The Nation by the Numbers: A Citizen's Guide

A Summary of the FY 2007 Financial Report of the U.S. Government

"We might hope to see the finances of the Union as clear and intelligible as a merchant's books, so that every member of Congress and every man of any mind in the Union should be able to comprehend them, to investigate abuses, and consequently to control them."
President Thomas Jefferson to Treasury Secretary Albert Gallatin, 1802

Financial Condition of the U.S. Government: An Overview

The *Fiscal Year 2007 Financial Report of the United States Government (Report)* provides the President, Congress, and the American people a comprehensive view of how the Federal Government is managing taxpayer dollars. This *Citizen's Guide* is a summary of that Report, which attempts to make sense of the trillions of dollars that the Government receives from taxpayers and spends through thousands of Government programs and services, such as national defense, Social Security, Medicare, and education each year, dwarfing even the largest companies worldwide. It discusses the Government's financial position and condition, its revenues and costs, assets and liabilities, and other responsibilities and commitments, as well as important financial issues that affect the Nation and its citizens both now and in the future. Table 1 summarizes several key indicators of the Government's financial health.

Table 1: The Nation By the Numbers - An Overview

billions of dollars	2005	2006	2007
Gross Costs	**$(3,174.6)**	**$ (3,127.7)**	**$ (3,157.3)**
Total Taxes and Other Revenues	**$ 2,185.5**	**$ 2,440.8**	**$ 2,627.3**
Net Operating Cost [1]	**$ (760.2)**	**$ (449.5)**	**$ (275.5)**
Assets	**$ 1,447.9**	**$ 1,496.5**	**$ 1,581.1**
Less: Liabilities, comprised of:			
Federal Debt held by the Public	$ (4,624.2)	$ (4,867.5)	$ (5,077.7)
Federal Employee & Veteran Benefits	$ (4,491.8)	$ (4,679.0)	$ (4,769.1)
Other Liabilities	$ (798.8)	$ (866.4)	$ (940.1)
Total Liabilities	**$(9,914.8)**	**$ (10,412.9)**	**$ (10,786.9)**
Net Position (Assets Net of Liabilities)	**$(8,466.9)**	**$ (8,916.4)**	**$ (9,205.8)**
Social Insurance Exposures (not included on the balance sheet): [2]			
Closed Group (current participants) [3]	$ (40,038)	$ (44,147)	$ (45,062)
Open Group (current + future participants) [4]	$ (35,689)	$ (38,851)	$ (40,948)
Budget Results			
Unified Budget Deficit	**$ (318.6)**	**$ (247.7)**	**$ (162.8)**

1 Total Net Operating Cost includes Earned Revenues (offset against Gross Costs) and 'Unmatched Transactions and Balances' not shown in this table.

2 present value of 75-year actuarial projections of benefit payments under current law for Social Security, Medicare, and other social insurance programs in excess of their scheduled contributions and earmarked taxes. Not considered liabilities on the balance sheet.

3 includes current participants (i.e., receiving and/or are eligible to receive benefits) ages 15 and over at the start of the period.

4 includes all current and future projected participants (i.e., individuals receiving and/or eligible to receive benefits ages 15 and over at the start of the period, PLUS participants estimated to receive and/or be eligible for benefits over the 75-yr horizon).

Each year, the Administration issues two reports that detail financial results for the Government:

- the ***President's Budget (Budget)***, the Government's primary financial planning and control tool, describes how the Government spent and plans to spend its money. The unified budget deficit, from Table 1 on the previous page shows that the Government spent $163 billion more than it received in fiscal year 2007 on a cash basis.
- the ***Financial Report of the United States Government*** (Report) includes the accrual-based cost of operations, the sources used to finance those costs, how much the Government owns and owes, and the outlook for its social insurance programs. Table 1 shows that the Government's *costs* exceeded its *revenues* by $275.5 billion for fiscal year 2007.

