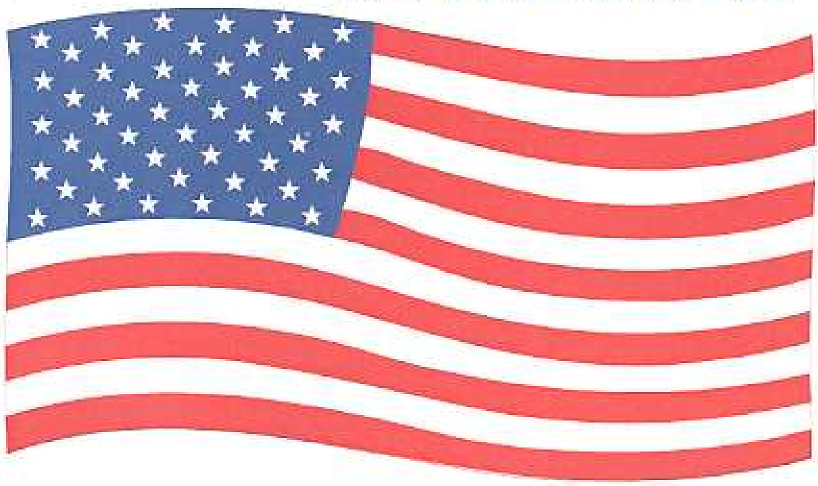
2001

FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT



Contents

Supplemental Information (Unaudited)

Appendix

List of Social Insurance Charts

A MESSAGE FROM THE SECRETARY OF THE TREASURY

I am pleased to present the fiscal year 2001 *Financial Report of the United States Government.* The Report includes audited financial statements that cover the executive branch, as well as parts of the legislative and judicial branches of the U.S. Government. In five years, we have made considerable progress but still have much to accomplish in order to reach our goal of timely and useful financial reporting.

Accrual based financial reporting is critical to gaining a comprehensive understanding of the U.S. Government's operations. For fiscal year 2001, our results were an accrual-based deficit of $515 billion in contrast to a $127 billion budget surplus reported last fall. The primary difference between the accrual deficit and the budget surplus is the recognition of expanded military retiree health benefit costs provided by the National Defense Authorization Act, which was signed into law on October 30, 2000, and other actuarial expenses. In fact, these expenses caused the government's future obligations to its military and civilian retirees to exceed the federal debt held by the public. As with other future obligations of the federal government, only accrual-based financial reporting provides this information in context to the public.

The drive to produce financial reports that better disclose our activities to the Congress and the public continues. This year, for the first time, we are presenting two years of data to facilitate comparative analysis. In addition, we have added two new financial statements. The Reconciliation of Net Operating Revenue/(Cost) to the Budget Surplus (unaudited) explains the differences between the accrual and budget results. The Disposition of the Budget Surplus (unaudited) explains how the budgetary surplus was utilized.

We have made progress toward the three goals I laid out last year.

- For fiscal year 2004, agencies' financial statements are due 45 days after the fiscal year-end with the consolidated Financial Report due by December 15th. This accelerated timing will finally allow adequate time to have the financial statements considered in the budget process. The ultimate goal of the financial information in this report is for it to be used by decision-makers to improve the management and programs of the Federal government.
- After completing our review, we are implementing a new process, developed in consultation with the Office of Management and Budget and the General Accounting Office, for preparing future financial statements which will enhance their integrity.
- The Treasury Department continues to develop a governmentwide accounting system that will greatly improve the agencies' access to data, reduce redundant data reporting, and eliminate reconciliations between the cash amounts shown on agency and Treasury books.

I believe that the American people deserve the highest standards of accountability and professionalism from their Government and I will not rest until we achieve them.

Paul H. O'Neill

Paul H. O'Neill

This page is intentionally blank.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

We are pleased to present the consolidated *Financial Report of the United States Government (Financial Report)*. This year, for the first time, we are presenting two years of financial information to facilitate comparative analysis, and have added two new financial statements to help explain the differences between the accrual-based deficit and the budget surplus, and to explain how the budgetary surplus was used. Although we continue to receive a disclaimer of opinion from our auditors, in this our 5th year of preparing financial statements, we are making progress in our quest to report the financial activities of the U.S. Government timely, reliably, and in a format useful to the readers. For the second consecutive year, all 24 of the largest departments and agencies completed their financial statements on time and 18 received an unqualified or clean opinion. We are committed and will continue to work to improve financial management, modernize the Government's financial management systems, and strengthen financial reporting. Our objective is to provide useful, timely reports of financial information to the American public and the world. To that end, we have set the objective of issuing this report for fiscal 2004 operations by December 15, 2004.

The accompanying *Financial Report* is required by 31 U.S.C. § 331(e)(1) to be submitted to Congress by March 31, and consists of Management's Discussion and Analysis (MD&A), Statements of Net Cost, Statements of Operations and Changes in Net Position, Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited), Dispositions of the Budget Surplus (Unaudited), Balance Sheets, Stewardship Information, Notes to the Financial Statements, and Supplemental Information. Each section is preceded by a description of its contents.

Executive Summary

With the arrival of the new Administration last year, a major new initiative, "The President's Management Agenda," was launched. The President's Management Agenda is a strategy for improving the management and performance of the Federal Government. Government likes to begin programs, but beginnings are not the measure of success. What matters in the end is achievement of results. The President's Management Agenda focuses on 14 areas of improvement where the Federal Government can begin to deliver on its promises. The 14 targeted areas address the most apparent deficiencies where the opportunity to improve performance is the greatest.

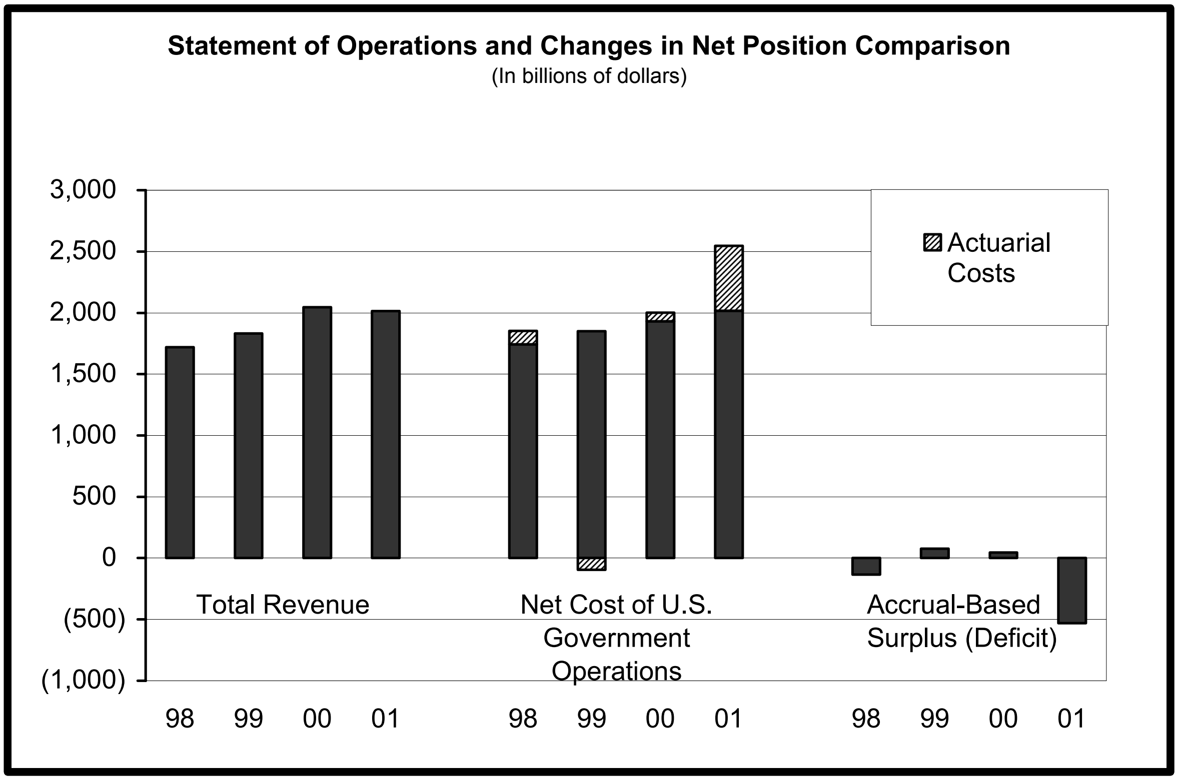
Five of the 14 targeted areas are Governmentwide initiatives, including:

- Strategic Management of Human Capital.
- Competitive Sourcing.
- Improved Financial Performance.
- Expanded Electronic Government.
- Budget and Performance Integration.

The remaining nine initiatives are program specific, including:

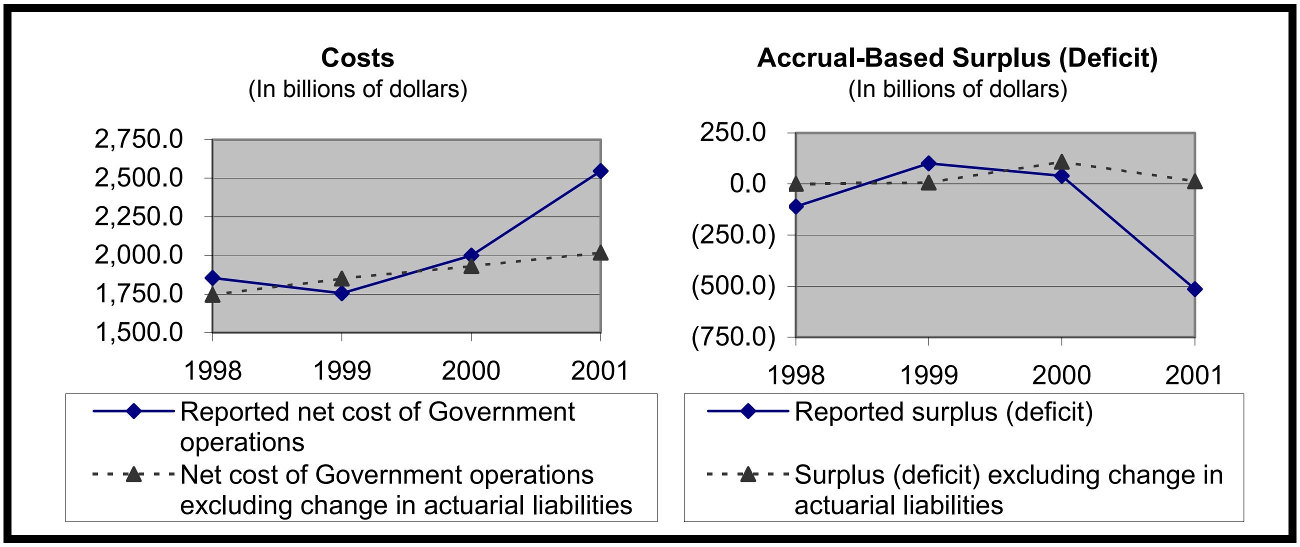
- Faith-Based and Community Initiative.
- Privatization of Military Housing.
- Better Research and Development Investment Criteria.
- Elimination of Fraud and Error in Student Aid Programs and Deficiencies in Financial Management.
- Housing and Urban Development Management and Performance.
- Broadened Health Insurance Coverage through State Initiatives.
- A "Right-Sized" Overseas Presence.
- Reform of Food Aid Programs.
- Coordination of Veterans Affairs and Defense Programs and Systems.

The President's Management Agenda is a starting point for management reform. It reflects the Administration's commitment to achieve concrete and measurable results in the near term. It focuses on remedies to problems generally agreed to be serious and commits to implement them fully. The goals of this agenda are being undertaken in advance of, not instead of, other needed management improvements. Additional goals will be undertaken as tangible improvements are made in this initial set of initiatives.



The above chart shows that the financial results moved to a deficit in fiscal 2001. In this report, the term surplus/deficit refers to accrual-based amounts, and references to budget-based surplus/deficit amounts will always be preceded by the term budget. The deficit was $514.8 billion in fiscal 2001, as compared to a surplus of $39.6 billion for fiscal 2000. Despite the deficit, the Government paid down an additional $90.1 billion in debt held by the public. As a result of sustained debt reductions and a significant increase in Federal employee and veteran benefits payable, this year debt held by the public is no longer the largest liability on the Government's balance sheets. As is also evident in the chart, revenues failed to increase in fiscal 2001; in fact they decreased modestly by $31.1 billion from fiscal 2000 due to lower corporate income tax receipts reflecting the impact of a weakening economy and the one-time shift of $23 billion of the September estimated corporate tax payments into October. The Net Cost of U.S. Government Operations increased significantly in fiscal 2001 by $545.4 billion when compared to fiscal 2000 costs. The largest reason for the increase is due to the effect of a new law that increased the military retirement health benefits liability by $293.0 billion. Under this legislation, TRICARE benefits are extended to military retirees and their beneficiaries who are eligible for Medicare, and a fund is established to pay these benefits (a new intragovernmental investment fund similar to those for other Federal pension programs). This resulted in civilian and military retirement and post-retirement health care becoming the largest liability of the Federal Government.

Over the past 4 fiscal years, significant adjustments to the actuarial liabilities have had large effects on the Governmentwide net cost of operations and the surplus (deficit). The following charts show that absent these adjustments, costs are trending upward at a 3 to 4 percent rate and the net cost has varied within a range from break-even to a $115 billion surplus. Actuarial liabilities include Federal employee and veteran benefits payable and are discussed in Note 11 of the Notes to the Financial Statements. In fiscal 1998 through 2001, there have been significant changes in the veterans compensation and burial benefits liability in the following amounts: increase of $109.8 billion in fiscal 1998, decrease of $94.9 billion in fiscal 1999, increase of $69.4 billion in fiscal 2000, and increase of $139.3 billion in fiscal 2001. These significant changes are a result of changes in interest rate and other actuarial assumptions. In addition to the $293.0 billion increase in the military retirement health benefits liability (as mentioned in the previous paragraph), there has also been a $91.3 billion increase in other actuarial assumption changes relating to the military retirement health benefits.



Mission and Organizational Structure

No other entity in the world compares in size, scope, and complexity to the U.S. Government. Its budgeted outlays were $1.9 trillion in 2001. A civilian Federal workforce of 2.7 million individuals plus 1.4 million Department of Defense active duty military personnel serves a diverse Nation of more than 278 million Americans.

To fulfill its constitutional mandates, the U.S. Government undertakes a wide variety of programs to:

- Maintain strong, ready, and modern military forces.
- Provide homeland security.
- Provide critical international leadership.
- Contribute to energy security.
- Protect the environment.
- Boost agricultural productivity.
- Facilitate commerce and support housing.
- Support the transportation system.
- Help economically distressed urban and rural communities.
- Assist States and localities in providing essential education and training.
- Promote health care.
- Foster income security.
- Provide benefits and services to veterans.
- Administer justice.

The form of Government that exists in the United States is a constitutional representative democracy. The following organization chart illustrates the constitutionally mandated separation of powers into the three main branches of Government. It also illustrates the breadth and complexity of the executive branch.

THE GOVERNMENT OF THE UNITED STATES

THE CONSTITUTION

LEGISLATIVE BRANCH

THE CONGRESS

SENATE HOUSE

Architect of the Capital
United States Botanic Garden
General Accounting Office
Government Printing Office
Library of Congress
Congressional Budget Office

EXECUTIVE BRANCH

THE PRESIDENT
THE VICE PRESIDENT
Executive Office of the President

White House Office
Office of the Vice President
Council of Economic Advisers
Council on Environmental Quality
National Security Council
Office of Administration
Office of Homeland Security (*)
Office of Management and Budget
Office of National Drug Control Policy
Office of Policy Development
Office of Science and Technology Policy
Office of the U.S. Trade Representative
(*) Per Executive Order # 13228, signed 10/08/01

JUDICIAL BRANCH

THE SUPREME COURT OF THE UNITED STATES

United States Courts of Appeals
United States District Courts
Territorial Courts
United States Court of International Trade
United States Court of Federal Claims
United States Court of Appeals for the Armed Forces
United States Tax Court
United States Court of Appeals for Veterans Claims
Administrative Office of the United States Courts
Federal Judicial Center
United States Sentencing Commission

DEPARTMENT OF AGRICULTURE
DEPARTMENT OF COMMERCE
DEPARTMENT OF DEFENSE
DEPARTMENT OF EDUCATION
DEPARTMENT OF ENERGY
DEPARTMENT OF HEALTH AND HUMAN SERVICES
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
DEPARTMENT OF THE INTERIOR
DEPARTMENT OF JUSTICE
DEPARTMENT OF LABOR
DEPARTMENT OF STATE
DEPARTMENT OF TRANSPORTATION
DEPARTMENT OF THE TREASURY
DEPARTMENT OF VETERANS AFFAIRS

INDEPENDENT ESTABLISHMENTS AND GOVERNMENT CORPORATIONS

African Development Foundation
Central Intelligence Agency
Commodity Futures Trading Commission
Consumer Product Safety Commission
Corporation for National and Community Service
Defense Nuclear Facilities Safety Board
Environmental Protection Agency
Equal Employment Opportunity Commission
Export-Import Bank of the U.S.
Farm Credit Administration
Federal Communications Commission
Federal Deposit Insurance Corporation
Federal Election Commission
Federal Emergency Management Agency
Federal Housing Finance Board
Federal Labor Relations Authority
Federal Maritime Commission
Federal Mediation and Conciliation Service
Federal Mine Safety and Health Review Commission
Federal Reserve System
Federal Retirement Thrift Investment Board
Federal Trade Commission
General Services Administration
Inter-American Foundation
Merit Systems Protection Board
National Aeronautics and Space Administration
National Archives and Records Administration
National Capital Planning Commission
National Credit Union Administration
National Foundation on the Arts and the Humanities
National Labor Relations Board
National Mediation Board
National Railroad Passenger Corporation (Amtrak)
National Science Foundation
National Transportation Safety Board
Nuclear Regulatory Commission
Occupational Safety and Health Review Commission
Office of Government Ethics
Office of Personnel Management
Office of Special Counsel
Overseas Private Investment Corporation
Peace Corps
Pension Benefit Guaranty Corporation
Postal Rate Commission
Railroad Retirement Board
Securities and Exchange Commission
Selective Service System
Small Business Administration
Social Security Administration
Tennessee Valley Authority
Trade and Development Agency
U.S. Agency for International Development
U.S. Commission on Civil Rights
U.S. International Trade Commission
U.S. Postal Service

Source: *U.S. Government Manual 2001-2002*

The United States is impressive in its position as one of the world powers. The following table illustrates several interesting facts about the United States, as compared with other countries.

Item of Interest	Amount for the United States	Information as of	Country Rank	Comments
Land area	9,158,960 square kilometers		4th	Russia, China, and Canada are larger
Population	278.1 million	July 2001 est.	3rd	China and India are greater
Gross domestic product	$9.963 trillion	2000 est.	1st	China was second with $4.5 trillion
Gross domestic product–per capita	$36,200	2000 est.	2nd	Luxembourg was first with $36,400
Electricity–production	3.678 trillion kilowatt-hour	1999	1st	China was second with 1.173 trillion
Military expenditures–percent of gross domestic product	3.20 percent	Fiscal 1999 est.	41st	North Korea was first with an estimate of 25-33 percent
SOURCE: Central Intelligence Agency's *The World Factbook 2001*				

Financial Results

The deficit as shown in these financial statements for fiscal 2001 is $514.8 billion, as compared to a budget surplus of $127.0 billion. The primary components of the difference between the budget and accrual numbers are increases in the liability for military health liabilities of $388.6 billion, and an increase in the liability for veterans disability of $115.2 billion. For a detailed reconciliation showing the differences, see the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited) statement in the Financial Statements section.

In fiscal 2000, the financial statements showed a surplus of $39.6 billion, as compared to a budget surplus of $236.9 billion.

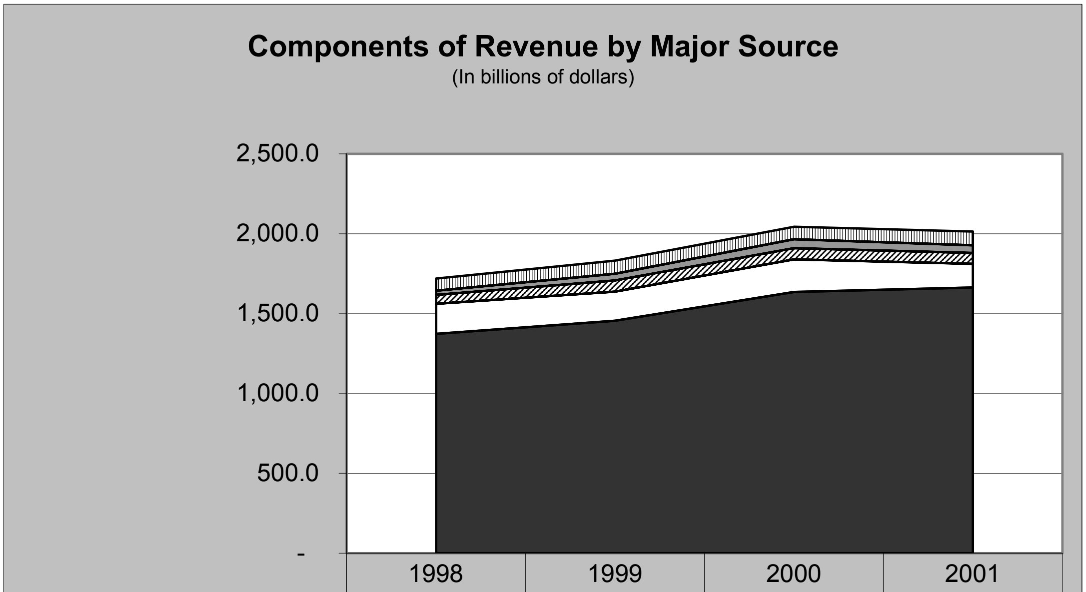
Revenue and Cost Summary

Revenue

Government revenue comes from two sources: nonexchange transactions and exchange transactions. Nonexchange revenues arise primarily from exercise of the Government's power to demand payments from the public (e.g., taxes, duties, fines, and penalties). Nonexchange revenue is the U.S. Government's primary source of revenue and totaled $2,001.4 billion in fiscal 2001, as compared to $2,040.0 billion in fiscal 2000. More than 98 percent of this total came from tax receipts, with the remainder coming from customs duties and other miscellaneous receipts. The reduction in nonexchange revenue was due to lower corporate income tax receipts reflecting the impact of a weakening economy and the one-time shift of September estimated corporate tax payments into October. The shift amounted to roughly $23 billion moving into October. The Government also issued $35.2 billion in tax rebate checks to individual taxpayers during the fiscal year.

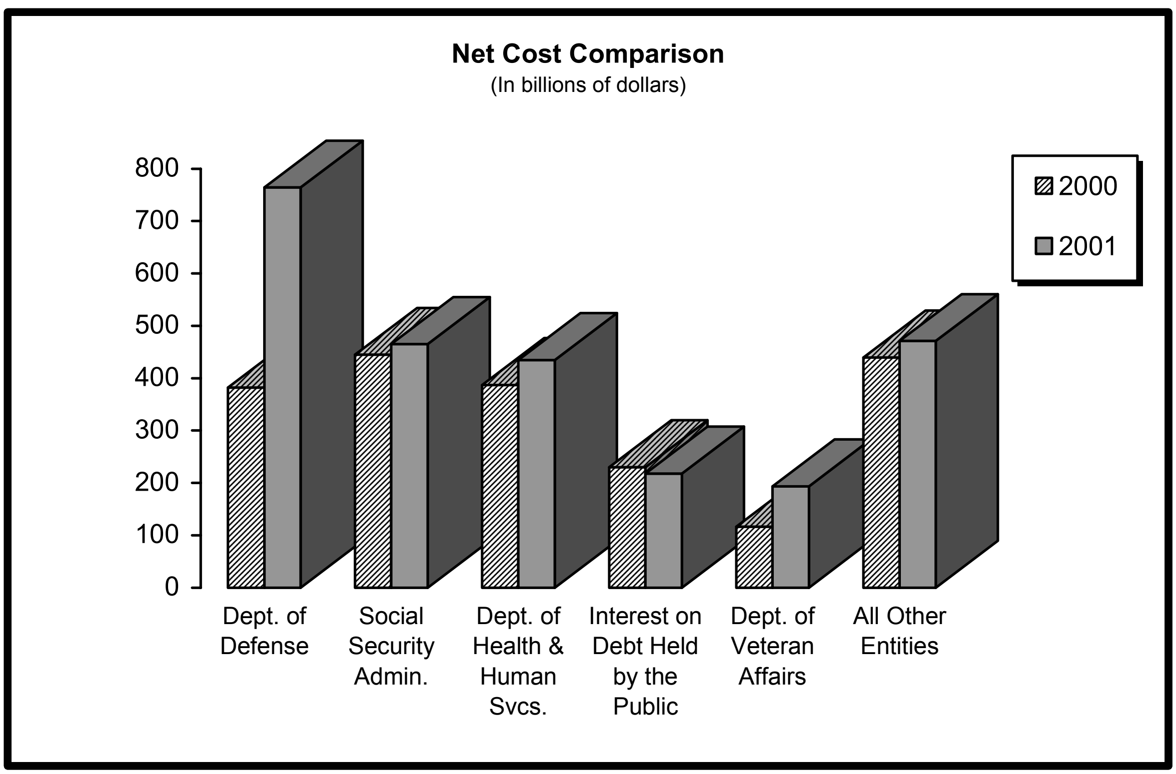
Exchange revenues arise when a Government entity provides goods and services to the public for a price. Another term for exchange revenue is earned revenue. Examples of exchange revenues are the mailing and postage revenue for the U.S. Postal Service and Medicare Part B premiums collected by the Department of Health and Human Services. During fiscal 2001, the U.S. Government earned $172.3 billion in exchange revenue, as compared with $161.7 billion in fiscal 2000. Of these revenues, $160.0 billion is offset against the gross cost of the related agencies' programs to arrive at the agencies' net cost, as compared with $156.9 billion for fiscal 2000. Also included is $12.3 billion ($4.8 billion in fiscal 2000) that was earned by the U.S. Government but not offset against the cost of any program (e.g., royalties on the Outer Continental Shelf Lands).

The following chart shows the components of revenue by major source.



	1998	1999	2000	2001
All others	75.5	82.2	79.7	86.0
Other taxes and receipts	26.6	42.0	56.3	48.9
Excise taxes	57.6	70.5	69.3	67.3
Corporation income taxes	186.3	182.2	204.3	147.9
Individual income tax and tax withholdings	1,374.2	1,456.0	1,635.2	1,663.6

Cost



The above chart compares significant elements of net cost by fiscal year. As noted earlier, the significant increase in Department of Defense cost reflected the effect of the extension of medical benefits to retired personnel in the amount of $293.0 billion, plus another $91.3 billion in other actuarial assumption changes. The second largest change was the increase in the Department of Veterans Affairs in the amount of $76.9 billion for actuarial assumption changes for veterans compensation and burial benefits. The net costs of the Department of Health and Human Services increased by $47.3 billion due primarily to a $22 billion increase in Medicare and a $12 billion increase in Medicaid.

The net cost of U.S. Government operations was $2,545.8 billion for fiscal 2001, as compared to $2,000.4 billion for fiscal 2000. Net cost represents the gross cost of operations less related earned revenues. The Statement of Net Cost reflects the cost incurred to carry out the national priorities identified by the President and the Congress, and are shown by major agency or entity.

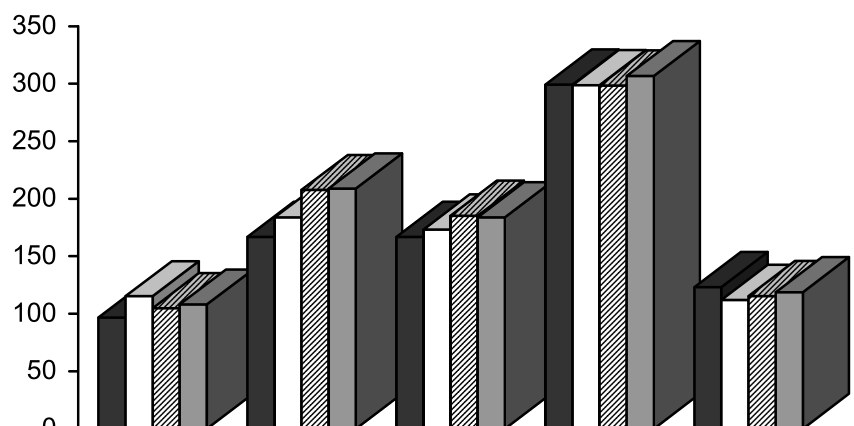
Asset and Liability Summary

Assets

The assets of the U.S. Government are the tangible resources available to pay liabilities or to satisfy future service needs. The accompanying chart depicts a four-year comparison of the major categories of reported assets as of September 30, for fiscal years 1998 through 2001.

Assets - Key Items Comparison

(In billions of dollars)



	Cash and Other Monetary Assets	Loans Receivable	Inventories and Related Property	Property, Plant and Equipment	All Other Assets
1998	96.8	166.8	166.8	299.3	123.1
1999	115.2	183.7	173.3	298.8	112.0
2000	104.9	207.6	185.2	298.5	115.3
2001	108.0	208.9	183.8	306.7	118.7

As can be seen from the above chart, in fiscal 2001, assets remained relatively constant from fiscal 2000. However, the assets presented on the Balance Sheets are not a comprehensive list of Federal resources. Natural resources, stewardship land (national parks, forests, and grazing lands), national defense assets, heritage assets, and the Government's sovereign powers to tax, regulate commerce, and set monetary policy are examples of resources that are not included in the assets reported on the Balance Sheets. Detailed information about national defense assets, stewardship land, and heritage assets can be found in the Stewardship Information section. Another example, the U.S. Government's most important financial resource, its ability to tax and regulate commerce, cannot be quantified and is not reflected.

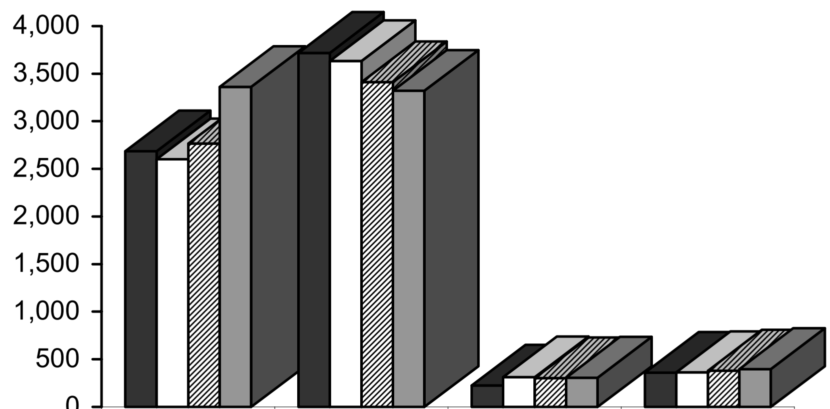
Liabilities

At the end of fiscal 2001, the U.S. Government reported liabilities of $7,384.9 billion, as compared with $6,856.9 billion for September 30, 2000. The largest component of these liabilities ($3,360.8 billion) is represented by pension, disability, and health care costs for Federal civilian and military employees as well as for veterans, as compared to $2,764.7 billion for September 30, 2000. During fiscal 2001, the increase of $406.8 billion for military employee benefits was due mostly to reflecting the effect of the National Defense Authorization Act and other actuarial assumption changes. The increase of $139.3 billion for veterans compensation and burial benefits was the result of changes in interest rate and other actuarial assumptions. See Note 11 in the Notes to the Financial Statements for a more detailed explanation for these changes. During fiscal 2000, changes in actuarial and interest rate assumptions were the primary factors contributing to the increase of $69.4 billion for veterans compensation and burial benefits payable. The next largest liability ($3,319.8 billion) relates to Federal debt securities held by the public, as compared to $3,409.9 billion for September 30, 2000, and reflects a $90.1 billion pay down in the debt held by the public. Another liability is related to environmental cleanup costs associated with environmental damage/contamination. As of September 30, 2001, the recognized cost of cleaning up environmental damage/contamination across Government programs was estimated to be $306.8 billion, as compared to $301.2 billion for September 30, 2000.

The accompanying chart presents a four-year comparison of the major components of liabilities reported on the Balance Sheets as of September 30, for fiscal years 1998 through 2001.

Liabilities - Key Items Comparison

(In billions of dollars)



	Federal Employee and Veteran Benefits Payable	Federal Debt Securities Held by the Public	Environmental and Disposal Liabilities	All Other Liabilities
1998	2,685.1	3,717.7	224.5	359.9
1999	2,600.7	3,631.6	313.2	363.7
2000	2,764.7	3,409.9	301.2	381.1
2001	3,360.8	3,319.8	306.8	397.5

As clearly shown above, the Federal debt securities held by the public have decreased significantly over the past 3 years. The reduction in fiscal 2001 was $90.1 billion, as compared with a $222.7 billion reduction for fiscal 2000. The chart also shows the significant increases in Federal employee and veteran benefits payable for the past two fiscal years, as explained above. Significant future commitments that are not reported as liabilities are the Social Security and Medicare programs. Under existing accounting standards, the future costs of these programs are contained in the Stewardship Section and discussed under Future Commitments. We believe that one of the most important issues facing the newly reconstituted Federal Accounting Standards Advisory Board (FASAB) will be the treatment of social insurance.

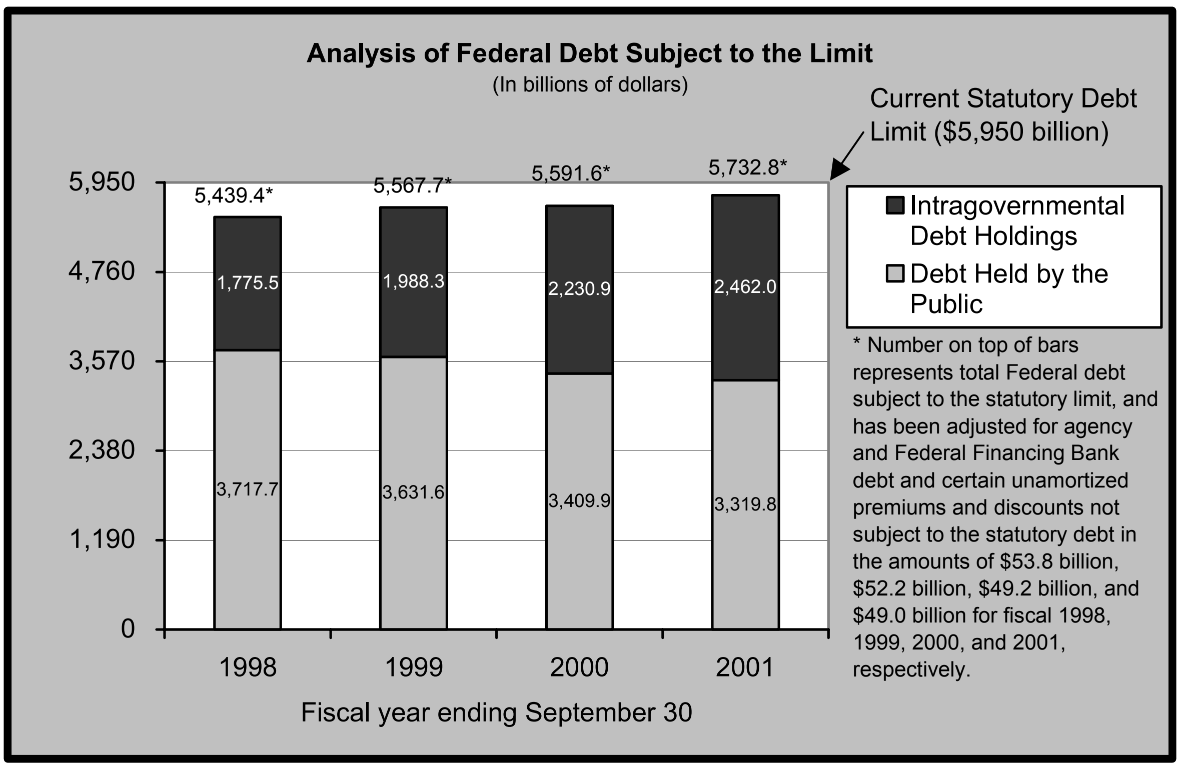
Federal Debt and Budget Surpluses

Although we have had 4 consecutive years of budget surpluses, it is important to understand the composition of budget surpluses, and the relationship that these excess funds have had on reducing or changing the composition of the Federal debt. There are two components of Federal debt: debt held by the public and intragovernmental debt holdings.

Debt held by the public includes all Federal debt held by individuals, corporations, State or local governments, Federal Reserve Banks, foreign Governments, and other entities outside of the U.S. Government. The types of securities held by the public include, but are not limited to, Treasury Bills, Treasury Notes, Treasury Bonds, U.S. Savings Bonds, State and Local Government Series securities, Foreign Series securities, and Domestic Series securities.

Intragovernmental debt holdings generally include nonmarketable securities held by various elements of the Government itself. The laws establishing Government trust funds (such as the Social Security and Medicare Trust Funds) generally require the balances to be invested in these special securities. Although intragovernmental debt holdings are used in the calculation of the Federal debt subject to the statutory debt limit, intragovernmental transactions are eliminated in the consolidation process of preparing this *Financial Report* since they are claims of one part of the Government against another part. However, they are important to an understanding of total debt because, as the intragovernmental securities are redeemed, other sources of funds will be used to fund the redemptions.

The following chart presents a 4-year comparison of the components of Federal debt subject to the statutory debt limit.



