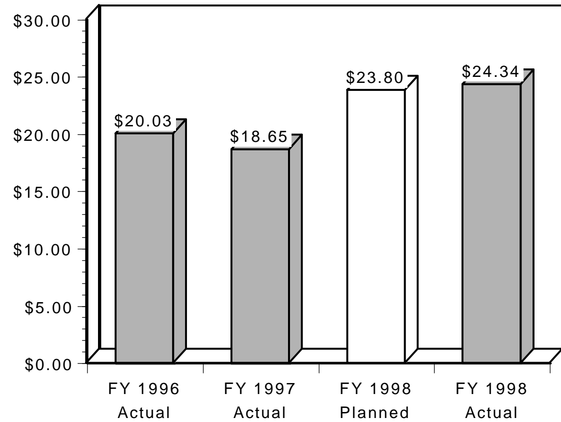
The mission of the **Bureau of Engraving and Printing (BEP)** is to securely and efficiently produce United States currency, postage stamps, and other government securities that satisfy the current and future needs of the American public and the government agencies they serve. In addition, BEP provides technical assistance and advice to other Federal agencies in the design and production of documents, which, because of their innate value or other characteristics, require counterfeit deterrence.

In FY 1998, BEP introduced the redesigned $20 Federal Reserve Note (FRN). With the introduction of the new $20 bill, the Bureau continued its efforts to redesign Federal Reserve Notes (FRN) by incorporating new advanced counterfeit deterrent features. The redesigned notes incorporate advanced counterfeit deterrent features to thwart technological advances available to counterfeiters and maintain the integrity of the Nation's currency, as well as enlarged numerals to aid the visually impaired. Redesigned $100 and $50 FRNs were introduced in 1996 and 1997, respectively. In FY 2000, rede-signed $5 and $10 FRNs will be introduced.

During 1998, 9.2 billion FRNs were delivered to the Federal Reserve System and 19.7 billion stamps were delivered to the U.S. Postal Service. Almost 40 percent of the FRN deliveries were of redesigned currency, and over 90 percent of the postage deliveries were pressure-sensitive (self-adhesive) stamps.

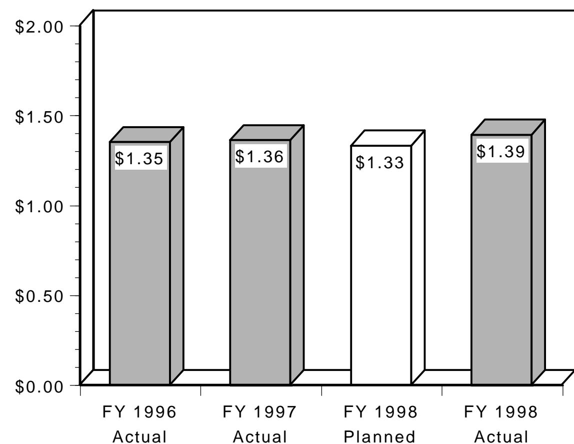
The following program performance measures, which reflect the efficiency and effectiveness of organiza-tional performance, are used to monitor progress towards established goals.

Manufacturing Cost for Currency (per 1,000 Notes)



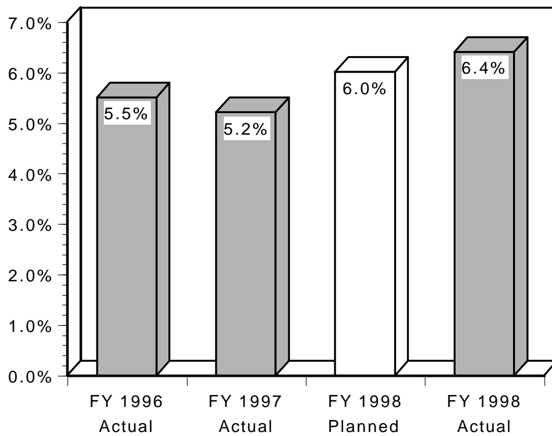
Manufacturing costs for the 100 Stamp Flag Coil were higher than planned, as a result of higher than anticipated spoilage and the wage increases that resulted from the resolution of wage negotiations.

Manufacturing Cost for the 100 Stamp Flag Coil (per 1,000 Stamps)

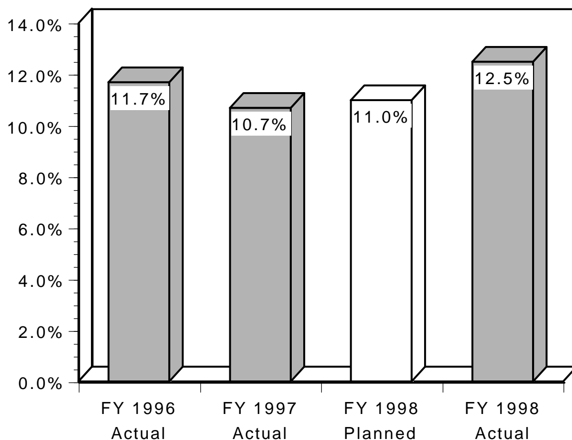


Billing rates and cost standards are developed annually based on the past year's performance, contractual price factors and anticipated productivity improvements. BEP does not receive Federal appropriations; therefore, customer billings are the only means of recovering the costs of operations and generating funds for capital investment.

Currency spoilage was higher than planned in 1998 as a result of higher than anticipated rejection rates during the transition to new electronic inspection equipment. This higher spoilage as well as unanticipated wage increases resulting from the resolution of wage negotiations contributed to manufacturing costs being higher than planned.

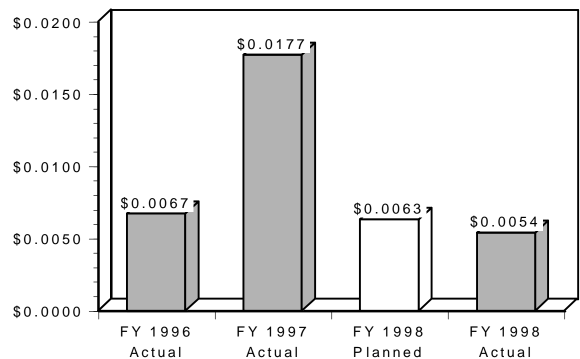


Postage stamp spoilage was higher than planned as a result of shorter production runs.



The mission of the **U.S. Mint** is to manufacture the highest quality circulating, numismatic, and bullion coins at the lowest possible cost and to deliver them in a timely manner, and to sell numismatic and bullion products at a reasonable price and profit. To support its mission, the Mint has identified three major business activities which govern its processes: Production of Circulating Coinage, Production and Sales of Numismatic and Bullion Coinage, and Protection of gold and silver at Ft. Knox and elsewhere.

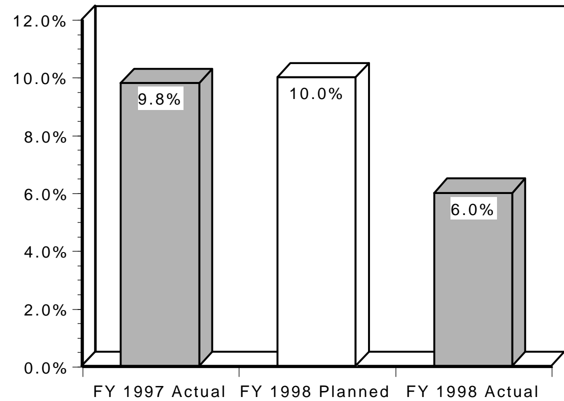
During FY 1998, the Mint produced 15.1 billion circulating coins and shipped 16.6 billion to the Federal Reserve for distribution to banks, a 10.6 percent increase above its projected shipments for the year. By comparison, in fiscal 1997, the Mint produced 14.1 billion coins, shipped 12.8 billion coins to the Federal Reserve. The Mint established performance measures to indicate the cost-efficiency of its production of each denomination of the circulating coins, and the average production cost for FY 1998 decreased significantly from FY 1997, and is well below the planned target.



Sought largely by bullion investors seeking capital gains, Uncirculated Gold American Eagles had their strongest sales performance in history, reaching sales of approximately 1.48 million ounces, nearly doubling the combined sales of FY 1997 and FY 1996. Several factors contributed to this increase in demand: foreign economic and political uncertainties, turbulent equity markets, and perceptions of bargain bullion prices. Sales of Uncirculated Platinum American Eagles continued strong in the second year of production: 143,200 ounces during FY 1998 versus 28,100 ounces in FY 1997.

Proof Platinum American Eagles also performed well in their second year, selling out three individual denominations and almost selling out its four-coin ensemble by the end of the fiscal year. Sales reached 72,412 coins by September 30, compared with 89,194 in fiscal year 1997, with the program year ending in December. The Mint's decision to change the reverse side of the coin each year plus its world-class promotional partnership with Platinum Guild International will carry the program forward.

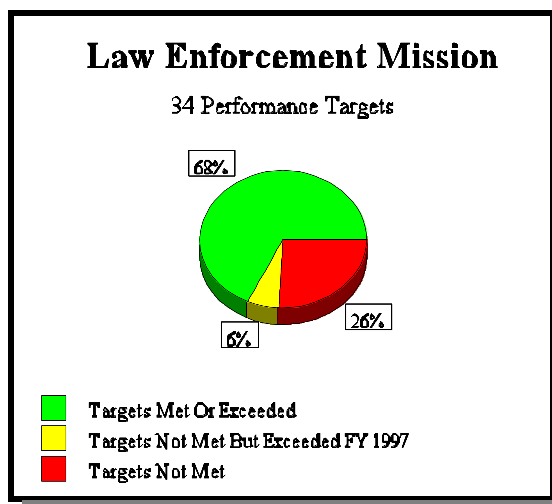
One of the main goals for Numismatic and Bullion Coinage is to increase the contribution of the numismatic/bullion operation by aggressively pursuing new customers, new market channels and new product lines. The Mint uses the Numismatic/Bullion contribution margin, which is based upon the profitability of its coin program, to evaluate how well the programs cover the general and administrative expenses. The Mint experienced unexpected and unprecedented demand for its Eagle bullion programs in FY 1998. Profit margins for these programs, which are statutorily mandated, are nominal and had an overall diluting effect on contribution margin as a percent of sales for Numismatics. Contribution margin would have exceeded Mint's performance goal if the Eagle uncirculated revenues mirrored the FY 1998 plan.



LAW ENFORCEMENT MISSION: PROTECT OUR FINANCIAL SYSTEMS AND OUR NATION'S LEADERS, AND FOSTER A SAFE AND DRUG-FREE AMERICA

Treasury's efforts in this mission area, which represents a significant amount of Federal law enforcement efforts, help foster a safer nation by protecting our borders, preventing drug smuggling, combating violent crime, suppressing counterfeiting, fighting money laundering, preventing financial crimes against the currency of the United States, and training the vast majority of Federal law enforcement personnel.

This mission is supported by the U.S. Customs Service Enforcement Programs, ATF, the U.S. Secret Service, the Financial Crimes Enforcement Network, the Internal Revenue Service (IRS), the Federal Law Enforcement Training Center, and the Treasury Forfeiture Fund.



Goal: Combat financial crimes and money laundering

The mission of the **Financial Crimes Enforcement Network (FinCEN)** is to support and strengthen law enforcement's anti-money laundering efforts by: preventing money laundering through regulatory programs and outreach efforts to the financial industry; providing focused and sophisticated analysis of the elements of major case law enforcement support including trends and patterns of money laundering; and serving as a catalyst to enlist valuable international support by promoting anti-money laundering measures worldwide.

FinCEN continues its Law Enforcement Outreach Program to increase the understanding and knowledge of what is available through FinCEN. As a result of these efforts, there has been an increased participation in its "platform" program. FinCEN established the "self-help" platform program to aid Federal agencies in their investigations by allowing agencies to send representatives to FinCEN to utilize its data sources and research tools to assist in their investigations. In FY 1998, FinCEN exceeded its performance goal, having 73 participants utilizing the system, with the training and assistance provided by FinCEN personnel.

FinCEN continued its "partnership efforts" with the law enforcement, regulatory, and financial communities. FinCEN's goal is to reduce the regulatory burden on financial institutions while at the same time maintaining the quality of regulatory data for law enforcement purposes. This includes an on-going effort to significantly reduce the number of times depository institutions must report large currency transactions. The Money Laundering Suppression Act of 1994 has set a goal for a 30 percent reduction in the Currency Transaction Reports (CTR) filed annually by banks. During FY 1998, FinCEN met its goal of a 5 percent reduction in the number of CTR filed as a result of Phase 1 of the CTR exemption regulations.

In the international area, Treasury, through FinCEN, plays a leadership role in the development of multilateral and bilateral initiatives that encourage the adoption and implementation of international anti-money laundering standards. FinCEN met its FY 1998 performance goal, completing 31 assessments that provided analysis of money laundering situations in a country or region. This demonstrates its efforts to aid countries in meeting the standards for creation of a Financial Intelligence Unit and to encourage governments to adapt international anti-money laundering standards.

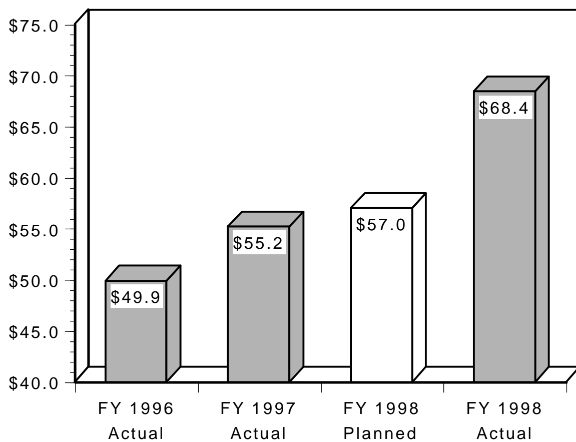
The **U.S. Customs Service's (Customs)** objective is to identify, disrupt, and dismantle the systems and criminal organizations that launder proceeds generated by smuggling, trade fraud, and export violations. Operation Casablanca, a three year multi-agency investigation, was concluded. It was the largest narcotics money laundering investigation ever conducted in the history of U.S. law enforcement. Casablanca involved the cooperation of State, local and foreign law enforcement agencies, as well as almost every Customs SAIC (Special Agent-In-Charge) office, and resulted in the identification and disruption of the essential financial functions of two notorious international criminal enterprises. The operation produced the seizure of over $100 million in drug trafficking proceeds, 2 tons of cocaine, 4 tons of marijuana, over 160 arrests, and the indictment of 26 foreign bank officials and 3 foreign banks.

Other successes include the establishment of the Money Laundering Coordination Center, which enables Customs to develop a more organized and coordinated attack on money laundering organizations. The expan-

of Asset Identification and Removal Groups (AIRGs)
of 30 percent in their seizure activity over FY 1997.

illegally were made totaling $68.4 million. Southwest
seizures increased from $10.4 million in
unreported outbound currency seized in
to $14.4 million, and the Port of Newark made a
ficant contribution by interdicting $11.2 million
in one outbound shipment. Customs was able to exceed
goal of $57 million in currency seizures due to the
increased effort to conduct outbound enforcement
and the implementation of formalized
outbound currency interdiction training.

Seizures of Currency Outbound Only (in Millions)



U.S. is responsible for the
investigation of counterfeiting of currency and securities;

thefts and fraud relating to Treasury electronic funds
transfers; financial access device fraud,
nications fraud, computer fraud, and telemarketing
insured financial institutions. The Secret Service focuses
particularly those involving counterfeiting of U.S.
financial institution fraud, Government program
significant multiple violations.

Financial
percent of Secret Service's criminal investigations
during FY 1998. The Secret Service closed
2,186 financial institution fraud cases, which resulted

reviewed and refined to keep a step ahead of counter-
and counterfeiting technologies. During FY 1998,
investigative cases that resulted in 4,103 arrests, which is

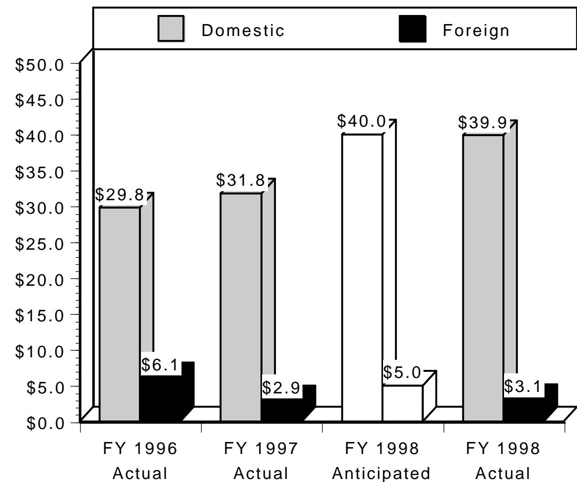
In addition, Secret Service seized abroad $80.5 million
in counterfeit U.S. currency prior to circulation, which
a 32 percent increase over FY 1997. The Secret
Service also suppressed 29 counterfeit plant operations

The Secret Service developed the following perform-ance

Over the last several years, the Secret Service has

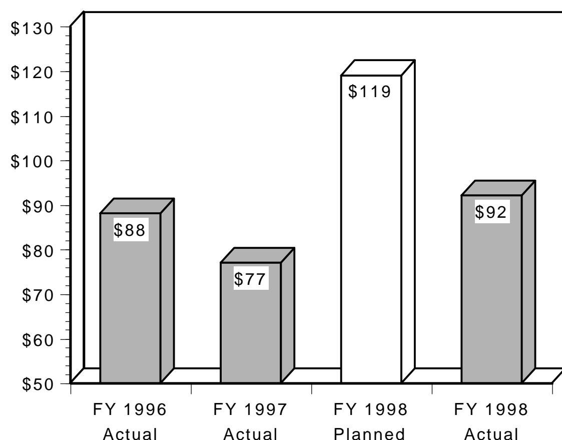
in foreign countries, and this is reflected in a general

Counterfeit Notes Passed



The performance measure, *Counterfeit Notes Passed*
,
is an indicator of the proportion of counterfeit currency

relative to the amount of genuine U.S. currency in circulation.



The **Department of the Treasury Forfeiture Fund (TFF)** was created in 1992 to consolidate all Treasury law enforcement organizations under a single forfeiture fund program administered by the Department. The principal goals of the Treasury forfeiture program are to: (1) punish and deter criminal activity by depriving criminals of property used in or acquired through illegal activities; (2) be cognizant of the due process rights of affected persons; (3) enhance cooperation among foreign, federal, state and local law enforcement agencies through the equitable sharing of forfeited assets; and (4) produce revenues to enhance the forfeiture program and strengthen law enforcement. During FY 1998, revenue generated from these activities totaled $167.2 million in forfeited currency, and the sale of forfeited property totaled $36.7 million.

FY 1998 was a banner year for equitable sharing with our state and local law enforcement partners. For FY 1998, equitable sharing with state and local law enforcement agencies was nearly $72 million, as compared to just over $42 million in FY 1997 and $47.7 million in FY 1996. In addition, the number of payments for equitable sharing was at an all time-high of 4,883 payments. These payments represent forfeited dollars shared directly with state and local law enforcement agencies for their role leading to the federal seizure of assets ultimately forfeited to the Government.

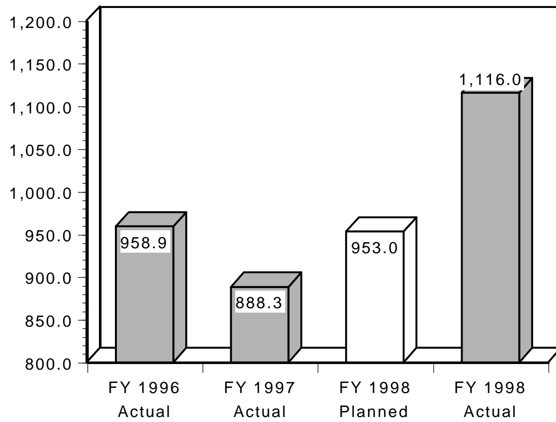
Goal: Reduce the trafficking, smuggling, and use of illicit drugs

The **U.S. Customs Service (Customs)** objective in achieving this goal is to reduce the levels of narcotics entering the United States by creating an effective narcotics interdiction, intelligence, and investigative capability that disrupts and dismantles smuggling organizations. Customs' ambitious narco-tics enforcement agenda included expansion of its enforcement targeting systems and improving intelligence cooperation with foreign governments. It also called for an increase in cooperation with international freight carriers and businesses to prevent smugglers from using their equipment or cargo to smuggle narcotics. Supporting this agenda was a strong continued commitment to improved enforcement training and to the use of nonintrusive technology, such as x-ray, to detect contraband. Finally, there was an increased effort to improve cooperation with other law enforcement agencies, such as the Justice Department, the Department of Defense, and the Drug Enforcement Administration.

SAIC Miami Special Response Team deploying from a Customs Blackhawk helicopter in support of a high-risk law enforcement operation.

These approaches, coupled with a strong investigative program and the Customs air and marine units, resulted in over one million pounds of heroin, cocaine and marijuana, and $368 million of monetary seizure by Customs in FY 1998, compared with 888.3 thousand pounds in seizure of heroin, cocaine and marijuana, and $184 million of monetary seizures during FY 1997.

Total Seizures of Heroin, Cocaine, and Marijuana (Pounds in Thousands)



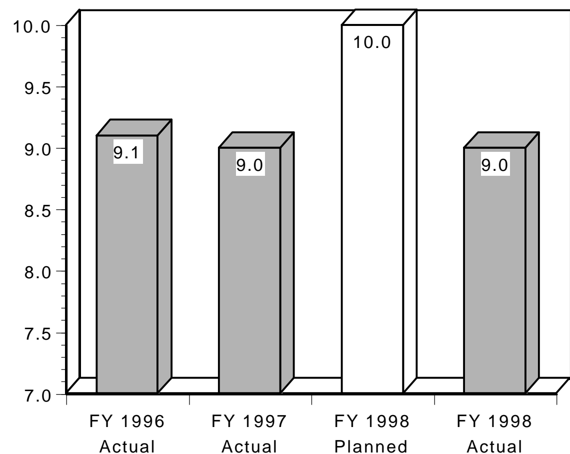
Customs continues to be the primary drug interdiction agency, often seizing more narcotics than all other Federal agencies combined. The quantity of all drugs (including Hashish, Opiates, Khat and Methamphetamiens) seized increased by 22 percent for FY 1998, and the number of seizures increased by 20 percent. The increase in seizures was the result of substantial increases in marijuana seizures.

Plastic tubes of cocaine were discovered hidden inside flower stems. The stems were hollowed out, the tubes inserted, and the ends of the stems reattached.

One of Customs' most notable operational successes this year was Operation Brass Ring, a cooperative Office of Field Operations/Office of Investigations effort conceived using Strategic Problem Solving techniques. During this six month operation, Customs seized 45 percent more drugs (47 percent more marijuana, 32 percent more cocaine, and 13 percent more heroin) than it had during the same time period in FY 1997. Customs also seized $40.5 million in drug proceeds during Brass Ring - an increase of 59%. Customs expanded its cooperative efforts with the trade community and with several Latin and South American countries. Through these programs 136 domestic and foreign seizures were made and 63,882 pounds of narcotics were seized.

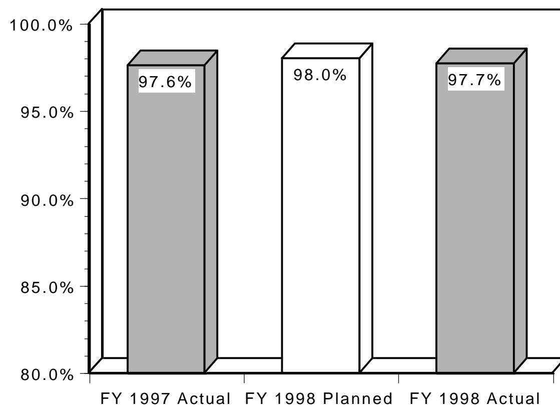
Customs established a performance measure, *Land Vehicle Targeting Efficiency*, to estimate how well it is selecting vehicles for inspection at land borders. Customs targeting efficiency remained at 9.0 times more productive than random selectivity. Current targeting capabilities appear to limit the ability of Customs to increase its targeting efficiency levels. In an effort to remedy this, Customs is embarking on a program to link Department of Motor Vehicle records into its lookout system. In FY 1999, a prototype Southwest border port will be used to test the validity of this approach. Full implementation will occur in FY 2000, if this approach proves to be effective and funding is available.

Land Vehicle Targeting Efficiency



Passenger processing is one of the most visible functions of Customs. Its goal is to ensure compliance

with laws and regulations by targeting, identifying, and examining high-risk travelers, and to allow the expeditious movement of low-risk travelers. Customs achieved an *Air Passenger Compliance Rate* of 97.7 percent for FY 1998, and the resulting 0.1% increase from 97.6% in FY 1997 represents approximately 62,000 compliant air passengers. To reach the 98 percent target, Customs will be working to improve its outreach program by identifying new methods and improving existing ones to disseminate advanced information to travelers, especially before they depart the U.S. Customs also will continue to focus on improvements to its targeting systems.



Goal: Fight violent crime

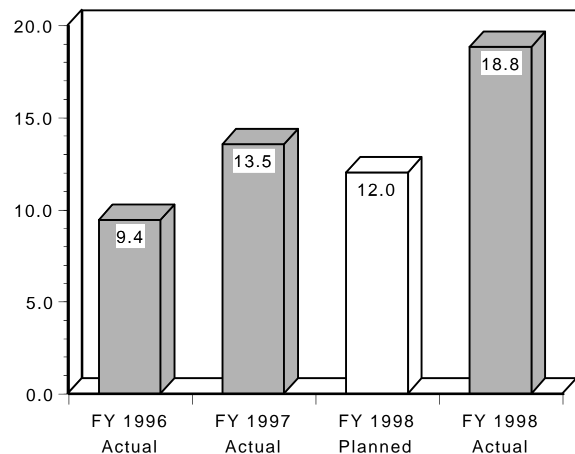
To support its unique mission, one of the strategic goals of the **Bureau of Alcohol, Tobacco and Firearms (ATF)** is to effectively contribute to a safer America by reducing the future number and cost of violent crimes. This goal is achieved through the following four programs.

Deny criminals access to firearms program

ATF developed various projects and services to focus on denying criminals access to firearms by identifying, deterring, and stopping the sources of and participation in illegal firearms trafficking. An important initiative is a focused component of ATF's nationwide *Illegal Firearms Trafficking Project*, which identifies and investigates the illegal sources of guns to youths and juveniles. ATF developed the *Youth Crime Gun Interdiction Initiative* in FY 1996 and the major goal is to trace all recovered crime guns in participating cities, which increased to 27 by the end of FY 1998. ATF also seeks to reduce thefts of firearms from Federal firearm licensees and interstate carriers transporting firearms through collecting and analyzing firearms licensee and interstate carrier theft information, and providing investigative leads to special agents.

ATF's National Tracing Center is the only operation of its kind in the world. This facility traces firearms recovered in crimes and from juveniles for any Federal, state, local or international law enforcement agency. A firearm trace result is frequently the crucial piece of evidence that can link a criminal to a firearm-related crime and allow law enforcement officials to make an arrest. At a minimum, firearms tracing information provides investigators with leads on the origin of the crime-related firearms in their investigations. This performance measure evaluates the period of time from the moment the data for the search is entered into the system to the time it receives a closing code showing its disposition. ATF's goal is to continue to provide timely service by reducing the number of working days it takes for tracing firearms.

Safeguard the Public from arson and explosives incidents program



ATF's arson and explosive projects are directed toward preventing the criminal misuse of explosives and the crime of arson, as well as providing effective post-incident response. ATF's efforts in conducting proactive investigations of arson-for-profit schemes

save money for the insurance industry, and ultimately the American public, by exposing millions of dollars in fraudulent claims annually. ATF's commitment in supporting the arson and explosive program is to maintain the highest standards of investigative expertise and technology necessary to most effectively respond to major bombing and arson incidents.

In 1996, at the request of Congress, ATF established a National Repository of information on arson incidents and the criminal misuse of explosives throughout the United States. This National Repository will be an extension of the ATF *Arson and Explosive Incidents System* (AEXIS) and will incorporate information from a variety of law enforcement and fire service sources. This system will assist authorized investigators in identifying trends and similarities between arson and explosive incidents, link thefts of explosive materials with the later criminal misuse of the explosives, and link investigators working on similar incidents.

Remove violent offenders from our communities program

This program involves projects and services to investigate, arrest and recommend for prosecution, the most violent criminals who use firearms and explosives in furtherance of their criminal activity. The *Achilles* project uses specific Federal firearm laws that mandate extended mandatory periods of incarceration to remove the most dangerous, armed career criminals and armed drug traffickers from the streets. In addition, through firearms tracing, the illegal firearms sources for these violent criminals are investigated under ATF's *Illegal Firearms Trafficking Project*. Under the *National Integrated Ballistics Information Network* program, ATF is utilizing a state-of-the-art system that allows firearms technicians to digitize and automatically correlate and compare bullet and shell casing signatures at a greatly accelerated rate.

Prevent violence through Community Outreach program

This program focuses on community efforts designed to encourage and participate in the prevention of violence. The *Gang Resistance Education and Training (GREAT) Program* provides classroom instruction for school-aged children and a wide range of community-based activities, resulting in the necessary life skills, a sense of competency, usefulness, and personal empowerment needed to avoid involvement in youth violence and criminal activity. Testimonies given to the Senate Appropriations Committee on behalf of the GREAT program by participating students and law enforcement officers resulted in a long-term plan to expand the program to non-school environments, such as Boys Clubs and Girls Clubs.

Goal: Protect our nation's leaders and visiting world leaders

The primary objective of the **U.S. Secret Service** is to provide the maximum physical protection possible for the President, the Vice President, and other dignitaries when the protectee is in residence or in a travel status. As a rule, efforts to provide security increase dramatically when the protectee is traveling. The Secret Service measures protectee travel activity in terms of travel stops, which is a city or other definable subdivision visited by a protectee. During FY 1998, the Secret Service provided physical protection at 5,131 travel stops. Protection was also provided at the Drug Summit and the United Nations General Assembly, both in New York City.

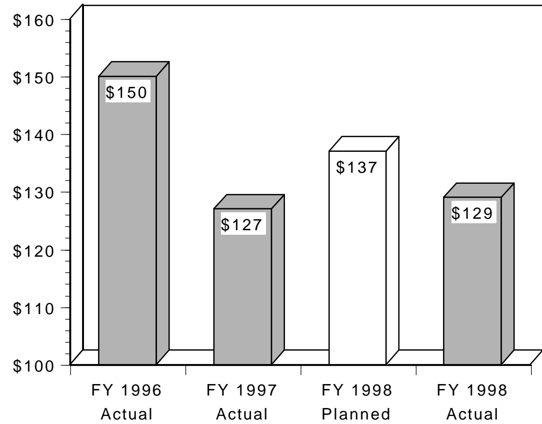
Goal: Provide high quality training for law enforcement personnel

The **Bureau of Alcohol, Tobacco and Firearms (ATF)** provided training and instruction in all aspects of explosives handling, storage, and destruction for Federal, state, local and foreign law enforcement officers, and members of the explosives and pyrotechnics industries. In 1989, the ATF began a joint formal training program with the Connecticut State Police for accelerant-detecting canines to support state and local jurisdictions (accelerant-detecting canines search for liquid catalysts that can be used to speed up the spread of fire). Through FY 1998, a total of 60 canines have been trained and certified by ATF for state and local agencies, including 6 additional canines in FY 1998. ATF also provides canine training for explosive detection to foreign countries to be used overseas in the war against terrorism and to protect Americans traveling abroad against terrorism. To date, ATF has trained 160 explosive detecting canine

teams which are deployed in eight countries worldwide, including 21 additional canine teams and two canine trainers in FY 1998. ATF also is the only Federal agency having two full-time fire protection engineers devoting solely to the analyses of origins and dynamics of fire as they pertain to criminal investigations. During FY 1998, ATF also provided 22 “train-the-trainer” classes to 668 police officers participating from across the United States in the ATF’s *Gang Resistance Education and Training Program (GREAT).*

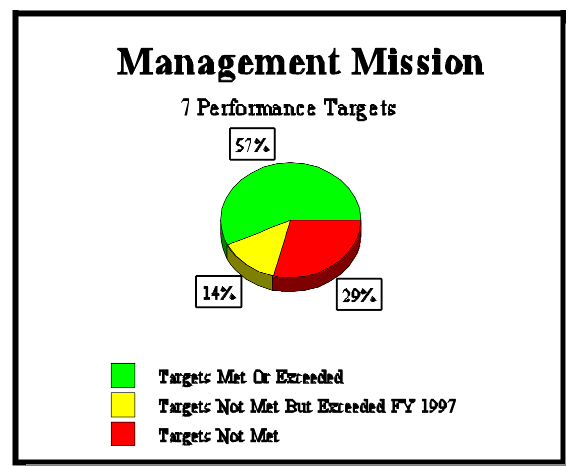
The **Federal Law Enforcement Training Center (FLETC)** is an interagency organization providing law enforcement training to the majority of the Federal, state, local, private sector security, and foreign law enforcement officers. Its goals are to provide law enforcement personnel with state-of-the-art knowledge and techniques used in the law enforcement profession; provide for all basic training direct costs from FLETC appropriations; and fully develop the cost effective potential through consolidation of Federal law enforcement training at FLETC.

FLETC established a performance measure, *Student Survey on Quality of Basic Training,* to evaluate the quality of its law enforcement training. This information will assist the FLETC in the continuing review of its program curricula. This performance was previously measured on a scale of 0-6, with 6 being highest quality. However, after years of data collection, it became clear that FLETC should change its reporting standard to a frequency (percentage) of students who answer satisfactory or better, rather than using an undefinable mean-value. Frequency reporting is the preferred method of researchers. Therefore, this performance goal for FY 1998 is changed to 80 percent of students who answered satisfactory or better, and this goal was achieved by FLETC.
FLETC also established a performance measure to evaluate whether it is providing the most effective, efficient, and innovative consolidated law enforcement training and related services.



MANAGEMENT MISSION: CONTINUE TO BUILD A STRONG INSTITUTION

This fourth mission area -- management -- focuses on the continued emphasis on a strong and efficient organization in order to succeed in accomplishing program goals. This mission area affects all bureaus. It includes objectives under the goal to improve management operations which address Human Resource Management, Equal Employment Opportunity (EEO), bureau oversight responsibilities, financial management, information technology, and procurement. Under the goal of improving program performance are objectives to improve customer service, foster partnerships, and modernize operations.



Goal: Improve management operations

Treasury continued to emphasize a strong and efficient organization in order to effectively accomplish our programmatic goals. Performance improvement initiatives were implemented in several areas, including financial, information, and human resource management, as well as customer service.

The **Office of the Assistant Secretary for Management and Chief Financial Officer** serves as the principal policy advisors on matters involving the internal management of the Department and its bureaus. One of the objectives is to improve Treasury's capacity to recruit, develop, and retain high-caliber employees. This is accomplished through efforts in improving our recruitment program which promotes quality and diversity, and enhancing the selection strategy. Efforts to recruit high caliber employees include establishing relationships with schools, including those having large minority populations.

The Department also undertook a major effort to transform human resources management and improve service delivery of human resources processes through a department-wide integrated human resources system. Through partnership with labor union and management, Treasury continues to implement more effective human resource management practices, and to create a ethnically diverse and competent workforce able to respond to changes in customer needs and the technologies of the workforce. In addition, efforts were made to provide resources for training opportunities, which allows the professional development of employees and enables the Department to achieve its unique missions.

