Fiscal Year 2003 Financial Report

DEPARTMENT OF COMMERCE

UNITED STATES OF AMERICA

Financial Management and Analysis

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Financial Management and Analysis

Introduction

The Office of Financial Management (OFM) within the Department of Commerce formulates and prescribes Department-wide financial management and accounting policies, procedures, and controls. OFM also develops and maintains a Departmental financial system Commerce Administrative Management System (CAMS), and provides assistance in the implementation of these measures.

OFM Mission

To provide financial information, services, and systems of a quality unparalleled in Government to meet the needs of the Department of Commerce's program managers and administrators.

OFM Vision

- Program managers must also be knowledgeable, responsible, and accountable fiscal managers;
- Accurate and timely financial data must be readily available to management and stakeholders; and
- Financial management must be conducted through a Department-wide financial management system that directly supports work and resource planning and program performance measurement.

Initiatives and Priorities

We are creating a financial management environment that complies with federal laws and regulations and that will provide our executives with timely, accurate financial and performance information. As part of this process, we are pursuing the following major initiatives:

- Improve financial accountability;
- Improve financial management systems;
- Improve administration of federal grant programs; and
- Develop human resources in the financial management community.

Improve Financial Accountability

Under the Secretary's leadership, we are continuing to give the highest priority to providing accurate financial data to our internal and external customers, and to our accountability for all assets. This is evidenced in part, by the Department's receipt of unqualified audit opinions for several years and the decrease in internal control weaknesses cited in our audits.

The Department received a “red” rating on the financial management section of the President’s Management Agenda. The rating was mainly due to the Department’s lack of a single integrated financial management system and a repeat material internal control weakness. However, during every quarter of FY 2003, we received a “green” rating from the Office of Management and Budget (OMB) for our planning and progress in this area. The Department plans to obtain a green status for FY 2004 with the resolution of the internal control material weakness in FY 2003, along with the implementation of a single integrated financial management system in the first quarter of FY 2004.

In FY 2003, we aggressively moved toward improving the Department’s overall financial management. This was evidenced by the following:

- The Department received an unqualified opinion on the FY 2003 consolidated financial statements.
- The Department submitted accelerated quarterly financial statements to OMB by the prescribed deadlines, and submitted the Performance and Accountability Report to OMB a month earlier than the prescribed deadline of January 30, 2004.
- As of October 2003, CAMS was implemented at the National Institute of Standards and Technology (NIST), the National Telecommunications and Information Administration (NTIA), and the Technology Administration (TA), completing the CAMS implementation phase.
- With CAMS being fully implemented, along with the improvement of automated budget controls, and the downgrading of the information technology (IT) general controls weakness to a reportable condition, the Department was able to resolve its remaining material weakness.

In addition, the Department concentrated on the President’s Management Agenda initiative to reduce erroneous payments. The Improper Payments Information Act of 2002 (Public Law 107-300) requires that, beginning in FY 2004, agencies are to review annually all programs they administer and identify those which may be susceptible to significant erroneous payments. For all programs where the risk of erroneous payments is significant, agencies shall estimate the annual amount of erroneous payments, and report the estimates to the President and Congress with a progress report on actions to reduce erroneous payments.

The Department has not identified any significant problems with erroneous payments; however, we recognize the importance of maintaining adequate internal controls to ensure proper payments, and our commitment to the continuous improvement in the disbursement management process remains very strong.

To determine the nature and extent of possible improper payments, and to assess the level of internal controls and the overall risk of erroneous payments within the Department, a comprehensive questionnaire on erroneous payments was issued to the Department’s payment offices. The payment office responses were analyzed and a consolidated risk assessment was completed.

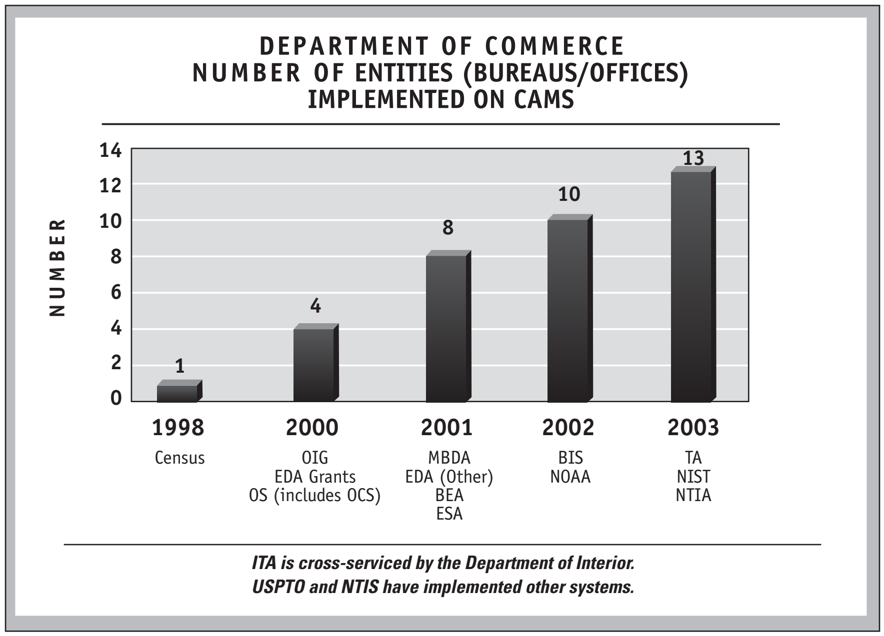
The results of our assessments demonstrate that overall, the Department has strong internal controls over the disbursement process, the amounts of erroneous payments in the Department are immaterial, and the risk of erroneous payments is low. However, we believe we can enhance our current process and will work with each of our payment offices to identify and implement additional procedures to prevent and detect erroneous payments. Procedures will include quarterly reporting to the Department on erroneous payments, identifying the nature and magnitude of the erroneous payment along with any necessary control enhancements. Also, we plan to complete the implementation of the recovery audit requirements for contracts by OMB’s December 31, 2004 deadline.

