

RECLAMATION

Managing Water in the West

2006 Annual Report



U.S. Department of the Interior
Bureau of Reclamation

Main canal flowing from Pinto Dam toward the
Soap Lake siphon and Ephrata, Columbia Basin Project, Washington.

2006 Annual Report



U.S. Department of the Interior
Bureau of Reclamation

Table of Contents

Letter from the Commissioner	iv
Management's Discussion and Analysis	1
Mission and History	2
Goals, Accomplishments, and Future Challenges	4
Managing for Excellence	5
Delivering Water	7
Generating Hydropower	16
Providing Other Programs and Benefits	20
Management Accountability	33
FY 2006 Performance Measure Highlights	42
Delivering Water	42
Generating Hydropower	44
Financial Analysis	47
Financial Statements	47
Improper Payments	54
Internal Controls Over Financial Reporting	54
Financial Statements and Notes	55
Auditor's Report	56
Response to Auditor's Report	72
Consolidated Balance Sheet	80
Consolidated Statement of Net Cost	82
Consolidated Statement of Changes in Net Position	83
Combined Statement of Budgetary Resources	84
Consolidated Statement of Financing	85
Notes to the Financial Statements for the Years Ended September 20, 2006, and 2005	86
Supplemental Section	123
Organization Chart	124
Region and Offices Map	125
Required Supplementary Information	126
Required Supplementary Stewardship Information	139

Letter from the Commissioner



Bob Johnson, Commissioner,
Bureau of Reclamation

It is my distinct pleasure to present the Bureau of Reclamation's 2006 Annual Report to the Congress and the American people.

In fiscal year 2006, Reclamation continued its role in developing and maintaining one of the most impressive water management infrastructures in the world, an infrastructure that is vital to bringing water and power to the people of the West and supporting the region's burgeoning economy.

Reclamation is the Nation's largest wholesale water supplier. The 348 reservoirs we administer have a total storage capacity of 245 million acre-feet of water. We bring water to more than 31 million people and provide 20 percent of Western farmers (140,000) with water to irrigate 10 million acres of farmland that produce 60 percent of the Nation's vegetables.

Reclamation is also the Nation's seventh largest power utility and second largest producer of hydroelectric power in the West. Our 58 powerplants provide more than 40 billion kilowatthours of energy each year equivalent to the energy provided by 80 million barrels of crude oil. These plants serve six million homes and generate nearly \$1 billion in power revenues for the U.S. Treasury.

Our core mission to deliver water and generate power in the 17 Western States has remained constant for a century. But the way we accomplish our mission has evolved considerably. At one time, our focus was on constructing facilities; today, it is primarily on managing and maintaining those facilities to ensure their continued effective performance.

As part of our efforts to remain ready to meet Western water management challenges and the associated needs of our customers and stakeholders, Reclamation funded an independent study of our organizational structure and work practices by the National Research Council of the National Academies. As a result of this study, Reclamation developed an action plan, *Managing for Excellence*, which outlines a process and timeframe to address the findings of the National Academies' report.

During fiscal year 2006, Reclamation made substantial progress on many initiatives to help the people of the West meet current and future water needs. For example, as the fiscal year ended, the Animas-La Plata Project in southwest Colorado was 41 percent complete, and it is on track to have construction completed within budget by 2012, with project closeout in 2013. In July, the Secretary of the Department of the Interior, Dirk Kempthorne, approved \$1.3 million in Water 2025 Challenge Grants to help fund 10 water conservation projects in 7 Western States. These funds, together with non-Federal contributions, represent a combined investment of more than \$5.6 million in infrastructure improvements that are intended to enhance water conservation and allow existing water supplies to be used more efficiently.

In fiscal year 2007, we plan to address a number of challenges: developing new Colorado River management strategies to address potential Lower Basin shortages and the operation of Lake Powell and Lake Mead under low reservoir conditions; ensuring guard and surveillance capabilities at our critical infrastructure facilities; and implementing a cooperative endangered species recovery program for the Platte River.

I have total confidence that the Bureau of Reclamation will, working with its partners, successfully meet future water management challenges. Reclamation has always been dedicated to getting the job done, and we continue our commitment to serving our customers and the public.



Management's Discussion and Analysis

Mission and History



The Bureau of Reclamation was created in 1902 to help settle the American West. Then called the “Reclamation Service,” Reclamation was authorized by the Congress to assist local communities in building water projects to “reclaim” the arid West.

In our first 60 years, Reclamation became a leader in engineering and constructing water storage and delivery projects. Our projects, including Hoover Dam on the Colorado River and Grand Coulee Dam on the Columbia River, provided irrigation water that allowed farmers to settle the West even during droughts. Our large hydropower facilities supplied power generation that allowed industries and large cities to flourish.

Today, as the largest wholesaler of water in the country, we furnish water to more than 31 million people. Reclamation is also the second largest producer of hydroelectric power in the Nation. Many of our projects have benefitted the West for 50 or 60 years—a few for more than 100 years. We have continued to provide water and hydropower during droughts and flood control during times of surplus water. Water from our projects has helped meet the needs of a growing Western population.

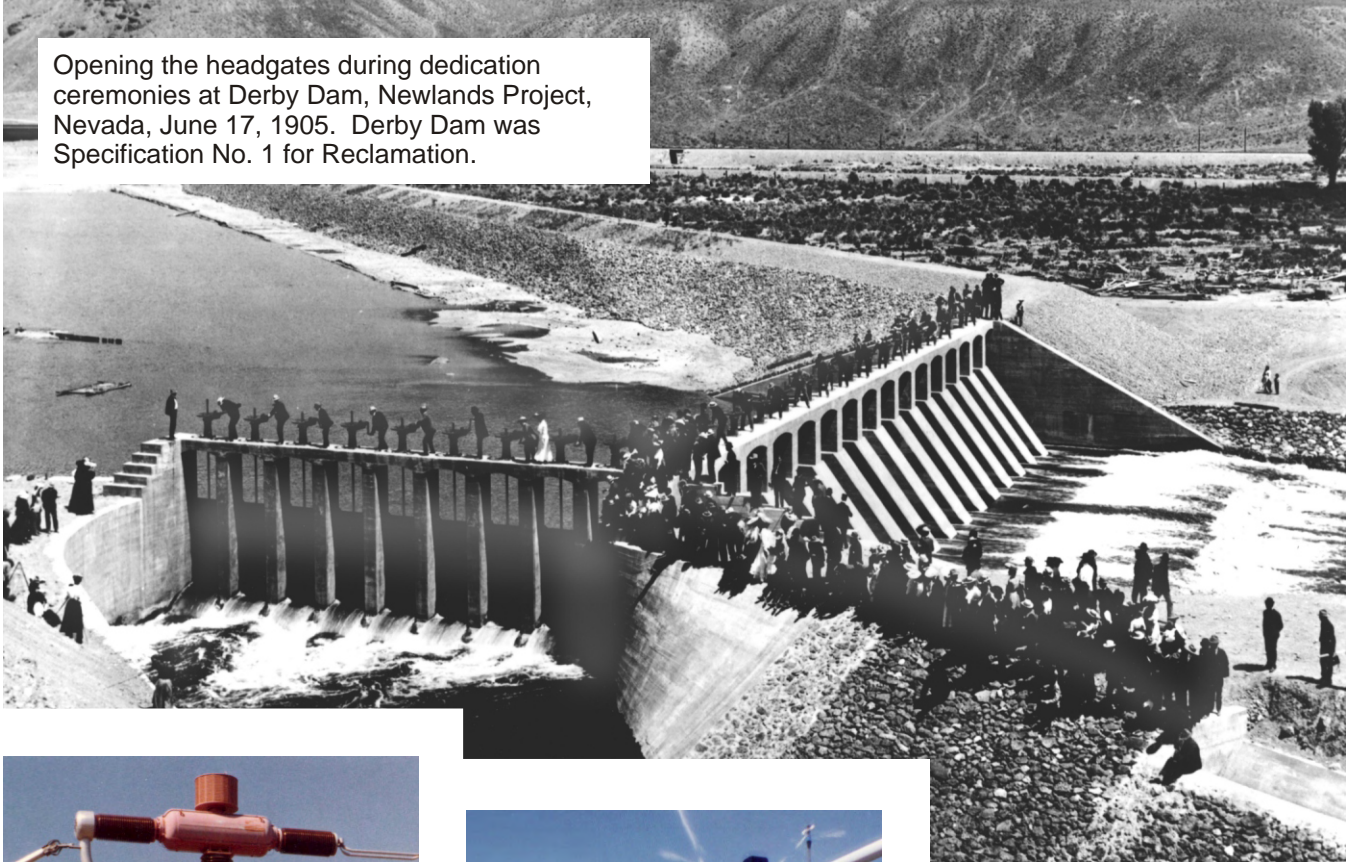
As new construction waned, our focus also changed to managing existing resources. Increased population demands for domestic water, recreational activities, and water to maintain ecosystems have resulted in increasing demands on existing water supplies. Our facilities play a major role in meeting these demands. Our expertise in managing water and researching new technologies helps us contribute to meeting these demands.

Water is still the most valuable and scarce resource in the West, and Reclamation continues to play a key role in making water available for the many demands placed on the West’s water systems.

Mission:

The mission of the Bureau of Reclamation is to manage, develop, and protect water and related resources in an environmentally and economically sound manner in the interest of the American public.

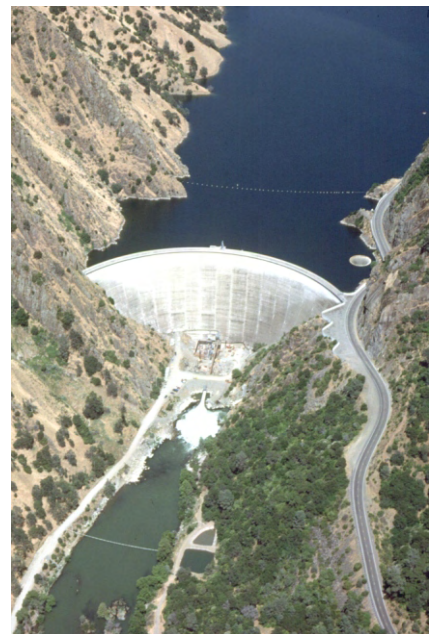
Opening the headgates during dedication ceremonies at Derby Dam, Newlands Project, Nevada, June 17, 1905. Derby Dam was Specification No. 1 for Reclamation.



Hydroelectric power generation



Center pivot irrigation



Monticello Dam

Goals, Accomplishments, and Future Challenges



Timely inspections and maintenance help ensure that Reclamation continues to meet the needs of the American public.

Reclamation has outlined four overarching goals that emphasize our mission to deliver water and generate hydropower while addressing other water use requirements and planning for future water needs to avoid crisis and conflict:

- Ensure the reliable delivery of water and generation of hydropower under Reclamation contracts.
- Optimize hydropower generation consistent with project purposes.
- Incorporate other considerations, such as recreation, fish and wildlife, environment, and Native American trust responsibilities, into our water and power operations.
- Identify and plan for future consumptive and nonconsumptive water supply needs by identifying unmet needs in the next 25 years.

To meet these goals and priorities in fiscal year 2006, Reclamation:

- Delivered approximately 30.8 million acre-feet of water (1 acre-foot supplies enough water for a family of four for 1 year).
- Generated about 44 billion kilowatthours (kWh) of hydroelectric energy—enough to meet the annual needs of 9 million people.
- Awarded more than \$1.3 million in Water 2025 Challenge Grants to fund 10 water conservation or development projects in 7 States.

Reclamation's priorities are to:

- Complete security assessments for designated facilities and proceed with efforts to ensure the long-term security of all Reclamation facilities.
- Fund and complete critical activities on high profile projects (e.g., Water 2025, Animas-La Plata, and Middle Rio Grande) on schedule.

- Improve management of cost estimates on construction projects.
- Expand and enhance Reclamation's scientific expertise and coordination with other agencies, including desalination research, invasive species control and management, and Endangered Species Act (ESA) related activities.

Managing for Excellence

Reclamation is preparing for the challenges of the 21st century by thoroughly examining our core capabilities in a number of key areas and our ability to respond in an innovative and timely manner to future needs. The *Managing for Excellence* Action Plan, published in February 2006, outlines a process and timeframe for identifying and addressing the specific 21st century challenges to fulfill our mission.

Managing for Excellence Action Plan

An important catalyst for this evaluation effort is the recently published National Research Council (NRC) Report, "Managing Construction and Infrastructure in the 21st Century Bureau of Reclamation," which examines several facets of our organization, practices, and culture. Each of the NRC Report's recommendations is addressed in this *Managing for Excellence* Action Plan. The underlying principles and benchmarks that guide the *Managing for Excellence* Project are to:

- Improve the management and leadership processes, applications, responsibilities, and outcomes in Reclamation activities to effectively respond to future needs and challenges.
- Attain a synergistic balance of centralized policy development (Reclamation Manual) and decentralized operations.
- Determine the appropriate level and organizational structure to deliver Reclamation's core capability necessary for mission fulfillment.
- Define Reclamation's stewardship responsibility as the owner of Federal facilities.
- Ensure transparency and value of construction and operation and maintenance (O&M) costs.

The *Managing for Excellence* Action Plan outlines 41 specific action items based on these principles and benchmarks. These action items are organized under eight key functional areas to identify and implement needed changes or improvements. The table below outlines the functional areas and objectives we plan to achieve.

Functional Areas and Objectives
<p><u>Relationships with Customers and Other Stakeholders</u></p> <ul style="list-style-type: none"> • Strengthen stakeholder relationships • Improve communication • Create transparent decisionmaking processes
<p><u>Policies and Organization</u></p> <ul style="list-style-type: none"> • Refine the balance between centralized policy and oversight with current, effective decentralized operational organization • Implement the most effective, efficient organizational structure
<p><u>Engineering and Design Services</u></p> <ul style="list-style-type: none"> • Define core capabilities to fulfill Reclamation's mission • Foster a Center of Excellence for our engineering and technical capabilities • Provide engineering standards and design services that meet Federal customer needs
<p><u>Major Repair Challenges</u></p> <ul style="list-style-type: none"> • Devise methods to help customers finance their allocated share of major repair projects • Develop processes or measuring tools to determine whether a major repair project is warranted • Use innovation to add value to major repair projects
<p><u>Project Management</u></p> <ul style="list-style-type: none"> • Develop policies and practices to provide an appropriate degree of continuity and project management oversight from project inception through the planning process to construction and into operations
<p><u>Asset Sustainment</u></p> <ul style="list-style-type: none"> • Better understand construction and O&M costs • Increase value of construction and O&M activities • Increase opportunities for: <ul style="list-style-type: none"> ○ O&M outsourcing ○ O&M transfer ○ Title transfer
<p><u>Research and Laboratory Services</u></p> <ul style="list-style-type: none"> • Increase partnerships and technology transfers in research and development
<p><u>Human Resources/Workforce</u></p> <ul style="list-style-type: none"> • Enhance employee competencies in key skills such as project management, collaboration, decisionmaking, and leadership

FY 2006 Accomplishments

In February, Reclamation established several teams to address and implement these action items. As part of this effort, Reclamation is seeking feedback from within and outside Reclamation, where appropriate.

In April, Reclamation participated in a national stakeholder meeting hosted by the National Water Resources Association (NWRA). The Family Farm Alliance, Western States Water Council, and the American Public Power Association also participated. The meeting initiated a dialogue with stakeholders on *Managing for Excellence* action items and plans for future public involvement. In July, Reclamation held its first public meeting in Las Vegas, Nevada, where the public could participate in breakout sessions and comment on approaches and proposals. A second public meeting was held in Salt Lake City, Utah, in September 2006. A third meeting will be held in Sacramento, California, in November 2006.

During FY 2006, Reclamation completed Action Item 2 (Increase Availability of the Reclamation Manual) by highlighting the Reclamation Manual Directives and Standards on the Reclamation Web site; Action Item 3 (Incorporate Transparency and Value into Policy Development) by revising the policy development process and developing a process to waive the requirements of the Reclamation Manual; and Action Item 5 (Clarify Delegations of Authority) by updating the Reclamation Manual to include delegations of authority. Work was begun on an additional 26 action items.

In 2006, Reclamation launched internal and external Web sites to provide information to employees and the public on *Managing for Excellence*. Please visit <http://www.usbr.gov/excellence> for more information.

Delivering Water

One of Reclamation's primary missions is delivering and storing water throughout the 17 Western States. In an average year, Reclamation projects deliver approximately 30.8 million acre-feet of water. Ongoing droughts and burgeoning Western populations continue to make this job ever more challenging. We continuously evaluate our management strategies and incorporate new technologies to develop new water supplies and use water more efficiently.

The Water 2025 Challenge Grant Program: Preventing Crises and Conflict in the West

Water is the lifeblood and the foundation of the American West's economy. It is also the scarcest resource in some of the fastest growing areas of the country. Water 2025 focuses attention on the realities of major conflicts among competing uses of water, including the explosive population growth in Western urban areas, the emerging need for water for environmental and recreational uses, and the national importance of the domestic production of food and fiber from Western farms and ranches.

In some areas of the West, existing water supplies are, or will be, inadequate to meet competing demands for water even under normal water supply conditions. Water 2025 recognizes that States, tribes, and local governments should have a leading role in meeting these challenges and that the U.S. Department of the Interior should focus its attention and resources on areas where scarce Federal dollars can provide the greatest benefits to the West and the rest of the Nation.

The Water 2025 Challenge Grant Program provides a basis for public discussion of the realities that face the West so that decisions can be made at the appropriate level in advance of water supply crises. It also sets forth a framework to identify the problems, solutions, and a plan of action as Interior works with States, tribes, local governments, and the private sector to meet water supply challenges.

The Challenge Grant Program is an important aspect of Water 2025. Challenge Grant funding is provided on a minimum 50 percent, non-Federal cost-share basis to irrigation and water districts, Western States, and other entities with water delivery authority. These entities use the funding to implement projects that stretch existing water resources. Challenge Grant projects focus on modernizing aging water delivery infrastructure, improving water use efficiency and conservation, and marketing water. Projects are selected through a competitive process that emphasizes projects that will achieve demonstrated results within 24 months from the date of award.

Since its inception in 2004, the Water 2025 Challenge Grant Program has funded 78 projects that represent approximately \$64.1 million in water system and water management improvement across the West, including non-Federal cost-share contributions of approximately \$47.7 million and a Federal investment of approximately \$16.4 million.

FY 2006 Highlights of Water 2025 Challenge Grants

In FY 2006, for the third year in a row, Reclamation received more than 100 proposals for Challenge Grant funding. The proposals represent a combined request for more than \$19 million in Federal funding to complete more than \$63 million in water delivery system improvements across the West (costs include non-Federal cost-share amounts).

This year, Reclamation invited State governmental entities with water management authority (e.g., State Departments of Water Resources, State Engineers' Offices, etc.) in the 17 Western States, in addition to tribes, irrigation districts, water districts, and other organizations with water delivery authority, to submit applications for Challenge Grant cost-share funding.

In July 2006, 10 projects, totaling \$1.3 million in Water 2025 Challenge Grants for projects across the West, were selected for funding. Including the matching contributions of non-Federal partners, the selected projects represent a combined investment of more than \$5.4 million in water management improvements.

FY 2006 Highlights for Other Water 2025 Activities

The Water 2025 Program has also improved technologies used to stretch limited water supplies. In FY 2005, \$1.7 million in Water 2025 funds was awarded through Reclamation's Science and Technology Program. This program uses competitive grants. Agencies or organizations that receive these grants are required to share the costs.

Reclamation worked to improve technology through a number of partnerships to implement congressional earmarks (an earmark is a specific amount of spending for a specific project) in Water 2025's FY 2006 budget. For example, Reclamation worked with a consortium of universities in Ohio to develop advanced remote sensing technologies (\$1.0 million). All of these technologies help Reclamation manage water resources in areas where there are current or potential water conflicts.

Reclamation also worked with the Middle Rio Grande Conservancy District in New Mexico to modernize its water delivery facilities. Reclamation and the district have a cost-share partnership to implement water efficiency measures, including installing flow measurement devices, lining canals, and automating weather stations and diversion dams throughout the district (Reclamation funding was \$1.75 million in FY 2005 and \$1.0 million in FY 2006).

Reclamation worked with the Desert Research Institute in Nevada on projects such as an investigation of the human health and environmental safety of using polyacrylamide (PAM) to reduce canal seepage in unlined canals and development, testing, and implementation of tools to optimize the operations of the Truckee River (\$2.0 million in FY 2005 and \$2.0 million in FY 2006).

Reclamation also entered into an agreement with the New Mexico Interstate Stream Commission to improve water efficiency and supplement water supplies on the Pecos River. Pipelines will deliver water from wells in the Seven Rivers areas to augment Brantley Reservoir (\$1.0 million in FY 2006).

Using Alternative Sources of Usable Water—Desalination

Desalting sea water and inland brackish waters offers new drought-proof water supplies that can help Reclamation manage water more effectively. Water quality and desalination projects and research helped provide clean water for Native Americans, rural areas, municipal and industrial water users, and other users. Reclamation's investments in desalination come through various budget line items and programs: the Desalination and Water Purification Research and Development Program, the Science and Technology Program, the Water Reuse Program—Title XVI, Water 2025, and the Yuma Desalting Plant Title I. All provide funding. In FY 2006, ongoing projects continued to show the value of innovative desalination techniques including:

- **Expeditionary Unit Water Purification (EUWP) Verification Testing:** Reclamation recently tested an EUWP at the new Groundwater National Desalination Research Facility, Alamogordo, New Mexico, research center, which verified that the EUWP produces water that meets the Environmental Protection Agency drinking water standards.
- **Dewvaporation:** Low-cost desalination, using evaporation, uses heated and cooled air to evaporate water from saline feeds and is currently being pilot tested.
- **Reverse Osmosis Treatment for San Joaquin Drainage Program:** A pilot study confirmed the technical feasibility of using reverse osmosis treatment to desalt agricultural drainage, separate selenium contamination, and recover 50 percent of the drainage as clean product water that can be reused for irrigation.

- **Vertical Tube Evaporator Thermal Desalination Pilot Test:** This test demonstrated the technical and economic feasibility of using geothermal energy to produce potable water where potable water is needed, steam heat is available, and there is a source of impaired water nearby (e.g., the Salton Sea).
- **Large Diameter Membrane Development:** Use of a new, larger membrane is expected to result in \$25 million in cost savings over 20 years for a 50 million-gallons-per-day seawater plant.
- **Improving Product Water Recovery at the Yuma Desalting Plant:** Using a demonstration-scale test unit located in its onsite research facility, the engineers perfected a new operating process to increase product water recoveries to 85 percent.

Current Scientific Findings on Saltcedar (Tamarisk) Water Salvage Potential

Previous Reclamation Annual Reports discussed the potential water use of saltcedar based on limited available information, which suggested that saltcedar control might lead to significant water savings. However, recent scientific findings on saltcedar water use suggest that previous estimates of potential water savings may be overly optimistic. Much of the scientific evidence obtained recently does not support the assumption that saltcedar has unusually high rates of water use. It now appears that saltcedar may actually use water at a rate similar to other riparian vegetation. These findings mean that the potential benefit of saltcedar control or removal for water savings may be limited or undetectable. At this time, the evidence suggests that water-saving potential is likely to be much less than previously expected, difficult to maintain, and hard to realize as flow in a stream. The Research and Development Office is continuing to fund research and work with partners to help scientifically define the potential for water savings.

Construction

Most of Reclamation's construction is to support the Dam Safety Program or is performed as part of other specific projects the Congress has authorized. Portions of this program and other authorized projects have been contracted to Indian tribes pursuant to the Indian Self-Determination and Education Assistance Act, Public Law (P.L.) 93-638.

Animas-La Plata Project

In FY 2006, Reclamation's major construction efforts were on the Animas-La Plata Project in southwestern Colorado. Since 2002, construction contracts of more than \$211 million have been awarded for the Animas-La Plata Project. Reclamation is constructing this water delivery project under the Colorado Ute Indian Water Rights Settlement Act of 1988, as amended in 2000. The project will provide water for the Ute Mountain Ute and Southern Ute Indian Tribes and the Navajo Nation, as well as benefit four other entities: the Animas-La Plata Water Conservancy District, Colorado; the State of Colorado; the San Juan Water Commission, New Mexico; and the La Plata Water Conservancy District, New Mexico.

Reclamation construction on Ridges Basin Dam and Durango Pumping Plant, two key components of the Animas-La Plata Project, continued in FY 2006. The dam will create Lake Nighthorse, which will provide the Four Corners area (meeting point of Utah, Colorado, New Mexico, and Arizona) with 120,000 acre-feet of long-term water storage. When the entire project is completed, municipal and industrial users within Colorado and New Mexico will also use this water.

At the end of FY 2006, Reclamation had completed more than 41 percent of the entire Animas-La Plata Project and:

- Placed embankment materials for Ridges Basin Dam and built the dam to a height of more than 100 feet from the foundation to the top.
- Worked on the outlet tunnel through the left abutment of the dam.
- Placed concrete for the Durango Pumping Plant.
- Completed the final design of components to the Navajo Nation Municipal Pipeline and the Ridges Basin Inlet Conduit.

The schedule for the Animas-La Plata Project is driven by the availability of funds. The project is currently scheduled to be completed in 2012, including filling of the reservoir. Estimated total cost is \$500 million, plus indexing for inflation.

Central Arizona Project

Reclamation constructed the Central Arizona Project (CAP), a multipurpose water resource development and management project that delivers Colorado River water, either directly or indirectly, into central and southern Arizona. Reclamation's actions in FY 2006 included the following:

- Acquired a significant amount of the right-of-way for lands needed for the San Tan Lateral and sections of the San Tan Canal, Pima Lateral, and portions of the South Side Canal as part of the Gila River Indian Community's Pima-Maricopa Irrigation Project. Began construction on both the San Tan Laterals and on a portion of the South Side Canal.
- Continued project investigations with the San Carlos Apache Tribe to help develop a mutually agreeable project configuration. Reclamation hosted the San Carlos Apache Tribal Council in May 2006 at Hoover Dam to present the technical data developed to date. The work included agricultural consulting services and preparation of an estimate to address a Black River Diversion tunnel option.
- Completed 60 percent of the work under the contract for the San Xavier District's farm rehabilitation.
- Conducted a "turnover inspection" and awarded a contract for the remediation work in the Schuk Toak Farm and the Tohono O'odham Nation. When the work is completed and accepted, Reclamation will transfer O&M responsibilities to the Nation, and the Secretary of the Interior's obligations to the Tohono O'odham Nation for Schuk Toak Farm development will be considered, by both parties, as satisfied and complete.
- Initiated planning on the Tonto Apache Tribe's options for using its CAP water allocation.

Savage Rapids Dam

Reclamation awarded a \$28 million contract for construction of the Savage Rapids pumping plant and subsequent removal of a major portion of Savage Rapids Dam, located on southwest Oregon's Rogue River. This work will permanently resolve fish passage and protective issues at the dam, as directed by a court order, while ensuring an uninterrupted water supply for patrons.

Flood Control

Significant flood control operations during 2006 prevented serious flooding in the Pacific Northwest, where nearly every basin faced a flood threat at some point during the year that required close monitoring and appropriate actions. For example, flood control operations on the Boise River lasted nearly 5 months, with more than a month of flows at or near flood stage throughout the city of Boise.

Drought Response

Reclamation's approach to addressing drought conditions begins with storing water for times of shortage. During the recent, prolonged drought in many areas of the West, our reservoirs performed well, meeting water requirements in most areas of the West despite precipitation shortages.

Reclamation also actively engages in drought planning by working with States, water users, and other entities to prepare in advance, so that when drought occurs, we have steps in place to manage it. Part of this advance planning involves interagency efforts such as the Drought Action Teams, working with the U.S. Department of Agriculture.

The Water 2025 Challenge Grant Program and our Water Conservation Field Services Program provide grants to help water users make more efficient use of water, particularly during times of drought.

In addition, Reclamation responds to emergencies by using our authority under Title I of the Reclamation States Emergency Drought Relief Act of 1991, as amended, and extended with P.L. 109-234 until 2010. This supplemental appropriations bill also included \$9 million for the drought program to minimize or mitigate drought damages or losses. Reclamation made funds available through letter contracts under the emergency operations provisions of the Federal Acquisitions Regulations to allow on-

the-ground work to begin immediately. Reclamation also initiated work on drilling municipal wells and designing, monitoring, and testing wells, along with water hauling projects. In FY 2006, we made available more than \$9.3 million in emergency drought relief to a number of entities:

- Five communities in New Mexico to drill municipal wells.
- Temporary supplies of water purchased in New Mexico to provide flows for endangered fish in the Pecos River and the Rio Grande.
- Water hauling services for an Indian tribe in Arizona.

Colorado River Management Strategies

At the direction of the Secretary of the Interior, Reclamation started to develop Lower Basin shortage guidelines and coordinated management strategies for Lake Powell and Lake Mead under low-reservoir conditions in FY 2005. In 2006, Reclamation prepared a draft alternatives report and prepared a draft environmental impact statement (EIS) to address the proposed guidelines and strategies. Reclamation anticipates the draft to be available in February 2007, and the final EIS will be completed in December 2007.

A remnant Colorado River channel is excavated near Yuma, Arizona, to redirect flow away from direct impact to the river levee.



Collaborating to Meet Future Water Supply Needs

In 2004, the State of Washington, Reclamation, and three irrigation districts agreed to cooperate to optimize water management of the Columbia River and Reclamation's Columbia Basin Project. State legislative action established a program to aggressively pursue development of water supplies to benefit both instream and out-of-stream uses through storage, conservation, and voluntary regional water management agreements. Numerous studies are ongoing under this partnership.

Generating Hydropower

Reclamation's hydroelectric power facilities serve as some of the West's most important electrical resources, with 58 hydroelectric powerplants having an installed capacity of more than 14 million kilowatts.

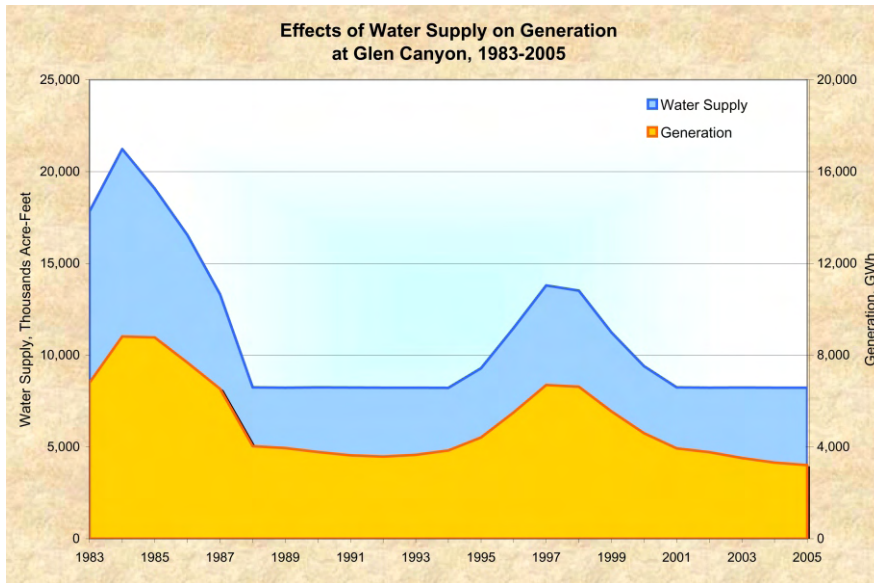
Each year, Reclamation's powerplants generate about 44 billion kWh of hydroelectric energy, enough to meet the annual needs of 9 million people, or the energy equivalent of more than 80 million barrels of crude oil.

The Western Area Power Administration (Western) and Bonneville Power Administration (BPA) market the power generated by Reclamation facilities that is surplus to project needs.

In February 2005, Reclamation entered into a partnership agreement with the U.S. Army Corps of Engineers (USACE) to promote a long-term working relationship and collaborate on efforts to manage water and related land resources within their respective missions. In particular, the agreement encourages the two agencies to share needed technical expertise, improve resource management, and leverage each agency's limited resources to improve public services and make more efficient use of limited public funds.

Evaluating Drought Impacts on Hydropower Generation

The ongoing drought in the Western United States has significantly impacted Reclamation's hydropower production and has negatively impacted customer power rates.



The Glen Canyon Powerplant can provide the electric power for about 1.8 million people across the marketing area (Arizona, Utah, Colorado, Wyoming, New Mexico, and Nevada). The Glen Canyon Powerplant accounts for approximately 70 percent of the power generation for the total Colorado River Storage Project.

The Upper Colorado River Basin experienced 5 consecutive years of extreme drought from September 1999 through September 2004. In the summer of 1999, Lake Powell was essentially full, with reservoir storage at 97 percent of capacity. Inflow volumes for 5 consecutive water years were significantly below average. Lake Powell storage decreased through this 5-year period, with reservoir storage reaching a low of 8.0 million acre-feet (33 percent of capacity) on April 8, 2005. During water year 2005, Lake Powell storage increased by 2.77 million acre-feet (31 feet in elevation) and was 105 percent of average. Unfortunately, in 2006, there was a return to drier conditions in the Colorado River Basin. Unregulated inflow to Lake Powell in water year 2006 was 73 percent of average, or 8.77 million acre-feet.