Treasury has been focusing much effort and resources to address the **Year 2000 compliance** issue. Treasury participated in the Year 2000 Financial Institutions Working Group under the President's Year 2000 Commission to ensure improvement and modernization of the U.S. financial system. This Group's goals are to map the pathways traveled by all financial transactions, making sure each link in each pathway is Year 2000 compliant and tested from one end to the other, and to coordinate the government agencies' Year 2000 demands on financial institutions to avoid overlapping requirements.

Treasury's Year 2000 compliance process entails three key components: renovation; validation; and implementation. The following table provides the status of Treasury's progress as of September 30, 1998.

323 Mission Critical IT Systems

Compliant	Being Replaced	Being Repaired	Being Retired
204	26	88*	5

* 86.8% have completed Renovation, 70.5% have completed Validation, and 62.4% have completed Implementation.

3,964 Mission Critical Non-IT Systems

Compliant	Being Replaced	Being Repaired	Being Retired
2,575	55	78	7

As of September 30, 1998, Treasury's total budget estimate for Year 2000 compliance was $1.9 billion.

Significantly, three bureaus (U.S. Customs Service, Engraving and Printing and the Office of Thrift Supervision) are fully Year 2000-compliant and all others are in or beyond the validation stage. We anticipate 99% compliance by March 1999 and full compliance well ahead of the millennium. The Office of the Comptroller of the Currency and Office of Thrift Supervision, in their supervisory capacities, have been working effectively with banks and thrifts, as well as with the Federal Reserve, to ensure the continued stability of our national financial systems regarding Year 2000 exposures. Similarly, FMS has been working closely with the Social Security Administration, and Year 2000 testing efforts to date on payments to beneficiaries have gone quite well.

Status of Contingency Planning:

A business continuity planning consultant has been engaged to assist system and infrastructure managers in accomplishing contingency planning. The consultant will develop detailed written guidance and workshop materials, and provide training to managers and their personnel.

Status of Business Continuity and Contingency Plans

A Business Continuity Planning Project has been established to provide the Departmental Offices (DO) with the guidance, training and assistance needed to develop Business Continuity Plans (BCPs) for their operations. A seven step business continuity planning process has been established, and a BCP Handbook has been developed which provides the DO with detailed procedures for accomplishing this process. In addition, BCP Workshops are being conducted to provide DO planners with training in the development, preparation, and implementation of their BCPs.

Because Year 2000 compliance is perhaps our highest priority, we are devoting all possible resources to this issue and providing constant management oversight on progress throughout the Department.

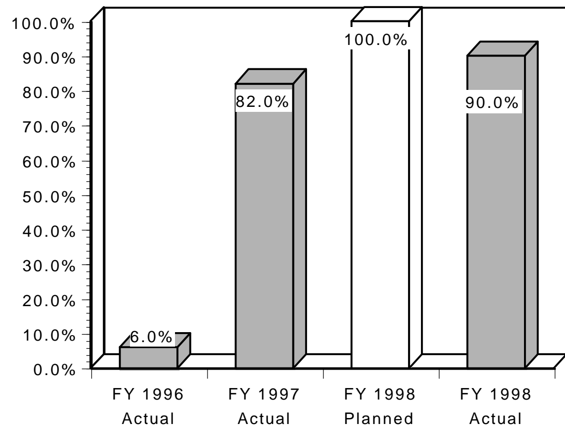
The **Office of Inspector General** reorganized its Office of Investigations to meet the increasing demand of conducting quick-response investigations and special inquiries of importance to the Department, the Congressional committees and the public. The OIG exceeded its performance goal for potential dollar savings identified through audit activities by more than 200 percent. Two program audits generated approximately $65 million in potential revenue enhancements.

Goal: Improve program performance

Treasury significantly increased its compliance with the GPRA requirements by implementing the reporting requirements of Results Act ahead of schedule, in order to use it as a tool to improve program performance and management.

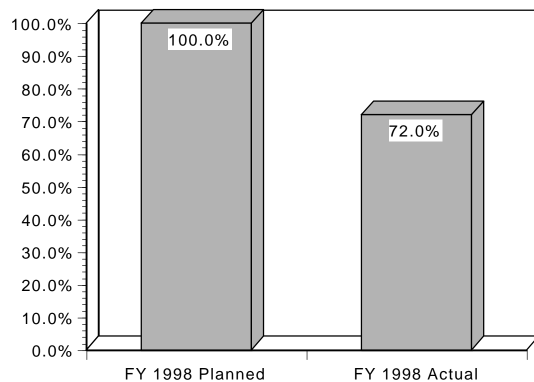
Significant progress has been made during this past year to improve and refine performance measures throughout the Department, striving specifically to present key measures of program ***results*** rather than the traditional output-oriented or workload measures. Consequently, many of the measures from FY 1996 have been changed for FY 1999 and FY 2000.

Compliance With GPRA



In response to Executive Order #12862 and direction in the Treasury Strategic Plan, the bureaus established a total of 105 customer service standards for FY 1998. The goal was to meet these standards at least 90 percent of the time, and 72 percent of the 105 customer service standards met this goal in FY 1998. Treasury recognizes that some of the feedback mechanisms need improvement.

Customer Service Standards Met At Least 90 % of the Time



Significant progress was made in reorganizing and restructuring the **Internal Revenue Service (IRS)**, shifting from a focus on revenue collection and enforcement to a taxpayer-service oriented organiza-tion. In January 1998, the Commissioner announced a Concept for Modernizing the IRS. This Concept calls for serving taxpayers better and productivity through a quality work environment. Major portions of the Concept were mandated in the IRS Restructuring and Reform Act (RRA) of 1998. IRS also restated

its mission to emphasize serving the public and meet taxpayer needs and expanded taxpayer rights in several areas.

The RRA also established the position of National Taxpayer Advocate (NTA) who reports directly to the IRS Commissioner and was given expanded authority and independence to assist taxpayers. The NTA also has the authority to issue a Taxpayer Assistance Order which can provide relief to taxpayers in hardship situations.

The **Treasury Franchise Fund** completed its second year of operation as an entrepreneurial governmental enterprise. The Fund was established (pursuant to the Government Management and Reform Act of 1994) to provide common administrative support services to other components within Treasury and/or to outside agencies, on a competitive and fully cost-reimbursable basis. The Fund operates in a business-like manner by creating and maintaining a business relationship and environment that promotes customer participation and satisfaction.

FY 1998 was another year of significant transition and growth for the Department of the Treasury's Franchise Fund. Efforts continued to improve the organization, customer service, operating techniques, customer relationships and outlook -- striving to create a more dynamic, service-driven organization that continues its emphasis on products that "exceed expectations" of customers. The key strategies employed to improve and strengthen the Fund's operations include:

- Improving its competitive position through creativity and innovation, best practices, and benchmarking;
- Making quality the motivating force behind not only every product/service, but every task performed in the delivery of the product or service. The Fund wants its customers to be satisfied not only with what it sells but with how it sells; and
- Maintaining cost-effectiveness by reducing bureaucracy, removing divisional boundaries and embracing the intelligence and creativity of its employees.

The table represents the overwhelming success in Treasury Franchise Fund's effort to reinvent and modernize operations to achieve efficiencies.

TREASURY FRANCHISE FUND
KEY FINANCIAL DATA

(In Millions)

	FY 1998	FY 1997	% Change
Total Revenue	$80.398	$38.484	109%
Net Income	$2.393	1.473	62%
Total Assets	$27.822	$14.325	94%
Cumulative Results of Operations	$6.738	$3.211	110%

The revenue increase is reflective of: 1) Five new business activities that began operations under franchising in FY 1998 (generating approximately $17 million); and 2) increased sales from those existing business activities (approximately $25 million).

Efforts continued to reinvent and modernize Treasury's operations to achieve efficiencies. **The Electronic Funds Transfer (EFT) '99 Program** continued to progress according to schedule which include the issuance of EFT regulation (Final Rule 208) and the draft notice of ETA (Electronic Transfer Account). The EFT '99 Public Education Campaign was initiated with the distribution of print and video marketing materials, and the broadcasting of public service announcements by major TV stations. The campaign also involves regional community outreach effort which encompasses five regions nationwide with teams in place to work with local and regional financial organizational, consumer and community based organizations to educate individual Federal payment recipients about EFT 99 through materials distribution and "in-touch" workshops and seminars.

SIGNIFICANT ISSUES AND CHALLENGES

Overall Priorities

Secretary Rubin and senior management officials have developed a comprehensive list of Departmental priorities for the coming year which cover a broad range of activities, from tax and budget issues to drug interdiction and gun control, from dealing with the global financial crisis to addressing inner city poverty, from the management of the government's debt to the reform of the regulatory structure of the U.S. financial system to the promotion of economic growth both at home and abroad. More specifically, these priorities include:

1. ***Maintaining fiscal responsibility:*** This includes the FY 2000 budget, social security reform, review of the income tax code to simplify and streamline reporting requirements and defend the code's integrity, Federal debt management practices, Medicare reform issues and defining our role in management of privatizations and identifying further opportunities for privatization.

2. ***Providing leadership in the global economy:*** This includes activities related to the global financial crisis, international financial architec-ture reform, trade issues, growth in the industri-alized nations such as Japan, Europe and United States, and international tax policies.

3. ***Enhancing financial security:*** This includes activities related to consumer education and protection, consumer-oriented financial crimes, and bankruptcy reform.

4. ***Bringing low-income people into the economic mainstream:*** -- This includes improving the economic prospects of people in the inner cities and distressed rural communities, and helping to build safe communities in which economic activities can expand.

5. ***Maintaining a strong and healthy financial system:*** This includes pursuing financial modernization of the national banking system

and electronic commerce initiatives, anti-counterfeiting efforts, and the fight against financial crimes.

6. ***Building safer communities:*** This includes initiatives on drug control and border enforcement, firearms violence reduction, terrorism enforcement and alcohol policy for teens.

7. ***Strengthening Treasury as an institution:*** This includes human resources reform, IRS restructuring efforts, improving overall management practices and debt collection efforts, ensuring Year 2000 compliance, and continuing to improve Government-wide audited financial statements.

Year 2000 Compliance

This is one of the highest priorities and time-sensitive issues facing Treasury. Treasury's information systems, especially those related to revenue collection and disbursement of funds, are crucial to the financial operations of the Federal government. Further, Treasury's systems have a direct influence on many facets of the U.S. and world economies. The rapid approach of the new millennium and its impact on Treasury's information systems require the most cost-effective approach to plan and manage the century date conversion effort. Senior management at the Treasury bureaus and the Department are strongly committed in this resource-intensive effort.

Treasury also has expanded its Year 2000 work to encompass a number of related systems issues. During the past six months, Treasury has devoted additional resources to both its general security program and the security functions falling under the Chief Information Officer. This overall effort also has included establishing security criteria earlier in the systems development life cycle, and providing a greater level of Departmental guidance to the bureaus on systems security issues.

Data and EDP Security

Financial statements audits at Treasury bureaus identified weaknesses relating to internal controls over the data in the automated systems. Major computer systems at several bureaus are still vulnerable to unauthorized access. Both GAO and Department's OIG consider this material weakness as one of the top management challenges to prevent unauthorized access to its program and financial systems and to protect sensitive data related to Treasury's missions. Some of the recommendations include: 1) improve computer security over mainframe and automated systems; 2) limit users' access to operating systems and perform periodic reviews of user access capability; 3) develop comprehensive disaster recovery plans; and 4) implement a single integrated core financial system.

Bureaus have developed corrective action plans to implement the audit recommendations, and management will monitor the progress and status of these corrective actions. Implementation of these audit recommendations is critical in ensuring the data integrity of information maintained in the automated systems and enabling Treasury to prepare financial statements that are fully auditable.

Treasury implemented the Treasury Information Executive Repository (TIER) system, a Department-wide financial management data warehouse, which receives selected monthly financial data from bureaus and other reporting entities. Enhancements are being made to the TIER system to meet the requirements of the FASAB standards and the additional financial statements. In addition, the Department is implementing the CFO Vision™ developed by the SAS Institute, which will perform analyses and generate reports based on the consolidated Departmental data in the TIER system. The CFO Vision™ will be used to produce the Department's consolidated financial statements in accordance with the OMB Bulletin No. 97-01, and analyze budget and accounting data.

Internal Revenue Service Modernization and Restructuring

In early FY 1998, Charles Rossotti was named Commissioner of the IRS following an extensive Treasury Department led search process. Mr. Rossotti has brought private sector management experience and talent to the IRS, and it is his

concept of modernization that will largely be implemented in the upcoming IRS restructuring. The Problem Solving Days were implemented in November, 1997 in response to Senate Finance Committee hearings on taxpayer problems. The Department partnered with IRS to bring these about and Secretary Rubin attended the first Problem Solving Day in Baltimore, Maryland. After the President announced the formation of Citizen Advisory Panels in early FY 1998, a joint Treasury/IRS task force completed foundation documentation and the planning necessary to launch the panels in accordance with the Federal Advisory Committee Act.

The IRS Restructuring and Reform Act of 1998 required significant changes in IRS' organization structure, business processes, and requirements. The Act created a nine-person Oversight Board, with six members from the private sector, to oversee the administration and strategic planning at the IRS. The Act also provided many important taxpayer protections which coincides with the Commissioner's modernization plan with its new mission statement: "***Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.***"

IRS has made progress in implementing recommendations to strengthen its modernization capability and improve its management processes. IRS had developed a Modernization Blueprint which outlines the manage-ment practices and development processes to manage the modernization. The Chief Information Officer plans to fully implement GAO's recommendations before IRS begins building its modernized systems, and IRS will reexamine its blueprint in light of the ongoing organizational restructuring. IRS also has an investment review board to select, control, and evaluate its information technology investments. IRS is working with its Prime Integration Support Contractor (PRIME) to define key components of the blueprint, to acquire and implement modernized tax systems in accordance with the blueprint, and to account for changes as a result of implementing the Restructuring and Reform Act of 1998.

Because of the importance and high cost of the modernization and because key recommendations provided by GAO have not been implemented, this issue is still considered as a "high risk" program by the GAO.

Financial Management Weaknesses

Management reviews and audits conducted by the GAO and the Treasury's Office of Inspector General identified financial management weaknesses which hinder Treasury's ability to achieve our missions and program objectives. These weaknesses also have a significant impact on the Treasury bureaus' ability to carry out their programs or prepare timely financial statements. In addition, these weaknesses are a major factor preventing the Department from receiving an unqualified opinion on its annual financial statements.

Part III of this Accountability Report provides specific financial management weaknesses for which the Department has initiated aggressive corrective actions to resolve. The majority of these weaknesses are concentrated in Financial Management Service, Internal Revenue Service, U.S. Customs Service, and Departmental Offices. The Department also recognized four new material weaknesses associated with the District of Columbia pension responsibilities, which were assumed in October 1997.

Consolidated Financial Statements (CFS) for the Federal Government

The Department of the Treasury is responsible for preparing consolidated financial statements of the Federal government. A number of problems were identified in the audit of fiscal year 1997 CFS which resulted in a disclaimer of audit opinion from the GAO. Significant deficiencies in the agencies' financial systems seriously hampered Treasury's ability to obtain timely and reliable information for the Government-wide financial statements. In addition, new Federal accounting standards and new reporting requirements continue to be a major challenge for the entire Federal government. GAO reported that problems with fundamental record-keeping, incomplete documentation,

and weak internal controls prevent the government from accurately reporting a large portion of assets, liabilities, and costs. GAO recommended that Treasury work with agencies to address some of these problems: 1) ensure proper accounting for basic transactions, especially those between governmental entities; 2) ensure information reported for the CFS is consistent with the agencies financial statements and that reconciliations are conducted on a periodic basis; and 3) ensure that all disbursements are properly recorded and reconciled with Treasury's records.

Treasury has developed action plans and is working with GAO, Office of Management and Budget (OMB), and key agencies to address these problems. Fixing these problems represents a significant challenge because of the size and complexity of the government, and the discipline needed to comply with the new accounting and reporting requirements. Meeting this challenge will require strong management commitment, adequate training of workforce and improved integrated financial systems at the Federal agencies.

IRS Accounts Receivable

The IRS accounts receivable and delinquent debt issues continue to be an IRS and Departmental management priority, and progress is being reported in Treasury's quarterly report on its Management Control Program. This report monitors specific actions taken by Treasury bureaus to resolve the Department's most significant material weaknesses.

IRS has developed action plans to resolve the workload of Tax Assessments and prioritize collectible assessments. The challenge is to maintain a balanced approach between collecting as early in the collection process as possible, while still aggressively pursuing non-compliance through enforcement actions in an effort to promote voluntary compliance.

IRS is continuing to develop systems that will help in dealing with the collection of tax assessments and prevent future delinquencies.

Debt Collection

The Debt Collection Improvement Act of 1996 enhanced the Federal Government's ability to service and collect debts. Individuals, businesses, and foreign governments owed Federal agencies in excess of $50 billion in delinquent non-tax debt. About $29 billion or 56 percent is referable to Treasury. A significantly smaller amount (between $860 million and $1 billion annually) is likely to be collectible.

FMS is working with approximately 50 agencies to increase debt referrals. In January 1999, the Tax Refund Offset Program was merged into the Treasury Offset Program. This merger is one of the most important DCIA goals. The number of participants in the offset program increased from 17 to 37 agencies. Debt referrals increased from $9.4 billion in FY 1997 to nearly $17 billion in FY 1998.

Efforts continue to put a complete infrastructure in place to maximize the collection of delinquent debts. Detailed information on debt collection efforts is described in Part IV of this report (Supplemental Information).

Department of the Treasury

Consolidated Balance Sheet
As of September 30, 1998
(In Millions)

ASSETS	
Entity Assets:	
Intra-governmental Assets	
Fund Balance (Note 2)	$36,440
Loans & Interest Receivable (Note 3)	46,976
Investments and Related Interest (Note 4)	17,066
Other Intra-governmental Assets	156
Total Intra-governmental Assets	100,638
Cash, Foreign Currency, and Other Monetary Assets (Note 5)	21,235
Loans and Interest Receivable, Net (Note 3)	503
Investments and Related Interest (Note 4)	7,120
Reserve Position in the International Monetary Fund (Note 6)	21,155
Investments in International Financial Institutions (Note 7)	5,012
Inventories and Related Property, Net (Note 8)	365
Property, Plant & Equipment, Net (Note 9)	1,461
Other Assets	179
Total Entity Assets	157,668
Non-Entity Assets:	
Intra-governmental Assets	
Fund Balance (Note 2)	47,891
Due from the General Fund (Note 10)	5,247,189
Accounts Receivable & Related Interest, Net	152
Advances to the Black Lung Trust Fund (Note 11)	5,857
Investments and Related Interest (Note 4)	343
Loans and Interest Receivable (Note 3)	154,234
Total Non-Entity Intra-governmental Assets	5,455,666
Cash, Foreign Currency, and Other Monetary Assets (Note 5)	41,792
Gold & Silver Reserves (Note 12)	11,041
Tax/Trade, Other Non-entity Receivables, and Related Interest, Net (Note 13)	30,164
Other Assets	20
Total Non-Entity Assets	5,538,683
Total Assets	$5,696,351

The accompanying notes are an integral part of these statements

Department of the Treasury

Consolidated Balance Sheet

As of September 30, 1998

(In Millions)

LIABILITIES

Liabilities Covered by Budgetary and Other Resources	
Intra-governmental Liabilities	
Loans Payable & Interest (Note 14)	$50,601
Other	471
Total Intra-governmental Liabilities Covered by Budgetary Resources	51,072
Interest Payable on Debt (Note 17)	45,417
Certificates Issued to Federal Reserve Banks (Note15)	9,200
Allocations of Special Drawing Rights (Note 5)	6,719
Gold Certificates Issued to Federal Reserve Banks (Note 12)	11,017
Refunds & Drawbacks Payable	1,384
DC Pension Liability (Note 16)	3,451
Other Liabilities	2,725
Total Liabilities Covered by Budgetary Resources	130,985
Liabilities Not Covered by Budgetary and Other Resources	
Intra-governmental Liabilities	
Federal Debt & Interest Payable (Note 17)	1,785,180
Other	144
Total Intra-governmental Liabilities Not Covered by Budgetary Resources	1,785,324
Federal Debt & Interest Payable (Note 17)	3,694,516
DC Pension Liability (Note 16)	5,157
Other Liabilities	1,281
Total Liabilities Not Covered by Budgetary Resources	5,486,278
Net Position (Note 19)	79,088
Total Liabilities & Net Position	$5,696,351

The accompanying notes are an integral part of these statements

Department of the Treasury

Consolidated Statement of Net Cost

For the Year Ended September 30, 1998
(In Millions)

Costs:	Combined	Elimination	Consolidated
Program A --Economic: Promote Prosperous and Stable American and World Economies			
Intragovernmental Costs	$62		$62
With the Public	2,870		2,870
Total	2,932		2,932
Less Earned Revenues	2,054		2,054
Net Program Costs	878		878
Program B -- Financial: Manage the Government's Finances			
Intragovernmental Costs	$6,805		$6,805
With the Public	9,558		9,558
Total	16,363		16,363
Less Earned Revenues	6,892		6,892
Net Program Costs	9,471		9,471
Program C -- Law Enforcement: Protect Our Financial Systems and Our Nation's Leaders and Foster a Safe and Drug Free America			
Intragovernmental Costs	$565		565
With the Public	1,495		1,495
Total	2,060		2,060
Less Earned Revenues	82		82
Net Program Costs	1,978		1,978
Costs not assigned to programs:			
Reimbursable Costs Incurred for Other Treasury Suborganizations	385	(385)	0
Other	1,093		1,093
Total	1,478		1,093
Less earned revenues not attributed to programs:			
Reimbursements Earned from Other Treasury Suborganizations	385	(385)	0
Other	340		340
Total	725		340
Net Unassigned Costs	753		753
DEFERRED MAINTENANCE (Note 9)			
NET COST OF TREASURY OPERATIONS	$13,080		$13,080
FEDERAL DEBT INTEREST COSTS	363,333		363,333
OTHER FEDERAL COSTS - Note 20	8,011		8,011
NET COST OF OPERATIONS AND FEDERAL DEBT INTEREST	$384,424		$384,424

NOTE: The Combined Statement of Financing does not include intra-agency eliminations

The accompanying notes are an integral part of these statements

Department of the Treasury

Consolidated Statement of Changes in Net Position

For the Year Ended September 30, 1998
(In Millions)

Net Cost of Operations	$384,424
Non-Exchange Revenues and Financing Sources	
Appropriation Used	391,964
Revenue from Forfeiture	139
Interest Revenue	21
Imputed Financing Sources	668
Transferred in	57
Transferred out	(705)
Other (Note 24)	(4,401)
Total Financing Sources	387,743
Net Results of Operations	3,319
Prior Period Adjustments (Note 19)	4
Net Change in Cumulative Results of Operations	3,323
Increase (Decrease) in Unexpended Appropriation	(7,720)
Change in Net Position	(4,397)
Net Position as of 10/1/97	83,485
Net Position as of 9/30/98	$79,088

The accompanying notes are an integral part of these statements

Department of the Treasury

Combined Statement of Budgetary Resources

For the Year Ended September 30, 1998

(In Millions)

Budgetary Resources	
Budget Authority	$393,097
Unobligated Balance	42,535
Spending Authority from Offsetting Collections Earned	9,275
Adjustments, Anticipated for Rest of Year	329
Total Budgetary Resources	445,236
Status of Budgetary Resources	
Obligations Incurred	397,514
Unobligated Balances Available	46,898
Unobligated Balances Not Available	824
Total Budgetary Resources	445,236
Outlays	
Obligations Incurred	397,514
Spending Authority from Offsetting Collections and Adjustments	(9,732)
Obligated Balance, Net-Beginning of the Period	8,509
Obligated Balance Transferred, Net	(115)
Obligated Balance, Net-End of Period	(8,628)
Total Outlays	$387,548

The accompanying notes are an integral part of these statements

Department of the Treasury

Combined Statement of Financing

For the Year Ended September 30, 1998
(In Millions)

Obligations and Nonbudgetary Resources	
Obligations Incurred	$397,514
Less: Spending Authority from Offsetting Collections and Adjustments	(9,732)
Donations Not in the Budget	0
Imputed Financing	668
Transfers-in (out)	(595)
Exchange Revenue Not in the Budget	(103)
Other	(5,320)
Total Obligations as Adjusted and Nonbudgetary Resources	382,432
Resources Not Funding Net Cost of Operations	
Change in Undelivered Orders	(510)
Capitalized Costs	(890)
Financing Sources that Fund Costs of Prior Periods	(2,243)
Other	(396)
Total Resources Not Funding Net Costs of Operations	(4,039)
Costs Not Requiring Resources	
Depreciation and Amortization	251
Revaluation of Assets and Liabilities	7
Other	571
Total Costs Not Requiring Resources	829
Financing Sources Yet to Be Provided	5,202
Net Cost of Operations	$384,424

The Accompanying Notes are Integral Part of these Statements

Department of the Treasury

Consolidated Statement of Custodial Activity

For the Year Ended September 30, 1998
(In Millions)

Sources of Custodial Revenue & Collections	
Revenue Received	
Individual Income & FICA Taxes	$1,472,205
Corporate Income Taxes	212,992
Estate and Gift Taxes	24,631
Excise Taxes	59,209
Duties	19,118
Fees, and Licenses	1,690
Unemployment Taxes	6,479
Deposit of Earnings, Federal Reserve System	24,540
Fines, Penalties, Interest & Other Revenue	18,469
Total Revenue Received	1,839,333
Less payments from permanent, indefinite appropriations for refunds of taxes and duties (including related interest), duty drawback, and earned income credit	(153,057)
Net Revenue Received	1,686,276
Accrual Adjustment	36
Total Revenue	1,686,312
Disposition of Custodial Revenue & Collections	
Amounts Provided to Non-Federal Entities	306
Amounts Provided to Fund the Federal Government (Note 30)	1,685,970
Accrual Adjustment	36
Total Disposition of Custodial Revenue & Collections	1,686,312
Net Custodial Revenue Activity	$0

The accompanying notes are an integral part of these statements.

NOTES TO THE FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

A. Reporting Entity

The Department was created by Act (1 Stat.65) on September 2, 1789. Many subsequent acts have figured in the development of the Department, delegating new duties to its charge and establishing the numerous bureaus and divisions that now comprise the Department. As a major policy advisor to the President, the Secretary has primary responsibility for formulating and managing the domestic and international tax and financial policies of the Federal Government.

Further, the Secretary is responsible for recommending and implementing United States domestic and international economic and tax policy; fiscal policy; governing the fiscal operations of the Government; maintaining foreign assets control; managing the Federal debt; overseeing the law enforcement functions carried out by the Department; managing the development of financial policy; representing the United States on international monetary, trade and investment issues; overseeing Departmental overseas operations; and directing the activities of the Department in manufacturing coins, currency, and other products for customer agencies and the public.

The Department is comprised of Departmental Offices, the Office of Inspector General, the Treasury Forfeiture Fund, the Exchange Stabilization Fund, the Federal Financing Bank, the Financial Crimes Enforcement Network, and the Community Development Financial Institutions Fund, as well as the following eleven bureaus: Bureau of Alcohol, Tobacco and Firearms; Office of the Comptroller of the Currency; U.S. Customs Service; Bureau of Engraving and Printing; Federal Law Enforcement Training Center; Financial Management Service; Internal Revenue Service; U.S. Mint; Bureau of the Public Debt; U.S. Secret Service; and Office of Thrift Supervision.

The accompanying financial statements reflect the activities of the U.S. Department of the Treasury. The Department's financial statements reflect the reporting of its own entity activities which includes appropriations it receives to conduct its operations and revenue generated from those operations. They also reflect the reporting of certain non-entity (custodial) functions it performed on behalf of the Federal Government and others. Non-entity activities include the collection of Federal revenue, servicing the Federal debt, disbursing certain Federal funds, and maintaining certain assets and liabilities for the Federal Government as well as for others.

The fiscal year 1998 presentation differs from the Department's fiscal year 1997 presentation. In fiscal year 1997, the Department used two separate sets of financial statements to report its entity related activities versus its non-entity activities. However, the Department streamlined its fiscal year 1998 report by including all of its activities in a single set of financial statements. Another significant change in FY 1998 was re-classifying, as entity activities, the International Assistance Programs. This re-classification resulted in an increase to beginning net position of approximately $59 billion.

The Department engages in certain transactions between its non-entity related activities and its entity related activities. However, as a matter of policy, the Department does not eliminate these transactions for consolidation purposes, because the activities are viewed as separate and unique. If these transactions were eliminated, the Department's financial statements would not be complete in terms of reporting its total entity related activities and those non-entity related activities carried out on behalf of the Federal Government.

For example, the Federal Financing Bank (FFB) and the Community Development Financial Institutions Fund (CDFI), both entity activities of the Department, make loans to Federal agencies and to entities outside of the Federal Government. To fund this loan activity, these two entities borrow from the Federal Government, i.e., they borrow money from the Federal Government in order to make the loans. The Federal Government's loans receivable from FFB and CDFI are included in the Loans Receivable line item on the Department's balance sheet in the Non-Entity Assets section, because the Department's Bureau of the Public Debt maintains and reports on these assets (loans receivable), albeit in a "custodial" or non-entity capacity.

Therefore, in order to show full accountability for the Department's non-entity assets, i.e., those assets for which the Department has custody on behalf of another entity (in this case the Federal Government), the entity loans payable on the Department's balance sheet related to this activity are not eliminated against the non-entity loans receivable also reported on its balance sheet. At, the Government-wide level reporting, these transactions would be eliminated.

The Department thinks its policy not to eliminate these transactions follows the guidelines provided in the Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, *Entity and Display*. SFFAC No. 2, paragraph 77 states, "In reporting the transactions and balances of a federal reporting entity in its entirety, it is conceptually desirable, although not always practicable to eliminate the intra-entity transactions and balances. *Factors to consider are the utility of the information for the entity in its entirety if the intra-entity balances are not eliminated,* the misunderstanding that might result if the balances are not eliminated, and the cost-benefit of making the eliminations *(emphasis added)*." As described above, the Department thinks its policy improves the utility of the information presented.

B. Basis of Accounting & Presentation

Entity Components of the Financial Statements. The Department's financial statements with respect to the balance sheet, the statement of net cost, and the statement of changes in net position are reported using the accrual basis of accounting. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred (e.g. goods or services are received) without regard to receipt or payment of cash. The Department's statement of budgetary resources is reported using the budgetary basis of accounting. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds. It generally differs from the accrual basis of accounting in that obligations are recognized when new orders are placed, contracts awarded, and services received, that will require payments during the same or future period. The purpose of the Department's statement of financing is to provide a reconciliation which clarifies the relationship between the obligation basis of budgetary accounting, used for the statement of budgetary resources, and the accrual basis of financial (i.e., proprietary) accounting, used for the statement of net cost.

Non-Entity Components of the Financial Statements. The Department's non-entity revenue reported through the statement of custodial activity is recognized on a modified cash basis, reflecting accruals for tax/trade receivables as well as for interest earned. Refunds of taxes and interest, as well as Earned Income Tax Credit (EITC) payments, are also recognized on a modified cash basis, which includes accruals for tax refunds payable (see reference P below, Sources of Custodial Revenues and Collections).

The Department's financial statements are presented in accordance with the hierarchy of accounting standards described in OMB Bulletin 97-01, which is as follows:

- Individual standards recommended by FASAB and agreed to by the Director of OMB, the Comptroller General, and the Secretary of the Treasury and published by OMB and the General Accounting Office, as codified in the Statements of Federal Financial Accounting Standards (SFFAS);

- Interpretations related to the SFFASs issued by OMB in accordance with the procedures outlined in OMB Circular A-134, "Financial Accounting Principles and Standards;"

- Requirements contained in OMB's Form and Content Bulletin in effect for the periods covered by the financial statements;

- Accounting principles published by other Federal and private sector authoritative standard setting bodies and authoritative sources (a) in the absence of other guidance provided in this hierarchy and (b) if the use of such accounting principles improves the meaningfulness of the financial statements.

These financial statements are provided to meet the requirements of the Government Management Reform Act. They consist of the consolidated balance sheet, the consolidated statement of net cost, the consolidated statement of changes in net position, the combined statement of budgetary resources, the combined statement of financing, and the consolidated statement of custodial activity; all of which are prescribed by OMB Bulletin No. 97-01, Form and Content of Agency Financial Statements, as amended.

While these financial statements have been prepared from the books and records of the entity in accordance with the formats prescribed by OMB, these financial statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

These financial statements should be read with the realization that they are for a component of a sovereign entity, that liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

Because OMB prescribed new financial statement formats for fiscal year 1998, comparative information is not provided for fiscal year 1997.

C. Tax/Trade and Other Non-entity Receivables

The Department follows the provisions in the Statement of Federal Financial Accounting Standards (SFFAS) No. 7, *Accounting for Revenue and Other Financing Sources*, for recording tax/trade receivables. Tax/Trade receivables are not accrued until related tax returns are filed, assessments are made, and prepayments netted against liabilities. Accruals are made to reflect penalties and interest on tax/trade receivables through the balance sheet date. SFFAS No. 7 also distinguishes between assessments that should be reported on the balance sheet (tax/trade receivables) and those that should be disclosed as compliance assessments and write-offs. A summary of each category follows:

Tax/Trade Receivables consist of unpaid assessments (taxes and associated penalties and interest) due from taxpayers for which the Department can support the existence of a receivable through taxpayer agreement, such as filing a tax return without sufficient payment, or a court ruling in favor of the Department. Tax/Trade receivables are shown on the balance sheet net of an allowance for doubtful accounts. The allowance for doubtful accounts reflects an estimate of the portion deemed to be uncollectible.

Compliance Assessments are unpaid assessments in which neither the taxpayer nor a court has affirmed that the taxpayer owes amounts to the Federal Government. Examples include assessments resulting from an audit or examination in which the taxpayer does not agree with the results of the audit or examination. These assessments are not reported in the financial statements.

Write-offs consist of unpaid assessments on which the Department does not expect further collections due to factors such as the taxpayer's death, bankruptcy, or insolvency. These amounts are not reported on the balance sheet as they are deemed uncollectible. However, statutory provisions require that these accounts be maintained until the statute for collection expires.

Other non-entity accounts receivable and related interest are recognized for amounts due to the Federal Government. These amounts include interest outstanding on monies deposited in Federal Reserve Banks. It also includes amounts Federal agencies owe to the Federal Government for the payment of water and sewage service; a payment made by the Department on behalf of the Federal Government.

D. Investments

Entity and non-entity investments are stated at amortized cost, which is an approximation of fair value. Premiums and discounts on investments are amortized using the straight line method over the term of the investments.

Entity and non-entity intra-governmental investments are adjusted to market value if Treasury intends to sell the security prior to maturity and there is a reduction in the security that is more than temporary.

E. Inventories and Related Property

Inventories and related property include inventory, operating materials and supplies, and forfeited property. The Department utilizes various accounting methods to account for inventory and operating supplies which approximates historical costs. All operating materials and supplies are recorded as an expense when consumed in operations.

Recognition of revenue from the forfeiture of property is deferred until the property is sold, or transferred to a state, local, or federal agency, or to a foreign government. Revenue is not recorded if the forfeited asset is ultimately destroyed, such as counterfeit property.

F. Loans and Interest Receivable - from Other Federal Agencies

Intra-governmental entity Loans and Interest Receivable, from other Federal agencies, represent loans and interest receivable held by the Department. No subsidy costs were recorded for loans purchased from federal agencies, because these are guaranteed (interest and principal) by those agencies.