For FY 2003 and beyond, we will continue our efforts to ensure the integrity of our financial information and explore new ways to enhance our current processes. We will submit accelerated quarterly financial statement information to OMB and prepare for the submission of the FY 2004 Performance and Accountability Report by the mandated November 15, 2004 deadline. Monitoring the progress of correcting internal control weaknesses and identifying other areas for improvement will remain a high priority.

Improve Financial Management Systems

The lack of an integrated financial system was reported as a material weakness in the Department's Fiscal Year 2002 Federal Managers' Financial Integrity Act letter and in the Independent Auditors' Report. The Department fully implemented a detailed Federal Financial Management Improvement Act Remediation Plan and audit action plans to resolve this weakness. The implementation of CAMS was a key factor in meeting the needs of a single integrated system. CAMS has replaced most financial systems within the Department. Bureaus that were previously on compliant systems continue to use those systems with some entities planning on converting to CAMS at a future point in time. The financial information from these systems and CAMS is integrated in the Corporate Database (as discussed further below) for consolidated financial reporting.

We have completed implementation of CAMS. As of October 2003, CAMS was implemented at all 13 departmental entities that previously operated non-compliant financial management systems, including NIST, that provides cross-services to NTIA and TA. The graph to the right depicts progress and successes of the CAMS implementation schedule by the bureaus.



The Department evaluated and implemented a Corporate Database to produce consolidated financial reports. The Corporate Database provides an integrated solution to financial statements and Federal Agency Centralized Trial Balance System I (FACTS I) Adjusted Trial Balance reporting at the Department, bureau, and Treasury Appropriation/Fund Group level, and also provides the ability to perform data analysis.

During FY 2003, the Corporate Database was utilized to produce the quarterly financial statements that were submitted to OMB by the mandated deadline. Also, the database was updated to produce the Department's Statement of Financing, footnotes, FACTS I notes, financial analysis reports, and other additional information required for the government-wide financial statements.

Although the Department has an integrated financial system with the completed implementation of CAMS and the Corporate Database, there is a need to look forward to ensure the financial system will provide reliable, timely, and accurate financial data to management.

The Department, with the assistance of an independent contractor, has examined the organization, staffing, and funding necessary and has developed a plan to ensure CAMS can achieve and maintain Joint Financial Management Improvement Program compliance during its useful life.

Improve Administration of Federal Grant Programs

The Department ensures policy consistency across grant programs through its Office of Acquisition Management (OAM) under the Department's Chief Financial Officer and Assistant Secretary for Administration. OAM is charged with developing, issuing, and overseeing implementation of policies and procedures for the administration of the Department financial assistance programs, including grants, cooperative agreements, loans, and loan guarantees. OAM also works closely with the Office of the General Counsel, Office of the Inspector General (OIG), and the Grants Officers to develop, implement, and coordinate policies relating to financial assistance matters.

The Department's Grants and Cooperative Agreements Manual, issued in February 2002, provides agency-wide guidance on grants administration and provides a uniform set of minimum procedures for soliciting, reviewing, awarding, managing, and closing out grants.

The Department is in the final stages of implementing the Automated Standard Application for Payments (ASAP), which is an all-electronic payment and information system developed jointly by the Financial Management Service at the Department of Treasury and the Federal Reserve Bank of Richmond. ASAP is a system through which grantee organizations receiving federal funds can draw from accounts preauthorized by federal agencies. The bureaus have signed Memorandum of Understandings with Treasury and are at various stages of enrolling grant recipients to the ASAP system. Additionally, the CAMS and ASAP interface has been completed and certified by Treasury and the Federal Reserve Bank system.

In addition, OMB has designated the Department of Commerce as a partner Grants.gov agency. Grants.gov is a government-wide electronic portal that will include grant opportunity announcement (E-FIND) and electronic application (E-APPLY) capabilities. The Department's grants administration and program officials are working with information technology staff to review and prepare existing grants systems for successful integration with Grants.gov solutions.

Develop Human Resources

All of the Department's bureaus have established Chief Financial Officer (CFO) positions or similar positions of financial leadership. The Department has both a CFO Council and Finance Officer's Council that meet monthly to discuss common financial management issues and problems, including human resources, budget, procurement, and information technology systems, as well as financial accountability issues. Conferences of bureau finance officials are held as necessary, to ensure complete understanding and agreement with Departmental financial management objectives and approaches. OFM also participates in meetings of the government-wide CFO Council and of the Federal Financial Managers Council to address issues that cut across agencies. OFM works closely with bureau finance officers to assist in the proper implementation of Departmental standards and guidance. When specific issues arise, OFM conducts thorough studies and consults with the central agencies, the Federal Accounting Standards Advisory Board, the OIG, and similar organizations to develop the best possible financial management standards.

The Department's continuing professional education program enhances workforce development. This program requires a minimum of 40 hours of training and development activities per year for each financial management professional. In addition, the Department provides internships through a variety of sources to give finance and accounting majors an opportunity to gain hands-on accounting experience, while introducing potential future employees to the opportunities that exist at the Department. In FY 2003, the Department continued its partnership with the National Academy Foundation (NAF), and employed finance and technology interns from the NAF Internship Program.

Financial Management Indicators

OMB prescribes the use of quantitative indicators to monitor improvements in financial management. The table below shows our performance during FY 2003 against the target performance established by OMB and Treasury.

