Analysis of Financial Statements

Interior received, for the 12th consecutive year, an unqualified audit opinion on its financial statements. The statements were audited by the independent accounting firm of KPMG LLP. Preparing the financial statements is part of Interior's goal to improve financial management and to provide accurate and reliable information that is useful for assessing financial performance and allocating resources. Interior management is responsible for the integrity and objectivity of the financial information presented in the financial statements.

The financial statements and financial data presented in this Report have been prepared from Interior's accounting records in conformity with generally accepted accounting principles. Generally Accepted Accounting Principles (GAAP) for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board.

Information provided in the financial statements, the opinion presented as a result of the independent audit, and other disclosures and information provided in this Report provide assurance to the public that the information is accurate, reliable, and useful for decisionmaking.

Interior expects that balances of line items will fluctuate in the normal course of business. Therefore, while Interior notes these variances, any fluctuations of 10 percent or less are considered normal and will not be detailed specifically in this analysis.

Overview of Financial Position

Assets

At the end of FY 2008, Interior's assets totaled $70,679 million. This is an increase of $3,695 million or 6 percent over the previous year's assets, which totaled $66,984 million. Interior's assets reflected in the Balance Sheet are summarized below.

Interior's assets are primarily composed of the Fund Balance with Treasury and General Property, Plant, and Equipment (PP&E). The Fund Balance with Treasury is money that Interior is authorized to use to pay liabilities resulting from operational activity and consists of funds received from direct appropriations, transfers, offsetting receipts, recoveries, and funds held in budget clearing accounts.

General PP&E are primarily composed of land, structures, and facilities which are used for general operations, power, wildlife enhancement, and recreation. Most of Interior's structures and facilities are composed of dams, power, and irrigation facilities managed by BOR. The remainder consists of buildings and facilities used in Interior's operations (e.g., visitor centers, fish hatcheries, and IA schools).

Liabilities

In FY 2008, Interior's liabilities totaled $11,828 million. This is an increase of $849 million or 7 percent from the previous year's liabilities of $10,979 million. Interior's liabilities reflected in the Balance Sheet are summarized below.

Interior's liabilities are primarily composed of Accounts Payable, Debt, Federal Employee and Veteran Benefits, and Other Liabilities. Other Liabilities are primarily composed of Liability for Capital Transfer to the General Fund of the Treasury, Contingent, Advances, Deferred Revenues, and Custodial Liabilities.

Federal agencies, by law, cannot disburse money unless Congress has appropriated funds. Funded liabilities are expected to be paid from funds currently available to the Department. Interior's unfunded liabilities consist primarily of Environmental and Legal Contingent Liabilities and unfunded employee compensation costs, which include Federal Employment and Compensation Act and annual leave amounts. These liabilities will be paid from funds made available to Interior in future years. The associated expense is recognized in the period in which the liaiblity is established, regardless of budgetary funding considerations.

In FY 2008, Interior had several liability line items with variances meeting the threshold for analysis. Accounts Payable showed a change of approximately $196 million (14 percent). The largest portion of this variance is a $141 million increase in the Office of the Secretary's fund for payments in lieu of taxes. The appropriation and payables due in FY 2009 were received early and booked into FY 2008, causing an increase in accounts payable.

Total debt decreased for the year by $143 million (16 percent) due to repayments to the Bureau of the Public Debt by IA, BOR, and BLM. The bulk of the change was due to the BLM annual repayment of $120 million of Helium related debt.

The decrease of $5 million in Loan Guarantee liability is attributable to IA's subsidy reestimate in the Loan Guarantee program.

Condensed Assets

(dollars in thousands)	FY 2008	FY 2007
Fund Balance with Treasury	$ 37,932,964	$ 34,776,671
Investments, Net	7,546,611	7,485,899
General Property, Plant, and Equipment, Net	18,306,908	17,930,798
Accounts and Interest Receivable, Net	3,284,138	3,368,896
Other Assets	3,608,646	3,421,256
Total Assets	$ 70,679,267	$ 66,983,520

Condensed Liabilities

(dollars in thousands)	FY 2008	FY 2007
Accounts Payable	$ 1,571,833	$ 1,375,832
Debt	715,109	858,007
Loan Guarantee Liability	36,180	41,434
Federal Employee and Veteran Benefits	1,383,223	1,363,633
Environmental and Disposal Liabilities	155,548	147,514
Other Liabilities	7,965,752	7,192,494
Total Liabilities	$ 11,827,645	$ 10,978,914

Net Cost

(dollars in thousands)	FY 2008	FY 2007
Resource Protection	$ 3,780,366	$ 3,465,136
Resource Use	4,031,249	2,144,299
Recreation	2,632,479	2,455,348
Serving Communities	4,777,813	4,637,182
Reimbursable Activity and Other	1,081,461	936,721
Net Cost of Operations	$ 16,303,368	$ 13,638,686

The Other Liabilities line item, as presented in this summary statement, is a composite of all remaining liabilities in the Department not chosen for emphasis here. The large change (increase) of $773 million (11 percent) is, therefore, a result of many smaller changes to liability accounts in the fund. The most significant component causing the change is an increase of $1.1 billion in the MMS's Other Liabilities. MMS Contingent Liabilities increased by $766 million due to a change in the estimate of possible loss. MMS Custodial Liabilities also increased by $334 million due to the increase of onshore oil and gas prices, which yeilded increases in royalties reported and due.