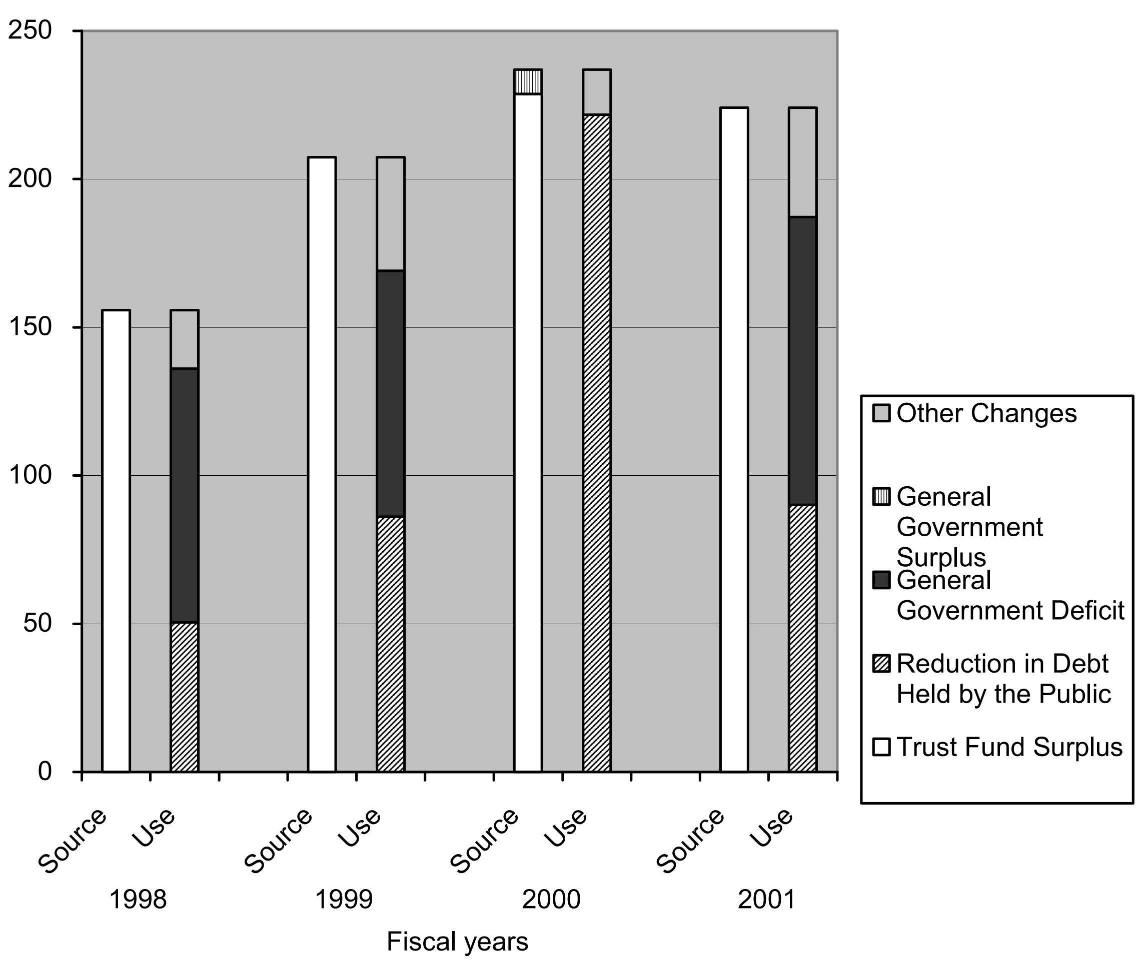
As can be seen from the above chart, debt held by the public has been reduced by almost $400 billion since 1998; however, total debt subject to the limit has risen by $293 billion over the same period. This is because the intragovernmental debt holdings have risen faster than the debt held by the public has been repaid. Treasury has requested that the statutory debt ceiling be raised to $6,700 billion. This was in response to the Administration's projection that the current debt ceiling, $5,950 billion, was expected to be reached by the end of March 2002. As of March 20, 2002, total Federal debt subject to the limit was $5,938 billion ($12 billion from the limit).

Treasury's need to borrow from the public has declined over the past several years. Debt maturing has exceeded the Government's cash surplus; therefore, new securities have continued to be issued. To adjust the Government's borrowing program, Treasury has taken a number of actions, including initiating a buyback program in fiscal 2000, which is a competitive redemption process by which Treasury accepts offers to redeem certain marketable Treasury securities (debt held by the public) prior to their maturity date. During fiscal 2001, a total of 23 buybacks occurred involving the redemption of $33.8 billion par amount of marketable Treasury securities at a total cost of $44.4 billion. This compares to a total of 13 buybacks involving the redemption of $21.3 billion par amount of marketable Treasury securities at a total cost of $26.7 billion for fiscal 2000.

Federal Government operations are composed of two parts: trust funds, which receive their funding from dedicated collections, and general Government, which is funded from general revenues. Many of the larger trust funds finance social insurance programs (such as Social Security and Medicare) and Federal military and civilian retirement programs. Other major trust funds finance highway and transit construction and airport development. The following chart illustrates a 4-year comparison of the budget surpluses or deficits of these two parts of Government and how the budget surpluses were used.

4-Year Comparison of Sources and Uses of the Budget Surplus

(In billions of dollars)



Source: United States Government Annual Report

Trust fund surpluses (the white area in the chart) are invested in Treasury securities. The cash invested in Treasury securities is mainly used for two purposes: to reduce the debt held by the public (the diagonally striped area) and to fund the general Government deficits (the black area). Other changes (the gray area) consist primarily of outlays under various loan programs. Therefore, in most years, only a portion of the budget surplus could be used to reduce the debt held by the public.

The budget surpluses, based primarily on a cash basis, are due almost entirely to the trust fund surpluses. General Government operations experienced budget deficits for fiscal 1998, 1999, and 2001, but had a budget surplus for fiscal 2000.

Future Commitments

September 11: A terrible wrong and a call to action

Americans will never forget the murderous events of September 11, 2001. The threat of mass-destruction terrorism is now a reality of life—a condition to which not just America, but the entire world, must adjust. New challenges of monumental scale and complexity confront our Nation as we wage war against terrorism and take measures to ensure the defense of our homeland. The war against terrorism will be waged on the financial, diplomatic, and intelligence fronts as much as on the battlefield. We must combat terrorism both abroad and at home, protect our people, and preserve our constitutional freedoms. Our military must be strengthened still further so it can act still more effectively to find, pursue, and destroy our enemies. We have priorities at home as well—restoring health to our economy above all.

This new war will be costly. Some of those costs will not show up directly on the Government's books. Terrorism has already inflicted considerable losses on the private economy, and now entrepreneurs and employers will have to shoulder the expense of still-tighter security at points of vulnerability. Government at all levels—Federal, State, and local—will have new bills to pay. Achieving our homeland security objectives will require vast sums of money, strenuous labor, and many years. Clearly, future decisions about how to use our Nation's vast resources will be influenced heavily by the compelling need to protect all Americans and our way of life.

Social Security and Medicare: Fiscal Challenges Looming on the Horizon

For 66 years, Social Security has provided retirement security for tens of millions of Americans. Like Social Security, Medicare also represents a promise the Nation has made to its citizens. As demographics change and costs increase, ensuring these two programs are strengthened for tomorrow's retirees and beneficiaries poses a long-term fiscal challenge. Reform is significantly easier to implement if done far in advance, so individuals and families have time to adjust their personal plans and changes can be phased in slowly over time.

Both Social Security's and Medicare's spending paths are unsustainable in the long run, because they are driven largely by demographic trends. First, longer life spans mean more benefit payments. Advances in health and well-being have led to significant increases in the average life span in the 21st century. The net result is that people spend a growing proportion of their lives in retirement and face the inevitable medical needs brought about by aging. While longer life spans are clearly desirable, they also mean additional years of Social Security and Medicare payments, and a dramatic long-term increase in Government obligations.

Compounding this problem is the long-term decline in the ratio of workers to beneficiaries. This means there will be fewer workers available to support each beneficiary once the baby boom generation starts to retire.

Under current legislation and using intermediate assumptions, the Trustees estimated in their 2002 report that by 2017, cash disbursements for the Social Security programs will exceed cash receipts from taxes, and by 2041, the combined trust fund assets, primarily investments in special Treasury securities, will be exhausted. By 2041, dedicated tax revenues would be sufficient to pay only approximately 73 percent of the benefits due. Additional information about the Social Security program, including updated information from the 2002 Trustees' Report, can be found in the Stewardship Information section of this *Financial Report*.

While demographic trends will change spending for both Social Security and Medicare dramatically, the problem is likely to be more pronounced in Medicare due to the expected increases in health care costs per beneficiary. Medicare per capita spending is projected to vastly outpace the consumer price index for the next 25 years.

While it is true that the Hospital Insurance Trust Fund is projected to have a surplus over the next 10 years, it is misleading to focus so much attention on only one of the program's two trust funds, which represents only 60 percent of total Medicare spending. A full assessment of Medicare's finances reveals spending exceeds the total of tax receipts and premiums dedicated to Medicare today, and the "financing gap" is projected to widen dramatically. This annual gap was $59 billion in fiscal 2000, growing to an estimated $216 billion (using constant dollars) in 2020, and an estimated $368 billion in 2030. Additional information on the Medicare program can also be found in the Stewardship Information section of this *Financial Report*.

Economic and Budgetary Results

The economy slowed as fiscal 2001 began, and tipped into recession in March 2001, according to the National Bureau of Economic Research, the official arbiter of cyclical turning points. Despite the downturn, the fundamental strengths of the U.S. economy remained intact, and productivity continued to grow even as output declined. Fiscal and monetary policies were put in place to stimulate the faltering economy and promote long-term growth. Those factors probably contributed to keeping the recession mild, and a recovery appeared to take hold in the first quarter of fiscal 2002. Budget results for fiscal 2001 were still very favorable, as the Federal Government recorded the second largest budget surplus in history and paid down $90.1 billion in debt. However, the effects of the weak economy and the spending requirements following the September 11 terrorists' attacks are expected to lead to a budget deficit in fiscal 2002.

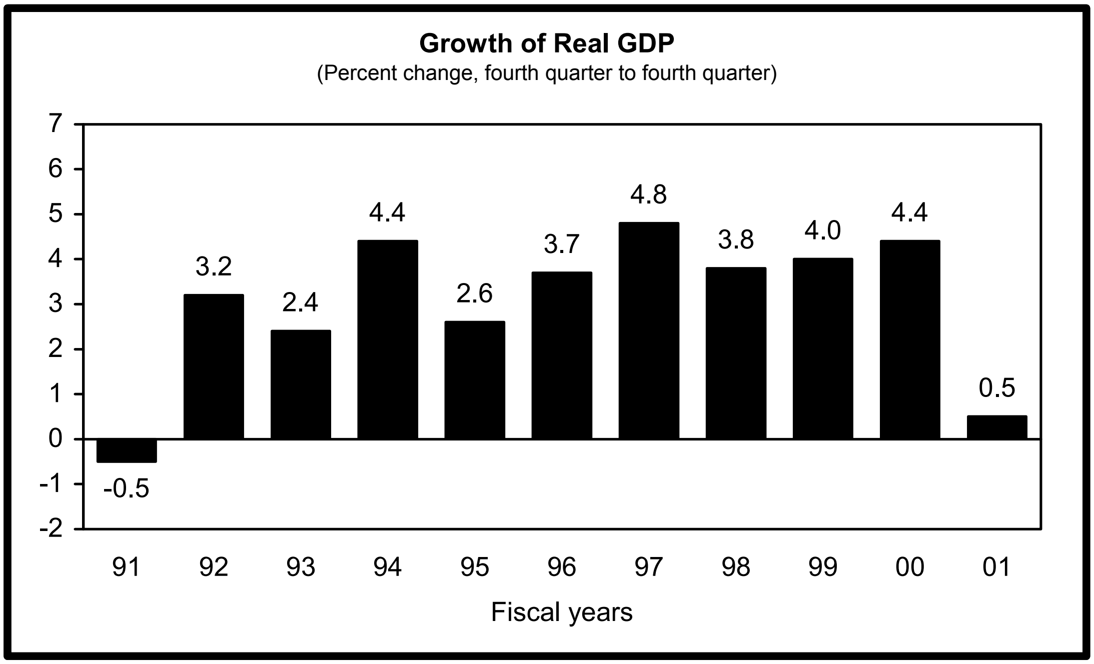
Budget Results

The U.S. fiscal situation continued to be favorable in fiscal 2001, although the deteriorating economy held the budget surplus below the level that had been projected in the April *Budget* and in the August *Mid-Session Review*. The unified budget was in surplus by $127.0 billion in the fiscal year, the second largest budget surplus on record. Receipts decreased by $34.1 billion or 1.7 percent, and eased to 19.6 percent in relation to gross domestic product (GDP) from a near-record 20.8 percent in the previous fiscal year. Outlays grew by $75 billion or 4.2 percent and represented an 18.4 percent share of GDP, unchanged from the previous year. The growth in outlays was less than the 5.1 percent increase registered in fiscal 2000.

The budget surplus allowed Federal debt held by the public to be paid down again in fiscal 2001 for the fourth year in a row. Debt was reduced by $90.1 billion, the second largest reduction in history. In relation to GDP, publicly held debt fell to 32.7 percent, down from 35.0 percent in the previous year and the lowest in nearly 20 years.

The Economy in Fiscal 2001

The economic slowdown that began in the final July-to-September quarter of fiscal 2000 turned into a recession during fiscal 2001, aggravated by the after-effects of the tragic September 11 events. Growth in real GDP diminished from a 1.9 percent annual rate increase in the first quarter of the fiscal year to a 1.3 percent decline by the fourth quarter. Over the four quarters of the fiscal year, GDP rose just 0.5 percent, the smallest gain since the last recession year in 1991 and much lower than the average 4.3 percent increase over the prior 4 fiscal years (see chart below).



Slower consumer spending and a contraction in demand for investment goods after extremely rapid growth in prior years were some of the factors contributing to the recession. Employment conditions weakened in the face of slack demand. Just 184,000 payroll jobs were added to the economy in fiscal 2001, compared to 2.6 million in the previous fiscal year. Much of the deterioration was in the manufacturing sector, where almost 1 million payroll jobs were lost over the fiscal year. The unemployment rate rose from 3.9 percent at the start of the year to 5.0 percent by the final month.

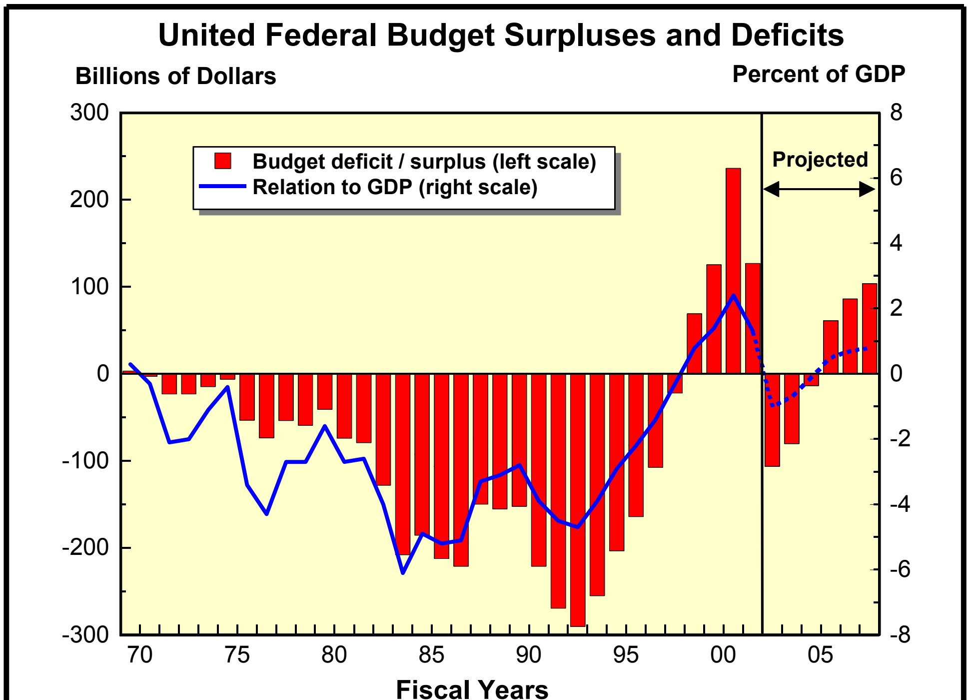
On the positive side, falling energy prices kept inflation well contained in fiscal 2001. Petroleum prices dropped nearly 25 percent over the fiscal year, holding the increase in the consumer price index to 2.6 percent, compared with 3.5 percent during the previous fiscal year when energy prices increased. Excluding energy and food, growth in "core" consumer prices was also moderate in fiscal 2001.

Fiscal policy measures were put in place last year that helped to offset some of the effects of the weakening economy. The Economic Growth and Tax Relief Reconciliation Act of June 2001 reduced individual income taxes by $1.35 trillion over 11 years, and some provisions were made retroactive to January 2001 in order to get rebate checks back to taxpayers quickly to help invigorate the economy. Additional spending initiatives in the wake of the September 11 attacks provided further assistance to get the economy back on track.

The Federal Reserve took timely action through the fiscal year in order to promote stronger economic growth, lowering short-term interest rates eight times. The targeted Federal funds rate (the rate that banks and other financial institutions charge one another for overnight loans) was reduced from 6.5 percent at the start of the fiscal year to 3.0 percent by fiscal year-end. The Federal Reserve lowered the discount rate (the rate the Federal Reserve charges banks for short-term funds) from 6.0 percent in the first month of the fiscal year to 2.5 percent by the end of the fiscal year. The Federal Reserve continued to cut interest rates in the first quarter of fiscal 2002 to levels not seen since the early 1960s, but decided in the second quarter to leave rates unchanged.

Budget Projections

The economic recession in fiscal 2001, tax cuts and other stimulus measures to promote growth, and the spending requirements of the war on terrorism and homeland security are expected to lead to a unified budget deficit of $106 billion for fiscal 2002. Budget deficits are projected to narrow in the following two years, however, and the budget is expected to return to surplus by fiscal 2005. Over the 10 years from fiscal 2002 to fiscal 2011, the cumulative budget surplus under the current services baseline (i.e., with no changes to tax and spending laws already enacted) is expected to total $2.2 trillion.



Source: OMB, FY-2003 Budget

Significant Performance Accomplishments

Progress on Audited Financial Statements

Results of FY 2001
Agency Financial Audits

Improvement
Clean: DOJ, DOT
Qualified: Education
Disclaimers: USDA, USAID

Unchanged
Clean: Commerce, Energy, HHS, HUD, DOI, DOL, State, Treasury, VA, EPA, GSA, NRC, NSF, OPM, SBA, SSA
Disclaimer: DOD

Deterioration
Qualified: FEMA
Disclaimer: NASA

For the second time, in fiscal 2001, all of the 24 largest agencies met the deadline for completing and submitting their audited financial statements. Eighteen agencies received clean opinions and five showed marked improvement. The Departments of Justice and Transportation moved from qualified to clean opinions. Other areas of improvement included the Federal Aviation Administration, an item on GAO's High-Risk list, which has cured many of its financial management weaknesses. At the Department of Agriculture, three of five major agency components received clean opinions on their financial statements. For the first time, all Agency for International Development statements were audited, and three of five received qualified opinions. The Department of Defense, which again received a disclaimer, has launched a major initiative to improve its business and financial processes and systems. Two agencies, the National Aeronautics and Space Administration and the Federal Emergency Management Agency, deteriorated from last year, but have initiated ambitious programs to reclaim their clean opinions. In addition, the Administration has taken a number of steps to improve the accuracy and timeliness of Government financial information, beginning in fiscal 2002. These include accelerating the delivery of audited statements; the implementation of quarterly versus yearly reporting; displaying financial information from the current year with the previous year's; improving financial management systems; and requiring the integration of accountability reports with performance reports produced under the Government Performance and Results Act.

Expanding the question from "How much?" to "How well?"

The Federal Government has taken a significant step on the long road to a results-oriented Government by beginning to use performance measures to develop policies, to make budget decisions, and to improve everyday program management. The goal is to create a Government that promotes the outcomes that Americans want—such as better education for our children, the freedom to travel safely, and protection of our health—and does this in a cost-effective and efficient way. Achieving better program performance—particularly better performance for each dollar spent—is a high priority of this Administration. Congressional interest, reflected in the Government Performance and Results Act of 1993, set agencies to identifying performance goals, planning to achieve them, and reporting on results. What has been missing is systematic use of these measures to make decisions. In particular, performance measures are not directly linked to the budget—and yet it is the budget that drives policy development, allocates resources, and has undeveloped potential to support better management.

To address this disconnect, the President's Budget for 2003 seeks to inaugurate an era of accountability in the conduct of the Nation's public business. It takes the first step toward reporting to taxpayers on the relative effectiveness of the thousands of purposes on which their money is spent. It commences the overdue process of seriously linking program performance to future spending levels. It asks not merely "How much?"; it endeavors to explain "How well?"

To develop the President's Budget for 2003, OMB and agencies collected evaluations, studies, and performance documentation of multiple sorts from all sources to assess which programs were effectively improving desired outcomes. Within the Executive Branch, preliminary assessments of these materials were discussed, and agencies were urged to improve program performance and to improve evidence of effectiveness and linkage with program cost. Below are some of the results of this performance-oriented process of policy development and budget allocation. The examples illuminate ways in which policy makers and program managers can help Government better serve its citizens.

- **Agriculture**: Numerous Government and private studies show that the Special Supplemental Nutrition Program for Women, Infants and Children (WIC) is one of the Nation's most successful and cost-effective early intervention programs. The program saves lives and improves the health of women, infants and children who are nutritionally at risk. The Budget reflects this demonstrated success by fully funding the program in 2003 to enable all eligible persons who seek services to receive them. The request is sufficient to provide 7.8 million persons with supplemental foods, nutrition education, and preventive health care each month in 2003.
- **Commerce:** The National Weather Service, an effective program, got an increase in funding and specific targets to increase hurricane warning lead time from 24 hours in 2002 to 28 hours in 2005, increase tornado lead time from 10 minutes today to 22 minutes by 2015, improve aviation forecasting accuracy by 13 percentage points by 2007, and improve temperature and river forecasts for a pilot region by 2004. Lives will be saved by more timely evacuations; airline and energy industry costs and energy use will be reduced. The National Hurricane Center achieved its most recent critical success when it correctly forecast that the brunt of dangerous Hurricane Michelle would just miss the Florida peninsula. Accurate forecasts of hurricane tracks translate to smaller areas required to prepare for evacuation, saving approximately $1 million per mile for coastal residents, businesses, and local governments.

- **Health and Human Services:** Funding for the National Institutes of Health, the world's leading research institution for biomedical and behavioral research, will increase to double its 1998 level. NIH conducts research in its own laboratories, but the vast majority of its funding supports researchers in universities, hospitals, and research institutes around the country through peer-reviewed grants. NIH has supported great advances in the detection and treatment of disease, and its recent work on the human genome, cancer, and many other diseases gives promise of accelerating breakthroughs.
- **Labor/Training:** This Budget begins a wide-ranging reform of Federal investments in training and employment. In 2002, there are at least 48 overlapping training and employment programs scattered around 10 agencies. For several programs that are duplicative or have a history of poor performance, funding is reduced or terminated, reducing the number of programs from 48 to 28. For the many other training programs where performance measures are inadequate or not comparable, a multi-year effort will begin to assess relative effectiveness, shift resources to programs that prove effective, and eliminate ineffective or duplicative programs.
- **National Science Foundation:** The NSF, a leader among Federal agencies that fund basic research, will get more funding and programs transferred from other agencies. Of NSF's grants, 94 percent are competitive, based on merit review. Each year, one-third of NSF's research and educational programs are evaluated for integrity, efficiency, and quality of results, so that all programs are reviewed in a three-year period. Of the dozen 2001 Nobel Prize winners in the sciences, NSF supported eight for the research that won them the award. NSF quickly redirects resources to areas of emerging opportunity, and invests one quarter of its research budget in areas where major breakthroughs are likely.
- **Social Security Administration:** SSA has targeted an increase in retirement claims processed within 14 days from 84 percent in 2001 to 87 percent by 2003, an increase in customer initiated services available electronically from 21 percent to 40 percent, and an increase in callers access to SSA's 800 number within five minutes of their first attempt from 92 percent in 2001 to 94 percent in 2003.

Looking to the Future: The President's Management Agenda

The President has called for a Government that focuses on priorities and executes them well. Securing the homeland, waging war on terrorism abroad and revitalizing the economy are the most important priorities, but even they will not be addressed by simply devoting money to them.

The assumption that more Government spending gets more results is not always true but is seldom tested. It is potentially wrong for two reasons. First, the program may not actually achieve the results everyone expects. Second, it ignores the fact that improvements in the management of programs can result in greater results for less money by realizing the same productivity gains found in the private sector. By focusing on performance, we can achieve the desired results at limited additional cost or, in some cases, a reduction in spending. We can all get more for less.

The President has ordered the pursuit of five Governmentwide initiatives that together will help Government achieve better results. These initiatives include strategic management of human capital, competitive sourcing, improved financial performance, expanded electronic Government, and the integration of budget with performance. Released in August 2001, the President's Management Agenda was designed to "address the most apparent deficiencies where the opportunity to improve performance is the greatest." The President's vision is guided by the principles that Government should be results-oriented, not process oriented; citizen-centered, not bureaucracy-centered; and market-based, promoting competition rather than stifling innovation.

The President's Agenda is a coordinated and coherent strategy to reform Federal management and improve program performance. It tackles long-neglected management problems and offers specific solutions to fix them. Five Governmentwide initiatives apply to every department and agency. Together they form a strategy to achieve breakthrough, not simply marginal, improvements in program performance.

The Human Capital Initiative aims to attract and retain talented and imaginative people into the Federal Government in order to improve the service provided to our citizens. The Competitive Sourcing Initiative exposes parts of the Government to competition so that they may better focus on what customers want while controlling cost. The Financial Management Initiative improves how the Government manages its money – reducing, for instance, the billions in erroneous payments the Government makes every year. The E-Gov Initiative harnesses the power of the Internet to make the Government more productive. The Budget Performance/Integration Initiative starts the process of linking results with resource decisions – the underlying information needed to hold Government accountable.

Keeping Score

Good intentions and good beginnings are not the measure of success. What matters in the end is completion: performance and results. Not just making promises, but making good on promises.

In order to ensure accountability for performance and results, the Administration is using an Executive Branch Management Scorecard. The Administration will use this scorecard to track how well departments and agencies are executing the management initiatives, and where they stand at a given point in time against the overall standards for success.

The scorecard employs a simple “traffic light” grading system common today in well-run businesses: green for success, yellow for mixed results, and red for unsatisfactory. Scores are based on five standards for success defined by the President’s Management Council and discussed with experts throughout Government and academe, including individual Fellows from the National Academy of Public Administration.

> The National Science Foundation (NSF) received the only “green” score. NSF did so in financial management because it has embraced advanced information technologies and operates in a paperless environment. Its grant workload more than doubled from $2.1 billion in 1990 to $4.4 billion in 2000, yet the number of employees actually decreased.

The initial scorecard shows a lot of poor scores. This was to be expected since, as the President indicated when selecting the Management Agenda items, the areas are “targeted to address the most apparent deficiencies where the opportunity to improve performance is the greatest.” The marks that really matter will be those that record improvement, or lack of it, from these starting points.

Executive Branch Management Scorecard 2001 Baseline Evaluation					
	Human Capital	Competitive Sourcing	Financial Management	E-Gov	Budget/ Performance Integration
AGRICULTURE	R	R	R	Y	R
COMMERCE	R	R	R	Y	R
DEFENSE	R	R	R	R	R
EDUCATION	R	R	R	R	R
ENERGY	R	R	R	R	R
EPA	R	R	R	Y	Y
HHS	R	R	R	R	R
HUD	R	R	R	R	R
INTERIOR	R	R	R	R	R
JUSTICE	R	R	R	R	R
LABOR	Y	R	R	Y	R
STATE	R	R	R	R	R
TRANSPORTATION	R	R	R	R	Y
TREASURY	R	R	R	R	R
VA	R	R	R	R	R
AID	R	R	R	R	R
CORPS OF ENGINEERS	R	R	R	R	R
FEMA	R	R	R	R	R
GSA	R	R	Y	R	R
NASA	R	R	Y*	R	R
NSF	R	R	G	Y	R
OMB	R	R	R	R	R
OPM	Y	R	R	Y	R
SBA	R	R	Y	Y	Y
SMITHSONIAN	R	R	R	Y	R
SSA	Y	R	Y	Y	R

*As a result of the disclaimer on NASA's fiscal 2001 financial statements, NASA will now move to red.

LEGEND: R = Red Y = Yellow G = Green

Over time, the scores should improve as departments and agencies correct the problems. The Administration will update this report twice a year and issue a mid-year report during the summer. This Administration will not indulge in grade inflation; we will hold ourselves responsible and report honestly when progress is too slow.

Systems, Controls, and Legal Compliance

Systems

The Federal Government faces agency-specific and Governmentwide challenges in modernizing its financial management systems. Many financial management systems need upgrading or replacing before they can provide information to support efforts to achieve the President's goal of a citizen-centered, results-oriented, and market-based Government.

The success of financial systems modernization efforts is dependent, in part, on standardized financial management across the Government. Towards this end, OMB, Treasury, and the Joint Financial Management Improvement Program (JFMIP) have been working together to better clarify and achieve consistency of standards for financial systems. In addition, OMB and Treasury are working together to develop a definitive set of information requirements that will ensure Governmentwide reporting requirements can be met through routine processes and system functions.

Controls

Numerous internal controls exist over Federal assets. Instances where these controls are not functioning as planned are described in the individual agency financial reports. Those deficiencies that materially affect the Governmentwide financial statements are described in the accompanying report prepared by GAO. Each agency is responsible for developing and implementing a corrective action plan. In addition, OMB and the Department of the Treasury will continue to work with Federal agencies to resolve crosscutting issues. In some cases, however, the resolution of these issues will require reengineering of current processes, which is currently being addressed.

Federal agencies have identified approximately $19 billion in annual erroneous benefit and assistance payments in just 13 Federal programs. The Administration has launched an initiative to determine and track error rates in additional programs, and to implement strategies and controls to bring the rates down in programs covering over $1.2 trillion in annual expenditures.

Legal Compliance

Federal agencies are required to comply with a wide range of laws and regulations, including appropriations, employment, health and safety, and others. Responsibility for compliance primarily rests with agency management; compliance is addressed as part of agency financial statement audits. Agency auditors tested for compliance with selected laws and regulations related to financial reporting. These auditors found no instances of material noncompliance that affected the Governmentwide financial statements. There were, however, instances that were material to an individual agency, and these were reported in the individual agencies' financial statement audit reports.

Basis of Accounting and Reporting Entity

Accounting Standards

The accompanying financial statements were prepared based on Generally Accepted Accounting Principles (GAAP) standards developed by FASAB, except as noted in our auditor's report.

GAAP for the Federal Government is tailored to the U.S. Government's unique characteristics and special needs. For example, the stewardship section of this report contains important information about diverse subjects such as land set aside for the use and enjoyment of present and future generations, heritage assets, weapon systems, and social insurance programs such as Social Security.

In fiscal 2001, two new financial statements were added at the Governmentwide reporting level: Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited) and Dispositions of the Budget Surplus (Unaudited). Both statements are unaudited for fiscal 2001, since they are not required by FASAB standards. FASAB is in the process of finalizing the format and content of these statements.

In addition, the presentation of the Statements of Net Cost has changed for fiscal 2001. The Statements now reflect the cost incurred to carry out the national priorities identified by the President and the Congress, and are shown by major agency or entity. Previously, net cost was shown by function.

Also, the Statement of Federal Financial Accounting Standard (SFFAS) No. 10 (Accounting for Internal Use Software) was implemented in fiscal 2001 at the Governmentwide reporting level. Under the provisions of this standard, internal use software is classified as "general property, plant and equipment" as defined in SFFAS No. 6 (Accounting for Property, Plant and Equipment).

Accrual Basis

GAAP requires that these financial statements be prepared using the accrual basis of accounting, but permits the use of modified cash accounting for taxes and duties. Under the accrual basis, transactions are reported when the events giving rise to the transactions occur, rather than when cash is received or paid (cash basis). Therefore, expenses are recorded when incurred, exchange revenue is recorded when earned, and taxes and duties (the majority of nonexchange revenue) are recorded on a modified cash basis of accounting (generally when received). In contrast, Federal budgetary reporting is generally on the cash basis in accordance with accepted budget concepts.

The most significant difference between these two bases involves the timing of recognition and measurement of revenues and costs. For example, GAAP requires recognition of liabilities for costs related to environmental cleanup when the events requiring such costs occur and, among other things, the Government has acknowledged responsibility for the event. By contrast, current budget concepts recognize such costs later, at the time payment is made for the cleanup. The differences are reflected in the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited), which can be found in the Financial Statements section of this Financial Report.

Coverage

These financial statements cover the executive branch, as well as parts of the legislative and judicial branches of the U.S. Government. A list of the significant entities included in these financial statements is in the Appendix. Information from the legislative and judicial branches is limited because those entities are not required by law to submit comprehensive financial statement information to Treasury. Due to its private ownership and independence, the Federal Reserve System is excluded. In addition, Government-sponsored but privately owned enterprises (such as Federal Home Loan Banks and the Federal National Mortgage Association) also are excluded.

Additional Information

Additional details about the information contained in these financial statements can be found in the financial statements of the individual agencies listed in the Appendix. In addition, related U.S. Government publications such as the *Budget of the United States Government*, the *Treasury Bulletin*, the *Monthly Treasury Statement of Receipts and Outlays of the United States Government*, the *Monthly Statement of the Public Debt of the United States*, the *Economic Report of the President*, and the Trustees' reports for the Social Security and Medicare programs may be of interest.

This page is intentionally blank.

GAO
Accountability * Integrity * Reliability

Comptroller General
of the United States

United States General Accounting Office
Washington, DC 20548

March 29, 2002

The President
The President of the Senate
The Speaker of the House of Representatives

Our report on the U.S. government's consolidated financial statements for fiscal years 2001 and 2000 is enclosed. As in the 4 previous fiscal years, we were unable to express an opinion on the consolidated financial statements because of certain material weaknesses in internal control and accounting and reporting issues. These conditions prevented us from being able to provide the Congress and American citizens an opinion as to whether the consolidated financial statements are fairly stated in conformity with U.S. generally accepted accounting principles.

Until the problems discussed in our report are adequately addressed, they will continue to (1) hamper the government's ability to accurately report a significant portion of its assets, liabilities, and costs, (2) affect the government's ability to accurately measure the full cost and financial performance of certain programs and effectively manage related operations, and (3) significantly impair the government's ability to adequately safeguard certain significant assets and properly record various transactions.

Progress is being made in addressing impediments to an opinion on the U.S. government's consolidated financial statements. For example, in fiscal year 2001, the Department of Agriculture and certain other key agencies made significant improvements in estimating the cost of the government's lending programs and the net loan amounts expected to be collected, which had contributed to our disclaimer of opinion in prior years. However, many of the pervasive and generally long-standing material weaknesses we have reported for the past 4 years remain to be fully resolved. The underlying causes of these issues are significant financial management systems weaknesses, problems with fundamental recordkeeping and financial reporting, incomplete documentation, and weak internal control.

Across government, there are financial management improvement initiatives that, if effectively implemented, will improve the quality of the government's financial management and reporting. For fiscal year 2001, 18 of the 24 Chief Financial Officers (CFO) Act agencies were able to attain unqualified audit opinions on their financial statements, which is the same number of agencies as last year and up from 6 agencies for fiscal year 1996. Also, the Office of Management and Budget (OMB) reported that, for the second consecutive year, all 24 CFO Act agencies met the statutory reporting deadline. Further, two agencies that did not receive unqualified opinions from their auditor last year were able to do so this year, including the Department of Justice, which received an unqualified opinion for the first time. However, two other agencies were unable to sustain the unqualified opinions received from their auditor last year. Additionally, reports of inspectors general and their contract auditors indicated that only 3 of the 24 CFO Act agencies had neither a material control weakness, an issue involving compliance with applicable laws and regulations, nor an instance of lack of substantial compliance with requirements of the Federal Financial Management Improvement Act (FFMIA) of 1996.

The largest impediment to an opinion on the consolidated financial statements continues to be the Department of Defense's (DOD) serious financial management problems, which we have designated as high-risk since 1995. DOD faces financial management problems that are pervasive, complex, long-standing, and deeply rooted in virtually all business operations throughout the department. To date, none of the military services or major DOD components has passed the test of an independent financial audit because of pervasive weaknesses in financial management systems, operations, and controls. Overhauling financial management represents a major management challenge that goes far beyond financial accounting to the very fiber of the department's business operations and management culture. Cultural resistance to change and military service parochialism have played a significant role in impeding previous attempts to implement broad-based management reforms at DOD. The department has acknowledged that it confronts decades-old problems deeply grounded in the bureaucratic history and operating practices of a complex, multifaceted organization, and that many of these practices were developed piecemeal and evolved to accommodate different organizations, each with its own policies and procedures. In September 2001, Secretary of Defense Rumsfeld announced a broad, top-priority initiative intended to transform the full range of the department's business processes, including decades-old financial systems that are not well interconnected.

Two other major impediments that must be overcome are the government's inability to account for billions of dollars of transactions between federal government entities and to properly prepare the consolidated financial statements. The heart of the intragovernmental transactions issue is that the government lacks clearly articulated business rules for these transactions so that they are handled consistently by agencies. Compounding this problem, agencies have not reconciled intergovernmental balances with their trading partners. As a result, information reported to the Department of the Treasury (Treasury) is not reliable. OMB and Treasury have initiatives underway to address this issue. With respect to properly preparing the consolidated financial statements, Treasury plans to develop a new system and procedures to prepare the financial statements. The continued leadership of both OMB and Treasury will be important to resolve both of these issues.

Many agencies have been able to obtain unqualified audit opinions only by expending significant resources to use extensive ad hoc procedures and making billions of dollars in adjustments to derive financial statements months after the end of a fiscal year. Also, irrespective of the unqualified opinions on their financial statements, many agencies do not have timely, accurate, and useful financial information, including cost data, and sound controls with which to make informed decisions and to ensure accountability on an ongoing basis. Auditors for 17 of the 24 CFO Act agencies reported at least one material control weakness. In addition, reports of inspectors general and their contract auditors indicated that 20 of the 24 CFO Act agencies' financial management systems were not in substantial compliance with FFMIA's three federal financial management systems requirements. For the remaining four CFO Act agencies, auditors provided negative assurance, meaning that nothing came to their attention indicating these agencies' financial management systems do not meet FFMIA requirements. The auditors for these four agencies did not definitively state whether these agencies' systems substantially complied with FFMIA's requirements, which we believe is required under the statute. Ultimately, to fully meet the goals of financial management reform legislation, agencies will need to be able to generate timely, accurate, and useful financial and management information, including reporting performance results, to make decisions and monitor government performance every day. Agencies will also need to have effective internal controls in place and must ensure compliance with applicable laws and regulations.

The President's Management Agenda Fiscal Year 2002 includes improved financial management performance as one of his five governmentwide management goals. Other governmentwide initiatives include strategic management of human capital, competitive sourcing, expanded electronic government, and budget and performance integration. These initiatives cannot be addressed in an isolated or piecemeal fashion, but must be addressed in an integrated way to ensure that they drive a broader transformation of the cultures of federal agencies. The administration plans to use the Executive Branch Management Scorecard, which includes broad standards, to highlight agencies' progress in achieving management and performance improvements embodied in *The President's Management Agenda Fiscal Year 2002*. This is a step in the right direction to improving management and performance, but the value of the scorecards is not in the scoring, but in the degree to which scores lead to sustained focus and demonstrable improvements. It will be important that there be continued rigor in the scoring process.