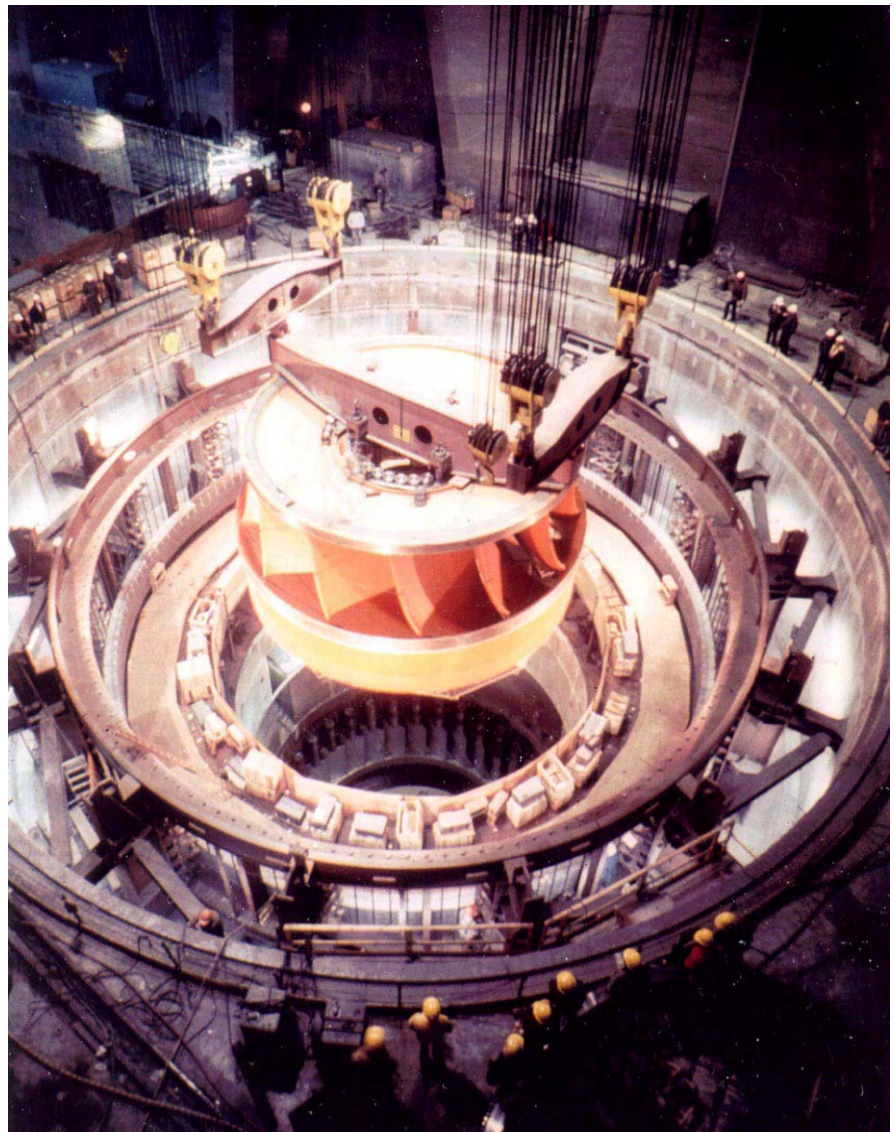
The effects of multiple years of drought and low inflow remain visible at Lake Powell. Lake Powell storage is currently 49 percent of capacity, with the water surface elevation nearly 100 feet below full pool. The declining lake level at Lake Powell has resulted in a reduction in Glen Canyon Powerplant's generation by approximately 25 percent, from an

average generation of 1,320 million kWh to about 990 million kWh. Consequently, Western has increased its composite firm power rate from 20.28 mills per kWh to 25.28 mills per kWh to accommodate increased purchase power expenses necessary to meet firm power contracts.

FY 2006 Highlights

Reclamation leads the hydropower industry for low costs and high reliability. We also have an outstanding record for reliable power delivery. We strive to keep our generators at their peak by rehabilitating or replacing older models. We continue to improve operating equipment; for example, installing more efficient turbine runners at Grand Coulee Dam (FY 2000 through FY 2012), Flaming Gorge Dam (FY 2005 through FY 2007), and Glen Canyon Dam (FY 2004 through FY 2014). We keep

The turbine runner replacement program on generators 1-18 at Grand Coulee Dam is an example of major work to improve operating equipment.



costs in check by maintaining reliable facilities and efficiently using financial resources to extend the life of our facilities.

Our Research and Technology Program is a key part of our efforts to meet future power demands. We are developing the technology needed to enhance O&M activities, reduce costs, increase efficiency, and improve system reliability, stability, and safety.

Reclamation's power program scored a 92 percent on the Office of Management and Budget's Program Assessment Rating Tool (PART) review and was rated "effective." Producing significant achievements in 2006, Reclamation's programs:

- Implemented Hydropower Asset Management Planning risk-based condition assessment tool (developed with the largest hydropower producers in North America and BPA).
- Completed 2006 Comprehensive Facility Reviews (CFR) on all scheduled power facilities (Power Resources Office published all Reclamation CFR reports for 2006 by December 2006).
- Certified compliance procedures with applicable industry-wide reliability requirements.
- Continued to form strong partnerships with national and international hydropower organizations, including the USACE and the Tennessee Valley Authority (TVA), to work on areas of mutual interest related to power O&M, benchmarking, and best practices.
- Completed an inventory of every Reclamation study conducted since 1939 that did not result in construction authorization to comply with the Energy Policy Act, Section 1840.

Future Challenges and Goals

While our forced outage rate is lower than the current industry average, our hydropower program must continue to improve performance and optimize generation, consistent with project purposes, to maintain this performance level. Reclamation conducts frequent assessments of O&M effectiveness at all of our powerplants and major pumping plants. We track recommendations to correct deficiencies or improve local programs to their completion.

The Energy Policy Act of 2005 introduced challenges and new opportunities. Mandatory reliability standards with financial penalties for noncompliance highlight our industry-leading, low forced outage rates and emphasize the importance of our O&M program. A report under the Energy Policy Act, Section 1834, will be completed by February 2007 and focuses on opportunities for increased hydropower at Federal facilities. The Energy Policy Act also expedites terms and conditions for hydropower license applications under the Federal Power Act and establishes procedures for hydropower license applicants to request “expedited trial-type hearings.”

Providing Other Programs and Benefits

In addition to water delivery and power generation, Reclamation is also responsible for maintaining and safeguarding its facilities, as well as other projects authorized by the Congress that provide benefits for Native American trust responsibilities, recreation, fish and wildlife, and the environment.

Safety, Security, and Law Enforcement Programs

The Safety, Security, and Law Enforcement (SSLE) Program's objective is to protect the public, Reclamation employees, and Reclamation's water and power delivery capability against terrorism and other illegal activity.

FY 2006 Highlights

Reclamation continued to implement security improvements at critical infrastructure facilities. We completed designs and began installing integrated security upgrades at three National Critical Infrastructure facilities: Folsom, Shasta, and Glen Canyon Dams. Security enhancements include barriers, video surveillance, intrusion detection, access control, communication systems, and guard forces.

In FY 2006, we completed the remaining initial security risk assessments for essential facilities. Decision documents have been completed for 120 of the 264 critical and project essential facilities, while the remaining 144 decision documents are nearing completion. A total of 2,321 recommendations have been approved through the security risk assessment process, and 1,391 of those recommendations have been completed.

Reclamation completed the following:

- New Directives and Standards for identifying and safeguarding information for Official Use Only and for certifying and procuring boat barriers.
- New Directives and Standards for uniforms.
- Interim Policy for purchasing firearms and explosives.

We implemented Personal Identity Verification-1 of the Homeland Security Presidential Directive-12 (HSPD-12), a Government-wide policy for common identification standards for Federal employees and contractors, and developed standard procedures for issuing and managing personal identity verification cards.

In April 2006, Reclamation promulgated the comprehensive Public Conduct Regulation required by P.L. 107-96. This rule enhances the security and safety of all Reclamation facilities by implementing legally enforceable public conduct standards and establishing Federal sanctions for violations. It also establishes procedures for closing, reopening, and creating special rules for individual facilities.

Reclamation collected, recorded, and investigated information for security and law enforcement related incidents, including suspicious activities. We shared information directly with dam and power transmission members and with appropriate intelligence agencies. Contract investigators and intelligence analysts also completed threat assessments and produced intelligence products to protect Reclamation and associated water and power transmission infrastructure.

We worked with other agencies to share information, including best practices, to protect critical infrastructure and to develop and refine risk assessment methodologies. We also worked with other Federal agencies and laboratories to enhance understanding of the effects of terrorist activities on dams and related resources.

We worked closely with the U.S. Department of Homeland Security and other agencies to develop the Federal Sector-Specific Critical Infrastructure Protection Plan for Dams as a key resource, which is part of the overall National Infrastructure Protection Plan developed by the U.S. Department of Homeland Security. This document will lead to

further interagency cooperation and coordination on all aspects of security for dams and related infrastructure.

In FY 2006, we established a Security Awareness Working Group to increase security awareness and education across Reclamation. This group is designing and implementing a comprehensive security awareness program to address all aspects of security, including operations.



Hoover Dam vehicle check site.

We developed an action plan to address the recommendations from the Office of Management and Budget's PART on the Security and Law Enforcement Program, and we implemented the five new performance measures established during the FY 2005 assessment.

For 2006, Reclamation received an appropriation of \$40 million for security, with congressional direction to collect another

\$10 million of project O&M costs for security guards and patrols from our project beneficiaries.

Future Challenges and Goals

In FY 2007, we will implement a reiterative Security Risk Assessment Program to periodically reassess Reclamation's 264 critical and project essential facilities. The program will provide a comprehensive security review every 6 years, a periodic security review every 3 years, and an annual security review. Reclamation will also continue to develop security-related policies, directives, and standards, including standards for training Reclamation guards and security professionals. Additionally, we will enhance the security of our facilities through implementing and enforcing our new public conduct regulations. We will continue to work closely with managing partners to implement effective security measures and will work with State, local, and tribal law enforcement entities to effectively promote law enforcement at our facilities.

Dam Safety

Dam safety activities are directly related to Reclamation's core mission of water and power delivery. The objectives of our Dam Safety Program are:

- To ensure that Reclamation facilities do not cause unreasonable risks to people, property, and/or the environment.
- To take appropriate action to reduce and manage risks in an efficient and cost-effective manner.

Reclamation is responsible for 472 dams and dikes that form a significant part of the water resources infrastructure for the 17 Western States. As these structures age, concern increases about their continued satisfactory performance. The 361 structures that could cause loss of human life or other significant losses through failure or misoperation are included in the Dam Safety Program.

FY 2006 Highlights

This year, we completed 44 comprehensive facility reviews; completed risk reduction activities at Grassy Lake Dam in Idaho, Keechelus Dam in Washington, Prosser Creek Dam in California, and Pineview Dam in Utah; continued ongoing risk reduction actions at Deer Creek Dam in Utah, Deer Flat Dam in Idaho, and Lauro Dam in California; and began risk reduction actions at Stony Gorge Dam in California.

In FY 2006, the Dam Safety Program was reviewed under the Office of Management and Budget's PART. The program received an overall rating of "effective"—the highest qualitative rating possible under this program. (Please see the "Management Accountability" section of this report for more information.)

Future Challenges and Goals

Reclamation has many multiyear contracts in place for the Dam Safety Program. The dam safety construction contracts are a major part of our continuing efforts to ensure that our structures do not present a safety risk to the public.

The Safety of Dams corrective action at Folsom Dam, California is, and will continue to be, the Dam Safety Program's highest priority because of the large population at risk downstream of the dam. Reclamation will continue to work with the USACE to find a joint resolution to complex and significant dam safety and flood control issues.

Reclamation continues to improve its emergency management capability by planning and conducting exercises in conjunction with Emergency Action Plans, Continuity of Operation Plans, Occupant Emergency Plans, the Emergency Notification System, and the Emergency Operations Center.

Information Technology Security Program

Reclamation uses Information Technology (IT) Security to maintain a reliable, high integrity, and appropriately confidential electronic information infrastructure. A strong IT Security Program is essential for conducting business efficiently and effectively in the 21st century. Reclamation's IT Security Program helps to ensure that our critical engineering, financial, personnel, and other mission-related information is accessible to those who need it, while remaining protected from unauthorized individuals and those with criminal intent.

Reclamation's IT Security Program is aligned with Department of the Interior (Interior's) program. The Federal Information Security Management Act (FISMA) principally governs the program.

FY 2006 Highlights

In FY 2006, Reclamation's IT Security Program made strong contributions to improve Interior's FISMA scorecard performance, particularly in awareness and role-based training, certification and accreditation of systems, and protection of critical cyber infrastructure.

In FY 2006, Reclamation instituted an Internal IT Security Assessment process to review our IT Security Program and systems. The review process will help identify and remedy system and programmatic weaknesses. This new process has already shown its potential in early reviews and will further improve our effectiveness.

We also maintain our existing and foundational IT Security Program components, including an active IT security training effort; risk identification, management, and mitigation components; incident

reporting and response capabilities; contingency planning; and procurement practices. The IT Security Program coordinated with Reclamation's SSLE Office to develop information handling and protection requirements for sensitive Reclamation information. The IT Security Program also employed the SSLE Office's resources to help ensure that the personnel responsible for Reclamation's IT systems and IT security were properly screened.

Reclamation made significant strides in adopting the newly released National Institute of Standards and Technology standards for IT security planning, security testing, and security certification. This included adjusting elements of the Reclamation certification and accreditation program to accommodate the new standards.

Reclamation completed management level IT security reviews (Internal Control Reviews) of all IT systems, as well as its IT Security Program. We also successfully completed an IT Security Program review led by Interior. The completed reviews found no significant weaknesses in management level IT security controls within Reclamation.

Future Challenges and Goals

Reclamation continues to face increasing pressure to design, fund, develop, and implement common, Government-wide IT solutions and to apply mandated IT requirements that do not always align well with our mission goals and objectives. Balancing these demands with legislative mandates, mission requirements, and changing threats will continue to be our greatest IT security challenge. The IT Security Program continues to focus on implementing cost-effective IT security solutions that support and enhance our infrastructure, communications, information management, operational capabilities, and mission.

Disaster Relief

Reclamation leads Interior's disaster recovery support to the USACE for ESF No. 3, Public Works and Engineering, under the National Response Plan. Reclamation coordinated the deployment of personnel from eight Interior bureaus and offices involved in the Katrina, Rita, and Wilma hurricane recovery operations.

From September 2005 through May 2006, Reclamation deployed, supported, and demobilized a total of 940 Interior employees in Louisiana, Mississippi, and Texas. Most of these personnel assisted the USACE as quality assurance inspectors in reviewing the installation of 195,000 temporary roofs and the removal of nearly 105 million cubic yards of debris. Interior employees constituted about 10 percent of the ESF-3 workforce during the Gulf Coast recovery.

Reclamation also provided technical assistance to the USACE for levee repair on Lake Pontchartrain and facilitated additional support from the

Reclamation employees were deployed to assist the USACE in quality assurance and overseeing temporary roofing, housing, and debris removal.



Thirteen days after Katrina made landfall, the emergency water purification unit sent from New Mexico converted seawater to potable water for the Biloxi Regional Medical Center. The 70,000 gallons per day was used to keep the hospital operational.



U.S. Geological Survey for light detection and ranging (LIDAR) imagery and flood stage monitoring.

The USACE has adopted the financial business practices, guidance materials, and spreadsheets Reclamation developed for the hurricane recovery operations as the standard for all other Federal agencies to use in compiling and submitting their billing packages to the USACE for reimbursement in future disaster operations.

Reclamation's Coordination Center continues to provide financial coordination, assistance, and guidance to other Reclamation employees who assemble billing packages, resolve reimbursement issues, and review and approve each billing package before sending it to USACE for payment. The USACE reimbursed all Reclamation Coordination Center costs associated with the operations and financial support of ESF-3.

Interior's ESF-3 has received approximately \$66.8 million in funding from the USACE for the 11 participating Interior bureau employee deployments during the 2005/2006 hurricane season. Of that amount, Reclamation will retain \$22.6 million; the remaining \$44.2 million will reimburse the other Interior bureaus.

Reclamation has also received approximately \$2.1 million in Federal Emergency Management Agency (FEMA) funding and approximately \$140,000 from the Office of Naval Research for water purification support.

Native American Program

Reclamation's Native American Program mission is to help make the benefits of Reclamation programs available to Indian tribes and to assist in fulfilling Interior's Indian trust responsibilities. The Native American Affairs Office (NAAO) provides central coordination and policy leadership for all Native American issues throughout Reclamation.

FY 2006 Highlights

The Native American Program provides technical and financial assistance to Indian tribes, institutions of higher education, national Indian organizations, and tribal organizations to increase opportunities for Indian tribes to develop, manage, and protect their water-related resources. Program activities include assisting tribes to better understand their water-related needs and helping them to develop their water resources, including

rural water supplies on Indian reservations. In FY 2006, NAAO provided approximately \$6.5 million to support tribal project requests, including such items as needs assessments and water management, quality, and measurement studies. Tribes performed some of this work under Title I and Title IV of P.L. 93-638, Indian Self-Determination Act. More than 50 tribes benefited from this technical assistance program.



Innovative well materials used at the Northern Cheyenne Tribe's Tongue River Enhancement Project in Montana.

Reclamation also continued to participate in the Secretary of the Interior's Indian Water Rights Settlement activities, providing approximately \$1.5 million for 17 Indian water rights negotiation teams and 9 water rights settlement implementation teams.

Future Challenges and Goals

Indian tribes continue to experience a tremendous need for adequate water supply infrastructure to ensure the health

and safety of reservation populations and to provide a base for economic development. While Reclamation cannot solve the problem of inadequate tribal water supply infrastructure alone, we will continue to assist federally recognized tribes located within the 17 Western States.

Recreation

Reclamation has more than 300 recreation sites that accommodate more than 90 million visits annually on more than 8 million acres of land and water. When possible, Reclamation enters into agreements with non-Federal managing partners to manage the recreation areas at our projects. In other instances, larger projects have been designated as National Recreation Areas by the Congress and are, in turn, managed by other Federal agencies with recreation expertise, such as the National Park Service. Some of the Reclamation project areas that are managed by other Federal agencies are Lake Powell (Glen Canyon National Recreation Area), Lake Mead National Recreation Area, Lake Roosevelt National Recreation Area, and Flaming Gorge National Recreation Area. Reclamation has 21 visitor centers on project lands.

FY 2006 Highlights

To determine how Reclamation can assist in the future success of our non-Federal recreation management partners, we completed comprehensive guidelines for estimating future recreation demand. Reclamation will use the results of studies using the guidelines to help direct future decisions on managing recreation.

During April 2006, new exhibits were installed at the Grand Coulee Dam Visitor Center that interpret Grand Coulee's role as one of the main irrigation, flood control, and hydroelectric dams in the Nation. Exhibits also address the effects the dam has had on various groups of people, including Native Americans and early settlers. Many of the exhibits are "hands-on," including a virtual tour of the dam and an interactive game on operating the dam. Exhibits are accessible and designed to appeal to all ages.

Future Challenges and Goals

Recreation and tourism is one of the largest industries in the Western United States and the second largest employer nationwide. Reclamation reservoirs and lands are primary recreation destinations for many Americans and foreign visitors. Recreation pursuits in and around reservoirs include hunting, camping, skiing, boating, fishing, and other water sports and activities. National surveys and statistics show that water-based recreation activities are among the most popular recreation experiences.

The steady increase in visitation is a challenge to public agencies that provide recreation facilities at Reclamation reservoirs. We are also concerned about providing accessible opportunities to all visitors. To ensure that Reclamation and our partners provide equal opportunities to participate, Reclamation initiated a 10-year plan in 2000 to monitor accomplishment toward providing facilities and programs that comply with accessibility laws. Reclamation and our non-Federal



Because Reclamation areas play host to many kinds of birds, including some that are endangered, "Birding" or bird watching often joins more traditional recreational activities at many Reclamation dams and reservoirs.



partners are cooperating to increase management efficiency; however, financing is limited for new services and recreation facilities.

Reclamation continues to pursue the goal of having all Reclamation-owned recreation sites managed by non-Federal partners, such as State and local agencies. Reclamation is focused on ensuring that all new contracts provide appropriate facilities and services necessary to meet the future public demand.

C.A.S.T. for Kids

Catch a Special Thrill (C.A.S.T.) is a nonprofit foundation officially created in 1992 in support of an extraordinary, outdoor event that teams the sponsors with area youngsters for a day of fishing sportsmanship. Reclamation works with the C.A.S.T. for Kids Foundation; various State, city, county and Federal agencies; and several Bass Anglers Sportsman Society Federations to provide the pleasures of fishing to children with disabilities. For some kids, this is their first experience fishing, or even spending the day on the water. The young anglers are educated about boating safety, angler ethics, and the importance of natural resources such as fish and water. During C.A.S.T. for Kids events, the children learn a skill they can use for the rest of their lives, and the volunteers learn an important lesson about life and the fulfillment of giving back to their community.

Approximately 250 Reclamation volunteers from the Pacific Northwest Region participate in six different C.A.S.T. events and work closely with the C.A.S.T. for Kids Foundation and other public and private sponsors to ensure fun-filled events.



Fish and Wildlife

Reclamation has responsibilities for fish and wildlife resources at its projects, based upon individual project authorizations and the mandates of other Federal statutes, such as the ESA. While delivering water and generating power is our primary mission, we also work to minimize impacts on fish and wildlife in cooperation with the U.S. Fish and Wildlife Service (FWS), National Oceanic and Atmospheric Administration National Marine Fisheries Service (NOAA-Fisheries), State fish and wildlife agencies, and others. Habitat provided or supported by Reclamation's projects can contribute significantly to fish and wildlife resources.

FY 2006 Highlights

Following are several examples of how Reclamation contributed to fish and wildlife resources in FY 2006:

- Implemented Reasonable and Prudent Alternatives for the Modified Roosevelt Dam Biological Opinion on impacts to the endangered Southwestern willow flycatcher and the requirements of the Gila River Basin Biological Opinion on impacts to imperiled native fishes.
- Complied with ESA responsibilities for several projects in the Upper Colorado Region, including the O&M of the Middle Rio Grande Project, Animas-La Plata Project, Pecos River Operations, and Glen Canyon Dam Adaptive Management Program.
- Led the multi-agency Lake Mohave Native Fish Work Group in the lower Colorado River basin, with the release of an estimated 10,000 fishes into Lake Mohave in 2006.
- Augmented flow from Reclamation's Snake River Project. We collaborated with the USACE and BPA to improve conditions for 12 anadromous fish species and 1 resident fish species in the Columbia and Snake River systems, as required by ESA biological opinions.

- Completed a final EIS for the Platte River Recovery Program with the FWS in May 2006 and a signed Record of Decision in September 2006. The Governance Committee Alternative is the preferred alternative. If implemented, this alternative would improve habitat conditions in the Central Platte Habitat Area by increasing target flows by an average of about 130,000 to 150,000 acre-feet a year and restoring habitat of wet meadow areas and areas of wide, unvegetated river channel.
- Implemented the Central Valley Project Improvement Act's requirements, making all reasonable efforts to double the natural production of six species of anadromous fish. Reclamation is also supplying water to Federal and State refuges and other migratory waterfowl habitats in the Central Valley and mitigating impacts of the Central Valley Project to other fish and wildlife.
- Improved juvenile and adult fish health through the California Trinity River Restoration Program activities. Increasing summer baseflows from 300 cubic feet per second to 450 cubic feet per second has improved temperature characteristics for juvenile steelhead, increasing overall health and reducing mortality.



Reclamation's stewardship of the West's water resources means we also have a major responsibility to the West's fish and wildlife.

Future Challenges and Goals

Recent court decisions in the Pacific Northwest regarding the adequacy of biological opinions issued by the FWS and NOAA-Fisheries will create challenges for compliance with the ESA. Reclamation



seeks to comply with the requirements of the ESA, while protecting local economies and preserving natural resources and ecosystems through the effective use of water.

Management Accountability

Managing to Perform Our Mission More Effectively

At Reclamation, management accountability is an ongoing commitment to improve business processes and customer satisfaction. Reclamation is dedicated to achieving management excellence through increased accountability and is improving program management, performance reporting, and financial accountability through increased leadership, expanded technical expertise, efficient operations, and improved customer service.

For FY 2006, all senior executive service (SES) member performance agreements are tied to Interior's strategic goals, Reclamation's Government Performance and Results Act of 1993 (GPRA) goals, the Presidential Management Agenda (PMA), and building collaboration and partnerships. SES members are evaluated on accomplishing specific performance targets to clearly measure their contribution to organizational goals and mission accomplishment.

Reclamation also implemented a new multilevel performance system in calendar year 2005, in accordance with Interior's new non-SES Performance Management System. All performance plans include GPRA and/or strategic goals, which establish a recognizable link between the employees' plan and Reclamation's mission goals.

Getting to Green: President's Management Agenda Scorecards

Office of Management and Budget (OMB) established an Executive Branch Management Scorecard, updated annually, to monitor department status and progress in attaining PMA goals. The objective of the scorecard is to strengthen agency accountability. Interior adapted this concept and developed its "Getting to Green" Scorecard to monitor the PMA progress of each bureau and office. Reclamation worked toward supporting PMA and mission goals, including improving internal control

Reclamation's Getting to Green Scorecard Ratings, as of September 30, 2005

Strategic Management of Human Capital	Green
Expanding E-Government	Green
Competitive Sourcing	Yellow
Budget and Performance Integration	Yellow
Improving Financial Performance	Yellow
Real Property	Green

Reclamation's Getting to Green Scorecard Ratings, as of September 30, 2006

Strategic Management of Human Capital	Green
Expanding E-Government	Green
Competitive Sourcing	Yellow
Budget and Performance Integration	Yellow
Improving Financial Performance	Yellow
Real Property	Red

processes by implementing revised OMB Circular A-123, Management's Responsibility for Internal Control. Reclamation ratings for the key areas are presented in the table above. Interior also added three additional scorecards in FY 2006: Transportation Management, Energy Management, and Environmental Stewardship.

Managing Human Capital to Maintain a Quality Workforce

As a world leader in developing and managing water resources, Reclamation requires a world-class workforce. Reclamation's highly competent and skilled staff of about 6,000 employees operate and maintain our vast water and power infrastructure; manage and support our technical programs; and address financial, acquisition, information technology, and business management challenges. Under the *Managing for Excellence* initiative, Reclamation is working on evaluating functional areas related to managing issues and challenges, existing infrastructure, and future construction. The outcome of these team initiatives and subsequent decisions by Reclamation management will be the focal point of our workforce and succession planning efforts in the future.

One of the *Managing for Excellence* teams is developing a workforce/succession plan and action plan for meeting the challenges we face in the future. This plan will update the previous versions of the Reclamation Workforce Plan, and Reclamation will update the plan

annually. We still face many of the same challenges we have encountered in managing our workforce and market competition, including:

- Retirement rates are increasing.
- Qualified engineers and scientists are difficult to attract.
- Candidates are less willing to relocate.
- A diverse labor force is difficult to recruit and retain.

Another team is identifying critical positions where we need competencies in collaboration. The team is refining position descriptions to include these competencies and will work with Reclamation's Human Resource offices to ensure that collaborative competencies are a part of each employee and manager's skill set.

Other initiatives to meet with workforce and succession challenges include a Reclamation-wide Outreach and Recruitment Team; Targeted Recruitment Plans for mission-critical occupations, as well as for people with disabilities; and the Student Educational Employment Program and the Federal Career Intern Program. Reclamation currently employs 254 students and 67 Federal career interns.

Expanding E-Government to Facilitate Access to Information and Services

Federal agencies are enhancing the delivery of IT services; modernizing IT and communications capabilities; and improving IT security, data safeguards, and capital planning results through the adoption and expansion of the electronic government (E-Government) principles and best practices under the PMA. Interior's E-Government "Getting to Green" Scorecard rating incorporates these goals and objectives for FY 2006, and Reclamation received "green" ratings from Interior for its E-Government programs and activities based on the progress made to date. Reclamation actively participated in several Government- and enterprise-wide initiatives to simplify, standardize, and improve infrastructure and communications capabilities (e.g., Enterprise Services Network, Enterprise Messaging System, and Active Directory). These initiatives are designed to improve system interoperability, knowledge sharing, and other operational efficiencies upon completion. Reclamation plans to build on these systems and create opportunities to operate efficiently through technology enhancements and streamlined business practices.

In FY 2006, Reclamation spearheaded and completed Interior's Water Resources Management Framework. Reclamation also initiated the first of several modernization blueprints for dam safety. These blueprints and the framework will continue to leverage existing IT capabilities to their maximum potential and to develop and deploy more efficient and customer-centered IT capabilities and services. Reclamation received high marks for leading in the water resources management area, with opportunities for collaboration and information sharing across Government. Other bureaus and offices within Interior, as well as non-Interior agencies and organizations, are expected to participate in and contribute to the water resources management initiative over the next few years.

Further, Reclamation received “green” scores from Interior for adopting and applying best practices in the areas of IT investment management and IT security. Reclamation continues to build upon these successes and is leading the way in complying with IT investment management practices and standards that the Government Accountability Office (GAO) prescribes. More importantly, Reclamation continues to manage IT investments effectively and has consistently kept cost variances for major IT investments below 10 percent, resulting in high marks from OMB. Reclamation also expects its IT Security Program to continue receiving high marks from Interior for complying with IT security guidance, investing in network and auditing security technologies, developing new techniques to monitor security activities, and supporting training programs to enhance skills of IT security personnel and general users.

Using Competitive Sourcing to Obtain the Best Value

Competitive sourcing is a tool for use in ensuring that citizens receive the best value from the Government. Competitive sourcing does not mean that functions will always be competitively sourced. Instead, competitive reviews provide a disciplined, periodic way to review and compare our current operations with alternatives: Are we the best we can be? Might a restructuring generate a more efficient organization? Might contracting with a provider free up resources that can be reallocated to other priorities? Some competitive reviews have produced substantial savings. Competitive sourcing involves conducting public-private competitions that compare the performance of a Government organization with that of a private sector or other non-Federal organization. Conducting a public-private competition is a highly structured process to ensure that both the

private and public sectors compete on a level playing field. For example, Reclamation initiated a formal competitive sourcing study of the Centennial Job Corps Center in Nampa, Idaho. We compared a proposed “most efficient organization” restructuring with private-sector options. Our approach produced savings of approximately \$400,000 per year. The “most efficient organization” was implemented, with its second performance year ending June 30, 2006.

Reclamation issued a formal notice announcing four streamlined (65 or fewer full-time equivalents) competitions for all operations at the Job Corp Civilian Conservation Centers (JCCCC) on September 29, 2005. The competitions were completed December 22, 2005. As determined by the cost comparison of the agency performance to the private sector, the most cost-effective source of the required services was continued performance by the Government employees in the most efficient organization. The performance period for these studies is 1 base year with 4 option years. The streamlined studies were conducted by the Competitive Sourcing Program Office, under the Denver Acquisition and Assistance Management Division. The most efficient organizations were implemented at all four centers, effective July 1, 2006.

Integrating Budget and Performance

Reclamation is building on its efforts to enhance budget and performance integration in line with Interior's initiative. During the quarterly review meeting with Interior, Reclamation's senior leadership provides an up-to-date forecast on meeting its published annual performance targets by the end of the fiscal year. When reaching a performance target may be in question, senior leadership identifies corrective actions that can be taken.

Reclamation also estimates the annual funding level against each end outcome goal during the quarterly reviews. Both Reclamation's budget and performance documents incorporate references to these outcome-oriented goals and measures and to the information used in quarterly reviews with senior leadership. Reclamation uses information compiled during our baseline analysis of several new measures to further develop and support our budget request. In addition to our budget documents, Reclamation publishes performance targets and goals in our operating plan.

Reclamation continues to refine its Activity Based Costing/Management (ABC/M) system. During the 2008 budget formulation's initial stages, Reclamation developed the costs of performance measures, based on project level activities.

Reclamation is reviewing and revising its "costing" capability to the measure level based on Interior's *Strategic Plan*. Specifically, Reclamation will tie program and projects costs to the *Strategic Plan* goals. This will be done by chartering a team that will focus directly on this effort: the Budget Performance Integration Improvement (BPII) Team. The BPII team will be comprised of a cross functional team of managers and program staff. The team will provide recommendations and refinements, goals, performance, and activity based costing measures including per unit costs at the project level for leadership review.

Currently, managers at all levels within Reclamation can extract reports on funding and performance data. Reclamation is improving its reporting capability to support using refined ABC/M data to better estimate marginal funding changes associated with changes in an end-outcome and intermediate performance measure target.

Real Property Asset Management

With over 77 percent of Interior's constructed assets, Reclamation is a capital-intensive organization which stores, delivers, and generates water and power products and services to a wide sector of the public and has a major stewardship role in managing its infrastructure and supporting assets. In any capital-intensive industry, effective asset maintenance is both a critical activity and a major source of cost for the organization. In addition, Reclamation is faced with a continual aging of its infrastructure, some of which is over 100 years old. The ultimate goal of asset maintenance is to ensure reliable delivery of products and services at the least life-cycle cost. Reclamation's policy is to allocate human, physical, and financial resources for the maintenance of its mission-critical assets to ensure sustained and reliable delivery of water and power to the public, and to serve other authorized project purposes, with emphasis on safety, cost effectiveness, and minimal environmental impact. Reclamation conducts reviews of its facility assets to assess their condition, identify and document problems, and establish corrective actions for any deficiencies.

In FY 2006, Reclamation received a rating of red in real property asset management from Interior due to the lack of accuracy and completeness of its inventory at fiscal year end and the failure to finalize and sign the asset

management plan. Reclamation has made significant progress in addressing Interior's issues with its inventory and anticipates completing the necessary actions by December 7, 2007, to improve its rating to yellow for FY2007. Reclamation will be reporting progress on its inventory activity to Interior on a quarterly basis. The financial records verification and validation project in relation to the asset inventory will be completed by April 30, 2008.

Using the Program Assessment Rating Tool

The Office of Management and Budget's Program Assessment Rating Tool is a systematic process to develop program performance ratings and use that information to make budget decisions. PART is comprised of assessment criteria on program performance and management. Each year, programs comprising approximately 20 percent of an agency's budget must be reviewed using PART, with the goal of reviewing all programs within 5 years. Programs receive a score of up to 100.

Determining the Rating

The answers to specific questions in the PART translate into section scores, which are weighted as follows to generate an overall score: program purpose/design, 20 percent; planning, 10 percent; management, 20 percent; and results accountability, 50 percent. PART scores are translated into qualitative ratings based on the ranges shown on page 39. Because overall scores could suggest a false degree of precision, only the overall ratings are made available to the public.

Rating	Range
Effective	85-100
Moderately effective	70-84
Adequate	50-69
Ineffective	0-49

Regardless of the overall score, a rating of "Results Not Demonstrated" is given when programs do not have acceptable long-term and annual performance measures. A program also receives a rating of Results Not Demonstrated when it lacks baselines and performance data to indicate how it has been performing. Program ratings are discussed on the following page.

In FY 2006, the Central Valley Project Improvement Act (CVPIA) and CALFED Bay-Delta programs underwent full PART assessments. Both programs developed performance metrics that will be used to report performance and support ongoing efficiency improvements in the programs. Final recommendations for program improvements will be finalized as part of the FY 2008 President's Budget.

CVPIA—Adequate

CVPIA seeks to achieve a reasonable balance among competing demands for use of Central Valley Project water, including the requirements of fish and wildlife and agricultural, municipal and industrial, and power contractors. The act also establishes the Restoration Fund, which is the primary funding resource to accomplish these purposes. Reclamation has primary responsibility for Restoration Fund management and the engineering, operational design, and construction related Program purposes. The FWS has primary responsibility for the biological purposes of the program. In the PART, the program scope is defined as those elements of CVPIA eligible for funding from the Restoration Fund.

CALFED Bay-Delta—Adequate

The purpose of the CALFED Bay-Delta Program is to develop and improve water management for beneficial uses of the Bay-Delta system. To achieve this purpose, CALFED comprehensively addresses problems of the Bay-Delta system within each of four resource categories: ecosystem quality, water quality, water supply reliability, and levee system integrity.

The CALFED Bay-Delta Program is a collaborative effort among Federal, State, and local agencies to coordinate and focus limited resources on addressing the four program objectives. The scope of this PART included only the work being accomplished by Reclamation.