Financial Performance Measures

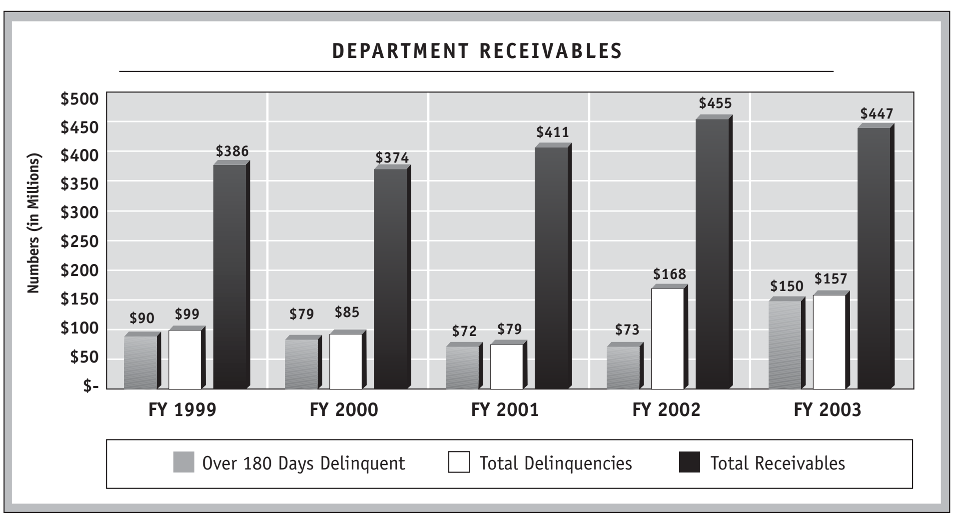
Financial Performance Measure	FY 2003 Performance	FY 2003 Target
Percentage of timely vendor payments	94%	95%
Percentage of payroll by electronic transfer	99%	74%
Percentage of Treasury agency location codes fully reconciled	100%	100%
Timely reports to central agencies	100%	95%
Audit opinion on FY 2003 financial statements	Unqualified	Unqualified
Material weaknesses as reported by OIG	0	0

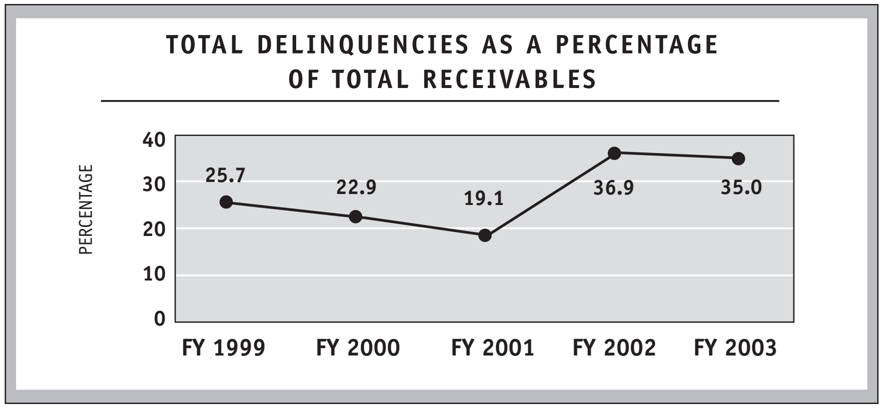
Debt Management

Receivables and Debt Management

The Department has incorporated the principles of the Credit Reform Act of 1990 into the operations of its credit and debt programs. Prescreening procedures, account-servicing standards, determined collection of delinquent debt, inventory management, and asset disposition standards have helped to diminish significantly the amount of risk inherent in credit programs. These procedures were established to ensure that credit costs are properly identified and controlled, that borrowers' needs are met, and that costs to the taxpayers are minimized.

Total Department receivables increased from $455 million in FY 2002 to $447 million in FY 2003, as reported on the Department's Treasury Report on Receivables (TROR). The TROR is the primary means for the Department to provide comprehensive information on the gross value of receivables and delinquent debt due from the public. Delinquent debt over 180 days has increased from $73 million in FY 2002 to $150 million in FY 2003. This increase was due primarily to a $92 million guaranteed loan default that moved into the 180 days delinquency category. Total delinquencies, as a percentage of total receivables for the Department, decreased slightly from 36.9 percent in FY 2002 to 35.0 percent in FY 2003.





The Debt Collection Improvement Act of 1996 established the Treasury Department as the collection agency for federal agency debts that are more than 180 days delinquent. It also established Treasury's Financial Management Service as the federal government's debt collection center. In FY 1998, the Department of Commerce signed a letter of agreement with Treasury for cross-servicing of debt more than 180 days delinquent. Almost $16 million in delinquent debt has since been referred to Treasury for cross-servicing.

During FY 2001, the issuance of the revised, "Federal Claims Collection Standards" and the revised OMB Circular No. A-129, "Policies for Federal Credit Programs and Non-Tax Receivables," provided agencies greater latitude to maximize the effectiveness of federal debt collection procedures. Since then, the Department has utilized all the tools available to improve the management of our debt.