In August 2001, the Principals of the Joint Financial Management Improvement Program (JFMIP)—Secretary of the Treasury O'Neill, Office of Management and Budget Director Daniels, Office of Personnel Management Director James, and I, as Comptroller General of the United States—began a series of periodic meetings that have resulted in substantive deliberations and agreements focused on key financial management reform issues such as better defining measures for financial management success. These measures include being able to routinely provide timely, accurate, and useful financial information and having no material internal control weaknesses or material noncompliance with laws and regulations and FFMIA requirements, which is essential to meeting the CFO Act's expectations, *The President's Management Agenda Fiscal Year 2002*, and Secretary of Defense Rumsfeld's business process transformation initiative. In addition, the JFMIP Principals have agreed to significantly accelerate financial statement reporting so that the government's financial statements are more timely and to discourage costly efforts designed to obtain unqualified opinions on financial statements without addressing underlying systems challenges.

Federal agencies have started to make progress in their efforts to modernize their financial management systems. However, the need for timely, accurate, and useful financial and performance management information is greater than ever given the increasing demands on the federal budget.[1] Indeed, the challenges of combating terrorism and ensuring our homeland security have come to the fore as urgent claims on our attention and on the federal budget. At the same time, the known fiscal pressures created by the retirement of the baby boom generation and rising health care costs remain. Correspondingly, the ultimate task of addressing today's needs without unduly exacerbating the long-range fiscal challenge has become much more difficult.

As we look ahead we face an unprecedented demographic challenge. A nation that has prided itself on its youth will become older. In fact, in 2008—only 6 years from now—the first wave of baby boomers become eligible to claim their Social Security benefits. As the share of the population over 65 climbs to more than 20 percent in 2035, federal spending on the elderly will absorb larger and ultimately unsustainable shares of the federal budget. Federal health and retirement spending are expected to surge as people live longer and spend more time in retirement. In addition, advances in medical technology are likely to keep pushing up the cost of providing health care. Absent substantive reform of these entitlement programs, a rapid escalation of federal spending for Social Security, Medicare, and Medicaid is virtually certain to overwhelm the rest of the federal budget.

On March 26, 2002, the Trustees of the Social Security and Medicare trust funds reported on the current and projected status of these programs over the next 75 years. The Trustees' reports highlight the need to address the long-term fiscal challenges facing the nation. The Trustees state that, while the near-term financial conditions have improved slightly since last year's reports, the programs continue to face substantial financial challenges in the not-too-distant future that need to be addressed soon. Once again, the Trustees underscored the fact that the most significant implication of these findings is that both Social Security and Medicare need to be reformed and strengthened at the

---

[1] Additionally, as of March 20, 2002, when we completed our field work, Treasury officials were anticipating that the current $5,950 billion debt ceiling for the government could be reached in the near future. Treasury officials were monitoring the situation closely and contemplating taking appropriate action if warranted, including exercising certain statutory authorities available to the Secretary of the Treasury.

earliest opportunity. The Trustees also stated that Medicare faces financial difficulties that in many ways are more severe than those confronting Social Security.

These long-term demographic and fiscal pressures and the new commitments undertaken after September 11 sharpen the need to look at competing claims and new priorities. While reforming health and retirement entitlement programs is essential to preserving fiscal flexibility in the long term, a fundamental review of all programs and operations can create much-needed fiscal flexibility to address emerging needs. There is a need to consider what the proper role of the federal government will be in the 21st century and how the government should do business in the future.

Timely, accurate, and useful financial and performance information can form the basis for reconsidering the relevance or "fit" of any federal program or activity in today's world and for the future. Such a review might identify programs that have proven to be outdated or persistently ineffective, or alternatively could prompt us to update and modernize activities through such actions as improving program targeting and efficiency, consolidation, or reengineering of processes and operations. In addition, the review should not be limited to only spending programs but should include the full range of more indirect tools of governance that the federal government uses to address national objectives. These tools include loans and loan guarantees, tax expenditures, and regulations. Ultimately, we should strive to hand to the next generation the legacy of a government that is effective and relevant to a changing society—a government that is as free as possible of outmoded commitments and operations that can inappropriately encumber the future.

The Congress and President Bush face the challenge of sorting out these many claims on the federal budget without the fiscal benchmarks that guided us through the years of deficit reduction into surplus. Going forward, new rules and goals will be important both to ensure fiscal discipline and to prompt a focus on the longer term implications of decisions. It is still the case that the federal government needs a decision-making framework that permits it to evaluate choices against both today's needs and the longer term fiscal future that will be handed to future generations. As stewards of our nation's future, we must begin to prepare for tomorrow. In this regard, we must determine how best to address these structural challenges in a reasonably timely manner in order to identify specific actions that need to be taken.

We appreciate the cooperation and assistance of Department of the Treasury and OMB officials, as well as the chief financial officers and inspectors general in carrying out our responsibility to report on the U.S. government's consolidated financial statements. We look forward to continuing to work with these officials and the Congress to achieve the goals and objectives of financial management reform.

Our report was prepared under the direction of Jeffrey C. Steinhoff, Managing Director, and Gary T. Engel, Director, Financial Management and Assurance. If you have any questions, please contact me on (202) 512-5500 or them on (202) 512-2600.

David M. Walker
Comptroller General
of the United States

GAO
Accountability * Integrity * Reliability

Comptroller General of the United States

United States General Accounting Office
Washington, DC 20548

The President
The President of the Senate
The Speaker of the House of Representatives

The Secretary of the Treasury, in coordination with the Director of the Office of Management and Budget (OMB), is required annually to submit financial statements for the U.S. government to the President and the Congress. GAO is required to audit these statements.[1] This is our report on the accompanying U.S. government's consolidated financial statements for the fiscal years ended September 30, 2001 and 2000[2] and associated reports on internal control and compliance with laws and regulations.

The government is responsible for (1) preparing annual consolidated financial statements in conformity with U.S. generally accepted accounting principles, (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the control objectives of the Federal Managers' Financial Integrity Act are met,[3] and (3) complying with applicable laws and regulations. Also, the 24 Chief Financial Officers (CFO) Act agencies are responsible for implementing and maintaining financial management systems that comply with the Federal Financial Management Improvement Act's (FFMIA) requirements. Our objective was to audit the consolidated financial statements for the fiscal years ended September 30, 2001 and 2000. Appendix I discusses the scope and methodology of our work.

A significant number of material weaknesses[4] related to financial systems, fundamental recordkeeping and financial reporting, and incomplete documentation continued to (1)

---

[1]The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. 331 (e). The government has elected to include certain financial information on the legislative and judicial branches in the consolidated financial statements as well.
[2]The consolidated financial statements for the fiscal years ended September 30, 2001 and 2000 consist of the Statements of Operations and Changes in Net Position, the Statements of Net Cost, the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited), the Dispositions of the Budget Surplus (Unaudited), and Balance Sheets, including the related notes to these financial statements and Stewardship Information (Unaudited).
[3]31 U. S. C. 3512 (c), (d). This Act requires agency heads to evaluate and report annually to the President on the adequacy of their internal controls and accounting systems and on actions to correct significant problems.
[4]A material weakness is a condition that precludes the entity's internal control from providing reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements or to stewardship information would be prevented or detected on a timely basis.

hamper the government's ability to accurately report a significant portion of its assets, liabilities, and costs, (2) affect the government's ability to accurately measure the full cost and financial performance of certain programs and effectively manage related operations, and (3) significantly impair the government's ability to adequately safeguard significant assets and properly record various transactions. Several of these material weaknesses (referred to hereafter as material deficiencies) resulted in conditions that continued to prevent us from expressing an opinion on the accompanying consolidated financial statements for the fiscal years ended September 30, 2001 and 2000.[5] There may also be additional issues that could affect the consolidated financial statements that have not been identified.

This year, upon early implementation of certain provisions of the National Defense Authorization Act for fiscal year 2002, the Department of Defense (DOD) reported that DOD's financial management systems are not able to provide adequate evidence supporting material amounts in its financial statements. DOD asserted that it is unable to comply with applicable financial reporting requirements for (1) property, plant, and equipment, (2) inventory and operating materials and supplies, (3) military retirement health care actuarial liability, (4) environmental liabilities, (5) intragovernmental eliminations and related accounting adjustments, and (6) cost accounting by suborganization/responsibility segment and major program.

Based largely on DOD's assertion, the DOD inspector general disclaimed an opinion on DOD's financial statements for fiscal year 2001 as it did for the previous 5 fiscal years. DOD's financial management systems and reporting weaknesses substantially impair our ability to determine the reliability of the financial information reported in the government's overall financial reports. Until DOD corrects these material weaknesses, they will continue to impede our ability to express an opinion on the U.S. government's consolidated financial statements. In addition, as noted later in this report, there are other material weaknesses that need to be corrected.

For the fiscal year 2001 *Financial Report of the United States Government*, the government has for the first time presented: (1) comparative financial statements;[6] (2) two new financial statements, namely, the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited), and the Dispositions of the Budget Surplus (Unaudited); and (3) a Statement of Net Cost that arrays information classified by agency rather than by function, as was shown in prior years.

DISCLAIMER OF OPINION ON THE CONSOLIDATED FINANCIAL STATEMENTS

Because we were unable to determine the reliability of significant portions of the accompanying U.S. government's consolidated Statements of Operations and Changes in

---

[5] We previously reported that material deficiencies prevented us from expressing an opinion on the fiscal year 1997, 1998, and 1999 consolidated financial statements.

[6] Numerous amounts previously reported for fiscal year 2000 have been restated in the accompanying consolidated financial statements. Given our disclaimer of opinion on the fiscal year 2000 consolidated financial statements and because the dollar amounts involved were not material, we did not audit these changes.

Net Position, Statements of Net Cost and Balance Sheets, for the fiscal years ended September 30, 2001 and 2000, we are unable to, and we do not, express an opinion on these consolidated financial statements. The Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus and the Dispositions of the Budget Surplus were not audited by us and, accordingly, we do not express an opinion on them.

As a result of the material deficiencies in the government's systems, recordkeeping, documentation, and financial reporting, readers are cautioned that amounts reported in the consolidated financial statements and related notes may not be reliable. These material deficiencies also affect the reliability of certain information contained in the accompanying Management's Discussion and Analysis and other financial management information--including information used to manage the government day to day and budget information reported by agencies--which is taken from the same data sources as the consolidated financial statements.

We have not audited and do not express an opinion on the Stewardship Information and Supplemental or Other Information included in the accompanying fiscal year 2001 *Financial Report of the United States Government*.[7]

Material Deficiencies

The government did not maintain adequate systems or have sufficient, reliable information to support information reported in the accompanying consolidated financial statements as described below. These material deficiencies contributed to our disclaimer of opinion and also constitute material weaknesses in internal control. Unless otherwise noted, the deficiencies existed for both fiscal year 2001 and 2000. Appendix II highlights the primary effects of these material weaknesses on the accompanying consolidated financial statements and on the management of government operations.

Property, Plant, and Equipment and Inventories and Related Property The government could not: satisfactorily determine that all such assets were included in the consolidated financial statements, verify that certain reported assets actually exist, or substantiate the amounts at which they were valued. A majority of the property, plant, and equipment and inventories and related property is the responsibility of DOD. Certain agencies, including DOD, did not maintain adequate systems or have sufficient records to provide reliable information on these assets.

Loans Receivable and Loan Guarantee Liabilities For fiscal year 2000, certain federal credit agencies responsible for significant portions of the government's lending programs, most notably the Department of Agriculture (USDA), were unable to properly estimate the cost of these programs, or estimate the net loan amounts expected to be collected, in conformity with U.S. generally accepted accounting principles and budgeting requirements. In fiscal year 2001, USDA and other key agencies made

[7] Although not required by U.S. generally accepted accounting principles to be reported in the consolidated financial statements, in prior years, the government reported certain significant information related to national defense assets in Stewardship Information. The government did not report such information in the accompanying consolidated financial statements.

significant improvements to these estimates, and as a result, this item is not a material deficiency contributing to our disclaimer of opinion on the fiscal year 2001 consolidated financial statements. However, significant adjustments to the initial estimates of program costs, net loan amounts to be collected, and related footnotes were required during the audit process at certain key agencies, indicating that material internal control weaknesses continue to exist in processes and procedures for making such estimates.

Liabilities and Commitments and Contingencies The government could not adequately support amounts reported for certain liabilities. For example, it could not develop an accurate estimate of key components of DOD's environmental and disposal liabilities and accurately estimate military postretirement health benefits liabilities included in federal employee and veteran benefits payable, which were reported at $581 billion in fiscal year 2001 and $192 billion in fiscal year 2000. In addition, the government could not determine whether commitments and contingencies, including those related to treaties and other agreements entered into to further the U. S. government's interests, were complete and properly reported.

Cost of Government Operations and Disbursement Activity The previously discussed material deficiencies in reporting assets and liabilities, material deficiencies in financial statement preparation, as discussed below, and the lack of effective agency disbursement reconciliations affect reported net costs. As a result, the government was unable to support significant portions of the total net cost of government operations, most notably related to DOD and USDA. As it relates to disbursement reconciliations, several major agencies did not effectively reconcile disbursements to the Department of the Treasury's (Treasury) records of disbursements, which is intended to be a key control to detect and correct errors and other misstatements in financial records in a timely manner. This is similar in concept to individuals reconciling their checkbooks with their bank statements each month. Although we have seen progress in this area over the past 5 years, there continued to be billions of dollars of unreconciled differences between agencies' and the Treasury's records of disbursements as of September 30, 2001 and 2000, which could also affect the balance sheet.

Accounting for and Reconciliation of Intragovernmental Activity and Balances For several years, OMB and Treasury have required the CFO Act agencies to reconcile selected intragovernmental activity and balances with their "trading partners."[8] However, numerous agencies did not fully perform such reconciliations for fiscal year 2000. Beginning with fiscal year 2001, OMB and Treasury required agency chief financial officers to report on the extent and results of intragovernmental activity and balances reconciliation efforts. The inspectors general reviewed these reports and communicated the results of their reviews to OMB, Treasury, and GAO. A substantial number of the CFO Act agencies did not fully perform the required reconciliations for fiscal year 2001 citing reasons such as (1) trading partners not providing needed data, (2) limitations and incompatibility of agency and trading partner systems, and (3) human resource issues. For fiscal years 2001 and 2000, amounts reported for agency trading partners for certain

[8]Trading partners are U.S. government agencies, departments, or other components included in the consolidated financial statements that do business with each other.

intragovernmental accounts were significantly out of balance. In addition, solutions will be required to resolve significant differences reported in other intragovernmental accounts, primarily related to appropriations.

To help address certain issues that contributed to the out of balance condition for intragovernmental activity and balances, OMB has stated that it is implementing the recommendations included in a study conducted for the Joint Financial Management Improvement Program in fiscal year 2001. OMB is also pursuing other changes to address core problems in this area, such as enhancing governmentwide business rules for transactions among trading partners, requiring quarterly reconciliations of intragovernmental activity and balances, and modifying certain standard general ledger accounts required to be used by federal agencies. Resolving this problem remains a difficult challenge and will require a commitment by the CFO Act agencies and continued strong leadership by OMB.

<u>Preparation of Consolidated Financial Statements</u> The government did not have adequate systems, controls, and procedures to properly prepare its consolidated financial statements, as described below. Also, disclosure of certain financial information was not presented in the consolidated financial statements in conformity with U.S. generally accepted accounting principles.

> *<u>Elimination of Intragovernmental Activity and Balances</u>* Consolidated financial statements are intended to present the results of operations and financial position of the components that comprise a reporting entity as if the entity were a single enterprise. When preparing the consolidated financial statements, the preparer must eliminate intragovernmental activity and balances between the agencies. Because of agencies' problems in handling their intergovernmental transactions, Treasury's ability to eliminate these transactions is impaired. Significant differences reported in intragovernmental accounts as noted above have been identified. Intragovernmental activity and balances are "dropped" or "offset" in the preparation of the consolidated financial statements rather than eliminated through balanced accounting entries. This contributes to the government's inability to determine the impact of these differences on amounts reported in the consolidated financial statements.
>
> *<u>Reconciling Operating Results With Budget Results</u>* The government did not have a process to effectively identify and report items needed to reconcile adequately the operating results, which for fiscal year 2001 showed a net operating cost of \$514.8 billion, to the budget results, which for the same period showed a unified surplus of \$127 billion.
>
> *<u>Consolidated Financial Statement Compilation</u>* The government could not adequately ensure that the information for each agency that was included in the consolidated financial statements was consistent with the underlying agency financial statements. This problem is compounded by the need for broad changes in the structure of the government's Standard General Ledger (SGL) accounts and the process for maintaining the SGL. For example, changes are needed that will result in direct alignment by SGL account from agencies' financial statement line items to like items reported in the consolidated financial statements.

To make the fiscal year 2001 consolidated financial statements balance, Treasury recorded a net $17.3 billion decrease to net operating cost on the Statement of Operations and Changes in Net Position, which it labeled unreconciled transactions. For the prior fiscal year, a net $4.8 billion in unreconciled transactions was recorded as a decrease to net operating revenue in the accompanying consolidated financial statements.[9] An additional net $3.9 billion and $.2 billion of unreconciled transactions were improperly recorded in net cost for fiscal years 2001 and 2000, respectively. Treasury attributes these net unreconciled transaction amounts primarily to the government's inability to properly identify and eliminate transactions between governmental entities, agency adjustments that affected net position, and other errors. However, Treasury was unable to adequately identify and explain the gross components of such amounts. Unreconciled transactions also may exist because the government does not have effective controls over reconciling net position.[10]

The net position reported in the consolidated financial statements is derived by subtracting liabilities from assets, rather than through balanced accounting entries. Further, the process used to prepare the consolidated financial statements requires significant human and financial resources and does not adequately leverage the existing work and work products resulting from federal agencies' audited financial statements.

Treasury plans to develop a new system and procedures to prepare the consolidated financial statements. These actions are intended to**,** among other things, directly link information from agencies' financial statements to amounts reported in the consolidated financial statements and facilitate the reconciliation of net position.

ADVERSE OPINION ON INTERNAL CONTROL

In addition to the material weaknesses noted above, we found three other material weaknesses in internal control as of September 30, 2001, which are described below. Because of the effects of the material weaknesses discussed in this report, in our opinion, the government did not maintain effective internal control to meet the following objectives: (1) transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements and stewardship information in conformity with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition and (2) transactions are executed in accordance with laws governing the use of budget authority and with other laws and regulations that could have a direct and material effect on the financial statements and stewardship information. Individual agency financial statement audit reports identify

---

[9] Last year a net $7.3 billion in unreconciled transactions was recorded as an increase in net position. As discussed in footnote 6 in this report, numerous amounts previously reported for fiscal year 2000 have been restated in the accompanying financial statements, including this amount.

[10] In prior years, the government reported unreconciled transactions as a change in net position. Although the government was unable to determine how much of the unreconciled transactions, if any, relate to operations, it reported unreconciled transactions as a component of net operating revenue/ (cost) in the accompanying consolidated financial statements.

additional reportable conditions[11] in internal control, some of which were reported by agency auditors as being material weaknesses at the individual agency level. These matters do not represent material weaknesses at the governmentwide level. Also, due to the issues noted throughout this report, additional material weaknesses may exist that have not been reported.

Improper Payments Across government, improper payments[12] occur in a variety of programs and activities, including those related to health care, contract management, federal financial assistance, and tax refunds. These payments often result from a lack of or an inadequate system of internal controls. Many federal programs are administered by entities other than the federal government. Most agencies have not estimated or reported the magnitude of improper payments in their programs.[13] *The President's Management Agenda Fiscal Year 2002* includes addressing erroneous payments (a term we consider synonymous with improper payments) as one of the two key elements for improving financial performance. While reported estimates of improper payments totaled approximately $19 billion for both fiscal years 2001 and 2000, the government did not estimate the full extent of improper payments in the consolidated financial statements. However, OMB now requires agencies to provide information on erroneous payment rates for directly administered federal programs over $2 billion.

Computer Security GAO has reported computer security as a governmentwide high-risk area since February 1997.[14] Computer security weaknesses are placing enormous amounts of government assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption. The government is not in a position to estimate the full magnitude of actual damage and loss resulting from federal computer security weaknesses because it is likely that many such incidents are either not detected or not reported. Agencies have not yet established comprehensive security management programs, which would provide the government with a framework for resolving computer security problems and managing computer security risks on an ongoing basis. The initial implementation of government information security reform provisions contained in the National Defense Authorization Act for fiscal year 2001, is a significant step in improving federal agencies' information security programs and addressing their serious, pervasive information security weaknesses. In its first report on the reform provisions, OMB commended agencies' improvement efforts, but noted that many agencies have significant deficiencies in every important area of security.

---

[11] Reportable conditions are matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of internal control that could adversely affect the government's ability to meet the internal control objectives described in this report.
[12] Improper payments include inadvertent errors, such as duplicate payments and miscalculations, payments for unsupported or inadequately supported claims, payments for services not rendered, payments to ineligible beneficiaries, and payments resulting from fraud and abuse by program participants and /or federal employees.
[13] U.S. General Accounting Office, *Financial Management: Improper Payments Reported in Fiscal Year 2000 Financial Statements,* GAO-02-131R (Washington, D.C.: Nov. 2, 2001).
[14] See, for example, U.S. General Accounting Office, *High-Risk Series: An Update,* GAO-01-263 (Washington, D.C.: Jan. 2001).

Tax Collection Activities Material internal control weaknesses and systems deficiencies continue to affect the government's ability to effectively manage its tax collection activities.[15] Due to errors and delays in recording activity in taxpayer accounts, taxpayers were not always credited for payments made on their taxes owed, which could result in undue taxpayer burden. In addition, the government did not always follow up on potential unreported or underreported taxes and did not always pursue collection efforts against taxpayers owing taxes to the government.

COMPLIANCE WITH APPLICABLE LAWS AND REGULATIONS AND FFMIA REQUIREMENTS

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited by the material weaknesses discussed above. Instances of noncompliance, some of which the agency auditors reported were material to individual agency financial statements, are included in individual agency audit reports. However, none of these instances were material to the accompanying consolidated financial statements.

Additionally, FFMIA requires auditors, as part of CFO Act agency financial statement audits, to report whether agencies' financial management systems substantially comply with federal financial management systems requirements, applicable federal accounting standards (U.S. generally accepted accounting principles), and the government's standard general ledger at the transaction level. For fiscal year 2001, auditors for 20 of the CFO Act agencies reported that agencies' financial management systems did not substantially comply with one or more of FFMIA's three requirements. For the remaining four CFO Act agencies, auditors provided negative assurance, meaning that nothing came to their attention indicating these agencies' financial management systems do not meet FFMIA requirements. The auditors for these four agencies did not definitively state whether these agencies' systems substantially complied with FFMIA's requirements, which we believe is required under the statute. While agencies continue to make some progress in addressing their financial management systems weaknesses, the serious shortcomings reported for these systems result in the lack of reliable financial information day-to-day that hampers effective financial management and is critical for implementation of the Government Performance and Results Act and the transition to a more results-oriented federal government. GAO plans to report to the Congress, by October 1, 2002, on agencies' FFMIA implementation for fiscal year 2001, as also required by FFMIA.

We caution that other noncompliance may have occurred and not been detected. Further, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

---

[15] U.S. General Accounting Office, *Financial Audit: IRS's Fiscal Years 2001 and 2000 Financial Statements,* GAO-02-414 (Washington, D.C.: Feb. 27, 2002).

We provided a draft of this report to Department of the Treasury and Office of Management and Budget officials, who expressed their commitment to address the problems this report outlines.

David M. Walker
Comptroller General
of the United States

March 20, 2002

APPENDIX I

SCOPE AND METHODOLOGY

The Government Management Reform Act of 1994 expanded the requirements of the CFO Act by making the inspectors general of 24 major federal agencies responsible for annual audits of agencywide financial statements prepared by these agencies and GAO responsible for the audit of the U.S. government's consolidated financial statements.[16] Our work was performed in coordination and cooperation with the inspectors general to achieve our joint audit objectives. This work included separate GAO audits of certain material agency components, as discussed below. Our audit approach focused primarily on determining the current status of the material deficiencies and the other material weaknesses affecting internal control that we had previously reported in our report on the consolidated financial statements for fiscal year 2000.[17] We performed sufficient audit work to provide this report on the consolidated financial statements, internal control, and the results of our assessment of compliance with applicable laws and regulations.

We separately audited the following material agency components.

- We audited and expressed an unqualified opinion on the Internal Revenue Service's (IRS) fiscal years 2001 and 2000 financial statements, which included approximately $2.1 trillion of tax revenue each year and $251 and $194 billion of tax refunds, and $20 billion and $22 billion of net federal taxes receivable for fiscal year 2001 and 2000, respectively.[18] In fiscal year 2001, we continued to report numerous material internal control weaknesses, which resulted in ineffective internal controls. We also reported one instance of noncompliance with applicable laws and regulations and lack of substantial compliance of IRS' financial management systems with FFMIA.

- We audited and expressed an unqualified opinion on the Schedules of Federal Debt managed by Treasury's Bureau of the Public Debt (BPD) for the fiscal years ended September 30, 2001 and 2000.[19] The schedules reported for these 2 fiscal years (1) over $3.3 (2001) and $3.4 (2000) trillion of federal debt held by the public comprising individuals, corporations, state and local governments, the Federal Reserve Banks, and foreign governments and central banks, (2) about $2.5 (2001) and $2.2 (2000) trillion of intragovernmental debt holdings, which represent federal debt issued by Treasury and held by certain federal government accounts such as the Social Security and Medicare trust funds, and (3) nearly $207 (2001) and $225 (2000) billion of interest on federal debt held by the public.[20] In fiscal year 2001, we

---

[16]The 1994 Act authorized OMB to designate agency components that also would receive a financial statement audit.

[17] U.S. General Accounting Office, *U.S. Government Financial Statements: FY 2000 Reporting Underscores the Need to Accelerate Federal Financial Management Reform*, GAO-01-570T (Washington, D.C.: Mar. 30, 2001).

[18]GAO-02-414.

[19]U.S. General Accounting Office, *Financial Audit: Bureau of the Public Debt's Fiscal Years 2001 and 2000 Schedules of Federal Debt,* GAO-02-354 (Washington, D.C.: Feb. 15, 2002).

[20] Treasury anticipates that the current debt ceiling of $5,950 billion could be reached in early 2002, and if so, appropriate action will need to be taken.

APPENDIX I

reported that BPD had effective internal control over financial reporting and compliance with laws and regulations related to the Schedules of Federal Debt. Further, we reported that there was no reportable noncompliance with a selected provision of a law we tested.

- We audited and expressed unqualified opinions on the December 31, 2000 and 1999 financial statements of the funds administered by the Federal Deposit Insurance Corporation (FDIC), including the Bank Insurance Fund, the Savings Association Insurance Fund, and the FSLIC Resolution Fund.[21] We reported that as of December 31, 2000, FDIC had effective internal control over financial reporting and compliance with laws and regulations. In addition, we performed audit procedures and tests of internal control over cash, investments and earned interest, and other material balances of the funds administered by FDIC as of September 30, 2001.

For fiscal year 2000, we performed tests of cash balances maintained by Treasury on behalf of the government. We provided the results of our work to the Treasury Office of Inspector General for consideration in its audit of Treasury's fiscal year 2000 departmentwide financial statements. For fiscal year 2001, the Treasury Office of Inspector General performed tests of cash balances.

We considered the CFO Act agencies' and certain other agencies' fiscal years 2001 and 2000 financial statements and the related auditors' reports prepared by the inspectors general or their contractors. Financial statements and audit reports for these agencies provide information about the operations of each of these entities. We did not audit, and we do not express an opinion on, any of these individual agency financial statements. We also considered the Department of Defense assertion provided to the DOD inspector general that DOD management prepared and submitted pursuant to the provisions of the National Defense Authorization Act for fiscal year 2002. We performed our work in accordance with U.S. generally accepted government auditing standards.

---

[21] U.S. General Accounting Office, *Financial Audit: Federal Deposit Insurance Corporation's 2000 and 1999 Financial Statements,* GAO-01-635 (Washington, D.C.: May 9, 2001).

APPENDIX II

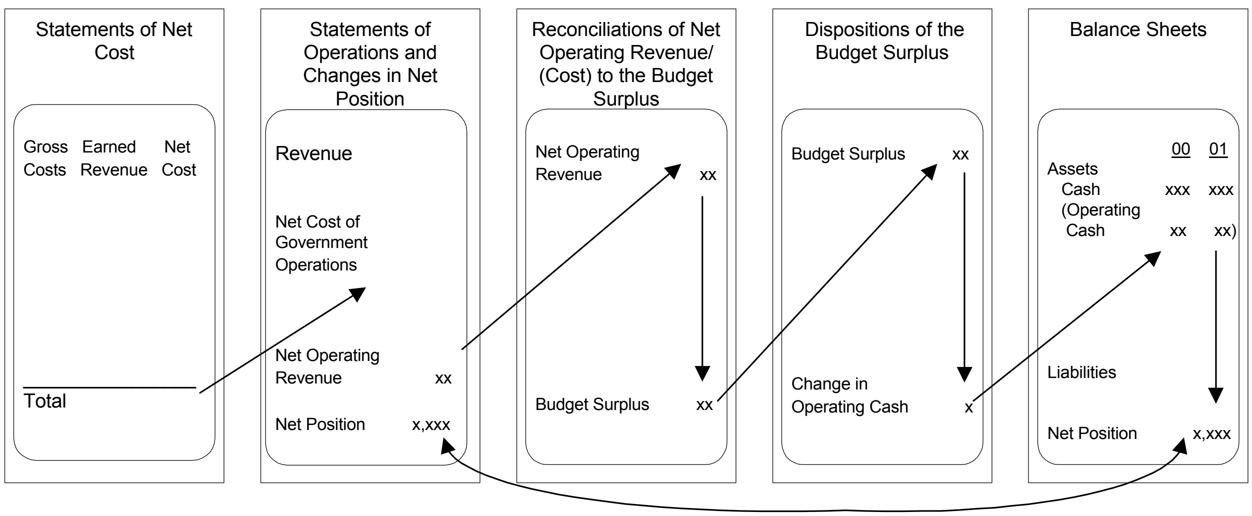
Primary Effects Caused by the Material Weaknesses and FFMIA Noncompliance Described in This Report

Areas Involving Material Weaknesses and FFMIA Noncompliance	Primary Effects on the Fiscal Year 2001 and 2000 Consolidated Financial Statements and the Management of Government Operations
Property, plant, and equipment and inventories and related property	Without accurate asset information, the government does not fully know the assets it owns and their location and condition and cannot effectively (1) safeguard assets from physical deterioration, theft, or loss, (2) account for acquisitions and disposals of such assets, (3) ensure the assets are available for use when needed, (4) prevent unnecessary storage and maintenance costs or purchase of assets already on hand, and (5) determine the full costs of programs that use these assets.
Loans receivable and loan guarantee liabilities	Weaknesses in the processes and procedures for estimating credit program costs affect the government's ability to support annual budget requests for these programs, make future budgetary decisions, manage program costs, and measure the performance of lending activities.
Liabilities	Problems in accounting for liabilities affect the determination of the full cost of the government's current operations and the extent of its liabilities. Also, improperly stated environmental and disposal liabilities and weak internal control supporting the process for their estimation affect the government's ability to determine priorities for cleanup and disposal activities and to allow for appropriate consideration of future budgetary resources needed to carry out these activities. In addition, when disclosures of commitments and contingencies are incomplete or incorrect, reliable information is not available about the extent of the government's obligations.
Cost of government operations and disbursement activity	Inaccurate cost information affects the government's ability to control and reduce costs, assess performance, evaluate programs, and set fees to recover costs where required. Improperly recorded disbursements could result in misstatements in the financial statements and in certain data provided by agencies for inclusion in the president's budget concerning obligations and outlays.
Accounting for and reconciliation of intragovernmental activity and balances	Problems in accounting for and reconciling intragovernmental activity and balances impair the government's ability to account for billions of dollars of transactions between governmental entities.
Preparation of consolidated financial statements	Weaknesses related to the preparation of the consolidated financial statements impair the government's ability to (1) effectively identify and report items needed to reconcile adequately the operating results reported in the consolidated financial statements with budget results, and (2) fully ensure that the consolidated financial statements were consistent with agency financial statements and were properly balanced.
Improper payments	Without a systematic measurement of the extent of improper payments, agency management cannot determine (1) if the problem is significant enough to require corrective action, (2) how much to invest in preventive internal control, (3) the success of efforts implemented to reduce improper payments, or (4) the magnitude or trends of improper payments, which limits the ability to pinpoint or target mitigation strategies.
Computer security weaknesses	Computer security weaknesses are placing enormous amounts of federal assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption.
Tax collection activities	Weaknesses in controls over tax collection activities continue to affect the government's ability to efficiently and effectively account for and collect revenue. Additionally, weaknesses in financial reporting affect the government's ability to make informed decisions about collection efforts. As a result, the government is vulnerable to loss of tax revenue and exposed to potentially billions of dollars in losses due to inappropriate refund disbursements.
FFMIA	When agency financial systems lack substantial compliance with FFMIA requirements, reliable financial information is not available for effective decision-making day to day.

(198058)

Financial Statements of the United States Government for the Years Ended September 30, 2001 and September 30, 2000

The following chart represents the order and flow of the data in the Financial Statements for fiscal 2001 and 2000. Two new statements are introduced this year—the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited) and the Dispositions of the Budget Surplus (Unaudited).



Statements of Net Cost

These Statements present the net cost of fiscal 2001 and 2000 Government operations. For the purposes of this document, "Government" refers to the United States Government. We have changed the format from the previous years' presentations. The new format was adopted to provide a more direct relationship to the departments and other significant entities that comprise the *Financial Report of the United States Government* (*Financial Report*). It categorizes costs by major departments, other Chief Financial Officer (CFO) Act entities, and other significant entities. It presents costs in much the same way as does the budget, except that costs are divided between the corresponding departments and entities mentioned above, based on generally accepted accounting principles (also known as GAAP). Interest on debt held by the public is presented separately.

These Statements contain the following three components:

- Gross Cost – This is the full cost of all the departments and entities. These costs may be traced directly, assigned on a cause-and-effect basis, or reasonably allocated to the corresponding departments and entities.
- Earned Revenue – This is revenue the Government earned by providing goods and services to the public at a price.
- Net Cost – This is computed by subtracting "Earned Revenue" from "Gross Cost."

Because of their specific functions, most of the costs originally associated with the General Services Administration (GSA) and the Office of Personnel Management (OPM) have been allocated to and reflected in the costs of their user agencies. The remaining costs for GSA and OPM on the Statements of Net Cost are the administrative operating costs, the expenses from prior and past costs from plan amendments, and the actuarial gains and losses for these agencies. The interest on the debt held by the public is part of the Department of the Treasury's (Treasury) responsibilities, but because of its importance, and the dollar amounts, it is reported separately in these statements. Net cost for governmentwide reporting purposes includes central agency allocations, and is net of intragovernmental eliminations. For this reason, individual agency net cost amounts will not agree with the agency's financial statements.

For further information concerning the mission and organization of the components of the Government of the United States, please refer to the Discussion and Analysis section.

Statements of Operations and Changes in Net Position

These Statements report the results of Government operations. These include unearned revenues that are generated principally by the Government's sovereign power to tax, levy duties, and assess fines and penalties. These Statements also cover the cost of Government operations, net of revenue earned from the sale of goods and services to the public (earned revenues). It further includes any adjustments and unreconciled transactions that affect the net position.

Revenue

"Individual Income Tax and Tax Withholdings" consist of Federal individual income taxes, Social Security taxes, Medicare taxes, and railroad retirement taxes, net of related refunds.

"Miscellaneous Earned Revenues" consist of earned revenues received from the public with virtually no associated cost. This category includes revenues generated by the Federal Communications Commission from the sale of spectrum licenses to promote open-air communication services to the public (spectrum auctions). It also includes rents and royalties on the Outer Continental Shelf Lands resulting from the leasing and development of mineral resources on public lands.

Net Cost of Government Operations

The "Net Cost of Government Operations" (which is gross cost less earned revenue) flows through from the Statement of Net Cost.

Unreconciled Transactions

"Unreconciled Transactions" are adjustments needed to bring the change in net position into balance due to unreconciled and unaccounted for differences in the consolidated financial statements. Please refer to Note 16—Unreconciled Transactions Affecting the Change in Net Position for detailed information.

Net Position, Beginning of Period

The "Net Position, Beginning of Period" reflects the net position reported on the prior year's Balance Sheet as of the end of that fiscal year.

Prior Period Adjustments

"Prior Period Adjustments" are revisions to adjust the beginning net position. Refer to Note 17—Prior Period Adjustments for detailed information.

Net Position, End of Period

This amount reflects the net position as of the end of the fiscal year.

The Federal Accounting Standards Advisory Board (FASAB) is studying what financial information should be presented in the Government's financial statements to reconcile the net operating revenue (cost) in such statements with the unified budget results in the President's Budget and whether additional information may be useful. Anticipating the disclosures that may be required, this Financial Report includes the following two financial statements: Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited) and Dispositions of the Budget Surplus (Unaudited).

Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited)

These Statements report the reconciliation of the results of operations (net operating revenue/(cost)) on the Statements of Operations and Changes in Net Position to the unified budget surplus in the President's budget.

Receipts and outlays in the President's budget are measured primarily on a cash or cash-equivalent basis and, therefore, differ from the accrued cost-basis measures used in the *Financial Report*. These Statements begin with the results of operations, reported on an accrued cost-basis in the Statements of Operations and Changes in Net Position, and arrives at the unified budget surplus. Reconciling items include accrued items, such as changes in liabilities for military, veteran and civilian benefits, as well as depreciation expense on fixed assets, and changes in environmental liabilities.

Components of Net Operating Revenue/(Cost) that are Not Part of the Budget Surplus

This information includes the operating components, such as the changes of benefits payable for veterans, military and civilian employees, and the environmental liabilities and depreciation expense, not included in the budget results.

Components of the Budget Surplus that are Not Part of Net Operating Revenue/(Cost)

This information includes the budget components not included in the operating results because of their long-term nature. These items are typically part of the Balance Sheets only, and are not part of the operating results.

Dispositions of the Budget Surplus (Unaudited)

These Statements reconcile the unified budget surplus (unaudited) to the change in operating cash during the fiscal year, and explains how the budgetary surplus was used. A budgetary surplus is the result of receipts (revenue) exceeding expenditures during a particular fiscal year.