Table 2: The Nation By the Numbers
Budget Deficit vs. Net Operating Cost

Dollars in billions	2006	2007
Unified Budget Deficit	**$247.7**	**$162.8**
Unfunded Postemployment Programs	$187.2	$90.1
Increase in Environmental Liabilities	$45.4	$36.8
Capitalized Fixed Assets, Net	($20.8)	($13.5)
Other	($10.2)	($0.6)
Net Operating Cost	**$449.5**	**$275.5**

The Budget's emphasis is on initiatives and how resources *will be used*, focusing on the Government's spending surplus or deficit. The Report focuses on the Government's net operating cost - how resources *have been used* to fund programs and services. How does the Government's largely *cash-based* spending deficit differ from the largely *accrual-based* net operating cost?

- The Budget shows *receipts*, or cash paid to the Government (e.g., income tax payments and national park fees received); while the Report presents *revenue*, or amounts that the Government has earned, some of which has not yet been received[1].
- The Budget reports cash outlays when the Government makes payments to individuals, businesses or other parties. The financial statements reflect costs in the period in which resources are consumed or liabilities increased.
- From Table 2, almost the entire difference between these two reports can be explained by a single item. The Budget does not include $90.1 billion in postemployment benefits earned by, but not yet due to be paid to, employees in fiscal year 2007.
- Similarly, the Budget does not include an estimated $36.8 billion of additional clean-up costs that the Government will eventually have to pay to fund environmental efforts (e.g., EPA Superfund).
- Conversely, the Budget does include more than $13 billion in net spending for Capitalized Fixed Assets. For Budget purposes, the entire purchase price for major assets, such as buildings or aircraft carriers must be shown as a cost in the year of outlay. However, due to their estimated longevity, agencies capitalize and depreciate (i.e., spread) the cost of these assets over their 'useful lives' in the financial statements.

Together, the Budget and the Report present a complementary perspective on the Nation's financial health and provide a valuable management tool for the country's leaders. The following pages will provide some insight into how the Government managed taxpayer dollars in 2007 and the prospects for the future.

[1] Under GAAP, most U.S. Government revenues are recognized on a 'modified cash' basis, or when they become measurable.

The Government's Financial Position and Condition

Financial position refers to the Government's financial health as of a distinct point in time (September 30 of each year), based on past events. The Government's financial statements provide a number of 'vital signs' of its health, including the assets that the Government owns, the liabilities owed, and the cost of running the Government's many operations and services. How and why the Government's financial position changed during the year, as discussed in the 'Financial Highlights' section of this Report, are also important indicators. As of the end of 2007, the Government's net position (assets net of liabilities) was a net liability of $9.2 trillion.

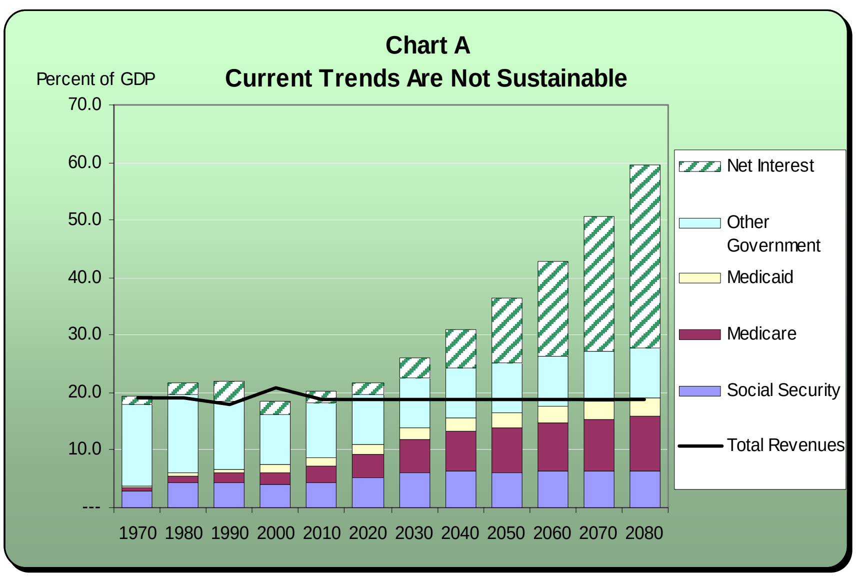
By comparison, the Government's financial or fiscal condition not only considers the Government's current and past performance, but also its capacity to meet future demands and responsibilities. For example, the growing responsibilities associated with future social insurance benefits (e.g., Social Security, Medicare) is a well-documented issue that impacts every citizen in the Nation, due in great part to the aging of the 'baby boom' generation and rising health care costs. The ***Statement of Social Insurance*** (SOSI) compares the resources that the Government expects to receive for these programs from dedicated sources (e.g., earmarked taxes, premiums) to what it expects to have to pay out in benefits over the next 75 years in current dollar terms.