Payment Practices

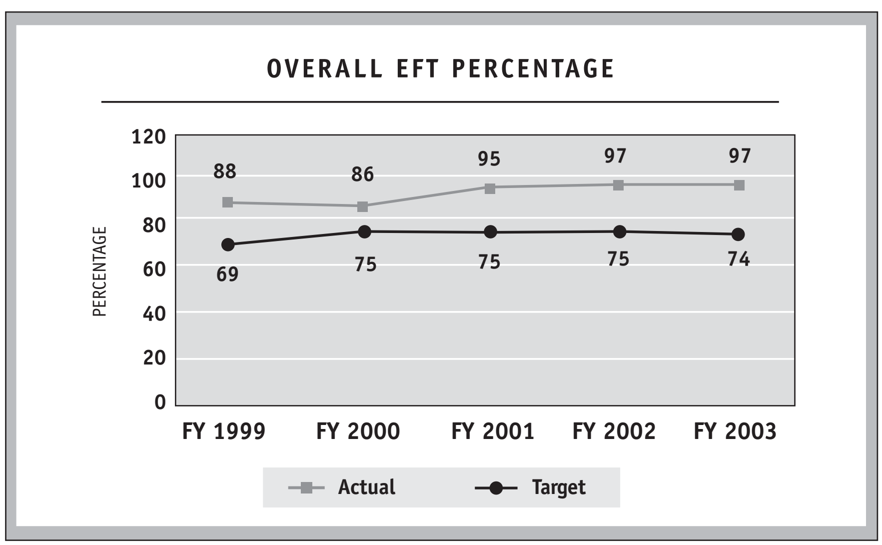
Electronic Funds Transfer (EFT)

During FY 2003, we continued our efforts to maximize the use of payment mechanisms compliant with Electronic Funds Transfer (EFT) as required by the Debt Collection Improvement Act of 1996. Our achievements in this area are illustrated in the table below:

Payment Category	FY 2003 EFT Percentage	FY 2002 EFT Percentage	FY 2003 Total Volume (Actual Count)	FY 2002 Total Volume (Actual Count)
Retirement Benefits	99%	99%	4,400	4,343
Salary	99%	98%	1,128,938	1,187,122
Vendor & Misc.[1]	94%	93%	507,696	664,280
TOTAL	**97%**	**97%**	**1,641,034**	**1,855,745**

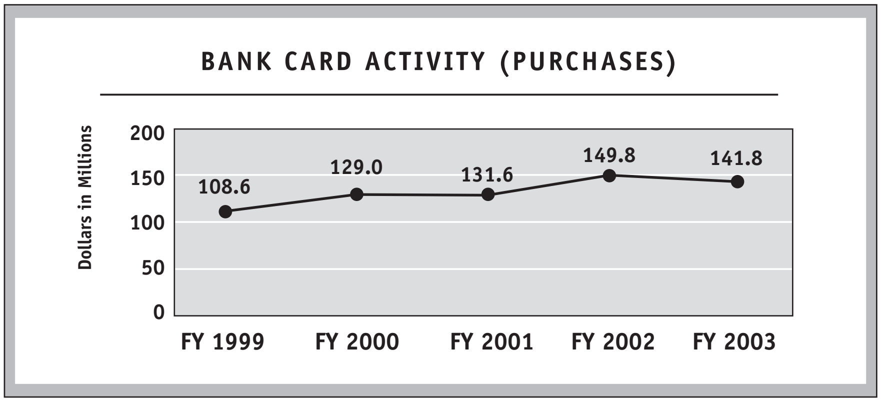
[1] *Includes purchase card transactions.*

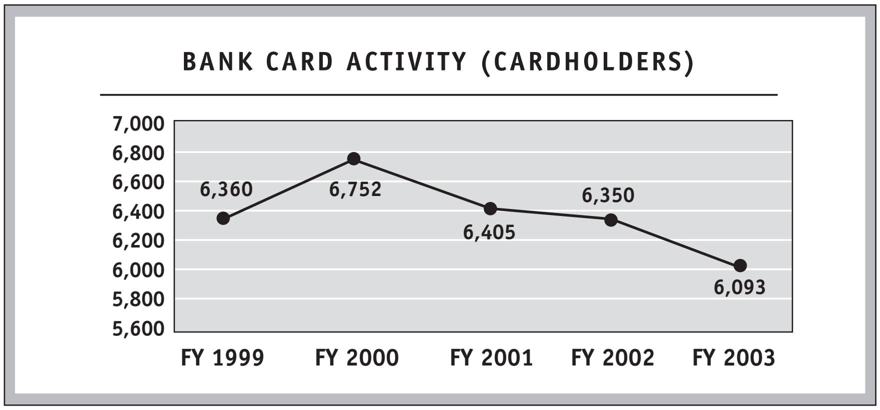
The Department's overall EFT percentage remained steady at 97 percent in FY 2003. We substantially exceeded Treasury's government-wide goal of 74 percent for FY 2003. The Department continued to progress with one percent increase in the EFT percentage for both vendor and miscellaneous payments, and salary payments.



Bankcard

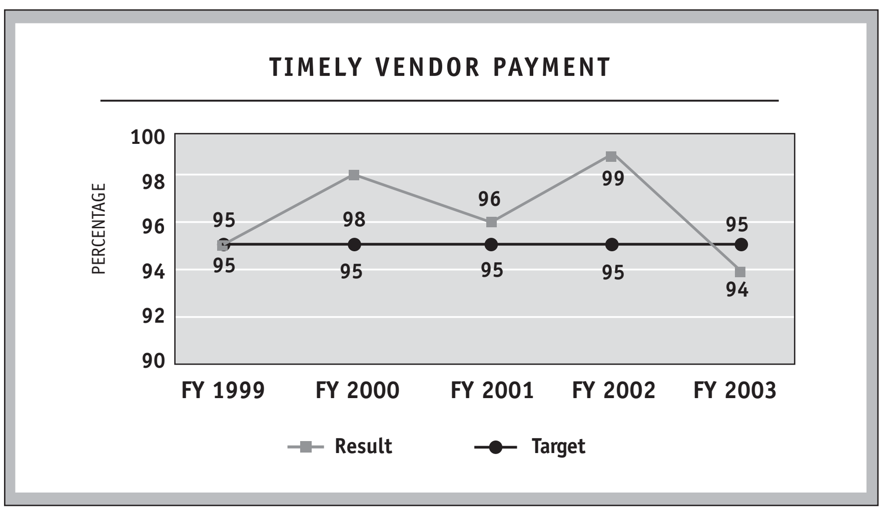
We are committed to the use of bank cards as a means of streamlining Departmental procurements. However, due to the conclusion of the Decennial Census disbursement activity in FY 2002, Departmental usage of the card declined slightly from 6,350 cardholders in FY 2002 to 6,093 in FY 2003. Concurrently, the amount of purchases declined from $149.8 million in FY 2002 to $141.8 million in FY 2003. The Department has continued to monitor the internal controls surrounding these purchases to ensure that all such purchases are legal and proper. As of September 30, 2003, the Department had an overall zero percent bankcard delinquency rate, compared to the government-wide one percent delinquency rate.