In depicting how the budget surplus was used, these Statements show that the greatest amount went to repay the debt held by the public. Other transactions also required cash disbursements and are not part of the repayments of the debt. These other transactions, such as the issuance of student loans or premiums on early buyback of public debt, required cash payments and contributed to the use of the surplus. These statements show the differences between accrual and cash budgetary bases, mainly because of timing differences in the financial statements. Other cash includes cash held outside of Treasury. Cash-like items include liquid assets, other than cash, that are based on the U.S. dollar (gold, coinage, etc.)

Balance Sheets

The Balance Sheets show the Government's assets and liabilities. When combined with Stewardship Information, this information presents a more comprehensive understanding of the Government's financial position. All of the line items on the Balance Sheets are described in the Notes to the Financial Statements. For example, Note 2—Cash and Other Monetary Assets provides information concerning the cash reported in the assets section.

Assets

Assets included on the Balance Sheets are resources of the Government that remain available to meet future needs. The most significant assets that are reported on the Balance Sheets are property, plant and equipment, inventories, and loans receivable. There are, however, other significant resources available to the Government that extend beyond the assets presented in these Financial Statements. Those resources include Stewardship Assets, including natural resources (see Stewardship Information section), and the Government's sovereign powers to tax, regulate commerce, and set monetary policy.

Selected assets are highlighted in the Stewardship Information section of this report to demonstrate the Government's accountability for these assets. Stewardship assets include national defense assets, stewardship land, and heritage assets.

Liabilities and Net Position

Liabilities are obligations of the Government resulting from prior actions that will require financial resources. The most significant liabilities reported on the Balance Sheets are Federal employee and veteran benefits payable and Federal debt securities held by the public. Liabilities also include social insurance benefits due and payable as of the reporting date.

As with reported assets, the Government's responsibilities and policy commitments are much broader than these reported Balance Sheet liabilities. They include the social insurance programs disclosed in Stewardship Information, a wide range of other programs under which the Government provides benefits and services to the people of this Nation, and certain future loss contingencies.

The magnitude and complexity of social insurance programs, coupled with the extreme sensitivity of projections relating to the many assumptions of the programs, produce a wide range of possible results. The Stewardship Responsibilities section describes the social insurance programs, reports long-range estimates that can be used to assess the financial condition of the programs, and explains some of the factors that impact the various programs. Using this information, readers can apply their own judgment as to the condition and sustainability of the individual programs.

Each of the social insurance programs has an associated trust fund to account for its activity. An explanation of the trust funds for social insurance and many of the other large trust funds is included in Note 19—Dedicated Collections. That note also contains information about trust fund receipts, disbursements, and assets.

A broad perspective on the Government's responsibilities is provided by the Current Services Assessment, which also can be found in the Stewardship Information section. Presented in accordance with the President's 2003 budget, this information estimates Federal expenditures and receipts for fiscal 2002 to 2007, assuming there are no changes to current law.

The Government has entered into contractual commitments requiring the future use of financial resources and has unresolved contingencies where existing conditions, situations, or circumstances create uncertainty about future losses. Commitments as well as contingencies that do not meet the criteria for recognition as liabilities on the Balance Sheets, but for which there is at least a reasonable possibility that losses have been incurred, are disclosed in Note 18—Commitments and Contingencies.

Because of its sovereign power to tax and borrow, and the country's wide economic base, the Government has unique access to financial resources through generating tax revenues and issuing Federal debt securities. This provides the Government with the ability to meet present obligations and those that are anticipated from future operations and are not reflected in net position.

This page is intentionally blank.

United States Government Statements of Net Cost for the Years Ended September 30, 2001 and September 30, 2000

(In billions of dollars)	2001			2000		
	Gross Cost	Earned Revenue	Net Cost	Gross Cost	Earned Revenue	Net Cost
Department of Agriculture	83.5	11.1	72.4	81.8	9.0	72.8
Department of Commerce	7.4	1.2	6.2	11.0	1.1	9.9
Department of Defense	776.8	12.6	764.2	393.5	11.3	382.2
Department of Education	39.9	4.1	35.8	32.9	3.3	29.6
Department of Energy	27.0	5.2	21.8	28.9	4.7	24.2
Department of Health & Human Services	459.2	24.7	434.5	410.2	23.0	387.2
Department of Housing & Urban Development	34.5	2.4	32.1	36.5	3.1	33.4
Department of Interior	11.7	0.3	11.4	13.3	2.9	10.4
Department of Justice	26.5	2.3	24.2	27.0	1.9	25.1
Department of Labor	42.3	-	42.3	32.8	1.2	31.6
Department of State	10.0	1.0	9.0	9.4	0.5	8.9
Department of Transportation	63.6	0.3	63.3	48.9	0.2	48.7
Department of the Treasury	60.0	4.4	55.6	65.4	6.3	59.1
Interest on debt held by the public	217.7	-	217.7	230.2	-	230.2
Department of Veteran Affairs	196.0	2.7	193.3	118.6	2.2	116.4
Agency for International Development	7.1	0.1	7.0	6.9	-	6.9
Environmental Protection Agency	8.4	0.5	7.9	8.3	0.3	8.0
Federal Emergency Management Agency	6.3	1.6	4.7	4.7	1.6	3.1
General Services Administration	0.1	0.3	(0.2)	0.3	0.3	-
National Aeronautics & Space Administration	9.2	0.1	9.1	11.7	0.1	11.6
National Science Foundation	3.7	-	3.7	3.5	-	3.5
U.S. Nuclear Regulatory Commission	0.6	0.4	0.2	0.6	0.4	0.2
Office of Personnel Management	0.2	-	0.2	0.2	-	0.2
Small Business Administration	0.8	0.2	0.6	0.9	0.3	0.6
Social Security Administration	465.3	0.3	465.0	448.7	3.9	444.8
Export-Import Bank of the United States	0.8	0.3	0.5	1.1	1.2	(0.1)
Federal Communications Commission	14.9	6.7	8.2	1.4	5.7	(4.3)
Federal Deposit Insurance Corporation	3.1	0.5	2.6	1.4	(0.5)	1.9
National Credit Union Administration	0.3	0.4	(0.1)	0.3	0.1	0.2
Pension Benefit Guaranty Corporation	2.3	0.8	1.5	0.6	0.8	(0.2)
Railroad Retirement Board	9.0	-	9.0	9.0	-	9.0
Tennessee Valley Authority	11.8	6.9	4.9	7.6	6.7	0.9
United States Postal Service	86.2	65.6	20.6	92.0	64.5	27.5
All other entities	19.6	3.0	16.6	17.7	0.8	16.9
Total	2,705.8	160.0	2,545.8	2,157.3	156.9	2,000.4

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Operations and Changes in Net Position
for the Years Ended September 30, 2001 and September 30, 2000

(In billions of dollars)	2001	2000
Revenue:		
Individual income tax and tax withholdings	1,663.6	1,635.2
Corporation income taxes	147.9	204.3
Unemployment taxes	26.7	26.6
Excise taxes	67.3	69.3
Estate and gift taxes	28.3	28.9
Customs duties	18.7	19.4
Other taxes and receipts	48.9	56.3
Miscellaneous earned revenues	12.3	4.8
Total revenue	2,013.7	2,044.8
Less net cost of Government operations	2,545.8	2,000.4
Unreconciled transactions affecting the change in net position (Note 16)	17.3	(4.8)
Net operating revenue/(cost)	(514.8)	39.6
Net position, beginning of period	(5,945.4)	(6,026.2)
Prior period adjustments (Note 17)	1.4	41.2
Net operating revenue/(cost)	(514.8)	39.6
Net position, end of period	(6,458.8)	(5,945.4)

The accompanying notes are an integral part of these financial statements.

United States Government
Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus for the Years Ended September 30, 2001 and September 30, 2000 (Unaudited)

(In billions of dollars)	2001	2000
Net operating revenue/(cost)	(514.8)	39.6
Components of net operating revenue/(cost) that is not part of the budget surplus:		
Increase in Liability for Military Employee Benefits:		
Increase in military pension liabilities	17.8	28.9
Increase/(decrease) increase in military health liabilities	388.6	(3.8)
Increase in other military benefits	0.4	14.5
Increase in liability for military employee benefits	406.8	39.6
Increase in Veteran Compensation and Burial Benefits:		
Increase in liability for veterans	115.2	61.3
Increase in liability for survivors	24.1	8.2
Decrease in liability for burial benefits	-	(0.1)
Increase in liability for veterans compensation	139.3	69.4
Increase in Liability for Civilian Employee Benefits:		
Increase in civilian pension liabilities	41.0	46.7
Increase in civilian health liabilities	7.2	18.3
Increase/(decrease) in other civilian benefits	1.9	(9.8)
Increase in liability for civilian employee benefits	50.1	55.2
Increase in Environmental Liabilities:		
Increase in energy's environmental liabilities	4.1	3.6
Increase in defense's environmental liabilities	0.1	15.1
Increase in all other's environmental liabilities	1.5	0.9
Increase in environmental liabilities	5.7	19.6
Depreciation expense	21.4	15.4
Increase in benefits due and payable	8.1	4.0
Decrease in taxes receivable	2.2	(0.6)
Increase in other liabilities	13.1	6.0
Prior period adjustments	(1.4)	1.2
Premium on early buyback of public debt	10.7	5.5
Seigniorage and sale of gold	(1.3)	(2.3)
Increase in accounts payable	4.7	5.2
Components of the budget surplus that are not part of net operating revenue/(cost):		
Capitalized Fixed Assets:		
Department of Defense	(11.1)	(12.0)
Civilian agencies	(23.3)	(19.6)
Total capitalized fixed assets	(34.4)	(31.6)
(Increase)/decrease in accounts receivable	(1.9)	2.7
Decrease in inventory	1.4	(11.9)
Increase in other assets	(3.7)	(5.4)
Principal repayments of precredit reform loans	19.9	24.0
Net amount of all other differences	1.1	1.3
Budget surplus	127.0	236.9

The accompanying notes are an integral part of these financial statements.

United States Government
Dispositions of the Budget Surplus
for the Years Ended September 30, 2001 and September 30, 2000 (Unaudited)

(In billions of dollars)		2001			2000	
Budget receipts		1,990.9			2,025.0	
Budget outlays		(1,863.9)			(1,788.1)	
Unified budget surplus			127.0			236.9
Debt Held by the Public:						
Repayment of debt held by the public	2,620.7			2,233.5		
Borrowings from the public	(2,530.6)			(2,010.8)		
Reduction in public debt outstanding		90.1			222.7	
Loan Programs:						
Net direct loan activity	19.1			21.7		
Net guaranteed loan activity	4.2			(4.3)		
Net activity in loan programs		23.3			17.4	
Interest Payable:						
Interest paid	175.8			184.4		
Interest accrued on debt with the public	(171.0)			(186.0)		
Reduction in interest payable		4.8			(1.6)	
Premium on early buyback of public debt		10.7			5.5	
Other Assets:						
Increase in special drawing rights	1.6			4.0		
Increase in other monetary assets	8.2			0.9		
Increase/(decrease) in other assets	1.6			(1.6)		
Increase/(decrease) in loans to the IMF	4.7			(6.4)		
Net change in other cash and cash-like assets		16.1			(3.1)	
Other Liabilities:						
(Decrease)/increase in deposit fund balances	(4.1)			1.2		
(Decrease)/increase in other liabilities	(4.1)			0.9		
Net change in other cash and cash-like liabilities		(8.2)			2.1	
Seigniorage and other equity		(1.3)			(2.3)	
Disposition of surplus			135.5			240.7
Operating Cash: (Note 2)						
Operating cash balance September 30, 2001 and September 30, 2000		44.2			52.7	
Operating cash balance September 30, 2000 and September 30, 1999		(52.7)			(56.5)	
Decrease in operating cash balance			(8.5)			(3.8)

The accompanying notes are an integral part of these financial statements.

United States Government Balance Sheets as of September 30, 2001 and September 30, 2000

(In billions of dollars)	2001	2000
Assets:		
Cash and other monetary assets (Note 2)	108.0	104.9
Accounts receivable (Note 3)	34.2	32.3
Loans receivable (Note 4)	208.9	207.6
Taxes receivable (Note 5)	21.1	23.3
Inventories and related property (Note 6)	183.8	185.2
Property, plant and equipment (Note 7)	306.7	298.5
Other assets (Note 8)	63.4	59.7
Total assets	926.1	911.5
Liabilities:		
Accounts payable (Note 9)	95.7	91.0
Federal debt securities held by the public (Note 10)	3,319.8	3,409.9
Federal employee and veteran benefits payable (Note 11)	3,360.8	2,764.7
Environmental and disposal liabilities (Note 12)	306.8	301.2
Benefits due and payable (Note 13)	86.0	77.8
Loan guarantee liabilities (Note 4)	27.7	37.3
Other liabilities (Note 14)	188.1	175.0
Total liabilities	7,384.9	6,856.9
Commitments and contingencies (Note 18)		
Net position	(6,458.8)	(5,945.4)
Total liabilities and net position	926.1	911.5

The accompanying notes are an integral part of these financial statements.

United States Government Stewardship Information for the Years Ended September 30, 2001 and September 30, 2000 (Unaudited)

Stewardship Assets

The Government holds "Stewardship Assets" for the benefit of the Nation. Because the Government has been entrusted with, and made accountable for, these resources and responsibilities, they are recognized in this *Financial Report*.

When acquired, stewardship assets are generally treated as expenses in the financial statements. This section provides more detailed stewardship information on these resources to highlight their long-term benefit and to demonstrate accountability. This information facilitates the understanding of the operations and financial condition of the Government.

National Defense Assets

"National Defense Assets" consist of property, plant and equipment that the Department of Defense (DOD) requires to perform military missions, such as combat operations, peacekeeping, and support of civilian authorities during civil emergencies, and vessels held in a preservation status by the Maritime Administration's National Defense Reserve Fleet.

While standards presently exist for reporting information on national defense assets, DOD is aware that FASAB, at DOD's request, is considering modifications to its national defense asset standard. DOD will not report any information on national defense assets until FASAB concludes its consideration of this matter and retains or changes existing standards.

Stewardship Land

"Stewardship Land" refers to federally-owned land that is set aside for the use and enjoyment of present and future generations and land on which military bases are located. Except for military bases, this land is not used or held for use in general Government operations. Stewardship land is land that the Government does not expect to use to meet its obligations, unlike the assets listed in the Balance Sheets. Stewardship land is measured in nonfinancial units such as acres of land and lakes, miles of parkways, and miles of wild and scenic rivers. Examples of stewardship land include national parks, national forests, wilderness areas, and land used to enhance ecosystems to encourage animal and plant species and to conserve nature. This category excludes lands administered by the Bureau of Indian Affairs and held in trust.

Most stewardship land managed by the Government was once part of the 1.8 billion acres of public domain land acquired between 1781 and 1867. Stewardship land accounts for 28 percent of the current U.S. land mass. Stewardship land acquired totaled $373.0 million and $306.5 million for the years ended September 30, 2001, and September 30, 2000, respectively. The table below depicts the stewardship land owned by the Government and administered by the Department of Interior, the Department of Defense, and the Department of Agriculture. Detailed information concerning stewardship land can be obtained in the financial statements of the Departments of Interior, Agriculture and Defense.

United States Government Stewardship Land as of September 30

Agency	Predominate Use	Millions of Acres 2001	Millions of Acres 2000	Percentage 2001	Percentage 2000
Bureau of Land Management	Public land	261.8	264.4	40.5	40.9
U.S. Forest Service	National forest system	192.4	192.2	29.8	29.8
U.S. Fish and Wildlife Service	National wildlife refuge system	90.1	88.7	14.0	13.7
National Park Service	National park system	78.9	78.2	12.2	12.1
Department of Defense	Defense facilities	16.8	16.8	2.6	2.6
Bureau of Reclamation	Water, power, and recreation	5.7	5.8	0.9	0.9
Total acres		645.7	646.1	100.0	100.0

Heritage Assets

"Heritage Assets" are Government-owned assets that have one or more of the following characteristics:

- Historical or natural significance.
- Cultural, educational, or artistic importance.
- Significant architectural characteristics.

The cost of heritage assets often is not determinable or relevant to their significance. Like stewardship land, the Government does not expect to use these assets to meet its obligations. The most relevant information about heritage assets is nonfinancial. The public entrusts the Government with these assets and holds it accountable for their preservation. Examples of heritage assets include Mount Rushmore National Memorial, Yosemite National Park, and museum objects on display at the Smithsonian Institution. Other examples of heritage assets include the Declaration of Independence, the U.S. Constitution, and the Bill of Rights preserved by the National Archives. Also included are national monuments/structures such as the Vietnam Veterans Memorial, the Jefferson Memorial, and the Washington Monument, as well as art and cultural treasures at the Smithsonian Institution and the Library of Congress (LC). Many other sites such as battlefields, historic structures, and national historic landmarks are also placed in this category.

Some heritage assets are used both to remind us of our heritage and for day-to-day operations. These assets are referred to as Multi-use Heritage Assets. One typical example is the White House. The cost of acquisition, betterment or reconstruction of all multi-use heritage assets is capitalized as general property, plant and equipment and is depreciated.

The following discussion of the Government's heritage assets is not all-inclusive. Rather, it highlights significant heritage assets reported by Federal agencies.

The Government classifies heritage assets into three broad categories:

- Collection-type.
- Natural.
- Cultural.

"Collection-type Heritage Assets" include objects gathered and maintained for museum and library collections. "Natural Heritage Assets" include national wilderness areas, wild and scenic rivers, natural landmarks, forests, and grasslands. "Cultural Heritage Assets" include historic places and structures, memorials and monuments, national cemeteries, and archeological sites.

Collection-Type Heritage Assets

The Smithsonian Institution holds some of the most prominent Federal museum collections. The Smithsonian acquires, protects, and preserves approximately 140 million individual objects for public exhibition, education, and research.

Similarly, the LC holds the world's largest library collection, comprising more than 115 million items. The LC receives two copies of every book, pamphlet, map, print, photograph, and piece of music registered for copyright in the United States.

The National Archives hold more than 2 million cubic feet of records. These records ensure ready access to essential information documenting the rights of citizens, the actions of Federal officials, and the effects of those actions on the national experience. These records include text and legislative records; cartographic and architectural records; motion picture, sound, and video records; and still pictures and graphics. The National Archives also maintains historically important documents such as the U.S. Constitution and the Louisiana Purchase Treaty.

Collection-type heritage assets acquired totaled $13.2 million and $61.4 million for the years ended September 30, 2001, and September 30, 2000, respectively.

Natural Heritage Assets

Congress has designated several wilderness areas to preserve their natural conditions. The Department of Interior (DOI) manages approximately 71 million acres of these wilderness areas comprised of almost 68.3 percent of the Nation's 104 million wilderness acres. The Cebolla Wilderness in New Mexico is one such area.

The "national wild and scenic rivers system" includes protected free-flowing rivers. The Government protects these areas because of their fish and wildlife, or for their scenic, recreational, geologic, historic, or cultural value. DOI manages 52.5 percent of these 11,294 river miles, including the Bluestone National Scenic River in West Virginia.

The Government also sets aside natural landmarks that exemplify a region's natural characteristics. The National Park Service manages 18 national natural landmarks, such as the Garden of the Gods in Colorado.

The U.S. Forest Service manages 155 national forests and 20 national grasslands on over 192 million acres of public land. These areas encompass significant heritage resources. Examples include the White Mountain National Forest in New Hampshire and the Thunder Basin National Grassland in Wyoming.

Natural heritage assets acquired totaled $51.0 million and $106.8 million for the years ended September 30, 2001, and September 30, 2000, respectively.

Any acreage cited above for natural heritage assets, such as wilderness areas, are also included in the acreage cited in the Stewardship Land section.

Cultural Heritage Assets

The National Register of Historic Places lists historic sites and structures. This is America's official list of cultural resources worthy of preservation. Official properties include districts, sites, buildings, structures, and objects significant to American history. It also includes significant architectural, archaeological engineering, and cultural properties. Forest Service land encompasses 887 such properties.

The Nation's monuments and memorials include the Washington Monument, the Vietnam Veterans Memorial, and the Jefferson Memorial in Washington, D.C. The National Park Service manages these. In addition, the American Battle Monuments Commission administers, operates, and maintains 24 permanent American Military Cemeteries on foreign soil and 27 stand-alone memorials, monuments, and markers around the world. This includes the Belleau Wood Marine Monument in France.

Archeological sites contain the remains of human activity. DOI manages numerous archaeological sites. The National Park Service manages 63,000 archeological sites; the Bureau of Land Management, the U.S. Fish and Wildlife Service and the Bureau of Reclamation manage 269,159 archaeological and historical properties. The ancient earthen mounds at the Hopewell Culture National Historic Site in Ohio are a notable example.

National cemeteries include the Arlington National Cemetery in Virginia and the Fort Logan National Cemetery in Colorado. The Department of the Army (Army) manages the Arlington National Cemetery. The Department of Veterans Affairs (VA) manages Fort Logan National Cemetery and other cemeteries.

Stewardship Responsibilities

"Stewardship Responsibilities" provides information on the social insurance programs: Social Security, Medicare, Railroad Retirement, Black Lung and Unemployment Insurance. The purpose of this information is to assist the American people in evaluating the financial condition and sustainability of these programs.

Social Insurance Update

The following table gives financial report users updated information on selected financial aspects of the Social Security and Medicare programs that became available subsequent to the preparation of the related data presented in the detailed social insurance disclosures on pages 57 to 74.

Specifically, the social insurance programs' actuarial analysis and assumptions that are included on pages 65 to 68 were prepared based on estimates as of January 1, 2001. On March 26, 2002, the Boards of Trustees for the Social Security and Medicare Trust Funds released annual reports that present information for these programs as of January 1, 2002. The table below compares selected key data elements from these sources.

Comparison of Trustees' Reports Updated Estimates with the Financial Report Estimates

	Trustees' Report Estimates as of January 1, 2002	Financial Report Estimates as of January 1, 2001
First Year Expenditures Exceed Tax Revenue:		
Social Security (OASI and DI)	2017	2016
Federal Old-Age and Survivors Insurance (OASI)	2018	2016
Federal Disability Insurance (DI)	2009	2008
Federal Hospital Insurance (Medicare Part A)	2016	2016
Year Trust Fund Assets Are Exhausted:*		
Social Security	2041	2038
Federal Old-Age and Survivors Insurance	2043	2040
Federal Disability Insurance	2028	2026
Federal Hospital Insurance	2030	2029
Actuarial Deficit as a Percentage of Taxable Payroll Over the 75-Year Projection Period:		
Social Security	1.87%	1.86%
Federal Old-Age and Survivors Insurance	1.54%	1.53%
Federal Disability Insurance	0.34%	0.33%
Federal Hospital Insurance	2.02%	1.97%
Annual Deficit as a Percentage of Taxable Payroll for the 75th Year of the Projection Period:		
Social Security	6.42%	6.05%
Federal Old-Age and Survivors Insurance	5.64%	5.33%
Federal Disability Insurance	0.78%	0.72%
Federal Hospital Insurance	7.37%[1]	7.35%
Present Value of Resources Needed Over the 75-Year Projection Period:		
Social Security	$4,562 billion[1]	$4,207 billion
Federal Hospital Insurance	$5,126 billion[1]	$4,730 billion

*See page 61 for more information on how trust funds are financed.

[1]Amount derived by the Office of the Actuary at SSA and CMS, respectively, for Trustees' Report projections.

In their 2002 Reports, the Trustees for the Social Security (OASDI) and Federal Hospital Insurance (Medicare Part A) programs reported some near-term improvement in the financial status of these programs. However, they continued to caution that long-term sustainability issues still need to be addressed, and that timely action to deal with the continuing long-term shortfall is needed. As the Trustees point out, "… the sooner adjustments are made the smaller and less abrupt they will have to be."

One factor with a large effect on this year's projections compared to last year was an increase in the long-term productivity assumption from a 1.5 percent annual growth rate to a 1.6 percent annual growth rate. In addition, the CPI inflation rate assumption was lowered (from 3.3 percent to 3.0 percent), there were several relatively small changes in the demographic assumptions, and some improvements in projection methods were incorporated into the estimates.

On balance, these changes extend the exhaustion date for the OASDI Trust Fund by three years (from 2038 to 2041) and for the HI Trust Fund by one year (from 2029 to 2030). Revenues fall behind expenditures a year later than last year (2017) for the OASDI Trust Fund but in the same year as last year (2016) for the HI Trust Fund. The 75-year actuarial deficits were slightly larger for both trust funds, as the changes in assumptions and methods didn't fully offset the addition of a new deficit year at the end of the 75-year projection period. Both funds remain substantially out of long-term actuarial balance. Compared to last year, the annual deficit (as a percentage of payroll) in the 75th projection year (2076) increased noticeably for the OASDI fund and was about the same for the HI fund.

The First Year Expenditures Exceed Tax Revenue represents the point at which the trust funds would have to start using interest income to make payments. Interest income is paid in the form of Treasury securities. In order to use the interest, the trust funds would have to redeem the securities. To finance redemption, the Government must raise taxes, increase borrowings from the public, cut spending for other programs, retire less debt, or some combination thereof. The Year Trust Fund Assets Are Exhausted represents the point at which all trust fund assets (Treasury securities) have been redeemed. After this date, these respective programs will not have adequate resources to pay promised benefits or obligations in a timely manner. In the year of trust fund exhaustion, 2041 for Social Security (OASDI) and 2030 for Medicare Part A, tax income is estimated to cover 73 percent and 68 percent of program expenditures, respectively. The Actuarial Deficit as a Percentage of Taxable Payroll Over the 75-Year Projection Period can be interpreted as the percentage that, if added to the current scheduled tax rates, would cover projected trust fund shortfalls over the 75-year period and have enough assets on hand at the end of the 75-year period to pay scheduled benefits in the following year. Similarly, the Annual Deficit as a Percentage of Taxable Payroll for the 75th Year of the Projection Period represents the increase in payroll taxes needed in year 2076 and 2075, respectively, to cover projected cash shortfalls for each 1-year period. The Present Value of Resources Needed Over the 75-Year Projection Period represents the discounted net excess of projected cash expenditures (outflow) over cash income (inflow) during the 75-year projection period. The trust fund assets at the beginning of the period are not reflected in the calculation of this amount.

Social Insurance

The social insurance programs were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the Government. Because taxpayers rely on social insurance in their long-term planning, social insurance programs should show their sustainability as currently constructed, as well as what their effect will be on the Government's financial condition. The resources needed to run these programs are raised through taxes and fees collections. Eligibility for benefits rests in part on earnings and time worked by the individuals. Social insurance program benefits sometimes are redistributed intentionally toward lower-wage workers. In addition, social insurance programs have uniform sets of entitling events and schedules that apply to all participants.

United States Statement of Social Insurance

The following table presents estimates for several key indicators of the status of the Social Security and Medicare programs. These estimates are based on long-range actuarial projections of the range of persons who are participants or eventually will participate in the programs as contributors or beneficiaries during a projected period of time sufficient to illustrate the financial status and sustainability of the program. The projection includes current workers, retirees, survivors, disabled persons who have not attained retirement age, as well as the participants who have attained retirement age, and those expected to become new participants in the future.

United States Government Statement of Social Insurance Present Value of Long-Range Actuarial Projections[1]

(In billions of dollars)	Contributions and Earmarked Taxes [2]		Benefit Payments [3]		Benefit Payments in Excess of Contributions and Earmarked Taxes	
	2001	2000	2001	2000	2001	2000
Participants Who Are Currently Receiving Benefits:						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	309	266	4,255	4,020	3,946	3,754
Federal Hospital Insurance (Medicare Part A)	113	97	1,693	1,681	1,580	1,584
Federal Supplementary Medical Insurance (Medicare Part B)	258	234	1,159	1,051	901	817
Railroad Retirement	56	2	81	27	25	25
Black Lung (Part C)[4]	8	8	4	4	(4)	(4)
Participants Who Are Not Currently Receiving Benefits:						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	12,349	11,335	18,944	17,217	6,595	5,882
Federal Hospital Insurance (Medicare Part A)	4,136	3,757	8,568	6,702	4,432	2,945
Federal Supplementary Medical Insurance (Medicare Part B)	1,845	1,527	7,415	6,094	5,570	4,567
Railroad Retirement	57	26	67	39	10	13
Future Participants: [5]						
Federal Old-Age, Survivors and Disability Insurance (Social Security)	11,035	10,088	4,700	4,297	(6,335)	(5,791)
Federal Hospital Insurance (Medicare Part A)	3,507	3,179	2,225	1,349	(1,282)	(1,830)
Federal Supplementary Medical Insurance (Medicare Part B)	593	404	2,206	1,514	1,613	1,110
Railroad Retirement	29	40	13	10	(16)	(30)

	Valuation Period	Valuation Date	Net Present Value of Negative Cashflow [6]
Federal Old-Age, Survivors and Disability Insurance (Social Security) 2000	1/1/2000 – 12/31/2074	1/1/2000	3,845
Federal Old-Age, Survivors and Disability Insurance (Social Security) 2001	1/1/2001 – 12/31/2075	1/1/2001	4,207
Federal Hospital Insurance (Medicare Part A) 2000	1/1/2000 – 12/31/2074	1/1/2000	2,699
Federal Hospital Insurance (Medicare Part A) 2001	1/1/2001 – 12/31/2075	1/1/2001	4,730
Federal Supplementary Medical Insurance (Medicare Part B) 2000	1/1/2000 – 12/31/2074	1/1/2000	6,494
Federal Supplementary Medical Insurance (Medicare Part B) 2001	1/1/2001 – 12/31/2075	1/1/2001	8,084
Railroad Retirement 2000	9/30/2000 – 12/31/2073	12/31/1998	8
Railroad Retirement 2001	1/1/2001 – 12/31/2076	1/1/2001	19
Black Lung (Part C) 2000	9/30/2000 – 9/30/2040	6/30/2000	(4)
Black Lung (Part C) 2001	9/30/2001– 9/30/2040	6/30/2001	(4)

The following notes are an integral part of this financial statement.

Notes to the Statement of Social Insurance

[1] Present values are computed based on the economic and demographic assumptions believed most likely to occur (the intermediate assumptions) as set forth in the related Trustees' reports.
[2] Contributions and earmarked taxes consist of payroll taxes from employers, employees, and self-employed persons; revenue from Federal income taxation of OASDI and railroad retirement benefits; monthly Medicare Part B premiums paid by, or on behalf of, beneficiaries; railroad work-hour tax; and excise tax on coal (Black Lung). Contributions and earmarked taxes for the Medicare Part B program presented in this report are presented on a consolidated perspective. Interest payments and other intragovernmental transfers have been eliminated. The Centers for Medicare & Medicaid Services' (CMS), formerly known as the Health Care Financing Administration (HCFA), 2001 Annual Report presents income from the trust fund's perspective, not a Governmentwide perspective. Therefore, CMS's Annual Report includes $8,084 billion for the present value of transfers from the general fund of the Treasury to the Medicare Part B Trust Fund that have been eliminated in this *Financial Report*.
[3] Benefit payments include administrative expenses.
[4] Black Lung disability benefits for current and future miners are not expected to be material.
[5] Includes births during the period and individuals below age 15 as of January 1 of the valuation year.
[6] The net present value of negative cashflow is the current amount of funds needed to cover projected shortfalls, excluding trust fund balances, over the 75-year period. The trust fund balances at the beginning of the valuation period that were eliminated for this consolidation were: $1,049 billion – Social Security, $177 billion – Medicare Part A, $44 billion – Medicare Part B, $19 billion – Railroad Retirement, and Black Lung Trust Fund, which had a negative balance of $7.2 billion.

The projection period for new entrants covers the next 75 years for the Social Security and Medicare programs. The projection period for current participants (or "closed group") would theoretically cover all of their working and retirement years, a period that could be greater than 75 years in a few instances. As a practical matter, the present values of future payments and contributions for/from current participants beyond 75 years are not material.

The actuarial present value of the excess of future benefit payments to current participants (that is, to the closed group of participants) over future contributions and tax income from them or paid on their behalf is calculated by subtracting the actuarial present value of future contributions and tax income by and on behalf of current participants from the actuarial present value of the future benefit payments to them or on their behalf. For Social Security and Medicare, further information can be obtained from the Social Security Administration and the Department of Health and Human Services: The 2001 Report of the Board of the Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, and The 2001 Report of the Board of the Trustees of the Federal Hospital Insurance Trust Fund.

Program Sustainability

Social Security (OASDI)

Under the intermediate assumptions (best estimates) of the Board of Trustees of the Federal OASDI Trust Funds, OASDI income from contributions on taxable earnings and from income taxes on benefits is expected to exceed total expenditures for this year and each of the next 14 calendar years. From 2010 through 2030, however, OASDI costs, relative to taxable earnings, are expected to increase rapidly as the "baby-boom" generation reaches retirement age. In contrast, the program's income from contributions due on taxable earnings and income taxes on benefits will remain a relatively constant percentage of taxable payroll.

In view of the size of the financial shortfall in the OASDI program over the next 75 years, the Board of Trustees of the Federal OASDI Trust Funds urges that the long-range deficits of both the OASI and DI Trust Funds be addressed in a timely way.

Medicare

Medicare has generally been viewed as a program in greater financial difficulty than Social Security because it will combine the rising costs of health care over time with the increase in beneficiaries as baby boomers become eligible. The approach of the last two decades, that of seeking improvements in the efficiency and effectiveness of health care delivery, will continue to be an important contributor to Medicare's future. The challenge facing the future financing of this program is how we will, as a society, share the costs of health care for a much larger aging population.

The Medicare Part A program is substantially out of financial balance in the long range. Under the intermediate assumptions of the Board of Trustees of the Medicare Part A Trust Fund, income is projected to continue to exceed expenditures moderately for the next 14 years, but to fall short by steadily increasing amounts in 2016 and later. The long-range outlook, however, remains extremely unfavorable, in large part as a result of the impending retirement of the baby boom generation. Over the full 75-year projection period, substantially greater changes in income and/or outlays are needed to bring the program into actuarial balance.

These projections indicate that without additional legislation, the fund would be exhausted in the future—initially producing payment delays, but very quickly leading to a curtailment of health care services to beneficiaries. In its 2001 annual report to Congress, the Board of Trustees of the Medicare Part A Trust Fund urged the Nation's policy makers to address the remaining financial imbalance facing the Medicare Part A Trust Fund by taking "further effective and decisive action, building on the strong steps taken in recent reforms." They also stated, "Consideration of further reforms should occur in the relatively near future."

The recent improvements in projected expenditures for Medicare Part B, while welcome, are not sufficiently large to diminish serious concerns with expenditure growth. The Board of Trustees of the Medicare Part B Trust Fund note that program costs have generally grown faster than the GDP and that this trend is expected to continue under present law. The projected increases are attributable in part initially to assumed continuing growth in the volume and intensity of services provided per beneficiary. Starting in 2010, the retirement of the post-World War II baby boom generation will also have a major influence on the growth in program costs.

Prior to the Balanced Budget Act of 1997, Medicare Part A Trust Fund assets were projected to be exhausted in the very near future. The urgency of this situation prompted considerable attention and led directly to the provisions in the Act to slow Medicare Part A expenditure growth. In contrast, the financing provisions for Medicare Part B prevent such crises. While Medicare Part B is in fact running a shortfall since premiums only cover about 25 percent of program costs, Part B remains solvent because of a growing infusion of general revenue funds. As a result, there has been substantially less attention directed toward the financial status of the Medicare Part B program than to the Medicare Part A program, even though Medicare Part B expenditures have increased faster than Medicare Part A expenditures in most years and are expected to continue to do so in the future.

Given the past and projected cost of the Medicare Part B program, the Board of Trustees of the Medicare Part B Trust Fund urges the Nation's policy makers to consider effective means of controlling Medicare Part B costs in the near term. For the longer term, legislative proposals need to be developed to address the large increases in Medicare Part B costs associated with the baby boom's retirement in partnership with Medicare Part A cost increases.

Railroad Retirement

The Railroad Retirement program is projected to have an $18.5 billion negative cashflow, based on a projection through 2076, on a consolidated basis. This negative cashflow will be financed through the redemption of securities that resulted from past program surpluses. The long-term stability of the program, however, is still questionable. Under the current financing structure, actual levels of railroad employment over the coming years will largely determine whether corrective action is necessary.

Subsequent event: On December 21, 2001, President Bush signed the "The Railroad Retirement and Survivors' Improvement Act of 2001" (RRSIA) into law. The new law enhances benefits and changes the funding of the retirement program.

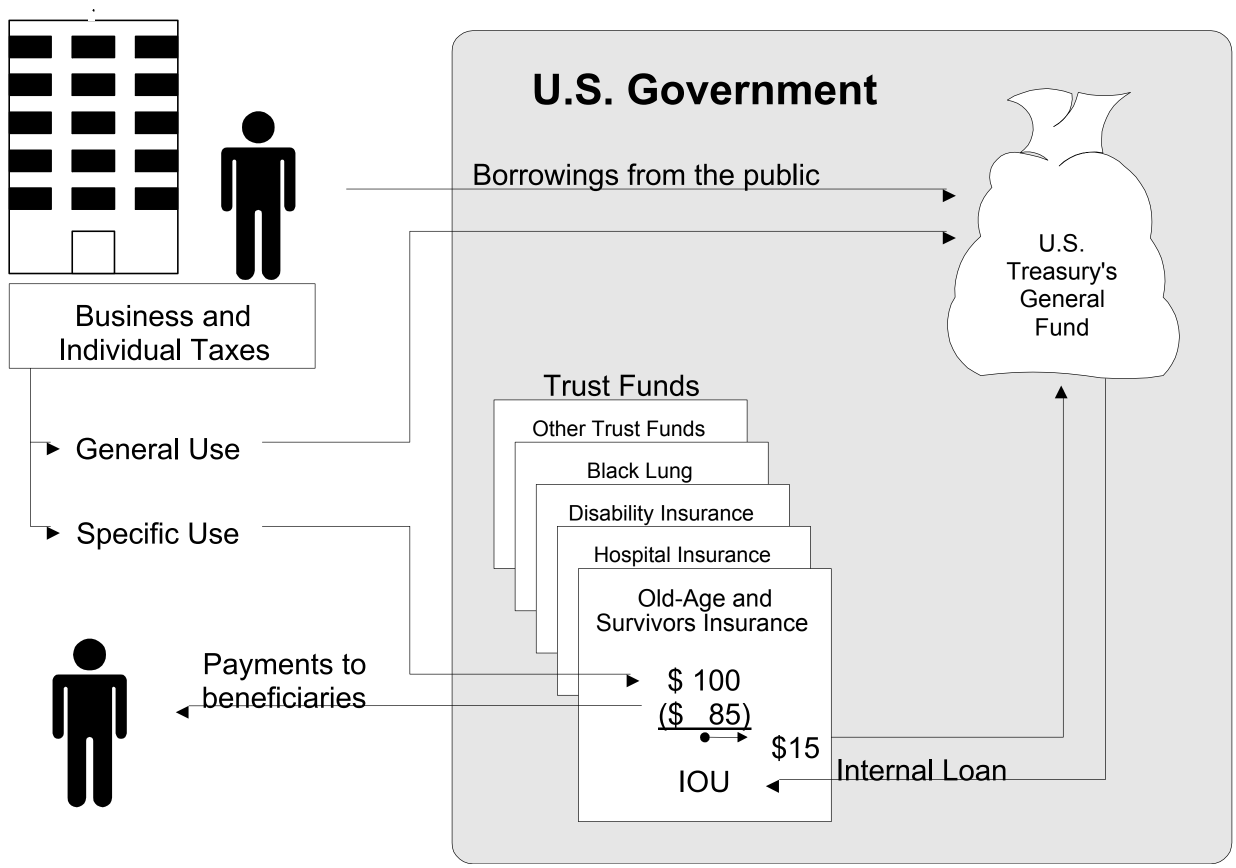
Benefits of the RRSIA of 2001 include:

- Increases the widow(er)s benefits by providing a guaranteed minimum amount of benefits.
- Restores full annuities to employees and their spouses who retire at age 60, instead of 62, with 30 years of railroad service.
- The vesting period is also reduced from 10 to 5 years.
- Creates a new National Railroad Retirement Investment Trust (Trust) to administer a new Railroad Retirement Investment Trust Fund (RRIT Fund).
- A new nongovernmental financial institution ("Disbursing Agent") will serve as a disbursing agent for all benefits payable under the Railroad Retirement Act.