Two components of the Water Supply/Management Program also completed work associated with the FY 2006 PART process but did not undergo full PART assessments. The Environmental Mitigation and Protection component of the program completed scoping requirements and draft performance measures, and the Planning and Construction component, originally assessed in FY 2004, continued its work to develop, refine, and populate performance measures in preparation for a reassessment in FY 2007.

In FY 2005, the planning and construction components of Reclamation's Dam Safety, Site Security, and the Water Management/Supply - O&M Programs were assessed by PART.

Dam Safety—Effective

The Dam Safety Program ensures that Reclamation water storage facilities do not present unreasonable safety risks to the public, property, and/or the environment. The program monitors and periodically evaluates the physical status of our facilities and, based on the results of those reviews, assesses the risk of any threat to loss of life, property damage, or loss of project benefits. The program then considers options of ameliorating that risk, weighs the cost and benefits, and acts accordingly.

Site Security—Moderately Effective

The Security and Anti-Terrorism Program protects Reclamation's dams and related facilities from terrorist attack and other plausible threats. The program's key objective is to reduce security-related risks through a combination of Preparedness, Prevention, Protection, and Response.

Operations and Maintenance—Adequate

The Water Management/Supply - O&M Program ensures the O&M of project features to deliver water to irrigators and municipal users and to provide storage to help mitigate flooding (hydropower operations, along with other purposes, but the Hydropower PART assessed that function). This program performs direct physical O&M and other related activities to ensure reliable project operations.

FY 2006 Performance Measure Highlights



Delivering water for agriculture is one of the uses measured for the Water Delivery Performance Goal.

The Government Performance and Results Act of 1993 requires Federal bureaus to establish performance goals, set annual accomplishment targets, and report annual accomplishments. Reclamation's goals stem from Interior's FY 2003–2008 *Strategic Plan*. All of Reclamation's performance information is now incorporated into Interior's unified strategic and annual plans and reported in Reclamation's Annual Operating Plan. This is found on Reclamation's GPRA Web site at <http://www.usbr.gov/gpra/>. Eight of our goals that best reflect our mission and key accomplishments are highlighted in this annual report.

Delivering Water

Reclamation has four key goals for delivering water: (1) the Water Delivery Performance Goal, (2) the Facility Reliability Performance Goal, (3) the Increase Water Availability Performance Goal, and (4) the Control Colorado River Salt Performance Goal.

The Water Delivery Performance Goal measures the amount of water releases or diversions from Reclamation-owned and -operated facilities. Water uses include agriculture, municipal and industrial uses, fish and wildlife, and other contracted and authorized purposes. This goal does not include water delivered from district operated works or facilities where Reclamation does not have substantial operational control. In FY 2006, Reclamation delivered approximately 30.8 million acre-feet of water to meet contract obligations and other water resource needs.

Goal:	Annual Target	Annual Accomplishment
Deliver Water		
Acre-feet of water delivered in million acre-feet (MAF)	28.0	30.8

The Facility Reliability Performance Goal measures reliable delivery of water from our facilities. We continue to monitor our dams and associated water facilities using a facility rating system. This system incorporates

operations, maintenance, dam safety, and management criteria to evaluate the facility's reliability. The FY 2006 ratings continue to show that nearly all of Reclamation's facilities are in the fair and good ranges.

Goal:	Annual Target	Annual Accomplishment
Facility Reliability		
Percent of dams with a good to fair reliability rating	94%	98%
Percent of associated features with a good to fair reliability rating	93%	97%

The Increase Water Availability Performance Goal measures the amount of water made available by Reclamation-funded projects with cost-sharing arrangements. Reclamation increased the amount of water available for use by 47,739 acre-feet through completing major phases of rural water distribution projects, water reuse and recycling, and aquifer ground water investigations. Projects were funded through grants, reimbursable agreements, direct pay contracts, and other financial arrangements.

This goal does not measure the actual acre-feet of water delivered by the project each year. Instead, it measures the potential acre-feet of water that could be delivered by the project based on estimated averages found in modeling and project construction agreements.

Goal:	Annual Target	Annual Accomplishment
Increase Water Availability		
Increase in acre-feet of water availability	34,349	47,739

The Control Colorado River Salt Performance Goal measures the tons of salt controlled or prevented from loading into the Colorado River each year. The Colorado River Salinity Control Program's goals are to maintain salinity below the water quality standards set for the Colorado River Basin and to reduce the economic damages of more than \$300 million that occur each year in the Lower Basin. This year, additional salinity control measures funded by Reclamation will prevent about 22,000 tons of salt from entering the Colorado River each year. Reducing the amount of water applied to saline soils is the single most cost-effective salinity

control measure. Reclamation has been able to reduce Colorado River salt control project costs from an average of \$70 per ton removed in the 1980s to an average of \$30 per ton today.

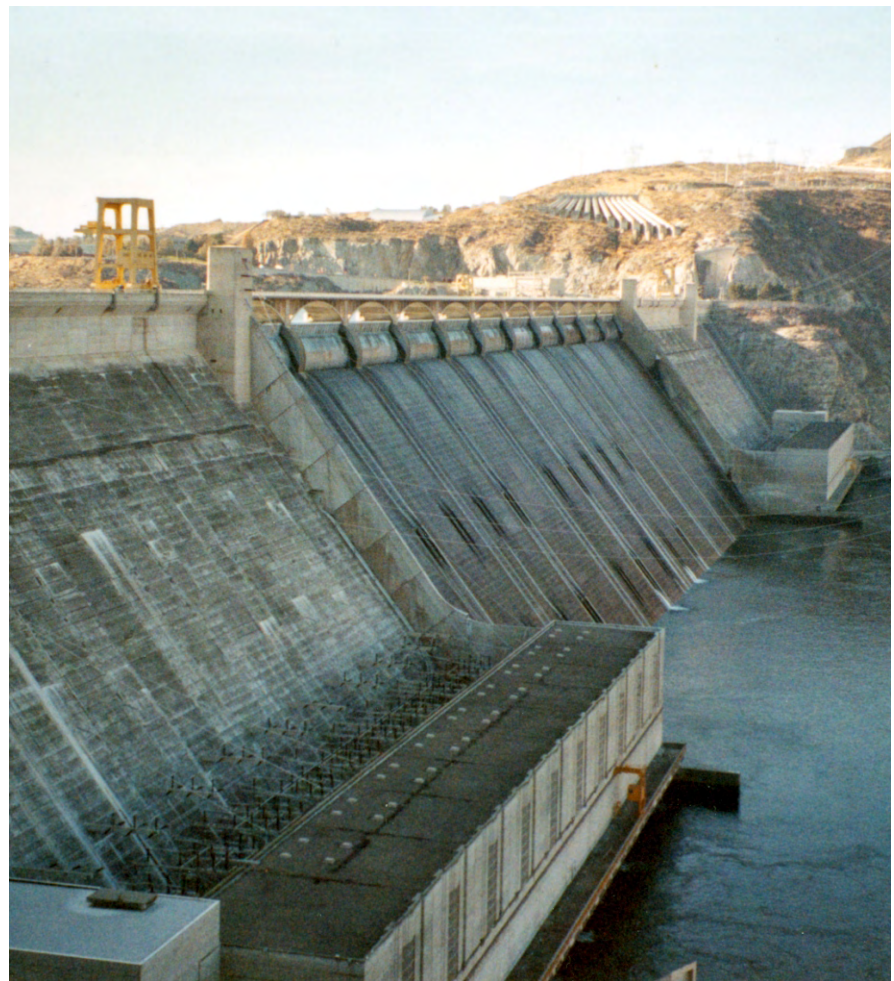
Goal:	Annual Target	Annual Accomplishment
Control Colorado River Salt		
Tons of salt loading eliminated	21,000	22,000

Generating Hydropower

Reclamation has three key hydropower goals and specific accomplishment activities this year: (1) the Power Production Cost Performance Goal, (2) the Forced Outage Performance Goal, and (3) the Facility Reliability Performance Goal.



Reclamation is successfully meeting its Hydropower Program goals. Grand Coulee Dam and switchyard are part of the hydropower generating system.



Goal:	Annual Target	Estimated Accomplishment
Power Production Cost		
Cost-effective power production	7.15%	≤7.21%

Goal:	Annual Target	Actual Accomplishment
Forced Outage		
Forced outage factor less than or equal to industry average	2.5%	1.20%

Goal:	Annual Target	Actual Accomplishment
Facility Reliability Rating—Power		
Percent of hydropower facilities in fair to good condition	96%	100%

Reclamation's Hydropower Program is successfully meeting its benchmarking goals. We compare our forced outage factor against industry performance. This year, our forced outage factor was below the current industry average of 2.5 percent. For our cost measure, this year we started to measure power delivery cost in the present year against a 5-year rolling average. We estimate the accomplishment for this year to be 7.21 percent or below in the 5-year rolling average increase of powerplant production costs, which is in line with our target. In addition, we have also performed all of our scheduled comprehensive facility reviews and have completed an equipment condition assessment for major power train components at each of our hydropower facilities.

Reclamation has established an internal rating system of facility reliability. In 2003, the Hydropower Program established a baseline to determine what percentage of Reclamation facilities ranked in fair to good condition. Since that year, 100 percent of facilities have been rated fair to good.

Fiscal Year 2006 Annual Assurance Statement on Internal Control

The Bureau of Reclamation is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA). Reclamation has conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with the Office of Management and Budget's (OMB) Circular A-123, *Management's Responsibility for Internal Control*, dated December 21, 2004. The objectives of this assessment were to ensure that:

- Programs achieved their intended results;
- Resources were used consistently with agency mission;
- Resources were protected from waste, fraud, and mismanagement;
- Laws and regulations were followed; and
- Reliable and timely information was maintained, reported, and used for decision-making.

In performing this assessment, Reclamation relied on the knowledge and experience management has gained from the daily operation of its programs and systems of accounting and administrative controls, and information obtained from sources such as internal control assessments, Office of Inspector General (OIG) and Government Accountability Office (GAO) audits, program evaluations and studies, audits of financial statements, and performance plans and reports.

Based on the results of the evaluation, Reclamation can provide reasonable assurance that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2006, were operating effectively and no material weaknesses were found in the design or operation of the internal controls.

In addition, Reclamation conducted its assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of Appendix A of OMB Circular A-123, and the Chief Financial Officers Council's Implementation Guide dated July 31, 2005, as implemented by the Department. The assessment focused on the specific financial reports and the related financial statement line items identified by the Department as material to the consolidated Department of the Interior financial reports. Based on the results of this assessment, Reclamation can provide reasonable assurance that its internal control over the specific financial reports and related line items identified by the Department as material to the consolidated Department of the Interior financial reports were suitably designed and operating effectively as of June 30, 2006, and no material weaknesses were found in the design or operation of the internal control over financial reporting. Further, subsequent testing through September 30, 2006, did not identify any reportable changes in key financial reporting internal controls.

Corrective actions for recommendations related to the material weakness on controls over the implementation of new accounting principle from the FY 2005 audited financial statement have been completed. The existence of the material weakness does not prevent Reclamation from providing reasonable assurance on the effectiveness of its internal control taken as a whole.

I also conclude that Reclamation's information technology systems generally comply with the requirements of the Federal Information Security Management Act (FISMA), and Appendix III of OMB Circular A-130, *Management of Federal Information Resources*.

Further, I conclude that Reclamation substantially complies with the three components of the Federal Financial Management Improvement Act (FFMIA): Financial system requirements, Federal accounting standards, and the U.S. Standard General Ledger at the transaction level.

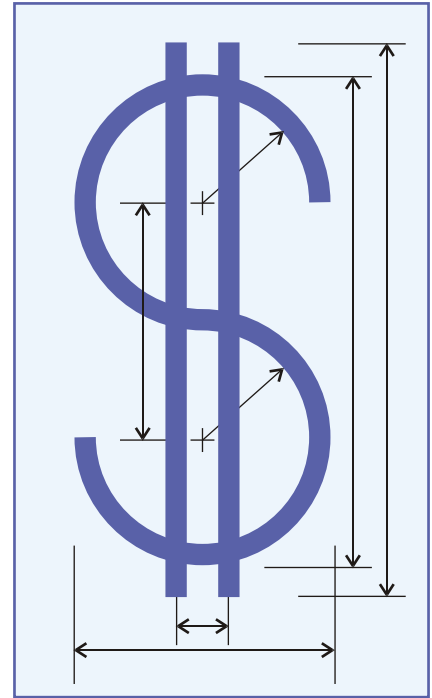
Financial Analysis

This section provides additional information about the Financial Statements and Notes, including how we have improved financial accountability.

Financial Statements

Reclamation's management is responsible for ensuring the integrity and objectivity of financial information in our financial statements. The financial statements and supplemental schedules in this year's annual report reflect the financial position and results of our operations and comply with the Chief Financial Officers Act of 1990, Government Management Reform Act of 1994 (GMRA), and 31 U.S.C. 3515(b). The statements' requirements are for a component of the United States Government (OMB Circular A-136, p. 118, section 11.1J). The statements have been prepared from Reclamation's books and records in accordance with Generally Accepted Accounting Principles (GAAP) for Federal entities and the OMB-prescribed formats. Reclamation uses these statements not only for financial reports but also to monitor and control budgetary resources.

The integrity of these statements is supported by our audit results, which an independent, certified public accounting firm conducted under contract with Interior's Office of the Inspector General (OIG). Reclamation achieved an unqualified audit opinion again this year. Unqualified means financial statements are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States. Since 1995, Reclamation has received unqualified audit opinions on all reports issued, which is a testament to our strong commitment to provide accurate and timely financial information. To ensure that future financial statements achieve unqualified audit opinions, we use internal control efforts, which comply with FFMIA and OMB Circular A-123, "Management's Responsibility for Internal Control." For example, we implemented improved internal controls over financial reporting and resolved an outstanding material weakness. Moreover, we have the discipline and staffing required to produce these audited financial statements, demonstrating that management is dedicated to improving



financial management and complying with applicable laws and regulations. These financial statements allow the Congress, external partners, and the general public to monitor how Reclamation uses the resources the Congress and our partners provide.

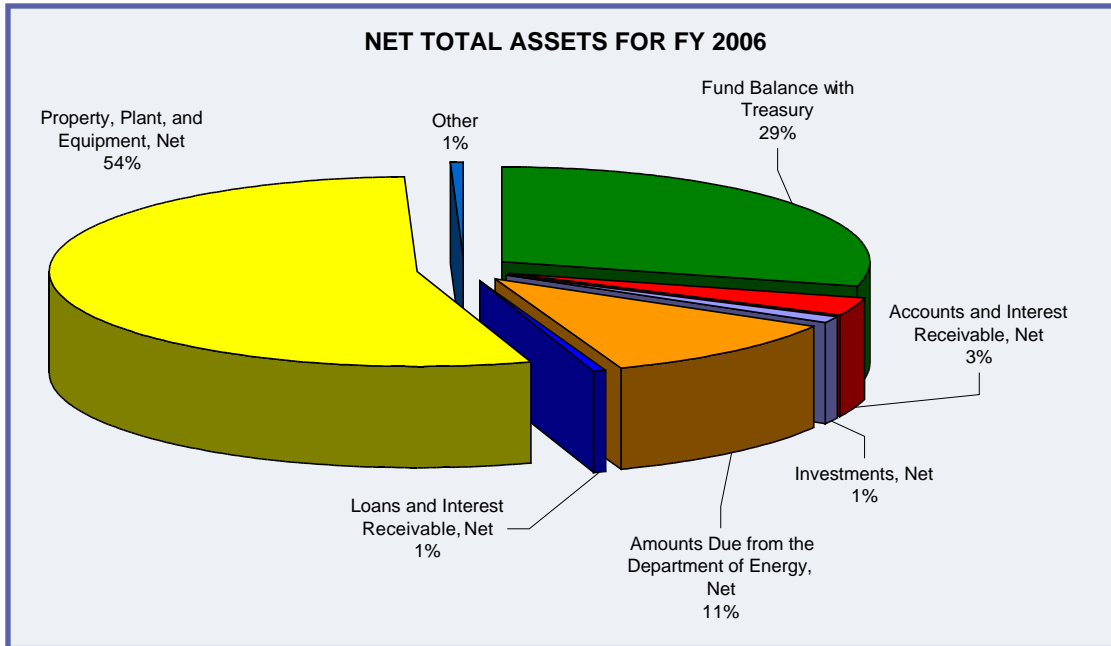
Reclamation is committed to improving financial performance to make certain that management receives accurate and timely financial information. We strive for innovation and further improvements to address future challenges and meet the Secretary of the Interior's key business principles of increasing accountability and advancing modernization/integration, as well as the public's increasing demand for better business management practices, improved efficiency, financial transparency, and mission accountability.

Consolidated Balance Sheet

Net Position: The Balance Sheet displays Assets, Liabilities, and Net Position. Our Net Position increased by \$1.2 billion in FY 2006. This increase is \$605 million less than the Net Position increase in FY 2005.

Total Assets FY 2006: Total Asset value is \$24 billion, an increase of \$1.3 billion over the FY 2005 Total Asset value. The table below shows the change by asset type.

Net Change in Assets (In Thousands)			
Type of Asset	FY 2006	FY 2005	Net Change
Fund Balance with Treasury	7,030,401	6,090,731	939,670
Accounts and Interest Receivable, Net	693,325	857,433	(164,108)
Investments, Net	322,045	-	322,045
Amounts Due from the Department of Energy, Net	2,631,887	2,458,075	173,812
Loans and Interest Receivable, Net	157,286	146,468	10,818
Property, Plant, and Equipment, Net	13,071,874	13,015,525	56,349
Other	142,359	199,838	(57,479)
Total	24,049,177	22,768,070	1,281,107



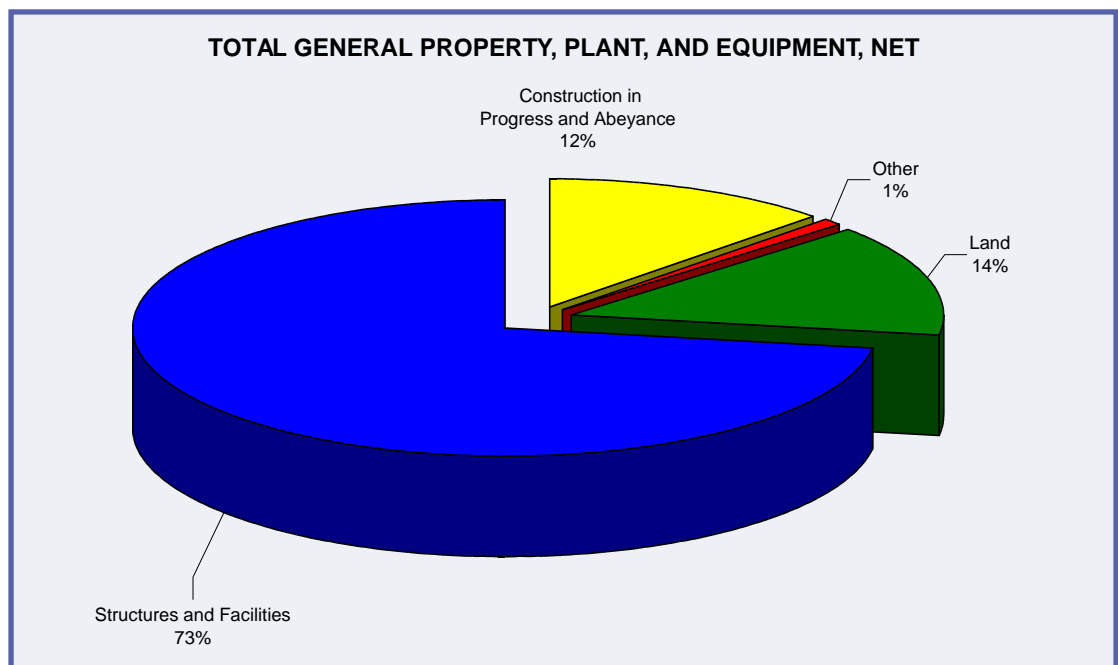
Fund Balance with Treasury: The Fund Balance with Treasury represents all undisbursed balances in Reclamation's accounts, including funds awaiting disbursement for goods and services received. The Fund Balance includes the Reclamation Fund (\$5.7 billion) and other unavailable (restricted) receipt fund balances. The Congress allocates most of our annual appropriations out of the Reclamation Fund. In accordance with Reclamation law, revenues received from our beneficiaries, including irrigation districts, municipalities, and power customers, for the reimbursable features of Reclamation's project costs are returned to the Reclamation Fund. Certain oil and gas and timber royalties are considered accretions to the Reclamation Fund. These funds are deposited into the Reclamation Fund due to legislative requirement and for which no matching costs were incurred by Reclamation.

The change in Fund Balance with Treasury is primarily the result of increased collections attributable to an increase in oil and gas production.

In FY 2006, Reclamation reported \$322 million in Investments for the Lower Colorado River Basin Fund and San Gabriel Restoration Fund. The Investments consist of nonmarketable, market-based securities issued by the Federal Investment Branch of the Bureau of the Public Debt. These securities are not traded on any securities exchange, but mirror the prices of marketable securities with similar terms. Interest on investments is accrued as it is earned. In FY 2005, no balance for Investments was reported, as the Investments had been redeemed before the reporting date.

General Property, Plant, and Equipment: Reclamation’s property, plant, and equipment (PP&E) consists of an extensive infrastructure of dams, powerplants, pumping stations, canals, and other water delivery systems used in Reclamation's day-to-day operations. These assets are reported as General PP&E in accordance with Federal GAAP. Our major PP&E asset categories are: Structures and Facilities, Land, Construction-in-Progress and Abeyance, and Other (i.e., equipment, vehicles, buildings, and internal use software).

Reclamation's PP&E \$13.1 billion balance accounts for approximately 75 percent of Interior's PP&E total reported in its annual report.



Total Liabilities: FY 2006 Total Liabilities are \$2.9 billion, a \$99 million increase from FY 2005. Most of the \$99 million increase results from Reclamation recording a liability to the General Fund liability for appropriations Reclamation receives from the General Fund that are expended for reimbursable project purposes. Reclamation is a bureau of the executive branch of the United States Government, a sovereign entity. Federal agencies, by law, cannot make any payments unless the Congress has appropriated funds. Accordingly, unfunded liabilities reported in the statements cannot be liquidated until the Congress enacts an appropriation, and ongoing operations are subject to appropriate appropriations. Reclamation's funded liabilities are paid out of funds currently available to Reclamation. Unfunded liabilities consist primarily of environmental and

Net Change in Liabilities (In Thousands)			
Type of Liability	FY 2006	FY 2005	Net Change
Accounts Payable	242,877	226,193	16,684
Debt	95,141	96,811	(1,670)
Accrued Employee Benefits and Payroll	69,130	70,343	(1,213)
Advances, Deferred Revenue, and Deposit Funds	502,335	464,070	38,265
Judgment Fund Liability to Treasury	47,950	47,950	-
Resources Payable to Treasury	1,844,710	1,780,970	63,740
Federal Employee Benefits, Actuarial	88,353	88,702	(349)
Environmental and Disposal Liabilities	46,871	35,360	11,511
Contingent Liabilities	962	9,515	(8,553)
Other	3,835	23,130	(19,295)
Total	2,942,164	2,843,044	99,120

legal liabilities to be paid out of funds made available to Reclamation in future years. Funded and unfunded liabilities are discussed in Notes to the Financial Statements.

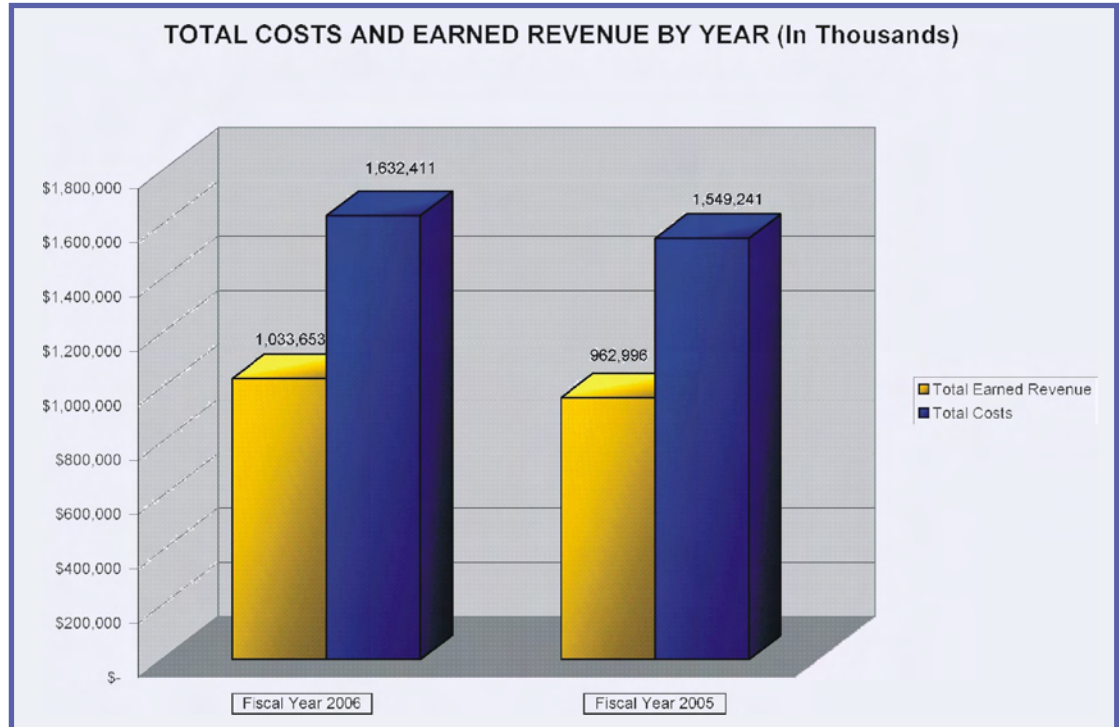
The increase in Advances, Deferred Revenue, and Deposit Funds is a result of increased advances from customers to construct irrigation facilities.

The increase of \$11.5 million in Environmental and Disposal Liabilities is primarily the result of recording additional sites where there is a probable outflow of resources.

Consolidated Statement of Net Costs

Net Cost of Operations: Reporting segments in the Consolidated Statements of Net Cost align to Interior's Strategic Plan Mission Goals/End Outcome Goals. Reclamation reports expenses and revenues in three of the four Interior mission goals: Resource Use, Resource Protection, and Recreation. Reclamation does not report on the fourth goal, which is Serving Communities.

In FY 2006, Reclamation reported \$1.3 billion of cost and \$865 million of earned revenues under the Resource Use mission goal. Our key mission activities are reported under this mission goal. This goal includes the costs for providing water and generating hydropower for our customers. It also includes hydropower and water sales revenue, which recovers the Government's costs to produce and deliver water and generate hydropower for our customers.



Centralized Program Support and Other's cost and revenues reflect administrative costs, working capital, and other costs and revenues incurred and earned to support Reclamation's mission goals. The Consolidated Statement of Net Cost displays the net cost of operations, which is the difference between revenues and expenses. Reclamation's total FY 2006 net cost of operations was \$598.8 million, an increase of \$12.5 million from the FY 2005 net cost of operations. A more detailed report, the Consolidating Statement of Net Cost, is in the Notes to the Financial Statements.

Revenues and Costs: Reclamation's earned revenues from providing goods or services are reported in the Consolidated Statement of Net Cost. Total FY 2006 earned revenue was \$1 billion, which is \$71 million, or 7 percent greater than was reported in FY 2005. FY 2006 costs were \$1.63 billion compared to \$1.55 billion in FY 2005, a 5-percent increase from FY 2005.

Combined Statement of Budgetary Resources

Budgetary Resources: The Combined Statement of Budgetary Resources and related disclosures provide information about budgetary resources and their end-of-the-year status. Reclamation's FY 2006 Total Budgetary Resources were \$2.69 billion compared to \$2.49 billion in FY 2005, an increase of \$194.6 million. Reclamation's major budget accounts are

broken down into five categories. Our funding is derived predominantly from three of the five categories: Total Budgetary Authority, Unobligated Balances (i.e., prior year carryforward balances), and Offsetting Collections. Refer to the Combined Statement of Budgetary Resources and the detailed budgetary information in the Supplemental Section for more information.

Financial Performance Measures

Financial performance measures are used to ensure the integrity of financial information needed for decisionmaking and to measure program

Measure/Indicator	What Does It Measure?	Goals (getting to green)	Reclamation Score (Sept. 2006)
Fund Balance with Treasury Agency fund balances should be equal to the balances recorded by Treasury, except for timing differences.	Identifies the difference between the fund balance reported in Treasury reports and the agency Fund Balance with Treasury.	2% or less of differences unreconciled	0% (100% balanced—no differences)
Suspense Clearing Suspense accounts are used for short-term holding of costs for which accounts cannot immediately be identified. To ensure costs are recorded to the proper accounts in a timely basis, suspense accounts are reviewed and cleared.	The timeliness of clearing and reconciling suspense accounts.	Zero dollars in unsupported transactions greater than 60 days	\$0 in unsupported transactions > 60 days
Delinquent Accounts Receivable from Public The Debt Collection Improvement Act of 1996 requires that all eligible 180+ Days Delinquent Debt be referred to Treasury for cross-servicing.	The percentage of 180+ Days Delinquent Debt referred to Treasury, Financial Management Service over the total dollar amount eligible for referral.	10% or less of delinquent receivables over 180 days old referred	Less than 1%
Electronic Funds Transfers/Payments The Debt Collection Improvement Act of 1996 requires that all payments with few exceptions must be paid using electronic payment technologies.	The percentage of the number of vendor payments paid via electronic means over the total vendor payments made.	96% or more of payments paid via electronic means	99.73%
Invoice Paid On Time The Prompt Payment Act of 1982, as amended, requires interest to be automatically included with payments if paid late (generally 30 days after receipt of invoice) and the interest amount is greater than \$1.00.	The percentage of the number of payments not requiring interest over the total number of payments subject to the Prompt Payment Act of 1982, as amended.	98% or more of invoices paid on time	98.74%
Travel Card Delinquency Rate Charge cards are the personal responsibility of employees to pay on time. The volume of activity and timeliness of payments affect rebates paid to the agency.	The percentage of the dollar amount 61+ days delinquent over the total balance due.	2% or less of balances over 61 days	Less than 1%

and financial performance. Reclamation's scores for financial management metrics, both Government-wide and Interior-specific, consistently exceeded the established goals. The table on page 53 depicts Reclamation's performance on some of the key metrics instituted to measure the financial management health of the Federal Government and to guide financial management reforms and target resources to areas where better stewardship of Federal financial resources is needed.

Improper Payments

Reclamation completed its FY 2006 Improper Payments risk assessment on the Water and Related Resources Program as required by the Improper Payments Information Act of 2002, P.L. 107-300. No major changes in policies, procedures, staffing, or systems implementation, which would pose a high risk of allowing improper payments to occur, were identified within the Acquisitions, Property, or Finance functions. Reclamation certified that there were no major operating changes from the risk assessment performed in FY 2005. Based on the information reviewed, the FY 2006 final risk assessment for the Water and Related Resources Program is low.

Internal Controls Over Financial Reporting

The passage of the Sarbanes-Oxley Act of 2002 served as an impetus for the Federal Government to reevaluate its current policies relating to internal controls over financial reporting and management's related responsibilities. In December 2004, OMB revised Circular No. A-123, "Management's Responsibility for Internal Control," which implements the requirements of the FMFIA. The revised circular is effective for FY 2006 for Interior-level agencies.

Interior has taken a "top down" approach for implementing the requirements of revised OMB Circular No. A-123 requirements. To support Interior's implementation plan, Reclamation developed review plans based on Interior's significant transaction processes, financial statements, and accounts. To assist Interior in implementing revised OMB Circular A-123, Reclamation focused on enhancing internal controls over financial reporting in three main areas: documentation, monitoring, and reporting. Reclamation tested key controls over its financial reporting processes. As a result, Reclamation provided Interior reasonable assurance that internal controls over financial reporting as of June 30, 2006, were operating effectively, and no material weaknesses were found in the design or operation of the internal controls over financial reporting.



Financial Statements and Notes



United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, DC 20240

Memorandum

FEB 12 2007

To: Commissioner, Bureau of Reclamation

From: Anne L. Richards *Anne L. Richards*
Assistant Inspector General for Audits

Subject: Independent Auditors' Report on the Bureau of Reclamation Financial Statements for Fiscal Years 2006 and 2005 (Report No. X-IN-BOR-0023-2006)

INTRODUCTION

This memorandum transmits the KPMG LLP (KPMG) auditors' report of the Bureau of Reclamation (Reclamation) financial statements for fiscal years 2006 and 2005 (Attachment 1). The Chief Financial Officers Act of 1990 (Public Law 101-576), as amended, requires the Inspector General or an independent auditor, as determined by the Inspector General, to audit the Department of the Interior (DOI) financial statements. Under a contract issued by DOI and monitored by the Office of Inspector General (OIG), the independent public accounting firm KPMG performed an audit of the Reclamation fiscal years 2006 and 2005 financial statements. The contract required that the audit be performed in accordance with the "Government Auditing Standards" issued by the Comptroller General of the United States and with Office of Management and Budget Bulletin No. 06-03, "Audit Requirements for Federal Financial Statements."

RESULTS OF INDEPENDENT AUDIT

In its audit report dated November 9, 2006, KPMG issued an unqualified opinion on the Reclamation financial statements. However, KPMG identified a reportable condition in internal controls over financial reporting, which was not considered to be a material weakness. KPMG also found one deficiency in Reclamation internal controls over Required Supplementary Information. In addition, KPMG identified one instance where Reclamation did not comply with laws and regulations, specifically the Federal Financial Management Improvement Act of 1996 (FFMIA). The report contains five recommendations that, if implemented, should resolve the findings.

STATUS OF RECOMMENDATIONS

In its December 20, 2006 response (Attachment 2) to the draft report, Reclamation partially agreed with one of the three findings and disagreed with the other two findings. Reclamation also addressed each recommendation, stating that it partially agreed with one

recommendation and disagreed with four of the recommendations (see Attachment 3, "Status of Audit Report Recommendations").

Two of the five recommendations are repeat recommendations that were made in last year's Report No. X-IN-BOR-0013-2005. In its response, Reclamation disagreed with the two repeat recommendations. We will refer these two repeat recommendations to the Assistant Secretary for Policy, Management and Budget for resolution. We will also refer the three new recommendations to the Assistant Secretary for resolution.

EVALUATION OF KPMG AUDIT PERFORMANCE

To fulfill our monitoring responsibilities, the OIG:

- assessed KPMG's approach and planning of the audit;
- evaluated the qualifications and independence of the auditors;
- monitored the progress of the audit at key points;
- participated in periodic meetings with Reclamation management to discuss audit progress, findings, and recommendations;
- reviewed and accepted KPMG's audit report; and
- performed other procedures we deemed necessary.

KPMG is responsible for the attached auditors' report and for the conclusions expressed in the report. We do not express an opinion on Reclamation financial statements or KPMG conclusions on the effectiveness of internal controls or compliance with laws, regulations, and FFMIA.