Chart A forecasts the Government's historical major spending programs and revenues over the next 75 years as a percent of Gross Domestic Product (GDP). The projection that revenue as a percent of GDP will remain relatively constant in future years is based on historical data and trends that are not expected to change. Since World War II Federal revenues as a share of GDP have been roughly constant at around 18 percent of GDP. Whenever taxes have risen above this range, policy actions have tended to pull them back.

<u>What Does This Mean to Me?</u>

Gross Domestic Product (GDP). GDP is one of the ways to measure the size of an economy. The GDP is the total market value of all final goods and services produced within a country during a period of time (usually a calendar year).

Simply said, holding revenues constant, required Medicare, Medicaid, and Social Security spending and the related deficit financing costs will far exceed the Government's ability to pay. Projections show that by 2070, total Government expenditures are projected to be 50 percent of GDP. Such levels of expenditures have only been witnessed once before, during World War II, when Government expenditures reached a record high of 44 percent of GDP. And by 2080, expenditures are projected to approach 60 percent of GDP. This would cause dramatic increases in deficit spending, and consequently, as explained later, Federal debt needed to finance them.



The spending for social insurance programs, in particular, is projected to grow at an alarming rate under current law. The precise amounts of the Government's future social insurance responsibilities are far from certain, as they are based on complex calculations and many assumptions, e.g., age, life expectancy, and the cost of health care. However, the magnitude of the problem and the need for a solution are evident and could have a significant impact on the economy in the future unless action is taken in the near future.

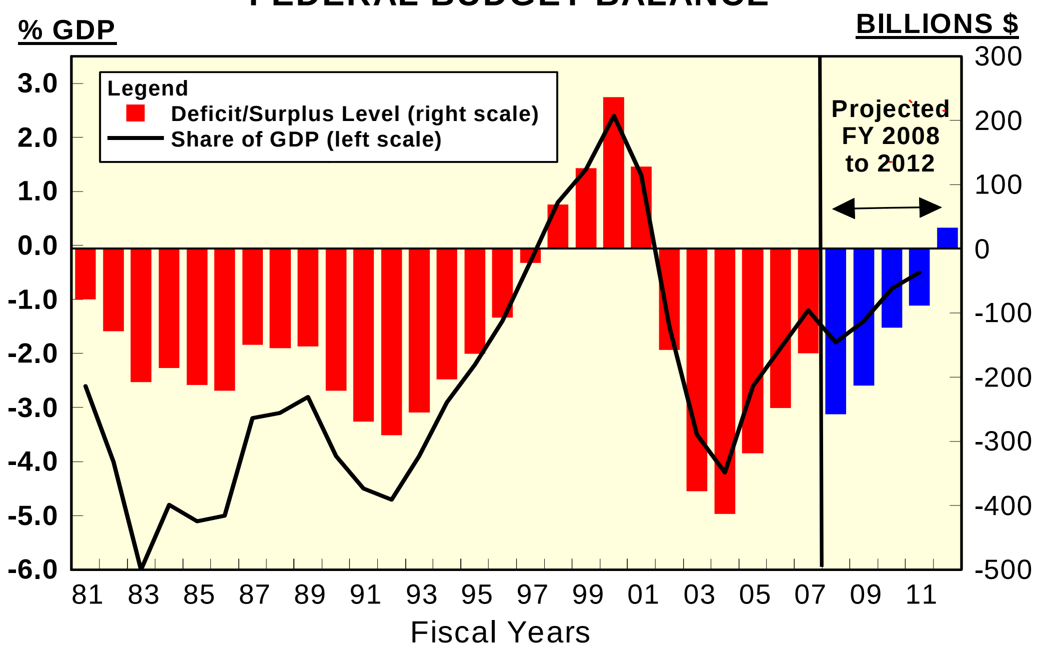
The Economy

The fiscal year 2007 unified budget deficit decreased $85 billion to $162.8 billion, the third consecutive annual decrease. The decrease was due almost entirely to a substantial increase in revenue. Net cost across agencies nearly broke even as the three largest increases (at the Departments of Health and Human Services and Defense, and the Social Security Administration) almost entirely offset the four largest decreases (at the Departments of Agriculture, Education, Homeland Security, and Veterans Affairs).