Prompt Payment

The Department made approximately 94 percent of all payments on time in FY 2003, compared to 99 percent reported in FY 2002. The number of invoices with late-payment interest penalties increased from 9,020 in FY 2002 to 15,144 in FY 2003. Our overall performance of 94 percent in FY 2003 is just slightly lower than the government-wide goal of 95 percent. The change in the prompt payment measure is mainly due to one bureau's conversion to an integrated financial system during the year. As a result, some payments were delayed during the conversion period from the old to new system. We will continue to monitor our bureaus' payment performance to maintain our timely vendor payment percentage.



Financial Review

This is the eighth annual submission of the Department's financial statements made in accordance with the requirements of the Chief Financial Officers Act as of 1990 amended by the Government Management Reform Act of 1994. These statements have been compiled according to the guidance issued by OMB. In order to comply with OMB Bulletin No. 01-09, and to fully disclose the Department's financial position and results, we have prepared consolidated financial statements. The independent auditor, contracted by OIG, is responsible for auditing the Department's consolidated financial statements.

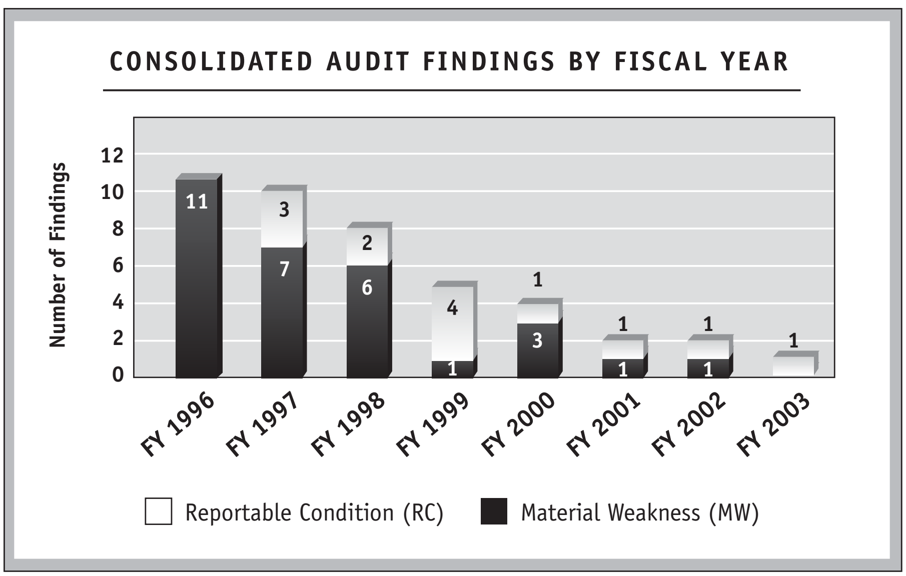
Unqualified Financial Statement Audits

The Department is committed to strong financial management, and has made much progress in this area. We have received unqualified opinions on our consolidated financial statements since FY 1999. This achievement results from our commitment to strong management control and accountability of our financial resources, a commitment that we are extending into the future as we seek to further improve management of our financial resources. Significant progress was also made in reducing internal control weaknesses. The Department currently has no material weakness, and one reportable condition related to improvements needed in financial management systems. The table and chart at the right illustrate our progression toward full attainment of unqualified audit opinions and our progress in correcting the material weaknesses and reportable conditions identified at the Department level.

Summary of Audit Opinions

Type of Opinion	FY 1998 Number of Reporting Entities	FY 1999 Number of Reporting Entities	FY 2000 Number of Reporting Entities	FY 2001 Number of Reporting Entities	FY 2002 Number of Financial Audits	FY 2003 Number of Financial Audits
Unqualified	11	14	9[1]	4[1]	3[1]	3
Unqualified/Balance Sheet Only	2	0	0	0	0	0
Disclaimer	1	0	0	0	0	0
Not Audited	1	1	0	0	0	0

[1] Decrease in number of reporting entities due to entities being combined for audit.



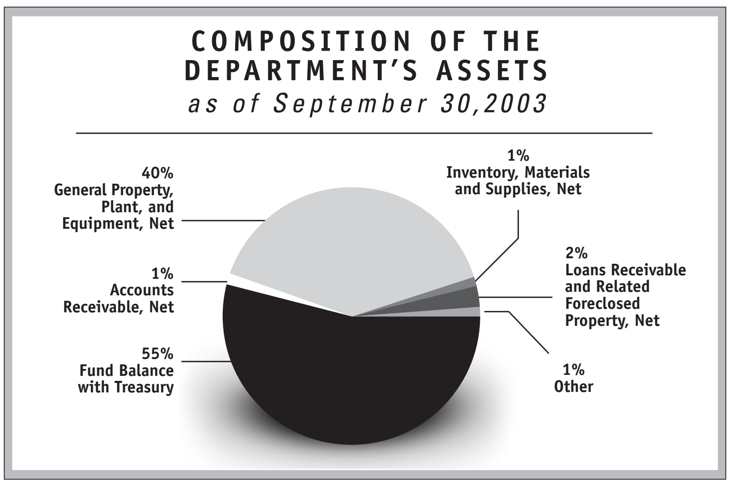
Analysis of FY 2003 Financial Conditions and Results