REPORT DISTRIBUTION

The legislation, as amended, creating the OIG requires semiannual reporting to the Congress on all audit reports issued, actions taken to implement audit recommendations, and recommendations that have not been implemented. Therefore, we will include this report in our next semiannual report. The distribution of the report is not restricted, and copies are available for public inspection.

We appreciate the courtesies and cooperation extended to KPMG and OIG staff during the audit. If you have any questions regarding the report, please contact me at 202-208-5512.

Attachments (3)

cc: Assistant Secretary, Water and Science
Audit Liaison Officer, Water and Science
Chief Financial Officer, Bureau of Reclamation
Audit Liaison Officer, Bureau of Reclamation
Acting Focus Leader, Management Control and Audit Follow-up, Office of Financial

Management
Focus Leader, Financial Reporting, Office of Financial Management

ATTACHMENT 1



KPMG LLP
Suite 2700
707 Seventeenth Street
Denver, CO 80202

Independent Auditors' Report

The Commissioner of the U.S. Bureau of Reclamation
and the Inspector General of the U.S. Department of the Interior:

We have audited the accompanying consolidated balance sheets of the U.S. Bureau of Reclamation (Reclamation) as of September 30, 2006 and 2005; the related consolidated statements of net cost, changes in net position, and financing; and the combined statements of budgetary resources (hereinafter referred to as "consolidated financial statements") for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these consolidated financial statements. In connection with our fiscal year 2006 audit, we also considered Reclamation's internal control over financial reporting, Required Supplementary Stewardship Information, and performance measures and tested Reclamation's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on these consolidated financial statements.

SUMMARY

As stated in our opinion on the consolidated financial statements, we concluded that Reclamation's consolidated financial statements as of and for the years ended September 30, 2006 and 2005 are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles.

As discussed in our opinion on the consolidated financial statements, Reclamation changed its method of accounting for and reporting of earmarked funds and heritage assets to adopt changes in accounting standards.

Our consideration of internal control over financial reporting, Required Supplementary Stewardship Information, and performance measures resulted in the following condition being identified as a reportable condition:

A. Controls over Design, Documentation, and Operating Effectiveness of Internal Controls

However, the reportable condition is not believed to be a material weakness.

We also noted the following deficiency in internal control over Required Supplementary Information that, in our judgment, could adversely affect Reclamation's ability to collect, process, record, and summarize this information.

B. Reporting the Condition of Heritage Assets

The results of our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements disclosed the following instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* issued by the Comptroller General of the United States and Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*.

C. Federal Financial Management Improvement Act of 1996

The following sections discuss our opinion on Reclamation's consolidated financial statements; our consideration of Reclamation's internal control over financial reporting, Required Supplementary Stewardship Information, and performance measures; our tests of Reclamation's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements; and management's and our responsibilities.

OPINION ON THE CONSOLIDATED FINANCIAL STATEMENTS

We have audited the accompanying consolidated balance sheets of the U.S. Bureau of Reclamation as of September 30, 2006 and 2005; the related consolidated statements of net cost, changes in net position, and financing; and the combined statements of budgetary resources for the years then ended.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Bureau of Reclamation as of September 30, 2006 and 2005, and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in Note 16 to the consolidated financial statements, Reclamation changed its method of accounting for and reporting earmarked funds in fiscal year 2006 to adopt the provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards (SFFAS) No. 27, *Identifying and Reporting Earmarked Funds*. Also as discussed in Note 1(k) to the consolidated financial statements, Reclamation changed its method of reporting for heritage assets and stewardship land in fiscal year 2006 to adopt the applicable provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards No. 29, *Heritage Assets and Stewardship Land*.

The information in the Management's Discussion and Analysis, Required Supplementary Stewardship Information, and Required Supplementary Information sections is not a required part of the consolidated financial statements, but is supplementary information required by U.S. generally accepted accounting principles and OMB Circular No. A-136, *Financial Reporting Requirements*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information, and accordingly, we express no opinion on it. As a result of such limited procedures, we believe that the Required Supplementary Information for heritage asset collections is not presented in conformity with U.S. generally accepted accounting principles because the Required Supplementary Information disclosures for heritage asset collections disclose the condition of the facility housing the collection rather than the condition of the underlying collection.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial

reporting that, in our judgment, could adversely affect Reclamation's ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the consolidated financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.

In our fiscal year 2006 audit, we noted a certain matter, discussed below, involving the internal control over financial reporting and its operation that we consider to be a reportable condition. However, the reportable condition is not believed to be a material weakness. Exhibit I presents the status of prior year audit findings.

A. Controls over Design, Documentation, and Operating Effectiveness of Internal Controls

As part of the financial statement audit, we tested controls over various business processes throughout Reclamation. Most of the business processes of Reclamation are executed at the regional offices, so it is important to have clearly defined standards, policies, and procedures Reclamation-wide related not only to the business processes, but also to the internal controls and documentation evidencing the controls are in place and operating effectively. In certain cases, we were unable to identify any internal control that was designed and placed in operation. In other cases, we noted instances whereby it was represented and corroborated that the management review of various procedures took place; however, these reviews were not always documented or dated as to their timeliness. Finally, in certain cases, we were unable to determine whether the internal control was in place and operating effectively. The following are the areas where we noted weaknesses in the design, documentation, and operating effectiveness of internal controls over business processes:

1. Deficiencies in the Design of Internal Controls

a. *Completeness of Environmental Liabilities*

Agencies are required to consider various factors in determining whether a future outflow of resources from a federal agency for environmental cleanup is probable in accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government* and the Federal Financial Accounting and Auditing Technical Release No. 2, *Determine Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

Reclamation does not have sufficient annual control procedures in place specifically to ensure that environmental liabilities are complete and fully disclosed in the consolidated financial statements, particularly as it relates to liabilities associated with tracts of land held by Reclamation over a period of time.

Region(s) with Control Exceptions Identified: All

b. *Review of Cost Structures*

At the onset of a project, the cost structures established are designed to capture the associated costs of the project and is approved by multiple individuals within the program, accounting, and budget offices to ensure compliance with applicable (1) program goals; (2) accounting standards, including SFFAS No. 6, *Accounting for Property, Plant, and Equipment*; and (3) budget compliance. However, Reclamation does not have sufficient controls in place to monitor that costs being charged to the cost

structures remain appropriate and that the costs remain appropriately accounted for. During the current fiscal year, management identified several instances where costs were initially capitalized that management later determined were capitalized in error. All of the significant instances were also detected in our sampling testwork.

In particular, one project in Region 2 was established in 1998 to track research and development costs for a potential construction project. Although the costs were not capital in nature, the project was established as a capital asset and capitalized into construction in progress (CIP). In 2000, when the project was approved for construction, an additional cost structure was established to accrue actual construction costs. Meanwhile, costs continued to be charged to the original cost structure; some charges represented capital costs and others represented noncapital costs. By 2006, accumulated charges in the original cost structure totaled approximately \$14 million, resulting in an overstatement of CIP. Management identified the exception and expensed the \$14 million in costs in the current year.

Also within Region 2, environmental study costs totaling approximately \$30 million from the 1990s were inappropriately capitalized into other assets. Management identified the exception and expensed the unamortized balance (approximately \$28 million) in the current year.

Further, within Region 1, management identified approximately \$49 million in assets that they did not have sufficient title claim. During the 1990s, Reclamation was awarded appropriations to perform Safety of Dams work on assets owned by other beneficiaries; the appropriation was awarded to prevent dam failure. Typically, Safety of Dams work is only performed by the entity with title to the asset. At the time the funds were spent, Reclamation should have recorded the costs as stewardship acquisition costs. However, Reclamation mistakenly capitalized costs into CIP and transferred the costs to completed plant upon completion.

Region(s) with Control Exceptions Identified: Regions 1 and 2

2. Deficiencies in the Documentation of Internal Controls

a. Monthly Fund Status Reports

Regional budget officers are provided monthly fund status reports (BOR 610) from the Washington Budget Office that provide regional management the ability to review budgeted amounts to actual expenditures. Although evidence exists that the reports are prepared and made available to regional management, there is no evidence that a review is being performed, who is performing the review, or the date the review is being performed.

Region(s) with Control Exceptions Identified: All

b. Charge Card Reviews

Reclamation, through the U.S. Department of the Interior (DOI), has provided charge cards to its employees in order to streamline acquisition and payment procedures and to reduce the administrative burden associated with traditional purchasing of travel items, supplies, and services. In conjunction with the issuance of charge cards, DOI has published guidance and instructions on charge card utilization through the Integrated Charge Card Programs Guide. This policy sets further restrictions on the use of the

charge cards as well as certain internal control procedures, including timely and complete reconciliation of the billing statements by the cardholders and approving officials.

Our audit identified internal control exceptions in 5 of 38 statements tested, resulting in a total of 6 exceptions. Two statements were not dated by the approving official; one statement was not reviewed by the approving official in a timely manner; two statements did not include receipts to support all of the charges on the statement at the time the review was performed; and one statement revealed two transactions for one purchase (one for \$2,499.99 and one for \$2,500.00), indicating a charge card was used to split purchases to circumvent the individual card limit.

Region(s) with Control Exceptions Identified: Regions 1, 2, and 8

3. Deficiencies in the Effectiveness of Internal Controls

a. *Quarterly Review of Open Obligations*

Regional finance representatives are required to certify, on a quarterly basis, the status of all open obligations greater than nine months old to ensure the validity of open obligations. Despite frequent requests by the oversight group in the Denver office, two regions did not respond with justifications for outstanding obligations during the third quarter certification process.

Region(s) with Control Exceptions Identified: Regions 8 and 9

b. *Quarterly Review of Open Accruals*

Reclamation has not fully implemented policies to ensure that control activities are performed, properly documented, and sufficiently reviewed by management. Regional finance representatives are required to certify, on a quarterly basis, the status of open payables to ensure the validity of open payables. As part of the certification process, Regions 3 and 4 requested that the Financial Policy Division (FPD) reverse specific accruals; however, the de-accrual was not performed in a timely manner.

Region(s) with Control Exceptions Identified: FPD

c. *Completeness of Interest During Construction and Interest on Investment*

Reclamation does not have adequate documented control procedures in place to ensure that interest during construction (IDC) and interest on investment (IOI) are being calculated and recorded in the Federal Financial System (FFS) at least annually for every applicable project.

In the prior year, we issued a finding stating Reclamation did not have a means for accurately identifying all projects requiring IDC and/or IOI calculations. In response to that finding, Reclamation implemented various controls at the regional level to help mitigate the risk of incomplete IDC and IOI. In an effort to test management's enhanced procedures, we requested a list of all projects where IDC and/or IOI are required. We noted that two projects initially selected for testing from the list provided did not have respective IDC and/or IOI components. Management asserts that the list provided represented projects that potentially required IDC and IOI; however, the request of management was to provide a complete list of projects requiring IDC and/or IOI. Since the list provided included projects where IDC and/or IOI were not applicable, we concluded that management had not implemented sufficient procedures and controls to ensure IDC and/or IOI was calculated on all applicable projects.

In addition to the procedure performed above, we requested that management provide evidence that a thorough review of projects requiring IDC and/or IOI was performed. Region 1 was not able to generate sufficient evidence that a review of projects was performed for IDC and IOI. Region 2 was able to provide sufficient evidence for IDC, but not for projects requiring IOI. Regions 3 and 6 provided evidence that sufficient procedures were in place but, at the time of our request, were not able to provide evidence that the procedures were being performed or being performed in a timely manner.

In order to assess the accuracy of IDC calculations, we reperformed a sample of program calculations. As a result of this testwork, we noted that Region 1, Region 2, and Region 4 were calculating IDC using different methodologies. Region 1 calculates IDC using the most recent applicable interest rate; Region 2 uses the applicable rate in the year the program was initiated; and Region 4 uses the applicable rate in each year, applied only to the disbursements during that year. Each region commented that their method of calculation was based upon the Reclamation Manual FIN 07-20 and did not relate to differing legislation requirements. Accordingly, the Reclamation Manual FIN 07-20 is not specific to ensure consistency between regions.

Region(s) with Control Exceptions Identified: Regions 1, 2, 3, and 6

Weaknesses in the design, documentation, and operating effectiveness of internal controls over business processes increase the risk that errors or irregularities may not be detected and corrected in a timely manner. In addition, internal control weaknesses increase the risk that Reclamation will not be able to provide support to DOI in their annual assurance statement related to the Federal Managers' Financial Integrity Act (FMFIA) and OMB Circular No. A-123, Appendix A. Leading practices in today's business environment require that internal controls be clearly understood, implemented consistently, and documented appropriately to evidence their effectiveness.

Recommendation

We recommend that the Commissioner, U.S. Bureau of Reclamation, perform a management assessment to ensure that internal controls are properly designed, documented, and operating effectively for the business processes noted above. Management should implement appropriate training and monitoring processes to ensure adherence to its internal control policies and procedures. Although the findings above identify specific regions where exceptions were identified, we recommend the assessment be performed across all regions to ensure consistency Reclamation-wide.

Management Response

Management has prepared an official response presented as a separate attachment to this report. In summary, management partially agreed with our recommendation to ensure that internal controls are properly designed, documented, and operating effectively for the business processes noted throughout finding A. While Reclamation agrees that it is important to have clearly defined standards, policies, and procedures Reclamation-wide, Reclamation believes certain procedures and controls are sufficiently documented. Reclamation management responded to each element of reportable condition A, as summarized below.

1. **Deficiencies in the Design of Internal Controls**

In summary, management disagreed with our finding regarding the completeness of environmental liabilities and partially agreed with our finding regarding cost structures. Reclamation's disagreement with the completeness of environmental liabilities portion of the

finding is based on management's belief that adequate policies and training are in place to ensure significant exposures are both limited and identified specifically through the conduct of environmental audits and the existence of Reclamation Manual Directives and Standards.

Reclamation partially agreed with our finding regarding the review of cost structures. Reclamation contends that the exceptions identified in the current year audit date back to the 1990s and were first identified by Reclamation management through its existing internal control structure.

Auditors' Response to Management's Response

Environmental liabilities represent a unique risk that all contaminations and the associated cleanup costs are not properly accounted for by Reclamation. Although Reclamation has policies and procedures documented in the Reclamation Manual Directives and Standards and other sources, there are not sufficient controls in place to ensure the policies and procedures are properly followed. Although environmental audits are performed, the audits are not performed consistently and routinely throughout the organization.

The key element of the cost structure finding is that material errors were identified in the current year representing inappropriately capitalized costs. The exceptions identified by management were not identified as a part of a systematic review of cost structures; rather, they were indirectly revealed as a result of reviews of other account activity. Although controls have been implemented and improved since the 1990s, Reclamation does not have sufficient controls in place to ensure existing cost structures continue to meet the definition and criteria under which the cost structures were initially established. Consequently, Reclamation does not have sufficient controls in place to ensure there are not additional costs inappropriately capitalized.

2. Deficiencies in the Documentation of Internal Controls

In summary, management disagreed with our finding regarding the consistent review of monthly fund status reports and agreed with our finding over charge card reviews. Reclamation's disagreement over the consistent review of monthly fund status reports is based on Reclamation's position that compensating evidence was available and provided by management and that not all documents must be evidenced by a signature and date to be in accordance with the provisions of OMB Circular A-123, Appendix A.

Auditors' Response to Management's Response

Although OMB Circular A-123, Appendix A, states that documentation may be in multiple forms, without a signature or other indicator, there is no mechanism in place for management to ensure review controls are being performed and being performed consistently. Although our preliminary focus was on the BOR 610 reports, Reclamation was not able to provide evidence that the BOR 610 or similar reports were being reviewed by management on a consistent basis Reclamation-wide.

3. Deficiencies in the Effectiveness of Internal Controls

In summary, management partially agreed with our findings regarding the quarterly review of open obligations and accruals and partially agreed with our finding regarding the completeness of IDC and IOI. The partial disagreement relating to the quarterly review of open obligations and payables is based on Reclamation's position that supporting documentation was available for the \$5 million payroll accrual. The partial disagreement relating to IDC and IOI is based on Reclamation's position that it may not be feasible or appropriate to establish a uniform calculation methodology.

Auditors' Response to Management's Response

Subsequent to our draft finding regarding insufficient documentation supporting the \$5 million payroll accrual, management provided appropriate and sufficient audit evidence supporting the accrual amount. Accordingly, we do not consider the \$5 million payroll accrual to be an exception nor a failure of internal controls. Further, we acknowledge that the Finance and Accounting Division (FAD) is responsible for reversing accruals, not FPD.

Regarding management's partial disagreement over the completeness of IDC and IOI, we acknowledge that it may not be feasible to have an established template that is appropriate in all cases. Nonetheless, management should consider the appropriateness of a standard template and at a minimum, document the rationale and legal basis for the calculation of IDC and IOI for each relevant project. Further, management should establish consistent policies and procedures across all regions for ensuring that IDC and IOI is recorded at least annually for all applicable projects.

INTERNAL CONTROLS OVER REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION AND PERFORMANCE MEASURES

Under OMB Bulletin No. 06-03, the definition of material weakness is extended to other controls as follows. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to the Required Supplementary Stewardship Information 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. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.

Our consideration of the internal control over the Required Supplementary Stewardship Information and the design and operation of internal control over the existence and completeness assertions related to performance measures reported in the Management's Discussion and Analysis section would not necessarily disclose all matters involving the internal control and its operation related to Required Supplementary Stewardship Information or the design and operation of the internal control over the existence and completeness assertions related to key performance measures that might be reportable conditions.

In our fiscal year 2006 audit, we noted no matters involving the internal control and its operation related to Required Supplementary Stewardship Information that we considered to be material weaknesses as defined above.

In our fiscal year 2006 audit, we noted no matters involving the design and operation of the internal control over the existence and completeness assertions related to key performance measures that we considered to be material weaknesses as defined above.

INTERNAL CONTROLS OVER REQUIRED SUPPLEMENTARY INFORMATION

We noted certain deficiencies in internal control over Required Supplementary Information described in the following paragraphs that, in our judgment, could adversely affect Reclamation's ability to collect, process, record and summarize Required Supplementary Information.

B. Reporting the Condition of Heritage Assets

Reclamation considers heritage asset collections to be in stable condition if the facility housing the collection is in stable condition. If a collection is housed in a poor facility, the condition of the collection would be considered "poor," regardless of the actual condition of the collection itself. If

that same collection is moved to a new facility that is in good condition, the collection would then be considered in “good” condition because the surrounding environment is in “good” condition, and any environmental problems contributing to the deterioration of the collection would improve because of the condition of the new facility.

Note 11 to paragraph 26 within SFFAS No. 29, *Heritage Assets & Stewardship Land*, states the following: “Condition is the physical state of an asset. The condition of an asset is based on an evaluation of the physical status/state of an asset, its ability to perform as planned, and its continued usefulness. Evaluating an asset’s condition requires knowledge of the asset, its performance capacity and its actual ability to perform, and expectations for its continued performance. The condition of a long-lived asset is affected by its durability, the quality of its design and construction, its use, the adequacy of maintenance that has been performed, and many other factors, including: accidents (an unforeseen and unplanned or unexpected event or circumstance), catastrophes (a tragic event), disasters (a sudden calamitous event bringing great damage, loss, or destruction) and obsolescence.”

Reclamation did not disclose the condition of heritage asset collections in accordance with SFFAS No. 29 as Reclamation disclosed the condition of the facility housing the collection rather than the condition of the underlying collection. As a result, Reclamation did not substantially comply with the federal accounting standard requirements of the *Federal Financial Management Improvement Act of 1996* (FFMIA) as discussed in deficiency C.

Recommendations

We recommend that the Commissioner, U.S. Bureau of Reclamation:

1. Assess and disclose the condition of heritage asset collections rather than the facility housing the collection. Although the condition of the facility may be an important criterion in determining the condition of the underlying collection, we recommend that Reclamation consider other factors, such as whether or not Reclamation intends to improve the collection, in defining the acceptable condition.
2. Improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with federal accounting standards.

Management Response

Management has prepared an official response presented as a separate attachment to this report. In summary, management disagreed with our recommendations to assess and disclose the condition of heritage asset collections rather than the facility housing the collections and to improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with federal accounting standards. Management indicated they believe reporting the condition of museum collections at the facility level is in accordance with SFFAS No. 29 and established industry practices.

Auditors’ Response to Management’s Response

Reclamation did not disclose the condition of heritage asset collections in accordance with federal accounting standards as Reclamation disclosed the condition of the facility housing the collection rather than the condition of the underlying collection, as required in Note 11 to paragraph 26 within SFFAS No. 29.

COMPLIANCE AND OTHER MATTERS

Our tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 06-03.

The results of our tests of FFMIA disclosed one instance, described below, where Reclamation's financial management systems did not substantially comply with the applicable federal accounting standards. The results of our tests of FFMIA disclosed no instances in which Reclamation's financial management systems did not substantially comply with federal financial management systems requirements or the United States Government Standard General Ledger at the transaction level.

C. Federal Financial Management Improvement Act of 1996

Reclamation did not disclose the condition of heritage asset collections in accordance with federal accounting standards, as Reclamation disclosed the condition of the facility housing the collection rather than the condition of the underlying museum collection.

Recommendation

We recommend that the Commissioner, U.S. Bureau of Reclamation:

1. Assess and disclose the condition of heritage asset collections rather than the facility housing the collection. Although the condition of the facility may be an important criterion in determining the condition of the underlying collection, we recommend that Reclamation consider other factors, such as whether or not Reclamation intends to improve the collection, in defining the acceptable condition.
2. Improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with the federal accounting standards.

Management Response

Management has prepared an official response presented as a separate attachment to this report. In summary, management disagreed with our recommendations to assess and disclose the condition of heritage asset collections rather than the facility housing the collections and to improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with federal accounting standards. Management indicated they do not believe heritage asset condition assessments are required under federal accounting standards at the collection level and, accordingly, does not believe this finding to be a substantial noncompliance with FFMIA.

Auditors' Response to Management's Response

FFMIA requires an entity's financial management system to comply with all relevant federal accounting standards. As discussed in deficiency B, Reclamation did not disclose the condition of heritage asset collections in accordance with federal accounting standards as Reclamation disclosed the condition of the facility housing the collection rather than the condition of the underlying collection, as required in Note 11 to paragraph 26 within SFFAS No. 29.

* * * * *

RESPONSIBILITIES

Management's Responsibilities. The United States Code Title 31 Sections 3515 and 9106 require agencies to report annually to Congress on their financial status and any other information needed to fairly present their financial position and results of operations. To assist the U.S. Department of the Interior meet these reporting requirements, Reclamation prepares consolidated financial statements in accordance with OMB Circular No. A-136.

Management is responsible for the consolidated financial statements, including:

- Preparing the consolidated financial statements in conformity with U.S. generally accepted accounting principles;
- Preparing the Management's Discussion and Analysis (including the performance measures), Required Supplementary Information, and Required Supplementary Stewardship Information;
- Establishing and maintaining effective internal controls over financial reporting; and
- Complying with laws, regulations, contracts, and grant agreements applicable to Reclamation, including FFMIA.

In fulfilling this responsibility, management is required to make estimates and judgments to assess the expected benefits and related costs of internal control policies.

Auditors' Responsibilities. Our responsibility is to express an opinion on the fiscal year 2006 and 2005 consolidated financial statements of Reclamation based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin No. 06-03. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Reclamation's internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall consolidated financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2006 audit, we considered Reclamation's internal control over financial reporting by obtaining an understanding of Reclamation's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 06-03. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to provide an opinion on Reclamation's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

As required by OMB Bulletin No. 06-03, in our fiscal year 2006 audit, we considered Reclamation's internal control over the Required Supplementary Stewardship Information by obtaining an understanding of Reclamation's internal control, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls. We limited our testing to those controls necessary to test and report on the internal control over Required Supplementary Stewardship Information in accordance with OMB Bulletin No. 06-03. However, our procedures were not designed to provide an opinion on internal control over the Required Supplementary Stewardship Information and, accordingly, we do not provide an opinion thereon.

As further required by OMB Bulletin No. 06-03, in our fiscal year 2006 audit, with respect to internal control related to performance measures determined by management to be key and reported in the Management's Discussion and Analysis section, we obtained an understanding of the design of internal controls relating to the existence and completeness assertions and determined whether these internal controls had been placed in operation. We limited our testing to those controls necessary to test and report on the internal control over key performance measures in accordance with OMB Bulletin No. 06-03. However, our procedures were not designed to provide an opinion on internal control over reported performance measures and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether Reclamation's fiscal year 2006 consolidated financial statements are free of material misstatement, we performed tests of Reclamation's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 06-03, including certain provisions referred to in FFMIA. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, contracts and grant agreements applicable to Reclamation. However, providing an opinion on compliance with laws, regulations, contracts, and grant agreements was not an objective of our audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 06-03 and FFMIA, auditors are required to report whether certain federal entities' financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To assist the auditors of the U.S. Department of the Interior meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

We noted certain additional matters that we have reported to management of Reclamation in a separate letter dated November 9, 2006.

RESTRICTED USE

This report is intended solely for the information and use of Reclamation's and DOI's management, DOI's Office of Inspector General, OMB, the U.S. Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 9, 2006

Exhibit I**U.S. BUREAU OF RECLAMATION**

Status of Prior Year Findings

September 30, 2006

Ref	Condition	Status
A	Controls over Implementation of New Accounting Principle	This condition has been partially corrected in fiscal year 2006. See management letter comment 2.
B	Security and Internal Control over Information Technology Systems	This condition has been partially corrected in fiscal year 2006. See management letter comment 1.
C	Controls over Charge Card Reviews	This condition has not been corrected and is repeated in fiscal year 2006. See reportable condition A.
D	Controls over Management Review and Approval of Process-level Activities	This condition has been partially corrected. See reportable condition A.
E	Controls over Credit Reform Loans	This condition has been partially corrected. See management letter comment 3.
F	Reporting the Condition of Heritage Assets and Related Deferred Maintenance	This condition has not been corrected and is repeated in fiscal year 2006. See deficiency B.
G	Federal Accounting Standards	This condition has been partially corrected in fiscal year 2006. See deficiency C.



United States Department of the Interior

BUREAU OF RECLAMATION
Washington, DC 20240

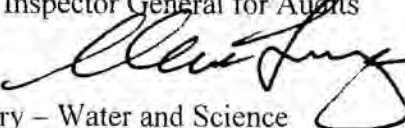


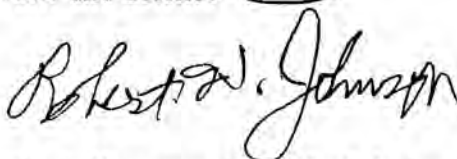
IN REPLY REFER TO:

84-27400
ADM-1.00

MEMORANDUM

To: Office of Inspector General
Attn: Assistant Inspector General for Audits

Through: Mark Limbaugh  DEC 20 2006
Assistant Secretary – Water and Science

From: Robert W. Johnson  D
Commissioner

Subject: The Bureau of Reclamation's Response to the Draft *Independent Auditors' Report on the Bureau of Reclamation Financial Statements for Fiscal Years 2006 and 2005*
(Assignment No. X-IN-BOR-0023-2006)

We appreciate the opportunity to review and comment on the draft audit report titled *Independent Auditors' Report on the Bureau of Reclamation Financial Statements for Fiscal Years 2006 and 2005*. Attached for your consideration is Reclamation's response to the recommendations as stated in the subject report.

If you have any questions or require additional information, please contact Reclamation's Acting Audit Liaison Officer, Ed Abreo, at 303-445-3423.

Attachment

cc: Associate Director - Financial Policy and Operations
Attn: Gordon Horwitz
(w/copy of incoming and att)

U. S. Bureau of Reclamation
KPMG, LLP Draft Audit Report
Response to Draft Audit Report Recommendations
December 2006

A. Controls over Design, Documentation and Operating Effectiveness of Internal Controls

Recommendation A

We recommend that the Commissioner, U.S. Bureau of Reclamation perform a management assessment to ensure that internal controls are properly designed, documented, and operating effectively for the business processes noted above. Management should implement appropriate training and monitoring processes to ensure adherence to its internal control policies and procedures. Although the findings above identify specific regions where exceptions were identified, we recommend the assessment be performed across all regions to ensure consistency Reclamation-wide.

Response

Partially concur. Reclamation agrees with KPMG that “it is important to have clearly defined standards, policies and procedures Reclamation-wide related to not only the business processes, but the internal controls and documentation evidencing the controls are in place and operating effectively.” Reclamation is committed to ensuring that internal controls over financial reporting are sufficient in terms of design and operation. Reclamation will continue to enhance our internal control environment through our efforts to support the Department’s compliance with the Office of Management and Budget’s Circular No. A-123, Management’s Responsibility for Internal Control, and our established audit follow-up process. Reclamation will perform management assessments to ensure that internal controls are properly designed, documented, and operating effectively, as necessary, for the individual areas discussed under this recommendation.

However, in our opinion, in some cases procedures and controls are sufficiently documented and further assessments are not required. Notwithstanding this position, as necessary, Reclamation will implement appropriate training and monitoring of processes to ensure adherence to internal control policies and procedures. Under each of the individual areas under this recommendation, Reclamation briefly addresses the specific conditions, as discussed in the draft audit report, and our response to the recommendations.

1. Deficiencies in the Design of Internal Controls

a. Completeness of Environmental Liabilities

Nonconcur. Reclamation considers existing procedures to be sufficient for identifying environmental liabilities on Reclamation land. Environmental liabilities result from hazardous substance releases from current operations, or from unknown past or current

activities (such as past operations on lands acquired prior to the requirement to conduct Environmental Site Assessments, illegal dumping, etc.). The risk that Reclamation's lands may have environmental liabilities is mitigated through the conduct of environmental audits and several Reclamation Manual Directives and Standards (D&S) that require environmental management of Reclamation's land. These D&S also require that all Reclamation employees report releases or evidence of releases on Reclamation land. Reclamation employees specifically include power plant operators, surveyors, hazmat coordinators, land managers, realty specialists, natural resource specialists, cultural resource specialists, recreation specialists, and outdoor recreation planners, among others.

The risk of environmental liabilities associated with unknown past or current activities are mitigated through the implementation of several policies and D&S, such as Reclamation's Policy ENV P-05 and D&S ENV 05-01, *Environmental Management Systems*. This Policy and D&S requires continual improvement in managing Reclamation's environmental liability and that management address all potential environmental impacts associated with the use of hazardous substances, oils, and generation of solid or hazardous waste associated with an appropriate facility's activities.

Reclamation's control to ensure that hazardous waste releases do not occur on Reclamation land is the Environmental Audit Program, D&S ENV 02-08, *Hazardous Materials and Hazardous Waste Auditing and Review Program Implementation*. In the unlikely event of a release, this D&S also ensures that such releases are quickly dealt with.

Additionally, D&S LND 12-01, *Identification and Reporting of Potential Hazardous Substances on Reclamation Acquired or Withdrawn Lands (Reclamation Lands)*, facilitates efficiency in identifying and reporting potential hazardous substances release sites by requiring all staff involved in any periodic or planned land review and inspection to be aware of the possible presence of potential hazardous material and site contamination on Reclamation lands and report such a condition using the required procedures.

Hazmat training for these employees is mandatory under D&S ENV 02-06, *Required Training and Medical Surveillance for Hazardous Waste Operations and Emergency Response*. All appropriate personnel are required to receive training on recognition of hazardous waste in the field, including wastes discovered incidentally to the performance of other duties.

b. Review of Cost Structures

Response

Partially concur. Reclamation does not agree with KPMG's contention that Reclamation does not have sufficient review controls in place to ensure that existing capitalized structures represent capital projects and that costs that are not capitalizable, within each

cost structure, are expensed in the year incurred.

The three instances in the condition are isolated incidents that date back to the 1990s, and that the condition is limited to these instances and adjusting entries only. Internal controls have been added and improved to reduce the risk of incorrectly capitalizing costs.

It should also be emphasized that it was management's internal controls that detected the misclassifications in Fiscal Year (FY) 2006, and it was Reclamation that made the adjusting entries that were subsequently included in KPMG's sample of transactions.

There are adequate review and approval controls at the budget, payroll, property, procurement, obligations and disbursement, program/project management, project operation and maintenance, and accounting process levels to reasonably ensure that costs are appropriately classified as capital or expense.

As part of its OMB Circular A-123 internal control assessments, Reclamation will conduct reviews of cost structures, as considered necessary.

2. Deficiencies in the Documentation of Internal Controls

a. Monthly Fund Status Reports

Response

Nonconcur. KPMG limited their review of the monthly fund status monitoring process to one aspect of the budget monitoring process. As a point of clarification, they reviewed the process and documentation pertaining to the Program and Budget System Monthly Progress of Funds (B21) report, not the Federal Financial System Fund Detail Report (BOR 610), as indicated in the draft audit report.

KPMG did not consider compensating control evidence provided by Reclamation. Reclamation provided monthly surplus and shortage reports prepared by the Washington Budget Office that track obligations and expenditures of all appropriations that clearly demonstrate management information on performance. Moreover, KPMG did not consult with Reclamation's Budget Officers to obtain an understanding of our practices as requested by Reclamation.

Reclamation intends to follow departmental guidance and continue to improve our internal control evaluation, training and procedures, as necessary. However, Reclamation believes KPMG has taken an unreasonable position requiring all documents reviewed by management be evidenced by a signature and date. Reclamation does not believe the issues identified correlate to this recommendation.

OMB Circular A-123, Appendix A, states that documentation might take many forms, such as paper, electronic files, or other media, and can include a variety of information,

including policy manuals, process models, desk procedures, flowcharts, job descriptions, documents, and forms. The form and extent of documentation will vary depending on the size, nature, and complexity of the entity or financial report.

b. Charge Card Reviews

Response

Concur. Reclamation will continue to implement procedures to ensure compliance with its established charge card procedures. During FY 2007, Reclamation will issue its Charge Card Management Plan, which is required by OMB Circular A-123, *Management's Responsibility for Internal Controls*. Furthermore, Reclamation has implemented reviews to ensure full compliance with these procedures.

Prior to the issuance of draft BOR-NFR 2006-1, *Charge Card Reviews*, Reclamation identified charge card control weaknesses during its FY 2006 implementation of OMB's Revised A-123 Internal Control Review. Consequently, Reclamation has been working on a corrective action plan to address the control weaknesses.

As part of these corrective actions, the Finance and Accounting Division, Acquisition and Assistance Management Services Division, and the Property and Office Services Division perform routine charge card reviews as part of Reclamation's ongoing charge card program oversight efforts. These reviews are identifying areas where cardholders and approving officials need to strengthen the internal controls. And finally, Reclamation continues to educate cardholders and approving officials to improve compliance with cardholder program requirements.

3. Deficiencies in the Effectiveness of Internal Controls

a. Quarterly Review of Open Obligations

b. Quarterly Review of Open Accruals

Response

Partially concur. Reclamation will continue to fully implement procedures to ensure that all obligations and accruals are valid. As a point of clarification, the Finance and Accounting Division is responsible for reversing accruals, not the Financial Policy Division, as stated in the draft audit report.