Black Lung

The Black Lung Part C disability program's net present value of future benefit payments for the 39-year period ending September 30, 2040 is $3.5 billion. The net present value of future excise taxes for the 39-year period is $7.9 billion, which results in a $4.4 billion excess of excise taxes over benefit payments. However, the net present value of total cash outflows, including interest payments and administrative costs, is $20.8 billion resulting in an excess of cash outflows over excise taxes of $12.8 billion.

Trust Fund Financing



The Government collects taxes from business and individuals. Each type of tax collected is classified for "General use" or for "Specific use." The taxes collected for general use are included in the general fund and are used to fund the Government's general operations.

The taxes collected for specific use are credited to the corresponding trust fund that will use these funds to meet a particular Government purpose. The beneficiaries from these earmarked trust funds are paid directly from the balance of each of the corresponding trust funds. If the collections from taxes and other sources exceed outlays to the beneficiaries, the excess collections are invested, normally in Treasury securities, which means that the excess collections are "loaned" to the Treasury's general fund. The reason for this is that the trust funds generally are not permitted to hold the excess cash collected. Usually, all excess collections as well as interest earnings must be invested by the trust funds in Treasury securities or Government-guaranteed securities. Therefore, the trust fund balances do not represent cash. These balances are the sum of all specific use collections plus interest and other receipts, less payments to beneficiaries over the life of the fund.

When payments to beneficiaries exceed receipts, the trust funds redeem a commensurate amount of their Federal debt securities holdings.

In addition to earmarked taxes, trust funds receive income from the interest earned on investments in Federal debt securities and, in some cases, from other sources as well.

Social Security

Congress passed the Social Security Act in 1935. The Act, as subsequently amended, includes programs that provide retirement and disability benefits. Congress established two trust funds for Social Security: The Federal Old-Age and Survivors Insurance (OASI) and the Federal Disability Insurance (DI) Trust Funds (combined as OASDI). OASI pays retirement and survivors' benefits and DI pays benefits to disabled workers and their dependents. At the end of calendar year 2000, OASDI benefits were paid to approximately 45 million beneficiaries. Revenue to the combined OASDI funds consists primarily of taxes on earnings paid by employees, their employers, and the self-employed. OASDI also receives revenue from the income taxes on some Social Security benefits and interest on its investments in Treasury securities. Social Security revenues not needed to pay current benefits or administrative expenses are invested in special-issue Treasury securities. Eligibility and benefit amounts are determined under the laws applicable for the period. Current law bases the amount of the monthly benefit payments for workers, or their eligible dependents or survivors, on the workers' lifetime taxable earnings histories.

The Board of Trustees of the OASI and DI Trust Funds provides in its annual report to the President and Congress short-range (10 year) and long-range (75 year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Board of Trustees uses three alternative sets of economic and demographic assumptions to show a range of possibilities. Assumptions are made about many economic and demographic factors, including gross domestic product, earnings, the Consumer Price Index (CPI), the unemployment rate, the fertility rate, immigration, mortality, and disability incidence and terminations. The assumptions used in the accompanying tables, generally referred to as the "intermediate assumption," reflect the best estimate of expected future experience, under current law.

Cashflow Projections

The present values of actuarial estimates as shown in the following sections were computed as of January 1, 2001, the beginning of the valuation period. The actuarial estimated income equals the sum of the present value of all estimated non-interest income during the period. The actuarial estimated expenditures equal the sum of the present value of all estimated payments during the valuation period. These estimates were prepared using the financing method deemed the most appropriate by Congress and the Board of Trustees. Estimates assume the program will cover future workers as they enter the labor force.

The primary receipts of OASDI are funds appropriated under permanent authority based on contributions payable by workers, their employers, and individuals with self-employment income. Revenue derived from subjecting a portion of OASDI benefits to Federal personal income taxation is dedicated to the OASDI and Hospital Insurance (HI) programs. All contributions, or taxes, are collected by the Internal Revenue Service (IRS) and deposited to the trust fund. Another source of income is interest received on the investments held by the trust funds, which is implicit in the present values presented in this report. The primary expenditures are for OASDI benefit payments and for expenses related to administration of the OASDI programs.

Under current legislation and using intermediate assumptions, the OASI and DI Trust Funds are projected to be exhausted in 2040 and 2026, respectively. Combined OASDI expenditures will exceed annual tax income beginning in 2016 and will exceed total annual income (including interest income) for calendar years 2025 and later. Thus, tax income plus a portion of interest income will be needed to meet expenditures for the years 2016 through 2024. Thereafter, in addition to tax income and interest income, a portion of the principal (combined OASDI assets) will be needed each year until the trust fund assets are totally exhausted in 2038. At that point, annual program tax income will be sufficient to pay only approximately 73 percent of the benefits due.

Chart 1 shows actuarial estimates of combined OASDI annual income (excluding interest) and expenditures for 1960-2075 in nominal dollars. The estimates are for the open group population, all persons projected to participate in the OASDI program as covered workers or beneficiaries, or both, during that period. Thus, the estimates include payments from, and on behalf of, workers who will enter covered employment during the period, as well as those already in covered employment at the beginning of that period. These estimates also include expenditures made to, and on behalf of, such workers during that period.

Currently, Social Security tax revenues exceed benefit payments, and the system is building large trust fund reserves to help finance the retirement of the baby boom generation. Under current estimates, benefit payments will begin to exceed taxes in 2016, and Social Security will start using annual trust fund interest to help pay benefits. Starting around 2025, Social Security will need to use the trust fund reserves themselves to help pay benefits; by about 2038, the trust fund reserves will be exhausted. The trust fund interest and reserves are in the form of Treasury securities that must be redeemed. The Government will need to raise taxes (other than OASDI payroll taxes), increase borrowing from the public, cut spending for other programs, change the laws under which the Social Security program provides benefits, or some combination thereof, to redeem the securities.

Chart 1—Estimated OASDI Income (Excluding Interest) and Expenditures 1960-2075

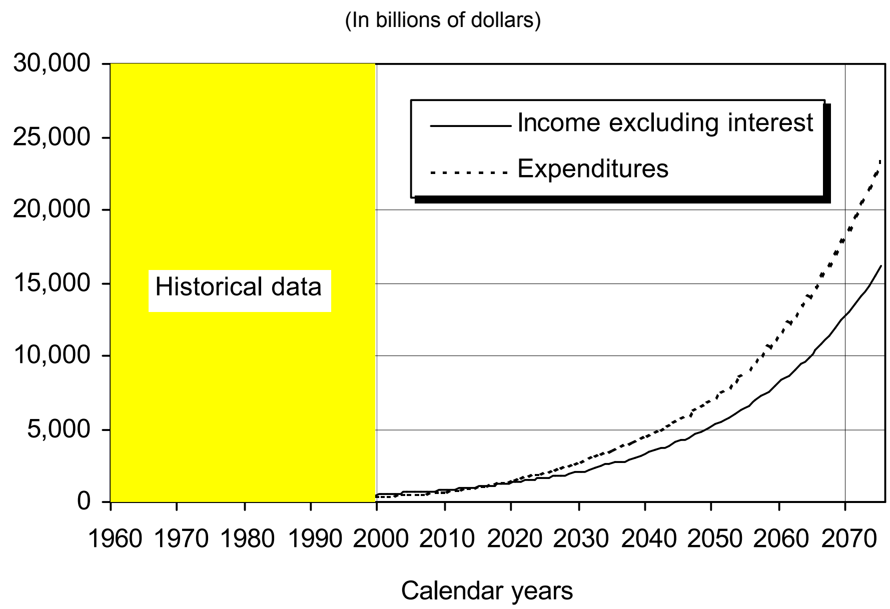


Chart 2 shows estimated annual income excluding interest and expenditures expressed as percentages of taxable payroll. As presently constructed, the program receives most of its income from the 6.2 percent payroll tax that employees and employers each pay on taxable wages and salaries (for a combined payroll tax rate of 12.4 percent of taxable payroll), and the 12.4 percent that is paid on taxable self-employment income. Because estimated annual income excluding interest consists primarily of payroll taxes, when expressed as a percentage of taxable payroll, it is close in magnitude to the OASDI payroll tax rate. The amount by which the income exceeds the tax rate reflects revenue transferred to the trust funds based on Federal income-taxation of OASDI benefits. When estimated expenditures are compared to income as percentages of taxable payroll, they necessarily reflect a similar pattern as when compared in nominal dollars. Whether expressed as percentages of taxable payroll or in nominal dollars, prior to 2016, estimated annual expenditures are less than estimated annual income, excluding interest, whereas in 2016 and thereafter expenditures are more.

The statement of social insurance on page 58 shows that the present value of the excess of income (excluding interest) over expenditures for the 75-year period is -$4,207 billion. If augmented by the trust fund assets at the start of the period (January 1, 2001), it is -$3,157 billion. This excess does not equate to the actuarial balance in the Trustees' Report. To reconcile these values, it should be considered that the excess (including the starting trust fund assets) would need to take into account the cost of attaining a target trust fund balance by the end of the period. The present value of this cost is $237 billion, which reduces the excess to -$3,394 billion. This reduced (more negative) excess, when expressed as a percent of taxable payroll, is defined by the Trustees in their annual reports to be the actuarial balance. Thus, the excess of -$3,394 billion equates to the actuarial balance of -1.86 percent of taxable payroll reported in the 2001 Trustees' Report.

One interpretation of this negative actuarial balance (-1.86 percent of the taxable payroll) is that it represents the magnitude of the increase in the combined payroll tax rate for the 75-year period that would result in an actuarial balance of zero. The combined payroll tax rate is 12.4 percent today and is currently scheduled to remain at that level. An increase of 1.86 percentage points in this rate in each year of the 75-year projection period—about 0.93 percentage points for employees and employers each, resulting in a total rate for each of 7.13 percent—is estimated to produce enough income to pay all benefits due under current law for that period. Equivalent benefit reductions, or combinations of both tax increases and benefit reductions, could be made to achieve the same effect. Any accumulation and subsequent redemption of substantial trust fund assets may have economic and public policy implications that go beyond the operation of the OASDI program itself. Discussion of these broader issues is not within the scope of this report.

Chart 2—Estimated OASDI Income (Excluding Interest) and Expenditures as a Percentage of Taxable Payroll 1960-2075

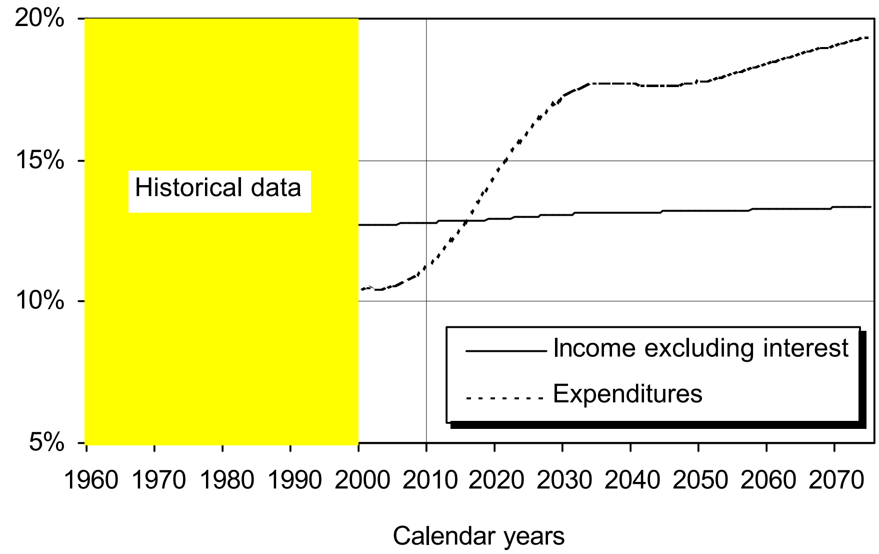
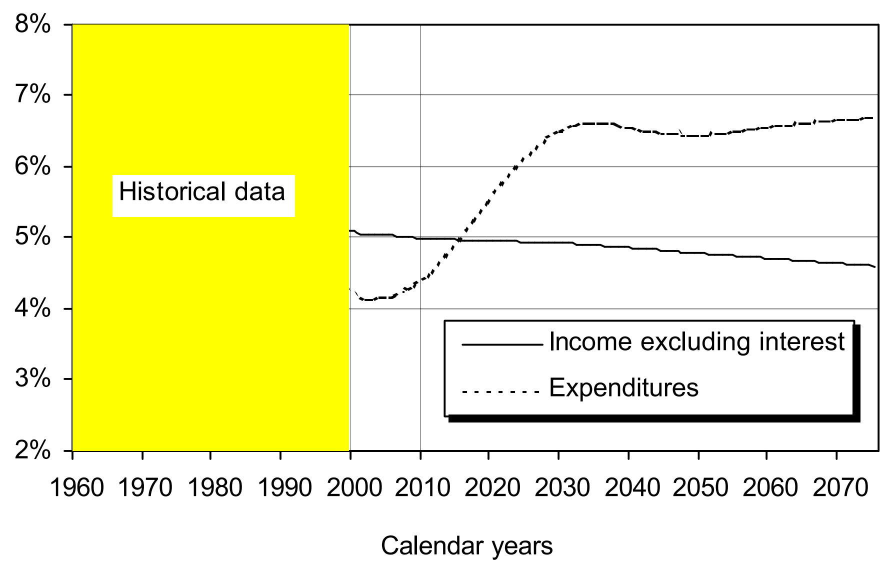


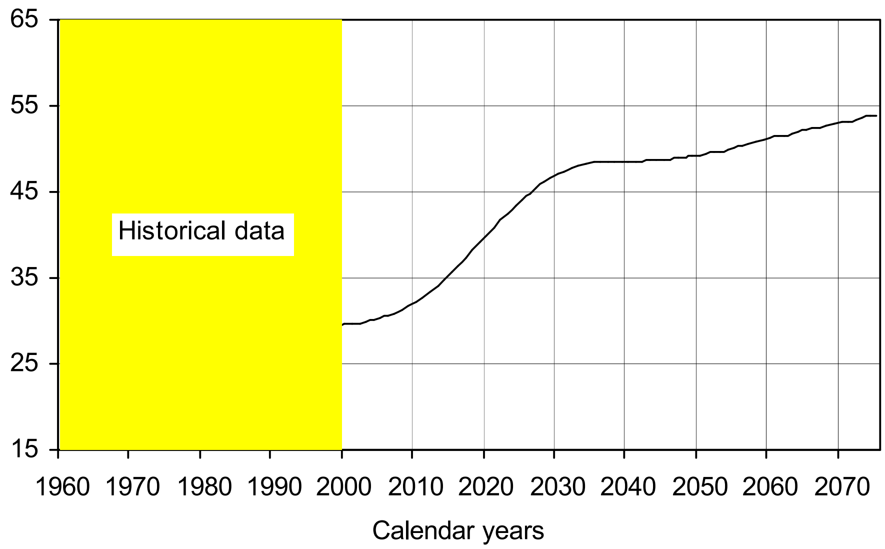
Chart 3 shows estimated annual income, excluding interest, and expenditures, expressed as percentages of GDP. Analyzing these cashflows in terms of percentage of the GDP, which represents the total value of goods and services produced in the United States, provides a measure of the size of the OASDI program in relation to the capacity of the national economy to sustain it.

Chart 3—Estimated OASDI Income (Excluding Interest) and Expenditures as a Percentage of GDP 1960-2075



As shown in Chart 4, there were about 30 OASDI beneficiaries for every 100 covered workers in 2000. As indicated, this ratio is expected to increase substantially in the future. The most rapid increase will occur as the relatively large number of persons born during the baby boom (from the end of World War II through the mid-1960s) reaches retirement age and begins to receive benefits. At the same time, the relatively small number of persons born during the subsequent period of low fertility rates will comprise the labor force. Between 2030 and 2050, the number of workers per beneficiary is estimated to remain relatively stable as the baby-boom generation diminishes in size. After 2050, this ratio is expected to continue to increase at a slower pace, reflecting the increasing numbers of beneficiaries due to projected increases in life expectancy. Under the intermediate assumption, by the end of the 75-year projection period, the number of OASDI beneficiaries per 100 covered workers is projected to increase to 54.

Chart 4—Number of OASDI Beneficiaries per 100 Covered Workers 1960-2075



Actuarial Assumptions and Sensitivity Analysis

Actual future income from OASDI payroll taxes and other sources, and actual future expenditures for benefits and administrative expenses, will depend upon a large number of factors: the size and composition of the population that is receiving benefits, the level of monthly benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers' earnings. These factors will depend, in turn, upon future marriage and divorce rates, birth rates, death rates, migration rates, labor force participation and unemployment rates, disability incidence and termination rates, retirement age patterns, productivity gains, wage increases, cost-of-living increases, and many other economic and demographic factors.

While it is reasonable to assume that actual trust fund experience will fall within the range defined by the three alternative sets of assumptions used in the Trustees' report, no definite assurance can be given that this will occur because of the uncertainty inherent in projections of this type and length. In general, a greater degree of confidence can be placed in the assumptions and estimates for the earlier years than for the later years. Nonetheless, even for the earlier years, the estimates are only an indication of the expected trend and potential range of future program experience.

The assumptions fluctuate in the earlier years of the projection period before reaching their ultimate values for the remainder of the 75-year projection period. The following table summarizes the ultimate values assumed for the key economic and demographic factors underlying the actuarial estimates shown in this report.

The estimates used in this presentation are based on the assumption that the programs will continue as presently constructed. They are also based on various economic and demographic assumptions, including those in the following table:

Social Security Intermediate Assumptions

Year	Total Fertility Rate[1]	Age-Sex-Adjusted Death Rate[2] (per 100,000)	Period Life Expectancy at Birth[3]		Net Annual Immigration (Persons per Year)	Real-Wage Differential[4] (Percentage Points)	Average Annual Percentage Change In:			Average Annual Interest Rate[7]
			Male	Female			Average Annual Wage in Covered Employment	CPI[5]	Real GDP[6]	
2001	2.06	796.5	74.0	79.6	840,000	1.9	4.9	3.0	3.1	5.6%
2005	2.04	773.7	74.6	80.0	900,000	1.2	4.4	3.2	2.3	6.2%
2010	2.02	751.1	75.3	80.3	900,000	1.0	4.3	3.3	2.0	6.3%
2020	1.97	701.7	76.4	81.1	900,000	1.0	4.3	3.3	1.7	6.3%
2030	1.95	649.4	77.3	81.9	900,000	1.0	4.3	3.3	1.7	6.3%
2040	1.95	603.3	78.2	82.6	900,000	1.0	4.3	3.3	1.7	6.3%
2050	1.95	562.6	79.0	83.3	900,000	1.0	4.3	3.3	1.6	6.3%
2060	1.95	526.6	79.8	84.0	900,000	1.0	4.3	3.3	1.6	6.3%
2070	1.95	494.5	80.5	84.7	900,000	1.0	4.3	3.3	1.6	6.3%

[1]The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The ultimate total fertility rate is assumed to be reached in 2025.

[2]The age-sex-adjusted death rate is the crude rate that would occur in the enumerated total population as of April 1, 1990, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

[3]The period life expectancy for a group of persons born in a given year is the average that would be attained by such persons if the group were to experience in succeeding years the death rates by age observed in, or assumed for, the given year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

[4]The real-wage differential is the difference between the percentage increases, before rounding, in the average annual wage in covered employment, and the average annual CPI.

[5]The CPI is the annual average value for the calendar year of the CPI for Urban Wage Earners and Clerical Workers (CPI-W).

[6]The real GDP is the value of total output of goods and services, expressed in 1996 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

[7]The average annual interest rate is the average of the nominal interest rates, which, in practice, are compounded semiannually, for special-issue Treasury obligations sold only to the trust funds in each of the 12 months of the year.

Present value amounts attempt to demonstrate what future cashflow amounts would be if shown in interest discounted dollars. This is done by discounting, or removing, the increase in these cashflows that is caused by interest. Even small changes in the estimated amount of future interest over the next 75 years have dramatic impact on present value calculations. Given the cashflow estimates between the high and low interest-rate assumptions, the present value of OASDI expenditures over income ranges from $6,125 billion to $3,025 billion using ultimate annual real interest rates of 2.2 percent to 3.7 percent, respectively, compared to $4,207 billion using the intermediate ultimate annual real interest rate of 3.0 percent. These interest rate assumptions do not influence the future cashflow in the OASDI program. If these charts were presented in nominal dollars, they would reflect a pattern similar to the present value charts shown here.

Charts of cashflows with varying assumptions that have not been adjusted for interest, as well as other assumptions that are not expected to have a material impact on OASDI, can be found in Social Security's Performance and Accountability Report and on the web at **www.ssa.gov/finance**.

These assumptions and the other values on which these displays are based reflect the intermediate assumptions of the 2001 Trustees' Report. Estimates made in certain prior years have changed substantially because of revisions to the assumptions based on changed conditions or experience, and to changes in actuarial methodology. It is reasonable to expect more changes for similar reasons in future reports.

Death Rates

The assumptions regarding future death rates have a substantial impact on estimated future cashflows in the OASDI program. The following table shows the present values of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about future reductions in death rates. The analysis was developed by varying the percentage decrease assumed to occur during 2000-2075 in death rates by age, sex, and cause of death. The decreases assumed for this period, summarized as average annual reductions in the age-sex-adjusted death rate, are 0.26, 0.68, and 1.23 percent per year, where 0.68 percent is the intermediate assumption in the 2001 Trustees' Report. (The resulting cumulative decreases in the age-sex-adjusted death rate during the same period are 17, 40 and 60 percent, respectively.) These assumptions do not apply uniformly to all ages. Some variation by age was assumed in recognition of historical patterns and to ensure that, in terms of the financial status of the OASDI program, estimates based on the summarized 0.26 percent and 1.23 percent reduction assumptions would be more optimistic and more pessimistic, respectively, than those based on the intermediate assumption.

As the following table demonstrates, if the reduction in death rate is changed from 0.68 percent, the Trustees' intermediate assumption, to 0.26 percent, meaning that people die younger, then the shortfall for the period of estimated OASDI income relative to expenditures would decrease to $2,980 billion from $4,207 billion; if the reduction is changed to 1.23 percent, meaning that people live longer, then the shortfall would increase to $5,574 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Death Rate Assumptions
Valuation Period: 2001-2075

Average Annual Reduction in Death Rates	0.26%	0.68%	1.23%
Expenditures in excess of income (In billions of present-value dollars)	$2,980	$4,207	$5,574

Real-Wage Differential

The following table shows the present value of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about the ultimate real-wage differential. These assumptions are that the ultimate real-wage differential will be 0.5, 1.0, and 1.5 percentage points, where 1.0 percentage point is the intermediate assumption in the 2001 Trustees' Report. The real-wage differential is the difference between the percentage increases in (1) the average annual wage in OASDI covered employment and (2) the average annual CPI. In each case, the ultimate annual increase in the CPI is assumed to be 3.3 percent (as used in the intermediate assumptions), yielding ultimate percentage increases in the average annual wage in covered employment of 3.8, 4.3, and 4.8 percent, respectively.

As the following table demonstrates, if the ultimate real-wage differential is changed from 1.0 percentage point, the Trustees' intermediate assumption, to 0.5 percentage point, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to $4,660 billion from $4,207 billion; if the ultimate real-wage differential was changed from 1.0 to 1.5 percentage points, then the shortfall would decrease to $3,559 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate Real-Wage Assumptions
Valuation Period: 2001-2075

Ultimate percentage change in wages, CPI	3.8% - 3.3%	4.3% - 3.3%	4.8% - 3.3%
Expenditures in excess of income (In billions of present-value dollars)	$4,660	$4,207	$3,559

Differences among the estimates of annual net cashflow based on the three assumptions about the ultimate real-wage differential become apparent early in the projection period. Higher real-wage differentials increase both wages and initial benefit levels. Because the effects on wages and, therefore, on payroll taxes are immediate, while the effects on benefits occur with a substantial lag, annual net cashflow is higher (less negative in later years) for higher assumed real-wage differentials. In the early years, when the effects on benefits are quite small and while the effects on wages are compounding, the patterns of the estimates of annual net cashflow based on the three assumptions diverge fairly rapidly.

Total Fertility Rate

The following table shows the present value of the estimated excess of OASDI expenditures over income for the 75-year period, using various assumptions about the ultimate total fertility rate. These assumptions are 1.7, 1.95, and 2.2 children per woman, where 1.95 is the intermediate assumption in the 2001 Trustees' Report. The total fertility rate is assumed to change gradually from its current level and to reach the selected ultimate value in 2025.

As the following table demonstrates, if the ultimate total fertility rate is changed from 1.95 children per woman, the Trustees' intermediate assumption, to 1.7, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to $4,636 billion from $4,207 billion; if the ultimate total fertility rate was changed to 2.2, then the shortfall would decrease to $3,737 billion.

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate Total Fertility Rate Assumptions Valuation Period: 2001-2075

Ultimate total fertility rate (children per woman)	1.7	1.95	2.2
Expenditures in excess of income (In billions of present-value dollars)	$4,636	$4,207	$3,737

Consumer Price Index

The following table shows the present value of the estimated OASDI expenditures in excess of income for the 75-year period, using various assumptions about the ultimate rate of change in the CPI. These assumptions are that the ultimate annual increase in the CPI will be 2.3, 3.3, and 4.3 percent, where 3.3 percent is the intermediate assumption in the 2001 Trustees' Report. In each case, the ultimate real-wage differential is assumed to be 1.0 percentage point (as used in the intermediate assumptions), yielding ultimate percentage increases in average annual wages in covered employment of 3.3, 4.3, and 5.3 percent, respectively.

As the following table demonstrates, if the ultimate annual increase in the CPI is changed from 3.3 percent, the Trustees' intermediate assumption, to 2.3 percent, then the shortfall for the period of estimated OASDI income relative to expenditures would increase to $4,537 billion from $4,207 billion; if the ultimate annual increase in the CPI was changed to 4.3 percent, then the shortfall would decrease to $3,863 billion. This seemingly counter-intuitive result—that higher CPI increases result in decreased shortfalls, and vice versa—occurs because varying CPI increases while retaining the same annual real-wage differentials affect earnings (and, therefore, taxes) sooner than benefits (and, therefore, expenditures).

Present Value of Estimated OASDI Expenditures in Excess of Income with Various Ultimate CPI-Increase Assumptions Valuation Period: 2001-2075

Ultimate percentage change in wages, CPI	3.3% - 2.3%	4.3% - 3.3%	5.3% - 4.3%
Expenditures in excess of income (In billions of present-value dollars)	$4,537	$4,207	$3,863

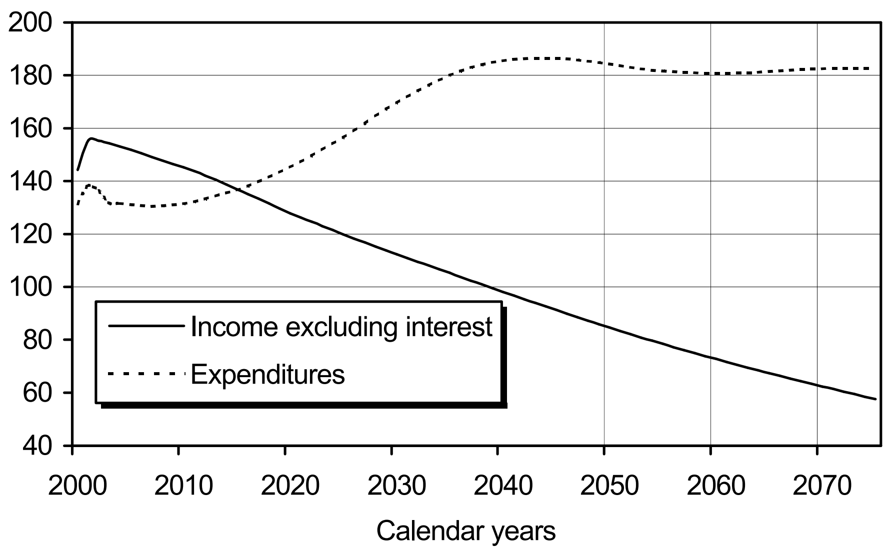
Hospital Insurance Medicare Part A

Federal Hospital Insurance (Medicare Part A) Trust Fund revenue consists primarily of taxes on earnings paid by employees, their employers, and the self-employed. The fund also receives revenue from part of the taxation of Social Security benefits and from interest on its investments in Treasury securities. Revenues not needed to pay current benefits of the Medicare Part A program or administrative expenses are invested in special issue Treasury securities.

The present values of actuarial estimates were computed as of the beginning of the valuation period, January 1, 2001. The contributions consist of the sum of the present value of various program income items expected to be received through fiscal 2075. The expenditure consists of the sum of the present value of estimated payments through fiscal 2075, claims incurred through September 30, 2001 that were unpaid as of that date, and administrative expenses related to those claims. Under intermediate assumptions from the 2001 Trustees' Report, and based on current legislation in place, the fund is projected to be exhausted in calendar year 2029.

Chart 5—Present Value of Estimated Medicare Part A Income (Excluding Interest) and Expenditures 2000-2075

(In billions of dollars)

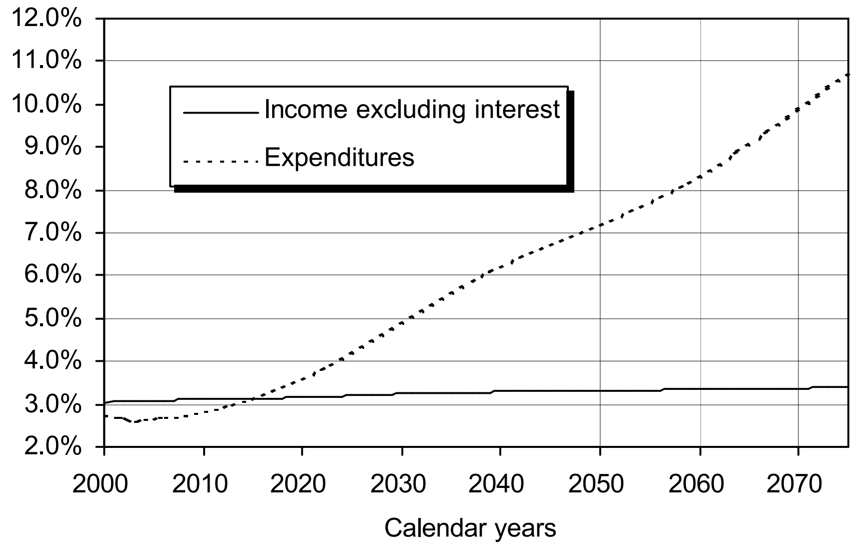


Medicare Part A Cashflow as a Percent of Taxable Payroll

Each year, estimates of the financial and actuarial status of the Medicare Part A program are prepared for the next 75 years. Because of the difficulty in comparing dollar values for different periods without some type of relative scale, income and expenditure amounts are shown relative to the earnings in covered employment that are taxable under the Medicare Part A program (referred to as "taxable payroll").

Chart 6 illustrates income excluding interest and expenditures as a percent of taxable payroll over the next 75 years. Although the long-range financial outlook for the Medicare Part A program has improved substantially in recent years because of the Balanced Budget Act of 1997, favorable economic conditions, and efforts to curb fraud and abuse, the program remains seriously underfunded through 2075. This is due in part to health care cost increases that exceed wage growth; a more significant cause, however, is the impending retirement of those born during the 1945-1965 baby boom.

Chart 6—Estimated Medicare Part A Income (Excluding Interest) and Expenditures as a Percentage of Taxable Payroll 2000-2075

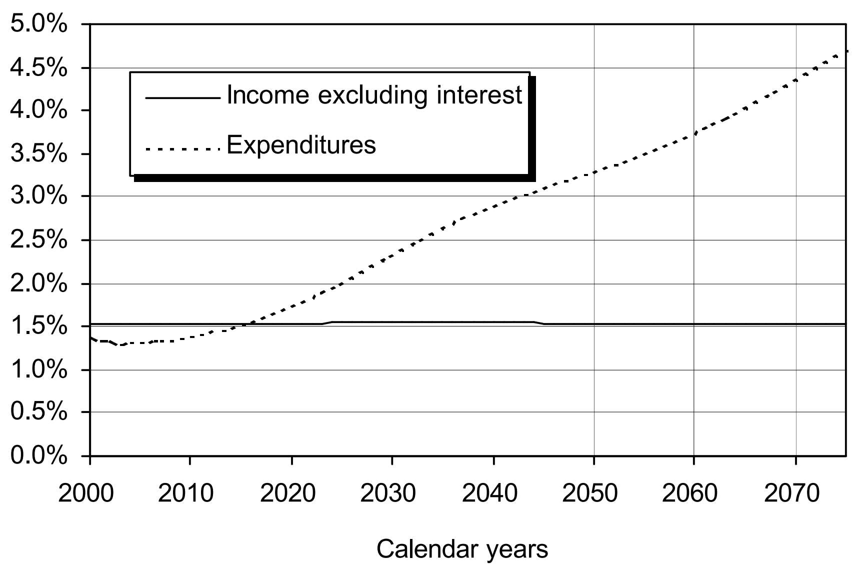


Medicare Part A Cashflow as a Percent of Gross Domestic Product (GDP)

Expressing Medicare-incurred disbursements as a percentage of GDP gives a relative measure of the size of the Medicare program compared to the general economy. GDP represents the total value of goods and services produced in the United States. This measure provides an idea of the relative financial resources that will be necessary to pay for Medicare services.

Chart 7 shows income excluding interest and expenditures for the Medicare Part A program over the next 75 years expressed as a percentage of GDP. In 2000, the expenditures were $131.1 billion, which was 1.32 percent of GDP. This percentage increases steadily throughout the entire 75-year period.

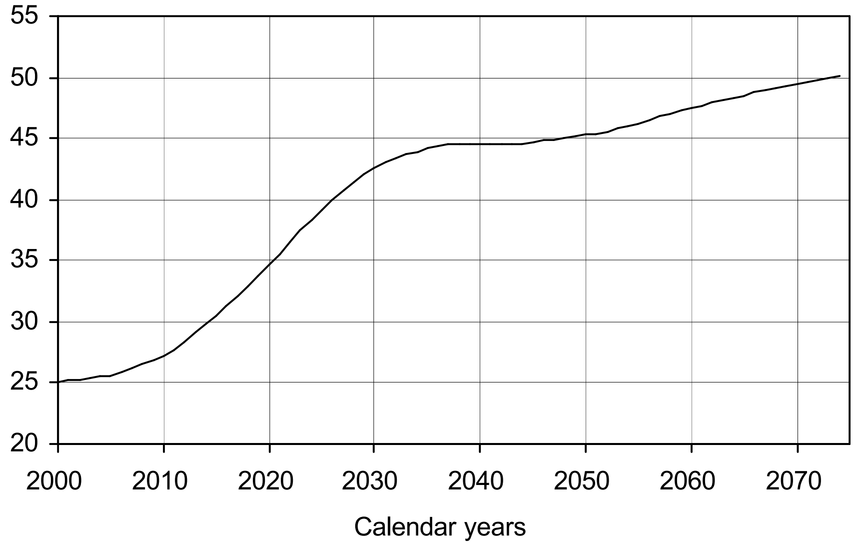
Chart 7—Estimated Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 2000-2075



Worker-to-Beneficiary Ratio

Another way to evaluate the long-range outlook of the Medicare Part A program is to examine the projected number of Medicare Part A beneficiaries per 100 covered workers. Chart 8 illustrates this ratio over the next 75 years. For the most part, current benefits are paid for by current workers. The retirement of the baby boom generation will therefore be financed by the relatively smaller number of persons born after the baby boom. In 2000, a group of 100 workers provided benefits for 25 beneficiaries. In 2030, however, after the last baby boomer turns 65, a group of 100 workers will provide benefits to 43 beneficiaries. The projected ratio continues to increase until there will be 50 beneficiaries per 100 workers in 2075.

Chart 8—Number of Medicare Part A Beneficiaries per 100 Covered Workers 2000-2075



Actuarial Assumptions and Sensitivity Analysis

In order to make projections regarding the future financial status of the Medicare Part A and Medicare Part B programs, various assumptions have to be made. First and foremost, the estimates presented here are based on the assumption that the programs will continue under present law. In addition, the estimates depend on many economic and demographic assumptions, including changes in wages and the CPI, fertility rates, immigration rates, and interest rates. In most cases, these assumptions vary from year to year during the first 5 to 30 years before reaching their ultimate values for the remainder of the 75-year projection period.

The following chart and amounts are presented for analysis of the major assumptions impacting estimates in Medicare's future cashflows. Present value amounts attempt to demonstrate what future cashflow amounts would be if shown in today's dollars. This is done by discounting, or removing, the increase in these cashflows that is caused by interest, sometimes referred to as inflation. Even small changes in the estimated amount of future interest over the next 75 years have dramatic impact on present value calculations. Given the cashflow assumptions between the highest and lowest expected interest assumptions, the present value of Medicare Part A expenditures over income ranges from $7,003 billion to $3,372 billion using interest rates of 2.2 percent to 3.7 percent, respectively.

Charts of cashflows with varying assumptions that have not been adjusted for interest, as well as other assumptions that are not expected to have a material impact on Medicare, can be found in the Centers for Medicare & Medicaid Services' (CMS) Performance and Accountability Report and on the web at **www.cms.gov**.