Intra-governmental non-entity Loans and Interest Receivable from Other Federal Agencies represent loans issued by the Department to Federal agencies on behalf of the Federal Government. The Department acts as an intermediary issuing these loans, because the agencies receiving these loans will lend these funds to others to carry out various programs of the Federal Government. Because of the Department's intermediary role in issuing these loans, the Department does not record an allowance or subsidy costs related to these loans. Instead, loan loss allowances and subsidy costs are recognized by the ultimate lender, the Federal agency who issues the loans.

G. Property Plant and Equipment

The Department's property, plant and equipment is recorded at cost and is depreciated using the straight line method over the estimated useful lives of the assets. Major alterations and renovations are capitalized, while maintenance and repair costs are charged to expense as incurred.

SFFAS No. 6, *Accounting for Property, Plant and Equipment,* does not set a capitalization threshold as an element of the property, plant and equipment (PP&E) definition. Instead, the Federal Accounting Standards Advisory Board (FASAB) adopted a materiality approach which allows each Federal entity to establish its own capitalization threshold, as well as guidance on applying the threshold. In reaching the conclusions in SFFAS No. 6, FASAB noted the diversity of Federal entities and concluded that one threshold would not be suitable for all entities. FASAB also noted that permitting management discretion in establishing capitalization policies leads to a more cost-effective application of accounting standards. The Department is comprised of many bureaus that are diverse both in size and in operating environment. Accordingly, the Department's capitalization policy uses ranges rather than setting specific capitalization thresholds. The Department's capitalization policy permits the management of each of the Department's bureaus to select an appropriate capitalization threshold within the range of $25,000 minimum and $50,000 maximum. The Department also uses ranges for bulk purchases: $250,000 minimum and $500,000 maximum for non-manufacturing bureaus and $25,000 minimum and $50,000 maximum for manufacturing bureaus. Bureaus determine the individual item cost that will be applied to bulk purchases. In addition, the Department's bureaus may expense bulk purchases if they conclude

that total period costs would not be materially distorted and the cost of capitalization is not economically feasible.

H. Federal Debt

Debt and associated interest is reported on the accrual basis of accounting. Certain debt securities are issued at a discount or premium. These discounts and premiums are amortized over the term of the security using the straight-line method.

I. Debt Prepayment Premium

The debt prepayment premium is calculated as the difference between the face amount of the Department's borrowing being prepaid and the present value of the expected future cash flows under the original terms, discounted at the Department's cost of borrowings on the prepayment date (the amount FFB must pay to order to prepay the debt). The nature of the debt prepayment is discussed in further detail in Note 14.

J. Pension Costs, Other Retirement Benefits, and Other Post Employment Benefits

The Department recognizes the full costs of its employees' pension benefits, however, the liability associated with these costs are recognized by Office of Personnel Management (OPM) rather than the Department.

Most employees of the Department hired prior to January 1, 1984, participate in the Civil Service Retirement System (CSRS), to which the Department contributed 8.51 percent and employees contributed 7 percent of base pay. For law enforcement officers under CSRS, the Department contributed 9.01 percent and law enforcement officers contributed 7.5 percent of base pay.

On January 1, 1987, the Federal Employees' Retirement System (FERS) went into affect pursuant to Public Law 99-335. Employees hired after December 31, 1983, are automatically covered by FERS and Social Security. A primary feature of FERS is that it offers a savings plan to which the Department automatically contributes 1 percent of base pay and matches any employee contributions up to an additional 4 percent of base pay. For most employees hired after December 31, 1993, the Department also contributes the employer's matching share for Social Security. For the FERS basic benefit the Department contributed 10.7 percent and employees contributed 0.8 percent of base pay. For law enforcement officers under FERS, the Department contributed 23.3 percent and law enforcement officers contributed 1.3 percent of base pay.

Similar to Federal retirement plans, Office of Personnel Management (OPM) rather than the Department, reports the liability for future payments to retired employees who participate in the Federal Employees Health Benefits Program (FEHBP) and Federal Employees Group Life Insurance (FEGLI) Program. As a result of SFFAS No. 5, the Department is required to report the full cost of providing other retirement benefits (ORB). In addition, SFFAS No. 5 also requires the Department to recognize an expense and liability for other post employment benefits (OPEB), which includes all types of benefits provided to former or inactive (but not retired) employees, their beneficiaries, and covered dependents.

Additionally, the Department's Office of the Comptroller of the Currency (OCC) and Office of Thrift Supervision (OTS) separately sponsor certain benefit plans for their employees. OCC sponsors a life insurance benefit plan for current employees who are not enrolled in FEGLI plans. This plan is a defined benefit plan, and OCC is fully responsible for the associated liability. Additionally, OTS provides certain health and life benefits for all retired employees that meet eligibility requirements.

K. DC Pension Fund

The Balanced Budget Act of 1997, which became effective on October 1, 1997, provides that the Secretary of the Treasury assume certain responsibilities for the District of Columbia pension system, including administration of fund assets and distribution of pension benefits. To varying degrees the Secretary is responsible for three District retirement programs:

- Police Officers and Firefighters Retirement Program
- Teachers Retirement Program
- Judges Retirement Program

For the Police Officers, Firefighters and Teachers, the Secretary acting on behalf of the Federal Government, will pay for benefits earned prior to and on June 30, 1997. The District Government will be responsible for paying benefits earned after June 30, 1997. For the Judges, the Secretary, acting on behalf of the Federal Government, will pay for benefits earned both before and after June 30, 1997.

As of September 30, 1998, the assets that are to be transferred to the Federal Government, pursuant to the Act, have not been identified nor transferred to the Trust Funds of the Federal Government. The financial statements reflect the equity in net assets held in trust for pension benefits, based on an estimated percentage, seventy-three percent, of the assets to be split between the Federal Government and the District as of the effective date of the Act October 1, 1997.

L. Certificates Issued to Federal Reserve Banks

Certificates issued to Federal Reserve Banks are stated at their face value. It is not practical to estimate the fair value of Certificates Issued to Federal Reserve Banks since these certificates contain no specific terms of repayment.

M. Allocation of Special Drawing Rights

Allocation of Special Drawing Rights are valued as of September 30, 1998, using current exchange rates which approximate their fair value. See Footnote Number 5 "Cash, Foreign Currency, and Other Monetary Assets" for the exchange rates.

N. Federal Employee Benefits Payable - FECA Actuarial Liability

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered Federal civilian employees injured on the job, and employees who have incurred a work-related injury or occupational disease. These future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical, and

miscellaneous costs for approved compensation cases. In 1998, the liability was determined by the Department of Labor using the paid losses extrapolation method calculated over the next 37-year period.

O. Revenue & Financing Sources

The Department's activities are financed either through exchange revenue it receives from others or through non-exchange revenue and financing sources (such as appropriations provided by the Congress and penalties, fines, and user fees collected). Exchange revenues are recognized when earned; i.e. goods have been delivered or services have been rendered. Non-exchange revenues are accounted for when received by the collecting entity. Appropriations used are recognized as financing sources when related expenses are incurred or assets are purchased. Revenue from reimbursable agreements is recognized when the services are provided. The Department also incurs certain costs that are paid in total or in part by other Federal entities, such as pension costs. These subsidized costs are recognized on the Consolidated Statement of Changes in Net Position as imputed financing sources equal to the cost paid by the providing entity. Other non-exchange financing sources such as donations, and transfers of assets without reimbursements also are recognized for the period in which they occurred.

The Department recognizes forfeited revenue it receives as non-exchange revenue on the Consolidated Statement of Changes in Net Position in accordance with SFFAS No. 7. The costs related to the forfeiture fund program are reported on the Consolidated Statement of Net Cost.

P. Sources of Custodial Revenues and Collections

Non-entity revenue reported on the Department's statement of custodial activity includes cash collected and received by the Department. It does not include revenue collected by other Federal agencies, such as user fees and other receipts, which are remitted for general operating purposes of the Federal Government or are earmarked for certain trust funds.

Revenue from taxes and duties are recognized when cash is received. However, the accrual method of accounting is used to recognize interest earned on loans provided by the Department on behalf of the General Fund.

Q. Tax Assessments and Abatements

Under the IRC Section 6201, the Department is authorized and required to make inquiries, determinations, and assessments of all taxes which have not been duly paid (including interest, additions to the tax, and assessable penalties) under the law. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as from tax compliance programs, such as examination, under reporter, substitute for return, and combined annual wage reporting.

The Department also has authority to abate the paid or unpaid portion of an assessed tax, interest, and penalty. Abatements occur for a number of reasons and are a normal part of the tax administration process, (e.g., correcting an assessment of taxes from an enforcement program, taxes discharged in bankruptcy, accepting offers in compromise for less than the full amount of taxes owed, amending tax returns, and abating penalties for reasonable cause.) The abatement process is also used by taxpayers to contest assessments made due to mathematical or clerical errors, and for contesting an assessment once the liability has been satisfied. Another form of abatement occurs when a qualifying corporation

claims a net operating loss that creates a credit that can be carried back to reduce a prior year's tax liability. Abatements may result in claims for refunds or a reduction of the unpaid assessed amount.

Types of Taxes

The type of taxes included on the Department's Consolidated Statement of Custodial Activity includes:

Individual Income & FICA Taxes -- Federal income and social security taxes paid under Subtitle A of the Internal Revenue Code (IRC). Pursuant to the Social Security Act, as amended by P.L. 94-202 effective January 1, 1978, Social Security taxes are collected through the Federal Tax Deposit (FTD) system and remitted to the Social Security trust fund.

Corporate Income Taxes -- Federal income taxes paid by businesses under Subtitle A of the IRC.

Estate and Gift Taxes -- Taxes paid under Subtitle B of the IRC.

Excise Taxes -- The Department collects excise taxes for various trust funds and accounts, including the Highway Trust Fund, Airport and Airways Trust Fund, and the Mass Transit Account. Excise taxes are collected on various items including the purchase of airline tickets, gasoline products, and many others. The Department also collects excise taxes on distilled spirits and imported liquor, tobacco, and firearms.

Unemployment Taxes -- The collection of unemployment taxes under Subtitle C of the IRC is administered by the IRS. Federal unemployment taxes are also collected through the FTD system and remitted to the Department of Labor's Unemployment Trust Fund.

Duties -- Amounts collected by Customs on imported goods.

Deposit of Earnings, Federal Reserve System -- Funds deposited by the Federal Reserve Bank, from earnings on deposits. Pursuant to Sec. 16 of the Federal Reserve Act, the Federal Reserve remits earnings and deposits to the General Fund.

Fines, Penalties, Interest, and Other Revenue -- Fines assessed for violations, or late charges and interest charged for delinquent payment of taxes. Interest revenue is from the loans provided on behalf of the General Fund to other Federal agencies. Other revenue includes other miscellaneous revenue collected by the Department and deposited into the General Fund.

Disposition of Custodial Revenue Collections -- Amounts are recognized as dispositions for: (1) funds deposited to the general fund and other entities; and (2) amounts to be transferred upon collection.

R. Judgment Fund

The Judgment Fund was established by Congress in the 1950s, as a permanent indefinite appropriation, to pay in whole or in part the court judgments and settlement agreements negotiated by the Justice Department on behalf

of Federal agencies, as well as certain types of administrative awards. The Judgment Fund recognizes an expense and records appropriations used for the full judgment or settlement rendered against the Federal Government.

S. Permanent and Indefinite Appropriations

Permanent and indefinite appropriations are used to disburse tax and duty refunds, duty drawbacks and earned income credits. These appropriations are not subject to budgetary ceilings established by Congress. Therefore, refunds payable at year-end are not subject to funding restrictions. Refund payment funding is recognized as appropriations used. Permanent indefinite authority is not stated as a specific amount and is available for an indefinite period of time.

Although funded through appropriations, refund and drawback activity is, in some instances, reported as a custodial activity of the Department. This presentation is appropriate because refunds are, in substance, a custodial revenue-related activity in that they are a direct result of taxpayer overpayments of their tax liabilities. Federal tax revenue received from taxpayers is not available for use in the operation of the Department and is not reported on the Statement of Net Cost. Likewise, the resultant refunds of overpayments are not recognized by the Department as an operating expense of the Department. Consequently, to present refunds as an expense of the Department on the Statement of Net Cost with related appropriations used, would be inconsistent with the reporting of the related Federal tax revenue and would materially distort the costs incurred by the Department in meeting its strategic objectives.

The Department also receives two permanent and indefinite appropriations related to debt related activity. One is used to pay the interest on the public debt securities; the other is used to pay the redemptions of securities that have matured, been called, or are eligible for early redemption.

Additionally, the Department also receives permanent and indefinite appropriations to make payments on behalf of the United States Government. These appropriations are provided to make payments to the Federal Reserve for services provided. It includes appropriations provided to make other disbursements on behalf of the Federal Government, including payments made to various individuals as the result of claims and judgements rendered against the United States.

T. Imputed Costs/Financing Sources

Federal Government entities often receive goods and services from other Federal Government entities without reimbursing the providing entity for all the related costs. In addition, Federal Government entities often incur costs that are paid in total or in part for other entities. These constitute subsidized costs which are recognized by the receiving entity. An imputed financing source is also recognized by the receiving entity. The Department of the Treasury recognized imputed costs and financing sources in fiscal year 1998 to the extent directed by the OMB. The Department recognizes imputed financing for pension costs which will be ultimately be paid OPM. The Department also recognizes imputed financing for judgements and claims rendered against the Department which will be paid from the Judgement Fund.

2. *Fund Balance*

Entity

Entity fund balance includes balances which are available to pay liabilities and to finance authorized purchase commitments. In addition to amounts received from appropriations to pay salaries and expenses, fund balance also includes amounts received from appropriations to make contributions to various international financial institutions (see Note 7). As of September 30, 1998 entity fund balance consisted of the following (in millions):

	Obligated	Unobligated Available	Unobligated Restricted	Total
Appropriated Funds	$21,878	$12,590	$76	$34,544
Trust Funds	71	60	0	131
Revolving Funds	701	232	0	933
Other Fund Types	17	167	648	832
Total	$22,667	$13,049	$724	$36,440

$19.2 billion of the $21.9 billion in obligated appropriated funds is for outstanding letters of credit issued to the International Monetary Fund (IMF) and Multi-lateral Development Banks (MLDBs), which can draw down on these letters of credit as funds are needed. Total draw downs on the outstanding letters of credit during fiscal year 1998 were $9.0 billion, including $7.4 billion by the IMF.

Non-Entity Fund Balance

Non-entity fund balance represents unused balances of appropriations received by various Treasury entities to conduct custodial operations such as the payment of interest on the Federal debt and refunds of taxes, duties, fees, and drawbacks. As of September 30, 1998, non-entity fund balance consisted of the following (in millions):

	Obligated	Unobligated Available	Unobligated Restricted	Total
Appropriated Funds	$46,046	$312	$40	$46,398
Revolving Funds	0	7	0	7
Other Fund Types	47	1,100	339	1,486
Total	$46,093	$1,419	$379	$47,891

Restricted amounts, both entity and non-entity, primarily include collections which can be used to offset certain costs of operations. However, these amounts are restricted from funding the cost of these operations until authority is granted through Appropriations Acts.

3. *Loans and Interest Receivable*

Loans and interest receivable represent loans held by the Department arising from its own operations (entity) and loans held on behalf of the Federal Government (non-entity).

Entity

As of September 30, 1998 intra-governmental loans and interest receivable consisted of the following (in millions):

Agency Loans Purchased	$17,785
Direct Loans Purchased	5,696
Guaranteed Loans	22,662
Interest Receivable, Intra-governmental Loans	1,051
Less Discount	(1)
Less Allowance on Loans & Interest Receivable	(217)
Total Entity Loans Receivable - Intragovernmental	$46,976

Agency loans purchased are either notes or pools of loans sold by Federal agencies in the form of certificates representing shares of ownership in the loan pool. The selling agencies guarantee the principal and interest repayments on the notes or certificates. Guaranteed loans are loans made to non-federal borrowers whose obligation to repay the principal and interest is guaranteed by a federal agency.

As of September 30, 1998, loans and interest receivable from non-federal entities consisted of the following (in millions):

Direct Loans	$501
Less Allowance/Subsidy Cost	(2)
Interest	4
Total Entity Loans Receivable	$503

Included in the amounts above are loans provided by the Department to the International Monetary Fund (IMF) through the General Arrangements to Borrow (1962) and the New Arrangements to Borrow (1998); to forestall or cope with an impairment to the international monetary system. Any loan to the IMF gives rise to a similar counterpart claim on the IMF. These claims are interest bearing and are liquid, as they may be exercised in short notice if the U.S. needs additional foreign currency reserves. These loans are recognized at cost adjusted for exchange rate gains and losses.

Non-Entity

Non-entity loans and interest receivable represent loans managed by the Department on behalf of the Federal Government. The Department is responsible for collecting these loans and transferring the proceeds to the General Fund.

These loans are provided to Federal agencies and the Department. The Department borrows these amounts to fund its mandated lending activities. Such borrowings, by the Department, are reflected

as entity related activities in the financial statements, while the non-entity loan balances are reflected as non-entity activities in the financial statements. Accordingly, these balances were not eliminated in the preparation of the financial statements.

As of September 30, 1998, non-entity loans and interest receivable consisted of the following (in millions):

	Loans Receivable	Interest Receivable	Loans and Interest Receivable
Federal Financing Bank	$34,036	$1,038	$35,074
Federal Direct Student Loan Program	35,097	0	35,097
Disaster Loan Fund	9,160	575	9,735
Rural Electrification and Telecommunication Fund	9,232	0	9,232
Commodity Credit Corporation	17,543	159	17,702
Rural Housing Insurance Fund	7,197	0	7,197
Federal Housing Administrations	6,579	0	6,579
Housing for the Elderly and Handicapped	5,293	180	5,473
Other	27,890	255	28,145
Total	$152,027	$2,207	$154,234

4. *Investments and Related Interest*

Entity

The Department invests funds in excess of its immediate needs in Government Account Series investments. A majority of these investments represent short term (31 days or less) non-marketable par value Federal debt securities. Investments in Federal Government securities are reported at acquisition cost, net of premiums and discounts.

The Department invests funds available for its exchange stabilization activities in securities outside the Federal Government. Securities that the Department has both the positive intent and ability to hold to maturity are classified as investment securities held to maturity and are carried at historical cost, adjusted for amortization of premiums and accretion of discounts.

Equity pooled investments held outside the Federal Government represents investments the Department acquired through the assumption of the DC Pension liability (see Note 16). The Department has title to these assets pursuant to the Balanced Budget Act of 1997 (the Revitalization Act). However, as of September 30, 1998, these investments were still in the custody of the District of Columbia.

As of September 30, 1998 entity investments consisted of the following (in millions):

Type of Investment	Cost	Amortized (Premium)/ Discount	Investment Net	Interest Receivable	Investment Balance
Equity in Pooled Investments	$3,350	$0	$3,350	$11	$3,361
Japanese T- Bills	2,762	3	2,765	3	2,768
German Bonds	759	(5)	754	19	773
German BUBIlls	203	2	205	2	207
Marketable Securities	11	0	11	0	11
Total Non-Federal	7,085	0	7,085	35	7,120
Intra-governmental					
Non-Marketable Par Value	16,590	(1)	16,589	5	16,594
Marketable Securities	462	5	467	5	472
Total Federal	17,052	4	17,056	10	17,066
Total	$24,137	$4	$24,141	$45	$24,186

As of September 30, 1998 required market value disclosure of Investments consisted of the following (in millions):

Equity in Pooled Investments	$3,361
Japanese T- Bills	2,766
German Bonds	782
German BUBIlls	205
Marketable Securities	11
Marketable Securities - Intragovernmental	474
Total	$7,599

Non-Entity

Non-entity investments include seized monetary assets that are invested in Government Account Series securities. As of September 30, 1998, the intra-governmental investments were as follows (in millions):

	Cost	Amortized (Premium)/ Discount	Investment Balance 9/30/98	Interest Receivable Other Adjustments	Investment Balance 9/30/98
Non-Marketable Par	$344	($1)	$343	$0	$343

5. *Cash, Foreign Currency, and Other Monetary Assets*

Entity

Entity cash, foreign currency, and other monetary assets primarily includes foreign currency denominated assets (FCDA), special drawing rights (SDR), and forfeited cash. SDRs and FCDAs are valued as of September 30, 1998, using current exchange rates. The amounts held as of September 30, 1998 were as follows (in millions):

Cash	$144
Foreign Currency	
German Marks	5,484
Japanese Yen	5,345
Other Monetary Assets	
Special Drawing Rights	10,176
Other	86
Entity Total	$21,235

Other includes U.S. dollars restricted for use by the International Monetary Fund, and are maintained in two accounts at the Federal Reserve Bank of New York.

Certain operations of the Department result in the holding of various FCDAs denominated assets. The foreign currency holdings are normally invested in interest bearing assets issued by or held through foreign governments or monetary authorities. FCDAs with original maturities of three months or less, except for foreign currencies under swap agreements with developing countries, were valued at $8.7 billion as of September 30, 1998. Other FCDAs with maturities greater than three months are also held and may at times include foreign currencies acquired under swap agreements with developing countries. As of September 30, 1998, FCDAs with maturities greater than three months were valued at $2 billion.

The SDR is an international reserve asset created by the International Monetary Fund (IMF). It was created as a supplement to existing reserve assets, and on several occasions SDRs have been allocated by the IMF to members participating in the IMF's SDR department. The value as a reserve asset derives, essentially, from the commitments of participants to hold and accept SDRs and to honor various obligations connected with its proper functioning as a reserve asset.

On a daily basis, the IMF calculates the value of the SDR using the market value, in terms of the U.S. dollar, from the amounts of each of five freely usable weighted currencies, as defined by the IMF. These currencies are the U.S. dollar, the Deutsche mark, the Japanese yen, the French franc, and the pound sterling. The Department's SDR holdings and allocations are revalued monthly based on the SDR valuation rate calculated by the IMF.

During Fiscal Year (FY) 1998, the Department purchased, at the prevailing rates, $590.5 million equivalent of SDRs received from the IMF by the General Fund of the U.S. Government as remuneration (interest) on the U.S. reserve position in the IMF, and paid the General Fund $4.1 million in FY 1998, in interest on dollars due the General Fund in return for SDRs received as remuneration. In addition, during FY

1998, the Department sold $400 million and $266 million equivalent of SDRs to Mexico and Argentina, respectively, at the prevailing rate.

Pursuant to the IMF Articles of Agreement, SDRs allocated to or otherwise acquired by the United States are resources unless:

a. canceled by the Board of Governors based on an 85 percent majority decision of the total voting power of the Executive Board of the IMF;
b. the SDR Department of the IMF is liquidated;
c. the IMF is liquidated; or
d. the United States chooses to withdraw from the IMF or terminate its participation in the SDR Department.

Except for the payment of interest and charges on SDR allocations to the United States, the payment of the Department's liability related to the SDR allocations is conditional on events listed above, in which the United States has a substantial or controlling voice. Allocations of SDRs were made on January 1, 1970, 1971, 1972, 1979, 1980 and 1981. Since 1981, the IMF has made no further allocations of SDRs. As of September 30, 1998, the amount of SDR allocations was the equivalent of $6.7 billion.

Non-Entity

Non-entity cash, foreign currency, and other monetary assets includes the Operating Cash of the Federal Government, managed by the Department. Also included is foreign currency maintained by various U.S. and military disbursing offices. It also includes seized monetary instruments, undistributed cash, and offers in compromise which are maintained as the result of the Department's law enforcement and tax collecting responsibilities. The amounts held as of September 30, 1998 were as follows (in millions):

Operating Cash of the Federal Government	$41,439
Undistributed Cash/Offers in Compromise	158
Seized Monetary Instruments	90
Foreign Currency	105
Non-Entity Total	$41,792

The Operating Cash of the Federal Government represents balances from tax collections, customs duties, other revenues, federal debt receipts, time deposits, and other various receipts net of checks outstanding, which are held in the Federal Reserve Banks, foreign and domestic financial institutions, and in U.S. Treasury tax and loan accounts.

The Operating Cash of the Federal Government includes compensating balances, totaling $4.6 billion as of September 30, 1998. These balances are deposited interest free to compensate commercial banks for services provided on behalf of the Federal Government (such as handling over the counter deposits for federal program agencies, providing lockbox services for agency collection programs, etc.)

Seized Monetary Instruments and Seized Property

Seized property as defined by SFFAS No. 3, *Accounting for Inventory and Related Property,* includes monetary instruments, real property, and tangible personal property of others in the actual constructive possession of the custodial agency. The Department seizes monetary instruments and property in terms of the definition provided by SFFAS No. 3 as the result of tax, forfeiture, criminal, and other enforcement actions. Seized property (including currency and monetary instruments) is recorded at its market value at the time of the seizure. The value is determined by the seizing organization and is usually based on market analysis such as third party appraisal, standard property value publications or bank statements.

The Department held $90 million in seized currency as of September 30, 1998. Of this amount $10 million was held as the result of tax and criminal enforcement actions and $80 million was held as the result of Treasury Forfeiture Fund Program.

The Department, through the Treasury Forfeiture Fund Program, seizes property such as real property, and tangible personal property of others that is in actual, constructive, or custodial possession of the Department, resulting from the enforcement of Federal law. Also included in seized property are prohibited items. Prohibited items are items with no legal market value in the United States and which will not be sold for export. They include explosives and pornography. Forfeited firearms that will not be sold due to Department policy are also considered to be prohibited items. Illegal drugs and other forfeited property are retained by the Department until final disposition.

The following tables provide detailed information about the Department's seized monetary instruments and property in relation to the Department's Forfeiture activities. Seized Currency on the Analysis of Change in Seized Assets includes $80 million reported on the Balance Sheet. It also includes seized currency invested in Government Account Series of $343 million.

Treasury, Analysis in Change in Seized Assets (Thousands)

Type of Asset	Balance October 1	Seizures	Remissions a/	Forfeitures	Adjustments b/	Value Change c/	Balance 9/30
Currency	$206,512	$447,636	$(53,054)	$(157,825)	$(19,940)	$(162)	$423,167
Other Monetary Instruments	29,579	9,989	(11,746)	(5,297)	(7,177)	150	15,498
Real Property	44,072	67,791	(14,563)	(14,956)	7,102	(642)	88,804
General Property	144,617	183,685	(111,980)	(25,293)	(6,900)	(50,473)	133,656
Vessels	3,933	11,774	(7,617)	(1,501)	(550)	(304)	5,735
Aircraft	2,029	28,356	(26,819)	(384)	(888)	(27)	2,267
Vehicles	15,080	56,859	(36,892)	(14,816)	(1,006)	(675)	18,550
Prohibited Property	---	---	---	---	---	---	---
Total Seized Assets	$445,822	$806,090	($262,671)	($220,072)	($29,359)	($52,133)	$687,677

Analysis of Change in Number of Seized Assets - Line Items

Type of Asset	Balance October 1	Seizures	Remissions a/	Forfeitures	Adjustments b/	Balance 9/30
Currency	(d)					(d)
Other Monetary Instruments	(d)					(d)
Real Property	289	188	(39)	(94)	8	352
General Property	10,640	22,429	(10,716)	(12,282)	590	10,661
Vessels	145	180	(62)	(121)	(17)	125
Aircraft	19	35	(27)	(6)	(1)	20
Vehicles	2,834	10,962	(4,168)	(6,379)	(184)	3,065
Prohibited Property	33,091	65,498	(1,579)	(62,489)	(2,757)	31,764
Total Seized Assets	47,018	99,292	(16,591)	(81,371)	(2,361)	45,987

a/ Remissions include seized items which were classified as prohibited, but subsequently returned to the owner once a legal right to possess the item was established. Examples include firearms or controlled substances obtained by prescription.

b/ Adjustments - include reclassification of property categories and minor adjustments to beginning balances. Additionally, adjustments include property turned over to state and local or other Federal Law enforcement agencies for prosecution or destruction prior to forfeiture.

c/ Value Change - is an adjustment to reflect the net value change of a seized asset from the initial appraisal to the latest appraisal. This could result in either a positive or negative change.

d/ Inconsistent methods have been used to record the number of seizures of currency and other monetary instruments. Therefore, numbers provided would not be compiled from a uniform base, and accordingly, are not provided.

6. Reserve Position in the International Monetary Fund

The IMF was established in 1945 with the mission of restoring international monetary cooperation and promoting a sound and growing world economy. For nearly thirty years, its operational focus was on maintaining exchange rate stability through the "par value" system, based on gold. With the second amendment of the Articles of Agreement, that focus shifted to the promotion of exchange stability through the maintenance of orderly exchange arrangements, with greater emphasis given to the surveillance of fundamental economic policies, including exchange rate policies.

The United States participates in the IMF, as do other members, through a quota subscription paid partly in the form of reserve assets such as foreign currencies or SDRs and partly through making dollars available as needed by the IMF. The reserve assets provided, plus any use by the IMF of its holdings of dollars, give rise to a counterpart U.S. claim on the IMF. This represents the U.S. reserve position in the IMF. The Reserve Position in the International Monetary Fund is revalued monthly based on the SDR valuation rate calculated by the IMF, and an unrealized gain or loss on revaluation is recognized. The dollar portion of the U.S. quota subscription is "held" by the IMF through its accounts at the Federal Reserve Bank of New York in the name of the IMF. A small portion, approximately 1/4 of one percent of the U.S. quota, is maintained in the form of cash balances, subject to minimum and maximum amounts, in an operational account used in conjunction with the IMF's transactions with other member countries. The vast bulk of the IMF's dollar "holdings" are maintained in the form of a letter of credit issued by the Treasury. The U.S. Quota in the IMF is SDR 26.5 billion, valued at $36.4 billion as of September 30, 1998. The quota includes the following amounts (in millions)

Currency Holdings	
* Letter of Credit	$14,884
U.S. Dollars Held by the IMF	85
Reserve Position	21,155
U.S. Quota in the IMF	$36,124

* This amount is included as entity obligated appropriated funds under Note 2.

The difference between the $36.1 billion in the table above and the quota of $36.4 billion is due to the depreciation of the dollar against the SDR at September 30, 1998. The IMF Articles of Agreement provide that a member country must maintain the value of its currency held by the IMF, which carries all currencies held in terms of the SDR. If necessary, as a result of depreciation of the dollar against the SDR, the United States is required to make a maintenance of value payment after the close of the IMF's fiscal year, April 30, with respect to dollars held by the IMF. Deferred gains and losses are accrued by the Department based on the IMF's Summary Statement of Position. When the dollar appreciates (depreciates) against the SDR, the IMF (the United States) incurs an obligation to make payments to the U.S. (IMF). Budget authority is provided for making such U.S. payments in years when the maintenance of value adjustment requires an increase in the amount of the IMF's dollar holdings, but such payments take the form of adjustments to the letter of credit and do not result in any immediate cash transfer to the IMF. At April 30, 1998, the appreciation of the dollar against the SDR resulted in a gain to the Department which decreased the IMF's letter of credit by $274.6 million.

The IMF has established a number of financial facilities which are potentially available to all members. The Enhanced Structural Adjustment Facility was created to provide assistance on concessional terms

to low-income developing country members with protracted payment problems. This facility is financed through loans and other contributions by IMF members rather than by quota resources. In Fiscal Year (FY) 1998 the Department contributed $24 million for this facility. This contribution represents an expense to the Department. Additionally, at September 30, 1998, $48 million is available to the Enhanced Structural Adjustment Facility in the form of a letter of credit.

To supplement the general resources available to the IMF, the U.S. and certain other members created the General Arrangements to Borrow (1962) and the New Arrangements to Borrow (1998). Funding from GAB and NAB can be made available when supplementary resources are needed by the IMF to forestall or cope with an impairment of the international monetary system. A loan to the IMF was made under GAB during FY 1998 in the amount of SDR 361 million, valued at $495 million at September 30, 1998. The remaining amount of credit available to the IMF at September 30, 1998 under GAB was SDR 3.9 billion valued at $5.3 billion. NAB was approved in October 1998 (FY 99) for SDR 2.5 billion and is valued at $3.5 billion. The amounts available from GAB and NAB are through Congressional appropriations. The IMF's borrowings, like its general resources, are denominated in SDRs. Any such loan gives rise to a similar counterpart claim on the IMF. These claims are interest bearing and liquid, as they may be exercised in short notice if the U.S. experiences any balance of payment problems and needs additional foreign currency reserves.

7. Investments in International Financial Institutions

The Department participates in MLDBs to support poverty reduction, private sector development, transition to market economies and sustainable economic growth and development, thereby advancing the United States' economic, political, and commercial interest abroad. The MLDBs consist of the World Bank Group, five regional development banks and the Global Environment Facility

Most of the contributions to financial institutions involve investments in MLDBs. The Department has the lead in negotiating the establishment and replenishment of resources for these financial institutions through multi-lateral agreements. These agreements specify the financial elements, underlying provision of resources, and longer-term policy framework within which these resources will be used. Congress appropriates funds for capital subscriptions and contributions to the multi-lateral development accounts in foreign operations appropriation acts. These appropriations were $1.5 billion in FY 1998. Appropriations can be used for three types of transactions: paid-in capital, callable capital, and replenishments (concessional loans/grants). Paid-in capital is the capital stock the U.S. buys with U.S. currency or a convertible currency. No dividends are received; however, on occasion, there have been net income transfers to the concessional loan programs. Callable capital is issued not for money, but for the good faith commitment of the member to pay in cash upon request by the bank. Callable capital subscriptions are subject to call, under limited circumstances, only when required to meet the obligations of the respective MLDBs created by borrowing. To date, there has not been, nor is there anticipated to be, a call on capital subscription. For this reason, beginning in fiscal year 1981, callable capital was no longer appropriated. Congress provided for callable capital through the use of program limitations in appropriation legislation instead of appropriations. Replenishments are funds provided to the banks for their concessional lending operations. These contributions are not expected to be paid back to the U.S. Rather, repayments of the concessional loans go back to the concessional window for further lending, thus reducing the burden on the member countries for future replenishments. FY 1998 contributions to the MLDBs were $1.5 billion.

U.S. payments to MLDBs are made by cash transfers, non-interest-bearing letters of credit, or a combination of the two. The Department authorizes both the cash payments and letters of credit issued to the institutions. The Federal Reserve Bank of New York administers the letters of credit.

The Department currently values its investments in these financial institutions for paid in capital at cost. Contributions to these international financial institutions for paid-in capital are reported as investments.