U.S. economic growth edged up in fiscal 2007, but growth was partly restrained by continued weakening in the residential homebuilding sector and growing financial market uncertainty. Employment gains tapered off through the year, although the unemployment rate remained low. Inflation rose in the first half of the year, due in part to swings in oil and gasoline prices, as well as noticeable increases in food prices, but declined in the second half.

Image 1

FEDERAL BUDGET BALANCE



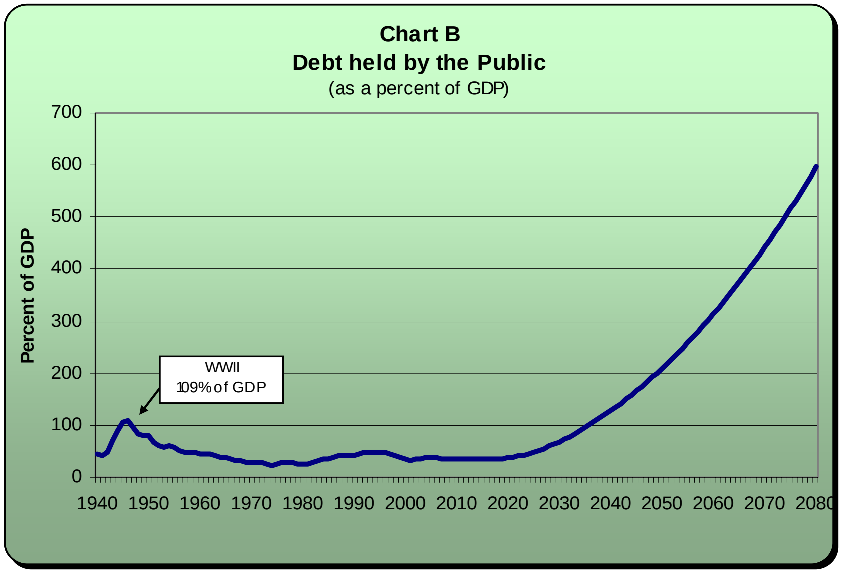
Source of Projections: FY 2008 Mid-Session Review

The Financial and Housing Markets

Financial market turbulence this past summer reflected concern over growing mortgage defaults and a realization that some mortgage-backed securities contained substantially more risk than originally assumed. This caused some investors to move to less risky investments (e.g., Treasury debt). The uncertainty created by those difficulties prompted market participants to reappraise values of assets in a broader array of markets for equities, sovereign debt, and corporate debt. A widening of spreads reflected this repricing of risk: for example, the spread between the Baa corporate bond yield and the comparable U.S. Treasury yield widened to a two year high in mid-September 2007.

The Government's Debt

The Government must borrow from the public at home and abroad to fund its deficits. The projected increases in interest expenditures as a percent of GDP in Chart A above and in total public debt in Chart B indicate that the anticipated social insurance spending shortfall could have a dramatic and extended impact on the Government's financial health. As shown in Chart B, under current policy, the confluence of these trends would cause the Government's debt levels to more than triple by 2040 (well above even the WWII peak of 109 percent), to double again by 2060, and approach six times GDP levels by 2080. At some point before the debt reaches such unprecedented levels, the world's financial markets would likely cease lending to the United States. Although the precise point at which this would occur is unknown, it is clear that these projected debt levels cannot be sustained indefinitely. As indicated earlier, such dramatic projections are based on a wide array of assumptions about the future. Nonetheless, it is clear that action will be required in the future to bridge this emerging fiscal imbalance.