The following table shows some of the underlying assumptions used in the projections of Medicare spending displayed in this report. Further details on these assumptions are available in the OASDI, Medicare Part A, and Medicare Part B Trustees' Reports for 2001.

Medicare Intermediate Assumptions

Year	Fertility Rate[1]	Net Immigration	Real Wage Differential[2]	Annual Percentage Change in: Wages	CPI	Real GDP	Real Interest Rate[3]
2001	2.05	900,000	1.9	4.9	3.0	3.1	2.6
2005	2.04	900,000	1.2	4.4	3.2	2.3	2.9
2010	2.02	900,000	1.0	4.3	3.3	2.0	3.0
2020	1.97	900,000	1.0	4.3	3.3	1.7	3.0
2030	1.95	900,000	1.0	4.3	3.3	1.7	3.0
2040	1.95	900,000	1.0	4.3	3.3	1.7	3.0
2050	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2060	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2070	1.95	900,000	1.0	4.3	3.3	1.6	3.0
2075	1.95	900,000	1.0	4.3	3.3	1.6	3.0

[1] Average number of children per woman.
[2] Difference between percentage increase in wages and the CPI.
[3] Average rate of interest earned on new trust fund securities, above and beyond rate of inflation.

Estimates made in prior years have changed substantially sometimes because of revisions to the assumptions, which are due either to changed conditions or to more recent experience. Furthermore, it is important to recognize that actual conditions are very likely to differ from the projections presented here, since the future cannot be anticipated with certainty. In order to illustrate the magnitude of the sensitivity of the long-range projections, three of the key assumptions were varied individually to determine the impact on the Medicare Part A actuarial present values and net cashflow. The assumptions varied were health care cost factors, the fertility rate, and real-wage differential.

The sensitivity of the projected Medicare Part A net cashflow to variations in future mortality rates is also of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per-beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Medicare Part A mortality sensitivity. CMS is sponsoring a current research effort that is expected to provide the information necessary to produce such estimates.

For this analysis, the intermediate economic and demographic assumptions in the *2001 Annual Report of the Board of Trustees of the Federal Hospital Insurance Trust Fund* are used as the reference point. Each selected assumption is varied individually to produce three scenarios. All present values are calculated as of January 1, 2001, and are based on estimates of income and expenditures during the 75-year projection period.

Health Care Costs

The following table shows the net present value of cashflow during the 75-year projection period under three alternative assumptions of the annual growth rate in the aggregate cost of providing covered health care services to beneficiaries. These assumptions are that the ultimate annual growth rate in such costs, relative to taxable payroll, will be 1 percent slower than the intermediate assumptions, the same as the intermediate assumptions, and 1 percent faster than the intermediate assumptions. In each case, the taxable payroll will be the same as that which was assumed for the intermediate assumptions.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Health Care Cost Assumptions			
Annual cost/payroll relative growth rate	-1 percentage point	Intermediate assumptions	+1 percentage point
Expenditures in excess of income (In billions of present-value dollars)	$811	$4,730	$11,155

Under the low cost assumption, the annual absolute change in aggregate cost is equal to the intermediate assumption less 1 percent of the contemporaneous increase in taxable payroll. The above table demonstrates that if the ultimate growth rate assumption is 1 percentage point lower than the intermediate assumptions, the deficit of income over expenditures decreases from $4,730 to $811. Under the high cost assumption, the annual absolute change in aggregate cost is equal to the intermediate assumption plus 1 percent of the contemporaneous increase in taxable payroll. If the ultimate growth rate assumption is 1 percentage point higher than the intermediate assumptions, the deficit increases substantially to $11,155 billion.

Fertility Rate

The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The table below shows the net present value of cashflow during the 75-year projection period under three alternative ultimate fertility rate assumptions: 1.7, 1.95, and 2.2 children per woman.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Fertility Rate Assumptions			
Ultimate fertility rate	1.7	1.95	2.2
Expenditures in excess of income (In billions of present-value dollars)	$4,878	$4,730	$4,569

The table above demonstrates that if the assumed ultimate fertility rate is decreased from 1.95 to 1.7, the projected deficit of income over expenditures increases from $4,730 billion to $4,878 billion. On the other hand, if the ultimate fertility rate is increased from 1.95 to 2.2 children per woman, the deficit decreases to $4,569 billion.

Real-Wage Differential

The following table shows the net present value of cashflow during the 75-year projection period under three alternative ultimate real-wage differential assumptions: 0.5, 1.0, and 1.5 percentage points. In each case, the CPI is assumed to be 3.3 percent, yielding ultimate percentage increases in average annual wages in covered employment of 3.8, 4.3, and 4.8 percent, respectively.

Present Value of Estimated Medicare Part A Expenditures in Excess of Income under Various Real-Wage Assumptions			
Ultimate percentage increase in wages – CPI	3.8% - 3.3%	4.3% - 3.3%	4.8% - 3.3%
Ultimate percentage increase in real-wage differential	0.5%	1.0%	1.5%
Expenditures in excess of income (In billions of present-value dollars)	$4,988	$4,730	$4,539

The above table demonstrates that if the ultimate real-wage differential assumption is decreased from 1.0 percentage point to 0.5 percentage point, the deficit of income over expenditures increases from $4,730 billion to $4,988 billion. On the other hand, if the ultimate real-wage differential assumption is increased from 1.0 percentage point to 1.5 percentage points, the deficit decreases to $4,539 billion.

Federal Supplementary Medical Insurance Medicare Part B

The Medicare Part B program differs fundamentally from the Medicare Part A program by the way it is financed. In particular, Medicare Part B financing is not based on payroll taxes; instead, it is based on monthly premiums and income from the general fund of the U.S. Treasury. General fund transfers account for approximately 75 percent of the Medicare Part B Trust Fund's income.

Since the income to the Medicare Part B Trust Fund from beneficiary premiums and the general fund is adjusted annually to match expected costs, the trust fund is always in actuarial balance. By law, Medicare Part B income and expenditures will continue to be virtually the same. However, as shown in the trust fund illustration on page 61, transfers from the general fund of the U.S. Treasury draw from the same resources as any other social insurance program that is experiencing a negative cashflow. Moreover, the general fund transfers occur from one account of the Government to another and do not represent an external, earmarked source of tax or other revenue. Therefore, for the purposes of this report, with the objective of presenting the financial operations of these programs from a Governmentwide consolidated perspective, transfers from the general fund of the Treasury are excluded. This is the same reason that interest earned on Treasury securities is eliminated for this and all other social insurance programs—again, because such payments represent intragovernmental transfers.

The elimination of this major revenue source to the Medicare Part B Trust Fund produces information that appears to be significantly different from that presented in CMS's Annual Performance and Accountability Report, as well as the annual Trustees' Report on the Medicare Part B Trust Fund. From the perspective of the financial status of the Medicare Part B Trust Fund (as shown in the CMS financial statement and the Trustees' report), it is appropriate to consider all sources of income to the fund. Thus, the accounting treatment of Medicare Part B general revenues (and trust fund interest earnings) varies appropriately depending on whether an overall consolidated or trust fund perspective is shown.

Chart 9 shows the actuarial estimates of Medicare Part B premiums and disbursements for each of the next 75 years, in nominal dollars. Income includes monthly premiums paid by, or on behalf of, beneficiaries. Disbursements include benefit payments as well as administrative expenses.

Estimated Medicare Part B Premiums and Expenditures

Chart 9—Medicare Part B Income, Premiums, and Expenditures 2000-2075

(In billions of dollars)

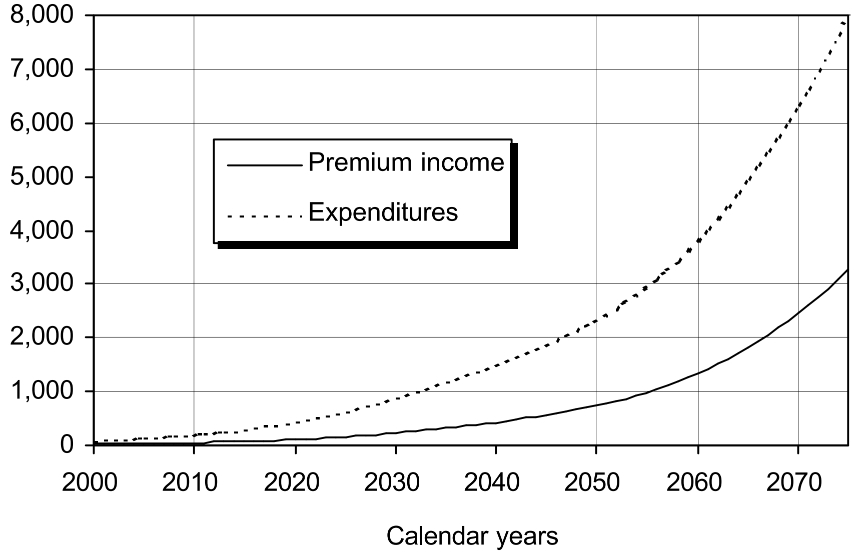
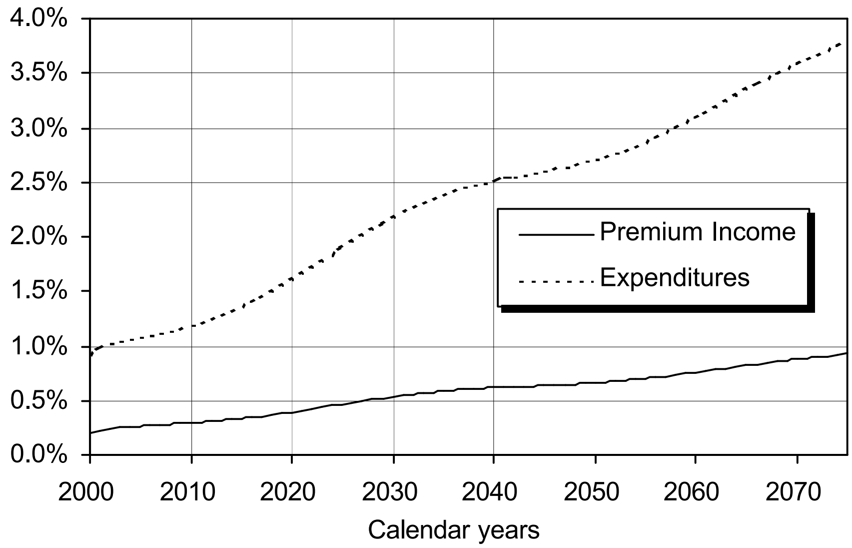


Chart 10 shows expenditures for the Medicare Part B program over the next 75 years expressed as a percentage of GDP. In 1999, Medicare Part B expenditures were $90.7 billion, which was 0.92 percent of GDP. This percentage is projected to increase steadily through 2035, reflecting growth in the price, use, and intensity of Medicare Part B services that is expected to exceed GDP growth for many years, together with the effects of the baby boom retirement. After 2035, it levels off because Medicare Part B projections by assumption are tied directly to GDP plus 1 percentage point, and because relatively fewer number of persons born after the baby boom will be eligible for Medicare Part B benefits. Medicare Part B premium increases during the initial 25-year period are assumed to decline gradually in the last 12 years to the same rate as GDP per capita plus 1 percentage point and then to continue at the same rate as GDP per capita plus one percentage point in the last 50 years.

Chart 10—Estimated Medicare Part B Premiums and Expenditures as a Percent of GDP 2000-2075



Estimated Medicare Part B Premiums and Expenditures

The Medicare Part B program's actuarial assumptions are the same as those used in Medicare Part A, presented on pages 71-72. Since the unique funding mechanism of Medicare Part B allows its trust fund to remain in actuarial balance, the data on various sensitivity analyses are not routinely compiled. It is planned that future editions of the *Financial Report* will regularly contain this information.

Railroad Retirement

Railroad retirement pays full annuities when eligible persons reach full retirement age with 10 years of service or age 62 with 30 years of service. It pays reduced annuities to eligible beneficiaries who are age 62 with 10 to 29 years of service, or age 60 with 30 years of service (See subsequent event, last paragraph). The Railroad Retirement program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as Social Security beneficiaries.

The Railroad Retirement Board (RRB) and Social Security Administration (SSA) share jurisdiction over the payment of retirement and survivor benefits. RRB has jurisdiction over the payment of retirement benefits if the employee had at least 10 years of railroad service. Additionally, for survivor benefits, RRB requires that the employee's last regular employment before retirement or death was in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee's railroad retirement credits to SSA. SSA treats them as Social Security credits.

Payroll taxes paid by railroad employers and their employees provide the primary source of income for the Railroad Retirement Survivor Benefit program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: financial interchanges with the Social Security trust funds; interest on investments; Federal income taxes on railroad retirement benefits; and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits).

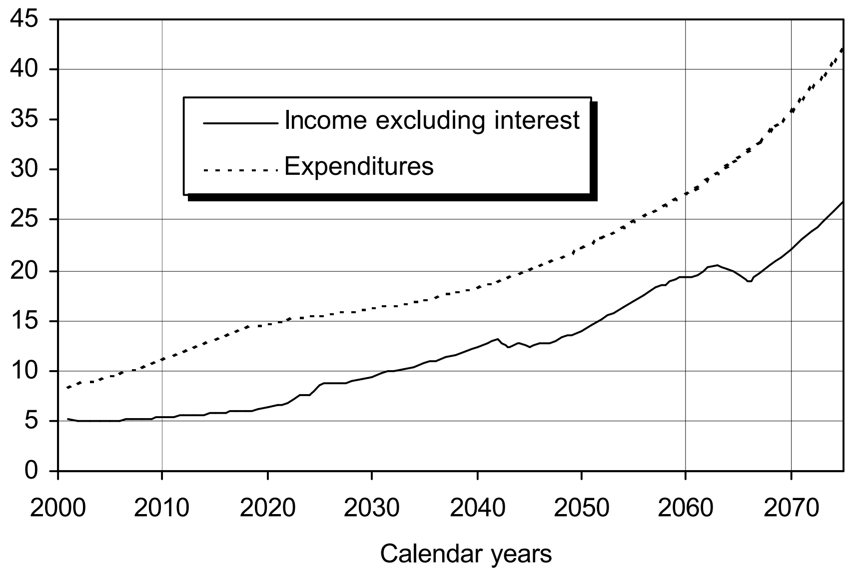
Subsequent event: On December 21, 2001, President Bush signed the "The Railroad Retirement and Survivors' Improvement Act of 2001" (RRSIA) into law. The new law enhances benefits and changes the funding of the retirement program.

Benefits of the RRSIA of 2001 include:

- Increases the widow(er)s benefits by providing a guaranteed minimum amount of benefits.
- Restores full annuities to employees and their spouses who retire at age 60, instead of 62, with 30 years of railroad service.
- The vesting period is also reduced from 10 to 5 years.
- Creates a new National Railroad Retirement Investment Trust (Trust) to administer a new Railroad Retirement Investment Trust Fund (RRIT Fund).
- A new nongovernmental financial institution ("Disbursing Agent") will serve as a disbursing agent for all benefits payable under the Railroad Retirement Act.

Chart 11—Estimated Railroad Retirement Income (Excluding Interest) and Expenditures 2000–2075

(In billions of dollars)



Railroad Retirement Program Actuarial Surplus or (Deficiency) [1,2]
Under Employment Assumption 2
75-Year Projection as of January 1, 2001

(In billions of present-value dollars)

Estimated future income [3] received from or on behalf of:	
Former employees and dependents	56.7
Current employees and dependents	57.0
Future employees and dependents	28.6
All participants	142.3
Estimated future expenditures: [4]	
Former employees and dependents	80.6
Current employees and dependents	67.3
Future employees and dependents	12.9
All participants	160.8
Estimated future excess of income over expenditures	(18.5)

[1] Represents combined values for the Railroad Retirement Account, Social Security Equivalent Benefit Account and Railroad Retirement Supplemental Account.
[2] The data used reflect the provisions of the Railroad Retirement and Survivors' Improvement Act (RRSIA) of 2001. Comparable data for prior years is not available and would not be meaningful.
[3] Future income includes tier I taxes, tier II taxes, supplemental annuity taxes, income taxes on benefits, financial interchange income, advances from general revenues and repayments of advances from general revenues. The calculations assume that all future transfers required by current law under the financial interchange will be met.
[4] Future expenditures include benefit and administrative costs.

Note: Detail may not add to totals due to rounding. Employee and beneficiary status are determined as of 1/1/2000, whereas present values are as of 1/1/2001.

Estimated Expenditures in Excess of Income
with Intermediate Employment Assumption
Valuation Period 2001-2075

Average yearly employment at end of valuation period	111,000
Expenditures in excess of income (In billions of nominal dollars)	18.5

The average railroad employment is assumed to be 246,000 in 2000. The employment assumption, which is based on a model developed by the Association of American Railroads, assumes that (1) passenger employment will remain at the level of 46,000, and (2) the employment base, excluding passenger employment, will decline at a constant 3.0 percent annual rate for 25 years, at a reducing rate over the next 25 years, and remain level thereafter.

Black Lung (Part C)

The Black Lung Disability program compensates eligible coal miners who are disabled because of employment-related pneumoconiosis (black lung disease). The program provides both medical and survivor benefits. Under Part C, the Black Lung Disability Trust Fund (BLDTF) provides benefit payments to eligible disabled miners when no responsible mine operator can be assigned the liability. The Department of Labor (DOL) administers Part C of the Black Lung Disability Benefits program.

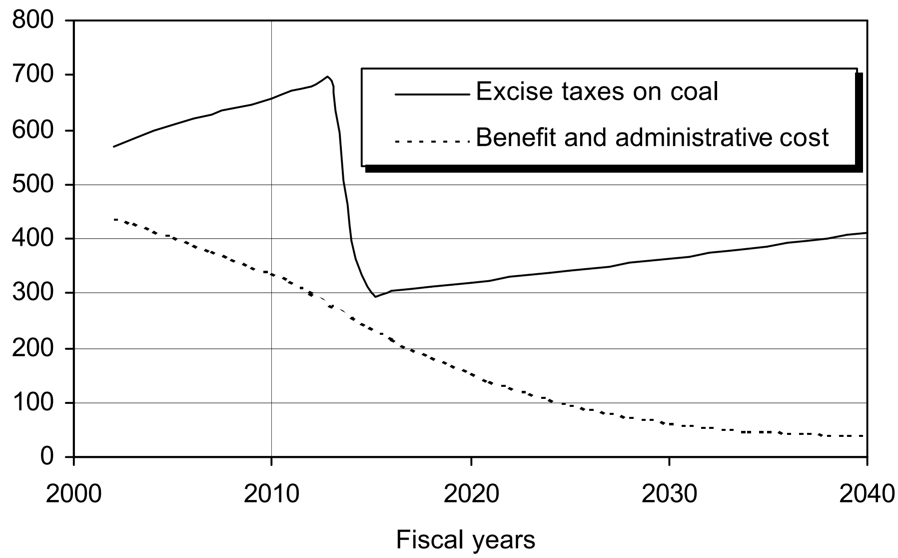
Excise taxes on coal mine operators, based on the sale of coal, partially fund the black lung disability payments and the related administrative and interest costs. Intragovernmental advances to the BLDTF, which must be repaid with interest, fund the shortfall.

Under current conditions, analysts project that scheduled reduction in taxes on coal sales will decrease cash inflows for the year 2014 and beyond. Between the years 2013 and 2015, projections estimate a 54 percent decrease in excise tax collections. By the year 2040, the rate reduction is expected to decrease cash inflows by a total of more than $12.9 billion.

Chart 12 shows the estimated Black Lung expenditures (excluding interest payments) and excise tax collections for the period 2002 through 2040. Under the intermediate assumptions for the next 39 years, the Black Lung Trust Fund will collect $17.2 billion in excise taxes on coal and pay $7.3 billion for benefits and administrative costs. However, this favorable cashflow will not be sufficient to repay the intragovernmental debt that resulted from previous deficits. Currently this debt is $7.2 billion. Cumulative net cash outflows including interest payments on the debt are projected to reach $43.1 billion by the year 2040, increasing the debt to $50.3 billion on September 30, 2040.

Chart 12—Estimated Black Lung Expenditures and Excise Tax Collections 2002-2040

(In millions of dollars)



Unemployment Insurance

The Unemployment Insurance program was created in 1935 to provide temporary, partial wage replacement to unemployed workers who lost their jobs. The program is administered through a unique system of Federal and State partnerships, established in Federal law, but executed through conforming State laws by State officials. The Department of Labor provides broad policy guidance and program direction, while program details such as benefit eligibility, duration and amount of benefits are established through individual State unemployment insurance statutes and administered through State unemployment insurance agencies.

The program is financed through the collection of Federal and State unemployment taxes that are deposited in the Unemployment Trust Fund and reported as Federal tax revenue. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for Federal and State administration of the unemployment insurance program, veterans' employment services, State employment services, and the Federal share of extended unemployment insurance benefits. Federal unemployment taxes also are used to maintain a loan account within the Unemployment Trust Fund, from which insolvent States may borrow funds to pay benefits.

Estimated Unemployment Trust Fund Contributions and Expenditures September 30, 2002 – September 30, 2011 (Expected Economic Conditions)

Contributions to September 30, 2011	386.1
Expenditures to September 30, 2011	405.0
Expenditures in excess of contributions (In billions of nominal dollars)	18.9

Charts 13 through 15 demonstrate the effect on accumulated Unemployment Trust Fund assets of projected total cash inflows and cash outflows over a 10-year period ending September 30, 2011, under expected economic conditions, and mild recessionary and deep recessionary unemployment scenarios. Each scenario uses an open group that includes current and future participants of the Unemployment Insurance programs.

For expected economic conditions, the estimates are based on an expected unemployment rate of 4.78 percent during fiscal 2002, decreasing to 4.60 percent in fiscal 2005 and thereafter. Under the mild recessionary scenario, the expected unemployment rate will peak at 7.43 percent in fiscal 2004, and for the deep recession scenario the expected unemployment rate will rise to 10.15 percent in fiscal 2005.

Chart 13—Estimated Unemployment Fund Cashflow Using Expected Economic Conditions 2002-2011

(In billions of dollars)

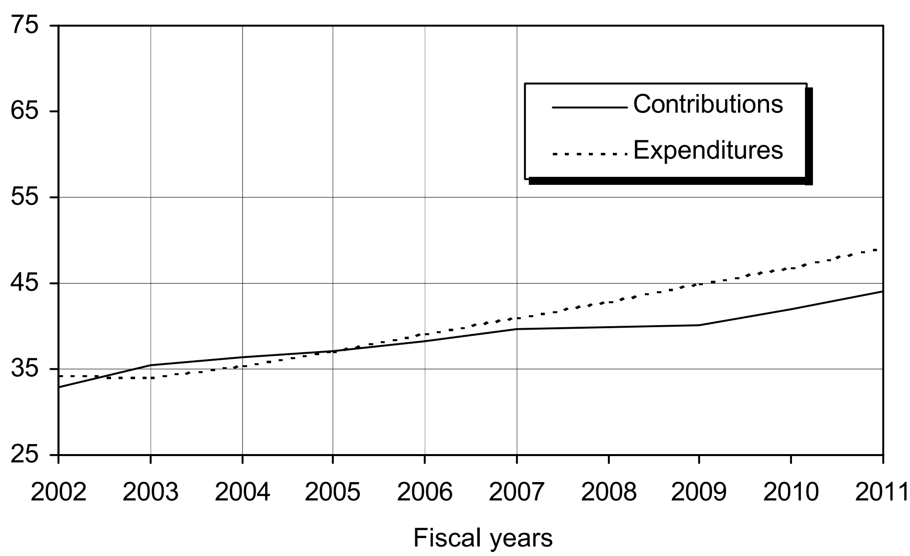


Chart 14—Estimated Unemployment Fund Cashflow Using a Mild Recessionary Unemployment Rate 2002-2011

(In billions of dollars)

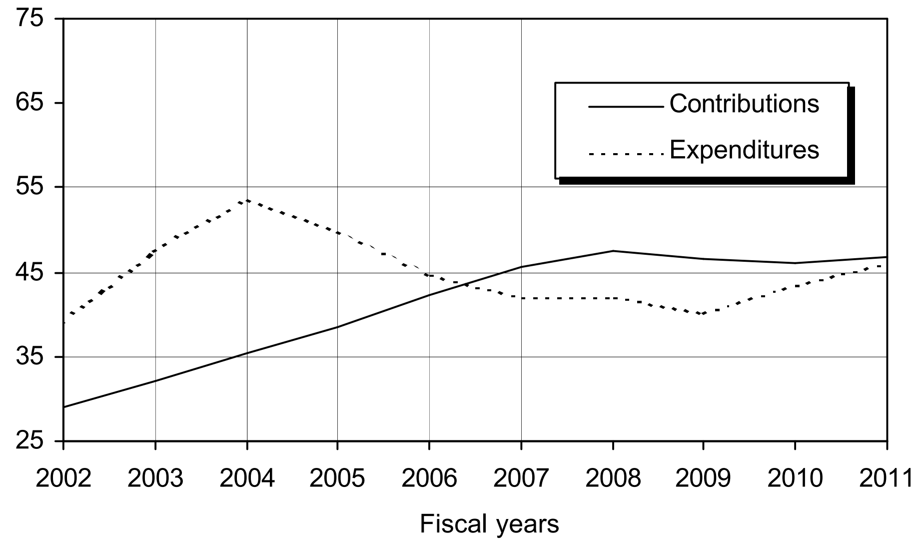
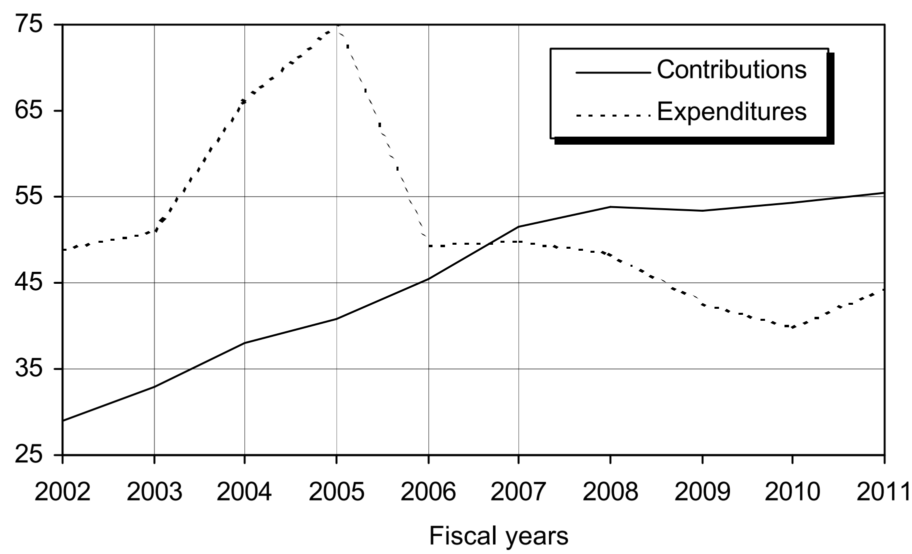


Chart 15—Estimated Unemployment Fund Cashflow Using a Deep Recessionary Unemployment Rate 2002-2011

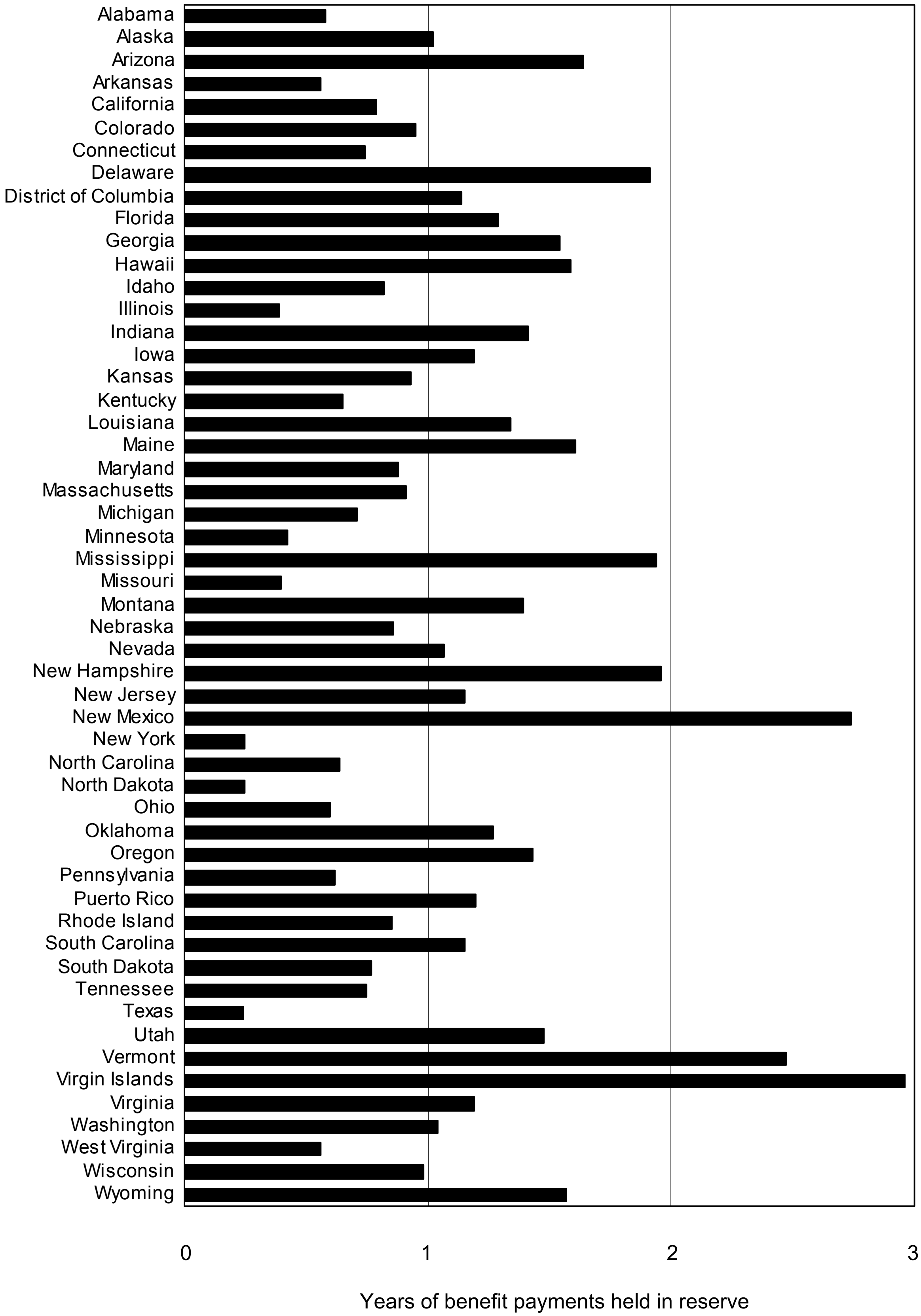
(In billions of dollars)



Unemployment Trust Fund Solvency

Chart 16 shows the adequacy of each State's accumulated Unemployment Trust Fund assets to provide for future unemployment benefits. To be considered minimally solvent, a State's reserve balance should provide for one year's projected benefit payment needs based on the highest level of benefit payments experienced by the State.

Chart 16—Unemployment Trust Fund Solvency



Stewardship Investments

"Stewardship Investments" focus on Government programs aimed at providing long-term benefits by improving the Nation's productivity and enhancing economic growth. These investments can be provided through direct Federal spending or grants to State and local governments for certain education and training programs, research and development, and federally financed but not federally owned property, such as bridges and roads. When incurred, these investments are included as expenses in determining the net cost of operations.

Stewardship Investments for the Years Ended September 30

(In billions of dollars)	Fiscal 2001	Restated Fiscal 2000	Restated Fiscal 1999
Investments in non-Federal physical property	45.3	44.5	38.4
Investments in human capital	50.8	42.8	46.3
Research and development:			
Investments in basic research	19.9	18.6	17.2
Investments in applied research	18.9	16.7	16.5
Investments in development	40.7	39.0	41.3
Total investments	175.6	161.6	159.7

Non-Federal Physical Property

The Government makes grants and provides funds for the purchase, construction, and/or major renovation of State and local government physical properties. Cost for non-Federal physical property programs are included as expenses in the Statements of Net Cost and are reported as investments in the table above. They are measured on the same accrual basis of accounting used in the *Financial Report* statements.

Human Capital

The Government runs several programs that invest in human capital. Those investments go toward increasing and maintaining a healthy economy by educating and training the general public. Costs do not include training expenses for Federal workers.

Research and Development

Federal investments in research and development comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other future benefits.

- Investments in basic research are for systematic studies to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind.
- Investments in applied research are for systematic studies to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met.

- Investments in development are the systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems, or methods, including the design and development of prototypes and processes.

Current Services Assessment

The Current Services Assessment table shows the Office of Management and Budget's (OMB's) estimate of budget receipts, outlays, and surplus or deficit if no changes were made to laws that are already enacted. Receipts and mandatory outlays, such as Social Security benefits and net interest, involve ongoing activities that generally operate under permanent legal authority authorized by legislation. The current services estimates of receipts and mandatory spending assume that receipts and mandatory spending continue in the future as specified by current laws. The current services estimates for discretionary spending assume discretionary funding for fiscal 2002 equals appropriations enacted by Congress. It also assumes that discretionary funding for subsequent years holds constant in real terms. Because laws already enacted provide the bases for current services estimates, they do not constitute a proposed budget, nor do they predict the most likely budget outcomes.

The current services estimates may be used to help assess the sustainability of programs under current law. That is, they may be used to project whether future resources can sustain public services and meet obligations as they come due. In this way, they can warn of future problems inherent in current law. They also can provide a benchmark against which tax and spending proposals can be compared and the magnitude of proposed changes can be assessed. Moreover, they can provide an analytical perspective of Government by showing the short- and medium-term direction of current programs.

The following schedule presents the actual budget results for fiscal 2002 and the current services estimates for all Federal taxes and spending programs for the subsequent 6 years. It shows receipts by source and outlays by function. The estimates for these years are the same as the current services estimates published in the President's budget for fiscal 2003. They are, therefore, based on the same underlying economic, programmatic, and other technical assumptions as the current services estimates in that document.

Current Services Assessment Receipt and Outlay Estimates as Presented in the President's Budget

(In billions of dollars)	Base Year 2001	Fiscal Year 2002	2003	2004	2005	2006	2007
Receipts by Source:							
Individual income taxes	994	950	1,009	1,064	1,120	1,167	1,233
Corporation income taxes	151	203	208	215	242	248	259
Social insurance and retirement receipts	694	708	750	792	839	872	914
Excise taxes	66	67	69	71	74	75	78
Other receipts	86	83	84	93	91	98	98
Total receipts	1,991	2,011	2,121	2,234	2,366	2,461	2,581
Outlays by Function:							
National defense	309	348	354	364	375	381	387
Social Security	433	460	476	495	519	546	575
Medicare	217	226	233	241	257	265	284
Income security	270	311	320	324	333	344	351
Health	173	195	231	253	270	290	311
Veteran benefits and services	46	52	56	58	63	63	62
Education, training, employment, and social services	57	72	79	81	82	83	85
Transportation	55	62	60	61	63	64	66
Other programmatic functions	153	173	175	182	179	180	184
Net interest	206	177	175	178	174	168	160
Undistributed offsetting receipts	(55)	(55)	(78)	(94)	(98)	(94)	(99)
Total outlays	1,864	2,020	2,080	2,142	2,218	2,289	2,366
Surplus or deficit (-)	127	(9)	41	92	148	172	215

Note: Details may not add to totals due to rounding.

This page is intentionally blank.

United States Government Notes to the Financial Statements for the Years Ended September 30, 2001 and September 30, 2000

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

This *Financial Report* includes the financial status and activities of the executive branch and most of the legislative branch, and the expenses of the judicial branch of the Government. This includes corporations that are part of the Government. The Appendix contains a list of significant Government entities included in these financial statements, as well as a partial list of entities excluded. The financial reporting period ends September 30 and is the same used for the annual budget.

Material intragovernmental transactions were eliminated in consolidation, except as described in Note 16—Unreconciled Transactions Affecting the Change in Net Position.

B. Basis of Accounting and Revenue Recognition

This *Financial Report* is based on Generally Accepted Accounting Principles (GAAP). These principles typically recognize:

- Expenses when incurred.
- Non-exchange (unearned) revenues on a modified cash basis of accounting. Non-exchange revenues arise primarily from the exercise of the Government's power to tax and levy duties, fines and penalties. Remittances of non-exchange revenue are recognized when received. Related receivables are recognized when measurable and legally collectible. Refunds and other offsets are recognized when measurable and legally payable and are netted against non-exchange revenue.
- Exchange (earned) revenues when earned. Exchange (earned) revenues arise when a Government entity provides goods and services to the public for a price. Earned revenue represents revenue earned from user charges, such as admission fees to Federal parks and insurance premiums that are recognized when the Government provides the goods or services.

This basis of accounting differs from that used for budgetary reporting, which is primarily on a cash basis according to accepted budget concepts and policies. (See "Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited" page 50.)

This Financial Report presents comparative fiscal 2000 data. Some balances previously reported for fiscal 2000 are restated. The ending net position for fiscal 2000 was restated from ($5,937.1) billion to ($5,945.4) billion. This change was the net of certain restatements of agencies' fiscal 2000 financial statements.

In fiscal 2001, two new financial statements were added: Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus (Unaudited) and Dispositions of the Budget Surplus (Unaudited). Both statements are unaudited for fiscal 2001.

New for fiscal 2001 is the implementation of SFFAS No. 10 (Accounting for Internal Use Software). Under the provisions of this statement, internal use software is classified as "general property, plant and equipment" as defined in SFFAS No. 6 (Accounting for Property, Plant and Equipment). This standard requires the capitalization of the cost of internal use software whether it is commercial (off-the-shelf), contractor-developed, or developed internally. The standard also provides guidance regarding the types of cost elements to capitalize, the timing thresholds, amortization periods, and other help.

C. Direct Loans and Loan Guarantees

Direct loans obligated and loan guarantees committed after fiscal 1991 are reported based on the present value of the net cashflows estimated over the life of the loan or guarantee. The difference between the outstanding principal of the loans and the present value of their net cash inflows is recognized as a subsidy cost allowance; the present value of estimated net cash outflows of the loan guarantees is recognized as a liability for loan guarantees. The subsidy expense for direct or guaranteed loans disbursed during a year is the present value of estimated net cash outflows for those loans or guarantees. A subsidy expense also is recognized for modifications made during the year to loans and guarantees outstanding and for reestimates made as of the end of the year to the subsidy allowances or loan guarantee liability for loans and guarantees outstanding.