As of September 30, 1998, investments in international financial institutions consisted of the following (in millions):

Inter-American Development Bank	$1,301
Asian Development Bank	381
International Bank for Reconstruction & Develop.	1,985
African Development Bank	135
Multilateral Investment Guarantee Agency	22
European Bank for Reconstruction & Development	367
North American Development Bank	174
International Buffer Stocks	78
International Finance Corporation	569
Total	$5,012

8. *Inventories and Related Property, Net*

Inventories and related property includes inventories, operating materials and supplies, and forfeited property held by the Department, that as of September 30, 1998 are as follows (in millions):

Inventories and Related Property:	
Inventories, Net	$244
Materials and Supplies	97
Forfeited Property	24
Total	$365

Inventories, Net

The Department's manufacturing entities, the Bureau of Engraving and Printing (BEP) and the United States Mint, maintain inventory accounts or balances (e.g., metals, paper, etc.) for use in manufacturing currency and coins. The cost of these items are included in inventory costs, and are recorded as cost of goods sold upon delivery to customers. The Financial Management Service also holds inventory for check processing activities. These inventories as of September 30, 1998 are as follows (in millions):

Inventory Category:	Acquisition Cost	Allowance for Losses	Inventory Net
Inventory held for current sale	$245	($1)	$244
Composition of Inventory:			
Raw Material & Supplies	$195		
Work in Process	33		
Finished Goods	16		
Total	$244		

Operating Materials and Supplies, Net

The Department's operating materials and supplies primarily consist of aircraft and marine parts used to repair and maintain aircraft and vessels for enforcement related activities. Operating materials and supplies are also maintained for the production of bureau products. As of September 30, 1998, operating materials and supplies was as follows (in millions):

Composition of Materials:	
Held for Use	$97
Held in reserve for use	0
Excess, Obsolete and Unserviceable.	0
Total Materials & Supplies	$97

Forfeited Property, Net

As a consequence of enforcing various laws, certain property is seized by the Department's enforcement bureaus. The seized assets may be subsequently forfeited to the government through abandonment or administrative or judicial procedures. Information concerning seized assets activity can be found under footnote five, Cash and Other Monetary assets. As of September 30, 1998, forfeited property held by the Department was as follows (in thousands):

Property held for sale	$25,632
Property to be shared with Federal, state or local, or foreign governments	186
Total Forfeited Property (Gross) 9/30/98	$25,818
Less: allowance for mortgages and claims Property held for sale	(1,598)
Total Forfeited Property (Net) 9/30/98	$24,220

Forfeited property is recorded at estimated fair value at the time of seizure. However, based on historical sales experiences for the year, properties are adjusted to reflect the current fair market value at the end of the fiscal year. Property forfeited in satisfaction of a taxpayers liability is recorded when title to the property passes to the Federal Government and a corresponding credit is made to the related accounts receivable. Direct and indirect holding costs are not capitalized for individual forfeited assets. Forfeited currency is reported as Cash, Foreign Currency and Other Monetary Assets in the accompanying Consolidated Balance Sheet.

Mortgages and claims on forfeited assets are recognized as a valuation allowance and a reduction of deferred revenue from forfeited assets when the asset is forfeited. The allowance includes mortgages and claims on forfeited property held for sale and a minimal amount of claims on forfeited property previously sold. Mortgages and claims expenses are recognized when the related asset is sold and are reflected as a reduction of sales of forfeited property.

Also included in forfeited property are prohibited items. Prohibited items are items with no legal market value in the United States and which will not be sold for export. They include explosives and pornography. Forfeited firearms that will not be sold due to Department policy are also considered to be prohibited items. Illegal drugs and other forfeited property are retained by the Department until final disposition.

The following schedule presents the changes in the forfeited property balances from October 1, 1997 to September 30, 1998 (in thousands):

	10/1/97 Financial				10/1/97							
	Statement Balance		Adjustment		Carrying Value		Forfeitures		Deposits/Sales		Disposals/Transfers	
	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number
Currency	$18,103	-----	$0	-----	$18,103	-----	$157,825	-----	$(165,593)	-----	$(35)	-----
Other Monetary Instruments	1,236	0	170	0	1,406	0	5,297	0	(6,009)	0	(198)	0
Real Property	24,629	212	2,784	0	27,413	212	14,956	94	(20,448)	(131)	(1,400)	(19)
General Property	7,701	3,954	28,427	0	36,128	3,954	25,293	12,282	(33,960)	(3,301)	(2,036)	(1,661)
Vessels	797	53	468	0	1,265	53	1,501	121	(1,230)	(67)	(954)	(26)
Aircraft	138	4	(10)	0	128	4	384	6	(344)	(7)	(40)	(2)
Vehicles	4,710	1,001	500	0	5,210	1,001	14,816	6,379	(10,569)	(5,683)	(3,758)	(220)
Prohibited Items	-----	12,728	-----	(687)	-----	12,041	-----	62,489	-----	(60)	-----	(3,697)
Total Forfeited Property (Gross)	39,211	17,952	32,339	(687)	71,550	17,265	62,247	81,371	(72,560)	(9,249)	(8,386)	(5,625)
Grand Total	$57,314	17,952	$32,339	(687)	$89,653	17,265	$220,072	81,371	($238,153)	(9,249)	($8,421)	(5,625)

	Victim Restitution		Destroyed		Other Adjustments		Value Change		Fair Value Adjustment		9/30/98 Financial Statement Balance	
	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number
Currency	$0	-----	$0	-----	$7,200	-----	$38	-----	$0	-----	$17,538	-----
Other Monetary Instruments	0	0	(6)	0	47	0	(212)	0	(66)	0	259	0
Real Property	0	0	0	0	(1,152)	(15)	(563)	0	(2,399)	0	16,407	141
General Property	0	0	(1,192)	(7,379)	(4,036)	475	(2,904)	0	(13,591)	0	3,702	4,370
Vessels	0	0	(26)	(44)	422	8	(214)	0	(191)	0	573	45
Aircraft	0	0	0	0	37	0	0	0	25	0	190	1
Vehicles	0	0	(23)	(15)	(243)	26	(80)	0	(666)	0	4,687	1,488
Prohibited Items	-----	0	-----	-56039	-----	3033	-----	0	-----	0	-----	17,767
Total Forfeited Property (Gross)	0	0	(1,247)	(63,477)	(4,925)	3,527	(3,973)	0	(16,888)	0	25,818	23,812
Less Allowance											(1,598)	
Total Forfeited Property (Net)											24,220	
Grand Total	$0	0	($1,247)	(63,477)	$2,275	3,527	($3,935)	0	($16,888)	0	$41,758	23,812

Value change is an adjustment to reflect the net value of a forfeited asset from the initial appraisal to the latest appraisal. This could result in a positive or negative change.

The **fair value** adjustments above are necessary to convert forfeited property from unadjusted carrying value (market value at the time of seizure) to an estimate of the fair value at the time of forfeiture, which is the amount recorded in the financial statements. Other adjustments primarily represent property forfeited in prior fiscal years but reversed to seized status during the current fiscal year. Due to the varied mix of specific types of assets within each asset category, the number of items presented in the 10/1/97 balance represent qualities calculated using many different units of measure. Due to the use of different units of measure, within each asset category, the usefulness of this quantity disclosure is questionable. In FY 1998, in order to present a more meaningful quantity, the number presented for each class of property represents the number of seizure line items recorded regardless of the unit of measure of quantity.

Other adjustments above primarily represent minor reclassifications or adjustments to beginning balances.

9. Property, Plant and Equipment, Net

As of September 30, 1998, property, plant and equipment consists of the following (in millions):

	Depr Method	Service Life	Acquisition Cost	Accumulated Depreciation	Net Book Value
Land	N/A	N/A	$19	$0	19
Structures, Facilities	S/L	3-50 yrs	473	(176)	297
ADP Software	S/L	2-10 yrs	145	(73)	72
Equipment	S/L	2-20 yrs	949	(529)	420
Assets under Capital Lease	S/L	2-25 yrs	187	(74)	113
Construction in Progress	N/A	N/A	45	0	45
Aircraft	S/L	12-20 yrs	397	(177)	220
ADP Equipment	S/L	5-10 yrs	612	(439)	173
Vessels	S/L	5-10 yrs	32	(24)	8
Vehicles	S/L	3-9 yrs	74	(56)	18
Other	S/L	2-30 yrs	278	(202)	76
Total	N/A	N/A	$3,211	($1,750)	$1,461

* N/A -Not Applicable

The Department leases land and buildings from the General Services Administration (GSA) to conduct most of its operations. GSA charges a standard level users fee which approximates commercial rental rates for similar properties.

The Treasury Complex (Main Treasury Building and Annex) was declared a national historical landmark in 1972. The Treasury Complex is treated as a heritage asset and is expected to be preserved indefinitely. Accordingly, it is not capitalized. Renovations and improvements to the Main Treasury Building and Annex amounted to $ 1.6 million in FY 1998.

In FY 1998, the Department reported $5 million in deferred maintenance on general property plant and equipment. The $5 million represents deferred maintenance on vehicles and buildings and structures owned by the Department. The Department uses condition assessments surveys to measure deferred maintenance as follows (in millions):

	Asset Condition	Cost to Return to Acceptable Condition
Building & Structures	Fair to Poor	$4
Equipment	Poor	1
Total		$5

10. *Due from the General Fund, Net*

The Department is responsible for managing various assets and liabilities on behalf of the Federal Government. Assets managed by the Department on behalf of the General Fund includes cash, silver reserves, loans, advances, and tax/trade receivables. In terms of liabilities, the Department manages the Federal Debt as well as tax refunds on behalf of the Federal Government.

Because these assets and liabilities belong to the Federal Government, the Department does not report the net related effect of these transactions in net position. Instead, the Department reports this net effect in the account, "Due from the General Fund." As of September 30, 1998, Due from the General Fund (Net) included the following (in millions):

Liabilities Requiring Funding From the General Fund:	
Federal Debt & Interest Payable	$3,694,516
Federal Debt & Interest Payable - Intragovernmental	1,785,180
Refunds & Drawbacks	1,173
Other Liabilities	11
Sub-total	5,480,880
Less Assets to be Distributed to the General Fund:	
Fund Balance	(1,646)
Advances to the Black Lung Trust Fund	(5,857)
Cash, Foreign Currency and Other Monetary Assets	(41,617)
Gold & Silver Reserves	(24)
Loans & Interest Receivable - Intragovernmental	(154,234)
Accounts Receivable - Intragovernmental	(141)
Tax/Trade and Other Non-Entity Receivables	(30,164)
Other Assets	(8)
Sub-total	(233,691)
Total	$5,247,189

Netted in the computation of "Due from the General Fund" are certain non-entity assets the Department holds for others. The following is summary of these accounts:

(1) Non-Entity Fund Balance

Amount Provided for Interest Payable to the Public on the Federal Debt	$45,430
Amounts Provided for the Payment of Contingencies and Drawbacks	243
Amounts for Deposit Funds and Other Liabilities	572
Total Fund Balance Payable to Others	46,245
Fund Balance Payable to the General Fund	1,646
Total Non-Entity Fund Balance	$47,891

(2) Cash, Foreign Currency and Other Monetary Assets

Seized Monetary Assets	90
Undistributed Cash/Offers in Compromise	85
Total Cash, Foreign Currency and Other Monetary Assets Held for Others	175
Cash, Foreign Currency and Other Monetary Assets Held for the General Fund	41,617
Total Cash, Foreign Currency and Other Monetary Assets	$41,792

(3) Gold and Silver Reserves - the Department issues gold certificates to the Federal Reserve for gold it holds on behalf of the Federal Government. Upon issuance of gold certificates, the Department receives cash from the Federal Reserve which is deposited into the General Fund. Therefore, all of the Department's certificates are payable to the Federal Reserve. The Department held $11,017 million in gold, all of which is reflected as a liability in gold certificates. Additionally, the Department held $24 million in silver, which is payable to the General Fund. The total of gold and silver reserves, as of September 30, 1998 was $11,041 million.

11. Advances to the Black Lung Trust Fund

Advances have been provided to the Black Lung Trust Fund from the General Fund pursuant to 26 USC 9501, and are used to carry out the purposes of this trust fund. The principal and interest on these advances are to be repaid to the General Fund when the Secretary of the Treasury determines that monies are available in the Black Lung Trust Fund for such purposes. Interest is charged from the date funds are advanced to the trust fund. As of September 30, 1998, these advances and accrued interest totaled $5,857 million.

12. Gold & Silver Reserves, and Gold Certificates Issued to Federal Reserve Banks

The Department is responsible for safeguarding most of the Federal Government's gold and silver reserves in accordance with 31 USC 5117. The Consolidated Balance Sheet also reflects gold being held in the Federal Reserve Bank of New York.

Gold Reserves being held by the Department are offset by a liability for gold certificates issued by the Secretary of the Treasury to the Federal Reserve as provided under 31 USC 5117. Since 1934, Gold certificates have been issued in non-definitive or book-entry form to the Federal Reserve. The Department's liability incurred by issuing the Gold Certificates is limited to the gold being held by the Department at the legal standard value established by law. Upon issuance of gold certificates to the Federal Reserve, the proceeds from the certificates are deposited into the operating cash of the Federal Government. Therefore, all of the Department's certificates issued are payable to the Federal Reserve.

Absent any historical cost records to determine the acquisition cost of the gold and silver over several decades, the statutory rates of $42.2222 per fine troy ounce (FTO) for gold and $1.2929292 per FTO

for silver are used to value the entire custodial reserves held by the Mint. As of September 30, 1998, the Gold and Silver Reserves consisted of the following:

	FTO's	Statutory Rate	Statutory Rate (Millions)	Market Value	Market Value (Millions)
Gold	247,477,782.820	$42.2222	$10,449	$293.85	$72,721
Gold Held by Federal Reserve Banks & in Transit	13,450,412.867	42.2222	568	293.85	3,952
Subtotal - Gold	260,928,195.687		11,017		76,673
Silver	18,725,238.080	1.2929292	24	5.39	101
Total Gold and Silver Reserves			$11,041		$76,774

13. Tax/Trade and Other Non-Entity Receivables, and Related Interest, Net

Tax/trade and other non-entity accounts receivable includes receivables from tax assessments, custom duties, excise taxes, fees, penalties, and interest assessed and accrued, reduced by an estimate for uncollectible amounts. Also included in non-entity receivables are earnings due on monies deposited in Federal Reserve Banks as follows (in millions):

Tax Trade Receivable, Gross	$82,164
Receivable, Deposit of Earnings, Federal Reserve	1,099
Other Receivables & Interest	2,228
Total Tax/Trade Other Non-Entity Receivables - Gross	85,491
Allowance	(55,327)
Tax/Trade Receivable & Other Receivables Net	$30,164

An allowance for doubtful accounts was established for the difference between the gross receivables and the portion deemed collectible. The portion of tax/trade receivables estimated to be collectable and the allowance for doubtful accounts are based on projections of collectibility from a statistical sample of taxes receivable. The Department does not establish an allowance for the receivable on deposits of Federal Reserve earnings.

IRS Federal taxes receivable constitute the largest portion of the receivables. IRS Federal taxes receivable consists of tax assessments, penalties, and interest which were not paid or abated, and which were agreed to by either the taxpayer and the Service, or the courts.

Other Receivables includes certain loans and credits issued by the United States to various foreign governments. The agreements with each debtor government vary as to dates, interest rates, method of payment, and billing procedures. All such loans and credits represent legally valid and outstanding obligations of foreign governments, and the U.S. Government has not waived or renounced its rights with respect to any of them. All such loans and credits remain due and payable.

14. Loans Payable & Interest

The Department finances its lending activities with borrowings from the General Fund. Interest rates on these loans ranged from 4.731 percent to 16.241 percent, during fiscal year 1998. The maturity dates on these borrowings ranged from October 1, 1998 to December 31, 2031.

Additional borrowings are outstanding with the Civil Service Trust Fund, which is administered by the Office of Personnel Management. The interest rates on these borrowings range from 8.75 percent to 9.25 percent, and the maturity dates range from June 30, 2003 to June 30, 2005. As of September 30, 1998, loans payable consisted of the following (in millions):

	Beginning Balance	New Borrowings	Repayments	Ending Balance
Borrowing from the General Fund	$35,151	$139,287	$(140,217)	$34,221
Borrowing from the Civil Service Trust Fund	15,000	0	0	15,000
Subtotal - Principal	50,151	139,287	(140,217)	49,221
Interest Payable				1,380
Total				$50,601

Debt Prepayment Premium

Under the terms of its master promissory note with the General Fund, the borrowings from the General Fund must be liquidated at the same time as loans receivable financed by those borrowings are liquidated. The maturity and, except for a one-eighth of one percent spread, the interest rate on the loans receivable is normally matched with the maturity and interest on borrowings. In addition, for most of the loans, premiums or discounts resulting from loan prepayments are equivalent to the premiums or discounts paid or received when the borrowings from the General Fund are simultaneously prepaid. Premiums or discounts arise to the extent that market interest rates at the prepayment date differ from rates stated in the loan agreements. The effect of these policies is to mitigate the Department's risk from interest rate fluctuations.

However, Congress authorized certain Rural Utility Service's (RUS) guaranteed borrowers to prepay their loans at par rather than market value up to a specified dollar limit. Legislation also authorized borrowers in the foreign military sales program guaranteed by Department of Defense to prepay, at par, certain loans meeting specific criteria. The effect of these statutes was to waive the borrowers' premium payments, which would otherwise have resulted in interest rates at the dates of prepayment being less than the rates in the loan agreements. Notwithstanding the fact that the borrowers' premiums were waived, the Department remained liable for premiums due on its debt to the General Fund and incurred prepayment penalties. There were no debt prepayments in fiscal year 1998. However, the Department incurred interest expenses on the debt prepayment premium payable. On September 18, 1998 the Department borrowed funds from the General Fund to pay the debt prepayment premium and related interest expense.

Forgone Interest

Under Title III of the Rural Electrification Act of 1936, the Department receives interest on certain loans to the RUS at an interest rate which is less than the contractual interest rate stated in the loan agreements to RUS. This interest credit is calculated based on the balance in an RUS Liquidating Fund. The Department has no control over the balances in the RUS Liquidating Fund. The Department does not have recourse against RUS and must absorb the cost of the interest credit (i.e. "forgone interest"). However, the Department is obligated to pay contractual interest on its borrowing from the General Fund.

Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan" requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or based on the fair market value of the loan or underlying collateral. SFAS No. 114 considers a loan to be impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the original agreement. Management of the Department has determined that certain RUS loans are impaired as defined by SFAS No. 114 since the Department will not receive all interest due in accordance with the original terms of the loan agreements.

As a consequence of the legislative requirements that resulted in the foregone interest and the loan prepayments as described above, the Department has incurred significant losses. To make up these losses, the Department sought, and subsequent to year end, received an appropriation in FY 1999 from Congress (See Note 31).

15. Certificates Issued to Federal Reserve Banks

The Special Drawing Rights Act of 1968 authorized the Secretary of the Treasury to issue certificates, not to exceed the value of SDR holdings, to the Federal Reserve Bank in return for interest free dollar amounts equal to the face value of certificates issued. The certificates may be issued to finance the acquisition of SDRs from other countries or to provide resources for financing other exchange stabilization fund operations. Certificates issued are to be redeemed by the Department at such times and in such amounts as the Secretary of the Treasury may determine.

As of September 30, 1998, the amount of certificates outstanding was $9,200 million while the value of SDR holdings was $10,176 million, for a difference of $976 million.

16. DC Pension Liability

On October 1, 1997, the Department took full responsibility (assets and liabilities) for certain District of Columbia retirement plans. Plan assets assumed of $3.8 billion and liabilities of $8.6 billion, resulted in an unfunded liability of $4.8 million on October 1, 1997. The transfer of that unfunded liability was treated as an adjustment to Net Position. As of September 30, 1998, the funds assets were $3.7 billion, and liabilities were $8.8 billion, resulting in an unfunded liability of 5.1 billion. The costs incurred by the plans for the year are included in the statement of net costs.

Pursuant to the Balanced Budget Act of 1997, as amended, the Secretary of the Treasury established the Federal Supplemental District Pension Fund (the Supplemental Fund) that shall be used for the accumulation of funds in order to finance obligations of the Federal Government for benefits and necessary administrative expenses under the provision of the Revitalization Act.

At the end of each applicable fiscal year, the Secretary shall promptly pay into the Supplemental Fund from the General Fund an amount equal to the annual amortization amount. The amount is based on the original unfunded liability, which is the present value as of the freeze date of future benefits payable from the Supplemental Fund. The Secretary is further directed to pay from the General Fund into the Supplemental Fund, during each applicable fiscal year, amounts not to exceed the covered administrative expenses for the year.

17. Federal Debt & Interest Payable

The Department is responsible for administering the Federal Debt on behalf of the Federal Government. The Federal Debt includes borrowings from the public as well as borrowings from Federal agencies. The Federal Debt managed by the Department does not include debt issued by other governmental agencies such as the Tennessee Valley Authority, or the Department of Housing and Urban Development. The Federal Debt as of September 30, 1998 is as follows (in millions):

Intragovernmental	
Beginning Balance	$1,583,459
New Borrowings*	166,512
Premium/Discount	4,727
Interest Payable, Not Covered by Budgetary Resources	30,482
Total, Not Covered by Budgetary Resources	1,785,180
Interest Payable, Covered by Budgetary Resources	32
Total	$1,785,212

*New Borrowings (Intra-governmental) - represent the net increase in amounts borrowed.

Debt Held by the Public	
Beginning Balance	$3,814,687
New Borrowings	2,127,992
Repayments	(2,181,457)
Premium/Discount	(66,720)
Interest Payable, Not Covered by Budgetary Resources	14
Total, Not Covered by Budgetary Resources	3,694,516
Interest Payable, Covered by Budgetary Resources	45,417
Total	$3,739,933

Debt held by the public approximates the federal government's competition with other sectors in the credit markets. This affects interest rates and private capital accumulation.

In contrast, debt held by Federal entities, primarily trust funds, represents the cumulative annual surpluses of these funds (i.e. excess of receipts over disbursements plus accrued interest). Debt held by Federal

entities does not have any of the economic effects of borrowings from the public. It is not a current transaction of the government with the public; it does not compete with the private sector for available funds in the credit markets. It reduces the need to borrow from the public and so may hold down interest rates. Unlike debt held by the public, debt held by federal entities does not represent an immediate burden on current taxpayers. Rather it is a claim on future resources. The surplus is held in Treasury securities which gives the Federal entities a claim on the Federal Government, equal to the value of those securities. When the securities have to be redeemed, the Department must come up with the cash. Actions that could be taken to meet these cash needs include lowering spending, increasing taxes, and increasing borrowings from the public.

Federal Debt Held by Federal Agencies

Certain Federal agencies are allowed to invest excess funds in debt securities issued by the Department on behalf of the Federal Government. The terms and the conditions of debt securities issued are designed to meet the cash needs of the Federal Government. The vast majority are non-marketable securities issued mostly at par value. Most non-marketable debt securities are issued at par value, but some are issued at market prices whose prices and interest rates reflect market terms. The average interest rate for GAS securities in fiscal year 1998 was 7.1 percent.

The Federal Debt also includes marketable debt securities that certain agencies are permitted to buy and sell on the open market. The investments held, at par value, by the various Federal agencies as of September 30, 1998 are as follows (in millions):

SSA: Federal Old-Age and Survivors Insurance Trust Fund	$653,282
OPM: Civil Service Retirement and Disability Fund*	431,757
DOD: Military Retirement Fund	133,843
HHS: Federal Hospital Insurance Trust Fund	118,250
SSA: Federal Disability Insurance Trust Fund*	76,996
DOL: Unemployment Trust Fund*	70,641
HHS: Federal Supplementary Medical Insurance Trust Fund	39,502
FDIC: The Bank Insurance Fund	27,445
DOT: Highway Trust Fund	17,926
OPM: Employees' Life Insurance Fund	19,377
RRB: Railroad Retirement Account	19,764
Treasury: Exchange Stabilization Fund	15,981
HUD: FHA – Liquidating Account	14,344
VA: National Service Life Insurance Fund	12,008
Nuclear Waste Disposal Fund	11,169
Other Programs and Funds	87,686
Total Federal Debt Held By Federal Entities, Par Value	$1,749,971

* These amounts include marketable Treasury securities as well as Government Account Series (GAS) securities as follows (in millions):

	GAS Securities	Marketable Treasury Securities	Total
Civil Service Retirement and Disability Fund, Par Value	$430,595	1,162	$431,757
Federal Disability Insurance Trust Fund, Par Value	$76,947	49	$76,996
Unemployment Trust Fund, Par Value	$70,598	43	$70,641

Social Security Administration (SSA); Office of Personnel Management (OPM); Department of Defense (DOD); Department of Health and Human Services (HHS); Department of Labor (DOL); Federal Deposit Insurance Corporation (FDIC); Department of Transportation (DOT); Railroad Retirement Board (RRB); Department of the Treasury (Treasury); Department of Housing and Urban Development (HUD); Department of Veterans Affairs (VA).

Federal Debt Held by the Public

As of September 30, 1998, Federal Debt held by the Public consisted, at par value, of the following (in millions):

Securities		Average Interest Rates	Term
Treasury Bills	$637,648	5.2%	One year or less
Treasury Notes	2,051,046	6.2%	More than one year up to ten years
Treasury Bonds	625,675	8.6%	More than ten years
Total Marketable	3,314,369		
Non-Marketable	446,853	6.2%	On Demand to more than ten years
Total Federal Debt Held by the Public	$3,761,222		

Marketable bills are issued at a discount and repaid at the par amount of the security upon maturity. The average interest rate on a Treasury Bill represents the average effective yield on the security.

Marketable notes and bonds are issued as long term securities that pay semi-annual interest based on the security's stated interest rate. These securities are issued at either par value, or at an amount that reflects a discount or a premium. The average interest rate represents the stated interest rate adjusted for any discount or premium. As of September 30, 1998, marketable notes include $41,863 million of Inflation Indexed Notes and the marketable bonds included $16,960 million of Inflation Indexed Bonds.

Non-Marketable securities primarily consist of $186,006 million in U.S. Savings Securities and $164,431 million in securities issued to state and local governments. Non-marketable securities are issued at

both par and discounted values. The average interest rate on the non-marketable securities represents the weighted effective yield.

18. Commitments, Contingencies and Other Risks

Contingencies represent certain pending and threatened legal matters reported by the Internal Revenue Service (IRS), Federal Law Enforcement Training Center (FLETC), United States Secret Service, United States Customs Service (Customs), Bureau of Alcohol, Tobacco, and Firearms (ATF), and Departmental Offices.

At September 30, 1998, the Department recorded a total probable liability of $70 million that is included in other liabilities. This includes $17 million reported by the IRS for pending and threatened legal matters which, in the opinion of IRS's Chief Counsel, are probable losses associated with pending and threatened legal matters. These liabilities could change depending on the ultimate outcome of cases.

Further, additional losses from pending and threatened legal matters, considered reasonably possible by IRS's Chief Counsel, are estimated to be $8 million. The IRS is also involved in various legal actions for which amounts will be payable from the Judgment Fund, which is managed by Treasury on behalf of the Federal Government. Of the $17 million accrued by the Service, $15 million will be payable from the Judgment Fund for judgments, and settlements relating to Service litigation and claims.

FLETC is involved in various legal actions and administrative proceedings incidental to its operations. As of September 30, 1998, FLETC recorded contingent liabilities of $2.2 million for these pending claims and lawsuits. Secret Service is a party to various administrative proceedings, legal actions, and claims brought by or against it. Most financial liabilities resulting from unfavorable court decisions will be funded from the Judgement Fund. At September 30, 1998, Secret Service has identified $12.8 million as contingent liabilities on the Balance Sheet. Additionally, it is reasonably possible that Secret Service would be liable for an additional $19 million as of September 30, 1998.

Customs recorded a probable liability of $37 million as of September 30, 1998, of which $33.8 million would be funded by Customs and $2.7 million from various claims and judgement funds maintained by Treasury. Further, Customs Counsel determined that it is reasonably possible that Customs will be liable for an additional $185.7 million as of September 30, 1998, of which $149.5 million would be funded by Customs and $36.2 million from various claims and judgement funds managed by Treasury on behalf of the Federal Government. Of the probable liability of $36.5 million Customs reported as of September 30, 1998, $31.4 million was related to contingencies for trade litigation.

Additionally, Customs has been involved with litigation involving the collection of Harbor Maintenance Fees. Customs collects Harbor Maintenance Fees which are used for the maintenance of U.S. harbors. The collections are recorded in the Harbor Maintenance Fee Trust Fund. During FY 1998, the Supreme Court ruled that the assessment of a Harbor Maintenance Fee on exports violates the United States Constitution. Collections received during the judgement period totaled $1.1 billion at September 30, 1998. The refunds are to be paid from a permanent indefinite appropriation managed by the Department on behalf of the Federal Government.

ATF identified and accrued $967,000 as a probable liability. The contingent liability reported by ATF represents administrative tort and employee claims brought against ATF. It also includes personnel

and EEO cases which counsel has identified as a probable liability that would be referred to the Judgement Fund for payment. ATF also identified a $21.1 million liability as reasonably possible resulting largely from personnel and EEO cases, in addition to administrative tort and employee claims brought against ATF. The chart below provides a summary of the Departments contingent liabilities as follows (in millions):

Entity	Not Covered by Budgetary Resources Probable & Estimatable	Covered by Budgetary Resources Probable & Estimatable	Total
Customs	$6	$31	$37
IRS	17	0	17
Secret Service	13	0	13
FLETC	2	0	2
ATF	1	0	1
Total	$39	$31	$70

The Department may enter into swap agreements with other countries that provide for drawings of dollars by those countries and\or drawings of foreign currencies by the Department. Any balances the Department may hold under such agreements are generally held for other than trading purposes. The Department is exposed to credit risk on foreign currency agreements in the event of default by counter parties only to the extent they are reported on the Consolidated Balance Sheet. Market risk occurs as a result of fluctuations in currency exchange rates.

The Department is not exposed to market risk on foreign countries' drawings, because, under these agreements, the Department will receive an agreed upon amount in dollars upon maturity regardless of fluctuations in currency exchange rates. As of September 30, 1998, there are no outstanding swap agreements with foreign governments or central banks.

The Department enters into guarantee agreements with lenders and/or investors that provide for repayment of all or part of the principal and/or interest on certain debt obligations of a borrower and/or issuer. The Department is exposed to credit risk on guarantees in the event that it has to honor a guarantee and is unable to recover from the borrower amounts advanced under the guarantee. As of September 30, 1998, there were no guarantee agreements held by the Department.

The Department has subscribed to additional capital for certain multi-lateral development banks (MLDBs), portion of which are callable. However, these subscriptions are callable under certain limited circumstances to meet the obligations of the respective MLDBs. There has never been, nor is there anticipated, a call on the Department's subscriptions. As of September 30, 1998 U.S. callable capital in MLDBs is as follows (in millions):

	Callable Capital
Inter-American Development Bank	$25,679
Asian Development Bank	4,591
International Bank for Reconstruction & Development	22,642
African Development Bank	947
Multilateral Investment Guarantee Agency	178
European Bank for Reconstruction and Development	940
North American Development Bank	1,275
Total	$56,252

In addition to the callable portion of the U.S. capital stock in the International Bank for Reconstruction and Development, an additional $5.7 billion has been authorized by Public Laws 79-171 and 86-48 to be available for borrowing by the Bank under a borrowing authority in the event the Bank is unable to meet its commitments. Any borrowing made by the Bank would be exchanged for callable capital stock of the Bank.

19. Net Position

As of September 30, 1998, Net position consisted of the following (in millions):

	Revolving Funds	Trust Funds	Appropriated Funds	Special Funds	Total
Unexpended Appropriations					
Unobligated-Available	$744	$172	$12,719	$0	$13,635
Unobligated-Unavailable	0	0	164	0	164
Obligations/Undelivered Orders	1	62	20,814	0	20,877
Total Unexpended Appropriations	745	234	33,697	0	34,676
Cumulative results of Operations	21,872	(5,086)	26,384	1,242	44,412
Total	$22,617	($4,852)	$60,081	$1,242	$79,088

Unexpended Appropriations. Represents the amount of spending authorized as of year-end that is unliquidated or unobligated and had not lapsed, been rescinded, or withdrawn. No-year appropriations remain available for obligation until expended. Annual appropriations remain available for upward or downward adjustment of obligations until expired. The amount reported for undelivered orders in this note is different than the amount reported on the Combined Statement of Budgetary Resources. The difference is attributed to the Balance Sheet being prepared on a consolidated basis versus the Statement of Budgetary Resources being prepared on a combined basis.

Cumulative Results of Operations. Represents the net results of operations since inception plus the cumulative amount of prior period adjustments, and includes cumulative amounts related to investments in capitalized assets and donations and transfers of assets in and out without reimbursement. Also included as a reduction in Cumulative Results of Operations are accruals for which the related expenses require funding from future appropriations and assessments. These future funding requirements include,

among others (a) accumulated annual leave earned but not taken, (b) accrued workers compensation, and expenses for contingent liabilities. Also included in cumulative results of operations are prior period adjustments. Prior period adjustments primarily involved accounting corrections related to prior year activity.

20. Consolidated Statement of Net Costs & Net Costs of Treasury Suborganizations

The Department's Consolidated Statement of Net Cost displays information both on a combined and a consolidated basis. The complexity of the Department's organizational structure and operations requires that supporting schedules be included in the notes to the financial statements. The supporting schedules provide consolidating information which fully displays the costs of each sub-organization.

The programs displayed on the Department's Consolidated Statement of Net Cost are equivalent to the missions identified in the Department's FY 1997-2002 Strategic Plan.

The classification of sub-organizations has been determined in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 4 which states that the predominant factor is the reporting entity's organization structure and existing responsibility components, such as bureaus, administrations, offices, and divisions within a department.

Each sub-organization is responsible for accumulating costs. The assignment of the costs to the Department-wide programs is the result of using the following cost assignment methods: (1) direct costs; (2) cause and effect; and (3) cost allocation.

The Department's FY 1997-2002 Strategic Plan includes a management mission. Costs related to the management mission are not displayed as a separate program. The rationale is that the strategic plan (for fiscal years 1997-2002) does not consider the Management Mission to be programmatic. In addition, SFFAS No. 4, recognizes that "A reporting entity and its segments may incur general management and administrative support costs that cannot be traced, assigned, or allocated to segments and their outputs. These unassigned costs are part of the organization costs, and they should be reported on the entity's financial statements (such as the Statement of Net Cost) as costs not assigned to programs." Accordingly, high level general management and administrative support costs are displayed as costs not assigned to programs. Costs not assigned to programs also include non-production costs (costs that are linked to events other than the production of goods and services) that cannot be assigned to one of the programs.

In addition, Intra-Departmental costs/revenues resulting from the provision of goods and/or services on a reimbursable basis among Departmental sub-organizations and costs incurred among sub-organizations, for which the receiving sub-organization recognizes an imputed cost and financing source, are reported as costs not assigned to programs by providing sub-organizations. This is because such costs are reported by sub-organizations, which receive the goods and/or services, as program costs. Accordingly, such costs are eliminated in the consolidation process.

To the extent practical or reasonable to do so, earned revenue is deducted from the gross costs of the programs to determine their net cost. There are no precise guidelines to determine the degree to which

earned revenue can reasonably be attributed to programs. The attribution of earned revenues requires the exercise of managerial judgment.

The Department's Consolidated Statement of Net Cost also presents interest expense on the Federal Debt and other Federal costs incurred on behalf of the Federal Government (payments made to/by the Judgment Fund, the Resolution Funding Corporation, the District of Columbia, etc.). These costs are not reflected as program costs related to the Department's strategic plan missions.