However, debt held by the public accounts for only approximately half of the Government's gross debt. The other half is primarily held in the form of special nonmarketable securities by various parts of the Government. This intragovernmental debt does not appear on the balance sheet because, under current accounting principles, claims of one part of the Government against another are eliminated when consolidated governmentwide financial statements are prepared so that the statements do not appear to be inflated. Accounting principles prevent such 'left hand owing the right hand' amounts from distorting results.

Gross Federal debt, excluding some adjustments, is subject to the statutory debt limit. Prior to 1917, the Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress established a dollar ceiling for Federal borrowing, which has been periodically increased over the years (most recently from $9.0 trillion to $9.8 trillion in 2007). At the end of fiscal year 2007, the amount of debt subject to the limit was $8.9 trillion, $893.7 billion under the limit.

Financial Highlights

The Government's financial position and condition have traditionally been expressed through the Budget, focusing on the impact of surpluses and deficits. While this primarily cash-based discussion of the Government's net outlays (deficit) or net receipts (surplus) tells an important part of the story, the rest is told by the changes in its assets and liabilities. The Government Accountability Office (GAO) is responsible for conducting the audit of the Government's financial statements. For FY 2007, GAO has again issued an audit opinion 'disclaimer', as it has in each of the past eleven years, on the consolidated financial statements for the fiscal years ended September 30, 2007 and 2006. This means that the auditors did not have sufficient information to determine whether the financial results were reliable. Material weaknesses in internal control and other scope limitations resulted in conditions that prevented GAO from forming and expressing an opinion. However, FY 2007 marks the first year that the Government earned an unqualified audit opinion on a Report component - - the Statement of Social Insurance (SOSI).

The following highlights the Federal Government's financial results for FY 2007 and shows how the various statements relate to each other.

Image 2
Navigating the Government's Financial Statements

I

Statements of Net Cost

(in billions)	2007	2006
Gross Cost	$ (3,157.3)	$ (3,127.7)
(-) Earned Revenue	247.8	226.4
(=) Net Cost [1]	**$ (2,909.5)**	**$ (2,901.3)**

How does Net Operating Cost affect Net Position?

II

Statements of Operations and Changes in Net Position

(in billions)	2007	2006
Net Position (beginning)	**$ (8,916.4)**	**$ (8,466.9)**
(+) Revenue	2,627.3	2,440.8
(-) Net Cost [1]	(2,909.5)	(2,901.3)
Net Operating Cost [2]	**(275.5)**	**(449.5)**
(=) Net Position (end) [3]	**$ (9,205.8)**	**$ (8,916.4)**

How does cost differ from the budget deficit?

IV

Statements of Changes in Cash Balance from Unified Budget Deficit & Other Activities

(in billions)	2007	2006
Unified Budget Deficit [4]	**$ (162.8)**	**$ (247.7)**
Increase (Decrease) in operating cash balance, Net	26.1	15.7
(+) Operating Cash (begin)	**43.6**	**27.9**
(=) Operating Cash (end) [5]	**$ 69.7**	**$ 43.6**

How does the deficit relate to cash?

III

Reconciliation of Net Operating Cost & Unified Budget Deficit

(in billions)	2007	2006
Net Operating Cost 2	**$ (275.5)**	**$ (449.5)**
Increase (Decrease) in Postemployment Liabilities, Environmental Liabilities, Other, Net:	112.7	201.8
Unified Budget Deficit [4]	**$ (162.8)**	**$ (247.7)**

V

Balance Sheet

(in billions)	2007	2006
Assets:		
Cash [5]	$ 128.0	$ 97.9
Property	691.1	688.5
Other	762.0	710.1
Total Assets	**1581.1**	**1496.5**
Liabilities:		
Debt held by the Public	5077.7	4867.5
Postemployment Benefits	4769.1	4679.0
Other	940.1	866.4
(-) Total Liabilities	**(10,786.9)**	**(10,412.9)**
Net Position [3]	**$ (9,205.8)**	**$ (8,916.4)**

What does the Govt own and owe?

Net Position also shown in II

What about Social Security and Medicare?

VI

Statement of Social Insurance (SOSI)*

Expenditures for future Scheduled Benefits, Net of Contributions and Earmarked Taxes

	2007	2006
Social Security	$ (6,763)	$ (6,449)
Medicare	$ (34,085)	$ (32,305)

*Note - The SOSI presents actuarial estimates of the present value of future expenditures, in excess of contributions over a 75-yr period. SOSI amounts are future sustainability estimates over an extended period. These amounts are for future benefit payments not yet due and therefore are NOT reflected in the balance sheet or other principal statements.

1 The Statements of Net Cost presents the Government's net operating expense, which, when combined with tax and other revenue in the Statement of Operations and Changes in Net Position, yields the Government's Net Operating Cost and shows how the Government's Net Position changed during the year.

2 . Net Operating Cost is the Government's net cost, less any 'unearned' revenue (e.g., taxes, fees). The 'Reconciliation Statement' shows the primary differences between the Government's accrual-based Net Operating Cost and cash-based unified budget deficit. Net Operating Cost includes t$6.7 billion adjustment for unreconciled transactions.

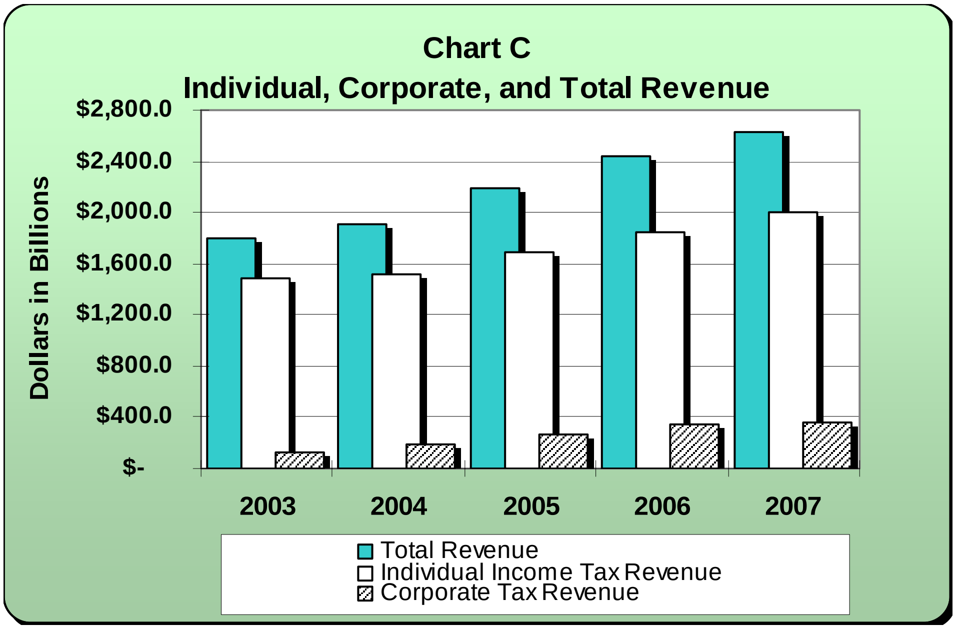
3 The Net Position from the Statement of Operations and Changes in Net Position agrees to the Net Position on the Balance Sheet, which is based on the difference between the Government's reported assets and liabilities.

4 The unified budget result is used in the Reconciliation of Net Operating Revenue (or Cost) and Unified Budget Surplus (or Deficit) and the Statement of Changes in Cash Balance from Unified Budget and Other Activities to show how the Federal Government's spending deficit is related to its Net Operating Cost.

5 The Federal Government's ending operating cash balance from the Statement of Changes in Cash Balance from Unified Budget and Other Activities is the same as the operating cash component of the "Cash and other monetary assets" line on the Balance Sheet.

Revenue: "What Came In"

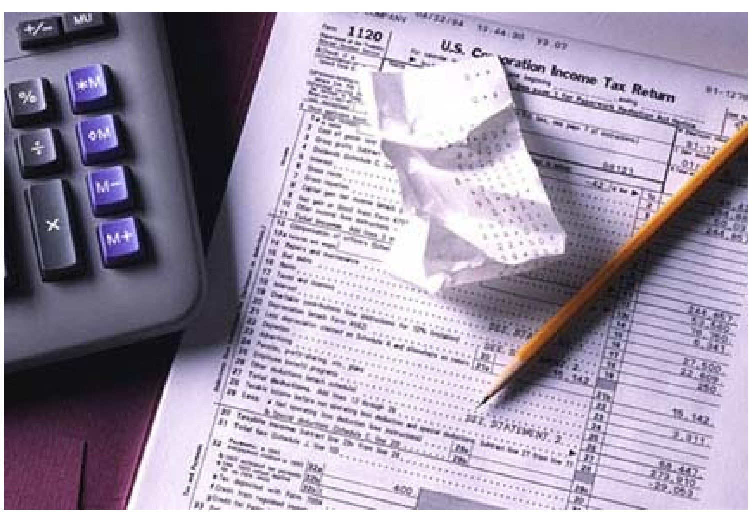
The Government's ***Statement of Operations and Changes in Net Position***, much like a corporation's income statement, shows the Government's 'bottom line' (i.e., its net revenues and costs). The Government's revenue is mostly comprised of individual and corporate income taxes. In 2007, revenues grew to $2.6 trillion, establishing a new record.



Facts and Figures:

- 2007 marked the fourth consecutive fiscal year of substantial revenue growth. A combination of solid economic growth and improved corporate tax yields have contributed to revenue collections that exceed 2003 levels by 46 percent.

- In 2007, the Government collected $2.6 trillion. Cash collections have increased by an average of $200 billion per year since 2003, contributing to a reduction of both the unified budget deficit and net operating cost.



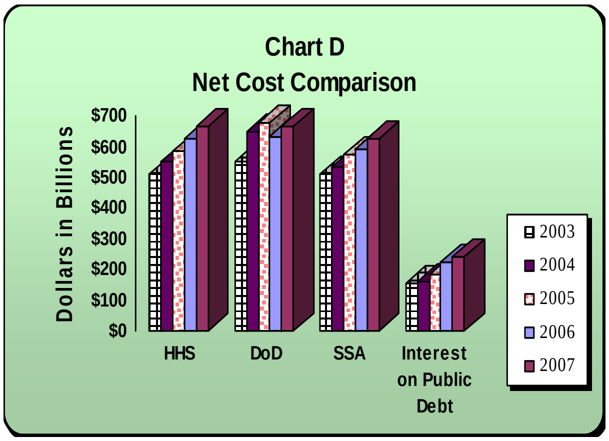
IRS

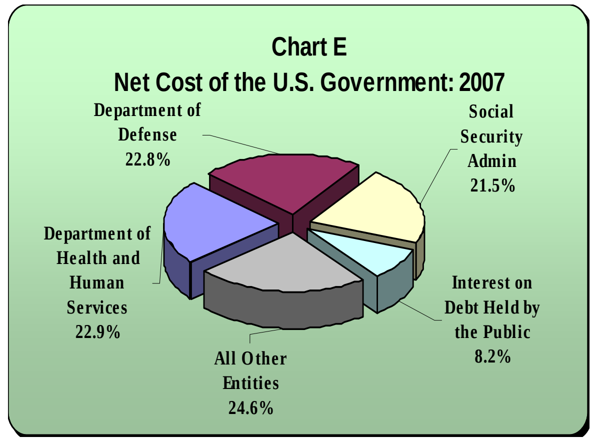
Department of the Treasury
Internal Revenue Service

IRS e-file

Cost: "What Went Out"

The Government nets its costs against both earned revenues from Government programs (e.g., Medicare premiums, national park entry fees) and taxes and other revenue. Taxes account for the vast majority of total revenues. The government's 'bottom line' is its net operating cost. The Government must finance any costs as they are paid that cannot be covered by revenues with Federal debt, subject to the statutory debt limit.





Facts and Figures:

- Gross costs, which increased slightly to $3.2 trillion in 2007, have increased by an average of 5.7 percent over the past five years, including a slight decline in 2006.
- The Departments of Health and Human Services, and Defense, as well as the Social Security Administration and interest on public debt, accounted for approximately three-fourths of the Government's total net costs in FY 2007.
- Much of the annual fluctuation in actuarial costs stems from the methodology and assumptions used by the Department of Veterans Affairs to calculate post-employment benefit liabilities.