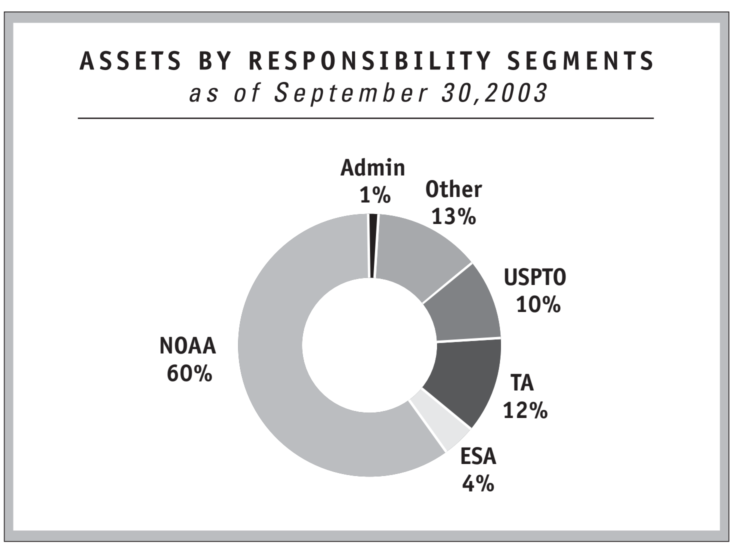
(Dollars in Thousands)

Composition of Department of Commerce Assets and Assets by Responsibility Segments

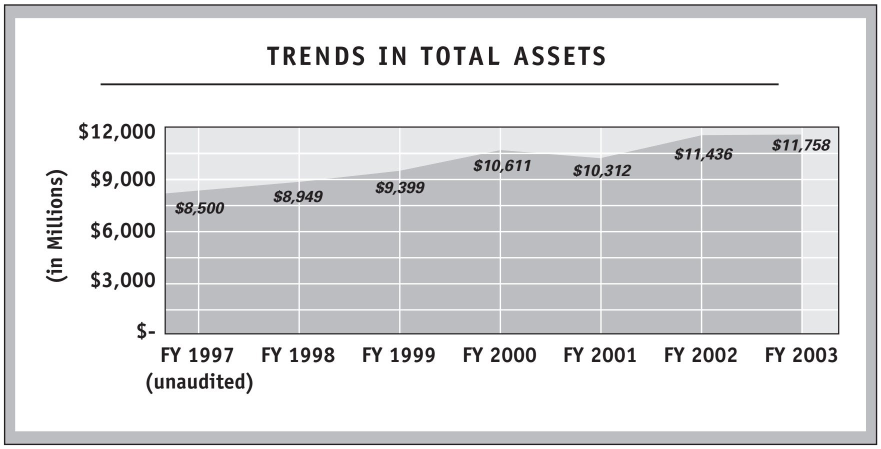
The composition and distribution of the Department's assets remained generally consistent from FY 2002 to FY 2003.

At September 30, 2003, Fund Balance with Treasury of $6.50 billion is the aggregate amount of funds available to make authorized expenditures and pay liabilities. General Property, Plant, and Equipment, Net of Accumulated Depreciation (General PP&E) of $4.67 billion includes $1.25 billion of satellites and weather measuring and monitoring systems, $2.51 billion of Construction-In-Progress, primarily of satellites and weather systems, and laboratories and other property, plant, and equipment totaling $910 million. Loans Receivable and Related Foreclosed Property, Net of $273 million primarily results from the National Oceanic and Atmospheric Administration's (NOAA) direct loan programs.