The following tables present the gross costs, earned revenue, and net costs for each program by sub-organization of the Department for the year ended September 30, 1998. Also presented are the gross costs, earned revenue, and net costs by sub-organization for the line items, "Cost not Assigned to Programs," for the year ended September 30, 1998 (in millions):

Economic: Promote Prosperous and Stable American and World Economies	--------------- Program Costs ---------------				
Suborganization	Intra-governmental	With the Public	Total Costs	Earned Revenues	Net /Total Program Costs
Departmental Offices	$24	$51	$75	$10	$65
Exchange Stabilization Fund	4	919	923	1,523	(600)
Alcohol Tobacco and Firearms	5	50	55	0	55
Bureau of the Public Debt	2	14	16	0	16
Office of the Comptroller of the Currency	17	359	376	385	(9)
Office of Thrift Supervision	0	145	145	136	9
Community Development Financial Institutions Fund	1	55	56	0	56
Treasury International Assistance Programs	9	1,277	1,286	0	1,286
Totals	$62	$2,870	$2,932	$2,054	$878

Financial: Manage the Government's Finances	--------------- Program Costs ---------------				
Suborganization	Intra-governmental	With the Public	Total Costs	Earned Revenues	Net /Total Program Costs
Departmental Offices	$23	$41	$64	$3	$61
Federal Financing Bank	4,611	0	4,611	4,507	104
Alcohol Tobacco and Firearms	5	46	51	0	51
U.S. Customs Service	365	1,178	1,543	177	1,366
Internal Revenue Service	1,546	6,351	7,897	51	7,846
Financial Management Service	130	298	428	122	306
Bureau of the Public Debt	34	271	305	5	300
Bureau of Engraving and Printing	36	431	467	436	31
U.S. Mint	55	942	997	1,591	(594)
Total	$6,805	$9,558	$16,363	$6,892	$9,471

Law Enforcement: Protect Our Financial Systems and Our Nation's Leaders, and Foster a Safe and Drug Free America	--------------- Program Costs ---------------				
Suborganization	Intra-governmental	With the Public	Total Costs	Earned Revenues	Net /Total Program Costs
Departmental Offices	$20	$15	$35	$3	$32
Alcohol Tobacco and Firearms	32	310	342	27	315
U.S. Customs Service	159	585	744	30	714
Financial Crimes Enforcement Network	1	24	25	0	25
Federal Law Enforcement Training Center	109	1	110	21	89
Treasury Forfeiture Fund	99	32	131	0	131
U.S. Secret Service	145	528	673	1	672
Total	$565	$1,495	$2,060	$82	$1,978

Costs Not Assigned to Programs

Suborganization	Costs Intra-Treasury Reimbursable	Costs Other	Earned Revenues Intra-Treasury Reimbursable	Earned Revenues Other	Net /Total Unassigned Costs
Departmental Offices	$175	$125	$175	$20	$105
Franchise Fund	9	72	9	73	(1)
Alcohol Tobacco and Firearms	26	72	26	0	72
U.S. Customs Service	84	0	84	0	0
Financial Crimes Enforcement Network	2	0	2	0	0
Federal Law Enforcement Training Center	7	0	7	0	0
Internal Revenue Service	50	0	50	98	(98)
U.S. Secret Service	12	0	12	0	0
Financial Management Service	19	0	19	0	0
Bureau of the Public Debt	1	0	1	0	0
Community Development Financial Institutions Fund	0	3	0	0	3
Office of Thrift Supervision	0	0	0	8	(8)
DC Pension Fund	0	821	0	141	680
Total	$385	$1,093	$385	$340	$753

Supporting Net Cost Schedule - by Suborganization

Year Ended September 30, 1998

(In Millions)

Suborganization	Net/ Total Program Costs	Net/ Total Unassigned Costs	Total Net Costs
Departmental Offices	$158	$105	$263
Exchange Stabilization Fund	(600)	0	(600)
Federal Financing Bank	104	0	104
Franchise Fund	0	(1)	(1)
Alcohol Tobacco and Firearms	421	72	493
U.S. Customs Service	2,080	0	2,080
Financial Crimes Enforcement Network	26	0	26
Federal Law Enforcement Training Center	89	0	89
Internal Revenue Service	7,846	(98)	7,748
Treasury Forfeiture Fund	131	0	131
U.S. Secret Service	671	0	671
Financial Management Service	306	0	306
Bureau of the Public Debt	316	0	316
Office of the Comptroller of the Currency	(9)	0	(9)
Office of Thrift Supervision	9	(8)	1
Bureau of Engraving and Printing	31	0	31
U.S. Mint	(593)	0	(593)
Community Development Financial Institutions Fund	55	3	58
Treasury International Assistance Programs	1,286	0	1,286
DC Pension Fund	0	680	680
Total	$12,327	$753	$13,080

21. Pricing Policies - Exchange Revenues

A portion of the earned revenue displayed on the Department's Statement of Net Cost is generated by the provision of goods or services to the public or to other Federal entities.

Other than as described below, exchange revenues resulting from work performed for other Treasury sub-organizations or Federal entities represent reimbursements for the full costs incurred by the performing entity. Reimbursable work between Federal appropriations is subject to the Economy Act (31 U.S.C. 1535). Prices associated with revenue earned from the public are based on recovery of full cost or are set at a market price.

As a result of the Bureau of Engraving and Printing's (BEP) success in reducing working capital requirements, currency prices were set at a level that would decrease working capital (result in a loss) for 1998. Several unforeseen expenses, including the settlement of wage negotiations with BEP's unions, wage increases enacted by Congress for the BEP's security personnel, and an increase in the actuarial liability for workers' compensation, further affected operating results for the year. As working capital needs continued to decrease during the year, these costs were also funded from existing working capital resulting in a larger than anticipated loss in the currency program and a loss in the postage program.

The Federal Law Enforcement Training Center (FLETC) receives appropriated funds to cover the cost of basic training provided to Federal, state and local law enforcement officers. FLETC charges tuition to recover the full cost of training and labor related to advanced training. FLETC recovers the full cost of food & lodging and miscellaneous expenses associated with both basic and advanced training. FLETC charges prices which recover the full cost of training private and foreign law enforcement officers.

22. Total Cost and Earned Revenue by Federal Budget Functional Classification

Total Cost and Earned Revenue
by Budget Functional Classification (in millions)

Total Cost by Functional Classification	Total Cost	Earned Revenue	Net Cost
International Affairs	$2,209	$1,523	$686
Commerce and Housing Credit	521	530	(9)
Community and Regional Development	58	0	58
Education, Training, Employment and Social Services	254	0	254
Veterans Benefits and Services	285	0	285
Administration of Justice	3,708	218	3,490
General Government	13,025	2,591	10,434
Interest	373,732	4,506	369,226
Total	$393,792	$9,368	$384,424

23. Statement of Changes in Net Position by Suborganization (In Millions)

	Departmental Offices	Exchange Stabilization Fund	Federal Financing Bank	Franchise Fund	Alcohol Tobacco & Firearms	U.S. Customs Service	FINCEN	FLETC	Internal Revenue Service	Treasury Forfeiture Fund	U.S. Secret Service
Net Cost of Operations	$277	$(600)	$104	$(1)	$493	$2,080	$26	$89	$7,748	$131	$671
Non-Exchange Revenues and Financing Sources											
Appropriation Used	269	0	0	0	457	1,716	25	77	7,413	0	654
Revenue from Forfeiture	0	0	0	0	0	0	0	0	0	139	0
Interest Revenue	0	0	0	0	0	0	0	0	0	21	0
Imputed Financing Sources	7	0	0	2	25	115	1	15	426	0	27
Transferred in	0	0	0	0	0	7	0	0	0	50	0
Transferred out	0	0	0	0	0	0	0	0	0	(8)	0
Other	0	0	0	0	0	295	0	0	0	0	0
Total Financing Sources	276	0	0	2	482	2,133	26	92	7,839	202	681
Net Results of Operations	(1)	600	(104)	3	(11)	53	0	3	91	71	10
Prior Period Adjustments	0	0	0	1	0	(17)	0	(1)	0	0	(7)
Net Change in Cumulative Results of Operations	(1)	600	(104)	4	(11)	36	0	2	91	71	3
Increase (Decrease) in Unexpended Appropriation	25	0	0	0	97	(45)	(1)	20	376	0	10
Change in Net Position	24	600	(104)	4	86	(9)	(1)	22	467	71	13
Net Position -- (10/1/97)	112	24,170	(3,168)	3	25	1,456	6	143	466	273	102
Net Position -- (9/30/98)	$136	$24,770	($3,272)	$7	$111	$1,447	$5	$165	$933	$344	$115

FINCEN - Financial Crimes Enforcement Network
FLETC - Federal Law Enforcement Training Center

	Financial Management Service	Bureau of Public Debt	Office Comptroller of the Currency	Office of Thrift Supervision	Bureau of Engraving and Printing	U.S. Mint	CDFI	Treasury International Assistance Programs	DC Pension Fund	Total
Net Cost of Operations	$8,303	$363,649	$(9)	$1	$31	$(593)	$58	$1,286	$680	$384,424
Non-Exchange Revenues and Financing Sources										
Appropriation Used	8,288	363,641	0	0	0	0	63	9,000	361	391,964
Revenue from Forfeiture	0	0	0	0	0	0	0	0	0	139
Interest Revenue	0	0	0	0	0	0	0	0	0	21
Imputed Financing Sources	9	7	15	4	8	7	0	0	0	668
Transferred in	0	0	0	0	0	0	0	0	0	57
Transferred out	0	0	0	0	0	(563)	0	(134)	0	(705)
Other	0	0	0	0	0	0	0	134	(4,830)	(4,401)
Total Financing Sources	8,297	363,648	15	4	8	(556)	63	9,000	(4,469)	387,743
Net Results of Operations	(6)	(1)	24	3	(23)	37	5	7,714	(5,149)	3,319
Prior Period Adjustments	0	0	0	0	0	0	0	28	0	4
Net Change in Cumulative Results of Operations	(6)	(1)	24	3	(23)	37	5	7,742	(5,149)	3,323
Increase (Decrease) in Unexpended Appropriation	37	(9)	0	0	0	0	17	(8,247)	0	(7,720)
Change in Net Position	31	(10)	24	3	(23)	37	22	(505)	(5,149)	(4,397)
Net Position -- (10/1/97)	47	37	139	143	563	375	90	58,503	0	83,485
Net Position -- (9/30/98)	$78	$27	$163	$146	$540	$412	$112	$57,998	($5,149)	$79,088

24. Other Non-Exchange Revenue and Financing Sources

Other non-exchange revenue primarily includes the assumption of the net D.C. Pension Liability as described in Note number 16.

25. Adjustments to Budgetary Resources Available At the Beginning of the Year & Other Information - Statement of Budgetary Resources

The Department has the following information to report as of September 30, 1998 (in millions):

Net Amount of Budgetary Resources Obligated for Undelivered Orders	$6,521
Available Borrowing and Contract Authority	$5,719
Adjustments During the Reporting Period to Budgetary Resources, Available at the Beginning of the Year	$37

26. Existence, Purpose, and Availability of Permanent, Indefinite Appropriations

Permanent and indefinite appropriations are used to disburse tax and duty refunds, duty drawbacks and earned income credits. These appropriations are not subject to budgetary ceilings established by Congress. Therefore, refunds payable at year-end are not subject to funding restrictions. Refund payment funding is recognized as appropriations used. Permanent indefinite authority is not stated as a specific amount and is available for an indefinite period of time.

Although funded through appropriations, refund and drawback activity is, in some instances, reported as a custodial activity of Treasury. This presentation is appropriate because refunds are, in substance, a custodial revenue-related activity in that they are a direct result of taxpayer overpayments of their tax liabilities. Federal tax revenue received from taxpayers is not available for use in the operation of the Department and is not reported on the Statement of Net Cost. Likewise, the resultant refunds of overpayments are not available for use by the Department in its operations. Consequently, to present refunds as an expense of the Department on the Statement of Net Cost with related appropriations used, would be inconsistent with the reporting of the related Federal tax revenue and would materially distort the costs incurred by the Department in meeting its strategic objectives.

The Department also receives two permanent and indefinite appropriations related to debt related activity. One is used to pay the interest on the public debt securities; the other is used to pay the redemptions of securities that have matured, been called, or are eligible for early redemption.

Additionally, the Department also receives permanent and indefinite appropriations to make payments on behalf of the United States Government. These appropriations are provided to make payments to the Federal Reserve for services provided. It includes appropriations provided to make other disbursements on behalf of the Federal Government and to include payments made to various individuals as the result of claims and judgement rendered against the United States.

27. Legal Arrangements Affecting the Use of Unobligated Balances of Budget Authority

Included in cumulative results of operations for special funds is $850 million that represents Treasury's authority to assess and collect user fees relating to merchandise and passenger processing, to assess and collect fees associated with services performed at certain small airports or other facilities, and to retain amounts needed to offset costs associated with collecting duties, taxes and fees for the Government of Puerto Rico. These special fund balances are restricted by law in their use to offset specific costs incurred by the Department. In addition, the Department is required to maintain $30 million in its User Fees Account. Part of the passenger fees in the user Fees Account, totaling approximately $639.6 million as of September 30, 1998 is restricted by law in its use to offset specific costs incurred by the Department and are available to the extent provided in Appropriation Acts.

In the trust fund balance, $51 million results from the Department's authority to use the proceeds from general order items sold at auction to offset specific costs incurred by Treasury relating to their sale, to use available funds in the Salaries and Expense Trust Fund to offset specific costs for expanding border and port enforcement activities, and to use available funds from the Harbor Maintenance Fee Trust Fund to offset administrative expenses related to the collection of the Harbor Maintenance Fee.

28. Collections of Federal Revenue

The Department collects the majority of the Federal Revenue from income and excise taxes and duties on imported goods. Collection activity, by revenue type and tax year was as follows for the fiscal year ended September 30, 1998 (in millions):

	Cumulative Collections Received FY 1998	---------- Tax Year ----------			
		1998	1997	1996	Prior Years
Individual Income & FICA Taxes	$1,472,205	$948,243	$501,999	$11,198	$10,765
Corporate Income Taxes	212,992	139,269	63,800	1,353	8,570
Estate and Gift Taxes	24,631	0	21,675	985	1,971
Excise Taxes	59,209	40,999	17,957	58	195
Duties	19,118	19,118	0	0	0
Fees, and Licenses	1,690	1,686	4	0	0
Unemployment Taxes	6,479	4,638	1,746	41	54
Deposit of Earnings, Federal Reserve System	24,540	18,439	6,101	0	0
Fines, Penalties, Interest & Other Revenue	18,469	15,703	2,760	0	6
Total	$1,839,333	$1,188,095	$616,042	$13,635	$21,561

Amounts reported for Corporate Income Taxes, in Tax Year 1998, includes 1999 corporate taxes of $7 billion. Individual income & FICA taxes, includes $44 billion in payroll taxes collected from other federal agencies. Of this amount, $9 billion represents the portion paid by the employers.

29. *Federal Tax Refund Activity*

Refund activity, broken out by revenue type and by tax year, was as follows for the fiscal year ended September 30, 1998 (in millions):

	Refunds Disbursed FY 1998	---------- Tax Year ---------- 1998	1997	1996	Prior Years
Individual Income & FICA Taxes	$122,908	$652	$113,351	$5,822	$3,083
Corporate Income Taxes	26,799	1,672	11,688	3,187	10,252
Estate and Gift Taxes	608	0	509	25	74
Excise Taxes	1,207	790	286	50	81
Duties	1,386	471	185	237	493
Fees, and Licenses	1	1	0	0	0
Unemployment Taxes	113	1	80	13	19
Fines, Penalties, Interest & Other Revenue	35	0	11	8	16
Total	$153,057	$3,587	$126,110	$9,342	$14,018

Individual income & FICA taxes, and other refunds amount includes EITC refunds. The EITC was originally authorized by the Tax Reduction Act of 1975 (Public Law 94-12) and made permanent by the Revenue Adjustment Act of 1978 (Public Law 95-600). The EITC is a special credit for taxpayers who work and whose earnings fall below the established allowance ceiling. Qualified taxpayers can receive partial credit in advance in each paycheck. In FY 98, the Department issued $23.2 billion in EITC refunds, of which $108 million was applied to Advance EITC. An additional $6.6 billion of EITC refunds were applied to reduce taxpayer liability.

30. *Amounts Provided to Fund the Federal Government*

Revenue collected by the Department is deposited into the General Fund. The Department transferred approximately $603.8 billion from the General Fund to Government Trust Funds (GTF), which are available for expenditure by the responsible program agencies. The Department is responsible for managing GTFs, investing all excess trust fund collections, and liquidating securities as funds are needed. The GTFs are reported on the financial statements of the responsible program agencies.

During FY 1998 the distributions to the GTFs are as follows (in millions):

Trust Fund	Disposition of Treasury Net Tax Collections
Federal Old Age & Survivors Trust Fund	$375,001
Federal Hospital Insurance Trust Fund	126,982
Federal Disability Insurance Trust Fund	58,762
Highway and Mass Transit Trust Fund	26,628
Airport and Airway Trust Fund	8,111
Unemployment Trust Fund	6,369
Other Trust Funds	1,950
Total Trust Funds	$603,803

Social Security Tax Collections

The amounts disclosed above for the Social Security Trust funds (Federal Disability Insurance Trust Fund, Federal Hospital Insurance Trust Fund, and Federal Old Age & Survivors Trust Fund) are based upon estimates provided by the Social Security Administration (SSA). Treasury reviews the estimates for reasonableness. SSA later certifies actual tax collections.

Excise Tax Collections

The Department estimates monthly excise tax collections utilizing various economic models. The Department also confers with the Council of Economic Advisors and the Office of Management and Budget in developing these estimates. The estimated amounts are transferred to GTFs. Estimates are needed because taxpayers are not required by law to identify the specific taxes included in their payments. After taxpayers provide quarterly tax returns with the details of the specific taxes, IRS certifies actual collections. The Department then adjusts the GTFs for the differences between the estimates and collections.

The amounts disclosed above are based on actual collections for three quarters and estimates for the fourth quarter for those trust funds which receive excise tax collections (i.e. Highway and Mass Transit Trust Fund, Airport and Airway Trust Fund, and certain other trust funds).

31. Subsequent Events

Public Law 105-277, approved October 21,1998, appropriated $3.3 billion to the Department to liquidate certain debts and to eliminate the accumulated deficit described in Note 14.

On November 6, 1998, Secretary Rubin agreed that the United States would provide up to $5 billion from the ESF to participate in a multilateral guarantee of a Bank for International Settlements (BIS) Credit Facility for Brazil. In this regard, on December 18, 1998, the Department authorized the Federal Reserve Bank of New York to invest approximately $1.57 billion in Treasury non-marketable securities on behalf of the ESF, corresponding to the ESF's share of the guarantee of Brazil's $4.18 billion drawing on the BIS Credit Facility on that date. Further such investments would be needed if Brazil were to make additional drawings on the BIS Facility. Under the terms of the BIS Facility, Brazil can seek

subsequent drawings or renew drawings until December 5, 1999, which is one year after the effective date of the Credit Facility.

On February 3, 1999, the ESF provided to the General Fund in exchange for dollars an amount of approximately $3.7 billion equivalent of euros for the payment of the reserve asset portion of the U.S. quota increase in the International Monetary Fund (IMF). This is in accordance with procedures agreed by the IMF membership, under which 25 percent of the quota increase was transferred to the IMF in the form of reserve assets. The remaining 75 percent was made available in the form of an increase in the letter of credit issued to the IMF by the General Fund.

The Secretary's Letter of Assurance

Consistent with the provisions of the Government Management Reform Act of 1994, and with the approval of the Office of Management and Budget, the Department of the Treasury has consolidated several statutorily required reports into its Accountability Report. This is the second year the Department did not issue a separate standalone report for Federal Managers' Financial Integrity Act (FMFIA); instead, the results of the Department's evaluations under FMFIA for the period ending September 30, 1998 are included in this Accountability Report. Reporting under Federal Financial Management Improvement Act (FFMIA) is also included in this section of the report.

Based on internal management evaluations, and in conjunction with the results of independent financial statement audits, the Department, except as noted below, can provide reasonable assurance that the objectives of Section 2 of FMFIA (internal controls) have been achieved. The Department, taken as a whole, is not able to provide reasonable assurance that the objectives of Section 4 of FMFIA (financial management systems) have been achieved. Similarly, due to the same weaknesses in financial management systems, the Department cannot state that it is in substantial compliance with the FFMIA.

Departmentwide, there are 60 material weaknesses attendant to FMFIA and FFMIA considerations as of September 30, 1998. The majority of these are concentrated in Financial Management Service (FMS)(17), Internal Revenue Service (IRS)(15), Customs (8), and Departmental Offices (6). In addition, the Department recognized four new material weaknesses associated with the District of Columbia pension responsibilities, which were assumed in October 1997. Detailed information on each material weakness, including status summaries, is provided by bureau within this section of the Accountability Report.

The Department has initiated aggressive corrective actions to resolve these issues. Thirty material weaknesses were closed during FY 1998 and several others are anticipated to be closed by early to mid calendar 1999. These positive results have been made possible in part through: (1) a renewed emphasis on management control program responsibilities throughout the Department; (2) the increased level of senior management attention given to these issues; and (3) the conscientious efforts by the bureaus to develop responsible plans for resolving weaknesses in a timely manner. I am confident that Treasury's significant progress will continue, and that improved levels of assurance can be provided for FY 1999 and beyond.

Sincerely,

Robert E. Rubin

Federal Managers' Financial Integrity Act & Federal Financial Management Improvement Act Compliance

Overall Results

During FY 1998, Treasury had a net increase of nine material weaknesses. That is, although 30 weaknesses were closed during the year, this decrease was more than offset by the addition of 39 new weaknesses. A total of 60 material weaknesses was pending as of September 30, 1998. Six of the new material weaknesses have been assigned to Departmental Offices and pertain primarily to the need to improve administrative oversight on those bureaus having common or longstanding unresolved material weaknesses in various areas. Another four new weaknesses pertain to pension operations conducted by the government of the District of Columbia, for which Treasury is now responsible. The increased total number of weaknesses is also attributable to the FMS, which took its one general systems security weakness and broke it down into seven separate weaknesses to improve the ability to monitor progress in resolving the associated difficulties. Thus, although the number of weaknesses increased during FY 1998, many items pertain to administrative, rather than systems, issues and can be resolved fairly quickly. Moreover, reasonable progress was made on every complex material weakness, where short term solutions are not possible. The increases in oversight, emphasis and resources being devoted to management control issues generally, and to material weaknesses specifically, should provide for significant progress during FY 1999.

Section 2, Management Controls

Of the 466 internal control weaknesses identified since the inception of the program (fiscal years 1983 through 1998), 438 have been corrected and closed, leaving 28 unresolved items as of September 30, 1998. Twelve of the 28 unresolved weaknesses were identified during FY 1998 review process. The sixteen unresolved items are from prior years represent complex, systemic weaknesses which by their nature require a protracted corrective action period. We have closed 23 internal control weaknesses in FY 1998.

Number of Material Weaknesses

Period Reported	Number Reported for the First Time	For That Year, Number Corrected	For That Year, Number Still Pending
Prior Year	431	422	9
1996 Report	5	4	1
1997 Report	16	10	6
1998 report	14	2	12
Total	466	438	28

Of the total number corrected, **23** were corrected in 1998.

Section 4, Financial Management Systems

Of the 497 accounting systems non-conformances identified since the beginning of the program, 32 remain unresolved as of September 30, 1998. Twenty of the 32 unresolved weaknesses were identified during the FY 1998 review process. In order to achieve systems modernization, many non-conformances are being resolved through the installation or modification of complex, computerized systems. We have closed seven financial systems non-conformances in FY 1998.

Number of Material Weaknesses

Period Reported	Number Reported for the First Time	For That Year, Number Corrected	For That Year, Number Still Pending
Prior Year	468	457	11
1996 Report	1	1	0
1997 Report	3	2	1
1998 report	25	5	20
Total	497	465	32

Of the total number corrected, **7** were corrected in 1998.

Federal Financial Management Improvement Act (FFMIA)

Among other things, the FFMIA mandates that agencies "... implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the United States government Standard General Ledger at the transaction level." FFMIA also requires that remediation plans be developed for any entity which is unable to report substantial compliance with these requirements.

Based on the results of FY 97 financial statement audits and management assessments, it was determined that four bureaus (Internal Revenue Service (IRS), Financial Management Service (FMS), U.S. Customs Service and the U.S. Mint) were not in substantial compliance with these requirements. Accordingly, the Department oversaw the development of remediation plans at these four bureaus, and submitted these plans to the Office of Management and Budget (OMB) in August 1998. In addition, subsequent to the submission of the plans to the OMB, it was determined that non-conformances exist at the U.S. Secret Service and Executive Office of Asset Forfeiture (EOAF) as well. The remediation plans are being developed by the Secret Service and EOAF. Finally, in the course of its FY 1998 financial statement audit work at the IRS, the GAO identified additional components in an existing material weakness tied to financial management (administrative) systems. The IRS is developing new corrective actions, which will be incorporated into the overall remediation plan
In the fall of 1998, the U.S. Mint successfully implemented its Consolidated Information System (COINS) as scheduled, effectively completing its remediation plan. The Department is closely monitoring all other remediation plans at the other five bureaus.

Summary of Open FMFIA Material Weaknesses and FFMIA Compliance
As of September 30, 1998

Bureau		**Number of Material Weaknesses for FMFIA Section 2**			**Number of material Instances of Non-Conformance for FMFIA Section 4**			**Substantial Compliance to FFMIA?**
	Grand Total	Carry over from Prior Years	New This Year	Total	Carry over from Prior Years	New This Year	Total	
ATF	**0**	0	0	0	0	0	0	Yes
BEP	**0**	0	0	0	0	0	0	Yes
BPD	**0**	0	0	0	0	0	0	Yes
CDFI	**0**	0	0	0	0	0	0	Yes
Customs	**8**	4	1	5	3	0	3	No
DO	**6**	0	6(net*)	6	0	0	0	Yes
DC Pension Funds	**4**	0	4	4	0	0	0	Yes
EOAF	**4**	0	0	0	0	4	4	No
FLETC	**1**	1	0	1	0	0	0	Yes
FMS	**17**	0	0	0	1	16(net*)	17	No
Treasury Franchise Fund	**0**	0	0	0	0	0	0	Yes
IRS	**15**	10	1	11	4	0	4	No
Mint	**2**	0	0	0	2	0	2	No
OCC	**0**	0	0	0	0	0	0	Yes
OTS	**0**	0	0	0	0	0	0	Yes
USSS	**3**	1	0	1	2	0	2	No
Total	**60**	**16**	**12(net*)**	**28**	**12**	**20 (net*)**	**32**	**[10] [6]**

Recap. Of Material Weaknesses (MWs):	Section 2	Section 4	Total
Balance at the Beginning of FY 98:	37	14	51
New MWs during the FY 98 *:	14	25	39
Closed during the FY 98*:	(23)	(7)	(30)
Balance at the End of FY 98:	28	32	60

* There were 7 MWs (2 for DO & 5 for FMS) opened and closed during the year.

SECTION 2 SUMMARY OF PENDING MATERIAL INTERNAL CONTROL WEAKNESSES AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
CUSTOMS (CS-93-01)	*There is a lack of control in Customs' in-bond program.*	*As of 10/28/98, all three parts of the "Tin Man" are operational including new on-line functions, new EDI In-bond capability, and automated random sampling for exams and post audit reviews. Customs will evaluate the effectiveness of the system as it becomes fully operational in FY 1999.*
CUSTOMS (CS-94-02)	*Inadequate Controls over Access to Sensitive Data Files; Lack of a Disaster Recovery Plan.*	*Short term action – through 9/99 – Based on Treasury decision, develop plans and costs for an emergency backup site at former IRS facility in Detroit, MI.* *Long Term – To Be Determined – Once funding has been established for a backup center, bring the backup center into operation and test critical recovery applications.*
CUSTOMS (CS-95-01)	*Inappropriate access to ADP files, inadequate control of emergency change process and inappropriate separation of duties.*	*Short term action – through 9/99 – Restrict programmer access to production programs; implement certification/ re-certification for TECS/SEACATS; transfer security functions and duties from TECS/SEACATS to AISSD.* *Long Term – 3/31/00 – Limit application programmer's access to programs and data files (ACS-DBCO); fully install Endeavor software to control changes in application software.*
CUSTOMS (CS-97-01)	*There is a lack of an enterprise information technology architecture.*	*Short term action – through 12/98 – After Treasury review of Phase II of the enterprise architecture, Phase III will be delivered.*
CUSTOMS (CS-98-01)	*Discrepancies exist in Customs Outbound Air Manifest Process.*	*Short term action – through 6/99 – After training and outreach, analyze reports from manifest reviews and post audits to identify continuing discrepancies; conduct a statistically valid national survey.*
DEPARTMENTAL OFFICES (DO-98-01)	*OASIA's financial management and reporting need improvement.*	*Short term action – through 1/99 – International Affairs work with FMS on verifying policies and procedures for reporting activities which FMS provided the accounting cross-services.* *After review of the financial statement, OASIA certifies completeness of the financial statement as it pertains to foreign loans.*

SECTION 2 SUMMARY OF PENDING MATERIAL INTERNAL CONTROL WEAKNESSES AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
DEPARTMENTAL OFFICES (DO-98-02)	***Management and reporting of IRS revenue collection and related activities need improvement.***	***Short term action – through 3/99 – Treasury DCFO's Office of Financial Systems Integration (FSI) is the focal point. Currently working with IRS on modification to its plan.*** ***FSI ensuring development of financial systems remediation plans, and Treasury DCFO's Office of Accounting and Internal Control (AIC) monitoring progress on specific corrective actions.***
DEPARTMENTAL OFFICES (DO-98-04)	***EDP general controls designed to safeguard data, protect computer application programs, prevent system software from unauthorized access, and ensure continued computer operations need to be strengthened at IRS, Customs, FMS, and ATF.***	***The Treasury's Chief Information Officer (CIO) has expanded oversight of bureaus on systems security issues to ensure that the corrective actions at each bureau are achieved in a timely manner.***
DEPARTMENTAL OFFICES (DO-98-06)	***Weaknesses in property management at IRS, FMS, Secret Service, and the Departmental Offices needs improvement.***	***A corrective action plan has not been received, but the FMFIA statement indicated completion in 1999. Departmental oversight has increased, and DO's material weakness has been downgraded. One material weakness at FMS was closed, and the other weakness (FMS-98-03) is expected to be resolved prior to the FY 99 audit. The weakness at IRS will be closed by mid-FY 1999.***
DEPARTMENTAL OFFICES (DO-98-07)	***Improved accountability and reporting over the Department's seizure and forfeiture activities are needed.***	***New management was installed in the EOAF and control processes are being evaluated and revamped as necessary.***
DEPARTMENTAL OFFICES (DO-98-08)	***Improved Compliance with the Federal Financial Management Improvement Act is needed.***	***Short term action – through 3/99 – AIC and FSI ensure that bureaus with noncompliant financial management systems have developed a comprehensive remediation plan meeting FFMIA requirements. Such plans for all relevant bureaus were delivered to OMB during August 1998.*** ***AIC and FSI will monitor progress under the remediation plans and ensure appropriate actions are taken if intermediate target dates are not met. Bureaus are reporting progress on a quarterly basis.*** ***AIC and FSI will compile financial systems remediation plans from IRS and other bureaus and forward them to OMB for review and evaluation.***

SECTION 2 SUMMARY OF PENDING MATERIAL INTERNAL CONTROL WEAKNESSES AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
DC Pension (DCP- 98-01)	*Treasury's overall administration of pension responsibilities needs improvement.*	*Plans are being developed.*
DC Pension (DCP-98-02)	*The financial reporting of pension assets needs improvement.*	*Plans are being developed.*
DC Pension (DCP- 98-03)	*Various improvements in benefits administration are needed.*	*Plans are being developed.*
DC Pension (DCP- 98-04)	*Information technology and Y2K compliance need improvement.*	*Plans are being developed.*
FEDERAL LAW ENFORCEMENT TRAINING CENTER (FLETC-91-01)	*An environmental problem exists at the FLETC Glynco, Georgia outdoor firearms ranges.*	*Short term action – through 12/01 – Complete the environment restoration of the area and reconstruction of the Outdoor Firearms Ranges through the FLETC's Remedial Plan.*
IRS (IRS-83-01)	*Property Management -- IRS has identified weaknesses in the procedures and control over the information, use and accountability of capitalized property.*	*Short term action – through 5/99 – The Senior Council for Management Controls (SCMC) will validate the effectiveness of the results indicator, determine that it has been achieved.*
IRS (IRS-96-02, 88-01)	*Tax Assessment Issues -- IRS needs to control access to the Examination Returns Controls System; The IRS' workload of Tax Assessments and prioritizing Collectible Assessments.*	*Short term action – through 1/99 – The SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.* *Long term action – through 12/00 – Roll out Inventory Delivery System (IDS) nationwide and the SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.*
IRS (IRS-94-03)	*A material weakness exists in the Internal Controls over Telecommunications Costs.*	*Short term action – through 3/99 – Implement new set of standardized Billing analysis Reporting Tool (BART) queries and quarterly BART reviews concentrating on Potential waste, fraud and abuse of Telecom resources, and the SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.*
IRS (IRS-95-02)	*Forms related to Tax-Exempt Bond issuances are not being processed.*	*Short term action – through 4/00 – Resolved entity and posting problems to Master File at Philadelphia Service Center, and the SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.*

SECTION 2 SUMMARY OF PENDING MATERIAL INTERNAL CONTROL WEAKNESSES AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
IRS (IRS-95-03)	***Tax Processing Systems need to be replaced.***	***Long term action – through 4/10 – IRS Commissioner requested that the legacy tax processing systems be replaced, and IRS has awarded the PRIME System Integration Services Contractor on 12/08/1998. Additionally, the IRS will implement the necessary processes required to manage Information Technology Investments consistent with the Software Engineering Institute's Software Development and Software Acquisition Capability Maturity Model (CMM) Level 3. Early implementation of CMM Level 3 process will focus on the model as it related to modernization activities with a phased approach for building organizational maturity.***
IRS (IRS-97-02, 97-03, 97-04, & 97-05)	***Security Issues -- IRS has identified various security issues with respect to the Computing Center, Service Centers and District Offices. Weaknesses were identified in the area of physical security, logical security, data communications management, risk analysis, quality assurance, internal audit and security, security awareness, and contingency planning.***	***Long term action – through 4/03 – The Office of Systems Standards and Evaluation is working with the district offices to mitigate their security weaknesses. The approach includes base lining the condition of security, and developing and implementing action plans to improve the district offices' continuity of operations plans, physical security, logical security, communications security, personnel and administration security, operating practices, and software quality assurance activities. The SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.***
IRS (IRS-98-01)	***Need to eliminate the Use of Business Statistics in the Services' Business Review and Performance in order not to impose or suggest quotas or goals or to evaluate enforcement officers and their immediate supervisors.***	***Short term action – through 6/99 – Conduct employee/NTEU briefings, revise Internal Revenue Manual (IRM) to reflect Restructuring and Reform Act of 1998, complete first independent review, and the SCMC will validate the effectiveness of the results indicator, determine that it has been achieved.***
UNITED STATES SECRET SERVICE (SS-97-01)	***No automated system for tracking real Property; "PAMS" has numerous errors; and reconciliations not performed.***	***Short term action – through 1/99 – Correct PAMS errors; research exception reports; and perform reconciliations.***

SECTION 4 SUMMARY OF PENDING MATERIAL INSTANCES OF NON-CONFORMANCE AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL NON-CONFORMANCES	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
CUSTOMS (CS-93-01)	Core Financial Systems do not provide complete and accurate information that could be used to prepare Customs Principal Statements.	Short term action – through 3/99 – Pilot the resource data warehouse; pilot an initial version of the accounts receivable subsidiary ledger. Long term action – through 9/05 – Establish an integrated financial system based on Automated Commercial Environment (ACE) development.
CUSTOMS (CS-93-02)	The Automated Systems and Manual Processes for Tracking and Accounting for Seized Property cannot be relied upon (SEACATS).	Short term action – through 9/99 – Automate the currency and property functions to generate a complete analysis of changes in seized and forfeited property.
CUSTOMS (CS-93-04)	Customs has problems with the integrity of data in its Fines, Penalties, and Forfeitures (FP&F) files.	Short term action – through 9/99 – In Phase II of SEACATS development, implement remaining case, financial, and reporting functions of SEACATS necessary for data integrity in FP&F files.
EXECUTIVE OFFICE OF ASSET FORFEITURE (AF-98-01)	U.S. Customs Service' Seized Assets and Case Tracking System (SEACATS) does not contain accurate and sufficient data that can be relied upon to prepare the analysis of changes in seized and forfeited property without substantial manual manipulation and reconciliation.	Short term action – through 9/99 – Work with Executive Agent, Customs, to ensure adequate control over the reporting of financial assets and to develop an effective internal control system.
EXECUTIVE OFFICE OF ASSET FORFEITURE (AF-98-02 & 98-03)	Accounting records are primarily maintained on a cash basis; The Fund's general ledger does not record all balances and transactions that are reflected in the financial statements.	Short term action – through 9/00 – Fund management has undertaken to deploy a single inventory system to support the three non-Customs bureaus participating in the Fund. Contracting for the deployment of IRS' AFTRAK system to support the change in inventory analysis requirements of the financial statements should be completed by the end of FY 2000. Long term action – through 9/01 – Fund management views that IRS' AFTRAK system be diversified and further deployed to the US Secret Service and the Bureau of Alcohol, Tobacco and Firearms to ensure their inventory is tracked in a manner that will support their individual changes in inventory analyses.
EXECUTIVE OFFICE OF ASSET FORFEITURE (AF-98-04)	Inadequate Accounting and Reporting of Seized and Forfeited Property Transactions exists.	Analysis of Changes in Seized and Forfeited Property of the IRS (Asset Forfeiture and Narcotics Section) compiled at year end did not account for and properly report property transactions for financial reporting purposes in accordance with Statement of Federal Financial Accounting Standards #3. Short term action – through 12/99 – Fund management will work closely with IRS to ensure that management issues related to AFTRAK are fully resolved.

SECTION 4 SUMMARY OF PENDING MATERIAL INSTANCES OF NON-CONFORMANCE AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL NON-CONFORMANCES	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
FMS (FMS-93-02)	There is a need for a more thorough utilization of existing security software protection for mainframe systems (ALERT).	Short term action – through 9/99 – Complete implementation of payment systems under CA-Top Secret as part of the conversion from VSE to MVS.
FMS (FMS-98-03)	Property transactions not posted monthly. FMS has had problems accurately accounting for its property, plant, and equipment. FMS has completed all other corrective actions for this weakness except this one. FMS has implemented a reconciliation procedure to reconcile the system data to the amount reported in the General Ledger to ensure that all property and equipment additions, deletions, and depreciation transactions are being posted monthly.	The FMS FY 98 Financial Statement audit revealed differences between the subsidiary and general ledgers as of year end. This condition is expected to be resolved before the FY 99 audit, and it remains an open material weakness as of FY 98 year end. Short term action – through 6/99 – FMS plans to validate the reconciliation procedure and test monthly reconciliation of property subsidiary ledger to general ledger.
FMS (FMS-98-06)	Inability to identify Intragovernmental Transactions - Financial Statement Audit	Short term action – through 4/99 – Review FY 98 FACTS data to investigate remaining differences between entities.
FMS (FMS-98-07)	Providing Methodology to Verify Net Cost Classifications - Financial Statement Audit	Short term action – through 9/99 – Identify and address other net cost issues in which financial reporting allocations differ from budget presentation.
FMS (FMS-98-08)	Inability to reconcile the CFS with the Budget Results - Financial Statement Audit	Short term action – through 9/99 – 1. Identify the information needed to reconcile the Change in Net Position with the budget deficit or surplus; 2. Determine the most effective method to reliably gather the information; and 3. Identify the additional reporting requirements and their impact. Long term action – through 1/01 – 1. Provide accounting guidance and training on how to implement the new requirements; 2. Develop a system (FACTS/Notes) to collect the data; and 3. Implement the system.

SECTION 4 SUMMARY OF PENDING MATERIAL INSTANCES OF NON-CONFORMANCE AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL NON-CONFORMANCES	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
FMS (FMS-98-09, 10, 13, 14, & 15)	General Control Weaknesses* Exist - in Computer Controls; Security Planning and Management; System Software, Physical and Segregation of Duties -(Access Controls) - EDP Controls.	* These individual weaknesses taken together create a "general control weakness" that is considered to be a material weakness. To ensure the correction of these individual weaknesses, FMS has assigned responsibility and accountability for correcting the specific individual weaknesses to designated persons who are required to report quarterly to the Commissioner on the status of the corrective actions. Short term action – through 12/99 – 1. Institute an entity-wide security management program which includes a comprehensive risk management program comprising a strong central security focal management point, periodic risk assessments, policy and controls implementation, promotion of computer control awareness, and evaluation and monitoring of policy and control effectiveness, and 2. Correct remaining corrective actions on the individual weaknesses identified during the GAO FY97 Financial Statement Audit.
FMS (FMS-98-12, 14, 16, 17, & 18)	CASHLINK System needs improvement in access controls and contingency planning.	Short term action – through 9/99 – Most of the individual weaknesses have been corrected and final two of the six remediation actions for the security planning and management are scheduled to be completed by 9/99.
FMS (FMS-98-20)	FMS needs to work with International Affairs on verifying policies and procedures for reporting activities which FMS provided the accounting cross-services.	(Transferred to the Department for actions in 12/99) Short term action – through 3/99 – The Assistant Secretary for International Affairs, with technical support from the Assistant Secretary for Management, will implement a proposal for financial reporting in accordance with generally accepted accounting principle.
FMS (FMS-98-21 & 22)	Treasury Receivable Accounting and Collection System (TRACS) balances need to be reconciled and the Miscellaneous Accounts needs a General Ledger Systems.	Short term action – through 9/99 – The development of standard operating procedures will be completed by 12/31/98 and the differences between STAR and TRACS will be reconciled. GLOWS, an off the shelf financial system has been implemented in 11/98.
IRS (IRS-93-01)	Management of Operating Funds: IRS' internal controls were not adequate to provide a reasonable basis for determining compliance with laws governing the use of budget authority or reasonable assurance that its disbursements were appropriate.	Short term action – through 1/00 – Implementation of Postage Budget Decentralization is to be completed by 10/99 and the Senior Council for Management Controls (SCMC) will validate the effectiveness of the results indicator and determine that it has been achieved.

SECTION 4 SUMMARY OF PENDING MATERIAL INSTANCES OF NON-CONFORMANCE AS OF SEPTEMBER 30, 1998

BUREAU	DESCRIPTION OF MATERIAL NON-CONFORMANCES	REMEDIAL ACTIONS AND KEY TARGET DATES FOR CORRECTION
IRS (IRS-94-01)	Erroneous Restricted Interest: Current system limitations require manual computations which results in a high number of erroneous assessments.	Short term action – through 1/00 – Decrease incorrect manual interest calculations/accruals and miscalculated TC 340 computations input. By 10/99, conduct field visitations to determine what extent erroneous manual restricted interest computations are still being made and determine an acceptable error rate, and by 1/00 the SCMC will validate the effectiveness of the results indicator and determine that it has been achieved.
IRS (IRS-94-02)	Duplicate Refunds/Manual Refunds: IRS' automated and manual refund systems are not adequately coordinated to prevent duplicate refunds.	Short term action – through 5/99 – Review programs and processes to ensure that it prevents duplication of MF/NMF manual refunds and prepare follow-up memorandum stating that controls are achieved.
IRS (IRS-95-01)	Financial Accounting of Revenue should provide detailed transactional data to support custodial financial reporting.	Long term action – through 1/09 – By 4/99 conduct Tax Type Fee/Code study; by 10/08 develop payment information data base and subsidiary ledger/Tax Account data base; and by 1/09 the SCMC will validate the effectiveness of the results indicator and determine that it has been achieved.
U.S. Mint (Mnt-93-02)	The Mint's Financial System comprises diverse mainframe, manual, and PC based systems.	Short term action – through 10/98 – The Consolidated Information System (COINS) is implemented as of 10/31/98, which closes this material non-conformance. No additional corrective actions are required.
U.S. Mint (Mnt-93-03)	Procedures for Data Consolidation from Non-General Ledger sources into Financial Statements are not documented.	Short term action – through 10/98 – The COINS is implemented as of 10/31/98, which closes this material non-conformance. No additional corrective actions are required.
U.S. SECRET SERVICE (SS-96-01)	Secret Service does not have reliable Seized Property Systems.	Short term action – through 10/99 – Conduct a physical inventory to establish values of seized assets as of 9/30/98; implement a new information system for storage and retrieval of information on seized property.
U.S. SECRET SERVICE (SS-97-02)	Material and supplies are not entered in the US Standard General Ledger.	Short term action – through 4/99 – Enter consumption of inventory and reimbursable transactions in the system.

SECTION 2 MATERIAL INTERNAL CONTROL WEAKNESSES OPENED AND CLOSED DURING FY 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	DESCRIPTION OF THE REMEDIAL ACTIONS
DEPARTMENTAL OFFICES (DO-98-05)	The process for distributing net tax revenue to various trust funds needs to be documented and improved.	This finding pertains to certain circumstances associated with the Office of Tax Analysis (OTA) and its management of trust funds. It was determined that the previous audit OIG-97-079 had addressed essentially identical findings and recommendations whose corrective actions had been completed.
DEPARTMENTAL OFFICES (DO-98-09)	IRS policies and procedures for certification of the distribution of Excise Tax Collections need to comply with the Internal Revenue Code.	This finding suggested that the Department ensure that the IRS develop an appropriate action plan for the related GAO recommendations and then monitor the IRS' efforts in implementing the plan. The Deputy CFO's Office of Accounting and Internal Control (AIC) ensured that such plans were developed and implemented. As a result, this finding and related recommendations were closed by the IRS, with the concurrence of the IRS' Senior Council for Management Control on 6/30/1998.

SECTION 4 MATERIAL INSTANCES OF NON-CONFORMANCE OPENED AND CLOSED DURING FY 1998

BUREAU	DESCRIPTION OF MATERIAL WEAKNESS	DESCRIPTION OF THE REMEDIAL ACTIONS
FMS (FMS-98-01, 98-02, & 98-04)	No itemized subsidiary records to support general ledger balance; Property custodians not adequately documenting write-offs, and Inadequate identification of excess or obsolete items.	FMS has completed all other corrective actions for this weakness except this one (See FMS-98-03 in the *Section 4 Summary of Pending Material Instances of Non-Conformance* above). FMS has implemented a reconciliation procedure to reconcile the system data to the amount reported in the General Ledger to ensure that all property and equipment additions, deletions, and depreciation transactions are being posted monthly.
FMS (FMS-98-05)	Providing consistency of CFS Information with Agency Audits. This material weakness is closed, pending validation.	The GAO audit of the FY 97 consolidated financial statements (CFS) of the US Government identified four material weaknesses pertaining to the preparation and accuracy of the CFS. These weaknesses impact the government's ability to (1) produce reliable CFS, and (2) perform the reconciliations needed to assure the reliability of CFS. One of the material weaknesses stated that it cannot ensure that information in the CFS is consistent with agency audited statements. During the FY 1998, the FMS has taken various corrective actions: It issued instructions to agencies for FACTS reporting including the due dates for submission of FACTS reports and final adjustments to Treasury; issued instructions to enhance and expand the FACTS verification process to facilitate CFS preparation; and provided ongoing support, assistance and training to agencies to ensure a successful verification process.
FMS (FMS-98-19)	An unclear reporting entity definition and inconsistent financial statement reporting practices exist for the Miscellaneous Accounts.	FMS has addressed audit recommendations by providing the Department the background and account information needed to move certain accounts to the Departments financial statements. In June 1998, the Department adopted a two year transition plan to implement these recommendations.

SUMMARY OF MANAGEMENT REPORT ON FINAL ACTIONS ON AUDIT RECOMMENDATIONS

Introduction

The Inspector General Act Amendments of 1988 (the Act), Public Law 101-504, requires that the Inspector General and the Secretaries of Executive Agencies and Departments submit semiannual reports to the Congress on actions taken on audit reports issued that identify potential benefits. Although the Treasury Office of the Inspector General (OIG) continues to issue its semiannual reports as standalone documents, beginning with this Accountability Report, the Department will discontinue producing the standalone Secretary's Semiannual Report to Congress and instead consolidate and annualize all relevant information and present it in each year's Accountability Report. This action is in accordance with provisions of the Government Management Reform Act, particularly as it pertains to the Governmentwide effort to streamline reporting.

Department-wide Management Control Program Activities

During FY 1998, several actions were taken to improve both the general administration of management control issues throughout the Department and the timeliness of the resolution of all findings and recommendations identified by the OIG. A new Assistant Director position within the DCFO organization was created, filled and assigned the responsibility of providing oversight on management controls on a Treasurywide basis. Various short term improvements were made to the Inventory Tracking and Closure System (ITCS), which is used for tracking all open audit findings, and the process for replacing the ITCS with a more modern system was set in motion. Departmental oversight of bureau management control program activities, as well as communication and coordination with the bureaus in general, was strengthened through a combination of: (1) on-site visits/reviews with bureau control personnel; (2) periodic management control program forums involving key persons from the OIG, all bureaus and program areas, and the Department; and (3) the establishment of a new Management Control Program Quarterly Report, which focuses on significant control issues throughout the organization and which is distributed to the Deputy Secretary, bureau heads, bureau CFOs and other key personnel. Finally, with respect to the resolution of recommendations in OIG reports that identify monetary benefits, the Department regularly reviews progress made by the bureaus in realizing those benefits, and coordinates with the OIG as necessary to ensure the consistency and integrity of information on monetary benefit recommendations being tracked.

Included in the summary figures are a number of factors which are generally grouped into three categories: Disallowed Costs, Better Used Funds, and Revenue Enhancements.

Disallowed Cost - It is a questioned cost that management has sustained, or has agreed would not be charged to the Government by a contractor.

Funds Put to Better Use - It is sometimes referred to as "Better Used Funds" which are amounts cited in an audit report recommendation which could, according to the audit report, be used more efficiently if management were to take actions to implement and complete the recommendation. Possible planned corrective actions which may be used to reallocate these funds more efficiently might involve reducing outlays to contractors or by avoiding unnecessary expenditures noted in pre-award reviews of contract agreements, or by avoiding costs with the implementation of recommended operational improvements. De-obligating funds from programs or operations that are not as

efficient or productive as they once were or planned them to be, as well as implementing any other savings which are specifically identified can also be classified as "Better Used Funds."

Revenue Enhancements - A revenue enhancement is an action recommended in an audit report which would, if implemented, enhance the General Fund receipts of the Federal Government without having any budgetary impact on any of the Treasury Department's appropriations. These revenue enhancements are a key element in the budgetary issues of the revenue collecting bureaus (IRS, ATF, USCS). If a bureau relies on the revenue collected for maintenance of those revenue producing areas, the revenue enhancements that are implemented can have a significant impact on the ability of these areas to operate efficiently while still providing the services that generate the revenue to the bureau.

Management Decision - The evaluation by management of the findings and recommendations included in an audit report and the issuance of a final decision concerning its response to such findings and recommendations, including actions considered to be necessary.

Report Summary and Highlights

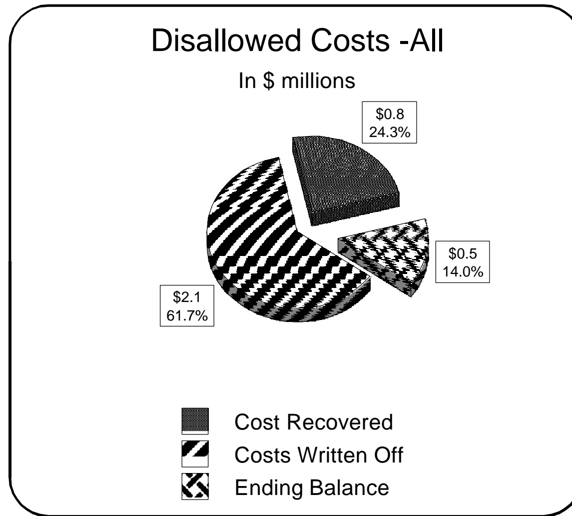
The statistical data in the following summary table and charts represents the Department's audit report activity for the period, October 1, 1997 through September 30, 1998. The data reflects information on reports that identified potential monetary benefits that were issued by the OIG, as well as those issued by the Internal Revenue Service's Office of the Chief Inspector.

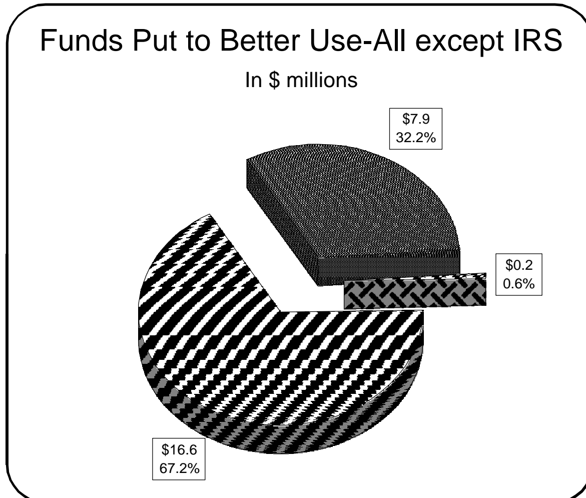
AUDIT REPORT ACTIVITY WITH POTENTIAL MONETARY BENEFITS
(OIG and IRS Chief Inspector)
October 1, 1997 through September 30, 1998
(Dollars in Millions)

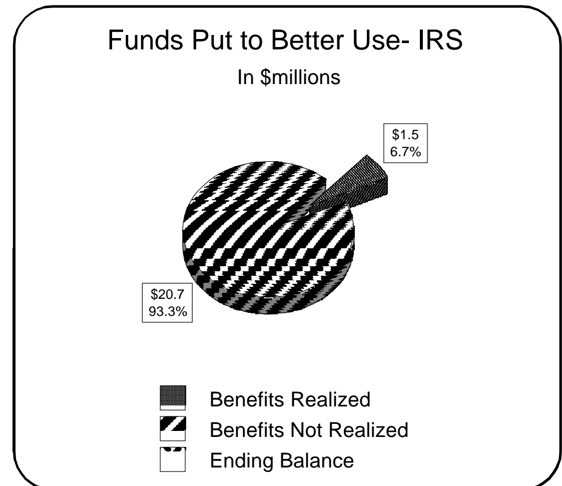
	Disallowed Costs		Better Used Funds		Revenue Enhancements		Total	
	Reports	Dollars	Reports	Dollars	Reports	Dollars	Reports	Dollars
Beginning Balance	3	$.5	4	$22.1	5	$83.7	12	$106.3
New Reports	15	2.9	18	24.8	5	47.3	38	75.0
Total Reports	18	3.4	22	46.9	10	131.0	50	181.3
Reports Closed	(15)	(2.9)	(21)	(46.7)	(9)	(118.6)	(45)	(168.2)
Ending Balance	**3**	**$.5**	**1**	**$.2**	**1**	**$12.4**	**5**	**$13.1**

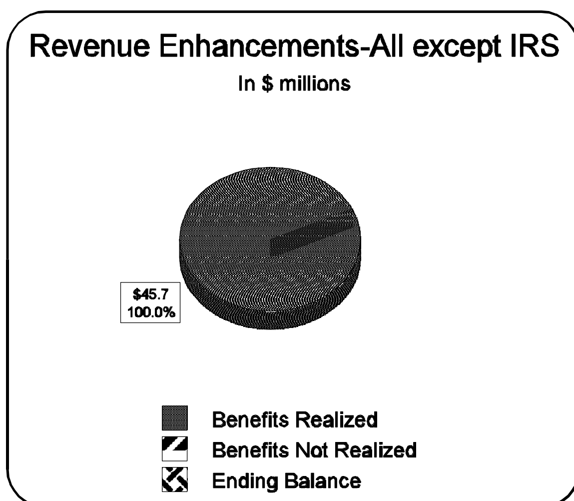
As shown, there were **thirteen** reports at the beginning of the period requiring action, with associated potential benefits of **$106.3 million**. **Thirty-eight** new reports were issued, with an associated dollar amount of **$75.0 million**. Final action was taken on **forty-five** reports during the period, with an associated dollar amount of **$168.2 million**, which left an ending balance of **five** reports and an associated dollar amount of **$13.1 million** still requiring management action.

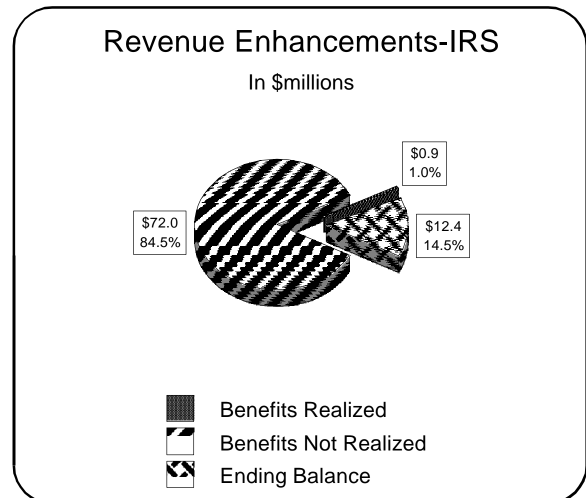
The following graphs present the summary data for FY 1998 for the three categories of *disallowed costs, better used funds,* and *revenue enhancements*.











Ending Balance - Supplemental Information

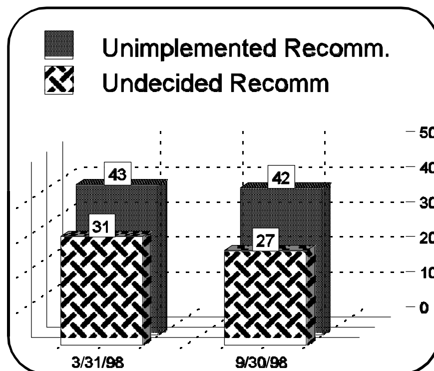
In addition to the $13.1 million ending balance of recommendations with monetary benefits which management has agreed to pursue, as of September 30, 1998, there were 27 OIG reports identifying $55.2 million in potential benefits, which have remained undecided by bureau management for more than six months. The Department is actively working with both the bureaus and the OIG to verify the continuing validity of the original recommendations and to ensure that, where appropriate, the bureaus remove the items from the undecided category and develop implementation action plans. The majority of the 27 reports are on contract audits and generally involve nominal amounts. Recommendations attendant to program audits at Customs (2 audits at $17.3 million) and ATF (2 audits at $27.1 million) comprise the majority of the outstanding potential benefits.

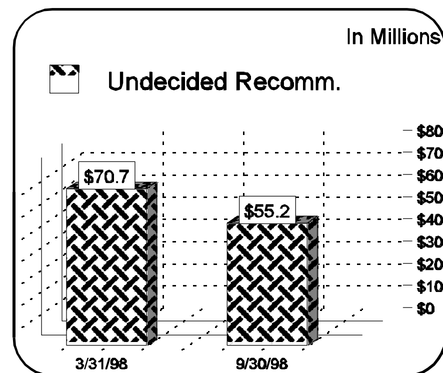
Undecided Audit Recommendations and Significant Unimplemented Recommendations

The number of Unimplemented Recommendations was 43 as of March 31, 1998. During the second half of FY 1998, ten audit reports have been resolved, but nine new reports were added to the list, ending with 42 as of September 30, 1998.

The Undecided Recommendations at the end of March 31, 1998 stood at 31 with monetary value of more than $70 million.

During the second half of the FY 1998, nine have been resolved, but five more were added, ending with 27 total Undecided Audit Recommendations for more than $55 million.





Department of the Treasury
Washington, D.C. 20220

Office of
Inspector General

March 25, 1999

MEMORANDUM FOR SECRETARY RUBIN

FROM: Richard B. Calahan
Deputy Inspector General

SUBJECT: Report on the Department of the Treasury's Fiscal Year 1998 Financial Statements

SUMMARY

Attached is our report on the Department of the Treasury's (the Department) Consolidated Balance Sheet as of September 30, 1998, and its Consolidated Statements of Changes in Net Position, Net Costs, and Custodial Activity, and its Combined Statements of Budgetary Resources and Financing for the year then ended (the "financial statements"). This audit is required by the Government Management Reform Act of 1994 (GMRA), which expanded the Chief Financial Officers Act of 1990 (CFO Act). These financial statements are incorporated in the accompanying *Department of the Treasury Accountability Report for Fiscal Year 1998*.

In accordance with generally accepted government auditing standards, the Report of the Office of Inspector General is dated March 3, 1999, the last date of audit field work.

DISCUSSION

Our report includes our qualified audit opinion on the financial statements. Our audit opinion was qualified because: (1) the Internal Revenue Service (IRS) was not able to provide sufficient evidence to support certain account balances in its financial statements, and (2) the Department did not eliminate certain intra-entity transactions in consolidation, as required by Federal accounting standards.

Our report discusses two material weaknesses and three other reportable conditions identified during our audit. The two material weaknesses relate to financial management and reporting at the IRS, and electronic data processing (EDP)

Page 2 - Secretary Rubin

general controls at certain bureaus. The other reportable conditions address financial management improvements needed at the Financial Management Service, Departmental Offices, and certain other component entities.

We noted three instances of noncompliance with applicable laws and regulations. The Department has reported that it is not in compliance with the Federal Financial Management Improvement Act of 1996. We concur with this assessment. Also, the IRS' installment agreements are not in compliance with the Internal Revenue Code. In addition, the United States Customs Service did not conduct a biennial review of reimbursable fees and charges, as required by the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended by the CFO Act.

The overall FY 1998 audit results clearly reflect the progress the Department has made during the past year in meeting its financial management objectives. All of the individual component entity audits resulted in unqualified opinions, except for the IRS. Also, significant improvements have been made in the internal control structures at certain of the Department's component entities. This resulted in significantly fewer material weaknesses reported in connection with the FY 1998 financial statement audits. Finally, for the most part, the Department was able to successfully implement significant new Federal accounting standards which became effective for FY 1998.

A key challenge for the Department as we move ahead to FY 1999 is to firmly address the continuing financial management and reporting issues at the IRS. This will require the strong commitment and direct involvement by IRS' executive management to develop and implement effective corrective action plans. The Department should continue to be actively engaged with the IRS in this effort.

The Department also should work closely with the other Treasury component entities to address remaining material weaknesses, other reportable conditions and non-compliances with laws and regulations. Resolution of these matters would enable accurate, useful and timely financial information throughout the year for informed decision making, in addition to facilitating successful annual audits.

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Finally, the Department should reconsider its elimination policy for intra-entity transactions, in order to conform with Federal accounting standards.

Your continued support is essential for the Department to build upon its recent accomplishments and meet the continuing challenges. We are committed to working with the Department to achieve its financial management goals.

In accordance with the Department of the Treasury Directive No. 40-01, we request a corrective action plan be provided to us within 30 days of the date of this memorandum. We recognize that certain corrective actions have already been undertaken. We encourage these efforts and will continue to provide advice and assistance to the Department during the implementation of the necessary improvements to its internal control structure.

Should you or your staff have questions, you may contact me at (202)927-5240 or a member of your staff may contact William H. Pugh, Deputy Assistant Inspector General for Audit (Financial Management), at (202)927-5430.

Attachment

cc: Nancy Killefer
Assistant Secretary for Management and Chief Financial Officer

REPORT ON THE DEPARTMENT OF THE TREASURY'S FISCAL YEAR 1998 FINANCIAL STATEMENTS

OIG-99-054 MARCH 25, 1999

Office of Inspector General

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United States Department of the Treasury

REPORT OF THE OFFICE OF INSPECTOR GENERAL

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To the Secretary of the Treasury

We audited the Department of the Treasury's (the Department) Consolidated Balance Sheet as of September 30, 1998, and the related Consolidated Statements of Net Cost, Changes in Net Position, and Custodial Activity, and the Combined Statements of Budgetary Resources and Financing, for the year then ended. These financial statements are incorporated in the accompanying *Department of the Treasury Accountability Report for Fiscal Year 1998 (FY 1998 Accountability Report).*

This report presents our qualified opinion on these financial statements. Our audit disclosed the following material weaknesses, as defined on page 6 of this report:

- Financial Management and Reporting at the Internal Revenue Service (IRS) Needs Improvement (Repeat Condition) (see page 6).

- Electronic Data Processing (EDP) General Controls Over Financial Systems Should be Strengthened (Repeat Condition) (see page 8).

In addition, our audit disclosed the following reportable instances of noncompliance with laws, regulations, and government-wide policies:

- IRS' installment agreements are not in compliance with section 6159 of the Internal Revenue Code (see page 15).

- The U.S. Customs Service (Customs) did not conduct a biennial review of fees and charges for its reimbursable projects as required by the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended (COBRA), and the Chief Financial Officers Act of 1990 (see page 15).

- The Department's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA) (Repeat Condition) (see page 16).

We considered these material weaknesses and instances of noncompliance in determining our audit procedures and in forming our opinion on whether the Department's fiscal year (FY) 1998 financial statements are presented fairly, in all material respects, in conformity with the accounting policies described in Note 1 to the financial statements. These weaknesses and

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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instances of noncompliance, other than those noted in the opinion section of this report, do not affect our opinion on these financial statements.

These findings, along with other reportable conditions, are described in more detail in the following sections of this report.

MANAGEMENT'S RESPONSIBILITIES

Management is responsible for:

- Preparing the financial statements in conformity with the hierarchy of Federal accounting standards, as described in Note 1 to the financial statements, which is a comprehensive basis of accounting other than generally accepted accounting principles.

- Preparing the Management Discussion and Analysis (MD&A) of the Department, Supplemental Information, and other accompanying information.

- Establishing and maintaining internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the benefits and related costs of internal accounting policies and procedures.

- Complying with laws, regulations, and government-wide requirements applicable to the Department.

SCOPE OF AUDIT

Except as discussed in the Opinion on the Financial Statements section of this report, we conducted our audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 98-08, *Audit Requirements for Federal Financial Statements,* as amended (OMB Bulletin No. 98-08). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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In planning and conducting our audit of the Department's financial statements for the year ended September 30, 1998, we considered its internal control over financial reporting and compliance with laws and regulations. Specifically, we obtained an understanding of the design of the Department's internal controls, determined whether these internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting and compliance with laws and regulations. Consequently, we do not provide an opinion on such controls.

In addition, with respect to internal controls related to performance measures reported in the MD&A, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions and determined whether they had been placed in operation. Our procedures were not designed to provide assurance on internal control over reported performance measures, and, accordingly, we do not provide an opinion on such controls.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Department's compliance with: (1) certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts; and (2) certain other laws and regulations specified in OMB Bulletin No. 98-08, including the requirements referred to in the FFMIA. Providing an opinion on compliance with laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

Under FFMIA, we are required to report whether the Department's financial management systems substantially comply with the following three general requirements: Federal Financial Management Systems Requirements (FFMSR), Federal accounting standards, and the United States Government Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance using the implementation guidance for FFMIA included in Appendix D of OMB Bulletin No. 98-08.

RESULTS OF AUDIT

OPINION ON THE FINANCIAL STATEMENTS

As discussed in Note 1 to the financial statements, the Department's financial statements were prepared in conformity with the hierarchy of Federal accounting standards prescribed in OMB Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, as amended (OMB

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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Bulletin No. 97-01), which is a comprehensive basis of accounting other than generally accepted accounting principles.

The scope of our audit was limited because, as described on page 6 of this report, IRS was unable to provide sufficient evidence to support: (1) non-payroll expenses reported in the Consolidated Statement of Net Cost related to Program B – Financial: Manage the Government's Finances, and (2) IRS related budgetary balances reported in the Combined Statements of Budgetary Resources and Financing.

In addition, the Department did not eliminate its investments in Federal debt securities and related earnings. These investments in Federal debt securities and related earnings represent intra-entity transactions that, in our opinion, should be eliminated in order to conform with the basis of accounting described in Note 1 to the financial statements. If these eliminations were performed, the Entity Intra-governmental Investments and Related Interest, and the Intragovernmental Federal Debt & Interest Payable in the Consolidated Balance Sheet would be reduced by approximately $17.1 billion. Also, earned revenues of approximately $900 million included in Net Cost of Treasury Operations would be eliminated against Federal Debt Interest Costs in the Consolidated Statement of Net Cost.

In our opinion, except for the effects of: (1) such adjustments, if any, as might have been determined to be necessary had we been able to examine evidence regarding IRS' non-payroll expenses and budgetary balances; and (2) not performing the eliminations as discussed in the preceding paragraph, the Department's financial statements present fairly, in all material respects, its assets, liabilities, and net position as of September 30, 1998, and its net costs, changes in net position, budgetary resources, reconciliation of net costs to budgetary obligations, and custodial activity for the year then ended, on the basis of accounting described in Note 1 to the financial statements.

As discussed in Note 1 to the financial statements, the presentation of the Department's FY 1998 financial statements differs from that of its FY 1997 statements. For FY 1997, the Department reported its administrative activities in a set of consolidated statements and its custodial activities in a set of consolidated schedules. For FY 1998, the Department is reporting all of its activities in a single set of financial statements. In addition, for FY 1998, the Department reclassified the International Assistance Programs to report them as part of its entity activities.

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OTHER INFORMATION

Our audit was conducted for the purpose of expressing an opinion on the Department's financial statements for the year ended September 30, 1998, referred to above. The information contained in the MD&A, and Supplemental Information, and other accompanying information, is not a required part of the financial statements but is required by OMB Bulletin No. 97-01. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it. However, we compared this information for consistency with the financial statements and, based on this limited work, we found no material inconsistencies.

INTERNAL CONTROL

Internal control is a process, effected by the Department's management and other personnel, designed to provide reasonable assurance that the following objectives are met:

- Reliability of financial reporting - transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements in accordance with the hierarchy of Federal accounting standards prescribed in OMB Bulletin No. 97-01, which is a comprehensive basis of accounting other than generally accepted accounting principles, and the safeguarding of assets against loss from unauthorized acquisition, use, or disposition;

- Compliance with applicable laws and regulations - transactions are executed in accordance with: (1) laws governing the use of budget authority and other laws and regulations that could have a direct and material effect on the financial statements, and (2) any other laws, regulations, and government-wide policy requirements identified in OMB Bulletin No.98-08; and

- Reliability of performance reporting - transactions and other data that support reported performance measures are properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management.

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

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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As defined in OMB Bulletin No. 98-08, reportable conditions are matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of the internal control, that could adversely affect the Department's ability to meet the internal control objectives as defined above. Material weaknesses are reportable conditions in which the design or operation of the internal control does not reduce to a relatively low level the risk that errors, fraud, or noncompliance in amounts that would be material in relation to the financial statements being audited or material to a performance measure or aggregation of related performance measures may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We identified the following matters involving the internal control and its operation that we consider to be material weaknesses and other reportable conditions as defined above. Material weaknesses and other reportable conditions that we identified in our *Report on the Department of the Treasury's Fiscal Year 1997 Custodial Schedules and Administrative Statements* (OIG-98-066, issued March 30, 1998), and that continued to exist during FY 1998, are identified as "Repeat Condition."

MATERIAL WEAKNESSES

Financial Management and Reporting at IRS Needs Improvement (Repeat Condition)

The audit of the IRS' FY 1998 financial statements disclosed that pervasive weaknesses continued to exist in the design and operation of the IRS' financial management and reporting systems, accounting procedures, documentation, record keeping, and internal control. These weaknesses prevented the IRS from reliably reporting on its administrative activities. Consequently, the IRS received disclaimers of opinion on its Statements of Net Cost, Changes in Net Position, Budgetary Resources, and Financing, and a qualified opinion on its Balance Sheet.

The IRS was able to report reliably on its FY 1998 custodial activities, including tax revenue received, tax refunds disbursed, and taxes receivable due from the public. This resulted in an unqualified opinion on its Statement of Custodial Activities. However, this achievement required extensive, costly, and time-consuming ad hoc procedures to overcome pervasive and long-standing internal control and systems weaknesses.

The material weaknesses reported at the IRS are summarized below:

- IRS did not have adequate control over its financial reporting process to provide reasonable assurance that its financial statements were fairly presented. Specifically, IRS':

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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(1) custodial and administrative general ledger systems which support the financial statements were not in conformance with the SGL at the transaction level and did not provide a complete audit trail for recorded transactions; (2) material balances reported on its financial statements related to administrative activities were not supported by sufficient evidence, including non-payroll expenses of $2.1 billion, fund balance with Treasury of $2.0 billion, undelivered orders of $1.0 billion, property and equipment (P&E) of $202 million, and accounts payable of $103 million; and (3) financial statements were not subject to sufficient management oversight to provide reasonable assurance that significant errors and omissions were identified and corrected before they were issued.

- IRS did not have a detailed listing, or subsidiary ledger, which tracks and accumulates unpaid assessments by taxpayer on an ongoing basis. Additionally, IRS continued to have significant problems locating supporting documentation for unpaid assessment transactions. However, improvement was noted in the documentation provided for the FY 1998 audit.

- IRS continued to have insufficient controls over refunds to ensure that inappropriate payments for tax refunds were not disbursed. In FY 1998, inappropriate refund payments were issued due to: (1) IRS comparing the information on tax returns and third party data such as W-2s (Wage and Tax Statement) too late to identify and correct discrepancies between these documents, (2) significant levels of invalid Earned Income Tax Credit (EITC) claims, (3) deficiencies in controls that allowed duplicate refunds to be issued, and (4) errors or delays in posting assessments to taxpayer accounts.

- IRS did not reconcile its administrative fund balance with Treasury account on a timely basis to central agency accounting records maintained by the Financial Management Service (FMS). After the fiscal year-end, IRS provided what it considered to be reconciliations for the 12 months of FY 1998. During testing of these reconciliations, it was found that material amounts on the reconciliations did not agree with FMS and IRS records. In addition, reconciling items listed on the reconciliations were not investigated and resolved. Without performing timely and thorough reconciliations, IRS had no assurance that its fund balance with Treasury was fairly stated. This weakness also has an impact on IRS' ability to ensure that it complies with laws governing the use of its budget authority.

- IRS could not ensure the completeness of its reported P&E balance because it did not have policies and procedures in place to ensure that all P&E purchases were identified and capitalized at the appropriate cost and all disposals were properly recorded. Audit testing identified computer system hardware and software projects that should have been capitalized but were not. In addition, significant property disposals were noted which were not reflected

REPORT OF THE OFFICE OF INSPECTOR GENERAL
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in IRS' detailed P&E records. IRS also did not record individual property transactions in its P&E general ledger account throughout the year. Instead, IRS recorded adjustments at year-end for all P&E activity for the year to make its P&E general ledger account agree with its P&E subsidiary records. Consequently, the general ledger did not contain the transaction detail information necessary to allow IRS to reconcile it to the detailed subsidiary records.

- Although IRS has made significant progress in improving its computer security, serious weaknesses continue to exist in the following functional areas: (1) entity-wide security program planning and management, (2) access control, (3) application software development and change controls, (4) system software, (5) segregation of duties, and (6) service continuity. Continued weaknesses in these areas could render IRS unable to perform its basic functions such as processing tax returns, maintaining sensitive taxpayer data, calculating interest and penalties, and generating refunds. These weaknesses could also result in unauthorized disclosure, modification, or destruction of taxpayer data.

Recommendations:

Recommendations to address the weaknesses discussed above will be issued in a supplemental report in connection with the audit of IRS' FY 1998 financial statements. Given the significance of these weaknesses to IRS' custodial and administrative responsibilities and their effect on the Department's financial statements, we recommend that, on behalf of the Deputy Secretary of the Treasury, the Assistant Secretary for Management and Chief Financial Officer ensure that IRS develops and implements an appropriate corrective action plan that will fully address the material weaknesses and reportable conditions identified in the FY 1998 IRS audit report.

EDP General Controls Over Financial Systems Should be Strengthened (Repeat Condition)

EDP general controls, which provide the structure, policies and procedures that apply to every computer operation within the Department, need to be strengthened at certain component entities. The details of the general control weaknesses and audit recommendations were, or will be, provided to the respective bureau's management separately, and in some instances, due to the sensitive nature of the weaknesses, in separate reports with limited official distribution.

EDP general controls cover a variety of areas, which are generally grouped into the following six categories: (1) entity wide security program planning and management, (2) access control, (3) application software development and change controls, (4) system software, (5) segregation of duties, and (6) service continuity.

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The entity-wide security program planning and management process provides for identifying and assessing risks, deciding what policies and controls are needed, periodically evaluating the effectiveness of these policies and controls, and acting to address any identified weaknesses. Access control weaknesses make systems vulnerable to damage and misuse by allowing individuals and groups to inappropriately modify, destroy, or disclose sensitive data or computer programs for purposes such as personal gain or sabotage. Application software development and change controls prevent unauthorized software programs or modifications to programs from being implemented. System software controls limit and monitor access to the powerful programs and sensitive files associated with the computer systems operation. Segregation of duties refers to the policies, procedures, and organizational structure that help ensure that one individual cannot independently control key aspects of a processor computer-related operation and thereby conduct unauthorized actions or gain unauthorized access to assets or records without detection. Service continuity controls ensure that when unexpected events occur, critical operations continue without undue interruption and critical and sensitive data are protected.

Although some improvements have been made, previously reported weaknesses in these general controls at certain bureaus continued to exist during FY 1998. Absence of effective general controls over computer based financial systems makes the Department vulnerable to losses, delays, or interruptions in service, and compromises the integrity and reliability of the information systems and data.

Recommendations:

In addition to the recommendations that were, or will be, provided to bureau management, we further recommend that the Department's Chief Information Officer develop a plan to ensure that the specific recommendations detailed in the above referenced reports, and the related plans for corrective actions are implemented completely and timely by the various bureaus.

REPORTABLE CONDITIONS

Continued Improvement in FMS Financial Management is Needed (Repeat Condition)

Our prior year audit disclosed that FMS did not report all of its operations and activities as a cohesive and complete reporting entity. Instead, FMS prepared separate sets of financial statements for: (1) its Salaries and Expense appropriation; and (2) the collection of approximately 150 accounts maintained by FMS related to international monetary programs, multilateral lending assistance, deposit funds, general fund receipt accounts, and certain other activities (collectively referred to as the Miscellaneous Accounts). This fragmented financial

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reporting inhibited a meaningful presentation of the full range and interrelationships of FMS' financial operations and activities, and increased the risk of material omissions from the financial statements.

FMS significantly improved its financial reporting for FY 1998 by: (1) identifying the Miscellaneous Accounts for which FMS had specific program responsibility, and (2) consolidating these accounts with its Salaries and Expense appropriation accounts into a single set of audited financial statements. For those Miscellaneous Accounts for which FMS provided accounting services but did not have program responsibility, FMS worked with the Department to identify the proper financial reporting entity within the Department. As a result of this effort, the Miscellaneous Accounts related to international monetary programs, multilateral lending assistance, and loans by the United States to foreign countries were reported for the first time in a separate set of financial statements.

Although financial reporting by FMS improved overall, our FY 1998 audit disclosed weaknesses in FMS' controls over property, and reconciliations of fund balances with Treasury. These conditions are discussed in more detail below:

- FMS implemented a new P&E subsidiary ledger system during FY 1998 but did not reconcile its detail property records to general ledger balances during the fiscal year. Additionally, manually-prepared depreciation schedules did not agree to the detail records of capitalized property in the subsidiary ledger. Monthly posting of all property transactions also did not occur. The effectiveness of FMS' controls to ensure property accountability and accurate financial reporting were further diminished because: (1) full physical inventories were not performed at all FMS locations, (2) physical inventory count sheets were not maintained for audit trail purposes, and (3) property balances were not updated to reflect the results of physical inventories.

- As one of its central banking functions on behalf of the Federal government, FMS maintains the Treasury Receivable Accounting and Collection System (TRACS). Among its other functions, this subsidiary ledger system accounts for reissued government checks sent to payees when payees report that initial checks were not received. Our prior year audit found that FMS had not reconciled fund balance with Treasury and accounts payable balances recorded in TRACS with FMS' accounting system for its central banking activities (STAR). During FY 1998, FMS made efforts to quantify the extent of the unreconciled differences related to prior periods, and segregated those differences from daily activity so that they could be reported separately in suspense and liability accounts. However, as of fiscal year-end, FMS had not resolved prior year differences and continued to have difficulty reconciling

the fund balance with Treasury in TRACS with that recorded in STAR for current year activity.

- FMS also did not properly reconcile fund balance with Treasury account balances reflected in its general ledger systems for the Salary and Expense appropriation accounts and certain Miscellaneous Accounts to central agency accounting records. Absent timely and proper reconciliations of fund balances with Treasury, FMS' financial accounting systems for its Salary and Expense appropriation and Miscellaneous Accounts may not include all financial activity that occurred, or there may have been activity that occurred and was not properly reflected in the central agency accounting records.

Recommendations:

Our separate report on FMS' FY 1998 financial statements includes specific recommendations to FMS management for correcting the conditions noted above. These recommendations will be tracked and monitored at the FMS level. We will also follow up on FMS' progress in implementing the recommendations as part of our audit of the Department's FY 1999 financial statements.

Financial Management at the Departmental Offices

Organized as a separate bureau within the Department, Departmental Offices (DO) is a collection of offices supporting the Secretary of the Treasury in policy formulation and implementation.

DO presently prepares financial statements that incorporate the DO Salaries and Expense appropriation as well as several other funds administered under the DO umbrella. However, these financial statements exclude certain activities under DO's purview; specifically, the activities of the International Assistance Programs (IAP), and the assets, liabilities and related activities resulting from the Department's assumption of responsibility for certain liabilities of the District of Columbia Pension System (DC Pension).

- IAP consists of international monetary programs, multilateral lending assistance, and loans by the United States to foreign countries managed by DO's Office of International Affairs (OIA). As mentioned in the previous finding, the first financial statements issued by OIA for these programs were for FY 1998. It relegated the preparation responsibility to FMS whose role was limited to providing IAP with accounting services.

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Because it is an economic policy making office, and unfamiliar with financial management issues, OIA had little or no involvement in: (1) making accounting policy decisions, (2) making adequate accounting estimates, including valuation of assets, (3) implementing effective internal controls over financial reporting, and (4) preparing informative financial statement disclosures. Considerable guidance had to be provided by the Department's Deputy Chief Financial Officer's office and the auditors to ensure OIA understood its financial management and reporting responsibilities over these programs.

- The Balanced Budget Act of 1997 (the 1997 Act) transferred to the Department: (1) the responsibility for pension benefits for certain employees of the District of Columbia (DC), and (2) certain assets of the plans. It also required that the Department hire a Trustee for the management, investment, control, and auditing of the DC Pension trust fund assets, the making of Federal benefit payments, and such other matters as the Secretary deems appropriate.

  Under the provisions of a Memorandum of Understanding (MOU) between the Department, DC, and the DC Retirement Board (DCRB), DC continues to administer the retirement programs and the DCRB continues to administer the retirement funds on behalf of the Department. The Secretary designated senior officials within DO to carry out the Department's responsibilities under the 1997 Act and the MOU.

  As with the IAPs above, the financial statements of DO did not include the accounts of the DC Pension. The Bureau of Public Debt (BPD), whose role was limited to providing DC Pension with accounting services, provided financial information directly to the Office of Accounting and Internal Control for inclusion in the Department's financial statements.

Not integrating financial management responsibilities with the management of program activities limits the effectiveness of program accounting and reporting functions and may result in incomplete or inconsistent financial reporting.

The DO financial statements also exclude certain other DO activities, such as the Federal Financing Bank, the Exchange Stabilization Fund, the Community Development Financial Institutions Fund, and the Treasury Forfeiture Fund (TFF). Audited financial statements related to these activities are issued separately because they are subject to stand-alone reporting requirements. However, there may be opportunities to incorporate them into a consolidating set of DO financial statements which would satisfy their separate reporting requirements.

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The presentation of DO activities needs to be reevaluated. Fragmented financial reporting inhibits a meaningful presentation of the full range and interrelationships of DO's program activities and financial operations and increases the risk of material omissions from the financial statements. Financial reporting by DO in a comprehensive set of financial statements would provide a more complete and informative presentation. This should include DO activities whose financial records are maintained by entities outside of DO. An additional benefit of this consolidation of DO's financial reporting would be opportunities to streamline the audit process.

Recommendations:

We recommend that the Assistant Secretary for Management and Chief Financial Officer:

1. Ensure that financial and program management responsibilities are properly integrated for all DO activities.

2. Reassess the DO reporting entity and consider presenting a comprehensive set of financial statements for DO which includes all program activities for which it has responsibility.

Financial Management at the Department's Component Entities Needs Improvement

Our audits of the component entities' FY 1998 financial statements identified continued weaknesses in various financial management areas of certain entities that affect their ability to produce accurate, reliable, and timely information. These weaknesses involved core financial systems, account reconciliations, seized and forfeited property activities, and the management of certain trade activities. To compensate for these conditions, the component entities had to perform extensive manual procedures and analyses to process certain routine transactions and to prepare financial statements and required disclosures as of the fiscal year-end. This, in turn, contributed to significant delays by certain component entities in providing the Department with reliable financial information for consolidation in the Department's financial statements.

These weaknesses are discussed below:

- Core financial systems at IRS, the U.S. Mint (the Mint), Customs, and TFF did not provide management with useful and timely information for managing operations. In each case these financial systems were not fully integrated. In addition, they did not capture all transactions as they occurred during the year, nor were the transactions properly recorded on a consistent basis.

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- IRS, FMS, and BPD did not perform certain essential account reconciliations. Specifically, reconciliations of fund balances with Treasury accounts to central agency accounting records maintained by the FMS were not always performed or were performed improperly. Additionally, detailed subsidiary ledgers for P&E were not always reconciled to the general ledger.

- Although significant improvement has been made to Custom's seized and forfeited property system, it was still unable to properly record all seized currency transactions during FY 1998. Also, required disclosures of seized and forfeited property activity were either incorrect or incomplete at IRS and the U.S. Secret Service (Secret Service).

- Customs' controls over in-bond shipments continued to need improvement during FY 1998. Customs was unable to ensure that goods moving in-bond were not diverted into the United States commerce without proper appraisement. While Customs did make certain planned improvements to its operating and system controls, these improvements were not fully implemented until September 1998.

The above conditions need to be addressed and corrected if the Department is to successfully accomplish planned improvements in its financial reporting process.

Recommendations:

The audit reports on the component entities' FY 1998 financial statements provided recommendations to address the weaknesses described above. In addition, we recommend that:

1. The Chief Information Officer should ensure that component entities develop appropriate plans to improve and integrate their financial management systems, and monitor the implementation of these plans.

2. The Assistant Secretary for Management and Chief Financial Officer should reiterate the Department's policy that essential account reconciliations be performed, reviewed by a supervisor on a regular and timely basis, and that reconciling items be investigated and resolved.

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Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

We noted other matters involving internal control and its operation that we will communicate to the Department's management separately.

COMPLIANCE WITH LAWS AND REGULATIONS

The results of our tests of compliance with laws, regulations, and government-wide policy requirements, exclusive of FFMIA, disclosed the following two instances of noncompliance with laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 98-08:

- Section 6159 of the Internal Revenue Code authorizes IRS to enter into installment agreements with taxpayers to satisfy the taxpayer's liability. During the FY 1998 audit, numerous instances were identified in which IRS had entered into installment agreements where the terms of payment will not be sufficient to satisfy the taxpayers' outstanding tax liability prior to the expiration of the statutory collection period for these tax liabilities. Because these agreements will not result in full satisfaction of the outstanding tax liability, they are not in compliance with Section 6159 of the Internal Revenue Code. IRS' management issued specific guidelines during 1998 requiring that the payments under any new installment agreement be adequate to satisfy the taxpayer's outstanding liability, and plans to update the Internal Revenue Manual.

- The Chief Financial Officers Act of 1990 requires Customs to conduct a biennial review to determine the appropriateness of fees and other charges it imposes for services and things of value it provides. Similarly, COBRA requires Customs to conduct a biennial review of user fees imposed under COBRA at the close of each even-numbered fiscal year. Customs did not conduct the biennial review of fees and charges for its reimbursable projects. However, it attempted to analyze COBRA fees based on FY 1997 data but the data was not complete and, as a result, it could not determine if fees should be adjusted.

Except for the instances described above, the results of our tests of compliance disclosed no other instances of noncompliance with other laws, regulations, and government-wide policy requirements, exclusive of FFMIA, that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 98-08.

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The results of our tests disclosed instances where the Department's financial management systems did not substantially comply with the requirements of FFMIA. In the Secretary of the Treasury's Letter of Assurance, included in Part III of the accompanying *FY 1998 Accountability Report*, the Secretary represented that the Department cannot provide an assurance that it is in substantial compliance with FFMIA.

The following are summaries of instances of noncompliance with the requirements of FFMIA that were identified during our tests and that the Department has included in Part III of the *FY 1998 Accountability Report* along with planned remedial actions and related time frames, where developed:

- IRS' custodial and administrative financial management systems: (1) do not allow for the reliable preparation of certain financial statements required by OMB Bulletin No. 97-01; (2) do not include a general ledger that conforms with the SGL; (3) lack subsidiary ledgers for unpaid assessments, accounts payable, and undelivered orders; and (4) lack an effective trail from the general ledger to the subsidiary detailed records and transaction source documents. In addition, IRS does not consistently capture cost information in accordance with Federal accounting standards. IRS has developed and is executing a remedial plan to address the weaknesses related to its custodial financial management systems. IRS is currently revising its remedial plan to address the weaknesses related to its administrative financial management systems.

- The Mint's core financial management system does not comply with OMB Circulars A-123, *Management Accountability and Control*; A-127, *Financial Management Systems*; and A-130, *Management of Federal Information Resources*, the FFMSR issued by the Joint Financial Management Improvement Program; and the SGL. Subsequent to the end of the fiscal year, the Mint implemented its Consolidated Information System. This system's compliance with the requirements of FFMIA and other OMB guidance will be assessed as part of the audit of the FY 1999 financial statements.

- Customs' financial systems do not provide complete and accurate information for financial reporting and the routine preparation of the financial statements and related disclosures in accordance with OMB Bulletin No. 97-01. In addition, Customs' automated systems for tracking and accounting for seized currency and property are not in compliance with FFMSR.

- Secret Service's automated system for valuing and accounting for seized property was not in compliance with the applicable requirements of FFMSR. In addition, the Secret Service did not enter materials and supplies transactions in its general ledger system as inventory was

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used, and reimbursable services are not recorded when goods or services are rendered or received.

- FMS' financial management systems had material weaknesses in EDP access controls over information security and contingency planning. Additionally, balances in TRACS needed to be reconciled. FMS also had weaknesses related to its responsibility to prepare the government-wide consolidated financial statements (CFS) required by the Government Management Reform Act of 1994 (GMRA). The weaknesses included the inability to identify and eliminate intragovernmental transactions and to reconcile the CFS with budget results, and the need to provide a methodology to verify net cost classifications.

- The Executive Office for Asset Forfeiture maintained its accounting records primarily on a cash basis and the general ledger system did not record all balances and transactions that are reflected in the financial statements of the TFF. Additionally, the analysis of changes in seized and forfeited property of the IRS compiled at fiscal year-end did not account for and properly report property transactions in accordance with Federal accounting standards.

- The material weakness regarding EDP general controls discussed on page 8 also constitutes non-compliance with FFMSR.

Recommendations:

The Assistant Secretary for Management and Chief Financial Officer should:

1. Ensure that the IRS develops and implements an appropriate corrective action plan to address recommendation(s) related to the IRS' noncompliance with Section 6159 of the Internal Revenue Code.

2. Ensure that Customs continues its efforts to review its user fees and other charges to comply with the Chief Financial Officers Act of 1990 and COBRA.

3. Continue to monitor and assess the progress of the bureaus in developing and implementing their remediation plans to address the identified instances of financial management systems noncompliance with the requirements of FFMIA, and in taking appropriate actions when key target dates are not met.

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OTHER OBSERVATIONS

In addition to the matters discussed above, we would like to offer the following observations with regard to strengthening financial management at Treasury and facilitating financial reporting in the future.

Treasury Corporate Financial Management

The requirement under GMRA for consolidated Department-wide financial reporting underscores the need and importance of strong corporate financial management at the Department. The utility of the Department's consolidated financial information is dependent upon the accuracy, consistency, timeliness and relevance of financial information provided by the bureaus. This in turn requires that the Department exert its corporate prerogative over financial management activities throughout the Department.

The Department has already taken significant actions in this regard. The Treasury Chief Financial Officer's Council, comprised of all Chief Financial Officer's and their Deputies within the Department, has been an active and positive vehicle for addressing financial management issues in a Department-wide context. Also, the Department's decision to submit an annual Accountability Report, which it has done since FY 1995 under a pilot program authorized by the GMRA, is a good indicator of its corporate financial management perspective. These and other initiatives aimed at strengthening the Department's corporate financial management function need to be continued and accelerated.

In addition, the Department should focus particular efforts on engaging top level bureau management to address key financial management issues affecting the integrity of their financial reporting. A prime example of this need is at the IRS. The continuing material weaknesses in internal control, which have been reported since financial statement audits were initiated in FY 1992, coupled with significant IRS management turnover and new Federal accounting standards, resulted in a disclaimer of an audit opinion on certain of the IRS FY 1998 financial statements. This in turn resulted in a qualified audit opinion on the Department's financial statements.

The "tone at the top" is a fundamental concept of management accountability. A direct commitment and involvement by top executive management is needed to focus attention and priority on critical issues facing an organization. Addressing pervasive financial management issues requires the active involvement of the chief executive and program operating heads, as well as the chief financial officer. The Department can in fact cite major financial management successes at certain bureaus in this regard. Customs and the Bureau of Alcohol, Tobacco and

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Firearms (ATF), along with IRS, were designated by OMB under the GMRA for stand-alone audited financial statements. Customs and ATF have established strong records of financial accountability with unqualified audit opinions since FY 1996. In both cases, the direct involvement of the agency head and top program managers in promoting and supporting financial accountability throughout their organizations, and their direct participation in the financial statement preparation and audit process, have been instrumental in achieving the desired audit results. Likewise, IRS would benefit substantially from a more active involvement by executive management in addressing financial management issues. The Department should actively seek to fully engage IRS executive management in this effort.

The Department is also encouraged to build upon its corporate financial management initiatives in other areas, such as financial management resource issues at the bureaus. The Department already plays a significant role in this regard in its capacity as principal advisor to the bureaus on management issues. Also, the Department has undertaken a major project to develop a streamlined Department-wide human resources system. Another key area where the Department can strengthen bureau financial management is by working closely with the bureaus to ensure that key financial management vacancies are filled on a timely basis with highly qualified financial managers. During the past year, for example, key permanent financial management positions at the IRS, Customs and FMS were open for extended periods. Active involvement by the Department in assessing qualitative and quantitative factors related to bureau accounting staffing levels would also enhance overall financial management across the Department.

Future Financial Statement Preparation

The Department made significant enhancements to its process for preparing its financial statements. These enhancements enabled more efficient identification and reconciliation of account balances and transactions necessary for the preparation of its FY 1998 financial statements. The Department also improved the accuracy and presentation of the financial statement data submitted by its component entities for consolidation.

Since the preparation of the FY 1995 Accountability Report, the Department has made strides towards submitting its audited financial statements on a timely basis. However, this is a continuing challenge, due in large part to the difficulty of its component entities in producing reliable and accurate financial information in a timely manner.

In an effort to improve this situation, the Department has developed the Financial Analysis and Reporting System (FARS), which serves as a centralized data source for its financial data. This system will receive and store in a data base monthly transmissions of trial balance information

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from each of the Department's component entities. This should allow the Department to prepare periodic consolidated financial statements for the Department during the year and should also expedite the preparation of the fiscal year-end consolidated financial statements.

While the implementation of FARS should enhance the Department's ability to generate timely financial information, the utility of this information depends on the integrity of the data. The financial information generated from FARS will only be as good as the component entity information that goes into the data base.

The Department should ensure that all of its component entities have financial management systems which are capable of producing accurate, timely, and reliable financial information throughout the year, not just at fiscal year-end. It should also consider extending the use of FARS to prepare the component entities' financial statements. Subject to the integrity of the data provided, these potential enhancements would enable the component entities to support interim audit tests of data, thus allowing for more timely completion of the audits of their annual financial statements, as well as those of the Department.

Application of Federal Accounting Standards

The Department manages significant assets (e.g., operating cash of the Federal government, taxes receivable, and gold and silver reserves) and liabilities (the Federal debt) on behalf of the Federal government. There are anomalies in the Federal accounting standards which create unique financial reporting issues for the Department with respect to the activities that it performs on behalf of the Federal government. In particular, the standards require separate reporting of entity and non-entity assets. Non-entity assets are defined as those that are held by an entity but not available to it. However, the standards do not provide for such a separation in reporting liabilities.

The standards also require that an amount equal to non-entity assets should be recognized as a liability. The Department obtained authorization from OMB to report an asset, due from the general fund, to offset the liabilities managed on behalf of the Federal government. These offsetting accounts result in a net due from the general fund, which is presented as a non-entity asset in the Department's FY 1998 Consolidated Balance Sheet.

The inconsistency in accounting and reporting for entity and non-entity with respect to assets versus liabilities affects the manner in which related balances are treated in consolidation, since entity and non-entity accounts are not eliminated against each other. It also raises questions as to whether the offsetting accounts with the general fund should be classified as entity or non-entity.

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We consulted with OMB regarding the appropriate accounting treatment under Federal accounting standards for activities performed by the Department on behalf of the Federal government. Except for the Department's investments in Federal debt securities and related earnings referred to in our audit opinion on page 3 of this report, transactions and balances related to activities performed on behalf of the Federal government are presented in accordance with agreements reached with OMB for FY 1998 reporting.

Although these issues were settled for FY 1998, a permanent resolution is needed to address inconsistencies in the present Federal accounting standards to make the financial statements of future reporting periods more clear and useful to readers. We are prepared to assist the Department in working with OMB and the Federal Accounting Standards Advisory Board to address these matters in a more comprehensive manner.

MANAGEMENT'S RESPONSE AND AUDITOR'S COMMENTS

Management agrees in principle with the findings in this report except for the qualification to our opinion on the financial statements related to the elimination of the Department's investments in Federal debt securities and related earnings. Management believes that these investments and related earnings should not be eliminated because it would result in incomplete reporting of its total activities. Management also believes that presenting this information in the principal financial statements improves the utility of the statements. A copy of the full text of Management's Response follows our report in this section of the FY 1998 *Accountability Report*.

The nature and complexity of the Treasury Department's activities create unique financial reporting challenges under Federal accounting standards. During our audit, the elimination policy for intra-Departmental transactions was discussed on numerous occasions at our regular meetings with representatives of the Department's Chief Financial Officer (CFO) and at the monthly audit status meetings with CFO staff and representatives of the General Accounting Office (GAO). Plausible arguments were made at these meetings to support differing views on the appropriate policy for intra-Departmental eliminations.

Accounting policies followed by Federal agencies must be within the framework of the hierarchy of Federal accounting standards prescribed in OMB Bulletin No. 97-01. Significant disagreements as to whether an agency's accounting policies meet this criterion should be resolved with OMB, which is the policy setter for the form and content of Federal financial statements. Accordingly, we consulted with OMB to resolve certain accounting issues, including the appropriate elimination policy for intra-Departmental transactions. Pursuant to considerable discussion with OMB involving our representatives, and representatives of the CFO and GAO,

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OMB confirmed that the Department's investments in Federal debt securities and related earnings should be eliminated from its financial statements.

Based on the results of our consultation with OMB, we reaffirm that the Department's elimination policy with respect to its investments in Federal debt securities and related earnings constitutes a departure from Federal accounting standards. We advise the Department to reconsider its elimination policy for future reporting periods.

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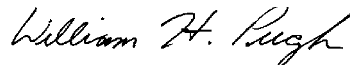
This report is intended solely for the information and use of the management of the Department of the Treasury, OMB, the U.S. General Accounting Office, and the Congress, and is not intended to be and should not be used by anyone other than these specified parties.



William H. Pugh
Deputy Assistant Inspector General for Audit
(Financial Management)
March 3, 1999

DEPARTMENT OF THE TREASURY
Washington, D.C.

Assistant Secretary

March 1999

MEMORANDUM FOR DAVID WILLIAMS
INSPECTOR GENERAL

FROM: Nancy Killefer
Assistant Secretary for Management
and Chief Financial Officer

SUBJECT: Management Response -- Report of the Inspector General on Treasury's Fiscal Year 1998 Financial Statements

This is in response to your report to Secretary Rubin on the Department's financial statements included in Treasury's fiscal year 1998 Accountability Report.

We appreciate your efforts to audit the Department's fiscal year 1998 financial statements. You identified two material weaknesses in your audit: Financial Management and Reporting at IRS Needs Improvement; and, EDP General Controls Over Financial Systems Should be Strengthened. My office, along with the Deputy Chief Financial Officer and the Chief Information Officer, will review and monitor the planned corrective actions of the affected bureaus to help ensure that these weaknesses are eliminated.

As you know, we still face a significant challenge in meeting the statutory due date of March 1 for completion of Treasury's Accountability Report. Working together, our offices need to establish and commit to a plan for the timely preparation and audit of the financial statements for fiscal year 1999.

Treasury has many successful financial management accomplishments to note for fiscal year 1998. Unfortunately, they are to a large extent overshadowed by the overall qualified opinion rendered. As you know, we are developing action plans to obtain more favorable results for fiscal year 1999.

Overall, I agree in principle with the findings in your audit report, except for one. In particular, I agree with your observation for Departmental Offices to consider presenting a comprehensive set of financial statements inclusive of all program activities subject to a single audit. However, I must take exception with the qualification in your audit opinion regarding the Department's elimination policy for entity investments in Federal debt securities.

As you know, the Department of the Treasury is a complex organization that has many roles and responsibilities that are conducted at three distinct levels -- Treasury Bureau, Treasurywide, and Treasury on behalf of the federal Government. As described in Note 1 to the financial statements, we explain this situation and the fact that the Department often engages in certain transactions between its entity and its non-entity activities. The Department does not eliminate these transactions for consolidation purposes, because the activities are viewed as separate and unique. If these transactions were eliminated, the Department's financial statements would not be complete in terms of reporting its total entity related activities and those non-entity related

activities carried out on behalf of the Federal Government. Also, our policy of not eliminating the entity investments in Federal debt securities in consistent with our policy of not eliminating between non-entity assets and entity liabilities.

The Department firmly believes that its policy not to eliminate these transactions follows, and is well within the flexibilities of, the guidelines provided in the Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, Entity and Display. SFFAC No. 2, paragraph 77 states, "In reporting the transactions and balances of a federal reporting entity in its entirety, it is conceptually desirable, although not always practicable to eliminate the intra-entity transactions and balances. *Factors to consider are the utility of the information for the entity in its entirety if the intra-entity balances are not eliminated*, the misunderstanding that might result if the balances are not eliminated, and the cost-benefit of making the eliminations (emphasis added)." As described above, the Department thinks its policy improves the utility of the information presented for both internal decision makers and the external, taxpayer audience.

Further, as noted in your audit report, we agree strongly that there are anomalies in the Federal accounting standards which create unique financial reporting issues for the Department. Certain provisions of OMB Bulletin 97-01, Form and Content of Financial Statements, also create unique reporting issues. With your office's participation, we actually began considering these reporting issues with the enactment of the Government Management and Reform Act in 1994. Since we produced the initial Departmentwide financial statements for fiscal year 1995, each subsequent year's statements have been revised to reflect both changing reporting standards and changing views as to how certain accounts, particularly those that present Treasury's governmentwide activities, were presented in our statements.

One of our main goals in establishing the Department's financial statements work group last year was to reach agreement among the various interested parties on how to present the Department's statements both for fiscal year 1998 and the foreseeable future. It is our view that the work group's efforts, which culminated in the presentation format approved by OMB in August 1998 and followed by the Department in preparing its fiscal year 1998 financial statements, have effectively addressed the Department's statement presentation issues.

We think our current reporting format provides readers with a clear and informative understanding of both the Department's "operating entity" and "governmentwide" financial activities. Accordingly, we do not anticipate re-visiting these issues in a wholesale manner for fiscal year 1999 or future years. Of course, we agree with you that existing Federal accounting standards have room for improvement, especially as they relate to entity and non-entity types of accounts. If the Federal Accounting Standards Advisory Board chooses to consider amending any of the existing standards, we would be pleased to provide our views and testimony directly to the Board.

I look forward to working with you and your office to address all of the Department's financial statement preparation and audit issues for fiscal year 1999.

SUPPLEMENTAL INFORMATION

INTRODUCTION

This section provides the Required Supplemental Information described in the Office of Management and Budget Bulletin 97-01, *Form and Content of Agency Financial Statements*, and also includes Other Accompanying Information and the Required Stewardship Supplemental Information, which provide additional financial information. Other program and financial information also are presented: Prompt Payment Act compliance; progress and status on the implementation of the Debt Collection Improvement Act of 1996; and the biennial review of user fees. This section also includes an abbreviated performance report for fiscal year 1998 on the results of selected key performance measures, as presented in Treasury's FY 2000 Budget-In-Brief dated February 1999.

SUPPLEMENTAL INFORMATION TO FINANCIAL STATEMENTS

Note A. Segment Information

Franchise Fund

The Department of Treasury's Franchise Fund is a fee-for-service organization that is fully reimbursable and competitive. The fund currently consists of six business activities - the Center for Applied Financial Management, the Federal Quality Consulting Group, and four former Cooperative Administrative Support Units (CASU) now operating as Treasury Franchise Businesses.

The Center for Applied Financial Management improves the quality of Government financial management by providing individualized accounting cross-servicing, financial systems consulting, financial management consulting, and financial education services.

Some of the major customers include: Administrative Offices of the U.S. Courts, Bureau of Indian Affairs, Defense Finance and Accounting Service, Library of Congress, U.S. Senate and various other Executive department's and agencies.

Treasury Franchise Fund
Segment Information
(Millions)

	Amounts
Fund Balance with Treasury	$ 10
Accounts Receivable	17
Property, Plant and equipment	1
Other Assets	0
Total Assets	28
Accounts Payable	18
Other Liabilities	3
Total Liabilities	21
Cumulative Results of Operations	7
Total Liabilities and Net Position	28
Total Costs	79
Exchange Revenue	80
Other Financing Sources	2
Excess of Revenues and Financing Sources over Costs	3

Working Capital Fund

The Departmental Office's Working Capital Fund is a fee-for-service organization that is fully reimbursable and competitive.