Reclamation does not concur with the lack of supporting documentation for approximately \$5 million in payroll accruals. Supporting documentation for the payroll accrual, \$22,515,185, and actual payroll expense, \$23,120,130, was provided. Since accruals are estimates, the difference of \$604,945, or 2.6 percent, was considered immaterial.

c. Completeness of Interest During Construction and Interest on Investment

Response

Partially concur. Reclamation will implement a process and procedures to ensure that Interest During Construction (IDC) and Interest on Investment is accurately computed on all projects, as applicable. Further, Reclamation will assess the feasibility of developing a uniform methodology for calculating IDC. In some cases, there may be certain circumstances, e.g., project authorizing legislation or other legislative requirements, which would preclude the use of a standardized methodology. Reclamation FIN 07-20, *Interest During Construction*, is intentionally non-specific in certain areas to accommodate the different requirements.

The responsible official is the Deputy Commissioner, Policy, Administration and Budget. The target date for performing necessary management assessments to ensure that internal controls are properly designed, documented, and operating effectively is June 30, 2007.

B. Reporting the Condition of Heritage AssetsRecommendation B.1

Assess and disclose the condition of heritage asset collections rather than the facility housing the collection. Although the condition of the facility may be an important criterion in determining the condition of the underlying collection, we recommend that Reclamation consider other factors, such as whether or not Reclamation intends to improve the collection, in defining the acceptable condition.

Response

Nonconcur. This is a repeat recommendation from the prior *Independent Auditor's Report on Bureau of Reclamation Financial Statement for Fiscal Year 2005 and 2004*, to which Reclamation provided a detailed response. Reclamation notes that the Department of the Interior, in an October 21, 2005, memorandum from the Assistant Secretary, Policy, Management and Budget, to the Office of Inspector General, has resolved this issue:

“Collections that are housed in facilities in good condition are deemed to be in good condition. Therefore, Interior’s policy of assessing the condition of museum objects based upon the condition of the facility housing the collection is considered appropriate and is supported by professional museum policy and practice.”

Reclamation’s approach to accounting for the condition of museum collections is in accordance with the Federal Accounting Standards Advisory Board’s Statement of Federal Financial Accounting Standard No. 29, *Heritage Assets and Stewardship Lands*, and established industry practices. Reclamation’s approach is consistent with the direction of the Government-wide task force developing implementation guidance for this standard, and with policy and instruction provided by the Department in reporting the

condition of museum collections based on the condition of the facilities that house collections. Reclamation's response is in concurrence with, and mirrors that of the Assistant Secretary, Policy, Management and Budget, in his November 15, 2006, response to the *Independent Auditor's Report for Fiscal Year 2006*.

Recommendation B.2

Improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with the federal accounting standards.

Response

Nonconcur. Reclamation is not aware of specific questions or analyses from the auditors to support this recommendation. The recommendation implies that Reclamation does not have sufficient procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with Federal accounting standards. Reclamation believes its internal controls are sufficient, and as implemented, will continue to ensure that its financial reporting disclosures are prepared in accordance with the Federal accounting standards.

C. Federal Financial Management Improvement Act of 1996

Recommendation C.1:

Assess and disclose the condition of heritage asset collections rather than the facility housing the collection. Although the condition of the facility may be an important criterion in determining the condition of the underlying collection, we recommend that Reclamation consider other factors, such as whether or not Reclamation intends to improve the collection, in defining the acceptable condition.

Response

Recommendation C.1 is the same as Recommendation B.1. See response to B.1 above.

Recommendation C.2

Improve procedures and internal controls to ensure that the financial reporting disclosures are prepared in accordance with the federal accounting standards.

Response

Recommendation C.2 is the same as Recommendation B.2. See response to B.2 above.

STATUS OF AUDIT REPORT RECOMMENDATIONS

<u>Recommendation</u>	<u>Status</u>	<u>Action Required</u>
A., B.2., and C.2.	Unresolved.	Recommendations will be referred to the Assistant Secretary for Policy, Management and Budget for resolution.
B.1. and C.1.	Repeated; unresolved.	Recommendations will be referred to the Assistant Secretary for Policy, Management and Budget for resolution.

2006 Bureau of Reclamation Annual Report

**U.S. Department of the Interior
Bureau of Reclamation
Consolidated Balance Sheet
As of September 30, 2006**

(In Thousands)	2006
ASSETS (Note 2)	
Intragovernmental Assets:	
Fund Balance with Treasury (Note 3)	\$ 7,030,401
Accounts Receivable	663,573
Investments, Net (Note 4)	322,045
Amounts Due from the U.S. Department of Energy, Net (Note 5)	2,631,887
Other:	
Advances and Prepayments	1,007
Total Intragovernmental Assets	<u>10,648,913</u>
Cash	117
Accounts and Interest Receivable, Net (Note 6)	29,752
Loans and Interest Receivable, Net (Note 7)	157,286
General Property, Plant, and Equipment, Net (Note 8)	13,071,874
Other:	
Advances and Prepayments	19,202
Power Rights, Net	122,033
Total Other Assets	<u>141,235</u>
Stewardship PP&E (Note 1.K)	
Total Assets	<u><u>\$ 24,049,177</u></u>
LIABILITIES (Note 9)	
Intragovernmental Liabilities:	
Accounts Payable	\$ 29,142
Debt (Note 10)	95,141
Other :	
Accrued Employee Benefits	22,033
Advances, Deferred Revenue, and Deposit Funds	5,285
Judgment Fund Liability	47,950
Resources Payable to Treasury	1,844,710
Other Liabilities	73
Total Other Liabilities	<u>1,920,051</u>
Total Intragovernmental Liabilities	<u>2,044,334</u>
Accounts Payable	213,735
Federal Employee Benefits, Actuarial	88,353
Environmental and Disposal Liabilities (Note 11)	46,871
Other:	
Accrued Payroll and Benefits	47,097
Advances, Deferred Revenue, and Deposit Funds	497,050
Contingent Liabilities (Note 11)	962
Other Liabilities	3,762
Total Other Liabilities	<u>548,871</u>
Commitments and Contingencies (Notes 11 and 12)	
Total Liabilities	<u>2,942,164</u>
NET POSITION	
Unexpended Appropriations - Earmarked Funds (Note 16)	249,501
Unexpended Appropriations - Other Funds	96,590
Cumulative Results of Operations - Earmarked Funds (Note 16)	20,550,111
Cumulative Results of Operations - Other Funds	210,811
Total Net Position	<u>21,107,013</u>
Total Liabilities and Net Position	<u><u>\$ 24,049,177</u></u>

The accompanying notes are an integral part of these statements.

**U.S. Department of the Interior
Bureau of Reclamation
Consolidated Balance Sheet
As of September 30, 2005**

(In Thousands)	2005
ASSETS (Note 2)	
Intragovernmental Assets:	
Fund Balance with Treasury (Note 3)	\$ 6,090,731
Accounts Receivable	825,974
Amounts Due from the U.S. Department of Energy, Net (Note 5)	2,458,075
Other:	
Advances and Prepayments	1,423
Total Intragovernmental Assets	<u>9,376,203</u>
Cash	100
Accounts and Interest Receivable, Net (Note 6)	31,459
Loans and Interest Receivable, Net (Note 7)	146,468
General Property, Plant, and Equipment, Net (Note 8)	13,015,525
Other:	
Advances and Prepayments	37,736
Power Rights, Net	160,579
Total Other Assets	<u>198,315</u>
Stewardship PP&E (Note 1.K)	
Total Assets	<u><u>\$ 22,768,070</u></u>
LIABILITIES (Note 9)	
Intragovernmental Liabilities:	
Accounts Payable	\$ 24,651
Debt (Note 10)	96,811
Other:	
Accrued Employee Benefits	21,357
Advances, Deferred Revenue, and Deposit Funds	8,781
Judgment Fund Liability	47,950
Resources Payable to Treasury	1,780,970
Other Liabilities	19,689
Total Other Liabilities	<u>1,878,747</u>
Total Intragovernmental Liabilities	<u>2,000,209</u>
Accounts Payable	201,542
Federal Employee Benefits, Actuarial	88,702
Environmental and Disposal Liabilities (Note 11)	35,360
Other:	
Accrued Payroll and Benefits	48,986
Advances, Deferred Revenue, and Deposit Funds	455,289
Contingent Liabilities (Note 11)	9,515
Other Liabilities	3,441
Total Other Liabilities	<u>517,231</u>
Commitments and Contingencies (Notes 11 and 12)	
Total Liabilities	<u>2,843,044</u>
NET POSITION	
Unexpended Appropriations	350,519
Cumulative Results of Operations	19,574,507
Total Net Position	<u>19,925,026</u>
Total Liabilities and Net Position	<u><u>\$ 22,768,070</u></u>

The accompanying notes are an integral part of these statements.

2006 Bureau of Reclamation Annual Report

**U.S. Department of the Interior
Bureau of Reclamation
Consolidated Statement of Net Cost
For the Years Ended September 30, 2006, and 2005**

(In Thousands)	2006	2005
RESOURCE USE		
Deliver Water in an Environmentally Responsible and Cost-Efficient Manner:		
Costs	\$ 1,089,295	\$ 1,065,165
Earned Revenues	(585,466)	(517,262)
Net Cost	<u>503,829</u>	<u>547,903</u>
Generate Hydropower in an Environmentally Responsible and Cost-Efficient Manner:		
Costs	242,354	257,373
Earned Revenues	(279,442)	(350,931)
Net Cost	<u>(37,088)</u>	<u>(93,558)</u>
RESOURCE PROTECTION		
Improve Health of Watersheds and Landscapes, Sustain Biological Communities, and Protect Cultural Resources:		
Costs	66,949	34,907
Earned Revenues	(27,279)	(1,910)
Net Cost	<u>39,670</u>	<u>32,997</u>
RECREATION		
Provide Quality and Fair Value in Recreation:		
Costs	33,065	27,720
Earned Revenues	(27,808)	(13,654)
Net Cost	<u>5,257</u>	<u>14,066</u>
CENTRALIZED PROGRAM SUPPORT AND OTHER		
Working Capital Fund, Policy and Administration, and Other:		
Costs	200,748	164,076
Earned Revenues	(113,658)	(79,239)
Net Cost	<u>87,090</u>	<u>84,837</u>
TOTAL		
Costs	1,632,411	1,549,241
Earned Revenues	(1,033,653)	(962,996)
Net Cost of Operations (Note 13)	<u>\$ 598,758</u>	<u>\$ 586,245</u>

The accompanying notes are an integral part of these statements.

U.S. Department of the Interior
 Bureau of Reclamation
 Consolidated Statement of Changes in Net Position
 For the Years Ended September 30, 2006, and 2005

(In Thousands)	Earmarked	All Other	2006 Consolidated	2005 Consolidated
UNEXPENDED APPROPRIATIONS				
Beginning Balance	\$ 286,742	\$ 63,777	\$ 350,519	\$ 325,934
Budgetary Financing Sources:				
Appropriations Received, General Funds	198,030	39,058	237,088	190,227
Appropriations Transferred In/(Out)	(6,980)	48,342	41,362	41,639
Appropriations Used	(226,473)	(54,217)	(280,690)	(205,939)
Other Adjustments	(1,818)	(370)	(2,188)	(1,342)
Total Budgetary Financing Sources	<u>(37,241)</u>	<u>32,813</u>	<u>(4,428)</u>	<u>24,585</u>
Ending Balance - Unexpended Appropriations	<u>\$ 249,501</u>	<u>\$ 96,590</u>	<u>\$ 346,091</u>	<u>\$ 350,519</u>
CUMULATIVE RESULTS OF OPERATIONS				
Beginning Balance	\$ 19,350,254	\$ 224,253	\$ 19,574,507	\$ 18,217,213
Budgetary Financing Sources:				
Appropriations Used	226,473	54,217	280,690	205,939
Royalties Retained	1,487,423	-	1,487,423	1,763,969
Non-exchange Revenue	4	-	4	17
Transfers In/(Out) Without Reimbursement	50,816	(54,356)	(3,540)	(78,763)
Other Budgetary Financing Sources	-	-	-	33,958
Other Financing Sources:				
Donations of Property	505	-	505	2,177
Transfers In/(Out) Without Reimbursement	(100,742)	13,257	(87,485)	(51,621)
Imputed Financing from Costs Absorbed by Others	107,556	20	107,576	67,863
Total Financing Sources	<u>1,772,035</u>	<u>13,138</u>	<u>1,785,173</u>	<u>1,943,539</u>
Net Cost of Operations	<u>(572,178)</u>	<u>(26,580)</u>	<u>(598,758)</u>	<u>(586,245)</u>
Net Change in Cumulative Results of Operations	<u>1,199,857</u>	<u>(13,442)</u>	<u>1,186,415</u>	<u>1,357,294</u>
Ending Balance - Cumulative Results of Operations	<u>\$ 20,550,111</u>	<u>\$ 210,811</u>	<u>\$ 20,760,922</u>	<u>\$ 19,574,507</u>

The accompanying notes are an integral part of these statements.

2006 Bureau of Reclamation Annual Report

**U.S. Department of the Interior
Bureau of Reclamation
Combined Statement of Budgetary Resources
For the Years Ended September 30, 2006, and 2005**

(In Thousands)	Total Budgetary Accounts		Non-budgetary Credit Program Financing Account	
	2006	2005	2006	2005
BUDGETARY RESOURCES				
Unobligated Balance, Beginning of Fiscal Year	\$ 666,008	\$ 602,241	\$ -	\$ -
Recoveries of Prior Year Unpaid Obligations	39,171	33,981	8	9
Budget Authority:				
Appropriations	1,154,951	1,080,755	-	-
Borrowing Authority	-	-	1,584	995
Spending Authority from Offsetting Collections:				
Earned:				
Collected	865,383	780,978	7,708	24,718
Change in Receivables from Federal Sources	(4,692)	4	-	-
Change in Unfilled Customer Orders:				
Advance Received	2,746	167,901	-	-
Without Advance from Federal Sources	(6,761)	6,279	-	-
Subtotal	2,011,627	2,035,917	9,292	25,713
Nonexpenditure Transfers, Net	(7,480)	2,000	-	-
Temporarily Not Available Pursuant to Public Law	(7,679)	(6,066)	-	-
Permanently Not Available	(16,766)	(177,798)	(3,255)	(18,282)
Total Budgetary Resources	\$ 2,684,881	\$ 2,490,275	\$ 6,045	\$ 7,440
STATUS OF BUDGETARY RESOURCES				
Obligations Incurred (Note 14):				
Direct				
Reimbursable	\$ 1,164,041	\$ 1,018,358	\$ 6,036	\$ 7,440
Total Obligations Incurred	868,061	805,909	-	-
Unobligated Balance Available:				
Apportioned	599,265	621,064	9	-
Exempt from Apportionment	53,514	44,944	-	-
Total Unobligated Balance Available	652,779	666,008	9	-
Total Status of Budgetary Resources	\$ 2,684,881	\$ 2,490,275	\$ 6,045	\$ 7,440
OBLIGATED BALANCE				
Obligated Balance, Net, Beginning of Fiscal Year:				
Unpaid Obligations	\$ 780,773	\$ 742,132	\$ 3,942	\$ 3,951
Less: Uncollected Receivables and Orders from Federal Sources	(73,472)	(67,189)	-	-
Total Unpaid Obligated Balances, Net, Beginning of Fiscal Year	707,301	674,943	3,942	3,951
Obligations Incurred	2,032,102	1,824,267	6,036	7,440
Less: Gross Outlays	(1,809,352)	(1,751,645)	(6,036)	(7,440)
Less: Recoveries of Prior Year Unpaid Obligations	(39,171)	(33,981)	(8)	(9)
Change in Uncollected Receivables and Orders from Federal Sources	11,453	(6,283)	-	-
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 902,333	\$ 707,301	\$ 3,934	\$ 3,942
OBLIGATED BALANCE, NET, END OF FISCAL YEAR - BY COMPONENT				
Obligated Balance, Net, End of Fiscal Year:				
Unpaid Obligations	\$ 964,352	\$ 780,773	\$ 3,934	\$ 3,942
Less: Uncollected Receivables and Orders from Federal Sources	(62,019)	(73,472)	-	-
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 902,333	\$ 707,301	\$ 3,934	\$ 3,942
NET OUTLAYS				
Gross Outlays	\$ 1,809,352	\$ 1,751,645	\$ 6,036	\$ 7,440
Less: Offsetting Collections	(868,129)	(948,879)	(7,708)	(24,718)
Less: Distributed Offsetting Receipts	(2,257,865)	(1,787,437)	-	-
Net Outlays (Receipts)	\$ (1,316,642)	\$ (984,671)	\$ (1,672)	\$ (17,278)

The accompanying notes are an integral part of these statements.

U.S. Department of the Interior
Bureau of Reclamation
Consolidated Statement of Financing
For the Years Ended September 30, 2006, and 2005

(In Thousands)	2006	2005
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated:		
Obligations Incurred	\$ 2,038,138	\$ 1,831,707
Less: Spending Authority from Offsetting Collections and Recoveries	(903,563)	(1,013,870)
Obligations Net of Offsetting Collections and Recoveries	1,134,575	817,837
Less: Offsetting Receipts	(2,257,865)	(1,787,437)
Net Obligations	(1,123,290)	(969,600)
Other Resources:		
Donations of Property	505	2,177
Transfers In/(Out) Without Reimbursement	(87,485)	(51,621)
Imputed Financing from Costs Absorbed by Others	107,576	67,863
Net Other Resources Used to Finance Activities	20,596	18,419
Total Resources Used to Finance Activities	(1,102,694)	(951,181)
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but Not Yet Provided	(149,885)	(41,464)
Change in Unfilled Customer Orders	(4,015)	174,179
Resources That Fund Expenses Recognized in Prior Periods	(17,016)	(39,650)
Budgetary Offsetting Collections and Receipts That Do Not Affect Net Cost of Operations:		
Credit Program Collections That Increase Liabilities for Allowances for Subsidy	9,775	24,717
Offsetting Receipts Not Part of the Net Cost of Operations	1,721,867	1,263,916
Resources That Finance the Acquisition of Assets	(188,555)	(265,129)
Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	101,679	153,511
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	1,473,850	1,270,080
Total Resources Used to Finance the Net Cost of Operations	371,156	318,899
COMPONENTS OF THE NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD		
Components Requiring or Generating Resources in Future Periods:		
Increase in Annual Leave Liability	27	121
Increase in Environmental and Disposal Liabilities	11,511	29,731
Upward (Downward) Re-estimates of Credit Subsidy Expense	(3)	(323)
(Increase) in Exchange Revenue Receivable from the Public	(43)	-
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	11,492	29,529
Components Not Requiring or Generating Resources:		
Depreciation and Amortization	178,967	189,438
Revaluation of Assets	6,248	2,602
Allocation Transfer Reconciling Items (Note 15)	28,591	37,923
Other	2,304	7,854
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	216,110	237,817
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	227,602	267,346
Net Cost of Operations	\$ 598,758	\$ 586,245

The accompanying notes are an integral part of these statements.

U.S. Department of the Interior Bureau of Reclamation Notes to the Financial Statements for the Years Ended September 30, 2006, and 2005

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The Bureau of Reclamation (Reclamation) was created June 17, 1902, by the Reclamation Act (32 Statute [Stat.] 388), to reclaim the arid and semiarid lands in the Western United States and to provide economic stability in the newly annexed portion of the United States. Reclamation's core mission is the delivery of water and power to customers, while incorporating other demands for water resources, water conservation, new technology, interagency collaboration and coordination, and improvements in management accountability. Reclamation is one of nine reporting bureaus within the U.S. Department of the Interior (Interior), a component of the Federal Government (Government).

B. Basis of Accounting and Presentation

These financial statements have been prepared to report the financial position, net cost of operations, changes in net position, budgetary resources, and reconciliation of net cost of operations to budgetary obligations of Reclamation as required of Interior by the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994. The financial statements have been prepared from Reclamation's books and records in accordance with the Office of Management and Budget's (OMB) Circular A-136, "Financial Reporting Requirements," dated July 24, 2006. Furthermore, the financial statements have been prepared in accordance with Interior's and Reclamation's accounting policies that are summarized herein.

Reclamation's accounting records are kept, and these financial statements have been prepared, in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by the Federal Accounting Standards Advisory Board (FASAB), recognized by the American Institute of Certified Public Accountants (AICPA) as the entity to establish GAAP for the Federal Government. Transactions are recorded on an accrual accounting basis. Under the accrual method, revenues are recognized when earned, and

expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. The accounts are maintained in accordance with the U.S. Department of Treasury's (Treasury) United States Standard General Ledger. Reclamation's fiscal year (FY) covers the period which begins on October 1 and ends on September 30 of the following year. Certain prior year balances have been reclassified to conform to the current year financial statement presentation.

The financial statements should be read with the realization that they are for a component of the Federal Government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides resources and legal authority to do so. Intragovernmental assets and liabilities arise from transactions with other Federal agencies.

The Balance Sheets, Statement of Net Cost, Statement of Changes in Net Position, and Statement of Financing are presented on a consolidated basis. Accordingly, all intrabureau transactions and balances have been eliminated. These transactions primarily pertain to intrabureau use of Reclamation's Working Capital Fund, which provides support services and equipment for Reclamation programs and activities, as well as for other Federal agencies. The Statement of Budgetary Resources is presented on a combined basis; therefore, intrabureau transactions and balances have not been eliminated from this statement.

C. Budgets and Budgetary Accounting

Reclamation receives the majority of its required funding to support its programs through appropriations authorized by the Congress, which are derived from special receipt funds or Treasury's General Fund. Additional budgetary resources are provided by permanent authority, contributed funds, revolving funds, operation and maintenance (O&M) reimbursements from water and power users, and transfers from other Federal agencies.

OMB Circular A-136 requires the Combined Statement of Budgetary Resources to be consistent with the Budget of the United States Government (President's Budget). These financial statements include all funds and accounts under the control of Reclamation, except for allocation transfers from other Federal agency appropriations. An allocation transfer is the amount of budget authority transferred, under specific legislative authority, from one Federal agency, bureau, or account that is set aside in a transfer appropriation account to carry out the purposes of the parent appropriation or fund. The budgetary activity and balances related to these allocation transfer accounts are not included in the Combined Statement of Budgetary Resources or the President's Budget for Reclamation, but the proprietary activity and balances are included in the Consolidated Balance Sheets, Consolidated Statement of Net Cost, and the Consolidated Statement of Changes in Net Position. All allocation transfer budget authority and related activity is reported by the parent appropriation in the President's Budget. The difference between the budgetary and proprietary accounting treatment of allocation transfer accounts is reconciled as part of the Consolidated Statement of Financing.

D. Fund Balance with Treasury

All Reclamation receipts and disbursements are processed by Treasury. The balance in Treasury represents all undisbursed balances in Reclamation's accounts, including funds awaiting disbursement for goods and services received. Also included in this balance are the Reclamation Fund and other unavailable (restricted) receipt funds. See Note 16 for further information on the Reclamation Fund.

E. Investments

Investments consist of non-marketable market-based securities issued by the Federal Investment Branch of the Bureau of the Public Debt. These securities are not traded on any securities exchange but mirror the prices of marketable securities with similar terms. It is expected that investments will be held to maturity; therefore, they are valued at cost and adjusted for amortization of premiums and discounts, if applicable. The premiums and discounts are recognized as adjustments to interest income, utilizing the straight-line method of amortization for short-term securities (i.e., bills) and the interest method for longer-term securities (i.e., notes). Interest on investments is accrued as it is earned.

F. Accounts Receivable

Accounts receivable consists of net amounts owed to Reclamation by other Federal agencies (intragovernmental) and the public. Accounts receivable is stated net of an allowance for uncollectible accounts. The allowance is determined by reviewing accounts receivable aging reports to identify receivables that are considered uncollectible based on various factors, including age, past experience, present market and economic conditions, and characteristics of debtors.

Intragovernmental accounts receivable consist primarily of accrued minerals lease revenue (royalties) which has not yet been transferred to Reclamation by the Minerals Management Service. All accounts receivable due from other Federal entities are unbilled and considered current and fully collectible.

G. Amounts Due from the U.S. Department of Energy

Amounts Due from the U.S. Department of Energy – Western Area Power Administration

Congressional appropriation and other legislative acts have authorized funds to be appropriated from the Reclamation Fund to the Western Area Power Administration (Western), a component entity of the U.S. Department of Energy (DOE) responsible for the transmission and marketing of hydropower generated at Reclamation's facilities. Western's appropriations from the Reclamation Fund are used for capital investment and

O&M activities related to these functions. Western recovers these capital investments, associated interest, and O&M costs through user fees collected from the sale of power and, subsequently, deposits amounts recovered into the Reclamation Fund. Reclamation records an intragovernmental receivable when appropriations are made to Western from the Reclamation Fund. The receivable is decreased when power transmission receipts are returned.

***Amounts Due from the U.S. Department of Energy –
Bonneville Power Administration***

The Bonneville Power Administration (BPA), a component of DOE, is responsible for the transmission and marketing of hydropower generated at Reclamation's facilities in the Pacific Northwest Region. Unlike Western, BPA does not receive appropriations from the Reclamation Fund but has legislatively assumed the repayment obligation for the appropriations used to construct Reclamation's hydropower generation facilities. This legislation, part of the BPA Appropriations Refinancing Act (16 United States Code 8381), requires BPA to recover Reclamation's appropriations related to hydropower generation facilities, plus interest, and to deposit these recoveries into the Reclamation Fund. This intragovernmental receivable is increased when BPA assumes the repayment obligation for power generation assets of the Pacific Northwest Region and decreased when deposits are made to the Reclamation Fund.

H. Loans Receivable

Reclamation operates loan programs that provide Federal assistance to non-Federal organizations for constructing or improving water resource projects in the West. Reclamation's loan programs are authorized under the Small Reclamation Projects Act of 1956 (Public Law [P.L.] 84-984), the Distribution System Loans Act (P.L. 84-130), the Rural Development Policy Act of 1980 (P.L. 96-355) as amended by P.L. 97-273, and the Rehabilitation and Betterment Act (P.L. 81-335). Loan interest rates vary, depending on the applicable legislation; and, in some cases, there is no interest accrued on agricultural and Native American loans. Interest on applicable loans does not accrue until the loan enters repayment status. The loan programs are classified into two major categories, Pre-Credit Reform Loans and Credit Reform Loans.

Pre-Credit Reform Loans

These loans were made prior to FY 1992, and the balances shown represent amounts due to Reclamation, net of an allowance for estimated uncollectible loan balances. The allowance is determined by management for loan balances where collectibility is considered to be uncertain based on various factors, including age, past experience, present market and economic conditions, and characteristics of debtors.

These loans are accounted for in a direct loan liquidating account as established by Treasury. The net loan receivable balance has a corresponding intragovernmental liability (Resources Payable to Treasury), as collections on these loan receivable balances will be transferred annually to Treasury's General Fund in accordance with the requirements of the Credit Reform Act of 1990 (see Note 1.M).

Credit Reform Loans

These loans were made after FY 1991, when the Credit Reform Act of 1990 (Credit Reform) (P.L. 101-508) required extensive changes in accounting for loans to the public. Prior to Credit Reform, funding for loans was provided by congressional appropriation from the general or special funds. Under Credit Reform, loans contain two components, the first of which is borrowed from Treasury. These Treasury borrowings, which will be repaid from loan repayments, are authorized by Credit Reform.

The second component represents the subsidized portion of the loan and is funded by a congressional appropriation. This component represents the estimated cost to the Government resulting primarily from the difference between the loan interest rate and the Treasury interest rate, estimated defaults, and fees associated with making a loan.

I. General Property, Plant, and Equipment

General property, plant, and equipment (PP&E) consists of that property which is used in Reclamation's operations. General PP&E includes the following categories: structures and facilities, land, construction in progress, equipment, vehicles and aircraft, buildings, and internal use software. Real property is not subject to a capitalization threshold, while equipment (including vehicles and aircraft) has a \$15,000 threshold per item. Internal use software is subject to a \$100,000 capitalization threshold. All costs under the applicable threshold are expensed as incurred.

Structures and facilities, comprised primarily of Reclamation's investment in its multipurpose water facilities, are recorded at acquisition cost, net of accumulated depreciation. Costs include direct labor and materials, payments to contractors, and indirect charges for engineering, supervision, and overhead. The costs for power and municipal and industrial (M&I) water facilities also include capitalized interest during construction (IDC), charged in accordance with authorizing legislation.

In general, structures and facilities are depreciated based on the composite service life of each project, using the straight-line method of depreciation. The composite service life is based on the weighted-average estimated useful life of a project's components. Project composite service lives range from 13 to 100 years. Structures and facilities that are included on the *National Register of Historic Places* are considered multiuse heritage assets. Reclamation's multiuse heritage assets are included in the PP&E balances and are further discussed in the "Supplemental Section" under "Federal Stewardship Assets."

Reclamation periodically transfers title of certain single-purpose projects and facilities to non-Federal entities. Before a project can be transferred, Reclamation policy requires that it must meet the following criteria: protect the Treasury's and taxpayers' financial interests, comply with applicable Federal laws, protect interstate compacts and interests, meet Native American trust responsibilities, and protect public aspects of the project. Proposed transfers require congressional authorization. The applicable net loss or net gain on disposition of assets is recorded when the transfer is completed. Title transfers are further discussed in the "Supplemental Section" under "Federal Stewardship Assets."

The land balance is comprised of the acquisition cost of land and permanent land and water rights, as well as the costs of relocating the property of other parties and clearing the land in preparation for its intended use. Lands which were withdrawn from the public domain do not have an acquisition cost and, accordingly, are not represented in this category. Such lands are accounted for as stewardship land, discussed in the "Supplemental Section" under "Federal Stewardship Assets."

Construction in progress is used to accumulate the cost of construction or major renovation of fixed assets during the construction period. Project costs are transferred from construction in progress to structures and facilities when a project or feature of a project is deemed to be substantially complete, is providing benefits and services for the intended purpose, and is generating project purpose revenue, where applicable. Until these three criteria are met, accumulated costs are retained in construction in progress.

Investigations and development costs represent expended funds for such activities as general engineering studies and surveys that are directly related to project construction. Reclamation capitalizes investigation and development costs that are incurred after the decision is made to pursue construction or after construction authorization. These capitalized costs of \$82 million and \$77 million as of September 30, 2006, and 2005, respectively, are included in construction in progress. Reclamation's accounting treatment for investigation and development costs not related to project construction, incurred prior to the decision to pursue construction, or incurred before construction authorization, results in these costs being expensed as incurred.

During the construction phase, Reclamation records imputed financing costs, referred to as IDC. IDC is the assessment of interest using a percentage rate stated in the statutory regulation which authorized the construction project for the Government borrowings to fund the project. These IDC costs are reflected in construction in progress and as imputed financing from costs absorbed by others.

Once the project is completed and operational, the construction costs are transferred to structures and facilities, and interest on investment (IOI) is computed and assessed. IOI applies to the unamortized balance (reimbursable plant costs less repayments realized) of costs allocated to power, M&I water, and other interest-bearing reimbursable functions. The appropriate percentage rate for IOI is also stated in the statutory regulation which authorized

the construction project. These IOI costs are reflected as expenses and as imputed financing from costs absorbed by others.

In past years, Reclamation began the planning of, and construction on, various features included in 12 projects located in Arizona, California, Colorado, North and South Dakota, and Washington, for which activities have either been placed in abeyance or intended benefits have never been provided. These capitalized costs are included in Construction in Abeyance. These projects were authorized to provide various benefits, among them irrigation, fish and wildlife conservation and enhancement, recreation, municipal water supplies, and flood control. Until congressional disposition of these assets is determined, maintenance costs have been, and will continue to be, budgeted and expended to minimize the erosive effects of weather and time and to keep the assets ready for potential completion. The calculation and recording of IDC is suspended after an asset is transferred to abeyance. If the asset is later transferred back to Construction in Progress-General, IDC will be retroactively computed.

Equipment is recorded at acquisition cost less depreciation which accumulates over its estimated useful life using the straight-line method. The estimated useful lives for calculating depreciation on equipment range from 2 to 50 years. When equipment is transferred within Reclamation from one project to another, the transfer is made at the net book value of the property.

Buildings consist of houses, garages, and shops owned by Reclamation and used in power, irrigation, M&I, or multipurpose operations that are not included in structures and facilities of a specific project. Buildings are valued at acquisition cost and are depreciated over their estimated useful lives using the straight-line method. The estimated useful lives for calculating depreciation on buildings range from 15 to 75 years.

Capitalized software includes commercial off-the-shelf (COTS) purchases, contractor-developed software, and internally developed software. For COTS software, the capitalized costs include the amount paid to the vendor for the software; and for contractor-developed software, it includes the amount paid to a contractor to design, program, install, and implement the software. Capitalized costs for internally developed software include the full cost (direct and indirect) incurred during the software development stage. These capitalized costs are limited to those incurred after: (1) management authorizes and commits to a computer software project and believes that it is more likely than not that the project will be completed and the software will be used to perform the intended function with an estimated life of 2 years or more; and (2) the completion of conceptual formulation, design, and testing of possible software project alternatives (the preliminary design stage). Amortization of software is calculated using the straight-line method, based upon an estimated useful life of 5 years.

J. Power Rights

Net power rights represent the original cost less the accumulated amortization of the right or privilege to use the facilities of others or the right to future power generation or power revenues when such rights are not subject to early liquidation. Amortization is calculated by using the straight-line method over the contract life of the agreement. These power rights expire in the year 2017.

K. Stewardship Assets

Heritage Assets

Reclamation's mission is to "manage, develop, and protect water and related resources in an environmentally and economically sound manner in the interest of the American public." Managing and protecting heritage assets are secondary to this mission. A number of Reclamation's non-collectible heritage assets are, in fact, part of Reclamation's infrastructure of dams, powerplants, and irrigation works, and receive high priority with regard to protection and maintenance. Other types of non-collectible heritage assets, in particular archaeological sites, are not related to Reclamation's primary mission, and their management and protection are dictated by Federal cultural resource laws, regulations, and reporting requirements.

The vast majority of Reclamation's collectible heritage assets (i.e., museum property) are archaeological items, and their protection also falls outside the agency's primary mission. Reclamation endeavors to manage these assets to the standards set in the *Departmental Manual 411, Policy and Responsibilities for Managing Museum Property* (411 DM), and other Federal authorities. Reclamation is in the final stages of acquiring an automated system for collection management. Currently, Reclamation reports museum property information to Interior through the Government Performance and Results Act (GPRA); Activity Based Costing; the *Federal Archaeology Program Report to Congress*; and the *Museum Property Summary Report*.