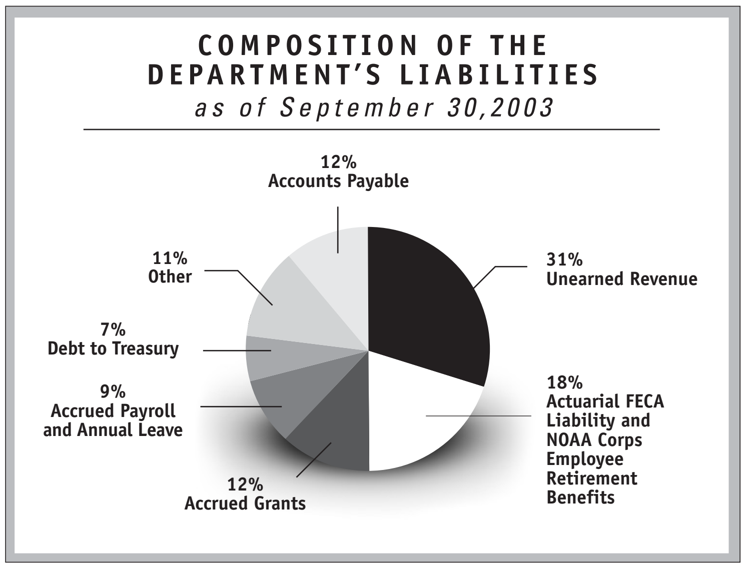




Trends in Assets



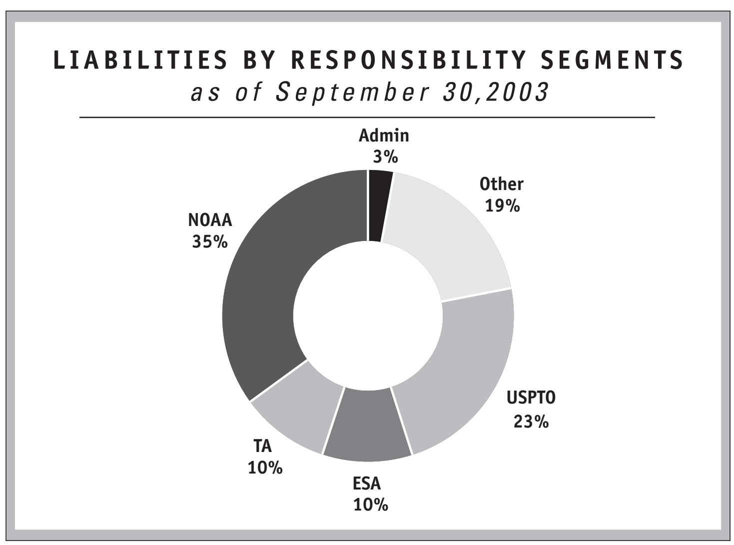
Total Assets increased $322 million or 3 percent, from $11.44 billion at September 30, 2002 to $11.76 billion at September 30, 2003. Fund Balance with Treasury increased $189 million or 3 percent, from $6.31 billion to $6.50 billion, primarily due to higher Appropriations Received and higher Undelivered Orders (Unpaid) resulting from the delay of receipt of the increased appropriations, because of the continuing resolution in the first half of FY 2003. General PP&E increased $126 million or 3 percent, from $4.54 billion to $4.67 billion, primarily due to the National Institute of Standard and Technology's (NIST) construction of the Advanced Measurement Laboratory building and NOAA's purchase, completed construction, and modernization of environmental satellites and weather measuring and monitoring systems. Advances and Prepayments decreased $8 million or 15 percent, from $53 million to $45 million, primarily due to the U.S. Patent and Trademark Office's (USPTO) reclassification of Leasehold Improvements to Construction-in-Progress from advance payments previously made to General Services Administration (GSA) for USPTO's consolidated site under construction in Alexandria, Virginia.



Composition of Department of Commerce Liabilities and Liabilities by Responsibility Segment

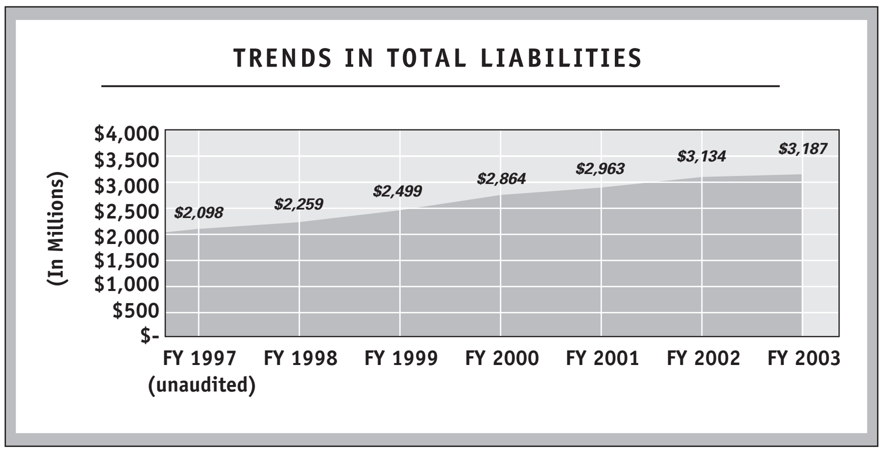
The composition and distribution of the Department's liabilities also remained generally consistent from FY 2002 to FY 2003.

Unearned Revenue of $999 million represents the portion of monies received from customers for which goods and services have not been provided or rendered by the Department. Actuarial FECA Liability and NOAA Corps Employee Retirement Benefits Liabilities of $569 million is composed of the actuarial present value of projected benefits for



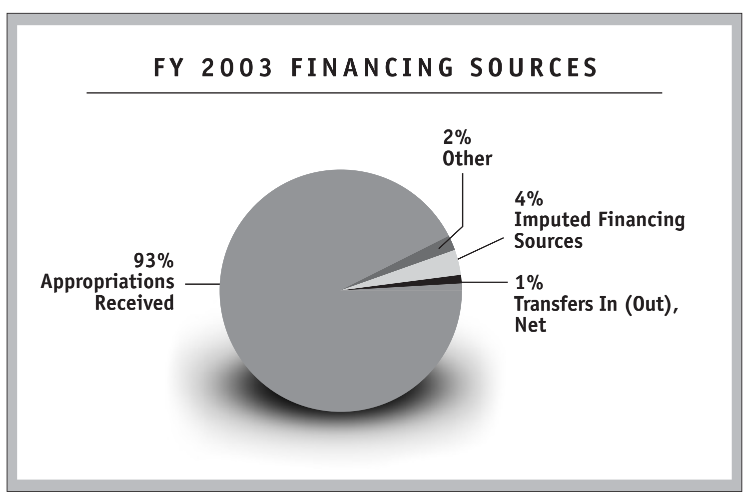
the NOAA Corps Retirement System ($327 million) and the NOAA Corps Post-Retirement Health Benefits ($42 million), and Actuarial FECA Liability ($200 million), which represents the liability for future workers' compensation benefits. Accrued Grants of $393 million, which relate to a diverse array of financial assistance programs and projects, include Economic Development Administration (EDA) accrued grants of $266 million for their economic development and assistance funding to state and local governments. Other liabilities of $356 million includes Liabilities for Loan Guarantees of $51 million, Environmental and Disposal Liabilities of $90 million, and Resources Payable to Treasury of $75 million. Accounts Payable of $368 million consists primarily of amounts owed for goods, services, or capitalized assets received, progress on contract performance by others, and other expenses due. Accrued Payroll and Annual Leave include salaries and wages earned by employees, but not disbursed as of September 30. Debt to Treasury of $212 million results from monies borrowed primarily for the Fisheries Finance Fund direct loans and the Emergency Steel Loan Guarantee Program.