The fund presently offers the following program services to various Treasury bureaus: telecommunications, payroll/personnel systems, printing and other.

Working Capital Fund
Segment Information
(Millions)

	Amounts
Fund Balance with Treasury	$ 237
Accounts Receivable	15
Property, Plant and equipment	2
Other Assets	2
Total Assets	256
Accounts Payable	29
Other Liabilities	227
Total Liabilities	256
Cumulative Results of Operations	0
Total Liabilities and Net Position	$ 256
Total Costs	$ 191
Exchange Revenue	191
Other Financing Sources	0
Excess of Revenues and Financing Sources over Costs	$ 0

Note B. Other Claims for Refunds and Drawbacks

The Department has estimated that $24.7 billion which may be paid out as other claims for tax refunds and drawbacks. This estimate represents amounts (principal and interest) that may be paid for claims pending judicial review by the Federal courts or internally. The total estimated payout (including principal and interest) for claims pending judicial review by the Federal courts is $9.8 billion and by Appeals is $14.9 billion. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5 for reporting the amounts in the Balance Sheet or for disclosure in the notes to the financial statements. However, they meet the criteria in SFFAS No. 7 for inclusion as supplemental information.

Note C. Unpaid Assessments

In accordance with SFFAS No. 7, some unpaid tax assessments do not meet the criteria for financial statement recognition as discussed in the Note 1 to the financial statements. Although compliance assessments and write-offs are not considered receivables under Federal accounting standards, they represent legally enforceable claims of the Federal government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

The components of the total unpaid assessments at September 30, 1998 were as follows:

Treasury Unpaid Assessments (Millions)	Amount
Gross Unpaid Assessments	$ 222,000
Less Compliance Assessments Written Off	$ (141,000)

* *This consolidating file has been modified to include only the gross unpaid assessments and compliance write-offs. The amounts provided do not include data provided by Customs. Please see the write-up below on Customs' business practices in relation to this note disclosure.*

To eliminate double counting, the compliance assessments reported above exclude trust fund recovery penalties, totaling $15 billion, assessed against officers and directors of businesses who were involved in the non-remittance of federal taxes withheld from their employees. The related unpaid assessments of those businesses are reported as taxes receivable or write-offs, but the Department may also recover portions of those businesses' unpaid assessments from any and all individual officers and directors against whom a trust fund recovery penalty is assessed.

U. S. Customs Service (Customs)

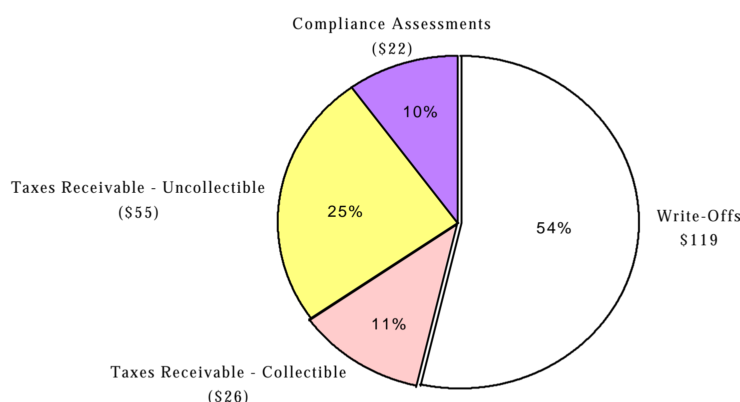
Customs reviews selected documents to ensure all duties, taxes, and fees owed to the Federal government are paid and to ensure regulations are followed. If Customs believes duties, taxes, fees, fines, or penalties are due in addition to estimated amounts previously paid by the importer/violator, the importer/violator is notified of the additional amount due. Customs regulations allow the importer/violator to file a protest on the additional amount due for review by the Port Director. A protest allows the importer/violator the opportunity to submit additional documentation supporting their claim of a lower amount due or to cancel the additional amount due in its entirety. Work in progress will continue until all avenues to file a protest have expired or an agreement is reached. During this protest period, Customs does not have a legal right to the importer/violator's assets, and consequently, Customs recognizes accounts receivable only when the protest period has expired or an agreement is reached. For Fiscal Year 1998, Customs had a legal right to collect $871 million of receivables. In addition, there is an additional $1.2 billion representing records still in the protest phase.

Internal Revenue Service (IRS)

The unpaid tax assessments balance was about $222 billion as of September 30, 1998. This unpaid assessments balance represents assessments resulting from taxpayers filing returns without sufficient payment; as well as from the Service's enforcement programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. A significant portion of this balance is not considered a receivable. Also, a substantial portion of the amounts considered receivables is largely uncollectible.

Under Federal accounting standards, unpaid assessments require taxpayer or court agreement to be considered Federal taxes receivable. Assessments not agreed to by taxpayers or the courts are considered compliance assessments and are not considered Federal taxes receivable. Assessments with little or no future collection potential are called write-offs.

Of the $222 billion balance of unpaid assessments, $119 billion represents write-offs. Write-offs principally consist of amounts owed by deceased, bankrupt or defunct taxpayer's, including many failed financial institutions liquidated by the Federal Deposit Insurance Corporation (FDIC) and the former Resolution Trust Corporation (RTC). As noted above, write-offs have little or no future collection potential, but statutory provisions require that these assessments be maintained until the statute for collection expires. In addition, $22 billion of the unpaid assessments balance represents amounts that have not been agreed to by either the taxpayer or a court. Due to the lack of agreement, these compliance assessments are less likely to have future collection potential than those unpaid assessments that are considered Federal taxes receivable.



Note D. Heritage/Stewardship Property Plant and Equipment

These assets include the Treasury Department building and the Treasury Annex building. The Department also has four multi-use heritage assets located in Puerto Rico.

Treasury
Heritage Assets, Stewardship Land

(Units - Actual)	Heritage Assets	Stewardship Land	Federal Mission PP&E
Beginning Balance	5	1	0
Additions	0	0	0
Withdrawals	0	0	0
Ending Balance	5	1	0

Note E. Statement of Budgetary Resources Dis-aggregated by Major Accounts

The following table represents a dis-aggregation of The Department of the Treasury's major budget accounts, which are aggregated in the Statement of Budgetary Resources.

Treasury
Statement of Budgetary Resources by Major Accounts
(MILLIONS)
As of September 30, 1998

Budgetary Resources	Appropriated Funds	Revolving Funds	Trust Funds	Other Fund Types	Total
Budget Authority	$385,131	$3,091	$4,243	$632	$393,097
Unobligated Balance	13,464	28,053	65	953	42,535
Spending Authority from Offsetting Collections Earned	537	8,169	526	43	9,275
Adjustments, Anticipated for Rest of Year	303	12	2	12	329
Total Budgetary Resources	399,435	39,325	4,836	1,640	445,236
Status of Budgetary Resources					
Obligations Incurred	385,839	10,076	924	675	397,514
Unobligated Balances Available	13,425	29,238	3,910	325	46,898
Unobligated Balances Not Available	171	11	2	640	824
Total Budgetary Resources	399,435	39,325	4,836	1,640	445,236
Outlays					
Obligations	385,839	10,076	924	675	397,514
Spending Authority from Offsetting Collections and Adjustments	(968)	(8,181)	(529)	(54)	(9,732)
Obligated Balance, Net-Beginning of the Period	6,721	1,302	289	197	8,509
Obligated Balance Transferred, Net	0	(115)	0	0	(115)
Obligated Balance, Net-End of Period	(7,346)	(671)	(357)	(254)	(8,628)
Total Outlays	$384,246	$2,411	$327	$564	$387,548

Other Accompanying Information

A. Tax Burden

The Internal Revenue Code provides progressive rates of tax, whereby higher incomes generally result in higher rates of tax. The chart below illustrates the latest available information on the income tax and related income, deductions, exemptions, and credits for individuals by income level and corporations by total assets.

Individual Income Tax Returns

(Tax Year 1996 data)

	Size of Adjusted Gross Income (in thousands)					
	< $15	$15 to $30	$30 to $50	$50 to $100	$100 to $200	> $200
Total Returns	42,673,765	29,547,114	22,116,289	20,160,813	4,612,244	1,524,048
Taxable Income (in thousands)	$60,751,843	$322,967,109	$558,587,366	$976,861,175	$468,615,932	$712,936,340
Total Tax Liability (in thousands)	$10,726,679	$48,648,432	$93,949,993	$186,713,424	$115,008,844	$234,221,163
Tax Burden % of Taxable Income	17.66%	15.06%	16.82%	19.11%	24.54%	32.85%
Average Tax per Return	**$251.36**	**$1,646.47**	**$4,248.00**	**$9,261.21**	**$24,935.55**	**$153,683.59**

Corporation Income Tax Returns

(Tax Year 1995 data)

	Size of Total Assets (in millions)					
	< $1	$1 to $10	$10 to $50	$50 to $100	$100 to $250	> $250
Total Returns	4,053,016	356,591	41,448	8,359	7,216	7,537
Taxable Income (in thousands)	$23,776,302	$24,489,972	$24,045,087	$14,844,318	$28,007,712	$449,569,626
Total Tax Liability (in thousands)	$5,734,339	$7,528,148	$7,788,947	$4,777,066	$8,767,868	$121,796,421
Tax Burden % of Taxable Income	24.12%	30.74%	32.39%	32.18%	31.31%	27.09%
Average Tax per Return	**$1,414.83**	**$21,111.44**	**$187,920.94**	**$571,487.74**	**$1,215,059.31**	**$16,159,801.11**

B. Tax Expenditures

Tax expenditures are the foregone federal revenue resulting from deductions and credits provided in the Internal Revenue Code. Since tax expenditures directly affect the amount of funds available for government operations, decisions to forego federal revenue are as important as decisions to spend federal revenue.

The resulting Tax Expenditure is calculated using the average Tax Burden percentage of Taxable Income applied to the Total Deductions. Total Credits against tax liability result directly in Tax Expenditure. A summary of the largest categories of tax expenditures follows.

Please note that FY 1996 is the most recent individual income tax return data available and FY 1995 is the most recent corporate income tax data available.

TAX EXPENDITURES TABLE

(In Thousands)

INDIVIDUAL INCOME TAX RETURNS (Tax year 1996 data)

Deductions for Taxable Income	***Deductions & Credits***	***Resulting Tax Expenditure***
Basic std deduction	*$415,113,986*	
Additional std deduction	*13,462,417*	
Itemized in excess of limitation	*18,901,571*	
Medical & dental expense	*26,787,262*	
Interest paid	*227,625,566*	
Taxes paid	*202,508,276*	
Charitable contribution	*84,264,918*	
Total Deductions	***$988,663,996***	***$219,780,006***
		22.23%
Credits against tax liability		
Child care credit	*$2,530,689*	
Credit for the elderly or disabled	*32,060*	
Foreign tax credit	*3,147,731*	
General business credit	*648,634*	
Minimum tax credit	*636,343*	
Earned Income Tax credit, offset tax liability	*5,763,150*	
Total Credits	***$12,758,607***	***$12,758,607***
Total Expenditure - Individual Tax Returns		***$232,538,613***

T A X E X P E N D I T U R E S T A B L E

(In Thousands)

CORPORATION INCOME TAX RETURNS (Tax year 1995 data)

Deductions		
Net operating loss	*$57,135,546*	
Dividends received	*23,365,442*	
Public utility dividends paid	*71,598*	
Total Deductions	***$80,572,586***	***$22,310,549***
		27.69%
Credits		
Foreign tax credit	*$30,420,276*	
U.S. possessions tax credit	*3,056,017*	
Nonconventional source fuel credit	*732,031*	
General business credit	*3,388,423*	
Total Credits	***$37,596,747***	***$37,596,747***
Total Expenditures - Corporation Income Tax		***$59,907,296***

PROMPT PAYMENT

The Prompt Payment Act requires Federal agencies to make timely payments to vendors for supplies and services, to pay interest penalties when payments are made after the due date, and to take cash discounts only when they are economically justified. The Department continued to reduce the percentage of interest payments through increased management attention on payment processes, enhanced financial systems, and staff training on Prompt Payment Act compliance. Treasury bureaus continued to increase the use of the Government Purchase Card for small purchases, third party drafts, and increased payments through Electronic Funds Transfer to ensure timely payments to vendors.

The Department's payments made from the Franchise Fund, due to its nature as a revolving fund, cannot be made to vendors until the Fund has enough cash to cover the disbursements. Therefore, a higher-than-average number of the vendor payments made by the Franchise Fund were past the due date. Management continued its effort to address this issue.

The following table provides information on Treasury's compliance with the Prompt Payment Act.

(In Thousands)	FY 1998	FY 1997
Total invoices paid:		
Dollar amount	$2,772,665	$2,126,882
Number	296	320
Total invoices paid late:		
Dollar amount	232,086	$93,895
Percentage	**8.09%**	**4.42%**
Number	23	25
Percentage	**7.48%**	**7.69%**
Late payment interest penalties paid:		
Dollar amount	$321	$249
Percentage	**0.009%**	**0.012%**
Number	8	8
Percentage	**2.72%**	**2.36%**

THE DEBT COLLECTION IMPROVEMENT ACT OF 1996

Introduction

The Debt Collection Improvement Act (DCIA) of 1996 was enacted through the cooperative efforts of the major credit granting agencies, the Office of Management and Budget, the Chief Financial Officers (CFO) Council, and the Department of Treasury. The Act is intended to enhance significantly the Federal Government's ability to service and collect debts. The Department has been working with other agencies and OMB to establish the policies, procedures and infrastructure necessary to implement fully the DCIA, and these efforts will continue until full implementation is achieved.

Under the DCIA, Treasury assumes a significant role for improving government-wide receivables management. Consequently, Treasury is working through the Chief Financial Officers Council, the Federal Credit Policy Working Group, OMB, and other agency officials to implement the Act.

Collection of Delinquent Debt

In Fiscal Year 1998, Treasury collected $14 million through cross-servicing and the administrative offset program. From 1995 through October 1997, Treasury had collected only $1.8 million in these two programs . In addition, $45 million in repayment agreements were established as a direct result of the cross-servicing effort. The dramatic increase in collections and repayment agreements is largely attributable to: the increase in collections at the Birmingham Debt Management Operations Center; inception of the Treasury Private Collection Agency (PCA) contract which collected $3.4 million since March, 1998 when actual collections started to accrue; and the revised Tax Refund Offset (TRO) process which increased agency debt referrals for the administrative offset program from $9.4 billion to $16.9 billion. Collections of delinquent Federal non-tax and child support debt through the Tax Refund Offset Program totaled $2 billion in FY 1998.

As of October 1997, the Report on Receivables Due From the Public reported that individuals, businesses and foreign governments owed Federal agencies in excess of $50 billion in delinquent, non-tax debt. This debt includes education loans, farm loans, housing loans, defaulted guaranteed loans, contractor loans, and vendor overpayments. However, only a portion of this debt is actually collectable and referable to the Financial Management Service (FMS). In order to better assess the portfolio of delinquent non-tax debt owed to the U.S. government, FMS contracted with Price Waterhouse to conduct a comprehensive analysis of the $52 billion portfolio of delinquent non-tax debts. Price Waterhouse calculated that only about 56 percent, or $29 billion -- of the $52 billion is referable to Treasury, and that a significantly smaller amount (between $860 million and $1 billion annually) is likely to be collectable under the Debt Collection Improvement Act. The analysis provided a more realistic picture of the composition and age of the debt portfolio, and FMS now has a quantitative basis on which to establish program goals and determine appropriate collection tools.

Agencies are required by the DCIA, with few exceptions, to refer all delinquent debt over 180 days old to FMS for offset and cross-servicing. In order to increase and strengthen agency compliance with DCIA referral requirements, FMS has continued an aggressive outreach effort to assist agencies in analyzing their eligible delinquent debts for transfer to FMS for offset and cross-servicing. Through this effort, we are working with approximately 50 agencies to increase debt referrals. As a result, 37 agencies referred debts totaling $16.9 billion in non tax delinquent debt to FMS for administrative offset and $2.0 billion cross-servicing in FY 1998. Once debts are referred, they are analyzed and the appropriate collection tools are applied. These tools could include Treasury Offset, demand letters from the Birmingham Debt

Management Operations Center, and referral to private collection agencies; to a debt collection center; or to the Department of Justice.

FMS is also taking a leadership role in DCIA implementation working groups such as the Federal Credit Policy Working Group (FCPWG). The FCPWG provides an interagency forum for resolving DCIA implementation issues such as the revision of government-wide write-off policy, debt referrals to Treasury for offset and cross-servicing, and performance measures for credit programs.

Treasury has revised the Treasury Report on Receivables (TROR) to include the requirements of the DCIA and to provide FMS with a more accurate report of the government's debt portfolio. The revised report will identify eligible debts for referral to FMS and will track collection efforts by the agencies. The new web-based applications will eliminate the agency system conflicts that plagued the former receivables reporting system and provide TROR data access to all internal and external stakeholders. The application development was completed in December 1998 and will be piloted with 5 agencies in first quarter FY 1999. Full roll-out is scheduled for the second quarter of FY 1999.

FIVE YEAR PLAN

Objective: Cross Service Other Agencies' Debts

The DCIA, with some exceptions, requires Federal agencies to refer all delinquent debt over 180 days old to Treasury for cross-servicing. Referrals at the end of fiscal year 1998 included debts from 36 agencies and totaled nearly $2 billion. This is a 310% increase over fiscal year 1997 levels, and of this amount, more than $8.3 million has been collected.

The DCIA requires the Secretary of the Treasury to designate debt collection centers on the basis of their prior performance in collecting delinquent debt. FMS has received a total of seven applications for debt collection center designations to cross service government-wide debt or to service internal agency debts only (referred to as a waiver). The Department of Education's request for a waiver to service student loans was approved. Applications from the Department of Veterans Affairs for both a waiver and Debt Collection Center status to cross service government wide debt was denied. Health and Human Services (HHS) request to be a Debt Collection Center to cross-service government-wide debt was denied. However, HHS has submitted a modified request that is currently under review. Applications from the Social Security Administration, the Small Business Administration and the Department of Agriculture are in various stages of review. The legislative history of the DCIA and further Congressional correspondence on this issue shows the Congressional intent that only agencies with the proven ability to collect delinquent debt are to be given a debt collection center designation. Consistent with this guidance, Treasury has adopted a conservative approach to designation of debt collection centers.

Objective: Merge all Offset Programs into the Treasury Offset Program

One of the most important DCIA implementation goals is the merger of the Tax Refund Offset Program (TROP) into the Treasury Offset Program (TOP). FMS and IRS originally planned to merge the two programs in January 1998 for the 1997 filing season. In lieu of a full merger in 1998, the IRS and FMS jointly developed a transition process designed to provide many of the benefits of a full merger while ensuring that further systems development efforts could proceed in preparation for the revised merger date of January 1999. This effort has been successful and the merger is on schedule for implementation in January of 1999. Efforts of the transition year process resulted in an increase in the number of TOP participants from 17 to 37 agencies and debt referrals have increased from $9.4 billion to $16.9 billion, an 80% increase.

In addition to tax refund payments, Treasury has initiated a salary offset pilot with the Department of Agriculture National Finance Center. Treasury also has an aggressive schedule for incorporating other offset processes in 1999/2000. These include:

- SSA Benefit Offset
- Automated Salary Offset
- State Tax Debt Offset
- Continuous Tax Levy

Much time was spent in fiscal year 1998 on system requirements and enhancement for implementation of these programs. In 1999, the effort to incorporate salary and benefits payments will require the involvement of numerous government agencies, including the Social Security Administration, Department of Veterans Administration, Department of Agriculture, Department of Defense, and Postal Service.

Objective: Pursue Contract for Private Debt Collection Agencies

In accordance with the legislative intent of the DCIA, Treasury is maximizing use of private sector expertise in the collection of delinquent debt. Thirteen contracts were awarded to private collection agencies and FMS began transferring delinquent debt to these contractors for collection on January 31st of 1998.

Referrals in FY 98 to Private Collection Agencies (PCAs) were 26,550 cases with a value of $910 million. Collections by the Private Collection agencies in FY 98 were $3.4 million since collections started accruing in March of 1998. Additionally, PCA's have entered into repayment agreements with 1,388 debtors valued at $6.5 million. The private collection agencies are to be paid based on a percentage of monies recovered from the debts referred by FMS. The performance period for each of the contracts is one year with three, one-year renewal options.

Objective: Improve Government-wide Debt Collection through Issuance of New Regulations

There are a substantial number of regulations that must be issued in order to implement the debt collection provisions of the DCIA. Treasury has made great strides by streamlining internal and Departmental processes, prioritizing efforts and closely monitoring the clearance process. In FY 1997, FMS published five regulations. In FY 1998, FMS published the following regulations:

Final Rule on *Administrative Offset to Collect Child Support* (8/28/98)
Final Rule on the *Offset of Tax Refund Payment to Collect Federal Non tax Debt* (8/28/98)
Final Rule for *Administrative Wage Garnishment (5/6/98)*
Interim Rule on *Salary Offset (4/28/98)*
Interim Rule *Transfer of Debt to Treasury for Collection (4/2/98)*

Notices of Proposed Rule Making (NPRM):

NPRM (4/22/98) and Final Rule *on Barring Delinquent Debtors (12/4/98)*
NPRM (8/4/98) and the Final Rule on *Tax Refund Offset to Collect Past due Support* (12/30/98)
NPRM and Interim Rule (8/21/98) and the Final Rule on *Federal Benefits Offset* (12/23/98).

Additionally, FMS published a withdrawal of the NPRM on *Taxpayer Identifying Number Requirement on Payment Vouchers* and issued a policy statement in its place.

BIENNIAL REVIEW OF "CHARGES"

The Chief Financial Officers (CFO) Act of 1990 requires that agencies biennially conduct a review of fees, royalties, rents, and other charges imposed by the agency and recommend any changes deemed necessary to cover the costs incurred.

The Department of the Treasury's Office of the Deputy Chief Financial Officer requested each Bureau to conduct reviews in Fiscal Years 1992, 1994, 1996 and again in 1998. For purposes of the review, charges include collections based on statutory requirements (e.g., Custom's user's fees, firearms licenses, explosive licenses, permit fees, etc.) and administrative costs (e.g., overhead for reimbursables). Charges that are excluded from review are collections associated with taxes, fines, or penalties.

Biennial reviews are intended to identify whether charges assessed by Treasury Bureaus cover the program and administrative costs associated with the assessed charge. Bureaus are responsible for conducting the reviews, and where the reviews indicate adjustments in the charges are needed, bureaus are to make those changes in the amount charged to recover the costs. In cases where legislative (statutory) changes are needed in order to change the charge (e.g., user fees) the bureau is to take action to submit legislative changes, proposing increases or decreases in the statutory charge that reflects the amount needed to cover the costs. The status of these reviews varies among the bureaus. Generally, each bureau performs a review that identifies the following:

- Type and purpose of charge.
- Authority of the charge (i.e., Economy Act for reimbursable charges, statutory legislation for user fees, etc.).
- Amount of charge
- An indication of whether the current charge covers costs.
- Scheduled dates of reviews to be performed for each charge.
- Date of last review performed.
- A listing of pertinent problems or concerns with reviewing or administering the charge.

Based on information provided to date on the status of bureau reviews, the Customs Service has been unable to adequately perform the biennial reviews of charges imposed statutorily. The information needed to perform an adequate review of these charges has not been available in the past. The relevant information is now being provided by the Cost Management Information System, and Customs plans on conducing a review of its charges in Fiscal Year 1999.

PERFORMANCE REPORT FOR FY 1998

The Government Performance and Results Act establishes formal requirements for strategic planning and performance measurement in the Federal government. The Act requires that agencies develop Strategic Plans by September 30, 1997, annual Performance Plans for FY 1999, and Performance Reports by March 31, 2000.

The following table provides an abbreviated performance report on selected key performance measures as presented in Treasury's FY 2000 Budget-In-Brief dated February 1999.

Note: Due to timing difference between the budget submission and issuance of the Accountability Report, the results for some performance measures may differ from the Management Discussion and Analysis (MD&A) section. The MD&A contains updated performance results from the bureaus' financial statement audits.

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
Economic Mission: PROMOTE A PROSPEROUS AND STABLE AMERICAN AND WORLD ECONOMY				
Departmental Offices				
Economic conditions in developing countries measured by quantitative indicators			Maintain or Improve	Improved
Economic conditions of foreign countries which are major U.S. trading partners measured by growth rate			Maintain or Improve	Improved
United States Customs Service				
Estimated compliance rate (estimate of % of all import entries that contain no discrepancy)	82.0%	81.0%	84.0%	83.0%
Office of the Comptroller of the Currency (Calendar Year Basis - 1998 Actual Data is for 9 Months, January - September 1998)				
Percentage of bank examinations started on schedule	87%	89%	100%	80%
National bank assessments compared to national bank overhead expenses	.72%	.64%	.70%	.62%
Office of Thrift Supervision (Calendar Year Basis - 1998 Actual Data is for 9 Months, January - September 1998)				
The % examined thrifts rating the value of the examination process as satisfactory or better	98%	98%	90%	99%
The % scheduled thrifts that received each type of examination:				
Safety and soundness	98.2%	96.2%	95%	96.6%
Compliance	99.7%	98.3%	95%	100.0%
Holding Company	96.7%	83.2%	85%	88.1%
Electronic Data Processing	78.6%	77.7%	80%	<80%
Trust	90.9%	63.3%	75%	82.1%

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
Community Development Financial Institutions Fund				
Number of CDFIs receiving assistance	31	51	51	112
Total volume of new activity within distressed communities by insured depository institutions ($million)	$60.1	$82.8	$100.0	$194.4
Number of Bank Enterprise Awards Program awardees that provide financial or technical assistance to CDFIs	38	55	79	79
Financial Mission: EFFECTIVELY MANAGE THE GOVERNMENT'S FINANCES				
Internal Revenue Service				
Improve Customer Service				
Telephone access (calls into IRS's call routing system divided by number of call attempts)	29.9%	65.1%	70.0%	89.9%
Tax law % accuracy on assisted telephone calls		96.1%	96.0%	93.8%
Taxpayer burden cost for IRS to collect $100	$8.66	$8.52	$8.53	$8.35
Initial contact resolution rate		78.8%	73%	65.8%
Increase Compliance [3]				
% of true tax liability collected	87.3%	87.3%	87.4%	87.4%
Workload Measure: Total net revenue collected (trillions)	$1.376	$1.504	$1.575	$1.616
,Increase Productivity				
Budget cost to IRS to collect $100	$0.53	$0.48	$0.47	$0.46
IRS Mission Effectiveness Indicator				
Collecting the proper amount of tax revenue at the least cost: tax revenue less the cost of the IRS budget and less the cost of the taxpayer tax return completion burden, divided by tax liability (the closer to 100%, the greater the efficiency)	79.3%	79.5%	79.5%	79.7%
Financial Management Service				
Payments				
Workload: % change in the number of electronic payments from the FY 1996 baseline (449.441M payments)	baseline	9.9%	18.1%	21.4%
% of payments and associated data made electronically	53%	58%	60%	63%
Government dollar savings by reducing the number of check payments ($M)	$5.77M	$11.00M	$.86M	$13.1M
% of checks that are released for on-time delivery	99.99%	99.99%	99.99%	99.99%
Collections				
$ value of electronic collections as a percentage of total collections	57%	52%	62%	68.5%
Government-wide Accounting				

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
% of days the Daily Treasury Statement is released on time	95%	97%	98%	100%
Debt Collection				
% of Federal Program Agencies with debt servicing requirements which have referred their debts in compliance with the Debt Collection Act of 1996	18%	46%	30%	74%
% increase over the FY 1997 baseline of FMS managed government-wide collected delinquent debt		baseline established $1.5M	5%	679%
Bureau of Public Debt				
% of savings securities issued within three weeks through Regional Delivery System	99.0%	99.9%	95.0%	99.9%
% customer service requests:				
completed within 4 weeks (savings bonds)		88%	80%	93%
completed within 3 weeks (Marketable Treasury Direct Securities)	94.7%	94.7%	90.0%	98.9%
% auction results completed within 60 minutes	97%	90%	90%	90%
Bureau of Alcohol, Tobacco, and Firearms				
Total Taxes and Fees Collected (billions)	$12.70	$12.70	$12.80	$12.40
Bureau of Engraving and Printing				
Workload: % change in Federal Reserve note orders from the FY 1995 baseline (9.9B notes)	-5.1%	-0.3%	-7.1%	-7.1%
Currency spoilage -- % of total units printed	5.5%	5.2%	6.0%	6.4%
Manufacturing Cost for Currency (cost per 1000 notes)	$20.03	$18.65	$23.80	$24.34
Workload: % change in postage stamp orders from the FY 1995 baseline (25B stamps)	-1.6%	-1.2%	-12.0%	-21.2%
Postage stamp spoilage -- % of total units printed	11.7%	10.7%	11.0%	12.5%
Manufacturing Cost for Stamps - 100 Stamp Flag Coil (cost per 1000 stamps)	$1.35	$1.36	$1.33	$1.39

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
United States Mint				
Workload: % change in Federal Reserve requests for coinage from the FY 1995 baseline (19.6B coins)	-0.5%	-19.9%	-28.6%	-22.97%
Frequency of time within 90% confidence interval of the coin demand forecast		100%	100%	75%
Frequency of time meeting a minimum inventory level			100%	81.8%
Shipment of commemorative coins within 4 weeks and recurring coins within 3 weeks of order date			98%	93%
Workload: % change in $ sales of numismatic and investment products (includes commemoratives, collectors, bullion coins and precious metals) from the FY 1995 baseline ($393M)	-16.6%	5.4%	-22.4%	70.9%
Numismatic/bullion contribution margin		9.8%	10.0%	6.0%
Average costs to produce circulating coinage (in cents)	$0.0067	$0.0177	$0.0243	$0.0054
1 cent coin	$0.0018	$0.0026	$0.0026	$0.0026
5 cent coin	$0.0043	$0.0072	$0.0072	$0.0066
10 cent coin	$0.0036	$0.0104	$0.0121	$0.0089
25 cent coin	$0.0043	$0.0206	$0.0193	$0.0168
50 cent coin	$0.0193	$0.0479	$0.0805	$0.0379
Losses as a % of reserve value	0.00005%	0.0001%	0.001%	0
Departmental Offices				
Index of calculating interest rates within one day of required pricing data	100%	100%	100%	100%
Index of borrowing policies and borrowing requirements to financial market participants in a timely manner (Reworded in FY 1999/2000 to read: "Announce borrowing policies and borrowing requirements to financial market participants in a timely manner")			90%	100%
Law Enforcement Mission: PROTECT OUR FINANCIAL SYSTEMS AND OUR NATION'S LEADERS, AND FOSTER A SAFE AND DRUG-FREE AMERICA				
United States Customs Service				
Seizures of heroin, cocaine, marijuana (pounds in thousands)	958.7	886.4	953.0	1,116.0
Seizures of currency ($millions, outbound only)	$49.0	$55.2	$57.0	$68.4
Passenger vehicle targeting efficiency (Violations found in targeted exams divided by violations found in random exams)	9.1	9.0	10.0	9.0
Compliance Rate (Air Travel)		97.6%	98.0%	97.7%
Air Passenger Cycle Time (in minutes)	5	5	5	5
Bureau of Alcohol, Tobacco and Firearms				

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
Accomplish 150,000 traces and respond in 12 working days	116,674	191,378	225,000	189,483
Average trace response time (in working days)	9.4	13.5	12.0	16.0
Crime related costs avoided ($billions)		$.93	$1.00	$1.00
United States Secret Service				
Counterfeit notes passed on to the public: ($millions)				
Domestic	$29.8	$31.8	$40.0	$40.0
Foreign	$6.1	$2.9	$5.0	$3.2
Counterfeit passed per million dollars of genuine U.S. currency	$88	$77	$119	$92
Total Criminal Cases Closed	27,393	32,430	28,000	27,429
Amount of counterfeit notes seized - domestic ($millions)	$63.7	$40.4	$45.0	$29.9
Number of credit card fraud/access device cases closed	2,957	2,497	3,000	2,078
Financial institutions fraud cases closed	2,143	2,462	3,000	2,186
Financial Crimes Enforcement Network				
Workload: % change in the number of queries on the Gateway system from the FY 1995 baseline of 35,000 queries	42.9%	64.7%	80%	80%
Number of efforts made to analyze information received through the Suspicious Activity Reporting system	25,215	59,795	60,000	60,850
Number of interagency matches (advisories that notify an agency that another agency has an interest in the same subject)	670	920	900	1,429
Number of targets identified through the use of artificial intelligence	1,032	867	1,755	2,042
Number of presentations provided to enhance outreach efforts	112	273	150	183
Number of FinCEN case lab intelligence products resulting from law enforcement community partnerships	9	49	20	45
Number of assessments that provide an analysis of the money laundering in a country or region	20	25	30	31
Number of efforts to determine vulnerabilities of rapidly advancing technologies		50	68	46
Number of queries using FinCEN's Gateway Platform (workload measure in 1999 plan)	50,015	57,633	63,000	69,335
Number of law enforcement and regulatory personnel provided a platform to do research (workload measure in 1999 plan)		49	65	73

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
% reduction to the reporting burden by banks resulting from elimination or reformulation of unnecessarily burdensome information collection rules and compliance requirements		3.7%	5%	5%
Number of enhancements to the secure web site used by FinCEN's international financial intelligence unit counterparts		2	5	6
Federal Law Enforcement Training Center				
Student survey on quality of basic training (scale 0-6, 6 being highest quality)	5.5	5.4	5.0	5.9%
Student survey of quality of services (scale 0-5, 5 being highest quality)	4.3	4.0	4.0	4.5%
Variable Unit Cost Per Basic Student-Week of Training Funded	$150	$127	$137	$129
Actual Basic Training Requested which is Conducted			100%	100%
Forfeiture Fund				
Number of days required to process equitable sharing payments	308	284	256	271
Number of days elapsing between forfeiture of property and disposal	246	330	222	421
Departmental Offices				
% reduction, from prior year, of backlogged financial transfer applications of Office of Foreign Assets Control (OFAC)	14% reduction	40% reduction	10% reduction	76% reduction
% reduction, from prior year, of backlogged OFAC civil monetary penalty cases in inventory		2% reduction	10% reduction	26% reduction
Management Mission: CONTINUE TO BUILD A STRONG INSTITUTION				
Treasury-wide				
Audit opinion on the consolidated Treasury-wide financial statements for FY 1997			Qualified Opinion	Met
% of customer service standards met by Treasury and its bureaus			100%	72%
% of Treasury bureaus in compliance with GPRA	6%	82%	100%	90%
Begin implementation of the HR prototype bureau, with remaining appropriated bureaus to follow			1 additional bureau	2 additional bureaus
Office of the Inspector General				
Potential $ savings identified ($millions)	$25.939M	$60.902M	$28.500M	$83.447M
Workload Measure: Number of referrals to other OIG components resulting from financial statement audit work	13	20	21	39

Summary Performance Measures and Workload Trends by Treasury Mission Area	FY 1996 Actual	FY 1997 Actual	FY 1998 Final Performance Plan	FY 1998 Actual
% of Reports of Investigation that do not require supplemental or follow-up (a measure of quality)		91%	91%	97%
% of Reports of Investigation completed within one year (a measure of timeliness)		51%	50%	22.5%
Workload Measure: Number of integrity/fraud awareness briefings presented to Treasury employees	20	32	30	33