Direct loans obligated and loan guarantees committed before fiscal 1992 are valued under two different methodologies within the Government: the allowance-for-loss method and the present-value method. Under the allowance-for-loss method, the outstanding principal of direct loans is reduced by an allowance for uncollectible amounts; the liability for loan guarantees is the amount the agency estimates would more likely than not require future cash outflow to pay default claims.

Under the present-value method, the outstanding principal of direct loans is reduced by an allowance equal to the difference between the outstanding principal and the present value of the expected net cashflows. The liability for loan guarantees is the present value of expected net cash outflows due to the loan guarantees.

D. Accounts and Taxes Receivable

"Accounts Receivable" represents claims to cash or other assets from entities outside the Government that arise from the sale of goods or services, duties, fines, certain license fees, recoveries, or other provisions of the law.

The category of "Taxes Receivable" consists primarily of uncollected tax assessments, penalties, and interest when taxpayers have agreed the amounts are owed, or a court has determined the assessments are owed. The Balance Sheets do not include unpaid assessments when neither taxpayers nor a court have agreed that the amounts are owed (compliance assessments) or the Government does not expect further collections due to factors such as the taxpayer's death, bankruptcy, or insolvency (writeoffs). Taxes receivable are reported net of an allowance for the estimated portion deemed to be uncollectible.

E. Inventories and Related Property

"Inventories" within the Government are valued using historical cost, net realizable value, and latest acquisition cost (see Note 6—Inventories and Related Property). Historical cost methods include first-in-first-out, weighted average, and moving average. Estimated repair costs reduce the value of inventory held for repair. Excess, obsolete, and unserviceable inventories are valued at estimated net realizable values. When latest acquisition cost is used to value inventory held for sale, it is adjusted for holding gains and losses in order to approximate historical cost.

The related property portion of the Inventory and Related Property line includes Operating Materials and Supplies, Stockpile Materials, Commodities, Seized and Monetary Instruments, and Forfeited Property. Operating Materials and Supplies are valued at historical cost, latest acquisition cost, and standard price using the consumption method of accounting. Operating Materials and Supplies that are valued at latest acquisition cost and standard pricing are not adjusted for holding gains and losses.

F. Property, Plant and Equipment

"Property, Plant and Equipment" used in Government operations are carried at cost. Depreciation and amortization expense applies to property, plant and equipment reported on the Balance Sheets except for land, unlimited duration land rights, and construction in progress. Depreciation is recognized using the straight-line method over the estimated useful lives of the assets. Refer to the Stewardship Information section for assets excluded in this section.

G. Federal Employee and Veteran Benefits Payable

Federal employee and veteran benefits payable are recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans and post-retirement health benefits are recorded at estimated present value of future benefits, less the estimated present value of future normal cost contributions.

Normal cost is the portion of the actuarial present value of projected benefits allocated as an expense for employee services rendered in the current year. Actuarial gains and losses (and prior and past service cost, if any) are recognized immediately in the year they occur, without amortization. Due to the effect of Public Law No. 106-398 (National Defense Authorization Act), TRICARE benefits are extended to veterans, and the present value of the future liability is an expense in the current year.

H. Environmental and Disposal Liabilities

"Environmental and Disposal Liabilities" are recorded at the estimated current cost of removing, containing and/or disposing of hazardous waste and environmental contamination, assuming the use of current technology. Hazardous waste is a solid, liquid, or gaseous waste that, because of its quantity or concentration, presents a potential hazard to human health or the environment. Remediation consists of removal, decontamination, decommissioning, site restoration, site monitoring, closure, and post-closure cost, treatment, and/or safe containment. Where technology does not exist to clean up hazardous waste, only the estimable portion of the liability, typically safe containment, is recorded.

I. Deferred Maintenance

"Deferred Maintenance" is maintenance that was not performed when it should have been or scheduled maintenance that was delayed or postponed. Maintenance is the act of keeping fixed assets in acceptable condition, including preventative maintenance, normal repairs, and other activities needed to preserve the assets, so they continue to provide acceptable services and achieve their expected life. Maintenance excludes activities aimed at expanding the capacity of assets or otherwise upgrading them to serve needs different from those originally intended. Deferred maintenance information is disclosed in the Supplemental Information to the Financial Statements.

Deferred maintenance expenses are not accrued in the Statements of Net Cost or recognized as liabilities on the Balance Sheets.

J. Commitments and Contingencies

In the normal course of business, the Government has a number of unfulfilled commitments that will require the use of its financial resources. Note 18—Commitments and Contingencies describes the components of the Government's actual commitments that need to be disclosed because of their nature and/or their amount. They include "Long-term Leases," "Undelivered Orders," and "Other Commitments."

Liabilities for contingencies are recognized on the Balance Sheets when both:

- A past transaction or event has occurred.
- A future outflow or other sacrifice of resources is probable and measurable.

The estimated contingent liability may be a specific amount or a range of amounts. If some amount within the range is a better estimate than any other amount within the range, then that amount is recognized. If no amount within the range is a better estimate than any other amount, then the minimum amount in the range is recognized.

Contingent liabilities that do not meet the above criteria for recognition, but for which there is at least a reasonable possibility that a loss has been incurred, are disclosed in Note 18.

K. Social Insurance

A liability for social insurance programs (Social Security, Medicare, railroad retirement, black lung and unemployment) is recognized for any unpaid amounts due as of the reporting date. No liability is recognized for future benefit payments not yet due. For further information, see the Stewardship Information section on Stewardship Responsibilities and Note 19—Dedicated Collections.

L. Related Party Transactions

Federal Reserve Banks (FRBs), which are not part of the reporting entity, serve as the Government's depositary and fiscal agent. They process Federal payments and deposits to the Department of the Treasury's (Treasury's) account and service Treasury securities. FRBs owned $558 billion and $527 billion of Treasury securities held by the public as of September 30, 2001 and 2000, respectively. FRB earnings that exceed statutory amounts of surplus established for FRBs are paid to the Government and are recognized as non-exchange revenue. Those earnings totaled $26.1 billion and $32.3 billion for the years ended September 30, 2001, and September 30, 2000, respectively. The primary source of these earnings is from interest earned on Treasury securities held by the FRBs.

FRBs issue Federal Reserve notes, the circulating currency of the United States. Specific assets owned by FRBs, typically Treasury securities, collateralize these notes. Federal Reserve notes are backed by the full faith and credit of the Government.

The Government does not guarantee payment of the liabilities of Government-sponsored enterprises such as the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, which are privately owned. These enterprises also are excluded from the reporting entity.

Note 2. Cash and Other Monetary Assets

Cash and Other Monetary Assets as of September 30

(In billions of dollars)	2001	2000
Operating cash	44.2	52.7
Other cash	14.2	3.6
Total cash	58.4	56.3
International monetary assets	38.1	35.2
Gold	10.9	10.9
Domestic monetary assets	0.6	2.5
Total cash and other monetary assets	108.0	104.9

Cash

Total cash consists of:

- Operating cash of the Government representing balances from tax collections, custom duties, other revenues, Federal receipts, and other various receipts, which are held in the Federal Reserve Banks, foreign and domestic financial institutions, and in the U.S. Treasury tax and loan accounts.

- Other cash representing the balances of petty cash and other funds held in agencies' books, plus time deposits in financial institutions, and are net of checks outstanding.

The Government maintains formal arrangements with numerous banks to maintain time deposits known as "compensating balances." These balances, which are included in other cash, totaled $13.4 billion and $6.0 billion as of September 30, 2001, and 2000, respectively, compensate the banks for services provided to the Government, such as maintaining zero-balance accounts for the collection of public monies. Operating cash of the Government is either insured (for balances less than $100,000) by the Federal Deposit Insurance Corporation, or collateralized by securities pledged by the depository institutions and held by the FRBs.

International Monetary Assets

"International monetary assets" include the U.S. reserve position in the International Monetary Fund (IMF), U.S. holdings of Special Drawing Rights (SDRs), official reserves of foreign currency, and gold.

The U.S. reserve position in the IMF reflects the reserve asset portion of the financial subscription that the United States has paid in as part of its participation in the IMF. The IMF promotes international monetary cooperation and a stable payments system to facilitate growth in the world economy. Its primary activities are surveillance of member economies, financial assistance as appropriate, and technical assistance.

Only a portion of the required payment to the IMF is made in the form of reserve assets; the remainder is payable in the form of a letter of credit from the United States to the IMF.

The balance available under the letter of credit totaled $29.3 billion and $34.4 billion for the years ended September 30, 2001, and September 30, 2000, respectively. The U.S. reserve position in the IMF has a U.S. dollar equivalent of $18.4 billion and $13.7 billion for the years ended September 30, 2001, and September 30, 2000, respectively.

SDRs are interest-bearing assets obtained through either IMF allocations, transactions with IMF member countries, interest earnings on SDR holdings, or U.S. reserve position in the IMF. SDR holdings are an asset of Treasury's Exchange Stabilization Fund (ESF), which held SDRs totaling $10.9 billion and $10.3 billion equivalent for the years ended September 30, 2001, and September 30, 2000, respectively.

The IMF allocates SDRs to its members in proportion to each member's quota in the IMF. The SDR Act of 1968 authorized the Secretary of the Treasury to issue SDR Certificates (SDRCs) to the Federal Reserve in exchange for dollars. The amount of SDRCs outstanding cannot exceed the dollar value of SDR holdings. The Secretary of the Treasury determines when Treasury will issue or redeem SDRCs. SDRCs outstanding totaled $2.2 billion and $3.2 billion for the years ended September 30, 2001, and September 30, 2000, respectively, and are included in Note 14—Other Liabilities.

As of September 30, 2001 and 2000, "Other Liabilities" included $6.3 billion and $6.4 billion respectively, interest-bearing liability, to the IMF on the ESF balance sheet for SDR allocations. The SDR allocation item represents the cumulative total of SDRs distributed by the IMF to the United States in allocations that occurred in 1970, 1972, 1979, 1980 and 1981.

Gold

"Gold" is valued at the statutory price of $42.2222 per fine troy ounce. The number of fine troy ounces was 258,713,310 and 258,713,310, as of September 30, 2001, and 2000 respectively. The market value of gold on the London Fixing as of the reporting date was $293.10 and $273.65 per fine troy ounce for the years ended September 30, 2001, and September 30, 2000, respectively. Gold totaling $10.9 billion for each year ended September 30, 2001, and September 30, 2000, was pledged as collateral for gold certificates issued and authorized to the FRBs by the Secretary of the Treasury. Treasury may redeem the gold certificates at any time. See Note 14—Other Liabilities.

Domestic Monetary Assets

"Domestic Monetary Assets" consist of liquid assets, other than cash, that are based on the U.S. dollar, including coins, silver bullion, and other coinage metals.

Note 3. Accounts Receivable

The category of "Accounts Receivable," that includes related interest receivable, represents claims to cash or other assets from entities outside the Government. An allowance for estimated losses due to uncollectible amounts is established when it is more likely than not the receivables will not be totally collected. The allowance method varies among the agencies in the Government. Methods include statistical sampling of receivables, specific identification and intensive analysis of each case, aging methodologies, and percentage of total receivables based on historical collection. Accounts receivable are net of an allowance for uncollectible accounts: The amounts are $17.2 billion and $15.8 billion for the years ended September 30, 2001, and September 30, 2000, respectively.

Accounts Receivable as of September 30

(In billions of dollars)	2001	2000
Agency:		
Department of Defense	4.6	4.7
Department of Energy	4.6	4.4
Social Security Administration	4.4	4.7
Department of Health and Human Services	4.2	4.0
Department of Education	2.6	2.3
Department of Agriculture	2.3	1.8
Export-Import Bank of the United States	1.8	-
Department of Interior	1.6	1.1
Department of Veterans Affairs	1.3	1.0
Federal Communications Commission	0.8	0.1
Department of Housing and Urban Development	0.8	1.0
Tennessee Valley Authority	0.7	0.7
Department of Labor	0.6	0.5
Environmental Protection Agency	0.5	0.7
Department of the Treasury	0.5	0.7
All other departments	2.9	4.6
Total accounts receivable	34.2	32.3

Note 4. Loans Receivable and Loan Guarantee Liabilities

The Government uses two methods, direct loans and loan guarantee programs, to accomplish the same goals. These goals are to promote the Nation's welfare by making direct loans and guaranteeing non-Federal loans to segments of the population not served adequately by non-Federal institutions. For those unable to afford credit at the market rate, Federal credit programs provide subsidies in the form of direct loans offered at an interest rate lower than the market rate. For those to whom non-Federal financial institutions are reluctant to grant credit because of the high risk involved, Federal credit programs guarantee the payment of these non-Federal loans and absorb the cost of defaults.

The long-term cost of loans and guarantees outstanding for loans obligated or guarantees committed after fiscal 1991 is the subsidy cost allowance for direct loans outstanding and the liability for loan guarantees outstanding as of the end of this fiscal year. The long-term cost for loans obligated or guarantees committed before fiscal 1992 is the allowance for uncollectible amounts (or present value allowance) for direct loans outstanding and the liability for loan guarantees outstanding. The long-term cost is based on all direct loans and guaranteed loans disbursed in this fiscal year and previous years that are outstanding as of the end of this fiscal year. It includes the subsidy cost of these loans and guarantees estimated as of the time of loan disbursement and subsequent adjustments such as modifications, reestimates, amortizations, and writeoffs.

Direct Loans and Loan Guarantees as of September 30

(In billions of dollars)	Face Value of Loans Outstanding		Long-term Cost of Loans and Guarantees Outstanding		Net Loans Receivable		Amount Guaranteed by the Government		Subsidy Expense for the Fiscal Year Ended September 30, 2000	
	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000
Direct Loan Programs:										
Federal Direct Student Loans	70.5	58.5	(4.3)	(4.4)	74.8	62.9			1.8	(3.9)
Rural Utilities Service	38.8	39.1	3.7	3.0	35.1	36.1			0.5	0.1
Rural Housing Service	28.8	29.2	5.3	7.7	23.5	21.5			1.1	0.2
Federal Family Education Loans	19.5	20.3	13.9	9.4	5.6	10.9			-	-
Food for Progress credits	10.5	10.8	5.9	6.7	4.6	4.1			-	0.6
Credit program—Direct Loan program	9.6	10.2	4.3	3.8	5.3	6.4			-	-
Housing and Urban Development	8.6	10.1	0.4	(0.9)	8.2	11.0			-	-
Agricultural Credit Insurance Fund	4.3	9.2	1.5	0.7	2.8	8.5			2.2	(0.6)
Direct Loans for Spectrum auction sales	5.6	8.2	(0.4)	(1.4)	6.0	9.6			(5.5)	-
Export Credit Guarantees	7.1	7.3	3.7	4.3	3.4	3.0			-	-
Export-Import Bank Loans	7.6	6.2	(0.1)	1.3	7.7	4.9			0.1	-
Disaster Loan programs	3.6	6.0	(0.1)	0.5	3.7	5.5			1.8	0.3
All other programs	29.5	30.0	1.3	6.8	28.2	23.2			(1.4)	1.3
Total	244.0	245.1	35.1	37.5	208.9	207.6			0.6	(2.0)
Guaranteed Loan Programs:										
Federal Family Education Loans	160.0	139.0	8.4	13.7			157.0	129.3	(0.3)	0.3
Subsidized Federal Housing Administration Loans	107.9	106.4	6.9	8.0			95.9	94.8	-	(0.1)
Export-Import Bank guarantees	29.6	28.7	3.2	6.3			29.6	28.7	1.3	2.6
Veterans Housing Benefit program	218.5	216.4	5.3	5.0			71.4	71.8	-	(0.6)
Small Business Loans	46.6	43.7	1.1	1.3			37.5	35.0	(0.1)	(0.3)
Israeli Loan Guarantee program	9.2	9.2	0.6	0.6			9.2	9.2	-	-
Urban and Environmental program	2.2	2.3	0.5	0.1			2.2	2.3	-	-
Overseas Private Investment Corporation Credit program	3.4	3.2	0.6	0.4			3.4	3.2	-	-
Rural Housing Service	13.0	11.5	0.4	0.4			11.6	10.4	-	0.2
Health Education Assistance Loans	3.2	3.2	0.4	0.3			3.2	3.2	-	-
Export Credit Guarantee programs	4.4	4.5	0.3	0.3			4.3	4.4	-	0.8
Unsubsidized Federal Housing Administration Loans	493.7	483.3	(0.9)	(0.5)			459.5	449.7	-	-
All other programs	21.3	25.1	0.9	1.4			18.9	20.3	(0.8)	0.4
Total	1,113.0	1,076.5	27.7	37.3			903.7	862.3	0.1	3.3

"Net Loans Receivable" includes related interest and foreclosed property, and is included in the assets section of the Balance Sheets.

The total subsidy expense is the cost of direct loans and loan guarantees recognized during the fiscal year. It consists of the subsidy expense incurred for direct and guaranteed loans disbursed during the fiscal year, for modifications made during the fiscal year of loans and guarantees outstanding, and for reestimates as of the end of the fiscal year of the cost of loans and guarantees outstanding. This expense is included in the Statements of Net Cost.

Major Loan Programs

The Department of Education has two major education loan programs. The Federal Direct Student Loan program, established in fiscal 1994, offers four types of education loans: Stafford, Unsubsidized Stafford, PLUS for parents, and consolidation loans. Evidence of financial need is required for a student to receive a subsidized Stafford loan. The other three loan programs are available to borrowers at all income levels. These loans usually mature 9 to 13 years after the student is no longer enrolled. They are unsecured. The second loan program, the Federal Family Education Loan program, formerly known as the Guaranteed Student Loan program, was established in fiscal 1965. Like the Federal Direct Student Loan program, it offers four types of loans: Stafford, Unsubsidized Stafford, PLUS for parents, and consolidation loans.

The Department of Agriculture, Rural Utilities Service loans are for the construction and operation of electric generating plants, transmission and distribution lines, telecommunication lines, and related systems. These loans carry an average maturity of greater than 20 years and are usually secured.

The major Federal rural housing programs are funded through the Rural Housing Insurance Fund program account. These programs include:

- Very low- and low-to-moderate-income home ownership loans and guarantees.
- Very low-income housing repair loans.
- Multifamily housing loans and guarantees.
- Domestic farm labor housing loans.
- Housing site loans.
- Credit sales of acquired property.

Loan programs are limited to rural areas that include towns, villages, and other places not part of an urban area. The majority of these loans mature in excess of 25 years and are secured by the property of the borrower.

The Department of Housing and Urban Development, Federal Housing Administration (FHA) provides mortgage insurance encouraging lenders to make credit available to expand home ownership. FHA predominately serves borrowers the conventional market does not serve adequately. This includes first-time home buyers, minorities, lower-income families, and residents of under-served areas.

The Department of Veteran Affairs, Veterans Housing Benefit program provides partial guarantee of residential mortgage loans issued to eligible veterans, reservists and service members by private lenders. This guarantee allows veterans, reservists, and service members to purchase a home without a substantial down payment.

The Export-Import Bank aids in financing and promoting U.S. exports. To accomplish its objectives, the bank's authority and resources are used to:

- Assume commercial and political risk that exporters or private institutions are unwilling or are unable to undertake.
- Overcome maturity and other limitations in private sector financing.
- Assist U.S. exports to meet foreign officially sponsored export credit competition.
- Provide leadership and guidance in export financing to the U.S. exporting and banking communities and to foreign borrowers.

Repayment terms for these loans are usually 1 to 7 years.

The U.S. Agency for International Development (USAID) provides economic assistance to selected countries in support of U.S. efforts to promote stability and security interests in strategic regions of the world.

Other loan programs include the Small Business Administration (SBA) general business loan guarantees and disaster loans; and the Farm Service Agency for farm ownership, emergency, and disaster loans.

Note 5. Taxes Receivable

"Taxes Receivable" are the gross tax receivables net of allowance for doubtful accounts.

Taxes Receivable as of September 30

(In billions of dollars)	2001	2000
Gross taxes receivable	82.2	83.7
Allowance for doubtful accounts	(61.1)	(60.4)
Taxes receivable, net	21.1	23.3

Note 6. Inventories and Related Property

Inventories and Related Property

(In billions of dollars)	Defense 2001	All Others 2001	Total 2001	Defense 2000	All Others 2000	Total 2000
Inventory held for sale, principally to Federal agencies	48.4	2.1	50.5	52.9	1.2	54.1
Operating materials and supplies	85.2	7.7	92.9	83.9	6.2	90.1
Stockpile materials	2.4	36.7	39.1	2.4	37.7	40.1
Other related property	-	1.3	1.3	-	0.9	0.9
Total inventories and related property	136.0	47.8	183.8	139.2	46.0	185.2

Inventory is tangible personal property that is (1) held for sale, principally to Federal agencies, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee.

"Inventory held for sale, principally to Federal agencies" is expected to be sold in the normal course of operations and includes the following categories:

- "Inventory held for future sale" is maintained because it is not readily available in the market or because it will not be used in the normal course of operations, but there is more than a remote chance that it will eventually be needed. The Department of Defense (DOD), which accounts for nearly all of the inventory held for sale and future sale in the Government, uses the Latest Acquisition Cost (LAC) method, which is revalued for holding gains and losses—of $27.1 billion and $25.3 billion for the years ended September 30, 2001, and September 30, 2000, respectively—in order to approximate historical cost.
- "Inventory held for repair" is damaged inventory that requires repair to make it suitable for sale. Inventory held for repair is reported net of an allowance for estimated repair costs.
- "Excess inventory" is that which exceeds the demand expected in the normal course of operations and which does not meet management's criteria to be held in reserve for future sale.
- "Obsolete inventory" is that which no longer is needed due to changes in technology, laws, customs, or operations.
- "Unserviceable inventory" is inventory damaged beyond economic repair.
- "Excess, obsolete, and unserviceable inventory" is reported at net realizable value.

"Operating materials and supplies" are tangible personal property to be consumed in normal operations and include the following categories:

- "Operating materials and supplies held for future use" are materials retained because they are not readily available in the market or because they will not be used in the normal course of operations, but there is more than a remote chance that they will eventually be needed. DOD, which accounts for most of the reported operating materials and supplies, uses LAC and Standard Price under the purchase and consumption methods of accounting to value operating materials and supplies and does not adjust for holding gains and losses, which does not approximate historical cost.
- "Excess operating materials and supplies" are materials that exceed the demand expected in the normal course of operations, and do not meet management's criteria to be held in reserve for future use.
- "Obsolete operating materials and supplies" are materials that are no longer needed due to changes in technology, laws, customs, or operations.
- "Unserviceable operating materials and supplies" are materials damaged beyond economical repair. DOD, which accounts for most of the reported excess, obsolete, and unserviceable operating materials and supplies, does not value excess, obsolete, and unserviceable operating materials and supplies at net realizable value.

"Stockpile materials" are strategic and critical materials held for use in national defense, conservation, or national emergencies due to statutory requirements; for example, nuclear materials and oil. The amounts reported include $2.1 billion and $1.8 billion of stockpile materials authorized for sale for the years ended September 30, 2001, and September 30, 2000, respectively.

"Other related property" consists of:

- "Commodities" include items of commerce or trade that have an exchange value used to stabilize or support market prices.
- "Seized monetary instruments" is comprised of only monetary instruments that are awaiting judgment to determine ownership. The related liability is included in "Other liabilities." Other property seized by the Government, such as real property and tangible personal property, is not included as a Government asset. It is accounted for in agency property-management records until the property is forfeited, returned, or otherwise liquidated.
- "Forfeited property" is comprised of monetary instruments, intangible property, real property, and tangible personal property acquired through forfeiture proceedings; property acquired by the Government to satisfy a tax liability; and unclaimed and abandoned merchandise.
- "Other property" not classified above.

Note 7. Property, Plant and Equipment

The category of "Property, Plant and Equipment" consists of tangible assets including land, buildings, structures, automated data processing software, and other assets used to provide goods and services. Certain types of tangible assets, collectively referred to as "Stewardship Assets," are not reported as property, plant and equipment or elsewhere on the Balance Sheets. This is in conformity with accounting standards that became effective for fiscal 1998. "Stewardship Assets" include "National Defense Assets," "Heritage Assets," and "Stewardship Land." These assets are presented in the Stewardship Information section.

Property, Plant and Equipment as of September 30

(In billions of dollars)	Cost 2001	Accumulated Depreciation/ Amortization 2001	Net 2001	Cost 2000	Accumulated Depreciation/ Amortization 2000	Net 2000
Buildings, structures, and facilities	292.8	141.6	151.2	287.3	135.6	151.7
Furniture, fixtures, and equipment	160.3	89.0	71.3	148.6	80.7	67.9
Construction in progress	54.4	N/A	54.4	51.0	N/A	51.0
Land and land improvements	32.0	8.8	23.2	30.0	7.2	22.8
Automated data processing software	5.7	2.9	2.8	4.1	2.3	1.8
Assets under capital lease	1.7	0.6	1.1	1.6	0.5	1.1
Leasehold improvements	3.1	1.4	1.7	2.8	1.2	1.6
Other property, plant and equipment	1.0	-	1.0	0.6	-	0.6
Total property, plant and equipment	551.0	244.3	306.7	526.0	227.5	298.5

Note 8. Other Assets

Other Assets as of September 30

(In billions of dollars)	2001	2000
Advances and prepayments	21.5	17.1
Securities and investments	21.6	19.1
Other	20.3	23.5
Total other assets	63.4	59.7

Securities and investments are presented at cost, net of unamortized premiums and discounts.

Note 9. Accounts Payable

Accounts Payable as of September 30

(In billions of dollars)	2001	2000
Interest on the Public Debt	39.5	44.3
Department of Defense	23.2	19.8
Department of Energy	3.7	3.3
Department of Transportation	3.5	1.1
Department of Agriculture	3.3	3.4
National Aeronautics and Space Administration	2.8	2.8
Department of Veterans Affairs	2.4	0.5
Department of Justice	2.0	2.4
United States Postal Service	2.0	4.5
General Services Administration	1.9	1.7
Department of Housing and Urban Development	1.5	1.2
Tennessee Valley Authority	1.4	0.9
Agency for International Development	1.2	1.3
Executive Office of the President	0.9	0.7
Department of Treasury - excluding interest on debt	0.7	0.7
Department of Health and Human Services	0.6	0.5
All other departments	5.1	1.9
Total accounts payable	95.7	91.0

The “Accounts Payable” table includes “Interest on Federal debt securities held by the public.” This reflects unpaid interest accrued on Federal debt securities held by the public (see Note 10) as of September 30. Other accounts payable are for goods and property ordered and received, and for services rendered by other than Federal employees.

Note 10. Federal Debt Securities Held by the Public

Definitions of Debt

Gross Federal Debt—All Government debt, whether issued by Treasury (Treasury securities) or by other agencies (agency securities). “Gross Federal debt” is held either by the public or by Federal Government entities.

Debt Held by the Public—Federal debt held outside the Government by individuals, corporations, State or local governments, Federal Reserve Banks, and foreign Governments and central banks.

Intragovernmental Debt Holdings—Federal debt held by Government trust funds, revolving funds, and special funds.

Federal Debt Securities Held by the Public as of September 30

(In billions of dollars)	Balance September 30, 2000	Net Change During Fiscal 2001	Balance September 30, 2001	Average Interest Rate During Fiscal 2001	Average Interest Rate During Fiscal 2000
Treasury Securities:					
Marketable securities	3,024.2	(93.5)	2,930.7	5.820%	6.631%
Non-marketable securities	2,650.0	226.8	2,876.8	6.303%	6.628%
Total Treasury securities	5,674.2	133.3	5,807.5		
Plus: Unamortized premium on Treasury securities	15.0	(1.8)	13.2		
Less: Unamortized discount on Treasury securities	75.5	(10.1)	65.4		
Total Treasury securities, net of unamortized premiums and discounts	5,613.7	141.6	5,755.3		
Agency Securities:					
Tennessee Valley Authority	25.4	(0.5)	24.9		
All other agencies	1.7	(0.1)	1.6		
Total agency securities, net of unamortized premiums and discounts	27.1	(0.6)	26.5		
Total Federal debt	5,640.8	141.0	5,781.8		
Less: Intragovernmental debt holdings, net of unamortized premiums and discounts	2,230.9	231.1	2,462.0		
Total Federal debt securities held by the public	3,409.9	(90.1)	3,319.8		

Types of marketable securities:
Bills – Short-term obligations issued with a term of 1 year or less.
Notes – Medium-term obligations issued with a term of at least 1 year, but not more than 10 years.
Bonds – Long-term obligations of more than 10 years.

"Federal Debt Securities Held by the Public" totaled $3,319.8 billion and $3,409.9 billion for the years ended September 30, 2001, and September 30, 2000, respectively. This table details Government borrowing to finance operations and shows marketable and non-marketable securities at face value. Unamortized premiums are added and unamortized discounts subtracted.

"Intragovernmental debt holdings" represent the portion of the gross Federal debt held as investments by Government entities. This includes major trust funds. For more information on trust funds, see Note 19—Dedicated Collections. These intragovernmental debt holdings are eliminated in the consolidation of these financial statements.

Securities that represent Federal debt held by the public are issued primarily by the Treasury and include:

- Interest-bearing marketable securities (bills, notes, and bonds).
- Interest-bearing nonmarketable securities (foreign series, State and local government series, domestic series, and savings bonds).
- Non interest-bearing debt (matured and other).

As of September 30, 2001 and 2000, respectively, $5,732.8 billion and $5,591.6 billion of debt was subject to a statutory limit (31 U.S.C. § 3101). That limit was $5,950 billion. The debt subject to the limit includes Treasury Securities held by the public and intragovernmental debt holdings, as well as Government guaranteed debt of Federal agencies.

Section 3111 of title 31, U.S.C., authorizes the Secretary of the Treasury to use money received from the sale of an obligation and other money in the general fund of the Treasury to buy, redeem, or refund, at or before maturity, outstanding bonds, notes, certificates of indebtedness, Treasury bills, or savings certificates of the Government. During fiscal 2001 and 2000, the Secretary of the Treasury authorized the redemption of $33.8 and $21.3 billion of outstanding unmatured marketable Treasury securities at a premium of $10.7 and $5.5 billion, respectively. These early redemption transactions are known as Treasury "buybacks." The net change of the Federal debt securities held by the public includes $33.6 billion and $21.2 billion during fiscal 2001 and 2000, respectively, related to these buybacks.

Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts as of September 30

(In billions of dollars)	Balance September 30, 2000	Net Change During Fiscal 2001	Balance September 30, 2001
Social Security Administration, Federal Old-Age and Survivors Insurance	893.5	140.6	1,034.1
Office of Personnel Management, civil service retirement and disability	512.0	30.6	542.6
Department of Health and Human Services, Hospital Insurance	168.9	28.2	197.1
Department of Defense, military retirement	149.3	7.7	157.0
Social Security Administration, Federal Disability Insurance	113.7	22.1	135.8
Department of Labor, unemployment	86.4	2.2	88.6
Department of Health and Human Services, Federal Supplementary Medical Insurance	45.1	(3.1)	42.0
Federal Deposit Insurance Corporation funds	42.6	1.4	44.0
Department of Transportation, Highway Trust Fund	31.0	(6.9)	24.1
Railroad Retirement Board	24.8	2.1	26.9
Office of Personnel Management, Employees' Life Insurance	22.4	1.3	23.7
Housing and Urban Development, Federal Housing	17.3	-	17.3
Veterans Affairs	14.2	(0.2)	14.0
Department of Transportation, Airport and Airway Trust Fund	13.1	0.6	13.7
Department of Energy, nuclear waste disposal	17.6	3.5	21.1
All other programs and funds	83.3	2.9	86.2
Subtotal	2,235.2	233.0	2,468.2
Less: Unamortized net discounts	4.3	1.9	6.2
Total intragovernmental debt holdings, net	2,230.9	231.1	2,462.0

Note 11. Federal Employee and Veteran Benefits Payable

The Government offers its employees life and health insurance, as well as retirement and other benefits. These benefits apply to civilian and military employees.

The Federal Government administers more than 40 pension plans. The Office of Personnel Management (OPM) administers the largest civilian plan. DOD, meanwhile, administers the largest military plan. The Government offers both defined benefit and defined contribution pension plans. The largest are defined benefit plans. The change in actuarial accrued post-retirement pension and health benefits liability and components of related expense for the years ended September 30, 2001, and September 30, 2000, respectively, are presented below.

Federal Employee and Veteran Benefits Payable as of September 30

(In billions of dollars)	Civilian 2001	Civilian 2000	Military 2001	Military 2000	Total 2001	Total 2000
Pension	1,112.9	1,071.9	708.3	690.4	1,821.2	1,762.3
Post-retirement health benefits	205.2	198.1	580.9	192.4	786.1	390.5
Veterans compensation and burial benefits	N/A	N/A	691.9	552.6	691.9	552.6
Liability for other benefits	41.1	39.2	20.5	20.1	61.6	59.3
Total Federal employee and veteran benefits payable	1,359.2	1,309.2	2,001.6	1,455.5	3,360.8	2,764.7

Change in Actuarial Accrued Pension Liability and Components of Related Expenses

(In billions of dollars)	Civilian [1]	Military	Total
Actuarial accrued pension liability as of September 30, 2000	1,071.9	690.4	1,762.3
Pension Expense:			
Normal costs	23.2	14.5	37.7
Interest on liability	74.3	42.4	116.7
Actuarial (gains)/losses	(7.6)	(4.8)	(12.4)
Total pension expense	89.9	52.1	142.0
Less benefits paid	48.9	34.2	83.1
Actuarial accrued pension liability as of September 30, 2001	1,112.9	708.3	1,821.2

[1] Does not include U.S. Tax Court and judicial branch.

Significant Assumptions Used in Determining Pension Liability and the Related Expense

(In percentages)	Civilian 2001	Civilian 2000	Military 2001	Military 2000
Rate of interest	6.75%	7.00%	6.25%	6.25%
Rate of inflation	3.75%	4.00%	3.50%	3.00%
Projected salary increases	4.25%	4.25%	3.50%	3.50%

Change in Actuarial Accrued Post-Retirement Health Benefits Liability and Components of Related Expenses

(In billions of dollars)	Civilian	Military	Total
Actuarial accrued post-retirement health benefits liability, as of September 30, 2000	198.1	192.4	390.5
Post-Retirement Health Benefits Expense:			
Normal costs	8.7	4.7	13.4
Interest on liability	12.8	11.6	24.4
Cost due to plan amendments	-	293.1	293.1
Actuarial (gains)/losses	(6.9)	86.3	79.4
Total post-retirement health benefits expense	14.6	395.7	410.3
Less claims paid	7.5	7.2	14.7
Actuarial accrued post-retirement health benefits liability, as of September 30, 2001	205.2	580.9	786.1

Significant Assumptions Used in Determining Post-Retirement Health Benefits and the Related Expense

	Civilian		Military	
(In percentages)	2001	2000	2001	2000
Rate of interest	6.75%	7.0%	6.25%	6.25%
Rate of health care cost inflation	7.0%	7.0%	4.8-13%	4.0-9.79%

Civilian Employees

Pensions

OPM administers the largest civilian pension plan, which covers approximately 90 percent of all Federal civilian employees. This plan includes two components of defined benefits. These are the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). The basic benefit components of the CSRS and the FERS are financed and operated through the Civil Service Retirement and Disability Fund (CSRDF).

CSRDF monies are generated primarily from employees' contributions, agency contributions, payments from the general fund, and interest on investments in securities. See Note 19—Dedicated Collections.

The Federal Retirement Thrift Investment Board, an independent Government agency, administers the Thrift Savings Plan (TSP) Fund. Federal employees and retirees covered by CSRS and FERS own the fund's assets. These financial statements exclude this fund because the employees own its assets.

Treasury securities held by the fund are included and classified as Treasury securities held by the public. FERS employees may contribute up to 11 percent of base pay to the plan, which the Government matches up to 5 percent. CSRS employees may contribute up to 7 percent of base pay with no Government match.

The TSP Fund held $36.8 billion and $31.8 billion in nonmarketable Treasury securities for the years ended September 30, 2001, and September 30, 2000, respectively. The Federal Government's related liability is included in "Total Federal Debt Securities Held by the Public" in the Balance Sheets.

Health Benefits

Civilian retirees pay the same insurance premium as active employees under the Federal Employees Health Benefits Program (FEHBP). These premiums cover only a portion of the costs.

Other Benefits

Employee and annuitant contributions and interest on investments fund a portion of the Federal Employees' Group Life Insurance (FEGLI) program. OPM administers this program, although claims are paid through private insurance companies.

Military Employees (Including Veterans)

Pensions

The DOD Military Retirement Fund finances military retirement and survivor benefit programs.

The military retirement system consists of a funded, noncontributory, defined benefit plan. It applies to the Army, Navy, Marine Corps, and Air Force. This system includes non-disability retirement pay, disability retirement pay, and retirement pay for reserve service and survivor annuity programs.

Health Benefits

Military benefits entitle retirees and their dependents to health care in military medical facilities if a facility can provide the needed care. Until they reach age 65, military retirees and their dependents also are entitled to be reimbursed for the cost of health care from civilian providers. A premium is charged to enroll in DOD's civilian care program. In addition, there are deductible and copayment requirements for civilian care. Medicare covers military retirees after they reach 65 years of age.

Military retiree health care figures include the cost of education and training, staffing, buildings and equipment, as well as the operation and maintenance of medical facilities. They also include claims paid to civilian providers and the cost of administering the program.

The $389 billion increase in Military Retirement Health Benefits liability as of September 30, 2001 includes $293 billion due to the effect of Public Law No. 106-398 (the National Defense Authorization Act) that was signed into law on October 30, 2000. Under this legislation, TRICARE benefits are extended to military retirees and their beneficiaries who are eligible for Medicare and a fund is established to pay these benefits. Another increase of $91.3 billion is associated with the change in medical trend assumptions as set by the Board of Trustees. The Act also included a number of other enhanced medical benefits in addition to the specific Medicare eligible benefits.

Some of the Act's provisions include:

- On April 1, 2001, Medicare eligible military retirees and their beneficiaries became eligible for a worldwide pharmacy benefit, including MTF, National Mail Order Pharmacy, and retail pharmacy benefit.
- On October 1, 2001, TRICARE became the second payer to Medicare for Medicare eligible military retirees and their beneficiaries.
- The catastrophic cap was reduced from $7,500 to $3,000 for retiree families and other active duty family benefits.

Compensation and Burial Benefits

The Government compensates disabled veterans and their survivors. Veterans compensation is payable as a disability benefit or a survivor's benefit. Entitlement to compensation depends on the veteran's disabilities having been incurred in, or aggravated during, active military service; death while on duty; or death resulting from service-connected disabilities, if not in active duty.

Burial benefits include a burial and plot or interment allowance payable for a veteran who, at the time of death, qualified to receive compensation or a pension, or whose death occurred in a Department of Veterans Affairs' facility.

The liability for veterans compensation and burial benefits payable increased by $139.3 billion and $69.4 billion in fiscal 2001 and 2000, respectively. The primary factors contributing to this increase were changes in interest rate and other actuarial assumptions.

Veterans Compensation and Burial Benefits as of September 30

(In billions of dollars)	2001	2000
Veterans	574.0	458.8
Survivors	115.1	91.0
Burial benefits	2.8	2.8
Total compensation and burial benefits payable	691.9	552.6

Other Benefits

Veterans insurance includes the following programs:

- United States Government Life Insurance, established in 1919 to handle new issues and the conversion of World War I Risk Term Insurance.
- National Service Life Insurance, established in 1940 to meet the needs of World War II service personnel.
- Veterans Special Life Insurance, established in 1951 for Korean veterans who did not have service-connected disabilities.
- Service-Disabled Veterans Insurance, established in 1951 for veterans with service-connected disabilities.
- Veterans Reopened Insurance, which established a 1-year reopening in 1965 of National Service Life Insurance for certain disabled World War II and Korean veterans.

Note 12. Environmental and Disposal Liabilities

Environmental and Disposal Liabilities as of September 30

(In billions of dollars)	2001	2000
Department of Energy:		
Environmental management baseline estimates	184.2	182.7
Active and surplus facilities–other programs	31.4	26.0
High-level waste and spent nuclear fuel disposition	14.6	14.3
Other	8.1	11.3
Total Department of Energy	238.3	234.3
Department of Defense:		
Chemicals weapons disposal	14.2	14.9
Training ranges and non-range unexploded ordnance	16.4	14.0
Active installations	13.1	15.4
Nuclear powered aircraft carriers and submarines	10.0	10.2
Other	9.6	8.7
Total Department of Defense	63.3	63.2
All other agencies	5.2	3.7
Total environmental and disposal liabilities	306.8	301.2

During World War II and the Cold War, the United States developed a massive industrial complex to research, produce, and test nuclear weapons. The nuclear weapons complex included nuclear reactors, chemical-processing buildings, metal machining plants, laboratories, and maintenance facilities.

At all the sites where these activities took place, some environmental contamination occurred. This contamination was caused by the production, storage and use of radioactive materials and hazardous chemicals, which resulted in contamination of soil, surface water, and groundwater. The environmental legacy of nuclear weapons production also includes thousands of contaminated areas and buildings, and large volumes of waste and special nuclear materials requiring treatment, stabilization, and disposal.

The resulting environmental liabilities consist of the costs associated with removing, containing, and/or disposing of this hazardous waste.

Of those environmental liabilities, this report presents only cleanup costs from Federal operations known to result in hazardous waste that the Government is required to clean up by Federal, State, or local statutes and/or regulations. Two of these statutes are the Nuclear Waste Policy Act of 1992, which provides for permanent disposal of the Nation's high-level radioactive waste and spent nuclear fuel; and Public Law 105-204, which requires a plan for the conversion of depleted uranium hexaflouride.

The Department of Energy (DOE) is responsible for the cleanup of facilities it operates or has operated. The components of the liability are environmental management baseline estimates including costs for environmental restoration; nuclear material and facility stabilization; and waste treatment, storage, and disposal activities at each installation. They also include costs for related activities such as landlord responsibilities, program management, and legally prescribed grants for participation and oversight by Native American tribes and regulatory agencies. Active and surplus facilities represent anticipated remediation costs for those facilities that are conducting ongoing operations but ultimately will require stabilization, deactivation, and decommissioning. High-level waste and spent nuclear fuel disposition include the full cost to provide for permanent disposal of the Nation's high-level radioactive waste and spent nuclear fuel. Projects with no current feasibility remediation approach are excluded from the estimate. Significant projects not included are:

- Nuclear explosion test areas (e.g., Nevada test site).
- Large surface water bodies (e.g., Clinch and Columbia Rivers).
- Most ground water (even with treatment, future use will be restricted).

DOD is required to clean up contamination resulting from waste disposal practices, leaks, spills and other activities that have created a public health or environmental risk. DOD must restore active installations, installations affected by base realignment or closure, and other areas formerly used as defense sites. DOD also bears responsibility for disposal of chemical weapons and environmental costs associated with the disposal of weapons systems (primarily nuclear powered aircraft carriers and submarines). DOD is responsible, as well, for training range and other non-range unexploded ordnance cleanup.

Note 13. Benefits Due and Payable

These amounts are the benefits owed to program recipients or medical service providers as of the fiscal yearend that have not yet been paid. For a description of the programs, see the Stewardship Responsibilities section under Stewardship Information.

Benefits Due and Payable as of September 30

(In billions of dollars)	2001	2000
Federal Old-Age and Survivors Insurance	32.4	31.0
Federal Hospital Insurance (Medicare Part A)	13.6	12.7
Grants to States for Medicaid	13.4	12.3
Federal Supplementary Medical Insurance (Medicare Part B)	13.5	11.5
Federal Disability Insurance	9.5	7.4
Supplemental security income	1.3	1.2
Railroad retirement	0.7	0.7
Unemployment insurance	1.4	0.8
Other benefits	0.2	0.2
Total benefits due and payable	86.0	77.8

Note 14. Other Liabilities

Other Liabilities as of September 30

(In billions of dollars)	2001	2000
Insurance programs	33.2	20.6
Deferred revenue	28.3	23.8
Accrued wages and benefits	27.3	26.2
Gold certificates	11.0	11.0
Other debt	9.7	10.4
Exchange stabilization fund	8.5	9.6
Deposited funds and undeposited collections	6.8	6.2
Advances from foreign Government	4.9	6.2
Contractual services	4.2	4.9
Energy Employees Occupational Illness Compensation Act	3.2	1.6
Advances from others	2.2	3.5
Other miscellaneous liabilities	48.8	51.0
Total other liabilities	188.1	175.0

Accrued wages and benefits consist of the estimated liability for civilian and military salaries and wages earned but unpaid. They also include funded annual leave and other employee benefits that have been earned but are unpaid.

Deferred revenue refers to revenue received but not yet earned, such as payments received in advance from outside sources for future delivery of products or services (NASA).

Insurance programs include bank deposit insurance, guarantees of pension benefits, and life and medical insurance. They also include insurance against damage to property (home, crops, and airplanes) caused by perils such as flooding and other natural disasters, risk of war, and insolvency.

Gold certificates include monetized portions of gold and certificates deposited in FRBs.

Other debt includes Government obligations, whether secured or unsecured, not included in public debt.

Exchange stabilization fund includes Special Drawing Rights (SDRs) certificates issued to the Federal Reserve Banks and allocations from the International Monetary Fund.

Advances from foreign Governments consist of amounts received from foreign Governments for goods and services to be provided.

Deposit funds are deposits held and maintained by the Government on behalf of a third party and includes unclassified deposited funds that are amounts offsetting undeposited collections, as well as funds deposited in clearing accounts and suspense accounts that await disposition or reclassification.

Contractual services consist of contractual obligations of the Department of Defense.

The Energy Employees Occupational Illness Compensation Act authorized compensation for certain illnesses suffered by the employees of the Department and contractors who performed work for the nuclear weapons program.

Advances from others are amounts received in advance for future delivery of goods or services.

Other miscellaneous liabilities include amounts accrued for contingent liabilities.

Note 15. Collections and Refunds of Federal Revenue

Collections of Federal Revenue for the Year Ended September 30, 2001

(In billions of dollars)	Federal Revenue Collections	Tax Year to Which Collections Relate: 2001	2000	1999	Prior Years
Individual income and tax withholdings	1,843.8	1,155.4	665.8	14.0	8.6
Corporation income taxes	186.4	99.2	79.8	0.7	6.7
Estate and gift taxes	29.2	0.6	25.1	1.2	2.3
Excise taxes	68.2	49.2	18.6	0.1	0.3
Custom duties	19.7	19.7	-	-	-
Fees and licenses	0.9	0.9	-	-	-
Unemployment taxes	27.0	25.0	1.9	-	0.1
Railroad retirement taxes	4.7	3.6	1.1	-	-
Federal Reserve earnings	26.1	21.6	4.5	-	-
Fines, penalties, interest, and other taxes	2.7	2.0	0.7	-	-
Total	2,208.7	1,377.2	797.5	16.0	18.0

Collections of Federal Revenue for the Year Ended September 30, 2000

(In billions of dollars)	Federal Revenue Collections	Tax Year to Which Collections Relate: 2000	1999	1998	Prior Years
Individual income and tax withholdings	1,764.3	1,132.3	612.5	11.6	7.9
Corporation income taxes	235.4	156.5	70.2	0.5	8.2
Estate and gift taxes	29.7	0.4	25.7	1.6	2.0
Excise taxes	70.2	51.4	18.3	0.1	0.4
Custom duties	20.5	20.5	-	-	-
Fees and licenses	2.1	2.1	-	-	-
Unemployment taxes	26.7	24.7	2.0	-	-
Railroad retirement taxes	4.7	3.6	1.1	-	-
Federal Reserve earnings	32.3	25.1	7.2	-	-
Fines, penalties, interest, and other taxes	3.4	2.9	0.5	-	-
Total	2,189.3	1,419.5	737.5	13.8	18.5

Treasury is the Government's principal revenue-collecting agency.

Collections of "Individual income and tax withholdings" include estimated income tax payments by individuals, Social Security and Medicare taxes, and individual income tax withholdings, but do not include Federal tax refunds.

"Individual income and tax withholdings" include refunds and Earned Income Tax Credit (EITC) payments. EITC is a refundable credit for taxpayers who work and whose earnings fall below the established ceiling. A refundable credit is first used to offset any individual taxes owed; any remaining amounts are issued to the taxpayer. In fiscal 2001, the Internal Revenue Service (IRS) issued $26.1 billion in EITC refunds and an additional $5.1 billion of the EITC credits was applied to reduce taxpayer liability. (In fiscal 2000, $26.1 billion of EITC refunds were issued, $81 million of which was applied to advance EITC, and an additional $5.1 billion of EITC refunds were applied to reduce taxpayer liability.) All of these EITC amounts are included in "Gross Cost" in the Statements of Net Cost as a component of the Department of the Treasury. Amounts reported for corporate income taxes in tax year 2001 include corporate taxes of $5 billion for tax year 2001. (Similarly, amounts reported for corporate income taxes collected in fiscal 2000 include corporate taxes of $7 billion for tax year 2000.) Taxes collected are reported in the Revenue section of the Statements of Operations and Changes in Net Position, and are presented on a modified cash basis. On the other hand, collections reported in the table in Note 15 are reported on a gross cash basis.

The Statement of Operations and Change in Net Position reports total revenue of $2,013.7 billion and $2,044.8 billion for fiscal 2001 and 2000, respectively. The difference between collections, net of refunds, and total revenue is primarily due to changes in taxes receivable, imputed revenue for the Earned Income Tax Credit and Child Tax Credit, other collecting entities and other earned revenue.

The "Current Service Assessment" (CSA) table in the Stewardship section of this document also includes the Government's receipts and outlays. The total amounts included in the table for the years 2001 and 2000 are the same as those described in Note 15 but classified differently. The classifications differ because the budget classifies some collections and refunds differently. For example, Note 15 nets part of the EITCs (amounts in excess of offsets to individual taxes owed) in receipts, while the budget reports them as outlays. Meanwhile, the Statement of Net Cost reports refunds and EITCs as expenses.

Federal Tax Refunds Disbursed for the Year Ended September 30, 2001

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate 2001	2000	1999	Prior Years
Individual income and tax withholdings	210.3	1.4	195.7	9.4	3.8
Corporation income taxes	38.6	1.3	14.8	8.2	14.3
Unemployment taxes	0.1	-	0.1	-	-
Excise taxes	0.9	0.3	0.4	-	0.2
Estate and gift taxes	1.0	-	0.3	0.4	0.3
Custom duties	0.9	0.4	0.2	0.1	0.2
Total	251.8	3.4	211.5	18.1	18.8

Federal Tax Refunds Disbursed for the Year Ended September 30, 2000

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate 2000	1999	1998	Prior Years
Individual income and tax withholdings	161.4	1.0	148.5	8.6	3.3
Corporation income taxes	31.1	1.4	10.4	7.0	12.3
Unemployment taxes	0.1	-	0.1	-	-
Excise taxes	0.7	0.3	0.4	-	-
Estate and gift taxes	0.8	-	0.2	0.3	0.3
Custom duties	1.2	0.5	0.3	0.1	0.3
Total	195.3	3.2	159.9	16.0	16.2

Note 16. Unreconciled Transactions Affecting the Change in Net Position

The reconciliation of the "Change in Net Position" requires that the difference between ending and beginning net position equals the excess of revenues over net cost, plus or minus prior period adjustments.

The unreconciled transactions needed to bring the change in net position into balance, amounted to a net value of $17.3 billion and $4.8 billion for the years ended September 30, 2001, and September 30, 2000, respectively.

The three primary factors affecting this out-of-balance situation are:

- Improper recording of intragovernmental transactions by agencies.
- Transactions affecting Balance Sheet assets and liabilities not identified properly by agencies as prior period adjustments.
- Timing differences and errors in reporting transactions.

The Federal financial community considers the identification and accurate reporting of these unreconciled transactions a priority.

Note 17. Prior Period Adjustments

Prior Period Adjustments to the Fiscal Year Beginning October 1, 1999 and 2000

(In billions of dollars)	Increases to Net Position 2001	2000
Department of Defense	(5.3)	31.6
Social Security Administration	5.1	-
Department of Agriculture	-	5.1
Veterans Administration	-	5.4
Department of Transportation	2.1	-
All other adjustments to prior periods	(0.5)	(0.9)
Total prior period adjustments	1.4	41.2

"Prior Period Adjustments" for fiscal 2001 consists of $1.4 billion adjustments to the corresponding opening net positions to correct errors in prior periods.

Significant components of this net adjustment include:

- A $5.3 billion adjustment by DOD for correction of errors and environmental cleanup liability.
- A $5.1 billion adjustment by Social Security Administration for correction of errors in determining eligibility for disability benefits.
- A $2.1 billion adjustment by Transportation to correct accruals, property and inventory.
- A $0.5 billion net adjustment to prior period resulting from a correction composed of smaller debits and credits from different agencies.

"Prior Period Adjustments" for fiscal 2000 consist of $41.2 billion adjustments to the corresponding opening net positions to correct errors in prior periods.

Significant components of this net adjustment include:

- A $5.4 billion adjustment to Veterans Administration Pension plan. The fiscal 2000 portion of this adjustment was restated in the balance sheet line item titled "Federal Employee and Veteran Benefits Payable".
- A $31.6 billion adjustment by DOD for correction of error in estimating the environmental cleanup liability. This adjustment was restated in the Reconciliations of Net Operating Revenue/(Cost) to the Budget Surplus.
- A $5.1 billion adjustment to previously reported valuations of the Department of Agriculture's property, plant and equipment, inventory balances, and other assets.
- A $0.9 billion net adjustment to the prior period resulting from a correction composed of smaller debits and credits from different agencies.

Note 18. Commitments and Contingencies

The Government has entered into contractual commitments that require future use of financial resources. It has significant amounts of long-term lease obligations as shown in the table below. "Undelivered Orders" represent the value of goods and services ordered that have not yet been received.

Contingent liabilities related to the loan guarantee programs are described in Note 4—Loans Receivable and Loan Guarantee Liabilities.

A contingency is an existing condition or situation involving uncertainty as to a possible loss. A loss is considered reasonably possible if the future confirming event(s) is more than remote, but less than probable. These contingencies do not include existing conditions or situations where the future occurring event is only considered remote, nor do they include contingencies that would result in a gain.

The Government is also subject to contingencies including litigation. These contingencies arise in the normal course of operations and their ultimate disposition is unknown. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the financial statements, except for litigation described in the next paragraph.

Numerous cases are pending involving, among many other matters, supervisory goodwill at savings and loan institutions, harbor maintenance fees, individual Native American money accounts and tribal accounts revenues. While it is likely that the United States will have to pay some amount of damages on these claims, it is difficult to predict the outcome of litigation and, therefore, the ultimate total costs cannot be reasonably estimated at this time.

The Government has unused statutory lines of credit to Government-sponsored enterprises totaling $10 billion, as well.

Commitments as of September 30

(In billions of dollars)	Capital Leases 2001	Operating Leases 2001	Capital Leases 2000	Operating Leases 2000
Long-term Leases:				
General Services Administration	0.3	17.2	0.3	16.6
U.S. Postal Service	0.8	9.4	0.7	9.0
Department of Justice	0.1	7.9	-	3.8
Department of Agriculture	0.1	2.4	0.2	2.0
Department of Commerce	-	2.2	-	-
Department of Veterans Affairs	-	1.4	-	1.3
Department of Health and Human Services	-	1.2	-	1.1
Department of State	0.1	0.7	0.2	1.0
Other long-term leases	1.2	3.7	0.9	2.9
Total long-term leases	2.6	46.1	2.3	37.7

	2001	2000
Undelivered Orders:		
Department of Housing and Urban Development	89.5	92.2
Department of Health and Human Services	60.6	56.5
Department of the Navy	42.7	43.4
Defense agencies	29.2	11.3
Department of the Air Force	26.4	28.2
Department of the Army	24.2	18.1
Department of Agriculture	21.1	15.6
Department of Education	20.3	23.4
Department of Justice	12.8	11.4
Environmental Protection Agency	9.6	9.6
Department of Labor	8.5	7.7
U.S. Agency for International Development	8.3	8.6
Department of Transportation	6.1	5.8
Federal Emergency Management Agency	5.6	5.6
National Science Foundation	4.9	4.0
Other undelivered orders	43.3	39.3
Total undelivered orders	413.1	380.7
Other Commitments:		
Multi-lateral development banks	69.4	60.8
Fuel commitments	9.5	9.0
National Oceanic and Atmospheric Administration satellites and weather systems	8.4	6.2
Department of Transportation	4.0	3.2
Real property activities	3.4	3.4
Department of Navy	-	2.0
All other programs	1.4	1.8
Total other commitments	96.1	86.4

Contingencies as of September 30

(In billions of dollars)	2001	2000
Insurance:		
Pension Benefit Guaranty Corporation	11.0	5.0
Federal Deposit Insurance Corporation	7.0	1.0
Other insurance programs	0.1	0.2
Total insurance programs	18.1	6.2
Unadjudicated Claims:		
Department of the Navy	-	3.1
Other unadjudicated claims	1.9	2.2
Total unadjudicated claims	1.9	5.3
Other Contingencies:		
Department of Army	8.8	-
Department of Commerce	7.0	3.0
Department of Agriculture	4.5	6.5
Administrative order against Tennessee Valley Authority	3.0	3.0
Department of Energy	1.9	2.0
Other contingencies	3.2	2.8
Total other contingencies	28.4	17.3

Financial Treatment of Loss Contingencies

Probability of Loss	Probable	Reasonably possible, more than remote but less than probable	Remote, chance of occurrence slight
Financial Treatment	Balance Sheet	Footnote disclosure	No disclosure

Note 19. Dedicated Collections

Dedicated Collections as of September 30*

(In billions of dollars)	Receipts		Disbursements		Trust Fund Net Assets		Less Intra-governmental Net Assets		Consolidated Assets	
	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000
Federal Old-Age and Survivors Insurance Trust Fund	518.5	486.5	377.1	358.4	1085.0	940.8	1083.8	939.4	1.2	1.4
Civil Service Retirement and Disability Fund	77.9	76.1	47.4	45.4	552.3	521.5	552.0	521.2	0.3	0.3
Federal Hospital Insurance Trust Fund (Medicare Part A)	173.7	163.3	143.9	129.2	203.7	173.5	203.7	172.2	-	1.3
Military Retirement Fund	40.6	39.5	34.2	32.9	169.2	162.7	169.2	162.7	-	-
Federal Disability Insurance Trust Fund	83.9	77.6	67.8	56.8	153.1	124.5	151.9	123.2	1.2	1.3
Unemployment Trust Fund	34.1	33.2	31.6	25.3	91.5	89.2	90.7	88.3	0.8	0.9
Federal Supplementary Medical Insurance Trust Fund (Medicare Part B)	95.3	89.5	98.4	89.0	42.7	45.8	42.7	45.8	-	-
Highway Trust Fund	31.5	35.0	37.4	32.6	26.2	30.2	26.2	30.2	-	-
Railroad Retirement Trust Fund	5.1	5.3	8.4	8.2	24.0	22.7	23.9	22.7	0.1	-
Airport and Airway Trust Fund	10.0	10.7	9.4	9.9	14.1	13.5	13.9	13.3	0.2	0.2
Hazardous Substance Superfund	1.1	1.2	1.3	1.6	4.3	4.7	3.8	4.7	0.5	-
Black Lung Disability Trust Fund	0.5	0.5	1.0	1.0	-	-	-	-	-	-

*By law, certain expenses (costs) related to the administration of the above funds are not charged to the funds and are financed by other sources.

In the Federal budget, the term "trust fund" means only that the law requires a particular fund be accounted for separately, used only for a specified purpose, and designated as a "trust fund." A change in law may change the future receipts and the terms under which the fund's resources are spent. In the private sector, "trust fund" refers to funds of one party held and managed by a second party (the trustee) in a fiduciary capacity.

"Trust Fund Net Assets" represent the unexpended balance from all sources of receipts and amounts due the trust funds, regardless of source, including related Governmental transactions. These are transactions between two different entities within the Government (for example, monies received by one entity of the Government from another entity of the Government).

"Intragovernmental Net Assets" are comprised of investments in Federal debt securities, related accrued interest, and fund balances with Treasury. These amounts were eliminated in preparing these financial statements.

"Consolidated Assets" represent only the net assets from activity with individuals and organizations outside the Government. All related Governmental balances are removed to present the Government's position as a whole.

The majority of trust fund assets are invested in intragovernmental Treasury securities. These securities require redemption if a fund's disbursements exceeds its receipts. Redeeming these securities will increase the Government's financing needs and require more borrowing from the public (or less repayment of debt), or will result in higher taxes than otherwise would have been needed, or less spending on other programs than otherwise would have occurred, or some combination thereof.

Federal Old-Age and Survivors Insurance Trust Fund

This trust fund provides assistance and protection against the loss of earnings due to retirement or death in the form of money payments. The Social Security Administration (SSA) administers the Federal Old-Age and Survivors Insurance Trust Fund.

Payroll and self-employment taxes primarily fund the Federal Old-Age and Survivors Insurance Trust Fund. Interest earnings on Treasury securities, Federal agencies' payments for the Social Security benefits earned by military and Federal civilian employees, and Treasury payments for a portion of income taxes paid on Social Security benefits provide the fund with additional income. The law establishing the Federal Old-Age and Survivors Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 401.

Civil Service Retirement and Disability Fund

The Civil Service Retirement and Disability Fund covers two Federal civilian retirement systems: the Civil Service Retirement System (CSRS), for employees hired before 1984, and the Federal Employee Retirement System (FERS), for employees hired after 1983. The Office of Personnel Management administers the CSRS and the FERS systems. The laws establishing the Civil Service Retirement and Disability Fund and authorizing the depositing of amounts to the credit of the trust fund are set forth in 5 U.S.C. § 8334-8348. Funding sources include:

- Federal civilian employees' contributions.
- Agencies' contributions on behalf of employees.
- Appropriations.
- Interest earned on investments in Federal debt securities.

Federal Hospital Insurance Trust Fund (Medicare Part A)

The Federal Hospital Insurance Trust Fund finances the Hospital Insurance program (Medicare Part A). This program funds the cost of inpatient hospital and related care for individuals age 65 or older who meet certain insured status requirements, and eligible disabled people. Department of Health and Human Services (HHS) administers the program.

The Federal Hospital Insurance Trust Fund is financed primarily by payroll taxes, including those paid by Federal agencies. It also receives income from interest earnings on Treasury securities and a portion of income taxes paid on Social Security benefits. The law establishing the Federal Hospital Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1395i.

Military Retirement Fund

The Military Retirement Fund provides retirement benefits for Army, Navy, Marine Corps, and Air Force personnel, and their survivors. The fund is financed by DOD contributions, appropriations, and interest earned on investments in Federal debt securities. DOD administers the Military Retirement Fund. The laws establishing the Military Retirement Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 10 U.S.C. § 1461-1467.

Federal Disability Insurance Trust Fund

The Federal Disability Insurance Trust Fund provides assistance and protection against the loss of earnings due to a wage earner's disability in the form of money payments. SSA administers the Federal Disability Insurance Trust Fund.

Like the Federal Old-Age and Survivors Insurance Trust Fund, payroll taxes primarily fund the Federal Disability Insurance Trust Fund. The fund also receives income from interest earnings on Treasury securities, Federal agencies' payments for the Social Security benefits earned by military and Federal civilian employees, and a portion of income taxes paid on Social Security benefits. The law establishing the Federal Disability Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 401.

Unemployment Trust Fund

The Unemployment Trust Fund protects workers who lose their jobs. The program is administered through a unique system of Federal and State partnerships, established in Federal law, but executed through conforming State laws by State officials. The Department of Labor (DOL) administers the Federal operations of the program.

Taxes on employers primarily fund the Unemployment Trust Fund. However, interest earned on investments in Treasury securities also provides income to the fund. Appropriations have supplemented the fund's income during periods of high and extended unemployment. The law establishing the Unemployment Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1104.

Federal Supplementary Medical Insurance Trust Fund (Medicare Part B)

The Federal Supplementary Medical Insurance Trust Fund finances the Supplemental Medical Insurance program (Medicare Part B) that provides supplementary medical insurance for enrolled eligible participants to cover physician and outpatient services not covered by Medicare Part A. HHS administers the program.

The law establishing the Federal Supplementary Medical Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1395t.

Highway Trust Fund

The Highway Trust Fund was established to promote domestic interstate transportation and to move people and goods. The fund provides Federal grants to States for highway construction and related transportation purposes. The Department of Transportation (DOT) administers the Highway Trust Fund. The law establishing the Highway Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9503. Funding sources include earmarked taxes on gasoline and other fuels, certain tires, and vehicle and truck use.

Railroad Retirement Trust Fund

During fiscal 2000 and 2001, the Railroad Retirement Trust Fund provided annuities and survivor benefits to eligible railroad employees and their survivors. The fund also paid disability annuities based on total or occupational disability. Payroll taxes paid by railroad employers and their employees provide the primary source of income for the Railroad Retirement Survivor Benefit program. The law establishing the Railroad Retirement Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 45 U.S.C. § 231n.

Subsequent to fiscal 2001, the Railroad Retirement and Survivors' Improvement Act of 2001 (Public Law 107-90) was enacted. (See the Stewardship Information section on Railroad Retirement).

Airport and Airway Trust Fund

The Airport and Airway Trust Fund provides for airport improvement and airport facilities maintenance. It also funds airport equipment, research, and a portion of FAA's administrative operational support. DOT administers the Airport and Airway Trust Fund. The law establishing the Airport and Airway Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9502. Funding sources include:

- Taxes received from transportation of persons and property in the air, as well as fuel used in non-commercial aircraft.
- International departure taxes.
- Interest earned on investments in Treasury securities.

Hazardous Substance Superfund

The Hazardous Substance Superfund was authorized to address public health and environmental threats from spills of hazardous materials and from sites contaminated with hazardous substances. The Environmental Protection Agency (EPA) administers the fund. The law establishing the Hazardous Substance Superfund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9507. Funding sources include:

- Excise taxes collected on petroleum, chemicals, and imported substances (expired in 1995).
- Environmental taxes from corporations with alternative minimum taxable income in excess of $2 million (expired in 1995).
- Fines, penalties, and cost recoveries from responsible parties.
- Appropriations.
- Interest earned on investments in Treasury securities.

Black Lung Disability Trust Fund

The Black Lung Disability Trust Fund provides benefits to coal miners who are totally disabled due to pneumoconiosis (black lung disease). It also covers surviving dependents of miners who died due to pneumoconiosis.

Excise taxes on coal mine operators, based on the sale of coal, partially fund black lung disability payments as well as related administrative and interest costs. Intragovernmental advances to the Black Lung Disability Trust Fund, which must be repaid with interest, fund the shortfall. The Department of Labor administers the Black Lung Disability Trust Fund. The law establishing the Black Lung Disability Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9501.

Note 20. Indian Trust Funds

The Indian Trust Funds differ from other dedicated collections reported in Note 19. The Department of the Interior (DOI) has responsibility for the assets held in trust on behalf of American Indian tribes and individuals. The trust funds are held in accounts for approximately 315 tribes, 247,000 individual Native American accounts, and other funds, including the Alaska Native Escrow Fund.

The assets held in trust for Native Americans are owned by the trust beneficiaries and are not the Government's assets. Therefore, these amounts are not reflected in these Financial Statements except for their holdings of nonmarketable Treasury securities, for which the Government's liability is included in Federal debt securities held by the public.

For further information concerning disclosures about the Indian Trust Funds, please refer to the financial statements of the Department of Interior, Note 26. Indian Trust Funds.

Indian Trust Fund balances presented below do not include trust land managed by the Government.

U.S. Government as Trustee for Indian Trust Funds
Held for Indian Tribes and Other Special Trust Funds
Statement of Changes in Trust Fund Balances
as of September 30
(Unaudited)

(In millions of dollars)	2001	2000
Receipts	536.1	495.8
Disbursements	467.3	355.4
Receipts in excess of disbursements	68.8	140.4
Trust fund balances, beginning of year	2,736.2	2,595.8
Trust fund balances, end of year	2,805.0	2,736.2

U.S. Government as Trustee for Indian Trust Funds
Held for Individual Indian Monies Trust Funds
Statement of Changes in Trust Fund Balances
as of September 30
(Unaudited)

(In millions of dollars)	2001	2000
Receipts	225.9	245.2
Disbursements	221.7	294.6
Receipts in excess of disbursements	4.2	(49.4)
Trust fund balances, beginning of year	399.9	449.3
Trust fund balances, end of year	404.1	399.9

This page is intentionally blank.

United States Government Supplemental Information for the Year Ended September 30, 2001 (Unaudited)

Deferred Maintenance

"Deferred Maintenance" is the estimated cost to bring Government-owned property to an acceptable condition. That results from not performing maintenance on a timely basis. Deferred maintenance excludes the cost of expanding the capacity of assets or upgrading them to serve needs different from those originally intended. The consequences of not performing regular maintenance could include increased safety hazards, poor service to the public, higher costs in the future, and inefficient operations. Estimated deferred maintenance costs are not accrued in the Statements of Net Cost or recognized as a liability on the Balance Sheets.

The amounts disclosed for deferred maintenance on the table below have been measured using the following three methods:

- Condition assessment surveys are periodic inspections of the Government-owned property to determine the current condition and estimated cost to bring the property to an acceptable condition.
- Life-cycle cost forecast is an acquisition or procurement technique that considers operation, maintenance, and other costs in addition to the acquisition cost of assets.
- Management analysis method is founded on inflation-adjusted reductions in maintenance funding since the base year.

Some deferred maintenance has been deemed critical. Such amounts and conditions are defined by the individual agencies with responsibility for the safekeeping of these assets. Low and high estimates are based on the materiality of the estimated cost of returning the asset to the acceptable condition versus the total value of the corresponding asset.

Deferred Maintenance as of September 30

	Deferred Maintenance Cost Range		
(In billions of dollars)	Low Estimate	High Estimate	Critical Maintenance
Asset Category:			
Buildings, structures, and facilities	10.2	25.0	4.4
Furniture, fixtures, and equipment	0.4	1.1	0.7
Assets under capital lease	-	-	-
General property, plant and equipment land	-	-	-
Other general property, plant and equipment	-	0.2	-
Total general property, plant and equipment	10.6	26.3	5.1
Heritage assets	0.6	1.0	-
National defense assets	1.1	1.2	-
Stewardship land	-	-	-
Total stewardship assets	1.7	2.2	-
Total deferred maintenance	12.3	28.5	5.1

Unexpended Budget Authority

"Unexpended Budget Authority" is the sum of the unobligated and obligated, but unliquidated, budget authority.

Unobligated budget authority, including trust fund balances, is the cumulative amount of budget authority that is not obligated and that remains available for obligation. In 1-year accounts, the unobligated balance is not available for new obligations after the end of the fiscal year. In multiyear accounts, the obligated balance may be carried forward and remains available for obligation for the period specified. In no-year accounts, the unobligated balance is carried forward until specifically rescinded by law or until the purposes for which it was provided have been accomplished. The total unobligated budget authority amount balance for fiscal 2001 is $341 billion.

Obligated budget authority is the cumulative amount of budget authority that has been obligated but not liquidated. This balance can be carried forward for a maximum of 5 years after the appropriation has expired. The total obligated budget authority amount balance for fiscal 2001 is $693 billion.

For further information for Unexpended Budget Authority concerning unobligated and obligated Budget Authority, please refer to the corresponding Agency Financial Statements.

Tax Burden

The Internal Revenue Code provides for progressive rates of tax, whereby higher incomes are generally subject to higher rates of tax. The tables present the latest available information on income tax and related income, deductions and credit for individuals by income level and for corporations by size of assets.

Individual Income Tax Returns for Tax Year 1999

	Size of Adjusted Gross Income			
	Under $30,000	$30,000 under $75,000	$75,000 under $150,000	Greater than $150,000
Tax burden, percentage of gross income	6%	11%	15%	25%
Average tax per return	$795	$5,318	$15,354	$106,186
Percent of total deductions on taxable income	32%	32%	19%	17%
Percent of total credits against tax liability	23%	44%	16%	17%

Corporation Income Tax Returns for Tax Year 1998

	Size of Total Assets			
	Under $10 million	$10 million under $50 million	$50 million under $250 million	Greater than $250 million
Tax burden, percentage of gross income	0.37%	0.59%	1.09%	1.43%
Average tax per return	$3,600	$182,309	$839,925	$14,648,677
Percent of total deductions on taxable income	9%	4%	7%	80%
Percent of total credits against tax liability	28%	9%	8%	55%

For further information, including greater detail for the above tables, please refer to the Financial Statements of the Department of the Treasury—Accountability Report—Supplemental Information section: Other Accompanying Information. The Internal Revenue Service (IRS) compiles this information.

Other Information (Unaudited)

Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest) that may be paid for claims pending judicial review by the Federal courts or, internally, by appeals. The total estimated payout (including principal and interest) for claims pending judicial review by the Federal courts is $7.7 billion and $8.4 billion for fiscal 2001 and 2000, respectively. For those under appeal, the estimated payout is $13.6 billion and $13.5 billion for fiscal 2001 and 2000, respectively. Although these refund claims have been deemed to be probable, they do not meet the criteria in Statements of Federal Financial Accounting Standards (SFFAS) No. 5 for reporting the amounts in the Balance Sheets or for disclosure in the Notes to the Financial Statements. However, they meet the criteria in SFFAS No. 7 for inclusion as supplemental information. To the extent judgments against the Government for these claims prompt other similarly situated taxpayers to file similar refund claims, these amounts could become significantly greater.

This page is intentionally blank.

Appendix: List of Significant Government Entities Included and Excluded from the Financial Statements

This *Financial Report* includes the executive branch with their corresponding departments and entities and parts of the legislative and judicial branches, and other independent establishments and Government corporations. Excluded are privately owned Government-sponsored enterprises such as the Federal Home Loan Banks and the Federal National Mortgage Association. The Federal Reserve System is excluded because organizations and functions pertaining to monetary policy are traditionally separate from, and independent of, other central Government organizations and functions.

Significant Entities Included in these Statements:

Department of Agriculture (USDA)
www.usda.gov
Department of Commerce (DOC)
www.doc.gov
Department of Defense (DOD)
www.defenselink.mil
Department of Education (ED)
www.ed.gov
Department of Energy (DOE)
www.energy.gov
Department of Health and Human Services (HHS)
www.hhs.gov
Department of Housing and Urban Development (HUD)
www.hud.gov
Department of the Interior (DOI)
www.doi.gov
Department of Justice (DOJ)
www.usdoj.gov
Department of Labor (DOL)
www.dol.gov
Department of State (State)
www.state.gov
Department of the Air Force (Air Force)
www.af.mil
Department of the Army (Army)
www.army.mil
Army Corps of Engineers
www.usace.army.mil
Department of the Navy (Navy)
www.navy.mil
Department of Transportation (DOT)
www.dot.gov
Department of the Treasury (Treasury)
www.ustreas.gov
Department of Veterans Affairs (VA)
www.va.gov
U.S. Agency for International Development (USAID)
www.usaid.gov
Commodity Credit Corporation (CCC)
Commodity Futures Trading Commission (CFTC)
www.cftc.gov
Environmental Protection Agency (EPA)
www.epa.gov
Executive Office of the President
Export-Import Bank of the United States (Ex-Im Bank)
www.exim.gov
Farm Credit Administration (FCA)
www.fca.gov
Federal Communications Commission (FCC)
www.fcc.gov
Federal Deposit Insurance Corporation (FDIC)
www.fdic.gov
Federal Emergency Management Agency (FEMA)
www.fema.gov
Federal Trade Commission (FTC)
www.ftc.gov
General Accounting Office (GAO)
www.gao.gov
General Services Administration (GSA)
www.gsa.gov
Government Printing Office (GPO)
www.gpo.gov
Library of Congress (LC)
www.loc.gov
National Aeronautics and Space Administration (NASA)
www.nasa.gov
National Archives and Records Administration (NARA)
www.nara.gov
National Credit Union Administration (NCUA)
www.ncua.gov
National Science Foundation (NSF)
www.nsf.gov
National Transportation Safety Board (NTSB)
www.ntsb.gov
Nuclear Regulatory Commission (NRC)
www.nrc.gov
Office of Management and Budget (OMB)
www.whitehouse.gov/omb/

Entities Included, cont.

Office of Personnel Management (OPM)
www.opm.gov
Pension Benefit Guaranty Corporation (PBGC)
www.pbgc.gov
Railroad Retirement Board (RRB)
www.rrb.gov
U.S. Securities and Exchange Commission (SEC)
www.sec.gov
Small Business Administration (SBA)
www.sba.gov
Smithsonian Institution
www.si.edu
Social Security Administration (SSA)
www.ssa.gov
Tennessee Valley Authority (TVA)
www.tva.gov
U.S. Postal Service (USPS)
www.usps.gov

Significant Entities Excluded from these Statements:

Army and Air Force Exchange Service
Board of Governors of the Federal Reserve System
(Including the Federal Reserve Banks)
Federal National Mortgage Association (Fannie Mae)
Farm Credit System
Federal Home Loan Banks
Federal Retirement Thrift Investment Board
Financing Corporation
Federal Home Loan Mortgage Corporation
(Freddie Mac)
Marine Corps Exchange
Navy Exchange Service Command
Resolution Funding Corporation
U.S.A. Education Inc. (Sallie Mae)
Thrift Savings Fund