Trends in Liabilities



Total Liabilities increased $53 million or 2 percent, from $3.13 billion at September 30, 2002 to $3.19 billion at September 30, 2003. Liabilities for Loan Guarantees increased $29 million or 132 percent, from $22 million to $51 million, due to the initial subsidy cost for a guaranteed loan of the Emergency Steel Loan Guarantee Program. Accrued Grants increased $42 million or 12 percent, from $350 million to $392 million, which is caused primarily by an increase in EDA grants. Unearned Revenue increased $61 million or 7 percent, from $938 million to $999 million, primarily due to increased unearned revenue from patent and trademark application and user fees that are pending action. Debt to Treasury decreased $51 million or 19 percent, from $263 million to $212 million, in large part due to a repayment of $50 million by the Emergency Steel Loan Guarantee Program. Environmental and Disposal Liabilities decreased $31 million or 26 percent, from $121 million to $90 million, due to a decrease in the Pribilof Island cleanup liability.

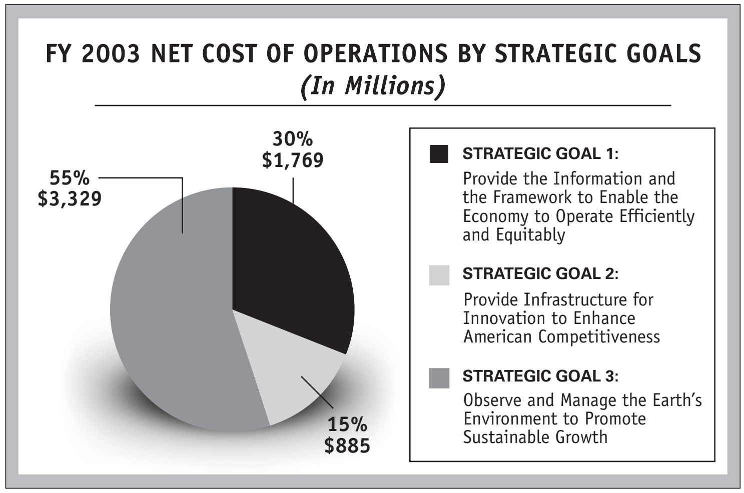
Trends in Financing Sources

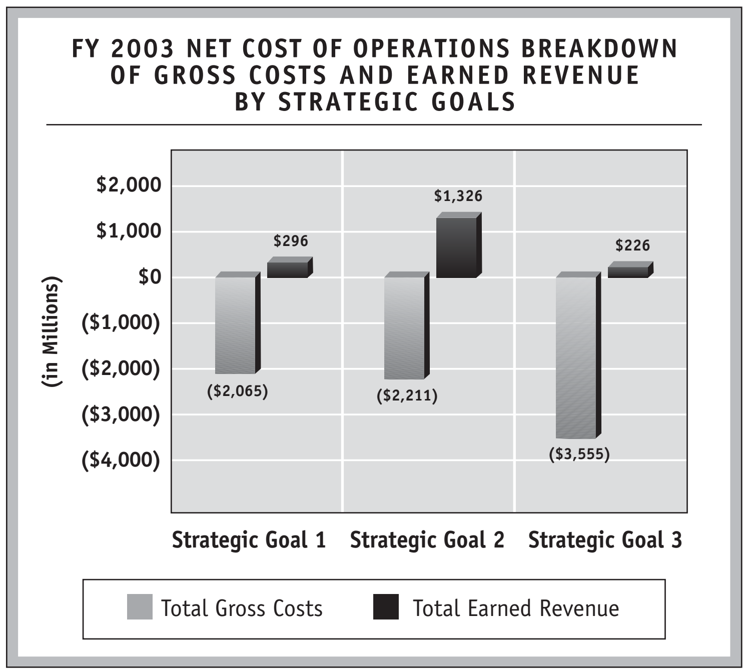


Most of the Department's Financing Sources are obtained from Appropriations Received. Total Financing Sources for FY 2003, shown on the Consolidated Statement of Changes in Net Position, increased $459 million or 8 percent, from $5.79 billion for the year ended September 30, 2002 to 6.25 billion for the year ended September 30, 2003. The increase was largely due to an increase in Appropriations Received of $279 million or 5 percent, from $5.51 billion to $5.79 billion.

Net Cost of Operations by Strategic Goal

In FY 2003, Net Cost of Operations amounted to $5.98 billion, which consists of Gross Costs of $7.8 billion less Earned Revenue of $1.85 billion. Strategic Goal 1 includes Gross Costs of $196 million related to the decennial census for the year 2000. Strategic Goal 2 includes Net Cost of Operations of $69 million (Gross Costs of $1.07 billion less Earned Revenue of $1.00 billion) for USPTO's patents program. Strategic Goal 2 also includes Net Cost of Operations of $466 million (Gross Costs of $541 million less Earned Revenue of $75 million) for NIST's Measurement and Standard's Laboratories. These laboratories are the stewards of the U.S.'s measurement infrastructure, and provide measurement methods, reference materials, test procedures, instrument calibrations, fundamental data, and standards that comprise essential tools for research, production, and buyer-seller transactions. Strategic Goal 3 includes Net Cost of Operations of $1.41 billion (Gross Costs of $1.48 billion less Earned Revenue of $69 million) related to NOAA's goal to advance short-term warning forecasts, which includes improving tornado, winter storm, and flash flood warning lead time and accuracy, and improving hurricane track and precipitation forecasts.





Limitations of the Financial Statements

These financial statements have been prepared to report the financial position and results of operations of the Department of Commerce, pursuant to the requirements of 31 U.S.C. 3515(b). While the statements have been prepared from the books and records of the Department in accordance with the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

These statements should be read with the realization that they are for a component of the U.S. government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides the resources to do so.