Reclamation's *Cultural Resources Management Policy* (LND PO1) affirms Reclamation's commitment to administering its collectible and non-collectible heritage assets in a spirit of stewardship and in compliance with Federal cultural resources laws and regulations. Tied to the policy statement are a number of Directives and Standards (D&S) that describe mandatory requirements of the cultural resources management program, clarify Reclamation's roles and responsibilities related to cultural resources, and provide direction for consistent implementation of Reclamation's cultural resources program throughout Reclamation. These D&S include *Cultural Resources Management* (LND 02 01); *Inadvertent Discovery of Human Remains on Reclamation Lands* (LND 07 01); and *Inadvertent Discovery of Native American Graves Protection and Repatriation Act (NAGPRA) Cultural Items on Tribal Lands* (LND 10 01).

A separate Museum Property Management Policy, and accompanying D&S, are currently undergoing internal review. These documents provide detailed instructions on managing collectible heritage assets and were developed specifically to address recent changes in Federal requirements not included in existing Reclamation Policy and D&S. Reclamation also maintains a Museum Management Plan (Plan) that is the basic planning and management tool used to track its museum property. The Plan identifies actions required to document, preserve, protect, and maintain museum property to established standards. It also describes problems, prioritizes corrective actions, identifies responsible personnel, and estimates budgets for Reclamation's Museum Property Program activities.

Stewardship Land

There are two types of lands obtained by Reclamation for project and related resource purposes: (1) those that were purchased at a cost to Reclamation projects and beneficiaries and (2) those that were withdrawn from the public domain at no cost to the projects or beneficiaries (in most cases, these lands were previously under the jurisdiction of the Bureau of Land Management or the USDA Forest Service). In Reclamation, these two types of lands are referred to as "acquired lands" and "withdrawn lands," respectively.

Both types of land directly support Reclamation's authorized project and related resource purposes of providing water for the primary project purposes of agricultural, municipal, and industrial uses; generating power; and providing flood control. In accordance with the *Statement of Federal Financial Accounting Standards (SFFAS) No. 29, "Heritage Assets and Stewardship Land,"* adopted in FY 2006, it has been determined that Reclamation's project withdrawn lands represent its stewardship lands. Reclamation reports its stewardship lands in terms of project units as opposed to total acres. This unit of measure corresponds to how Reclamation accounts for both its project lands and acquired inventories and withdrawn stewardship lands.

Reclamation safeguards its withdrawn lands to protect them against waste, loss, and misuse. Reclamation certifies that the condition of nearly all of this agency's withdrawn stewardship lands meets Interior's criteria of "acceptable condition." Thus, the lands are managed and protected in a manner sufficient to support the mission of the agency consistent with the statutory purposes for which the lands were withdrawn or otherwise acquired. There are methods, procedures, and internal controls utilized by Reclamation to assess the condition of these stewardship lands and to take action should the condition deteriorate.

The Reclamation D&S, entitled *Land Withdrawals, Withdrawal Reviews, and Withdrawal Revocations* (LND 03-01), sets forth the basic standards and gives references to the location of applicable procedures for making new land withdrawals, reviewing existing withdrawals, and revoking withdrawals. This D&S references procedures and processes for these three land management functions using the Federal Land Policy and Management Act and associated regulations found at 43 Code of Federal Regulations Part 2300.

Because of the depth of applicable information required by the field to successfully implement the mandatory D&S LND 03-01, the *Reclamation Land Withdrawal Handbook* was developed to provide detailed information and guidelines that complement the D&S. This handbook needs revision as it does contain some inaccurate discretionary guidance, especially relating to reconciliation of Reclamation withdrawn land records with the master plats held by Bureau of Land Management.

In addition, there is the D&S on *Land Disposal* (LND 08-02) that prescribes the procedures, methods, and criteria for disposing of Reclamation lands (excluding title transfer of project facilities under specific authorizing legislation) when Reclamation needs to dispose of or relinquish lands or land interests no longer needed for project purposes. With regard to withdrawn (stewardship) lands, this D&S prescribes general disposal requirements (which include, among other requirements environmental, cultural resources, and hazardous materials compliance reviews), as well as details about various specific statutes which authorize the sale of withdrawn lands.

L. Liabilities

Liabilities represent the amount of monies or other resources that are likely to be paid by Reclamation as the result of a transaction or event that has already occurred. However, no liability can be paid by Reclamation unless budgetary resources are made available through an appropriation or other funding source. The accompanying financial statements also include liabilities for which an appropriation has not been enacted and, thus, are presented as liabilities not covered by budgetary resources.

Reclamation has accrued environmental and disposal liabilities where losses are determined to be probable and the amounts can be estimated. In accordance with Federal accounting guidance, the liability for future cleanup of environmental hazards is probable only when the Government is legally responsible by having created the hazard or is otherwise related to it in such a way that it is legally liable to clean up the contamination. When the Government is not legally liable, but chooses to accept financial responsibility, the event is considered to be "Government-acknowledged." Government-acknowledged events are those of financial consequence to the Government because it chooses to respond to the event. When the Government accepts financial responsibility for cleanup, has an appropriation, and has begun incurring cleanup costs, any unpaid amounts for work performed are included in accounts payable. Changes in cleanup cost estimates are developed in accordance with Interior policy, which addresses systematic processes for cost estimating and will place added emphasis on development and retention of progress made in, and revision of, the cleanup plans, assuming current technology, laws, and regulations.

Contingent liabilities are evaluated on a quarterly basis, and a liability is recorded in the accounting records when an event leading to the probable payment of a liability has occurred, and a reasonable estimate of the potential liability is available. Contingent

liabilities involving legal claims and assertions may be paid by Treasury's Judgment Fund. Treasury provides agencies with information regarding the month and amount of payments actually made, at which time Reclamation recognizes an imputed financing source and cost. Dependent upon the nature of the claims, certain payments made by Treasury's Judgment Fund may be subject to repayment by Reclamation. In these instances, a liability is recognized rather than an imputed financing source.

M. Resources Payable to Treasury

Reclamation receives appropriations from Treasury's General Fund to construct, operate, and maintain various multipurpose projects. Many of the projects have reimbursable components, for which Reclamation is required to recover the capital investment and O&M costs through user fees, namely the sale of water and power. These recoveries are deposited in Treasury's General Fund.

Reclamation records an intragovernmental liability for appropriations determined to be recoverable from project beneficiaries and decreases the liability when payments are received from these beneficiaries and, subsequently, transferred to Treasury's General Fund. Interest is accumulated on this liability pursuant to authorizing project legislation or administrative policy. Interest rates used during FY 2006 and 2005 ranged from 2.63 percent to 8.47 percent. Repayment is generally over a period not to exceed 50 years from the time revenue producing assets are placed in service. Repayment to Treasury's General Fund is dependent upon actual water and power delivered to customers; as such, there is no structured repayment schedule. Actual repayments to Treasury's General Fund in FY 2006 and 2005 were \$10 million and \$128 million, respectively.

Reclamation also received appropriations for the disbursement of loans prior to the enactment of Credit Reform (see Note 1.H). This legislation requires collections of balances for loans obligated prior to FY 1992 be transferred to Treasury's General Fund on an annual basis.

Reclamation has recorded an intragovernmental liability for the net pre-Credit Reform loans receivable balance and total current year collections in the direct loan liquidating account. This liability is reduced when the collections for a given fiscal year are transferred to Treasury's General Fund. Repayments of pre-Credit Reform loan appropriations and interest to Treasury's General Fund totaled \$4 million in FY 2006. There were no transfers made in FY 2005.

N. Accrued Leave

Annual leave is accrued as it is earned by employees and included as part of accrued payroll and benefits. Sick leave is not a vested entitlement and is, therefore, expensed as used, with no liability recognized for unused amounts.

O. Retirement and Other Benefits

Reclamation employees belong to either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Reclamation and its employees contribute to these systems. Both are contributory pension plans. Although Reclamation funds a portion of pension benefits under CSRS and FERS relating to its employees and makes the necessary payroll withholdings from them, it does not report assets associated with these benefit plans. Such amounts are maintained and reported by the Office of Personnel Management (OPM). In accordance with SFFAS No. 5, "Accounting for Liabilities of the Federal Government," Reclamation recorded the FY 2006 and 2005 estimated cost of pension and other retirement benefits and the associated imputed financing sources which are paid by OPM on its behalf. Reclamation funds are not used to pay the cost of these benefits but are a Reclamation operating expense that is reflected as part of the cost of doing business. The estimated cost of pension and other retirement benefits computation rates are provided by OPM actuaries to the employer agencies.

The Department of Labor (DOL) administers the Workers' Compensation Program on behalf of the Government, and all payments to Workers' Compensation Program beneficiaries are made by DOL. Reclamation has two types of liabilities related to workers' compensation. First, Reclamation records a liability to DOL for the amount of actual payments made by DOL but not yet reimbursed by Reclamation. Reclamation reimburses DOL for these payments as funds are appropriated for this purpose. There is generally a 2- to 3-year time period between payment by DOL and receipt of appropriations by Reclamation. Second, Reclamation records an actuarial liability for the estimated amount of future payments for workers' compensation benefits. This actuarial liability represents the present value of the total expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. DOL determines this component on an annual basis using historical benefit payment patterns, wage inflation factors, medical inflation factors, and other variables. Posting of this unfunded liability is in accordance with SFFAS No. 4, "Managerial Cost Accounting: Concepts and Standards for the Federal Government."

P. Revenues and Financing Sources

Exchange Revenues

Exchange revenues earned by Reclamation are classified in accordance with their appropriate responsibility segments and are presented on the Consolidated Statement of Net Cost to match these revenues with their associated costs. Primary examples of exchange revenues are those received from water and power sales, as well as revenue from services provided on a reimbursable basis to governmental and public entities. Exchange revenues are recognized at the time goods or services are provided.

Revenue from Recovery of Reimbursable Capital Costs

To repay a portion of the Federal investment allocated to the construction of reimbursable irrigation and M&I water facilities, Reclamation enters into long-term repayment contracts

and water service contracts with non-Federal (public) water users who receive benefits from these facilities in exchange for annual payments. Also, power marketing agencies enter into agreements with power users, on Reclamation's behalf, to recover capital investment costs allocated to power. Costs associated with multipurpose plants are allocated to the various purposes (principally, power, irrigation, M&I water, fish and wildlife enhancement, recreation, and flood control) through a cost allocation process. Generally, only those costs associated with power, irrigation, and M&I water are reimbursable. Costs associated with purposes such as fish and wildlife enhancement, recreation, and flood control can be non-reimbursable. The typical repayment contract term is up to 40 years but may extend to 50 years or more if authorized by the Congress.

Unmatured repayment contracts are recognized on the Consolidated Balance Sheets when the annual repayment amount is earned, at which time current accounts receivable and current period exchange revenue are recorded. As of September 30, 2006, and 2005, amounts not yet earned under unmatured repayment contracts were \$2.4 billion and \$2.5 billion, respectively.

Under water service contracts and power sales, reimbursable capital costs are recovered through water and power ratesetting processes. Such rates include capital cost factors, among other components, for recovering the reimbursable capital cost over the applicable future payment period. For sales of water and power, a receivable and corresponding exchange revenue is recognized when the water or power has been delivered and billed to the customer.

Non-exchange Revenues and Other Financing Sources

Non-exchange revenues are presented as financing sources on the Consolidated Statement of Changes in Net Position. Non-exchange revenues are inflows of resources, both monetary and non-monetary, that the Government demands by its sovereign power or receives by donation or transfer.

Royalties and other revenue transfers are considered financing sources to Reclamation and are presented on the Consolidated Statement of Changes in Net Position. These financing sources are accretions to the Reclamation Fund, received due to legislative requirement and for which no matching costs were incurred by Reclamation.

Appropriations used is the current reporting period reduction of unexpended appropriations (component of net position), which is recognized as a financing source when goods and services are received and budgetary expenditures are recorded. Appropriations used consist of activities which are funded by Treasury's General Fund and exclude those funded by other sources such as the Reclamation Fund, revolving, or special receipt funds.

Imputed financing sources are a type of non-exchange revenue recognized when operating costs of Reclamation are incurred by funds appropriated to other Federal agencies. For example, certain costs of retirement programs are paid by OPM, and certain legal judgments against Reclamation are paid from Treasury's Judgment Fund.

When costs that are identifiable to Reclamation and directly attributable to Reclamation's operations are paid by other agencies, Reclamation recognizes these amounts as operating costs of Reclamation. Generally, Reclamation is not obligated to repay these costs. The total imputed cost, included in the Consolidated Statement of Net Cost, will not equal the total imputed financing source as shown on the Consolidated Statement of Changes in Net Position due to the capitalization of IDC.

Q. Use of Estimates

The preparation of financial statements requires management of Reclamation to make a number of estimates and assumptions relating to the reported amount of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amount of general PP&E, valuation allowances for receivables, environmental and legal liabilities, obligations related to contracts in progress, and obligations related to employee benefits. Actual results could differ from those estimates.

Note 2. Asset Analysis

Assets of Reclamation include entity, restricted (component of entity assets), and non-entity assets. Entity assets are those available for Reclamation to use in its operations. Restricted assets consist of the Reclamation Fund and other unavailable receipt accounts. Restricted assets cannot be used until appropriated by the Congress. Non-entity assets are not available to finance Reclamation's operations. These items consist of various receivables due from the public that, when collected, are deposited into Treasury's General Fund. Reclamation's assets as of September 30, 2006, and 2005 are summarized in the following tables.

2006 Bureau of Reclamation Annual Report

Asset Analysis
As of September 30, 2006
(In Thousands)

	Entity		Non-Entity	Total
	Unrestricted	Restricted		
ASSETS				
Intragovernmental Assets:				
Fund Balance with Treasury	\$ 1,309,182	\$ 5,721,219	\$ -	\$ 7,030,401
Accounts Receivable	4,879	658,694	-	663,573
Investments, Net	322,045	-	-	322,045
Amounts Due from the U.S. Department of Energy, Net	-	2,631,887	-	2,631,887
Other:				
Advances and Prepayments	1,007	-	-	1,007
Total Intragovernmental Assets	1,637,113	9,011,800	-	10,648,913
Cash	117	-	-	117
Accounts and Interest Receivable, Net	25,563	4,115	74	29,752
Loans and Interest Receivable, Net	157,286	-	-	157,286
General Property, Plant, and Equipment, Net	13,071,874	-	-	13,071,874
Other:				
Advances and Prepayments	19,202	-	-	19,202
Power Rights, Net	122,033	-	-	122,033
Total Other Assets	141,235	-	-	141,235
Total Assets	\$ 15,033,188	\$ 9,015,915	\$ 74	\$ 24,049,177

Asset Analysis
As of September 30, 2005
(In Thousands)

	Entity		Non-Entity	Total
	Unrestricted	Restricted		
ASSETS				
Intragovernmental Assets:				
Fund Balance with Treasury	\$ 1,432,747	\$ 4,657,984	\$ -	\$ 6,090,731
Accounts Receivable	7,735	818,239	-	825,974
Amounts Due from the U.S. Department of Energy, Net	-	2,458,075	-	2,458,075
Other:				
Advances and Prepayments	1,423	-	-	1,423
Total Intragovernmental Assets	1,441,905	7,934,298	-	9,376,203
Cash	100	-	-	100
Accounts and Interest Receivable, Net	26,592	4,860	7	31,459
Loans and Interest Receivable, Net	92,870	33,900	19,698	146,468
General Property, Plant, and Equipment, Net	13,015,525	-	-	13,015,525
Other:				
Advances and Prepayments	37,736	-	-	37,736
Power Rights, Net	160,579	-	-	160,579
Total Other Assets	198,315	-	-	198,315
Total Assets	\$ 14,775,307	\$ 7,973,058	\$ 19,705	\$ 22,768,070

Note 3. Fund Balance with Treasury

Reclamation's Fund Balance with Treasury and the Status of Fund Balance with Treasury as of September 30, 2006, and 2005, are shown in the following table.

Fund Balance with Treasury
As of September 30, 2006, and 2005
(In Thousands)

	2006	2005
Fund Balance with Treasury by Fund Type		
General Funds	\$ 824,678	\$ 725,354
Special Funds	5,829,949	4,779,510
Revolving Funds	242,230	491,021
Trust Funds	81,601	48,376
Other Fund Types	51,943	46,470
Total Fund Balance with Treasury by Fund Type	\$ 7,030,401	\$ 6,090,731
Status of Fund Balance with Treasury		
Unobligated:		
Available	\$ 352,129	\$ 675,316
Unavailable	271	238
Obligated Balance Not Yet Disbursed	915,814	721,584
Subtotal	1,268,214	1,397,138
Fund Balance with Treasury Not Covered by Budgetary Resources		
Unavailable Receipt Accounts	5,721,219	4,657,984
Deposit and Clearing Accounts	40,968	35,609
Subtotal	5,762,187	4,693,593
Total Status of Fund Balance with Treasury	\$ 7,030,401	\$ 6,090,731

Reclamation's fund types and purposes are described below:

General Funds. These funds consist of expenditure accounts used to record financial transactions arising from congressional appropriations.

Special Funds. These funds are credited with receipts from special sources that can be earmarked by law for a specific purpose.

Revolving funds. These funds account for cash flows to and from the Government resulting from operations of public enterprise and working capital funds. The revolving funds are restricted to the purposes set forth in the legislation that established the funds.

Trust Funds. These funds are used for the acceptance and administration of funds contributed from public and private sources and programs and in cooperation with other Federal and State agencies or private donors and other activities.

Other Fund Types. These include credit reform program and financing accounts, miscellaneous receipt accounts, and deposit and clearing accounts. Deposit and clearing accounts are maintained to account for receipts and disbursements awaiting proper classification.

Obligated and unobligated balances reported for the Status of Fund Balance with Treasury do not agree with the obligated and unobligated balances reported on the Combined Statement of Budgetary Resources because the Fund Balance with Treasury amounts include allocation transfer accounts, for which budgetary resources are not recorded. The unavailable receipt accounts category includes the Reclamation Fund, which had a balance of \$5.7 billion and \$4.6 billion as of September 30, 2006, and 2005, respectively.

Note 4. Investments, Net

Reclamation has investment authority authorized in the Lower Colorado River Basin Development Fund and the San Gabriel Basin Restoration Fund, both of which are classified as earmarked funds (see Note 16 for a further discussion of earmarked funds). The investments balance as of September 30, 2006, consists of the cost of non-marketable market-based securities purchased through the Federal Investments Branch of the Bureau of Public Debt (\$322 million), as well as accrued interest earned (\$45 thousand). The market value of these securities is equal to the cost.

The Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash receipts collected from the public for an earmarked fund are deposited in Treasury, which uses the cash for general purposes. Treasury securities are issued to Reclamation as evidence of its receipts. Treasury securities are an asset to Reclamation and a liability to Treasury. Because Reclamation and Treasury are both parts of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or a liability in the Government-wide financial statements.

Treasury securities provide Reclamation with authority to draw upon Treasury to make future expenditures. When Reclamation requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the Government finances all other expenditures.

Note 5. Amounts Due from the U.S. Department of Energy, Net

The following table shows the amounts due from the U.S. Department of Energy as of September 30, 2006, and 2005.

**Amounts Due from the U.S. Department of Energy, Net
As of September 30, 2006, and 2005
(In Thousands)**

	2006	2005
Principal	\$ 6,378,188	\$ 6,166,710
Interest	2,053,503	1,928,373
Cumulative Repayments	(5,778,102)	(5,615,306)
Allowance for Non-Reimbursable Costs	(21,702)	(21,702)
Total Amounts Due from the U.S. Department of Energy, Net	\$ 2,631,887	\$ 2,458,075

Interest rates vary by project and pertinent legislation and ranged from 2.5 to 12.4 percent and 1.25 to 12.4 percent for the years ended September 30, 2006, and 2005, respectively. Repayment terms are generally over a period not to exceed 50 years from the time revenue producing assets are placed in service.

Note 6. Accounts and Interest Receivable, Net

The following table shows the status of accounts receivable due from the public as of September 30, 2006, and 2005.

Accounts and Interest Receivable, Net, Due from the Public As of September 30, 2006, and 2005 (In Thousands)

	2006	2005
Current	\$ 7,583	\$ 4,578
1-180 Days Past Due	1,994	2,376
181-365 Days Past Due	88	370
1 to 2 Years Past Due	575	307
Over 2 Years Past Due	7,499	6,901
Total Billed Accounts and Interest Receivable	17,739	14,532
Unbilled Accounts and Interest Receivable	23,049	25,744
Total Accounts and Interest Receivable	40,788	40,276
Allowance for Doubtful Accounts	(11,036)	(8,817)
Total Accounts and Interest Receivable - Net of Allowance	\$ 29,752	\$ 31,459

Note 7. Loans and Interest Receivable, Net

Entity and non-entity loan balances are combined and presented together here and in the consolidated financial statements. Non-entity loans are disclosed in Note 2, Asset Analysis. The following tables show the status of the non-Federal loans receivable and associated interest receivable as of September 30, 2006, and 2005.

Loans and Interest Receivable, Net As of September 30, 2006 (In Thousands)

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Allowance for Subsidy Cost (Present Value)	Loans and Interest Receivable, Net
Direct Loans Obligated Prior to FY 1992:					
Small Reclamation Projects Act	\$ 35,510	\$ -	\$ (7,255)	\$ -	\$ 28,255
Distribution System Loans Act	3,526	-	-	-	3,526
Rural Development Policy Act	18,370	77	-	-	18,447
Rehabilitation and Betterment Act	4	-	-	-	4
Drought Relief	234	-	-	-	234
Total Direct Loans Obligated Prior to FY 1992	57,644	77	(7,255)	-	50,466
Direct Loans Obligated After FY 1991:					
Small Reclamation Projects Act	114,329	-	-	7,509	106,820
Total Direct Loans	\$ 171,973	\$ 77	\$ (7,255)	\$ (7,509)	\$ 157,286

2006 Bureau of Reclamation Annual Report

**Loans and Interest Receivable, Net
As of September 30, 2005
(In Thousands)**

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Allowance for Subsidy Cost (Present Value)	Loans and Interest Receivable, Net
Direct Loans Obligated Prior to FY 1992:					
Small Reclamation Projects Act	\$ 37,963	\$ -	\$ (7,255)	\$ -	\$ 30,708
Distribution System Loans Act	3,741	-	-	-	3,741
Rural Development Policy Act	18,730	78	-	-	18,808
Rehabilitation and Betterment Act	14	-	-	-	14
Drought Relief	327	-	-	-	327
Total Direct Loans Obligated Prior to FY 1992	60,775	78	(7,255)	-	53,598
Direct Loans Obligated After FY 1991:					
Small Reclamation Projects Act	117,881	-	-	(25,011)	92,870
Total Direct Loans	\$ 178,656	\$ 78	\$ (7,255)	\$ (25,011)	\$ 146,468

Reclamation had seven Credit Reform loans outstanding as of September 30, 2006, and 2005. Loan disbursements during FY 2006 and 2005 were \$8 thousand and \$10 thousand, respectively. Administrative expenses for the years ended September 30, 2006, and 2005, were \$54 thousand and \$78 thousand, respectively. In FY 2006, there were no changes in economic conditions, other risk factors, legislation, credit policies, and assumptions that have had a significant and measurable effect on subsidy rates, subsidy expense, and subsidy re-estimates. For FY 2006 and 2005, there are no additional loan appropriations; therefore, there is no budget subsidy rate.

Re-estimates of the subsidy cost allowance are performed annually. Technical re-estimates adjust the allowance for differences between the projected cash flows that were expected versus actual cash flows. Interest re-estimates adjust the subsidy allowance to provide for the prevailing interest rate at the time the loans were disbursed versus the interest rates assumed in the budget preparation process. These re-estimates resulted in a net downward re-estimate, which resulted in a net decrease to the subsidy cost allowance of \$13.6 million for the year ended September 30, 2006, and a net upward re-estimate of \$20.3 million for the year ended September 30, 2005.

Reconciliation of the subsidy cost allowance as of September 30, 2006, and 2005 is shown in the following table.

**Schedule for Reconciling Subsidy Cost Allowance Balances
(Post-1991 Direct Loans)
As of and for the Years Ended September 30, 2006, and 2005
(In Thousands)**

	2006	2005
Beginning Balance of the Subsidy Cost Allowance	\$ 25,011	\$ 9,477
Adjustments: Subsidy Allowance Amortization	(3,943)	(4,810)
Ending Balance of the Subsidy Cost Allowance Before Re-estimates	21,068	4,667
Add or (Subtract) Subsidy Re-estimates by Component:		
Technical/Default Re-estimate	(4,570)	17,224
Interest Rate Re-estimate	(8,989)	3,120
Ending Balance of the Subsidy Cost Allowance	<u>\$ 7,509</u>	<u>\$ 25,011</u>

Note 8. General Property, Plant, and Equipment, Net

Reclamation's general PP&E categories, with corresponding accumulated depreciation, as of September 30, 2006, and 2005 are shown in the following tables.

**General Property, Plant, and Equipment, Net
As of September 30, 2006
(In Thousands)**

Categories	Acquisition Cost	Accumulated Depreciation	Net Book Value
Structures and Facilities	\$ 17,464,432	\$ (7,982,373)	\$ 9,482,059
Land	1,854,949	-	1,854,949
Construction in Progress:			
Construction in Progress - General	1,059,101	-	1,059,101
Construction in Abeyance	568,624	-	568,624
Equipment, Vehicles, and Aircraft	105,878	(54,853)	51,025
Buildings	77,085	(27,987)	49,098
Internal Use Software:			
In Use	29,885	(23,983)	5,902
In Development	1,116	-	1,116
Total General PP&E	<u>\$ 21,161,070</u>	<u>\$ (8,089,196)</u>	<u>\$ 13,071,874</u>

General Property, Plant, and Equipment, Net
As of September 30, 2005
(In Thousands)

Categories	Acquisition Cost	Accumulated Depreciation	Net Book Value
Structures and Facilities	\$ 17,441,271	\$ (7,841,056)	\$ 9,600,215
Land	1,851,536	-	1,851,536
Construction in Progress:			
Construction in Progress - General	915,584	-	915,584
Construction in Abeyance	557,554	-	557,554
Equipment, Vehicles, and Aircraft	118,655	(66,730)	51,925
Buildings	59,877	(26,568)	33,309
Internal Use Software:			
In Use	24,311	(23,323)	988
In Development	4,414	-	4,414
Total General PP&E	\$ 20,973,202	\$ (7,957,677)	\$ 13,015,525

IDC is included in construction in progress. The authority for charging IDC is in the authorizing legislation for a particular project or administrative policy established pursuant to the law. Generally, the costs allocated to reimbursable functions, except irrigation, are subject to IDC unless otherwise provided by law. The interest rates used in computing IDC are specified in the authorizing legislation; or if rates are not specified, the rates are established by Reclamation laws or administrative policy and are based on the fiscal year in which construction began. The interest rates applied during FY 2006 ranged from 3.22 percent to 8.70 percent and during FY 2005 ranged from 2.125 percent to 11.07 percent. For the years ended September 30, 2006, and 2005, \$9 million and \$8 million, respectively, of IDC costs were capitalized. IDC was also adjusted in FY 2005 for the reallocation of project use and costs for the Bonneville Project in Utah, as authorized by P.L. 102-575 and 107-366. Costs were reallocated from M&I water functions, which are interest-bearing, to irrigation functions, resulting in a reduction to previously capitalized IDC of \$102 million.

The investment in projects held in abeyance as of September 30, 2006, and 2005 ranged from \$59.1 thousand to \$287 million per project, respectively. The investment covers a period from 1965 to the present. Continued planning or construction on these assets has been held in abeyance for various reasons, including such concerns as the execution of cost-share agreements with non-Federal entities and environmental, economic, and international treaty issues. The Congress and local interests continue to pursue acceptable alternatives for the completion of those projects in which there has been a substantial investment. As it is uncertain when construction will resume or benefits will be provided by these assets, classification into construction in abeyance provides the most meaningful and accurate status of their disposition. The Congress has not yet deauthorized any of these assets, nor should it be inferred from this classification that the future viability of them is necessarily in doubt.

Note 9. Liabilities

Liabilities covered by budgetary resources are funded liabilities to be paid with existing budgetary resources. Liabilities not covered by budgetary resources represent those unfunded liabilities for which congressional action is needed before budgetary resources can be provided. These liabilities as of September 30, 2006, and 2005 are combined and presented together in the Consolidated Balance Sheets and are detailed in the following tables.

Liabilities

As of September 30, 2006

(In Thousands)

	Covered by Budgetary Resources		Not Covered by Budgetary Resources		Total
	Current	Non-Current	Current	Non-Current	
Intragovernmental Liabilities:					
Accounts Payable	\$ 29,142	\$ -	\$ -	\$ -	\$ 29,142
Debt	-	95,141	-	-	95,141
Other:					
Accrued Employee Benefits	8,793	-	4,742	8,498	22,033
Advances, Deferred Revenue, and Deposit Funds	5,285	-	-	-	5,285
Judgment Fund Liability	-	-	-	47,950	47,950
Resources Payable to Treasury	-	-	46,118	1,798,592	1,844,710
Other Liabilities	-	-	-	73	73
Total Other Liabilities	14,078	-	50,860	1,855,113	1,920,051
Total Intragovernmental Liabilities	43,220	95,141	50,860	1,855,113	2,044,334
Public Liabilities:					
Accounts Payable	138,706	75,029	-	-	213,735
Federal Employee Benefits, Actuarial	-	-	-	88,353	88,353
Environmental and Disposal Liabilities	-	-	-	46,871	46,871
Other:					
Accrued Payroll and Benefits	19,717	-	-	27,380	47,097
Advances, Deferred Revenue, and Deposit Funds	156,043	-	47,205	293,802	497,050
Contingent Liabilities	-	-	-	962	962
Other Liabilities	3,671	-	-	91	3,762
Total Other Liabilities	179,431	-	47,205	322,235	548,871
Total Public Liabilities	318,137	75,029	47,205	457,459	897,830
Total Liabilities	\$ 361,357	\$ 170,170	\$ 98,065	\$ 2,312,572	\$ 2,942,164

Liabilities
As of September 30, 2005
(In Thousands)

	Covered by Budgetary Resources		Not Covered by Budgetary Resources		Total
	Current	Non-Current	Current	Non-Current	
Intragovernmental Liabilities:					
Accounts Payable	\$ 24,651	\$ -	\$ -	\$ -	\$ 24,651
Debt	-	96,811	-	-	96,811
Other:					
Accrued Employee Benefits	8,850	-	4,466	8,041	21,357
Advances, Deferred Revenue, and Deposit Funds	8,743	-	38	-	8,781
Judgment Fund Liability	-	-	-	47,950	47,950
Resources Payable to Treasury	-	-	44,525	1,736,445	1,780,970
Other Liabilities	-	-	-	19,689	19,689
Total Other Liabilities	17,593	-	49,029	1,812,125	1,878,747
Total Intragovernmental Liabilities	42,244	96,811	49,029	1,812,125	2,000,209
Public Liabilities:					
Accounts Payable	124,370	77,172	-	-	201,542
Federal Employee Benefits, Actuarial	-	-	-	88,702	88,702
Environmental and Disposal Liabilities	-	-	-	35,360	35,360
Other:					
Accrued Payroll and Benefits	21,632	-	-	27,354	48,986
Advances, Deferred Revenue, and Deposit Funds	105,578	-	42,379	307,332	455,289
Contingent Liabilities	-	-	-	9,515	9,515
Other Liabilities	3,326	-	-	115	3,441
Total Other Liabilities	130,536	-	42,379	344,316	517,231
Total Public Liabilities	254,906	77,172	42,379	468,378	842,835
Total Liabilities	\$ 297,150	\$ 173,983	\$ 91,408	\$ 2,280,503	\$ 2,843,044

Note 10. Debt

Reclamation makes loans which are subject to the provisions of Credit Reform. Under Credit Reform, loans consist of two components—the part borrowed from Treasury and the appropriated part to cover the estimated subsidy. The maturity dates for these loans as of September 30, 2006, range from 2012 to 2047. The interest rate used to calculate interest owed to Treasury as of September 30, 2006, and 2005 ranged from 4.67 percent to 7.59 percent and 6.01 to 6.82, respectively. As annual installments are received from loan recipients, any funds in excess of interest are applied against the outstanding principal owed to Treasury. The liabilities shown in the following table represent amounts borrowed from Treasury to fund Credit Reform loans as of and for the years ended September 30, 2006, and 2005.

Debt

As of and for the Years Ended September 30, 2006, and 2005
(In Thousands)

Intragovernmental Debt: Credit Reform Borrowings	2006	2005
Beginning Balance	\$ 96,811	\$ 114,098
New Borrowing	1,584	995
Repayments	(3,254)	(18,282)
Ending Balance	\$ 95,141	\$ 96,811

Note 11. Contingent Liabilities and Environmental and Disposal Liabilities

Reclamation is currently involved in various environmental cleanup actions and legal proceedings. Disclosure and recognition of these contingent liabilities have been made in accordance with SFFAS No. 5, "Accounting for Liabilities of the Federal Government." The liabilities are accrued when probable and reasonably estimable. Additionally, liabilities are disclosed in the estimated range of loss when the conditions for liability recognition are not met and the likelihood of loss is more than remote.

The accrued and potential environmental and disposal liabilities and contingent liabilities as of September 30, 2006, and 2005 are summarized in the following tables.

Contingent Liabilities and Environmental and Disposal Liabilities
As of September 30, 2006
(In Thousands)

	Accrued Liabilities	Total Estimated Range of Loss Including Accrued Amounts	
		Lower End of Range	Upper End of Range
Contingent Liabilities			
Probable	\$ 962	\$ 962	\$ 1,882
Reasonably Possible		200,100	200,100
Environmental and Disposal Liabilities			
Probable	46,871	46,871	92,725
Reasonably Possible		29	7,390

Contingent Liabilities and Environmental and Disposal Liabilities
As of September 30, 2005
(In Thousands)

	Accrued Liabilities	Total Estimated Range of Loss Including Accrued Amounts	
		Lower End of Range	Upper End of Range
Contingent Liabilities			
Probable	\$ 9,515	\$ 9,515	\$ 12,814
Reasonably Possible		201,000	234,300
Environmental and Disposal Liabilities			
Probable	35,360	35,360	65,255
Reasonably Possible		380	2,530

A. Contingent Liabilities – Legal Claims and Assertions

Reclamation is party to a number of lawsuits and other actions where monetary amounts are sought from Reclamation, including construction cost claims, lawsuits over repayment of certain project costs, and water rights claims.

B. Environmental and Disposal Liabilities

Reclamation has Government-related potential environmental and disposal liabilities associated with hazardous waste removal, containment, or disposal. Reclamation’s hazardous wastesites include vehicle maintenance facilities and landfills. These sites have various types of contamination, including soil contamination from waste petroleum, heavy metal, and other regulated toxic waste. Reclamation’s cleanup sites fall under the purview of the Resources Conservation and Recovery Act of 1976, the Clean Air Act, the Endangered Species Act, and the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, which created the Superfund Program.

The estimated range of loss includes the expected future cleanup costs and, for those sites where the future liability is unknown, the cost of studies necessary to evaluate response requirements. There are no material changes in total estimated cleanup costs that are due to changes in law or technology.

Note 12. Operating Leases

Most of Reclamation’s facilities are leased through the General Services Administration (GSA), which charges rent that is intended to approximate commercial rental rates. For property leased through GSA, Reclamation does not always execute an occupancy agreement; however, a 120- to 180-day notice to vacate is normally required. For the years ended

September 30, 2006, and 2005, the amount of lease expense for federally owned and non-federally owned property leased through GSA was \$20.1 million and \$20.5 million, respectively.

In addition to leases with GSA, Reclamation had, for the years ended September 30, 2006, and 2005, operating lease payments to non-Federal entities in the amount of \$3.0 million and \$2.8 million, respectively. These leases were primarily for office space and office equipment. Reclamation has an option to renew many of its operating leases at terms similar to the initial terms.

The following is a schedule by year of future minimum lease payments as of September 30, 2006. Future operating leases payments are calculated based on the terms of the lease or, if the lease is silent, an inflationary factor of 2.4 percent is applied for FY 2007 and beyond.

Operating Lease Commitments
As of September 30, 2006
(In Thousands)

Fiscal Year	GSA Real Property	Other Real Property	Personal Property	Total
2007	\$ 20,623	\$ 2,098	\$ 533	\$ 23,254
2008	21,118	2,017	487	23,622
2009	21,625	1,826	269	23,720
2010	22,144	1,488	4	23,636
2011	22,675	1,390	-	24,065
Thereafter	23,219	1,703	-	24,922
Total Future Operating Lease Payments	\$ 131,404	\$ 10,522	\$ 1,293	\$ 143,219

Note 13. Consolidated Statement of Net Cost

The Consolidated Statement of Net Cost is presented in accordance with the strategic plan in place for that fiscal year, as required under the Government Performance and Results Act. Consolidating Statements of Net Cost, shown by regional organization and reporting segment for the years ended September 30, 2006, and 2005, are presented at the end of Note 16.

Note 14. Combined Statement of Budgetary Resources

The Combined Statement of Budgetary Resources has been prepared to coincide with the amounts shown in the President's Budget. The FY 2005 amounts shown have been reconciled to the President's Budget without exception; however, the actual amounts for FY 2006 in the President's Budget have not been published at the time these financial statements were prepared. The President's Budget with the actual FY 2006 amounts is estimated to be released in February 2007 and can be located at the OMB Web site: (<www.whitehouse.gov/omb>).

Offsetting receipts are collections that are credited to general fund, special fund, or trust fund receipt accounts and offset gross outlays. Unlike offsetting collections, which are credited to expenditure accounts and offset outlays at the account level, offsetting receipts are not authorized to be credited to expenditure accounts and are used to offset outlays at the bureau level. The legislation that authorizes the offsetting receipts may earmark them for a specific purpose and either appropriate them for expenditure for that purpose or require them to be appropriated in annual appropriations acts before they can be spent.

Reclamation’s borrowing authority is provided under the Credit Reform Act of 1990 (refer to Note 7 for additional information on Credit Reform loans). The repayment terms and provisions of these loans are not more than 40 years from the date when the principal benefits of the projects first become available. The collections on these loans in excess of the interest due Treasury are applied to the outstanding principal owed Treasury.

Reclamation has two major budget accounts that are classified as permanent indefinite appropriations, which are available until expended. The Colorado River Dam Fund – Boulder Canyon Project is an available receipt fund into which various operating revenues of the Hoover Dam are covered, mainly from the sale of power generated at the dam. Reclamation Trust Funds include amounts received from public benefactors that are used to finance restoration and other activities. These permanent indefinite appropriation accounts are classified as exempt from apportionment.

Other Reclamation funds, including those not specifically mentioned here, are subject to annual apportionment by OMB and classified as Category B apportionments. Detailed amounts for each of Reclamation’s major budget accounts are included in the Combining Statements of Budgetary Resources located in the “Supplemental Section” of this report. All unobligated balances presented are available until expended.

All appropriation language contains specific and/or general authorizations. These authorizations may be defined as legislative parameters that frame the funding and Federal agency policy for executing programs. These authorizations also direct how Reclamation must treat other assets it may acquire as a result of executing operating programs. Since both specific and general authorizations are integral components of all legislation, Reclamation does not view them as restrictions or legal encumbrances on available funding.

Obligations incurred by budget category for Reclamation’s budgetary accounts and non-budgetary credit program financing account are presented in the following tables.

**Obligations Incurred by Budget Category
For the Year Ended September 30, 2006
(In Thousands)**

	Apportioned Category B	Exempt From Apportionment	Total
Direct	\$ 1,070,785	\$ 99,292	\$ 1,170,077
Reimbursable	868,061	-	868,061
Total Obligations Incurred	\$ 1,938,846	\$ 99,292	\$ 2,038,138

**Obligations Incurred by Budget Category
For the Year Ended September 30, 2005
(In Thousands)**

	Apportioned Category B	Exempt From Apportionment	Total
Direct	\$ 951,317	\$ 74,481	\$ 1,025,798
Reimbursable	805,909	-	805,909
Total Obligations Incurred	\$ 1,757,226	\$ 74,481	\$ 1,831,707

For the years ended September 30, 2006, and 2005, undelivered orders were \$706 million and \$556 million, respectively.

Note 15. Consolidated Statement of Financing

A. Allocation Transfer Reconciling Items

Reclamation receives budget resources from other Federal entities in the form of “allocation transfers.” The recipient agency (Child) reports the proprietary activity in their Consolidated Balance Sheets, Consolidated Statement of Net Cost, and Consolidated Statement of Changes in Net Position. However, the budgetary activity for these allocation transfers is reported by the providing agency (Parent) in their Combined Statement of Budgetary Resources, as required by OMB Circular A-11, “Preparation, Submission, and Execution of the Budget.” This treatment creates a reconciling difference between the proprietary statements and the Combined Statement of Budgetary Resources, which is shown in the Consolidated Statement of Financing.

The following table summarizes the allocation transfers and related amounts that are reported as reconciling differences in the Consolidated Statement of Financing.

Allocation Transfer Reconciling Items
As of and for the Years Ended September 30, 2006, and 2005
(In Thousands)

Trading Partner	Nature of Transfer	FY 2006	FY 2005
Reclamation as the Recipient Agency (Child):			
Department of Labor - Job Corps	Employment and Training Services	\$ 31,131	\$ 29,335
Department of the Interior - Office of the Secretary	Central Hazardous Materials Fund Programs	1,202	576
Department of the Interior - Bureau of Indian Affairs	Construction of Distribution Systems of the Navajo Indian Irrigation Project	(3,804)	7,410
Department of the Interior - Office of the Secretary	Natural Resources and Damage Assessment and Restoration Activities	62	91
Department of Transportation - Highway Trust Fund	Maintenance of Highways on Reclamation Lands	-	511
Net Allocation Transfer Reconciling Items		\$ 28,591	\$ 37,923

B. Change in Unfunded Liabilities

The Consolidated Statement of Financing includes a section depicting the change in certain unfunded liabilities. The amounts in this section do not necessarily correlate to the change in liabilities not covered by budgetary resources as shown in Note 9, Liabilities Analysis. Differences are primarily the result of certain Treasury requirements related to changes in various liabilities which are reported on the Consolidated Statement of Financing. These requirements are dependent upon whether the change results in an increase or decrease to the liability account. Additionally, some liability accounts not covered by budgetary resources are not included in the Consolidated Statement of Financing.

Note 16. Earmarked Funds

Reclamation receives revenues and financing sources from earmarked funds. In accordance with SFFAS No. 27, "Identifying and Reporting Earmarked Funds," effective October 1, 2005, these specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes and are accounted for separately from the Government's general revenues. Activity for earmarked funds in FY 2005 has not been restated in accordance with the provisions of SFFAS No. 27.

In FY 2006, there has been no change in legislation that significantly changes the purpose of Reclamation's earmarked funds or redirects a material portion of the accumulated balance. Reclamation has established unique cost centers within the accounting system for each of the specified activities under each earmarked fund.

Reclamation Fund

The Reclamation Fund was established by the Reclamation Act of 1902 (32 Stat. 388). It is a restricted, unavailable receipt fund into which a substantial portion of Reclamation's revenues (mostly repayment of capital investment costs, associated interest, and O&M reimbursements from water and power users) and receipts from other Federal agencies (primarily revenues from certain Federal mineral royalties and hydropower transmission) are deposited. No expenditures are made directly from the Reclamation Fund; however, funds are transferred from the Reclamation Fund into Reclamation's appropriated expenditure funds or to other Federal agencies pursuant to congressional appropriation acts to invest and reinvest in the reclamation of arid lands in the Western United States.

Water and Related Resources Fund

The Water and Related Resources Fund receives the majority of its funding from appropriations derived from the Reclamation Fund. These funds are used for Reclamation's central mission of delivering water and generating hydropower in the Western United States. Costs associated with multipurpose structures and facilities are allocated to the various purposes, principally: power, irrigation, M&I water, fish and wildlife enhancement, recreation, and flood control. Generally, only those costs associated with power, irrigation, and M&I water are reimbursable. Costs associated with purposes such as fish and wildlife enhancement, recreation, and flood control can be non-reimbursable. Capital investment costs are recovered over a 40-year period but may extend to 50 years or more if authorized by the Congress. Recovery of these capital investment costs and revenues generated from these activities are returned to the Reclamation Fund.

Lower Colorado River Basin Fund

The Lower Colorado River Basin Fund receives funding from multiple sources for specific purposes as provided under P.L. 90-537 and amended by P.L. 108-451. Funding sources include appropriations, Federal revenues from the Central Arizona Project, Federal revenues from the Boulder Canyon and Parker-Davis Projects, the Western Area Power Administration, Federal revenues from the Northwest-Pacific Southwest intertie in the States of Nevada and Arizona, and revenues earned from investing in Treasury securities. Funding sources may be retained and are available without further appropriation. The fund provides for irrigation development and management activities within the Lower Colorado River Basin including operation, maintenance, replacements, and emergency expenditures for facilities of the Colorado River Storage Project and participating projects.

Other Earmarked Funds

The Reclamation Fund, Water and Related Resources Fund, and the Lower Colorado River Basin Fund comprise 88 percent of Reclamation's total earmarked net position. Other earmarked funds are presented on an aggregated basis in the following table and include:

- Upper Colorado River Basin Fund
- Colorado River Dam Fund – Boulder Canyon Project
- San Gabriel Restoration Fund
- Central Valley Project Restoration Fund

2006 Bureau of Reclamation Annual Report

- Reclamation Trust Funds
- Klamath – Water and Energy
- North Platte Project – Facility Operations
- North Platte – Farmers Irrigation District – Facility Operations
- Reclamation Recreation, Entrance and Use Fees
- Reclamation Fund General Administration Expenses
- Job Corps Quarters Operation and Maintenance

Condensed financial information for Reclamation's earmarked funds are presented in the following table as of and for the year ended September 30, 2006.

Earmarked Funds

As of and for the Year Ended September 30, 2006

(In Thousands)

	Reclamation Fund	Water and Related Resources	Lower Colorado River Basin Fund	Other Earmarked Funds	Total Earmarked Funds
ASSETS					
Fund Balance with Treasury	\$ 5,699,905	\$ 730,745	\$ 38,647	\$ 365,020	\$ 6,834,317
Investments, Net	-	-	305,043	17,002	322,045
Accounts and Interest Receivable, Net	661,373	15,522	8,759	7,148	692,802
Loans and Interest Receivable, Net	2,631,887	-	-	-	2,631,887
General Property, Plant, and Equipment, Net	-	7,329,633	2,988,498	2,541,936	12,860,067
Other Assets	-	21,313	120,377	16	141,706
TOTAL ASSETS	\$ 8,993,165	\$ 8,097,213	\$ 3,461,324	\$ 2,931,122	\$ 23,482,824
LIABILITIES					
Accounts Payable	\$ 1	\$ 124,000	\$ 11,119	\$ 103,249	\$ 238,369
Resources Payable to Treasury	-	1,751,384	-	-	1,751,384
Other Liabilities	31	274,261	1,522	417,645	693,459
TOTAL LIABILITIES	32	2,149,645	12,641	520,894	2,683,212
NET POSITION					
Unexpended Appropriations	-	210,820	8,077	30,604	249,501
Cumulative Results of Operations	8,993,133	5,736,748	3,440,606	2,379,624	20,550,111
TOTAL NET POSITION	8,993,133	5,947,568	3,448,683	2,410,228	20,799,612
TOTAL LIABILITIES AND NET POSITION	\$ 8,993,165	\$ 8,097,213	\$ 3,461,324	\$ 2,931,122	\$ 23,482,824
COST/REVENUES					
Gross Costs	\$ (6,305)	\$ 1,124,451	\$ 163,008	\$ 302,560	\$ 1,583,714
Earned Revenues	(389,861)	(201,700)	(189,237)	(230,738)	(1,011,536)
NET COST OF OPERATIONS	\$ (396,166)	\$ 922,751	\$ (26,229)	\$ 71,822	\$ 572,178
NET POSITION					
Net Position, Beginning Balance	\$ 7,952,123	\$ 5,961,233	\$ 3,402,053	\$ 2,321,587	\$ 19,636,996
Appropriations Received/Transferred	-	92,250	24,808	72,174	189,232
Royalties Retained	1,487,423	-	-	-	1,487,423
Non-Exchange Revenue and Donations	4	9	496	-	509
Other Financing Sources:					
Transfers In/(Out) without Reimbursement	(842,623)	746,123	(4,903)	51,477	(49,926)
Imputed Financing from Costs Absorbed by Others	40	70,704	-	36,812	107,556
Net Cost of Operations	396,166	(922,751)	26,229	(71,822)	(572,178)
Change in Net Position	1,041,010	(13,665)	46,630	88,641	1,162,616
NET POSITION, ENDING BALANCE	\$ 8,993,133	\$ 5,947,568	\$ 3,448,683	\$ 2,410,228	\$ 20,799,612

2006 Bureau of Reclamation Annual Report

**U.S. Department of the Interior
Bureau of Reclamation
Consolidating Statement of Net Cost
For the Year Ended September 30, 2006**

(In Thousands)	Pacific Northwest Region	Mid-Pacific Region
RESOURCE USE		
Deliver Water in an Environmentally Responsible and Cost-Efficient Manner:		
Intragovernmental Costs	\$ 35,161	\$ 72,074
Public Costs	118,498	171,241
Total Costs	<u>153,659</u>	<u>243,315</u>
Intragovernmental Earned Revenues	(65,732)	(185)
Public Earned Revenues	(17,388)	(188,859)
Total Earned Revenues	<u>(83,120)</u>	<u>(189,044)</u>
Net Cost	<u>70,539</u>	<u>54,271</u>
Generate Hydropower in an Environmentally Responsible and Cost-Efficient Manner:		
Intragovernmental Costs	20,034	11,779
Public Costs	40,640	34,084
Total Costs	<u>60,674</u>	<u>45,863</u>
Intragovernmental Earned Revenues	(35,700)	(551)
Public Earned Revenues	(9,444)	(74,734)
Total Earned Revenues	<u>(45,144)</u>	<u>(75,285)</u>
Net Cost	<u>15,530</u>	<u>(29,422)</u>
RESOURCE PROTECTION		
Improve Health of Watersheds and Landscapes, Sustain Biological Communities, and Protect Cultural Resources:		
Intragovernmental Costs	204	360
Public Costs	500	302
Total Costs	<u>704</u>	<u>662</u>
Intragovernmental Earned Revenues	(306)	-
Public Earned Revenues	(81)	(83)
Total Earned Revenues	<u>(387)</u>	<u>(83)</u>
Net Cost	<u>317</u>	<u>579</u>
RECREATION		
Provide Quality and Fair Value in Recreation:		
Intragovernmental Costs	1,739	3,477
Public Costs	4,767	9,508
Total Costs	<u>6,506</u>	<u>12,985</u>
Intragovernmental Earned Revenues	(3,635)	(13)
Public Earned Revenues	(962)	(13,732)
Total Earned Revenues	<u>(4,597)</u>	<u>(13,745)</u>
Net Cost	<u>1,909</u>	<u>(760)</u>
CENTRALIZED PROGRAM SUPPORT AND OTHER		
Working Capital Fund, Policy and Administration, and Other:		
Intragovernmental Costs	15,542	19,993
Public Costs	35,340	47,033
Total Costs	<u>50,882</u>	<u>67,026</u>
Intragovernmental Earned Revenues	(38,093)	(56,956)
Public Earned Revenues	(8,551)	(7,611)
Total Earned Revenues	<u>(46,644)</u>	<u>(64,567)</u>
Net Cost	<u>4,238</u>	<u>2,459</u>
Total Intragovernmental Costs	<u>72,680</u>	<u>107,683</u>
Total Public Costs	<u>199,745</u>	<u>262,168</u>
Total Costs	<u>272,425</u>	<u>369,851</u>
Total Intragovernmental Earned Revenues	<u>(143,466)</u>	<u>(57,705)</u>
Total Public Earned Revenues	<u>(36,426)</u>	<u>(285,019)</u>
Total Earned Revenues	<u>(179,892)</u>	<u>(342,724)</u>
Net Cost of Operations	<u>\$ 92,533</u>	<u>\$ 27,127</u>

Lower Colorado Region	Upper Colorado Region	Great Plains Region	Commissioner's Office	Combined Total	Intrabureau Eliminations	Consolidated Total
\$ 31,926	\$ 78,121	\$ 29,037	\$ 50,039	\$ 296,358	\$ (7,723)	\$ 288,635
214,262	72,836	153,244	70,579	800,660	-	800,660
246,188	150,957	182,281	120,618	1,097,018	(7,723)	1,089,295
(17,882)	(9,835)	(8)	(77)	(93,719)	7,723	(85,996)
(207,750)	(51,066)	(34,341)	(66)	(499,470)	-	(499,470)
(225,632)	(60,901)	(34,349)	(143)	(593,189)	7,723	(585,466)
20,556	90,056	147,932	120,475	503,829	-	503,829
17,916	19,846	12,157	2,085	83,817	(3,102)	80,715
38,517	19,772	28,532	94	161,639	-	161,639
56,433	39,618	40,689	2,179	245,456	(3,102)	242,354
(33,448)	(4,014)	(51,898)	-	(125,611)	3,102	(122,509)
(42,211)	(20,512)	(10,031)	(1)	(156,933)	-	(156,933)
(75,659)	(24,526)	(61,929)	(1)	(282,544)	3,102	(279,442)
(19,226)	15,092	(21,240)	2,178	(37,088)	-	(37,088)
16,319	11,323	149	1,115	29,470	(1,475)	27,995
14,271	23,047	519	315	38,954	-	38,954
30,590	34,370	668	1,430	68,424	(1,475)	66,949
(1,456)	(1,878)	-	-	(3,640)	1,475	(2,165)
(15,036)	(9,757)	(156)	(1)	(25,114)	-	(25,114)
(16,492)	(11,635)	(156)	(1)	(28,754)	1,475	(27,279)
14,098	22,735	512	1,429	39,670	-	39,670
2,413	647	299	9	8,584	(98)	8,486
8,781	862	636	25	24,579	-	24,579
11,194	1,509	935	34	33,163	(98)	33,065
(764)	(125)	-	-	(4,537)	98	(4,439)
(7,893)	(648)	(134)	-	(23,369)	-	(23,369)
(8,657)	(773)	(134)	-	(27,906)	98	(27,808)
2,537	736	801	34	5,257	-	5,257
20,265	18,533	14,663	136,833	225,829	(337,217)	(111,388)
37,874	39,176	24,118	128,595	312,136	-	312,136
58,139	57,709	38,781	265,428	537,965	(337,217)	200,748
(45,590)	(49,770)	(33,476)	(184,197)	(408,082)	337,217	(70,865)
(12,884)	(8,665)	(1,648)	(3,434)	(42,793)	-	(42,793)
(58,474)	(58,435)	(35,124)	(187,631)	(450,875)	337,217	(113,658)
(335)	(726)	3,657	77,797	87,090	-	87,090
88,839	128,470	56,305	190,081	644,058	(349,615)	294,443
313,705	155,693	207,049	199,608	1,337,968	-	1,337,968
402,544	284,163	263,354	389,689	1,982,026	(349,615)	1,632,411
(99,140)	(65,622)	(85,382)	(184,274)	(635,589)	349,615	(285,974)
(285,774)	(90,648)	(46,310)	(3,502)	(747,679)	-	(747,679)
(384,914)	(156,270)	(131,692)	(187,776)	(1,383,268)	349,615	(1,033,653)
\$ 17,630	\$ 127,893	\$ 131,662	\$ 201,913	\$ 598,758	\$ -	\$ 598,758

2006 Bureau of Reclamation Annual Report

**U.S. Department of the Interior
Bureau of Reclamation
Consolidating Statement of Net Cost
For the Year Ended September 30, 2005**

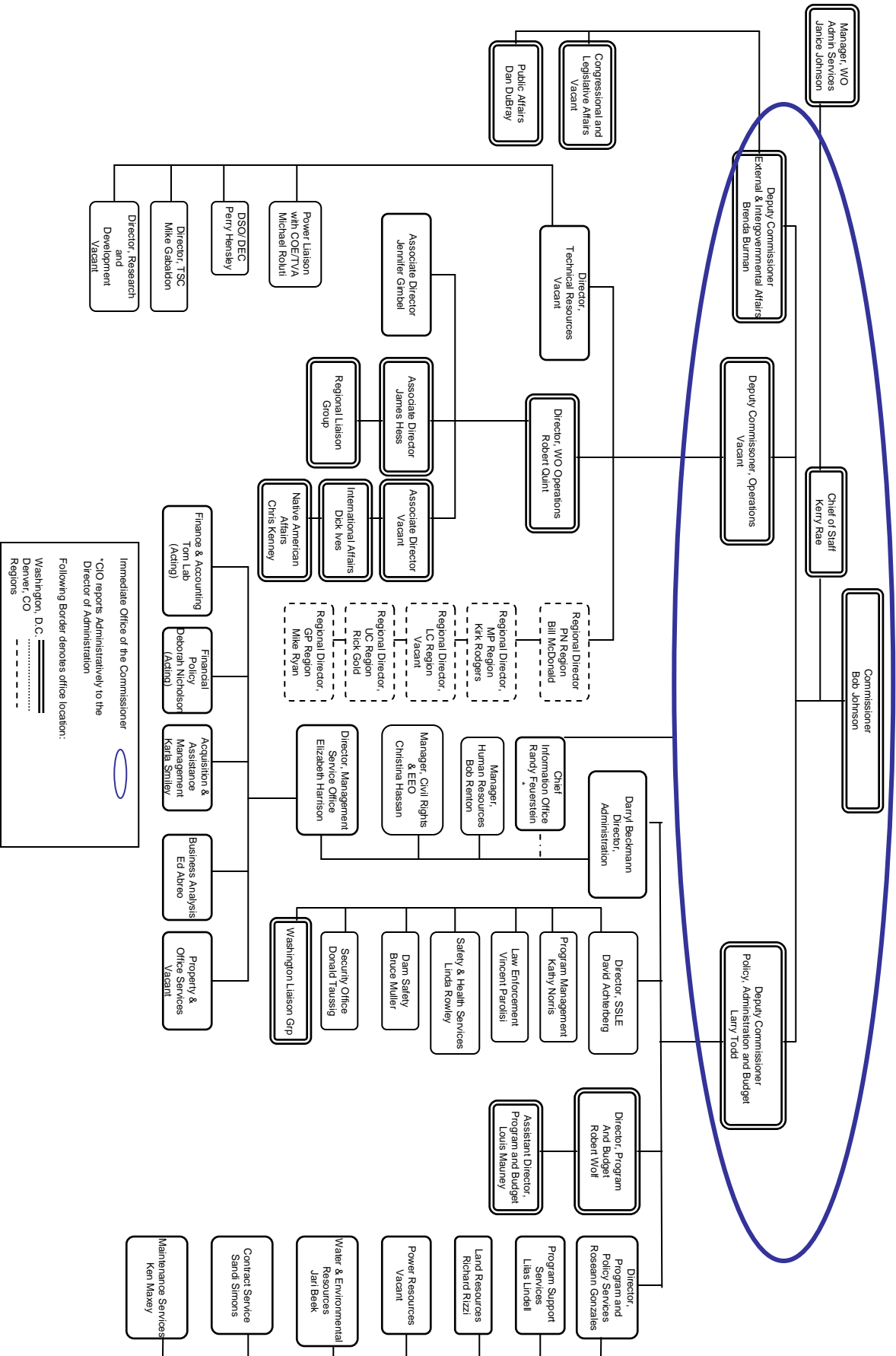
(In Thousands)	Pacific Northwest Region	Mid-Pacific Region
RESOURCE USE		
Deliver Water in an Environmentally Responsible and Cost-Efficient Manner:		
Intragovernmental Costs	\$ 34,345	\$ 99,464
Public Costs	77,318	141,114
Total Costs	<u>111,663</u>	<u>240,578</u>
Intragovernmental Earned Revenues	(691)	(117)
Public Earned Revenues	<u>(20,310)</u>	<u>(149,828)</u>
Total Earned Revenues	<u>(21,001)</u>	<u>(149,945)</u>
Net Cost	<u>90,662</u>	<u>90,633</u>
Generate Hydropower in an Environmentally Responsible and Cost-Efficient Manner:		
Intragovernmental Costs	22,864	14,443
Public Costs	40,746	28,728
Total Costs	<u>63,610</u>	<u>43,171</u>
Intragovernmental Earned Revenues	(99,564)	(700)
Public Earned Revenues	<u>(11,659)</u>	<u>(76,061)</u>
Total Earned Revenues	<u>(111,223)</u>	<u>(76,761)</u>
Net Cost	<u>(47,613)</u>	<u>(33,590)</u>
RESOURCE PROTECTION		
Improve Health of Watersheds and Landscapes, Sustain Biological Communities, and Protect Cultural Resources:		
Intragovernmental Costs	131	39
Public Costs	364	33
Total Costs	<u>495</u>	<u>72</u>
Intragovernmental Earned Revenues	(2)	-
Public Earned Revenues	<u>(26)</u>	<u>(8)</u>
Total Earned Revenues	<u>(28)</u>	<u>(8)</u>
Net Cost	<u>467</u>	<u>64</u>
RECREATION		
Provide Quality and Fair Value in Recreation:		
Intragovernmental Costs	1,753	3,627
Public Costs	4,344	4,724
Total Costs	<u>6,097</u>	<u>8,351</u>
Intragovernmental Earned Revenues	(35)	(72)
Public Earned Revenues	<u>(392)</u>	<u>(707)</u>
Total Earned Revenues	<u>(427)</u>	<u>(779)</u>
Net Cost	<u>5,670</u>	<u>7,572</u>
CENTRALIZED PROGRAM SUPPORT AND OTHER		
Working Capital Fund, Policy and Administration, and Other:		
Intragovernmental Costs	12,825	18,213
Public Costs	38,759	45,756
Total Costs	<u>51,584</u>	<u>63,969</u>
Intragovernmental Earned Revenues	(40,215)	(54,381)
Public Earned Revenues	<u>(8,930)</u>	<u>(6,453)</u>
Total Earned Revenues	<u>(49,145)</u>	<u>(60,834)</u>
Net Cost	<u>2,439</u>	<u>3,135</u>
Total Intragovernmental Costs	<u>71,918</u>	<u>135,786</u>
Total Public Costs	<u>161,531</u>	<u>220,355</u>
Total Costs	<u>233,449</u>	<u>356,141</u>
Total Intragovernmental Earned Revenues	<u>(140,507)</u>	<u>(55,270)</u>
Total Public Earned Revenues	<u>(41,317)</u>	<u>(233,057)</u>
Total Earned Revenues	<u>(181,824)</u>	<u>(288,327)</u>
Net Cost of Operations	<u>\$ 51,625</u>	<u>\$ 67,814</u>

Lower Colorado Region	Upper Colorado Region	Great Plains Region	Commissioner's Office	Combined Total	Intrabureau Eliminations	Consolidated Total
\$ 45,558	\$ 48,882	\$ 44,124	\$ 49,697	\$ 322,070	\$ -	\$ 322,070
242,810	66,968	143,160	71,725	743,095	-	743,095
288,368	115,850	187,284	121,422	1,065,165	-	1,065,165
(47,561)	(23,706)	(29,425)	(85)	(101,585)	-	(101,585)
(163,744)	(25,961)	(55,592)	(242)	(415,677)	-	(415,677)
(211,305)	(49,667)	(85,017)	(327)	(517,262)	-	(517,262)
77,063	66,183	102,267	121,095	547,903	-	547,903
28,838	18,647	17,441	1,878	104,111	-	104,111
22,599	27,232	33,689	268	153,262	-	153,262
51,437	45,879	51,130	2,146	257,373	-	257,373
(20,528)	(11,684)	(28,349)	(4)	(160,829)	-	(160,829)
(59,203)	(30,863)	(12,305)	(11)	(190,102)	-	(190,102)
(79,731)	(42,547)	(40,654)	(15)	(350,931)	-	(350,931)
(28,294)	3,332	10,476	2,131	(93,558)	-	(93,558)
10,005	4,453	191	1,211	16,030	(6,581)	9,449
10,213	14,136	381	331	25,458	-	25,458
20,218	18,589	572	1,542	41,488	(6,581)	34,907
(1,171)	(6,283)	-	-	(7,456)	6,581	(875)
(889)	(111)	-	(1)	(1,035)	-	(1,035)
(2,060)	(6,394)	-	(1)	(8,491)	6,581	(1,910)
18,158	12,195	572	1,541	32,997	-	32,997
2,639	242	285	2	8,548	-	8,548
8,770	984	331	19	19,172	-	19,172
11,409	1,226	616	21	27,720	-	27,720
(898)	(47)	(65)	-	(1,117)	-	(1,117)
(11,301)	(67)	(70)	-	(12,537)	-	(12,537)
(12,199)	(114)	(135)	-	(13,654)	-	(13,654)
(790)	1,112	481	21	14,066	-	14,066
15,189	15,092	14,163	123,412	198,894	(332,894)	(134,000)
39,088	33,935	25,376	115,162	298,076	-	298,076
54,277	49,027	39,539	238,574	496,970	(332,894)	164,076
(43,808)	(39,701)	(36,608)	(158,451)	(373,164)	332,894	(40,270)
(6,008)	(7,583)	(1,728)	(8,267)	(38,969)	-	(38,969)
(49,816)	(47,284)	(38,336)	(166,718)	(412,133)	332,894	(79,239)
4,461	1,743	1,203	71,856	84,837	-	84,837
102,229	87,316	76,204	176,200	649,653	(339,475)	310,178
323,480	143,255	202,937	187,505	1,239,063	-	1,239,063
425,709	230,571	279,141	363,705	1,888,716	(339,475)	1,549,241
(113,966)	(81,421)	(94,447)	(158,540)	(644,151)	339,475	(304,676)
(241,145)	(64,585)	(69,695)	(8,521)	(658,320)	-	(658,320)
(355,111)	(146,006)	(164,142)	(167,061)	(1,302,471)	339,475	(962,996)
\$ 70,598	\$ 84,565	\$ 114,999	\$ 196,644	\$ 586,245	\$ -	\$ 586,245

A photograph of a forest during autumn. The trees have yellow and orange leaves, and the ground is covered in fallen leaves. A semi-transparent blue rectangular box is overlaid on the upper part of the image, containing the text "Supplemental Section" in white. The text is centered within the box and is in a bold, sans-serif font. The background shows a dense stand of trees with varying trunk thicknesses and heights, all with vibrant autumn foliage. The lighting is soft, suggesting an overcast day or a shaded forest interior.

Supplemental Section

Bureau of Reclamation
February 5, 2007





**Bureau of Reclamation
Regional Boundaries and Offices**

Required Supplementary Information

Combining Statements of Budgetary Resources

The Combining Statements of Budgetary Resources, which are included as a principal financial statement, present information about the Bureau of Reclamation's (Reclamation's) total budgetary resources, including carry forward of unused, prior year funding, and spending authority created by reimbursements from other Federal agencies and non-Federal entities. The Combining Statements of Budgetary Resources present this information by major budget account.

Reclamation's largest budget account is Water and Related Resources, which supports the development and management of water and related resources in the 17 Western States. This account funds the operation and maintenance (O&M) of Reclamation facilities to deliver water and power, preservation of natural resources, and continued efforts towards water conservation and technology development.

The Working Capital Fund (WCF), the Lower Colorado River Basin Development Fund (LCRBDF), and the Upper Colorado River Basin Fund (UCRBF) are revolving funds that operate on a cost recovery basis. The WCF provides support services and equipment for Reclamation programs and activities, as well as for other Federal entities.

The Colorado River Dam Fund is an available receipt fund into which various operating revenues of the Hoover Dam are collected, primarily from the sale of power generated at the dam. These revenues are used to fund the O&M of the dam.

The Central Valley Project Restoration Fund provides funding for fish and wildlife habitat restoration, improvement, and acquisition activities. Revenues come from project beneficiaries and donations.

Reclamation Trust Funds collect amounts that are earmarked for specific purposes and are expended accordingly, primarily to finance activities such as fish and wildlife habitat restoration and other mitigation efforts.

The Policy and Administration budget account is used to finance all of Reclamation's centralized management functions that are not chargeable directly to a specific project or program. These functions include management of personnel, safety and health, and information resources. Also included are budgetary policy formulation and execution, procurement and general services, and public affairs activities.

The California Bay-Delta Restoration account provides funds that are distributed based on a program recommended by the State of California and Federal Agencies (CALFED) group and

approved by the Secretary of the Interior. The CALFED Bay-Delta Program was established in May 1995 to develop a comprehensive, long-term solution to the complex and interrelated problems in California's San Francisco Bay/Sacramento-San Joaquin Delta (Bay-Delta). The Bay-Delta system provides habitat for 120 fish and wildlife species, some listed as threatened or endangered. CALFED is comprised of a consortium of Federal and State agencies. Federal agencies include Reclamation, the United States (U.S.) Fish and Wildlife Service, the U.S. Environmental Protection Agency, and the National Marine Fisheries Service, with possible participation by other agencies in the future. State agency involvement includes oversight by the California Resources Agency and the participation of the State Department of Water Resources, the Department of Fish and Game, and the California Environmental Protection Agency.

The Other Budget Accounts balance includes several smaller activities within Reclamation, including the San Gabriel Restoration Fund (\$9.9 million), loan program, and financing funds. The upward subsidy re-estimate recorded in fiscal year (FY) 2006 was \$2.1 million.

**U.S. Department of the Interior
Bureau of Reclamation
Combining Statement of Budgetary Resources
For the Year Ended September 30, 2006**

(In Thousands)	Water and Related Resources	Working Capital Fund	Lower Colorado River Basin Development Fund
BUDGETARY RESOURCES			
Unobligated Balance, Beginning of Fiscal Year	\$ 276,153	\$ 27,882	\$ 266,952
Recoveries of Prior Year Unpaid Obligations	27,091	2,609	509
Budget Authority:			
Appropriations	892,556	-	-
Spending Authority from Offsetting Collections:			
Earned:			
Collected	236,740	349,975	190,137
Change in Receivables from Federal Sources	(4,315)	109	(944)
Change in Unfilled Customer Orders:			
Advance Received	12,642	(473)	(493)
Without Advance from Federal Sources	(6,761)	-	-
Subtotal	1,130,862	349,611	188,700
Nonexpenditure Transfers, Net	(103,962)	-	24,808
Temporarily Not Available Pursuant to Public Law	(7,017)	-	-
Permanently Not Available	(1,818)	-	(4,902)
Total Budgetary Resources	\$ 1,321,309	\$ 380,102	\$ 476,067
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred (Note 14):			
Direct	\$ 899,338	\$ -	\$ -
Reimbursable	236,569	352,072	147,164
Total Obligations Incurred	1,135,907	352,072	147,164
Unobligated Balance Available:			
Apportioned	185,354	28,030	328,903
Exempt from Apportionment	48	-	-
Total Unobligated Balance Available	185,402	28,030	328,903
Total Status of Budgetary Resources	\$ 1,321,309	\$ 380,102	\$ 476,067
OBLIGATED BALANCE			
Obligated Balance, Net, Beginning of Fiscal Year:			
Unpaid Obligations	\$ 441,972	\$ 32,038	\$ 28,255
Less: Uncollected Receivables and Orders from Federal Sources	(53,870)	(9,946)	(9,493)
Total Unpaid Obligated Balances, Net, Beginning of Fiscal Year	388,102	22,092	18,762
Obligations Incurred	1,135,907	352,072	147,164
Less: Gross Outlays	(962,567)	(349,269)	(151,616)
Less: Recoveries of Prior Year Unpaid Obligations	(27,091)	(2,609)	(509)
Change in Uncollected Receivables and Orders from Federal Sources	11,076	(109)	944
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 545,427	\$ 22,177	\$ 14,745
OBLIGATED BALANCE, NET, END OF FISCAL YEAR - BY COMPONENT			
Obligated Balance, Net, End of Fiscal Year:			
Unpaid Obligations	588,221	32,232	23,294
Less: Uncollected Receivables and Orders from Federal Sources	(42,794)	(10,055)	(8,549)
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 545,427	\$ 22,177	\$ 14,745
NET OUTLAYS			
Gross Outlays	\$ 962,567	\$ 349,269	\$ 151,616
Less: Offsetting Collections	(249,382)	(349,502)	(189,644)
Less: Distributed Offsetting Receipts	(368)	-	-
Net Outlays (Receipts)	\$ 712,817	\$ (233)	\$ (38,028)

Upper Colorado River Basin Development Fund	Colorado River Dam Fund	Central Valley Project Restoration Fund	Reclamation Trust Fund	Policy and Administration	California Bay-Delta Ecosystem Restoration Fund	Other Budgetary Accounts	Total Budgetary Accounts
\$ 18,267	\$ 15,394	\$ 110	\$ 42,445	\$ 2,052	\$ 15,789	\$ 964	\$ 666,008
2,962	306	3,450	81	878	1,259	26	39,171
-	71,448	52,219	41,124	57,917	37,000	2,687	1,154,951
84,374	-	-	-	-	-	4,157	865,383
458	-	-	-	-	-	-	(4,692)
(8,930)	-	-	-	-	-	-	2,746
-	-	-	-	-	-	-	(6,761)
75,902	71,448	52,219	41,124	57,917	37,000	6,844	2,011,627
62,274	-	-	-	-	(500)	9,900	(7,480)
-	-	(83)	-	(579)	-	-	(7,679)
(4,098)	(1,575)	-	-	-	(370)	(4,003)	(16,766)
\$ 155,307	\$ 85,573	\$ 55,696	\$ 83,650	\$ 60,268	\$ 53,178	\$ 13,731	\$ 2,684,881
\$ -	\$ 66,455	\$ 55,616	\$ 32,848	\$ 58,127	\$ 39,049	\$ 12,608	\$ 1,164,041
132,256	-	-	-	-	-	-	868,061
132,256	66,455	55,616	32,848	58,127	39,049	12,608	2,032,102
23,051	16,626	80	-	2,141	14,129	951	599,265
-	2,492	-	50,802	-	-	172	53,514
23,051	19,118	80	50,802	2,141	14,129	1,123	652,779
\$ 155,307	\$ 85,573	\$ 55,696	\$ 83,650	\$ 60,268	\$ 53,178	\$ 13,731	\$ 2,684,881
\$ 137,229	\$ 5,879	\$ 63,639	\$ 5,929	\$ 9,640	\$ 25,551	\$ 30,641	\$ 780,773
(163)	-	-	-	-	-	-	(73,472)
137,066	5,879	63,639	5,929	9,640	25,551	30,641	707,301
132,256	66,455	55,616	32,848	58,127	39,049	12,608	2,032,102
(135,578)	(65,356)	(46,005)	(7,897)	(58,255)	(14,674)	(18,135)	(1,809,352)
(2,962)	(306)	(3,450)	(81)	(878)	(1,259)	(26)	(39,171)
(458)	-	-	-	-	-	-	11,453
\$ 130,324	\$ 6,672	\$ 69,800	\$ 30,799	\$ 8,634	\$ 48,667	\$ 25,088	\$ 902,333
130,945	6,672	69,800	30,799	8,634	48,667	25,088	964,352
(621)	-	-	-	-	-	-	(62,019)
\$ 130,324	\$ 6,672	\$ 69,800	\$ 30,799	\$ 8,634	\$ 48,667	\$ 25,088	\$ 902,333
\$ 135,578	\$ 65,356	\$ 46,005	\$ 7,897	\$ 58,255	\$ 14,674	\$ 18,135	\$ 1,809,352
(75,444)	-	-	-	-	-	(4,157)	(868,129)
-	(71,448)	(54,872)	(41,124)	-	-	(2,090,053)	(2,257,865)
\$ 60,134	\$ (6,092)	\$ (8,867)	\$ (33,227)	\$ 58,255	\$ 14,674	\$ (2,076,075)	\$ (1,316,642)

2006 Bureau of Reclamation

**U.S. Department of the Interior
Bureau of Reclamation
Combining Statement of Budgetary Resources
For the Year Ended September 30, 2005**

(In Thousands)	Water and Related Resources	Working Capital Fund	Lower Colorado River Basin Development Fund
BUDGETARY RESOURCES			
Unobligated Balance, Beginning of Fiscal Year	\$ 268,836	\$ 28,231	\$ 210,729
Recoveries of Prior Year Unpaid Obligations	22,558	1,616	1,001
Budget Authority:			
Appropriations	864,637	-	-
Spending Authority from Offsetting Collections:			
Earned:			
Collected	195,253	345,124	154,440
Change in Receivables from Federal Sources	(1,945)	(64)	2,105
Change in Unfilled Customer Orders:			
Advance Received	7,578	(140)	855
Without Advance from Federal Sources	6,279	-	-
Subtotal	1,071,802	344,920	157,400
Nonexpenditure Transfers, Net	(83,480)	-	27,052
Temporarily Not Available Pursuant to Public Law	(5,534)	-	-
Permanently Not Available	(1,342)	-	(1,033)
Total Budgetary Resources	\$ 1,272,840	\$ 374,767	\$ 395,149
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred (Note 14):			
Direct	\$ 797,128	\$ -	\$ -
Reimbursable	199,559	346,885	128,197
Total Obligations incurred	996,687	346,885	128,197
Unobligated Balance Available:			
Apportioned	276,110	27,882	266,952
Exempt from Apportionment	43	-	-
Total Unobligated Balance Available	276,153	27,882	266,952
Total Status of Budgetary Resources	\$ 1,272,840	\$ 374,767	\$ 395,149
OBLIGATED BALANCE			
Obligated Balance, Net, Beginning of Fiscal Year:			
Unpaid Obligations	\$ 415,791	\$ 31,237	\$ 29,440
Less: Uncollected Receivables and Orders from Federal Sources	(49,536)	(10,011)	(7,388)
Total Unpaid Obligated Balances, Net	366,255	21,226	22,052
Obligations Incurred, Net	996,687	346,885	128,197
Less: Gross Outlays	(947,949)	(344,466)	(128,382)
Less: Recoveries of Prior Year Unpaid Obligations	(22,558)	(1,616)	(1,001)
Change in Uncollected Receivables and Orders from Federal Sources	(4,334)	64	(2,105)
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 388,101	\$ 22,093	\$ 18,761
OBLIGATED BALANCE, NET, END OF FISCAL YEAR - BY COMPONENT			
Obligated Balance, Net, End of Fiscal Year:			
Unpaid Obligations	441,971	32,039	28,254
Less: Uncollected Receivables and Orders from Federal Sources	(53,870)	(9,946)	(9,493)
Total Unpaid Obligated Balance, Net, End of Fiscal Year	\$ 388,101	\$ 22,093	\$ 18,761
NET OUTLAYS			
Gross Outlays	\$ 947,949	\$ 344,466	\$ 128,382
Less: Offsetting Collections	(202,831)	(344,984)	(155,295)
Less: Distributed Offsetting Receipts	(354)	-	-
Net Outlays (Receipts)	\$ 744,764	\$ (518)	\$ (26,913)

Upper Colorado River Basin Development Fund	Colorado River Dam Fund	Central Valley Project Restoration Fund	Reclamation Trust Fund	Policy and Administration	California Bay-Delta Ecosystem Restoration Fund	Other Budgetary Accounts	Total Budgetary Accounts
\$ 22,102	\$ 11,479	\$ 456	\$ 39,444	\$ 1,135	\$ 18,784	\$ 1,045	\$ 602,241
1,244	280	3,726	197	296	3,063	-	33,981
-	69,380	54,695	12,913	58,153	-	20,977	1,080,755
86,161	-	-	-	-	-	-	780,978
(92)	-	-	-	-	-	-	4
159,608	-	-	-	-	-	-	167,901
-	-	-	-	-	-	-	6,279
245,677	69,380	54,695	12,913	58,153	-	20,977	2,035,917
54,437	-	-	-	-	-	3,991	2,000
-	-	(67)	-	(465)	-	-	(6,066)
(173,925)	(1,498)	-	-	-	-	-	(177,798)
\$ 149,535	\$ 79,641	\$ 58,810	\$ 52,554	\$ 59,119	\$ 21,847	\$ 26,013	\$ 2,490,275
\$ -	\$ 64,247	\$ 58,700	\$ 10,109	\$ 57,067	\$ 6,058	\$ 25,049	\$ 1,018,358
131,268	-	-	-	-	-	-	805,909
131,268	64,247	58,700	10,109	57,067	6,058	25,049	1,824,267
18,267	12,938	110	-	2,052	15,789	964	621,064
-	2,456	-	42,445	-	-	-	44,944
18,267	15,394	110	42,445	2,052	15,789	964	666,008
\$ 149,535	\$ 79,641	\$ 58,810	\$ 52,554	\$ 59,119	\$ 21,847	\$ 26,013	\$ 2,490,275
\$ 137,059	\$ 4,029	\$ 49,093	\$ 3,982	\$ 8,960	\$ 31,759	\$ 30,782	\$ 742,132
(254)	-	-	-	-	-	-	(67,189)
136,805	4,029	49,093	3,982	8,960	31,759	30,782	674,943
131,268	64,247	58,700	10,109	57,067	6,058	25,049	1,824,267
(129,855)	(62,118)	(40,428)	(7,964)	(56,091)	(9,202)	(25,190)	(1,751,645)
(1,244)	(280)	(3,726)	(197)	(296)	(3,063)	-	(33,981)
92	-	-	-	-	-	-	(6,283)
\$ 137,066	\$ 5,878	\$ 63,639	\$ 5,930	\$ 9,640	\$ 25,552	\$ 30,641	\$ 707,301
137,229	5,878	63,639	5,930	9,640	25,552	30,641	780,773
(163)	-	-	-	-	-	-	(73,472)
\$ 137,066	\$ 5,878	\$ 63,639	\$ 5,930	\$ 9,640	\$ 25,552	\$ 30,641	\$ 707,301
\$ 129,855	\$ 62,118	\$ 40,428	\$ 7,964	\$ 56,091	\$ 9,202	\$ 25,190	\$ 1,751,645
(245,769)	-	-	-	-	-	-	(948,879)
-	(69,380)	(57,575)	(12,913)	-	-	(1,647,215)	(1,787,437)
\$ (115,914)	\$ (7,262)	\$ (17,147)	\$ (4,949)	\$ 56,091	\$ 9,202	\$ (1,622,025)	\$ (984,671)

Working Capital Fund

Reclamation operates a Working Capital Fund to efficiently finance support services and equipment for Reclamation programs and other Federal and non-Federal agencies. Balance sheet information on the financial position of the WCF as of September 30, 2006, and September 30, 2005, is presented below.

Working Capital Fund Balance Sheet As of September 30, 2006, and 2005

(In Thousands)	2006	2005
ASSETS		
Intragovernmental Assets:		
Fund Balance with Treasury	\$ 50,207	\$ 49,974
Accounts Receivable	10,050	9,919
Loans and Interest Receivable	2,749	1,900
Other:		
Advances and Prepayments	8	126
Total Intragovernmental Assets	63,014	61,919
Accounts and Interest Receivable, Net	23	91
General Property, Plant and Equipment, Net	40,492	34,823
Other:		
Advances and Prepayments	226	217
Total Assets	\$ 103,755	\$ 97,050
LIABILITIES		
Intragovernmental Liabilities:		
Accounts Payable	\$ 6,306	\$ 4,712
Debt	2,749	1,900
Other:		
Accrued Employee Benefits	4,432	7,185
Advances, Deferred Revenue, and Deposit Funds	1,663	1,709
Total Other Liabilities	6,095	8,894
Total Intragovernmental Liabilities	15,150	15,506
Accounts Payable	5,182	5,172
Other:		
Accrued Payroll and Benefits	16,170	17,707
Advances, Deferred Revenue, and Deposit Funds	240	667
Other	145	140
Total Other Liabilities	16,555	18,514
Total Liabilities	36,887	39,192
NET POSITION		
Cumulative Results of Operations	66,867	57,858
Total Net Position	66,867	57,858
Total Liabilities and Net Position	\$ 103,755	\$ 97,050

Although the WCF is operated as a single entity, it is divided into 23 activities and numerous subactivities to facilitate management of the fund. Among the largest of the activities is the Technical Service Center (TSC), which provides engineering and technical services to WCF customers.

The WCF is an intragovernmental revolving fund and recovers the full cost of doing business. The types of services provided by the WCF fall into three broad categories: (1) Engineering and Technical Services, (2) Administrative Services, and (3) Information Technology (IT) Services. The WCF Statements of Net Cost as of September 30, 2006, and September 30, 2005, are presented below. The presentation by major category of services is intended to provide information on the relative composition of the WCF.

**Supplemental Statement of Net Cost
Working Capital Fund
For the Year Ended September 30, 2006**

(In Thousands)	Engineering and Technical Services	Admini- strative Services	Information Technology Services	Total
Costs	\$ 104,377	\$ 221,325	\$ 16,986	\$ 342,688
Earned Revenues	(106,548)	(225,128)	(17,350)	(349,026)
Net Cost	\$ (2,171)	\$ (3,803)	\$ (364)	\$ (6,338)

**Supplemental Statement of Net Cost
Working Capital Fund
For the Year Ended September 30, 2005**

(In Thousands)	Engineering and Technical Services	Admini- strative Services	Information Technology Services	Total
Costs	\$ 103,323	\$ 223,499	\$ 18,534	\$ 345,356
Earned Revenues	(104,173)	(223,139)	(16,548)	(343,860)
Net Cost	(850)	\$ 360	\$ 1,986	\$ 1,496

The most significant activities in the Engineering and Technical Services category are technical services related to water resources management support provided by the TSC. Also included in this category are vehicles and aircraft used for engineering support.

Administrative services include accounting and finance support, overhead allocation distribution, and leave cost distribution. The Information Technology Services category includes software development and operations and maintenance on Reclamation information technology resources.

Deferred Maintenance

Reclamation owns a water resources management infrastructure with a combined total value of over \$21 billion (not adjusted for depreciation), as of September 30, 2006. This infrastructure consists of diversion and storage dams; hydroelectric powerplants; water conveyance facilities (canals, pipelines, siphons, tunnels, and pumps); recreational facilities; and associated buildings, bridges, and roads, as well as an inventory of related construction, maintenance, laboratory, and scientific equipment. The O&M of some of these assets is performed by Reclamation using annual or permanent appropriations or other funding sources available to it. The O&M of the remaining assets, consisting of approximately one-half of the combined total value of all assets, is performed by Reclamation's water and power customers or by others (collectively, "contractors") at their expense pursuant to contracts with Reclamation.

Reclamation employs a commercial, off-the-shelf maintenance management system on many of its larger, more complex facilities and performs condition assessment (site reviews) and other field inspections to estimate the condition of, and determine the need for any maintenance related to, its assets. Under these various review programs, essentially most of Reclamation's major assets, whether operated and maintained by Reclamation or its contractors, are assessed triennially. The monitoring and tracking of maintenance-related deficiencies and/or recommendations of water and power related infrastructure are generally conducted on an annual basis and are reported in the dam safety or power resources information system.

There are many factors that influence whether maintenance is performed as scheduled or deferred. These factors include, among others, limitations on access to facilities (e.g., due to water levels); intervening technological innovations or developments; seasonal or climatological considerations; reassessment of priorities; delays in the contract-award process; availability of, or delays related to, the contractor; and changes in funding priorities resulting, in some cases, from emergencies or unforeseen critical maintenance requirements. It is Reclamation's policy to give critical maintenance—that which addresses a threat to life, property, and safety—the highest priority in attention and resources.

The table below identifies Reclamation's estimate of deferred maintenance as of September 30, 2006, on those facilities (reserved works) operated and maintained by it. The reserved works' facilities, currently in operation and maintenance status, include general

**FY 2006 Deferred Maintenance Estimates
(In Thousands)**

	Item(s) Covered	Condition Category	Estimated Range of Deferred Maintenance for 2006							
			Note (1)	Note (2)	General PP&E		Stewardship PP&E		Total	
					Low	High	Low	High	Low	High
Roads Bridges and Trails	D	G, F, P	\$ 26	\$ 2,234	-	\$ 88	\$ 26	\$ 2,322		
Irrigation, Dams, and Other Water Structures	D	G, F, P	\$ 249	\$ 30,485	\$ 2,159	\$ 8,920	\$ 2,408	\$ 39,405		
Other Structures (e.g., Recreation Sites, Hatcheries, etc.)	D	G, F, P	\$ 79	\$ 2,376	\$ 2	\$ 77	\$ 81	\$ 2,453		
Total			\$ 354	\$ 35,095	\$ 2,161	\$ 9,085	\$ 2,515	\$ 44,180		

Note (1) Category:

A - Critical Health and Safety Deferred Maintenance: A facility deferred maintenance need that poses a serious threat to public or employee safety.

B - Critical Resource Protection Deferred Maintenance: A facility deferred maintenance need that poses a serious threat to natural or cultural resources.

C - Critical Mission Deferred Maintenance: A facility deferred maintenance need that poses a serious threat to a bureau's ability to carry out its assigned mission.

D - Compliance and other Deferred Maintenance: A facility deferred maintenance need that will improve public or employee safety, health, or accessibility: compliance with codes, standards, laws, complete unmet programmatic needs and mandated programs; protection of natural or cultural resources to a bureau's ability to carry out its assigned mission.

Note (2) Condition Assessment:

Good (G) - Facility/equipment condition meets established maintenance standards, operates efficiently, and has a normal life expectancy. Scheduled maintenance should be sufficient to maintain the current condition.

Fair (F) - Facility/equipment condition meets minimum standards but requires additional maintenance or repair to prevent further deterioration, increase operating efficiency, and to achieve normal life expectancy.

Poor (P) - Facility/equipment does not meet most maintenance standards and requires frequent repairs to prevent accelerated deterioration and provide a minimal level of operating function. In some cases that includes condemned or failed facilities. Based on periodic condition assessments, and indicator of condition is the percent of facilities and items of equipment in each of the good, fair, or poor categories.

(non-heritage) and stewardship (heritage assets) that are components of Reclamation projects.¹ Furthermore, the precision attributable to these estimates for the assets involved is based on current, available data.

Reclamation continues to refine its estimates by improving the documentation procedures and systems for tracking condition assessments and for reporting the scheduling and deferral of maintenance work. Reclamation uses budget estimates, the Dam Safety/Power Resources Information System, Accessibility and Data Management System, and Maintenance Management System (MAXIMO) as sources for potential deferred maintenance. It is expected that variations in reporting deferred maintenance can take place from year to year because of the type and kind of maintenance work that takes place on Reclamation facilities.

¹ The deferred maintenance of heritage assets that are part of active project features is reported under this section, not under the Heritage Assets section of "Stewardship Assets." Heritage assets that may have been a part of an active project, but no longer serve that purpose, are reported under the Heritage Assets section of "Stewardship Assets."

Federal Stewardship Assets

Stewardship Lands

For the fiscal yearend 2006 reporting period, according to the U.S. Department of the Interior’s (Interior’s) June 9, 2006, Required Supplementary Information call letter and the *Statement of Federal Financial Accounting Standards* (SFFAS) No. 29, Reclamation is now reporting those Stewardship Lands included within the boundaries of Federal Reclamation water and related projects in terms of the number of “projects” as opposed to the number of “acres” (see the following table). This is a change from prior years when the “units” reported were in acres. With this change, the reader will find that rarely there will be “additions” or “withdrawals” as these actions would represent: (a) new water projects being authorized and funded by the Congress, (b) revocations by the Bureau of Land Management or USDA Forest Service of all Stewardship Lands in a particular project, or (c) projects that have successfully completed the process of title transfers to a non-Federal entity. All three of these actions occur infrequently.

Stewardship Lands – Yearend FY 2006

Primary Land Management Category	2006 Beginning Balance (units)	Additions (units)	Withdrawals (units)	2006 Ending Balance	Condition	
					Acceptable	Needs Intervention
Reclamation - Federal Water and Related Projects ¹	146	0	² 1	145	³ 145	0
Total	146	0	1	145	145	0

¹ Units represent those projects which contain Stewardship Land. In Reclamation, Stewardship Land is land that was withdrawn from the public domain at no cost to the projects. This criterion is in accordance with SFFAS No. 29.

² All of the Stewardship Lands from the Upper Snake River, Lynn Crandall project, were disposed in August 2006 in Reclamation’s land inventory system due to a completed withdrawal revocation by the Bureau of Land Management.

³ Reclamation’s Stewardship Land is categorized as being in “acceptable condition” as this land meets the requirements of effectively supporting the Federal Reclamation water and related projects for which the land was withdrawn. There are, however, three hazardous waste sites on three separate water projects that are located on project withdrawn lands (Stewardship Lands) and are identified at Environmental Disposal Liabilities (EDL) sites. These sites are also listed on the U.S. Department of the Interior’s EDL system. These EDL sites are receiving intervention either to prepare or sustain the lands for their intended purpose.

Non-Collectible Cultural Heritage Assets

In accordance with Interior’s new reporting instructions for non-collectible heritage assets, only properties that have been Presidentially, congressionally, or departmentally designated are being reported. Reclamation is reporting on two categories: National Historic Landmarks (NHLs) and National Natural Landmarks (NNLs) (see the following table). Reclamation has previously reported on NHLs; this is the first year that Interior is requesting information on NNLs. In accordance with data provided to Reclamation on May 16, 2006, by the National Park Service (NPS), which administers the NNL program, there are three NNLs on Reclamation-owned land: Drumheller Channels, Washington; Grand Coulee, Washington; and Russell Lakes, Colorado. Since the NPS points of contacts for the three properties have been managing entities or other landowners, and not Reclamation, the existence of the NNLs was previously unknown to Reclamation. Reclamation is in the process of obtaining documentation from NPS on its three NNLs and verifying to what extent lands within the NNL boundaries are under its ownership. The beginning count of NNLs as of October 1, 2005, is shown as zero because this is the first year that they are being

reported. Condition information reported on Drumheller Channels and Russell Lakes was obtained from NPS, which is responsible for maintaining NNL Status Reports.

The types of non-collectible heritage assets reported under the category of NHLs include buildings, structures, and archaeological sites. Reclamation is reporting the addition of one NHL since the end of last fiscal year. The Secretary of the Interior officially designated Tule Lake Segregation Center an NHL on February 17, 2006. Reclamation and the State of California both own property within its boundaries.

No non-collectible heritage assets have been acquired through donation or devise during the reporting period.

Non-Collectible Heritage Assets – Yearend FY 2006

Category by Type	2006 Beginning	Additions	Withdrawals	2006 Ending	Condition ¹			
	Balance (Units)			Balance (Units)	Good	Fair	Poor	Unknown
National Historic Landmarks	5	1	-	² 6	2	3	-	1
National Natural Landmarks	-	3	-	³ 3	⁴ 2	-	-	1
Total	5	4	-	9	-	-	-	-

¹ "Good" condition means a site shows no clear evidence of negative disturbance or deterioration by natural forces or human activities. "Fair" means that a site shows clear evidence of negative disturbances or deterioration by natural forces and/or human activities. "Poor" means that a site shows clear evidence of negative disturbance or deterioration by natural forces and/or human activities, and no corrective actions have been taken to protect and preserve the integrity of the site. "Unknown" may mean that, due to the nature of the site, such as underwater, under snow, or under other structures, the condition cannot be determined or that, due to financial constraints, a bureau has been unable to determine condition.

² This number includes three districts and three individual properties. The new addition is Tule Lake Segregation Center, of which Reclamation is partial owner.

³ This is the first year "National Natural Landmarks" is a reporting category; therefore, the starting balance is zero.

⁴ Status reports obtained from NPS for Russell Lakes and Drumheller Channels NNLs identify the site condition of both as "satisfactory" and "no action needed."

Collectible Heritage Assets

Collectible heritage assets, also called museum property, are derived from their designation in 10 categories or disciplines. These are archaeology, art, ethnography, history, documents, botany, zoology, paleontology, geology, and environmental samples. Reclamation collects information on the size, location, and condition of its museum property collections.

Beginning in the third quarter FY 2006 reporting cycle, Reclamation reported collectible heritage assets that have been accessioned as museum property as defined and required by *Departmental Manual 411, 3.4.A*. The following table displays the count and condition of the number of Reclamation collections held in Interior and non-Interior facilities. Each facility contains one Reclamation collection; therefore, the number of collections reported is the same as the number of Interior and non-Interior facilities housing Reclamation collections. The table also documents the additions and withdrawals of Reclamation collections. All fiscal yearend 2006 additions were from authorized archaeological projects or from collections that were moved between facilities.

Collectible Heritage Assets – Yearend FY 2006

Interior Museum Collections	Beginning Collections	Additions	Withdrawals	Ending Collections	Condition of Facility Housing Collection ¹			
					Good	Fair	Poor	Unknown
Held at Interior Reclamation Facilities	19	2	11	10	8	–	–	2
Held at Non-Interior Reclamation Facilities	80	–	68	12	11	1	–	–
Total	99	2	79	22	19	1	–	2

¹Condition of museum collections is measured as defined by the standards in *Departmental Manual 411* and accepted industry practices. The condition is rated based on a facility's ability to answer affirmatively on a number of questions about its facility and management practices; less than 70 percent (%) = good; between 50% and 70% = fair; and greater than 50% = poor condition.

The large number of withdrawals from the yearend *FY 2005 Performance and Accountability Report* is primarily the result of the strict application of museum property as defined by *Departmental Manual 411* and of updating collection records. Museum property is defined as items or collections formally accessioned into a property management system. Because most of Reclamation's previously reported collections have not been accessioned, they cannot be classified as museum property. Reclamation expects to report significant additions in the number of collections as they are accessioned over the next 2 years. Actual management of these collections will not change.

Other withdrawals occurred because one non-Interior facility no longer holds Reclamation museum property, and two facilities previously reported as non-Reclamation have been removed from that category and are now reported as Interior facilities.

Eighty-six percent of Reclamation's assessed collections are in good condition.

Required Supplemental Stewardship Information

Stewardship Investments

Stewardship investments are substantial investments made by the Federal Government for the benefit of the Nation. The Federal Accounting Standard Advisory Board (FASAB) requires reporting for three categories of stewardship investments—Research and Development, Investment in Human Capital, and Investment in Non-Federal Physical Property. Reclamation identified stewardship investments in all three categories.

Research and Development

Reclamation invests in applied research programs to aid in the water and energy management challenges facing the arid West. These programs focus on the improvement of water management, the development of solutions pertaining to flood hydrology, water quality, irrigation return flows, and the delivery of hydropower to the West. The information obtained through these programs provides water management solutions and techniques that yield future benefits to the Nation. Research and Development activities support Reclamation's end outcome goal to deliver water consistent with applicable State and Federal law, in an environmental responsible and cost-efficient manner.

Investment in Research and Development (In Millions)

FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	Total
\$19.0	\$18.3	\$19.8	\$25.9	\$32.0	\$115.0

Investment in Human Capital

Reclamation operates six Job Corps Centers, based on an interagency agreement with the Department of Labor for the purpose of educating and training disadvantaged youth. On July 1, 2006, Reclamation acquired another Job Corps Center (Center) (Treasure Lake) from the U.S. Fish and Wildlife Service. As of September 30, 2006, Reclamation expended \$31.6 million in residential education and job training for these youth, including courses in computer technology, painting, woodworking, welding, culinary arts, and social and leadership development.

**Investment in Human Capital
(In Millions)**

Category	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	Total
Job Corps Program	\$28.6	\$29.9	\$30.0	\$29.8	\$31.6	\$149.9

Post-program job placement services are available to Job Corps students. The following table shows the number of Reclamation Center graduates as a percentage of the total Center enrollment and the number of graduates placed into jobs within 1 year of graduation as a percentage of the graduates in the placement pool.

Center	Graduates	Center Enrollment	%	Graduates Placed	Graduate Placement Pool	%
Centennial	255	261	97.70	311	343	90.67
Columbia Basin	190	232	81.90	236	268	88.06
Ft. Simcoe	165	229	72.05	211	238	88.66
Weber Basin	176	212	83.02	153	177	86.44
Collbran	152	203	74.88	176	191	92.15
Treasure Lake	128	156	82.05	110	131	83.97

Investment in Non-Federal Physical Property

Investment in Non-Federal Physical Property are expenses incurred by Reclamation for the purchase, construction, or major renovation of physical property owned by or given to State and local government or insular areas. Costs include major additions, alterations, replacements, the purchase of major equipment, and the purchase or improvement of other physical assets owned by non-Federal entities. Grants for O&M are not considered investment in non-Federal physical property.

The investments listed below provide assistance through a variety of measures, all related to dams and other water structures. For example, Reclamation incurs expenses for specific programs to provide for the construction or improvement of structures and facilities used in State and local irrigation projects and water quality improvement projects. Reclamation-wide programs that improve State and local fish and wildlife habitats through activities such as the construction or betterment of structures or facilities are also included.

**Investment in Non-Federal Physical Property
(In Millions)**

Category	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	Total
Water and Related Resources Management	\$118.9	\$124.4	\$106.6	\$138.1	\$196.5	\$684.5

Title Transfers to State and Local Governments

Assets constructed with Federal funding meet the criteria for non-Federal physical property at the time of transfer under Reclamation's title transfer program. The following tables present the status of transfer facilities for the period ending September 30, 2006, and completed transfers for the preceding 5 years.

Transfer of Facilities (In Thousands)

Project Name	Value Including Land Cost	
Pending Transfers		
Montecito Water Distribution Systems, California		\$135
Carson Lake and Pasture		65
Gila Project, Welton-Mohawk Division, Arizona		2,568
Fallon Rail Freight Loading Facility Property, Newlands Project, Nevada		5
Provo River Project, Utah		3,079
Rye Patch Dam and Reservoir, Humboldt Project, Nevada		6,911
Completed Transfer of Facilities to State and Local Government		
	Year Ending of Transfer	Value Including Land Costs
Carpinteria Water Distribution System, Cachuma Project, California	2006	\$ 35
<i>No Completed Transfers for 2005 as of September 30, 2005</i>		
Harquahala Valley Irrigation District, Central Arizona Project, Arizona	2004	29,348
Minidoka and Teton Basin Projects, Idaho		235
Sugar Pine Dam and Reservoir, Central Valley Project, California		31,520
Sly Park Dam and Research, Central Valley Project, California		1,911
Middle Loup Division, Pick-Sloan Missouri Basin Project, Nebraska	2003	7,457
North Poudre Supply Canal and Diversion Works, Colorado-Big Thompson Project, Larimer County, Colorado		287
La Feria Division, Lower Rio Grande Rehabilitation Project, Texas	2002	1,751
North Poudre Supply Canal and Diversion Works, Colorado-Big Thompson Project, Larimer County, Colorado		2,121

Internal Reviews and Audits of Reclamation Programs

Our goal is to provide accurate, relevant information to managers that withstands audit scrutiny and sets a high standard in financial reporting. To ensure financial accountability, we continue to place increased emphasis on the improvement of policies and practices related to accounting and financial reporting.

During FY 2006, Reclamation implemented revised OMB Circular A-123, *Management’s Responsibility for Internal Control*. Efforts focused on Appendix A – *Fiscal Year 2006 Annual Assurance Statement on Internal Control Over Financial Reporting* and developing and delivering internal control training to directors and managers.

During FY 2006, Reclamation completed one Alternative Internal Control Review (AICR), with no material weaknesses identified, for the Dam Safety Program.

In addition, Reclamation completed the internal control review report with recommendations for the cultural resources review of the Upper Colorado Region which was conducted during FY 2005. In FY 2006, Reclamation conducted a cultural resources review in the Pacific Northwest Region. The final report was issued to the region with recommendations for correction of deficiencies.

In addition, Reclamation completed four Departmental Functional Reviews with no material weaknesses revealed. Functional areas reviewed were:

- Sensitive Automated Information Systems
- Acquisition Management
- Personal Property Management
- Improper Payments

No corrective actions were added as a result of these reviews. In FY 2006, Reclamation also completed 49 corrective actions from previous reviews. As of September 30, 2006, 25 corrective actions remained.

During FY 2006, the Office of Inspector General (OIG) and Government Accountability Office (GAO) audit activity included Reclamation-specific audits, Interior- or Government-wide audits which included Reclamation issues. The OIG completed nine audits, and the GAO completed nine audits. Interior’s FY 2006 Government Performance Results Act (GPRA) Performance Goal for the Management Control and Audit Follow-up Programs (MCAF) was to implement 85 percent of the OIG/GAO recommendations in the MCAF GPRA performance goal. Reclamation exceeded Interior’s goal by implementing 100 percent of the recommendations scheduled for FY 2006. The following table is a summary of the status of audit recommendations.

	FY 2006 Recommendations	Recommendations Implemented/Closed/ Complied in FY 2006	Outstanding Recommendations ¹
OIG	33	33	–
GAO	–	–	1

¹ This outstanding recommendation is from a prior year audit.