Assets: "What We Own"

The Government's total assets, most of which are property, plant, and equipment, increased $84.6 billion to $1.6 trillion in 2007.

Facts and Figures:

- Net property, plant, and equipment has been the Government's largest asset over the past seven fiscal years, comprising more than 40 percent of total assets in FY 2007.

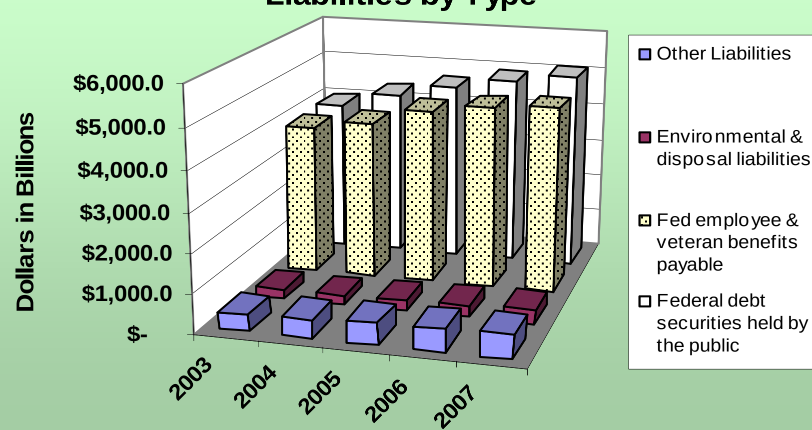
- In addition to the $1.6 trillion in total assets, the Government owns certain other assets such as stewardship land (e.g., national parks and forests) and heritage assets (e.g., national memorials, historic structures).

.

Liabilities: "What We Owe"

Total Liabilities increased $374.0 billion to nearly $10.8 trillion in fiscal year 2007. Most of this total is comprised of Federal debt held by (owed to) the public and accrued interest, and Federal employee and veteran benefits payable.

Chart F
Liabilities by Type



Facts and Figures:

- Debt held by the public and accrued interest, which increased $210.2 billion to $5.1 trillion in 2007, accounted for nearly 50 percent of the Government's total liabilities.

- After nearly doubling as a share of GDP over a 15-year period throughout the mid-1990s to about 50 percent in 1993, smaller deficits and a period of surpluses in the late 1990s led to a decline in the public debt as a percentage of GDP to 36.9 percent in 2007.

- Federal employee and veteran benefits payable make up another 44 percent of total liabilities. These liabilities have increased dramatically in recent years, from $2.6 trillion at fiscal year-end 1999, to $4.8 trillion in 2007.

- As of the end of 2007, the Government's liabilities exceeded its assets (net position) by $9.2 trillion.

What Does This Mean to Me?

Federal Debt held by the Public

Based on current estimates, every citizen's share of the Federal debt is over $17 thousand.

Nearly half of the U.S. public debt is held by foreign countries, so a substantial portion of government interest payments go abroad.

Looking Ahead

Fiscal responsibility requires the sound stewardship of taxpayer money. Once the Congress and the President decide on overall spending levels, taxpayer dollars should be managed to maximize results. The President's Management Agenda (PMA) is creating a results-oriented Government where agencies and programs are managed professionally and efficiently to achieve the results expected by the Congress and the American people.

The PMA's broad goal is to make the Government more results-oriented with a focus on achievement, efficiency, and accountability. It emphasizes improving Government operations by setting clear goals and action plans, and then following through on those plans. Agencies continue to manage to achieve better results. PMA standards for success are used to measure agencies' progress and achievement in meeting overall goals. Agency ratings and other related information are discussed in the Report and are available at: www.whitehouse.gov/results/agenda/standards.pdf

Find Out More

You will find details and more in-depth information on the issues discussed here in the full Financial Report of the U.S. Government. As the information in this Report potentially impacts every U.S. citizen, all are encouraged to explore the facts contained herein and to ask questions about how the Government manages taxpayer money.

This Report and other information about the Nation's finances are available on the Internet at:
http://www.fms.treas.gov/fr/index.html
http://www.whitehouse.gov/omb/financial/index.html
www.gao.gov