Net Position

Interior's Net Position at the end of 2008, disclosed in the Balance Sheet and the Statement of Changes in Net Position, was $58,852 million, an increase of about $2,847 million or 5 percent from the previous year.

Interior's Net Position consists of the sum of Unexpended Appropriations of $4,544 million and Cumulative Results of Operations of $54,307 million.

Results of Operations

Interior's net cost of operations for FY 2008 was $16,246 million. This is a increase of $2,607 million or 19 percent from the previous year's net cost of $13,639 million. Interior's net cost of operations as reflected in the Statement of Net Cost is summarized above.

Most costs incurred by Interior are directly related to providing services to the public. The Consolidated Statement of Net Cost is divided into the following five major program segments: Resource Protection; Resource Use; Recreation; Serving Communities; and Reimbursable Activity and Other.

In FY 2008, Net Cost of Operations increased by such a large margin due to Resource Use activity in the MMS. An unusually large increase in the price of oil and gas resulted in high dollars of royalties that were then payable to the states. Also, in FY 2008, MMS contingent lability was increased to reflect a $1.1 billion estimate of loss.

Revenue

During FY 2008, Interior earned approximately $2,134 million in revenue from the public and approximately $2,196 million in revenue from other Federal entities, for a total of $4,330 million. This is a decrease of about $241 million from September 30, 2007. In FY 2007, approximately $2,035 million was earned in revenue from the public and approximately $2,536 million was earned in revenue from other Federal entities, for a total of $4,571 million.

Interior classifies revenue as exchange or non-exhange revenue. Exchange revenues are those that derive from transactions in which both the Government and the other party receive value, including park and wildlife refuge entrance fees, map sales, and other products and services that are directly related to Departmental operations. Revenue collected from other Federal agencies consists of reimbursable activities such as construction, engineering, and other technical services. Most of the revenue received from Federal agencies is received from Interior Franchise Fund and National Business Center operations that provide shared administrative services. Interior also collects mineral lease revenues on behalf of the Federal government. These are presented in the Statement of Custodial Activity rather than the Statement of Net Cost.

Interior also collects various non-exchange revenues. Examples of non-exchange revenue are taxes, fines, and penalties that the Federal government collects as a result of its sovereign powers rather than as a result of providing goods or services for a fee.

Budgetary Resources

Interior receives most of its funding from general government funds administered by the U.S. Treasury and appropriated for Interior's use by the Congress. These resources consist of the balance at the beginning of the year, appropriations received during the year, and spending authority from offsetting collections, as well as other sources of budgetary resources. Other resources include Special and Trust Funds, such as Conservation Funds (the Land and Water Conservation Fund, Historic Preservation Fund, and the Environmental Improvement and Restoration Fund), the Reclamation Fund, and the Aquatic Resources Trust Fund. These funds are administered in accordance with applicable laws and regulations.

The Statement of Budgetary Resources provides information on how budgetary resources and nonbudgetary credit program financing were made available to Interior for the year and their status at fiscal year-end. Obligations of $21,920 million and $20,963 million were incurred as of September 30, 2008, and September 30, 2007, respectively on total budgetary resources in FY 2008 of $29,044 million, and in FY 2007, of $26,799.

Custodial Activity

In accordance with Federal accounting standards, receipts from mineral leasing revenue are presented in Interior's Statement of Custodial Activity, since the collections are considered to be revenue of the Federal Government as a whole rather than Interior. Mineral leasing revenue was $25,371 million and $10,984 million as of September 30, 2008, and September 30, 2007, respectively, and includes Outer Continental Shelf and onshore oil, gas, and mineral sales and royalties. The increase of $14,387 million is due to the large increase in the price of oil and gas in FY 2008.

Interior collects a portion of revenue as royalties in kind for transfer to the Strategic Petroleum Reserve. The current Strategic Petroleum Reserve initiative began in July 2007 and was discontinued in June 2008. The current estimated value of this initiative is $1,600 million which was reported as custodial revenue.

Stewardship Investments

In FY 2008, Interior implemented SFFAS 29. Stewardship assets are now detailed in a Note to the Financial Statements.

Stewardship investments represent expenses charged to current operations that are expected to benefit the Nation over time. Interior's Stewardship Investments include research and development programs, investments in human capital, and investments in nonfederal physical property.

Stewardship Iinvestments are summarized in the following table.

STEWARDSHIP INVESTMENTS (IN MILLIONS)

	FY 2008	FY 2007	Change	% Change
Non-Federal Physical Property	$667	$576	$+91	+14%
Research and Development	885	867	+18	+2%
Human Capital	$589	$565	$+24	+4%

Interior's reported values for Property, Plant, and Equipment exclude stewardship assets because they are considered priceless and do not have an identifiable value. Therefore, monetary amounts cannot be assigned. An in-depth discussion of these assets is presented in the Notes to the Financial Statements Section and the Required Supplementary Information section of the Performance and Accountability Report.

Limitations of Financial Statements

Management prepares the accompanying financial statements to report the financial position and results of operations for the Department of the Interior pursuant to the requirements of Chapter 31 of the U.S.C. Section 3515(b).

While these statements have been prepared from the records of the Department in accordance with GAAP and formats prescribed in OMB Circular No. A-136, "*Financial Reporting Requirements*," these statements are in addition to the financial reports used to monitor and control the budgetary resources that are prepared from the same records. These statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity.