Section III - Financial Statements, Notes, Supplemental and Other Accompanying Information

Message from the Chief Financial Officer

I am pleased to present the U.S. Department of Health and Human Services (HHS) FY 2002 Performance and Accountability Report. For the first time, HHS is presenting its program performance report with the Department's financial results and program management and accountability information in a single, integrated document. Our intent is to provide a more comprehensive picture of HHS' efforts over the past year in pursuing its strategic and performance objectives, and to demonstrate accountability for the resources entrusted to HHS.

The HHS' Office of Inspector General has issued an unqualified, or "clean," audit opinion on the FY 2002 consolidated statements for the fourth consecutive year. While we are proud of this accomplishment, much work and opportunities for improvement remain. As such, this report not only reflects on our many accomplishments of FY 2002, but also looks ahead to the challenges of the future. The ongoing development and implementation of the Unified Financial Management System is the foundation for continued improvement in our financial management and reporting capabilities.

The Department is committed to providing timely and accurate financial information to HHS managers and stakeholders, and to ensuring that our business processes are efficient and customer-driven. HHS has undertaken numerous efforts to improve program and resource management processes, not only in the eyes of the Administration as articulated in the President's Management Agenda, but more importantly, to those who depend on HHS' many services. Technology is the key to serving our customers and stakeholders, and we are focused on strengthening our technological infrastructure to improve both operating capability and systems security.

This report contains comprehensive information on the Department's program performance, resource management, and stewardship responsibilities. It addresses the strides that HHS has made relative to the President's Management Agenda, including our progress in addressing such critical issues as reducing the occurrence of erroneous payments and improving our financial reporting and management processes. This document fully demonstrates our accountability and stewardship. In closing, I would like to acknowledge the dedication and professionalism of HHS staff throughout the Department who contributed to this report.

Janet Hale
Chief Financial Officer

U.S. Department of Health and Human Services
Consolidated Balance Sheet
As of September 30, 2002 and 2001
(in millions)

	2002	Restated 2001
Assets (Note 2)		
Intragovernmental		
Fund Balance with Treasury (Note 3)	$ 84,772	$ 80,949
Investments, Net (Note 5)	273,867	244,931
Accounts Receivable, Net (Note 6)	843	907
Anticipated Congressional Appropriation - CMS (Note 7)	10,399	11,166
Other Assets (Note 11)	150	94
Total Intragovernmental	$ 370,031	$ 338,047
Accounts Receivable, Net (Note 6)	4,150	4,165
Loans Receivable and Foreclosed Property, Net (Note 8)	370	427
Cash and Other Monetary Assets (Note 4)	375	137
Inventory and Related Property, Net (Note 9)	165	67
General Property, Plant & Equipment, Net (Note 10)	2,756	2,331
Other Assets (Note 11)	61	7
Total Assets	**$ 377,908**	**$ 345,181**
Liabilities (Note 12)		
Intragovernmental		
Accounts Payable	$ 270	$ 30
Accrued Payroll and Benefits	76	67
Other Liabilities (Note 17)	967	1,026
Total Intragovernmental	$ 1,313	$ 1,123
Accounts Payable	775	643
Entitlement Benefits Due and Payable (Note 13)	44,576	40,441
Environmental and Disposal Costs (Note 15)	15	16
Accrued Grant Liability (Note 16)	3,480	3,075
Loan Guarantees Liabilities (Note 8)	276	312
Federal Employee & Veterans Benefits (Note 14)	8,174	7,501
Accrued Payroll & Benefits	792	713
Other Liabilities (Note 17)	862	775
Total Liabilities	**$ 60,263**	**$ 54,599**
Net Position		
Unexpended Appropriations	73,786	70,051
Cumulative Results of Operations	243,859	220,531
Total Net Position	**$ 317,645**	**$ 290,582**
Total Liabilities & Net Position	**$ 377,908**	**$ 345,181**

The accompanying "Notes to the Principal Financial Statements" are an integral part of these statements. In addition, detailed information can be found in the following supplemental schedules: "Consolidating Balance Sheet by Operating Division" and "Consolidating Balance Sheet by Budget Function." Detailed OPDIV information can be found in the individual OPDIV financial reports.

U. S. Department of Health and Human Services
Consolidated Statement of Net Cost
For the Fiscal Years Ended September 30, 2002 and 2001
(in millions)

	2002				Restated 2001
	OPDIV	Inter-OPDIV Eliminations		HHS	HHS
Operating Division	Consolidated Totals	Costs (-)	Earned/Exchange Revenues (+) [1]	Consolidated Totals	Consolidated Totals
ACF	$ 45,959	$ (27)	$ 4	$ 45,936	$ 43,666
AoA	1,104	(2)	-	1,102	959
AHRQ	276	(5)	-	271	221
CDC	4,553	(113)	93	4,533	4,059
CMS	384,924	(46)	1	384,879	352,330
FDA	1,298	(78)	19	1,239	1,112
HRSA	5,794	(102)	27	5,719	5,220
IHS	2,857	(29)	20	2,848	2,677
NIH	20,575	(438)	93	20,230	17,013
OS	1,285	(73)	115	1,327	842
PSC	946	(22)	208	1,132	2,161
SAMHSA	2,883	(34)	9	2,858	2,648
Net Cost of Operations	**$ 472,454**	**$ (969)**	**$ 589**	**$ 472,074**	**$ 432,908**

[1] *Eliminations for non-exchange revenue are reported in the Statement of Changes in Net Position*

The accompanying "Notes to the Principal Financial Statements" are an integral part of these statements. In addition, detailed information can be found in the following supplemental schedules: "Consolidating Statement of Net Cost by Budget Function" and "Gross Cost and Exchange Revenue." Detailed OPDIV information can be found in the individual OPDIV financial reports.

U.S. Department of Health and Human Services
Consolidated Statement of Changes in Net Position
For the Fiscal Year Ended September 30, 2002
(in millions)

	Cumulative Results of Operations	Unexpended Appropriations	Total Net Position
Beginning Balances	$ 220,531	$ 70,051	$ 290,582
Prior period adjustments (+/-) (Note 20)	(51)	(67)	(118)
Unreconciled Transactions Affecting Change in Net Position	11	-	11
Beginning balances, as adjusted	$ 220,491	$ 69,984	$ 290,475
Budgetary Financing Sources:			
Appropriations received	-	338,688	338,688
Appropriations transferred-in/out (+/-)	-	(307)	(307)
Other adjustments (rescissions, etc) (+/-)	36	(9,165)	(9,129)
Appropriations used	325,414	(325,414)	-
Nonexchange revenue	170,231	-	170,231
Donations and forfeitures of cash and cash equivalents	47	-	47
Transfers-in/out without reimbursement (+/-)	(884)	-	(884)
Other budgetary financing sources (+/-)	223	-	223
Other Financing Sources:			
Donations and forfeitures of property	1	-	1
Imputed financing from costs absorbed by others	363	-	363
Other (+/-)	11	-	11
Total Financing Sources	$ 495,442	$ 3,802	$ 499,244
Net Cost of Operations (+/-)	472,074	-	472,074
Ending Balances	**$ 243,859**	**$ 73,786**	**$ 317,645**

The accompanying "Notes to the Principal Financial Statements" are an integral part of these statements.

U.S. Department of Health and Human Services
Combined Statement of Budgetary Resources
For the Fiscal Year Ended September 30, 2002
(in millions)

	Budgetary	NonBudgetary Credit Program Financing Accounts	Total
Budgetary Resources:			
Budget Authority			
Appropriations Received	$ 624,555	$ -	$ 624,555
Net transfers (+/-)	149	-	149
Other	1,954	-	1,954
Unobligated Balances			
Beginning of Period	6,288	330	6,618
Net transfers, actual (+/-)	(1,958)	-	(1,958)
Spending Authority from Offsetting Collections			
Earned			
Collected	4,029	52	4,081
Receivable from Federal sources	43	-	43
Change in unfilled customer orders			
Advance received	374	-	374
Without advance from Federal sources	217	-	217
Transfers from trust funds	2,388	-	2,388
Subtotal	$ 7,051	$ 52	$ 7,103
Recoveries of prior year obligations	7,623	-	7,623
Temporarily not available pursuant to Public Law	(30,910)	-	(30,910)
Permanently not available (-)	(4,097)	-	(4,097)
Total Budgetary Resources	**$ 610,655**	**$ 382**	**$ 611,037**
Status of Budgetary Resources:			
Obligations Incurred			
Direct	$ 599,614	$ 28	$ 599,642
Reimbursable	2,953	-	2,953
Subtotal	$ 602,567	$ 28	$ 602,595
Unobligated Balances - Available			
Apportioned	5,338	-	5,338
Exempt from apportionment	150	354	504
Unobligated Balances - Not Available	2,600	-	2,600
Total Status of Budgetary Resources	**$ 610,655**	**$ 382**	**$ 611,037**
Relationship of Obligations to Outlays:			
Obligated Balance, Net – Beginning of Period	$ 72,194	$ -	$ 72,194
Obligated Balance, Net - End of Period			
Accounts receivable (-)	(1,536)	-	(1,536)
Unfilled customer orders from Federal sources (-)	(607)	-	(607)
Undelivered orders	69,404	-	69,404
Accounts payable	9,119	-	9,119
Outlays			
Disbursements	590,124	28	590,152
Collections (-)	(6,417)	(52)	(6,469)
Subtotal	$ 583,707	$ (24)	$ 583,683
Less: Offsetting receipts	25,965	-	25,965
Net Outlays	**$ 557,742**	**$ (24)**	**$ 557,718**

The accompanying "Notes to the Principal Financial Statements" are an integral part of these statements. In addition, detailed information can be found in the following supplemental schedule: "Combining Statement of Budgetary Resources."

U.S. Department of Health and Human Services
Consolidated Statement of Financing
For the Fiscal Year Ended September 30, 2002
(in millions)

	OPDIV Consolidated Totals	Inter-OPDIV Eliminations	HHS Consolidated Totals
RESOURCES USED TO FINANCE ACTIVITIES:			
Budgetary Resources Obligated			
Obligations Incurred	$ 602,595	$ -	$ 602,595
Less: Spending Authority from Offsetting Collections and Recoveries	14,726	-	14,726
Obligations Net of Offsetting Collections and Recoveries	$ 587,869	$ -	$ 587,869
Less: Offsetting Receipts	25,965	-	25,965
Net Obligations	$ 561,904	$ -	$ 561,904
Non-Budgetary Resources			
Donations and Forfeitures of Property	$ 1	$ -	$ 1
Imputed Financing From Costs Absorbed by Others	416	(53)	363
Other Non-Budgetary Resources	11	-	11
Net Non-Budgetary Resources Used to Finance Activities	$ 428	$ (53)	$ 375
Total Resources Used to Finance Activities	**$ 562,332**	**$ (53)**	**$ 562,279**
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS:			
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered but Not Yet Provided	$ 4,399	$ -	$ 4,399
Resources That Fund Expenses Recognized in Prior Periods	44,740	-	44,740
Budgetary Offsetting Collections and Receipts That Do Not Affect Net Cost of Operations:			
Credit Program Collections That Increase Liabilities for Loans Guarantees or Allowances for Subsidy	(49)	-	(49)
Other	(720)	-	(720)
Resources That Finance the Acquisition of Assets or Liquidations of Liabilities	631	-	631
Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	87,102	-	87,102
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	$ 136,103	$ -	$ 136,103
Total Resources Used to Finance the Net Cost of Operations	**$ 426,229**	**$ (53)**	**$ 426,176**
COMPONENTS OF NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD			
Components Requiring or Generating Resources in Future Periods:			
Increase in Annual Leave Liability	$ 28	$ -	$ 28
Increase in Environmental and Disposal Liability	3	-	3
Increase in Exchange Revenue Receivable from the Public	745	-	745
Other	1,116	-	1,116
Accrued Entitlement Benefit Costs (CMS only)	44,576	-	44,576
Total Components of Net Cost of Operations That Will Require or Generate Resources in Future Periods	**$ 46,468**	**$ -**	**$ 46,468**
Components Not Requiring or Generating Resources:			
Depreciation and Amortization	$ 142	$ -	$ 142
Losses or (Gains) from Revaluation of Assets and Liabilities	(1)	-	(1)
Other	(384)	(327)	(711)
Total Components of Net Cost of Operations That Will Not Require or Generate Resources	$ (243)	$ (327)	$ (570)
Total Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Period	46,225	(327)	45,898
NET COST OF OPERATIONS	**$ 472,454**	**$ (380)**	**$ 472,074**

The accompanying "Notes to Principal Financial Statements" are an integral part of these statements.

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U.S. Department of Health and Human Services
Notes to the Principal Financial Statements
For the Fiscal Years Ended September 30, 2002 and 2001
(in millions)

Note 1. Significant Accounting Policies

Reporting Entity
The Department of Health and Human Services (HHS) consists of 12 Operating Divisions (OPDIVs) that have diverse missions and programs. There are 12 financial reporting entities:

1. Administration for Children and Families (ACF)
2. Administration on Aging (AoA)
3. Agency for Healthcare Research and Quality (AHRQ)
4. Centers for Disease Control and Prevention (CDC)/Agency for Toxic Substances and Disease Registry (ATSDR)
5. Centers for Medicare & Medicaid Services (CMS)
6. Food and Drug Administration (FDA)
7. Health Resources and Services Administration (HRSA)
8. Indian Health Service (IHS)
9. National Institutes of Health (NIH)
10. Office of the Secretary (OS) – excluding PSC
11. Program Support Center (PSC)
12. Substance Abuse and Mental Health Services Administration (SAMHSA)

The Agency for Toxic Substances and Disease Registry is combined with the Centers for Disease Control and Prevention for financial reporting purposes; therefore, these footnotes will refer to them as one OPDIV. In FY 2002, nine of the 12 financial reporting entities listed have received or will receive full scope audits, while the remaining three, AoA, AHRQ, and OS, were reviewed as part of the Departmental consolidated audit. Each OPDIV is considered a responsibility segment for purposes of preparing the HHS-wide Statement of Net Cost. A responsibility segment is a component of a reporting entity that is responsible for carrying out a mission, conducting a major line of activity, or producing one or a group of related products or services. The managers of the segments report to the entity's top management directly and their resources and results of operations can be clearly distinguished from those of other segments of the entity.

Basis of Presentation
The financial statements have been prepared to report the financial position and results of operations of HHS, pursuant to the requirements of 31 U.S.C. 351 (b), the Chief Financial Officers Act of 1990 (P.L. 101-576), as amended by the Reports Consolidation Act of 2000 (P.L. 106-531). They have been prepared from Departmental records in accordance with the form and content guidance of the Office of Management and Budget (OMB) Bulletin 01-09 and accounting principles generally accepted in the United States (GAAP) of the Federal Government promulgated by the Federal Accounting Standards Advisory Board (FASAB) and recognized by the American Institute of Certified Public Accountants (AICPA) as Federal GAAP. These statements are therefore different from financial reports prepared pursuant to other OMB directives that are primarily used to monitor and control HHS' use of budgetary resources.

Note 1. Significant Accounting Policies (continued)

The financial statements consolidate the balances of about one hundred and forty discrete appropriations and fund accounts, and a number of accounts used for suspense, collection of receipts and general government functions. Material intra-HHS balances have been eliminated in the consolidation of the account balances from the financial statements of HHS' twelve OPDIVs, each of which is issued under separate cover. The effects of the intra-entity transactions are eliminated in the presentation of the Consolidated Balance Sheet, Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position and the Consolidated Statement of Financing. The Statement of Budgetary Resources is presented on a combined basis. Supplemental information is accumulated from the OPDIV reports, regulatory reports and other sources within HHS. Information is generally presented on a summary level, hence greater detail on OPDIV programs and activities is found in the annual reports prepared by the OPDIVs.

Basis of Accounting

For most HHS programs, transactions are recorded on an accrual accounting basis and a budgetary basis. Under the accrual method, revenues are recognized when earned and expenses are recognized when resources are consumed, without regard to the payment of cash. Budgetary accounting facilitates compliance with legal constraints over the use of Federal funds. CMS uses the cash basis of accounting in the Medicare program to record benefit payments disbursed during the fiscal year, supplemented by the accrual method to estimate the value of benefit payments incurred but not yet paid as of the fiscal year end. A number of other OPDIVs also use the cash basis of accounting for some programs with an accrual adjustment made by recording year-end estimates of unpaid liabilities.

Changes in Accounting Principles

In FY 2002, CDC reclassified the ATSDR appropriation to the Health budget function, whereas in prior years it was classified to the Natural Resources and Environment budget function, based upon the fact that in prior years the funds were transferred to ATSDR from the Environmental Protection Agency. In FY 2002, for consistency with the President's budget, CDC reported all ATSDR funds from FY 2001 and FY 2002 to the Health Budget classification.

In FY 2002 CDC also changed its accounting practice from reporting biological products inventory as an asset to expensing them as acquired.

Entity and Non-Entity Assets

Entity assets are assets that the reporting entity has authority to use in its operations. The authority to use funds in an entity's operations means entity management has the authority to decide how funds are used, or management is legally obligated to use funds to meet entity obligations.

Note 1. Significant Accounting Policies (continued)

Non-entity assets are held by the entity but are not available to the entity. An example of non-entity assets is Child Support Enforcement collections, which ACF collects for the U.S. Government but does not have the authority to spend.

The HHS financial statements do not report entity and non-entity assets separately on the face of the statement, but instead break out entity and non-entity assets in footnote Note 2 – Non-Entity Assets.

Fund Balance with Treasury
The Department maintains all cash accounts with the Treasury Department. The account, "Fund Balance with Treasury," represents appropriated, revolving, trust and other funds available to pay current liabilities. The U.S. Treasury processes cash receipts and disbursements for HHS.

Investments
Trust fund balances are investments (plus the accrued interest on investments) held by Treasury. Law requires that trust fund investments that are not necessary to meet current expenditures be invested in "interest-bearing obligations of the United States or in obligations guaranteed as to both principal and interest by the United States."

Accounts Receivable
Accounts Receivable consists of amounts owed to the Department by other Federal agencies and by the public. Amounts due from the public are presented net of an allowance for loss on uncollectible accounts. The allowance for loss is based on past collection experience and/or an analysis of the outstanding balances. Accounts receivable also includes interest due to the Department that is directly attributable to accounts receivable.

Loans Receivable
Loans are accounted for as receivables after funds are disbursed. In accordance with credit reform legislation, for loans obligated prior to October 1, 1991, loan principal, interest, and other costs are reduced by an allowance for loss based on historical data and current market factors. For loans obligated on or after October 1, 1991, the amount of gross loans receivables is reduced by an allowance equal to the present value of the subsidy costs associated with these loans. Loans receivable also include interest due to the Department for direct loans and/or defaulted loan guarantees.

Advances to Grantees/Accrued Grant Liability
Advances to Grantees are cash outlays made by the Department to its grantees. An accrued grant liability occurs when the year-end grant accrual for the Department exceeds advances to grantees outstanding at year-end. Progress payments on work in process are not included in grants. HHS grants programs are classified into two categories: "Programs Not Subject to the Expense Accrual" and "Programs Subject to the Expense Accrual."

Note 1. Significant Accounting Policies (continued)

Programs Not Subject to the Expense Accrual: These programs are formula grants (also referred to as "block grants") under which states provide a variety of services or payments to individuals and Federal agencies. Expenses are recorded as the grantees draw funds. These programs operate on an allocation basis as opposed to a reimbursable basis. Therefore, they are not subject to an expense accrual.

Programs Subject to the Expense Accrual: For programs subject to the accrual, grantees draw funds (recorded as Advances to Grantees in HHS' accounting systems) as bills or salary payments come due. The grantees report actual disbursements quarterly and the amounts are recorded as an expense and a reduction to the advance balance in the accounting systems. At year-end, the OPDIVs use actual grant payments when this data is available. When actual grant payments are not available, HHS adopted a process to estimate the year-end grant accrual by relying on historical spending patterns to predict unreported grantee expenditures. The year-end accrual for these non-block grants is equal to the estimate of fourth quarter disbursements, plus an average of two weeks expenditures for expenses incurred prior to cash drawdowns. (Refer to Note 16 "Accrued Grant Liability.")

Advances other than grant advances are reported in Note 11 "Other Assets."

Inventory and Related Property
Inventory and Related Property includes Inventory Held for Sale, Operating Materials and Supplies and Stockpile Materials. Inventory Held for Sale consists of small equipment and supplies held by the various OPDIV Service and Supply Funds for sale to HHS components and other Federal entities. Operating Materials and Supplies consist of pharmaceuticals, biological products, vaccines, and other medical supplies that are used in providing medical services and conducting medical research. Stockpile Materials represent supplies of biological materials and vaccines held for use in case of a national emergency or other unanticipated needs.

All inventories, with the exception of CDC biological products, are recorded as assets when purchased and are expensed when they are consumed or sold. Inventories may be recorded at either: (1) historical cost (or a method which reasonably approximates historical cost), or (2) the lower of cost (using a weighted-average cost method) or market. CDC expenses biological products as acquired.

General Property, Plant and Equipment
The basis for recording purchased Property, Plant and Equipment (PP&E) is full cost, which includes all costs incurred to bring the PP&E to a form and location suitable for its intended use. The cost of PP&E acquired under a capital lease is the amount recognized as a liability for the capital lease at its inception. The cost of PP&E acquired through donation is the estimated fair value when acquired. The cost of PP&E transferred from other Federal entities

Note 1. Significant Accounting Policies (continued)

is the net book value of the transferring entity. All PP&E with an initial acquisition cost of $25,000 or more and an estimated useful life of two (2) years or greater are capitalized.

PP&E are depreciated using the straight-line method over the estimated useful life of the asset. Land and land rights, including permanent improvements, are not depreciated. Normal maintenance and repair costs are expensed as incurred.

Accounting for Internal Use Software was instituted in fiscal year 2001 in compliance with the FASAB Accounting Standard No. 10, *Accounting for Internal Use Software.* The capitalization threshold for internal use software costs for appropriated fund accounts is $1,000,000 or above. The capitalization threshold for revolving funds is $500,000. Costs below the threshold levels are expensed. The software is depreciated for a period of time consistent with the estimated useful life used for planning and acquisition purposes.

Liabilities

Liabilities are recognized for amounts of probable future outflows or other sacrifices of resources as a result of past transactions or events. Since HHS is a component of the U.S. Government, a sovereign entity, its liabilities cannot be liquidated without legislation that provides resources to do so. Payments of all liabilities other than contracts can be abrogated by the sovereign entity. In accordance with Public Law and existing Federal accounting standards, no liability is recognized for future payments to be made on behalf of current workers contributing to the Medicare Hospital Insurance Trust Fund, since future Medicare benefits are not tied to prior Medicare contributions.

Liabilities Covered by Budgetary Resources are those liabilities funded by available budgetary resources including: (1) new budget authority, (2) spending authority from offsetting collections, (3) recoveries of unexpired budget authority, (4) unobligated balances of budgetary resources at the beginning of the year, and (5) permanent indefinite appropriation or borrowing authority.

Liabilities Not Covered by Budgetary Resources are incurred when funding has not yet been made available through Congressional appropriations or current earnings. HHS recognizes liabilities for employee annual leave earned but not taken, and amounts billed by the Department of Labor for Federal Employees Compensation Act (FECA) disability payments. Also included in this category is the actuarial FECA liability determined by Labor but not yet billed. For HHS revolving funds, all liabilities are funded as they occur.

Liabilities Covered by Budgetary Resources and Liabilities Not Covered by Budgetary Resources are combined on the balance sheet. The breakout of these resources is presented in Note 12 “Liabilities Not Covered by Budgetary Resources”, Note 13 “Entitlement Benefits Due and Payable”, Note 15 “Environmental and Disposal Costs” and Note 17 “Other Liabilities”.

Note 1. Significant Accounting Policies (continued)

Accounts Payable
Accounts Payable consists of amounts due for goods and services received, progress in contract performance, interest due on accounts payable, and other miscellaneous payables.

Entitlement Benefits
Entitlement Benefits represents benefits due and payable to the public from entitlement programs enacted by law. In HHS the largest entitlement programs, which comprise the bulk of HHS entitlement spending, are the CMS programs for Medicare and Medicaid. The ACF administers a number of entitlement benefit programs. The larger programs are Temporary Assistance to Needy Families (TANF), Social Services Block Grant, and Child Support Enforcement.

Federal Employee and Veterans' Benefits
Federal Employee and Veterans' Benefits consist of the actuarial portions of future benefits earned by Federal employees and veterans, but not yet due and payable. These costs include pensions, other retirement benefits, and other post-employment benefits. These benefits are normally administered by the Office of Personnel Management (OPM) and not by the Department of Health and Human Services, or any of the individual operating divisions of the Department. Therefore, HHS does not recognize any liability in the balance sheet for pensions, other retirement benefits, and other post-employment benefits. HHS does, however, recognize the imputed cost and imputed financing related to these benefits in the Consolidated Statement of Net Cost and the Consolidated Statement of Changes in Net Position.

The lone exception to this policy is the Public Health Service (PHS) Commissioned Corps Retirement System. The HHS-administered PHS Commissioned Corps Retirement System is discussed in Note 14 "Federal Employee and Veterans' Benefits."

Revenue and Other Financing Sources
Funding for the Department is classified as revenue or other financing sources. Revenue is an inflow of resources that the government demands, earns, or receives by donation. Revenue comes from two sources: exchange transactions and nonexchange transactions. Exchange revenues arise when a government entity provides goods and services to the public or another government entity for a price. Another term for exchange revenue is earned revenue. Nonexchange revenue arises primarily from exercise of the government's power to demand payments from the public (e.g., taxes, duties, fines, and penalties), but also includes donations received. Other Financing Sources include appropriations used, transfers of assets from other government entities, and imputed financing.

Other Financing Sources: Congressional appropriations are the primary funding source for most of the Department's programs. For financial statement purposes, appropriations used are recognized as a financing source as expenses are incurred.

Note 1. Significant Accounting Policies (continued)

Imputed financing consists of costs incurred by one Federal entity, which are paid for by another Federal entity. OMB has limited the reporting of imputed costs to the following: 1) employee's pension benefits; 2) health insurance, life insurance, and other benefits for retired employees; 3) other post-employment benefits for retired, terminated, and inactive employees, which include severance payments, training and counseling, continued health care, and unemployment and workers' compensation under the FECA; and 4) losses in litigation proceedings (FASAB Interpretation No. 2, Accounting for Treasury Judgment Fund transactions).

Nonexchange Revenue: Nonexchange revenues include income taxes, excise taxes, duties, fines, penalties, and other inflows of resources arising from the government's power to demand payments, as well as voluntary donations. Nonexchange revenue is recognized when a reporting entity establishes a specifically identifiable, legally enforceable claim to cash or other assets. It is recognized to the extent that the collection is probable and the amount is measurable. Nonexchange revenue is reported in the Consolidated Statement of Changes in Net Position.

Medicare's Hospital Insurance program, or Medicare Part A, is financed through the Hospital Insurance Trust Fund, whose revenues come primarily through the Medicare portion of payroll and self-employment taxes collected under the Federal Insurance Contribution Act (FICA) and Self-Employment Contribution Act (SECA). The Medicare payroll tax rate is 2.9 percent of annual wages. Employees and employers are each required to contribute 1.45 percent of employees' wages, with no limitation, to the Hospital Insurance Trust Fund. Self-employed individuals pay the full 2.9 percent themselves.

Medicare's Supplemental Medical Insurance program, or Medicare Part B, is financed primarily by general fund appropriations (Payments to the Health Care Trust Funds) provided by Congress and by monthly premiums paid by beneficiaries. Premium payments from Medicare beneficiaries are matched approximately 3 to 1 by Congressional appropriations.

Exchange Revenue: Revolving funds recognize exchange revenue at the time goods or services are provided to the public or to another government entity. Reimbursable service agreements between HHS and other Federal agencies generally recognize these revenues when the related expenses are incurred. Various user fees are collected to offset the cost of providing services. Exchange revenue is reported in the Consolidated Statement of Net Cost.

Contingencies

A contingency is an existing condition, situation or set of circumstances involving uncertainty as to possible gain or loss to the Department. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. With the exception of pending, threatened or potential litigation, a contingent liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is more

(in millions)

Note 1. Significant Accounting Policies (continued)

likely than not, and the related future outflow or sacrifice of resources is measurable. For pending, threatened or potential litigation, a liability is recognized when a past transaction or event has occurred, a future outflow or other sacrifice of resources is likely, and the related future outflow or sacrifice of resources is measurable.

Use of Estimates in Preparing Financial Statements
Preparation of financial statements in accordance with Federal accounting standards requires HHS to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent liabilities, as of the date of the financial statements. Estimates and assumptions also affect the revenues and expenses accrued and reported in the financial statements. Actual results may differ from those estimates.

Intragovernmental Relationships and Transactions
In the course of its operations, HHS has relationships and financial transactions with numerous Federal agencies. The more prominent of these are the Social Security Administration (SSA) and the Department of the Treasury. The SSA determines eligibility for Medicare programs, and also allocates a portion of Social Security benefit payments to the Medicare Part B Trust Fund for Social Security beneficiaries who elect to enroll in the Medicare Part B program. The Treasury receives the cumulative excess of Medicare receipts and other financing over outlays, and issues interest-bearing securities in exchange for the use of those monies. At the government-wide level, the assets related to the trust funds on HHS' financial statements and the corresponding liabilities on the Treasury's financial statements would be eliminated.

Note 2. Non-Entity Assets

	2002	2001
Intragovernmental:		
Fund balance with Treasury	$ 5	$ 45
Accounts receivable	3	122
Other	-	-
Total Intragovernmental	$ 8	$ 167
Accounts receivable	$ 377	$ 34
Cash and other monetary assets	-	-
Other	-	-
Total non-entity assets	$ 385	$ 201
Total entity assets	377,523	344,980
Total Assets	$ 377,908	$ 345,181

(in millions)

Note 3. Fund Balance with Treasury

HHS' undisbursed account balances at September 30, 2002 and 2001 are listed below by fund type. Other Funds include balances in deposit, suspense, clearing and related non-spending accounts.

Fund Balances:

	2002	2001
Trust Funds	$ 3,201	$ 508
Revolving Funds	803	752
Appropriated Funds	80,208	79,358
Other Fund Types	560	331
Total	$ 84,772	$ 80,949

Status of Fund Balance with Treasury

	2002	2001
Unobligated Balance		
Available	$ 5,537	$ 1,336
Unavailable	3,242	8,282
Obligated Balance not yet Disbursed	75,993	71,331
Total	$ 84,772	$ 80,949

Note 4. Cash and Other Monetary Assets

Cash and Other Monetary Assets are the total amount of time account balances at the Medicare contractors' commercial banks. The Checks Paid Letter-of-Credit method is used for reimbursing Medicare contractors for the payment of covered Medicare services. Medicare contractors issue checks against a Medicare Benefits account maintained at commercial banks. In order to compensate commercial banks for handling the Medicare Benefits accounts, Medicare funds are deposited into non-interest bearing time accounts. The earnings allowances on the time accounts are used to reimburse the commercial banks. The account balance in FY 2002 was $375 million and in FY 2001 the balance was $137 million.

Note 5. Investments, Net

HHS invests trust fund cash in excess of current needs in U.S. Treasury securities. The U.S. Treasury Department is HHS' agent and advisor for investing. The majority of HHS' investments in securities are held to maturity and no provision is made for unrealized gains or losses. Investments at September 30, 2002 and 2001 are summarized below. All investments are considered entity assets.

(in millions)

Note 5. Investments, Net (continued)

As of September 30, 2002

	Cost	Unamortized (Premium) Discount	Investments, Net	Other Adjustments	Market Value Disclosure
Intragovernmental Securities					
Marketable	$ 27	$ -	$ 27	$ -	$ 27
Non-Marketable: Par Value	267,711	-	267,711	-	267,711
Non-Marketable: Market-based	1,853	44	1,897	-	1,897
Subtotal	$269,591	$ 44	$269,635	$ -	$269,635
Accrued Interest	4,232	-	4,232	-	4,232
Total, Intragovernmental	$273,823	$ 44	$273,867	$ -	$273,867

As of September 30, 2001

	Cost	Unamortized (Premium) Discount	Investments, Net	Other Adjustments	Market Value Disclosure
Intragovernmental Securities					
Marketable	$ 22	$ -	$ 22	$ -	$ 22
Non-Marketable: Par Value	239,115	-	239,115	(1)	239,114
Non-Marketable: Market-based	1,762	56	1,818	-	1,818
Subtotal	$ 240,899	$ 56	$ 240,955	$ (1)	$240,954
Accrued Interest	3,977	-	3,977	-	3,977
Total, Intragovernmental	$ 244,876	$ 56	$244,932	$ (1)	$244,931

CMS invests in U.S. Treasury Special Issues that are special public obligations for exclusive purchase by the Medicare trust funds. Special issues are always purchased and redeemed at face value. Certificates are short term and pay 4 3/8 percent. The bond interest rates range from 5 ¼ percent to 8 ¾ percent. The accrued interest receivable as of September 30, 2002 and 2001 was $4,232 million and $3,977 million, respectively.

HRSA's Vaccine Injury Compensation Trust Fund (VICP) and Ricky Ray Hemophelia Relief funds are invested in market-based(MK) special securities and One-Day Certificates. These non-marketable MK securities are Treasury securities that are not traded on any securities exchange but mirror the prices of marketable securities with similar terms. Currently, securities held by the VICP will mature in fiscal years 2003, 2004, 2006, and 2008.

NIH invests trust fund cash that is in excess of current needs in U.S. Treasury securities.

See Note 1 “Significant Accounting Policies” for information on amortization methods used.

(in millions)

Note 6. Accounts Receivable, Net

HHS' accounts receivable at September 30, 2002 and 2001 are summarized below.

As of September 30, 2002

	Accounts Receivable Principal	Interest Receivable	Accounts Receivable, Gross	Allowance	Net OPDIV Receivables Combined	Intra-OPDIV Eliminations	Net OPDIV Receivables Consolidated	Inter-OPDIV Eliminations	Net HHS Receivables Consol.
Intragovernmental									
Entity	$ 2,841	$ -	$ 2,841	$ -	$2,841	$(1,876)	$ 965	$ (125)	$ 840
Non-Entity	3	-	3	-	3	-	3	-	3
Total, Intragovernmental	$2,844	$ -	$ 2,844	$ -	$2,844	$(1,876)	$ 968	$ (125)	$ 843
With the Public									
Entity									
Medicare	$ 6,336	$ -	$ 6,336	$ (3,667)	$ 2,669	$ -	$ 2,669	$ -	$ 2,669
Other	2,273	-	2,273	(1,169)	1,104	-	1,104	-	1,104
Non-Entity	383	7	390	(13)	377	-	377	-	377
Total, With the Public	$ 8,992	$ 7	$ 8,999	$ (4,849)	$ 4,150	$ -	$ 4,150	$ -	$ 4,150

As of September 30, 2001

	Accounts Receivable Principal	Interest Receivable	Accounts Receivable, Gross	Allowance	Net OPDIV Receivables Combined	Intra-OPDIV Eliminations	Net OPDIV Receivables Consolidated	Inter-OPDIV Eliminations	Net HHS Receivables Consol.
Intragovernmental									
Entity	$ 5,123	$ 10	$ 5,133	$ -	$ 5,133	$ (4,270)	$ 863	$ (78)	$ 785
Non-Entity	122	-	122	-	122	-	122	-	122
Total, Intragovernmental	$ 5,245	$ 10	$ 5,255	$ -	$ 5,255	$ (4,270)	$ 985	$ (78)	$ 907
With the Public									
Entity									
Medicare	$ 7,522	$ -	$ 7,522	$ (4,428)	$ 3,094	$ -	$ 3,094	$ -	$ 3,094
Other	1,267	-	1,267	(230)	1,037	-	1,037	-	1,037
Non-Entity	6	568	574	(540)	34	-	34	-	34
Total, With the Public	$ 8,795	$ 568	$ 9,363	$ (5,198)	$ 4,165	$ -	$ 4,165	$ -	$ 4,165

CMS' Medicare receivables are primarily due to overpayments to providers, beneficiaries, physicians and suppliers, and to claims where Medicare should be the secondary payer.

HHS non-entity receivable balances represent amounts that cannot be used by HHS once collected. Such receipts are transferred to the General Fund of the Department of the Treasury.

The allowance for loss on accounts receivable is based upon analytical procedures on both individual and group bases. Individual analysis considers the debtor's ability and willingness

(in millions)

Note 6. Accounts Receivable, Net (continued)

to pay, payment record, and probable recovery of amounts from secondary sources (i.e., liens, and garnishments). To estimate allowance for loss by groups, HHS stratifies receivables into groups exhibiting similar characteristics. Estimated losses are projected based upon statistical sampling or historical loss experience. The allowance is periodically reviewed and adjusted.

Note 7. Anticipated Congressional Appropriation

Medicaid – Beginning in FY 1996, CMS has accrued an expense and liability for Medicaid claims Incurred But Not Reported (IBNR) as of September 30th. In FY 2002, the IBNR expense exceeded the available unexpended Medicaid appropriations in the amount of $10,399 million. A review of the appropriation language by CMS' Office of General Counsel has resulted in a determination that the Medicaid appropriation's indefinite authority provision allows for the entire IBNR amount to be reported as a funded liability. Consequently, CMS has recorded a $10,399 million anticipated appropriation in FY 2002 for IBNR claims that exceeded the available appropriation. The amount of Anticipated Congressional Appropriation recorded as of September 30, 2001 was $11,166 million.

Note 8. Direct Loans and Loan Guarantee Programs

HRSA operates guaranteed loan programs for the Health Center and Health Education Assistance Loans (HEAL) programs. For HEAL, the Administration guarantees payment of principal and interest made by private lenders to medical students, in various approved fields of practice, in the event of default, death or permanent disability. Health Center Program (Post-1991) guarantees the loans to HRSA grantees, made by non-Federal lenders.

Total loans guaranteed under these programs, as of September 30, 2002 and 2001 are summarized as follows.

	2002		2001	
HEAL Loan Guarantees:	No. of Loans	Amount	No. of Loans	Amount
Pre-1992 loans	63,403	$ 483	87,000	$ 730
Post-1991 loans	94,238	2,254	108,000	2,444
Health Centers Loan Guarantees	1	4	1	4
Total	157,642	$ 2,741	195,001	$ 3,178

(in millions)

Note 8. Direct Loans and Loan Guarantee Programs (continued)

The receivable amount reported in the Balance Sheet represents defaulted loans, which have been paid to lenders under the guarantee. The lenders are required to perform certain procedures in an effort to collect amounts due prior to submitting the loan for payment under the guarantee. An allowance has been established for estimated uncollectible amounts on the loans. The allowance is based on management's assessment of the future collectibility analysis of these aged loans based on the last date of collection.

HHS' loans receivable at September 30, 2002 and 2001 are summarized below.

September 30, 2002: Defaulted Guaranteed Loans:	Loans, Receivable, Principal	Interest Receivable	Loans Receivable, Gross	Allowance	Loans, Receivable, Net
HEAL Loans (HRSA)					
Pre-1992 Loans	$ 492	$ 12	$ 504	$ (201)	$ 303
Post-1991 Loans	87	2	89	(22)	67
Subtotal	$ 579	$ 14	$ 593	$ (223)	$ 370
Other					
Pre-1992 Loans	-	-	-	-	-
Post-1991 Loans	4	-	4	(4)	-
Total	$ 583	$ 14	$ 597	$ (227)	$ 370

September 30, 2001: Defaulted Guaranteed Loans:	Loans, Receivable, Principal	Interest Receivable	Loans Receivable, Gross	Allowance	Loans, Receivable, Net
HEAL Loans (HRSA)					
Pre-1992 Loans	$ 496	$ 13	$ 509	$ (134)	$ 375
Post-1991 Loans	65	2	67	(15)	52
Subtotal	$ 561	$ 15	$ 576	$ (149)	$ 427
Other					
Post-1991 Loans	4	-	4	(4)	-
Total	$ 565	$ 15	$ 580	$ (153)	$ 427

(in millions)

Note 8. Direct Loans and Loan Guarantee Programs (continued)

The liability amount reported in the Balance Sheet represents future estimated payouts on defaulted loans under the loan guarantee program. The post-1991 loan guarantee liability is established based on criteria set forth in accordance to Credit Reform. This Act requires that the present value of cash outflows, associated with the estimated amount to be paid out under loan guarantees for each fiscal year, be calculated to determine the liability. The calculation is performed using a computer model established by OMB, utilizing assumptions made by the HEAL program based on historical data, such as default rates and interest rates. The liability is adjusted and accounted for independently each year based on loans issued annually under the guarantee. The pre-1992 loan guarantee liability for losses is established based upon an average default rate of approximately 3.95 percent in 2002 and 4.3 percent in 2001. The liability is adjusted each year for the change in default rates.

The loan guarantee liability is summarized as follows:

	2002	Restated 2001
Loan Guarantee Liabilities:		
HEAL Loans (HRSA)		
Pre-1992 Loans	$ 17	$ 30
Post-1991 Loans	256	282
Subtotal	$ 273	$ 312
Other		
Post-1991 Loans	3	-
Total Loan Guarantee Liabilities	$ 276	$ 312

Loan guarantee subsidy expense:
Current year post-1991 HEAL subsidy methodology, using the credit subsidy model, was revised in fiscal year 2001, to account for historical interest rates versus applying current interest rates to the prior year Cohorts. Loan guarantee subsidy expense for the year ended September 2002 and 2001 is summarized as follows:

	2002	2001
Loan Defaults (Net of Recoveries)	$ 9	$ 10
Interest cohort	(24)	(33)
Other write-offs	(20)	3
Total current year subsidy	$ (35)	$ (20)
Re-estimates	(32)	(39)
Total Loan Guarantee Subsidy Expense	$ (67)	$ (59)

(in millions)

Note 9. Inventory and Related Property, Net

HHS' inventory and related property, net at September 30, 2002 and 2001 are summarized below.

	2002	2001
Inventory Held for Sale:		
Inventory Held for Current Sale	$ 29	$ 27
Total Inventory Held for Sale	$ 29	$ 27
Operating Materials and Supplies:		
Operating Materials and Supplies Held for Use	$ 10	$ 10
Operating Materials and Supplies Reserved for Future Use	-	8
Total Operating Materials and Supplies	$ 10	$ 18
Stockpile Materials:		
Stockpile Materials Held for Emergency or Contingency	$ 126	$ 22
Total Stockpile Materials	$ 126	$ 22
Inventory and Related Property, Gross	$ 165	$ 67
Less: Allowance for Loss/Obsolescence/Spoilage	-	-
Inventory and Related Property, Net	$ 165	$ 67

HHS inventories are comprised of inventory held for sale, operating materials and supplies used in general operations, and stockpile materials. Inventories are valued at historical cost.

NIH has an inventory of materials to support their day-to-day activities. The NIH inventory is valued using the moving average method and stated at cost. CDC is mandated by law to maintain vaccine stockpiles to meet unanticipated needs for the vaccines, and for use in national emergencies. Vaccine stockpiles are maintained by the vaccine manufacturers and consist of several types of vaccines. The PSC, through its Perry Point Supply Services Center, maintains an inventory of pharmaceutical items for sale to HHS components and other Federal agencies.

In FY 2002, CDC changed its accounting practice from reporting biological products inventory as an asset to expensing them as acquired.

(in millions)

Note 10. General Property, Plant and Equipment, Net

Major categories of HHS Property, Plant and Equipment at September 30, 2002 and 2001 are listed below.

			2002			2001
	Depreciation Method	Estimated Useful Lives	Acquisition Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Land & Land Rights			$ 48	$ -	$ 48	$ 48
Improvements to Land	Straight Line	5-20 Yrs	-	-	-	-
Construction in Progress			890	-	890	649
Buildings, Facilities & Other Structures	Straight Line	5-50 Yrs	1,556	(785)	771	1,206
Equipment	Straight Line	3-20 Yrs	804	(388)	416	392
Internal Use Software	Straight Line	Various	70	(16)	54	11
Assets Under Capital Lease	Straight Line	Life of Lease	60	(9)	51	25
Leasehold Improvements	Straight Line	*Life of Lease	893	(367)	526	-
Totals			$ 4,321	$ (1,565)	$2,756	$ 2,331

*7 to 15 years or life of lease.

See Note 1. Significant Accounting Policies for capitalization criteria and thresholds. See the disclosure *Deferred Maintenance* in the Required Supplementary Information section for information on deferred maintenance for General PP&E.

Note 11. Other Assets

Other Assets at September 30, 2002 and 2001 are comprised of the following, all of which are considered entity assets.

	2002	2001
Intragovernmental		
Advances to Other Federal Entities	$ 430	$ 272
Other	-	13
OPDIV Combined, Intragovernmental	430	285
Less: Intra-OPDIV Eliminations	(277)	(187)
OPDIV Consolidated, Intragovernmental	153	98
Less: Inter-OPDIV Eliminations	(3)	(4)
HHS Consolidated, Intragovernmental	$ 150	$ 94
With the Public		
Prepayments and Deferred Charges	$ 3	$ 5
Travel Advances and Emergency Employee Salary Advances	4	2
Other	54	-
HHS Consolidated, With the Public	$ 61	$ 7

(in millions)

Note 12. Liabilities Not Covered by Budgetary Resources

	2002	2001
Intragovernmental:		
Accounts Payable	$ -	$ -
Accrued Payroll and Benefits	16	17
Other	702	367
Total Intragovernmental	$ 718	$ 384
Entitlement Benefits Due and Payable	$ 11,291	$ 7,779
Environmental and Disposal Costs	14	15
Federal Employees and Veterans' Benefits	8,174	7,501
Accrued Payroll and Benefits	370	335
Other	364	407
Total Liabilities Not Covered by Budgetary Resources	$ 20,931	$ 16,421
Total Liabilities Covered by Budgetary Resources	39,332	38,178
Total Liabilities	$ 60,263	$ 54,599

Note 13. Entitlement Benefits Due and Payable

Entitlement Benefits Due and Payable represents benefits due and payable to the public at year-end from entitlement programs enacted by law. In HHS the largest entitlement programs, which comprise the bulk of HHS entitlement spending, are the Medicare and Medicaid, which are managed by CMS.

Following is a summary of Entitlement Benefits Due and Payable at September 30, 2002 and 2001.

	2002			2001		
	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
Medicare	$ 28,236	$ -	$ 28,236	$ 27,081	$ -	$ 27,081
Medicaid	5,049	11,291	16,340	5,581	7,779	13,360
Totals	$ 33,285	$ 11,291	$ 44,576	$ 32,662	$ 7,779	$ 40,441

(in millions)

Note 14. Federal Employee and Veterans' Benefits

HHS' Federal Employee and Veterans' Benefits at September 30, 2002 and 2001 are summarized below. These liabilities are not covered by budgetary resources.

	2002	2001
With the Public		
Liabilities Not Covered by Budgetary Resources		
PHS Commissioned Corp Pension Liability	$ 5,913	$ 5,664
PHS Commissioned Corp Post-retirement Health Benefits	1,984	1,545
Workers' Compensation Benefits (Actuarial FECA Liability)	277	292
Total, Federal Employee and Veterans' Benefits	$ 8,174	$ 7,501

PHS Commissioned Corps: HHS administers the Public Health Service (PHS) Commissioned Corps Retirement System for approximately 5,672 active duty officers and 4,605 retiree annuitants or survivors. Authorized by Public Law 78-410, it is a defined benefit plan and is noncontributory. The plan does not have accumulated assets; funding is provided entirely on a pay as you go basis by Congressional appropriations. Administrative costs are borne by the plan. The plan provides pension payments and medical benefits to eligible retirees. At September 30, 2002, the actuarial present value of accumulated plan pension benefits was $5,913 billion of which $536 million was not vested, and the liability for medical benefits was actuarially determined to be $1,984 million.

Significant assumptions used by the actuary in its reports on the pension and medical programs as of September 30, 2002, were as follows: interest on Federal securities of 6.25 percent, annual basic pay scale increase of 3.5 percent, and annual inflation of 3.0 percent. Withdrawal and retirement rates are based on the historical trends of officers in the PHS retirement system. The aggregate entry age normal actuarial cost method is used for both programs in the determination of their liabilities.

Workers' Compensation Benefits: The actuarial liability for future workers' compensation benefits includes the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases.

FY 2002	FY 2001
5.20% in Year 1	5.21% in Year 1
5.20% in Year 2 and thereafter	5.21% in Year 2 and thereafter

The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payment related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the OMB's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting in FY 2002 and 2001 appear above.

(in millions)

Note 14. Federal Employee and Veterans' Benefits (continued)

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) are applied to the calculation of projected future benefits. These factors are also used to adjust the methodology's historical payments to current year dollars. The compensation COLAs and CPIMs used in projections are displayed below as follows:

FY	COLA	CPIM
2003	1.80%	4.31%
2004	2.67%	4.01%
2005	2.40%	4.01%
2006+	2.40%	4.01%

Note 15. Environmental and Disposal Costs

Environmental and Disposal Costs are the costs of removing, containing, and/or disposing of (1) hazardous waste from property, or (2) material and or property that consists of hazardous waste at a permanent or temporary closure or shutdown of associated PP&E.

Following is a summary of HHS' Environmental and Disposal Costs at September 30, 2002 and 2001. Based on guidance from the U.S. Department of Treasury[1], Intragovernmental costs of $3 million reported by FDA in FY 2001 have been reclassified as With The Public.

At September 30, 2002:

	With The Public		
	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
CDC	$ -	$ 3	$ 3
FDA	1	3	4
NIH	-	8	8
Consolidated HHS Totals	$ 1	$ 14	$ 15

At September 30, 2001:

CDC	$ -	$ -	$ -
FDA	1	4	5
NIH	-	11	11
Consolidated HHS Totals	$ 1	$ 15	$ 16

[1] Email message from Treasury Financial Management Service, dated August 21, 2002.

(in millions)

Note 16. Accrued Grant Liability

Grant advances are liquidated upon the grantee's reporting of expenditures on the quarterly SF-272 Report (Federal Cash Transaction Report). In many cases, these reports are received several months after the grantee actually incurs the expense, resulting in an understated grant expense in the financial statements. To mitigate this, HHS developed Department wide procedures to estimate and accrue amounts due grantees for their expenses, both realized and accrued, through September 30, 2002 and 2001.

At fiscal year-end when OPDIVs record the estimated accrual for amounts due to grantees for their expenses, if the amount of outstanding advances exceeds the amount of the accrual, the OPDIV reports an asset for "Advances to Grantees." Otherwise, the OPDIV reports a liability called "Accrued Grant Liability", equal to the amount that the accrual exceeds the outstanding advances. For additional information on this subject see Note 1 under "Advances to Grantees/Accrued Grant Liability".

	2002	2001
Grant Advances Outstanding (before year-end grant accrual)	$ 14,860	$ 12,609
Less: Estimated Accrual for Amounts Due to Grantees	(18,340)	(15,684)
Net Grant Advances (Liability)	$ (3,480)	$ (3,075)

All advances other than grant advances are reported in Note 11, "Other Assets."

Note 17. Other Liabilities

At September 30, 2002:	Intragovernmental			With the Public		
	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
Advances from Others	$ 1	$ -	$ 1	$ -	$ -	$ -
Deferred Revenue	535	-	535	384	-	384
Liabilities for Deposit Funds, Clearing Accounts and Undeposited Collections	2	-	2	18	-	18
Contingent Liabilities	-	269	269	-	103	103
Capital Lease Liability	-	49	49	-	6	6
Custodial Liabilities	-	383	383	-	-	-
Vaccine Injury Compensation Program	-	-	-	-	251	251
Other	58	1	59	96	4	100
Combined OPDIV Totals	$ 596	$ 702	$1,298	$ 498	$ 364	$ 862
Less: Intra-OPDIV Eliminations	(277)	-	(277)	-	-	-
Connsolidated OPDIV Totals	$ 319	$ 702	$1,021	$ 498	$ 364	$ 862
Less: Inter-OPDIV Eliminations	(54)	-	(54)	-	-	-
Consolidated HHS Totals	$ 265	$ 702	$ 967	$ 498	$364	$ 862

(in millions)

Note 17. Other Liabilities (continued)

At September 30, 2001:	Intragovernmental			With the Public		
	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total	Liabilities Covered by Budgetary Resources	Liabilities Not Covered by Budgetary Resources	Total
Deferred Revenue	$ 205	$ 187	$ 392	$ 226	$ 29	$ 255
Liabilities for Deposit Funds, Clearing Accounts and Undeposited Collections	15	-	15	38	-	38
Contingent Liabilities	-	-	-	6	-	6
Capital Lease Liability	-	22	22	6	1	7
Custodial Liabilities	-	345	345	-	50	50
Vaccine Injury Compensation Program	-	-	-	-	327	327
Other	4,714	-	4,714	92	-	92
Combined OPDIV Totals	$4,934	$ 554	$5,488	$ 368	$ 407	$ 775
Less: Intra-OPDIV Eliminations	(4,222)	(187)	(4,409)	-	-	-
Consolidated OPDIV Totals	$ 712	$ 367	$1,079	$ 368	$ 407	$ 775
Less: Inter-OPDIV Eliminations	(53)	-	(53)	-	-	-
Consolidated HHS Totals	$ 659	$ 367	$1,026	$ 368	$ 407	$ 775

Deferred Revenue of $535 million is for the provision of goods and services. The Vaccine Injury Compensation Program (VICP), administered by HRSA, provides compensation for vaccine-related injury or death. The VICP liability of $251 million represents the estimated future payment value of injury claims outstanding for VICP as of September 30, 2002.

Through the issuance of grants, HRSA supports the operation of certain health centers under the Health Centers Consolidation Act of 1996. These grantees, and many of their health professionals, are provided malpractice insurance under the Federally Supported Health Centers Assistance Act. Settlement and awards are paid from a separate Fund in the Treasury (Appropriation 75x0365). Accordingly, there are numerous malpractice legal actions pending against these grantees, which, if settled, will be paid by HRSA. For FY2002, a preliminary contingent liability by HRSA's actuarial contractor is estimated to be $101 million. No loss accrual had been made for these cases outstanding at September 30, 2001.

(in millions)

Note 18. Leases

Capital Leases: HHS and it's OPDIVS have entered into various capital leases with Indian tribes and the General Services Administrations (GSA) for office and warehouse space. Lease terms vary from one to twenty years. Capitalized assets acquired under capital lease agreements and the related liabilities are reported at the present value of the minimum lease payments.

Operating Leases: HHS and its components also have commitments under various operating leases with private entities and GSA for office, laboratory spaces, and land. Leases with private entities have initial or remaining noncancelable lease terms from one to twenty years. GSA leases in general are cancelable within 120 days notice.

Following is a Summary of Net Assets under Capital Lease and Future Minimum Lease Payments at September 30, 2002 and 2001.

Table 1. Summary of Assets Under Capital Lease	2002	2001
Land and Building	$ 58	$ 31
Machinery and Equipment	1	1
Other	1	-
Subtotal	$ 60	$ 32
Less: Accumulated Amortization	(9)	(7)
Assets Under Capital Lease	$ 51	$ 25

Table 2. Future Minimum Lease Payments	2002		2001	
	Capital Leases	Operating Lease	Capital Leases	Operating Lease
Year 1	$ 5	$ 214	$ 3	$ 186
Year 2	5	231	3	191
Year 3	5	244	3	196
Year 4	5	256	3	192
Year 5	5	270	3	194
Later Years	81	629	40	339
Total Minimum Lease Payments	$ 106	$ 1,844	$ 55	$ 1,298
Less: Imputed Interest	(51)		(26)	
Total Capital Lease Liability	$ 55		$ 29	

U.S. Department of Health and Human Services
Notes to the Principal Financial Statements
For the Fiscal Years Ended September 30, 2002 and 2001
(in millions)

Note 19. Consolidated Gross Cost and Exchange Revenue by Budget Functional Classification

HHS' consolidated gross cost and exchange revenue by budget functional classification for the fiscal year ended September 30, 2002 and 2001 are summarized below.

	2002									2001
	Education Training and Social Services	Health	Medicare	Income Security	Admin. of Justice	Natural Resources/ Environment	OPDIV Combined Totals	Intra-HHS Eliminations	HHS Consolidated Totals	HHS Consolidated Totals
Intragovernmental										
Gross Cost	$ 96	$ 4,217	$ 254	$ 24	$ -	$ 1	$ 4,592	$ (970)	$ 3,623	$ 1,910
Less: Exchange Revenue	(9)	(1,058)	-	-	-	-	(1,067)	590	(478)	(448)
Net Cost, Intragovernmental	$ 87	$ 3,159	$ 254	$ 24	$ -	$ 1	$ 3,525	$ (380)	$ 3,145	$ 1,462
With the Public										
Gross Cost	$ 17,156	$192,218	$256,837	$29,768	$ 28	$ 10	$496,016	$ -	$ 496,016	$ 456,258
Less: Exchange Revenue	-	(1,129)	(25,959)	-	-	-	(27,087)	-	(27,087)	(24,812)
Net Cost, With the Public	$ 17,156	$191,089	$230,878	$29,768	$ 28	$ 10	$468,929	-	$ 468,929	$ 431,446
Totals										
Gross Cost	$ 17,252	$196,435	$257,090	$29,792	$ 28	$ 11	$500,608	$ (969)	$ 499,639	$ 458,168
Less: Exchange Revenue	(9)	(2,187)	(25,958)	-	-	-	(28,154)	589	(27,565)	(25,260)
Net Cost of Operations	$ 17,243	$194,248	$231,132	$29,792	$ 28	$ 11	$472,454	$ (380)	$ 472,074	$ 432,908

Note 20. Prior Period Adjustments

Prior period adjustments are included in the calculation of the net change in cumulative results of operations to correct errors and accounting changes with retroactive effect. Following is a summary of the prior period adjustments as of September 30, 2002 and 2001.

Increases (Decreases) to Equity	2002	2001
Correction of Errors	$ (33)	$ (32)
Change in Accounting Principles	(2)	6
Departmental Adjustments to Beginning Net Position	(72)	(458)
Total	$ (107)	$ (484)

Departmental Adjustments to Beginning Net Position represent audit adjustments booked by OPDIVs after the HHS audit deadlines, as well as an additional net position adjustment related to prior year intra-HHS eliminations. These adjustments are not included in the OPDIV statement figures used to compile the department-wide figures. Therefore, the Department must enter an adjustment to Beginning Net Position to reflect the Department's true beginning net position balance.

Note 21. Custodial Activity

ACF receives monies from the Internal Revenue Service for outlay to the states for Child Support. These monies represent delinquent child support payments withheld from Internal Revenue tax refunds. Receipts are transferred to appropriation 75X6234 to cover outlays. During FY 2002, receipts amounted to $1,466 million and outlays amounted to $1,494 million.

FDA's custodial activity involves collections for civil monetary penalties (CMP) assessed by the Department of Justice on behalf of FDA. Penalties are assessed for violations in areas such as illegally manufactured, marketed, and distributed animal feeds and drug products. Total CMP collections in FY 2002 were $373.7 million ($61.6 million for FY 2001). CMP collections are immediately forwarded to the Department of the Treasury and cannot be used for FDA operation.

Note 22. Medicare Benefit Payments

Medicare Claims Estimated Improper Payments Federal government audits require the review of programs for compliance with federal laws and regulations. Accordingly, the OIG reviewed a statistically valid sample of CMS' Medicare claims to determine that claims were paid properly by Medicare contractors, and that services were actually performed and were medically necessary. Medicare, like other insurers, makes payments based on a standard claims form. The internal claims process involves reviewing claims as billed and paying the correct amount for the services rendered. Based on the OIG statistical sample, the point estimate of improper Medicare benefit payments made during FY 2002 was $13.3 billion or about 6.3 percent of the $212.7 billion in processed fee-for-service payments reported by CMS. The estimated range of the improper payments at 95 percent confidence level is $8.2 billion to $18.4 billion, or about four percent to nine percent. The majority of the errors fell into four broad categories: lack of medical necessity; insufficient or no documentation; incorrect coding; and noncovered/unallowable services.

Cost Report Settlement Process The cost report settlement process represents the value of final outlays to providers based on fiscal intermediary (FI) audits, reviews and final settlements of Medicare cost reports. Institutional providers are required to file Medicare cost reports. For providers paid under the Prospective Payment System (PPS), the cost report includes costs that are not covered under PPS, such as disproportionate share hospital payments, indirect medical education payments, and other indirect costs. For providers paid on a cost basis, the cost report represents the total costs incurred by the provider for medical services to patients and reflects the final distribution of these costs to the Medicare program.

In FY 2002, 30,430 cost reports totaling $88.5 billion were reviewed. Approximately $72.4 billion represented inpatient claims to PPS providers. The cost report settlements, therefore, focused on the remaining non-PPS balance of about $16.1 billion.

(in millions)

Note 22. Medicare Benefit Payments (continued)

Following is a summary of cost reports reviewed and the amount of costs claimed and disallowed as of September 30, 2002 and 2001.

	Cost Report Summary					
	2002			2001		
	Desk Reviews & Other	Audits	Total	Desk Reviews & Other	Audits	Total
Cost Reports Reviewed	27,098	3,332	30,430	30,393	3,725	34,118
Costs Claimed	$ 35,469	$53,076	$ 88,545	$36,810	$ 55,891	$92,701
Costs Disallowed	$ 119	$ (141)	$ (22)	$ 407	$ 350	$ 757

In FY 2002, the cost report audits did not result in cost savings (which would have shown a positive number, as was the case in FY 2001). Instead, the audits determined that in relation to the costs claimed on the cost reports, providers were due $141 million. When the amount due to providers (a negative balance of $141 million) is combined with the disallowed costs determined by the desk reviews of $119 million, a net of $22 million is due to providers.

Potential Liability The CMS routinely processes and settles cost reports and payment issues for institutional providers and healthcare insurers. As part of this process, some providers/insurers have filed suits challenging the amount of reimbursement to which they claim entitlement. The CMS cannot reasonably estimate the probability of the providers successfully winning their suits or the exact amount of the potential loss to the Medicare trust funds. In the opinion of management, the resolution of these matters will not potentially have a material impact on the results of operations and financial condition.

Note 23. Federal Matching Contribution

Supplemental Medical Insurance program (SMI) benefits and administrative expenses are financed by monthly premiums paid by Medicare beneficiaries and are matched by the federal government through the general fund appropriation, Payments to the Health Care Trust Funds. Section 1844 of the Social Security Act authorizes appropriated funds to match SMI premiums collected, and outlines the ratio for the match as well as the method to make the trust funds whole if insufficient funds are available in the appropriation to match all premiums received in the fiscal year. The monthly SMI premium per beneficiary was $50 from October 2001 through December 2001 and $54 from January 2002 through September 2002. Premiums collected from beneficiaries totaled $24.4 billion in FY 2002 and were matched by a $76.7 billion contribution from the Federal government.

(in millions)

Note 24. Contingencies

The Department and its components are parties to various administrative proceedings, legal actions, and claims brought by or against it. These contingencies arise in the normal course of operations and their ultimate disposition is unknown. Management, in consultation with legal counsel, has determined that it is reasonably possible that certain claims may result in an adverse outcome to the Department. However, an estimate of the range of possible liability cannot be determined. Based on information currently available, 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 of the Department.

Obligations Related to Cancelled Appropriations Payments may be required of up to one percent of current year appropriations for valid obligations incurred against prior year appropriations that have been cancelled. The total payments related to cancelled appropriations are estimated at $983 million and $1,197 million as of September 30, 2002 and 2001, respectively.

Note 25. Apportionment Categories of Obligations Incurred

Obligations incurred by apportionment categories are as follows:

	Direct	Reimbursable	Totals
Category A	$ 100,490	$ 2,831	$ 103,321
Category B	495,257	122	495,379
Exempt from apportionment	3,895	-	3,895
Total Obligations Incurred	$ 599,642	$ 2,953	$ 602,595

Note 26. Legal Arrangements Affecting Use of Unobligated Balances

Unobligated balances consist of appropriated funds, revolving fund, Management Fund, trust funds, NIH's Cooperative Research and Development Agreement (CRADA) fund and royalty's fund. Annual appropriations are available for new obligations in the year of appropriation and for adjustments to valid obligations for five subsequent years. Revolving funds are no year funds without any time limit. The NIH Management fund is available for two fiscal years. The trust funds are also no year funds without time limits. NIH's CRADA funds are available for the performance of the contractual agreement.

FDA has a Contingency Fund that was established in FY 1983 whereby funds are to be used for unusual direct costs of product emergencies (i.e., Tylenol incident, Breast Plant Hotline, etc.). Two rules were set for this fund: (1) only for emergency costs exceeding $100 thousand over the normal budget and (2) any use has to be specifically apportioned and approved by OMB. During FY 2002, FDA had funds of $1.1 million temporarily not available for national public health emergencies. FDA received $151.1 million in funding in FY 2002, to remain available until expended, to support Counter Terrorism projects.

Note 27. Exchange Revenue

The pricing policy for exchange revenue at HHS is to establish prices at full cost and to incur no profit or loss. Most OPDIVs either charge full cost, or are implementing procedures to do so. Several Operating Divisions at HHS collect revenue related to reimbursable agreements and recognize the revenue when expenses are incurred. In addition to reimbursable agreements, OPDIVs recognize exchange revenue related to collection of various user fees and recognize the exchange revenue when expenses are incurred.

Note 28. Explanation of Differences Between the Statement of Budgetary Resources (SBR) and the Budget of the United States Government

Statement of Federal Financial Accounting Standard (SFFAS) No. 7, "Accounting for Revenue and Other Financing Sources" calls for disclosure of "explanations of any material differences between the information required by paragraph 77 [of SFFAS 7] and the amounts described as 'actual' in the "*Budget of the United States Government"* (also called the "President's Budget"). Paragraph 77 of SFFAS 7 calls for presentation of total budgetary resources available to a reporting entity, the status of those resources, and outlays of the reporting entity. This information is provided in the Department's SBR (see page III.6).

The President's Budget with actual numbers for FY 2002 has not yet been published, and therefore no comparisons can be made between FY 2002 amounts presented in the SBR with amounts reported in the 'actual' column of the President's Budget. The President's Budget is expected to be released on February 3, 2003, and may be obtained from the Office of Management and Budget or the U.S. Government Printing Office at that time.

Note 29. Explanation of Differences Between Liabilities Not Covered by Budgetary Resources and Components Requiring or Generating Resources in Future Periods

The Balance Sheet uses proprietary accounts to disclose liabilities combining funded by budgetary resources and not funded by budgetary resources on the same line. The covered and not covered liabilities use budgetary accounts for the footnote disclosure in the financial statements.

The Statement of Financing reconciles the budgetary accounts with the proprietary accounts. The future funding of transactions included in net costs for the period, and the budgetary resources from future periods used for the obligations, are reconciling items. The reconciling items include liabilities and other transactions such as increases in exchange revenue from the public.

The differences between the liabilities not covered by budgetary resources and components requiring or generating resources in future periods are created by the budgetary basis of accounting required for reporting requirements and the proprietary basis of accounting required to prepare the Balance Sheet and FACTS I reporting.

Note 30. Permanent and Indefinite Appropriations

The HHS permanent and indefinite accounts have both budget authority available without current action by Congress and indefinite authority meaning there is no specific sum at the time the authority is granted. The list below includes the Treasury Fund Symbols, the availability (fiscal year or no year), and the titles of the accounts.

75 0340 – (fiscal year) Health Education Assistance Loans Program
75X0513 – (no year) Payments for Credits Against Health Care Contributions
75X0585 – (no year) Taxation on OASDI Benefits
75 1552 – (fiscal year) Temporary Assistance for Needy Families
75X1553 – (no year) Children's Research and Technical Assistance
75X4305 – (no year) Health Professions Graduate Student Loan Insurance Fund, Liquidating Account
75X8250 – (no year) Gifts and Donations
7520X8004 – (no year) Federal Supplementary Medical Insurance Trust Fund
7520X8005 – (no year) Federal Hospital Insurance Trust Fund

U.S. Department of Health and Human Services
Stewardship Property, Plant, and Equipment
For the Fiscal Year Ended September 30, 2002

HHS has two types of property, plant, and equipment (PP&E) for stewardship reporting: Heritage Assets and Indian Trust Lands. The Indian Health Service (IHS) reports both types.

Heritage Assets are PP&E of historical, natural, cultural, educational, or artistic significance. Heritage Assets are generally expected to be preserved indefinitely. This category includes buildings on the National Historic Register, cemetery sites, etc.

Stewardship Land includes land and land rights other than that acquired for or in connection with general PP&E. "Land" is defined as the solid part of the surface of the earth, excluding natural resources related to land. Examples of Stewardship Land include land used as forests and parks, and land used for wildlife and grazing.

Indian Trust lands are those lands that do not meet the definition of Stewardship Land, but are held by IHS as separate and distinct, because of the Federal government's long-term trust responsibility. All Indian Trust lands, when no longer needed by IHS in connection with its General PP&E, must be returned to the Department of the Interior's Bureau of Indian Affairs for continuing trust responsibility and oversight. IHS separately reports Indian Trust land parcels by site and installation numbers, and Indian Trust lands from General PP&E situated thereon.

IHS Stewardship Classes

Asset Descriptions	Number of Sites	Total Square Footage	Federal Hectares	Total Hectares
Heritage Assets	3	3,429	2 (5 acres)	2 (5 acres)
Indian Trust Lands	83	N/A	442.8 (1,107 acres)	442.8 (1,107acres)

Distribution of Stewardship Assets by Type and Area

	Heritage Assets			Indian Trust Lands	
	Number of Sites	Square Footage	Total Hectares	Number Of Sites	Total Hectares
Aberdeen				9	75
Alaska	2	1,134	2		
Albuquerque				4	4
Bemidji				2	9
Billings				7	48
Navajo				34	256
Oklahoma City				2	10
Phoenix	1	2,295		15	27
Portland				5	2
Tucson				5	12
Total-IHS	3	3,429	2	83	443

U.S. Department of Health and Human Services
Investment in Nonfederal Physical Property
For the Fiscal Year Ended September 30, 2002

Investment in Nonfederal Physical Property refers to expenses incurred by the Federal Government for the purchase, construction, or major renovation of physical property owned by state, local, or tribal governments: including major additions, alterations and replacements; the purchase of major equipment and the purchase or improvement of other physical assets. Cash grants related to nonfederal physical property programs are included in this decision, but grants for maintenance and operations are not considered investments. In HHS, the only investment in nonfederal physical property relates to former federal properties donated by the Indian Health Service (IHS).

Former federal properties are sites, built with federal funds, over which ownership has been transferred to state, local or Indian tribes through the Indian Self-determination and Education Assistance Act, Public Law 93-638, Section 105(f)(2), as amended. This act allows IHS to donate to an Indian tribe or tribal organization title to any personal or real property. Under this authority, the final regulations governing these transfers were developed and published on June 24, 1996, as 25 CFR Part 900.

During FY 1999, IHS transferred two properties in Oklahoma City, Oklahoma to tribal governments. HHS has made no new investments in nonfederal physical property since FY 1999.

U.S. Department of Health and Human Services
Investment in Human Capital
For the Fiscal Year Ended September 30, 2002

"Investments in Human Capital" are expenses incurred by federal education and training programs for the public, which are intended to maintain or increase national productive capacity. Two operating divisions of the Department conduct education and training programs under this category: Administration for Children and Families, and the National Institutes of Health.

Administration for Children and Families (ACF)

ACF is able to estimate investment in human capital for the Administration for Developmental Disabilities (ADD) using existing data collection activities. Under ADD, 55 grants were awarded for Projects of National Significance (PNS). PNS grants are awarded to public or private, non-profit institutions to enhance the independence, productivity, integration and inclusion into the community of people with developmental disabilities. Monies also support the development of national and state policy to serve this community. For FY 2002 and FY 2001, grants awarded totaled $6 million each year.

ACF is unable to provide baseline data for two of its programs for FY 2002 and FY 2001. Under both the Temporary Assistance to Needy Families (TANF) program and the Office of Refugee Resettlement (ORR), States have flexibility in how they spend their money.

National Institutes of Health (NIH)

The NIH Research Training and Career Development Program addresses the need for trained personnel to conduct medical research. The primary goal of the support that NIH provides for graduate training and career development is to produce new, highly trained investigators who are likely to perform research that will benefit the Nation's health. Our ability to maintain the momentum of recent scientific progress and our international leadership in medical research depends upon the continued development of new, highly trained investigators.

OPDIV/PROGRAM	2002	2001	2000	1999	1998
ACF					
Administration on Developmental Disabilities	$6	$6	$8	$6	$1
NIH					
Research Training and Career Development	1,248	1,118	871	820	660
Totals	**$1,254**	**$1,124**	**$879**	**$826**	**$661**

U.S. Department of Health and Human Services
Investment in Research and Development
For the Fiscal Year Ended September 30, 2002

OPDIV (1)	2002 Basic	2002 Applied	2002 Develop-Mental	2002 Total	2001 Total	2000 Total	1999 Total	1998 Total	Grand Total
ACF		$ 29		$ 29	$ 32	$ 30	$ 19	$ 13	$ 123
AHRQ		150		150	127	95	97	139	608
CDC		533		533	557	505	433	398	2,426
FDA		23	$ 6	29	26	26	19	53	153
HRSA		16		16	16	15	18	44	109
NIH	$11,435	7,623		19,058	16,007	14,690	13,580	11,038	74,373
Totals	**$11,435**	**$8,374**	**$ 6**	**$19,815**	**$16,765**	**$15,361**	**$14,166**	**$11,685**	**$77,792**

(1) ACF's and NIH's FY 2001 amounts have been restated.
AHRQ's FY 2000 amount has been restated.
FDA's FY 1999 amount has been restated.

The many research and development programs in HHS include the following:
FDA has two programs that meet the requirements of research and development investments: Orphan Products Development (OPD) Program and FDA Research Grants Program. While FDA's center components conduct scientific studies, FDA does not consider this type of research as "research and development" because it is used to support FDA's regulatory policy and decision-making processes.

The OPD Program was established by the Orphan Drug Act (PL 97-414, as amended) with the purpose of identifying orphan products and facilitating their development. An orphan product is a drug, biological product, medical device, or medical food that is intended to treat a rare disease or condition (i.e., one with a prevalence of fewer than 200,000 people in the United States.)

The FDA Research Grants Program is a grants program which is listed as No. 93-103 under the Catalog of Federal Domestic Assistance, whose purpose is to assist public and non-public institutions and for-profit organizations to establish, expand, and improve research, demonstration, education, and information dissemination activities concerned with a wide variety of FDA areas.

HIV/AIDS prevention, Infectious Diseases, and Environmental and Occupational Health were the primary areas where CDC's research and development was invested.

The NIH Research Program includes all aspects of the medical research continuum, including basic and disease-oriented research, observational and population-based research, behavioral research, and clinical research, including research to understand both health and disease states, to move laboratory findings into medical applications, to assess new treatments or compare different treatment approaches; and health services research. NIH regards the expeditious transfer of the results of its medical research for further development and commercialization of products of immediate benefit to improved health as an important mandate.

ACF, HRSA and AHRQ oversee research and development programs that contribute to a better understanding of how to improve the economic and social well being of families and children so that they lead more healthy and productive lives.

U.S. Department of Health and Human Services
Social Insurance
For the Fiscal Year Ended September 30, 2002

Medicare, the largest health insurance program in the country, has helped fund medical care for the nation's aged and disabled for almost four decades.

The required supplementary stewardship information (RSSI) contained in this section is presented in accordance with the requirements of the Federal Accounting Standards Advisory Board (FASAB). Included are a description of the long-term sustainability and financial condition of the program and a discussion of trends revealed in the data.

RSSI material is generally drawn from the *2002 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*,[1] which represents the official government evaluation of the financial and actuarial status of the Medicare trust funds. Unless otherwise noted, all data are for calendar years, and all projections are based on the Trustees' intermediate set of assumptions.

Printed copies of the Trustees Report may be obtained from CMS's Office of the Actuary (410-786-6386). The report is also available online at www.hcfa.gov/pubforms/tr/.

Please note that the 2002 Trustees Report for Medicare (issued March 26, 2002) was used as the source document for this FY 2002 financial report. We anticipate that the Government-wide financial statement report for FY 2002 (expected to be issued March 31, 2003) will contain updated information from the 2003 Trustees Report (which is expected to be issued on or near March 15, 2003). Thus, some data related to the Medicare trust funds contained in this FY 2002 financial report may differ from that contained in the FY 2002 *Financial Report of the United States Government*.

Actuarial Projections

Cashflow in Nominal Dollars

Using nominal dollars[2] for short-term projections paints a reasonably clear picture of expected performance with particular attention on cashflow and trust fund balances. Over longer periods, however, the changing value of the dollar can complicate efforts to compare dollar amounts in different periods and can create severe barriers to interpretation, since projections must be linked to something that the mind can comprehend in today's experience.

For this reason, long-range (75-year) Medicare projections in nominal dollars are seldom used and are not presented here. Instead, nominal-dollar estimates for the HI trust fund are displayed only through the projected date of depletion, currently the year 2030. Estimates for SMI are presented only for the next 10 years, primarily due to the fact that under present law, the SMI trust fund is automatically in financial balance every year.

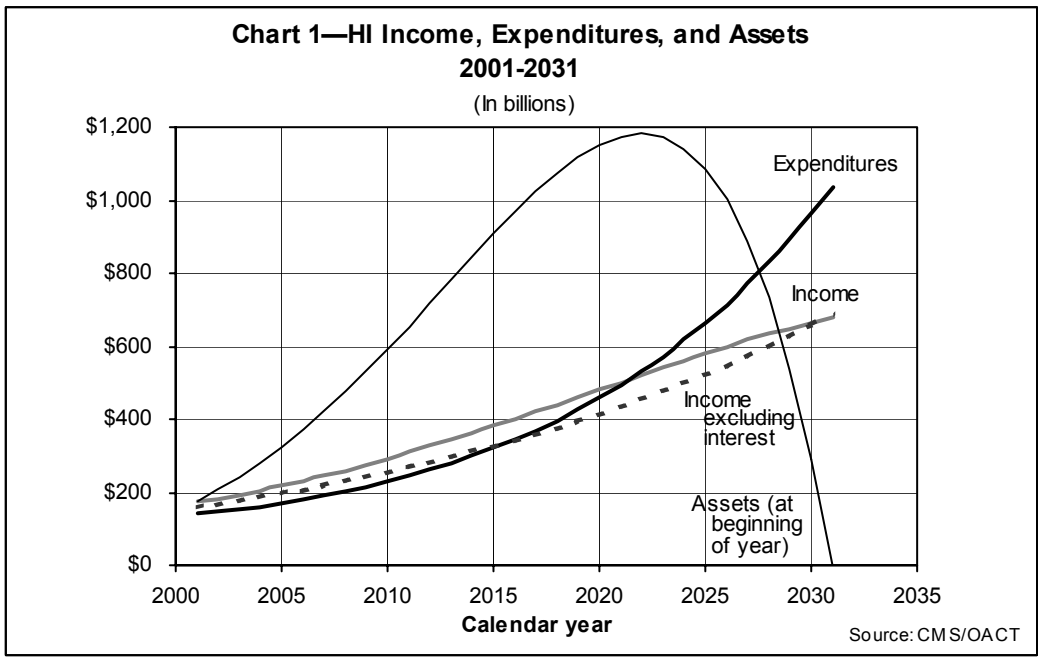
HI

Chart 1 shows the actuarial estimates of HI income, expenditures, and assets for each of the next 30 years, in nominal dollars. Income includes payroll taxes, income from the taxation of Social Security benefits, interest earned on the U.S. Treasury securities held by the trust fund, and other miscellaneous revenue. Expenditures include benefit

1. In past years, separate annual reports were issued for the HI and SMI trust funds. Beginning in 2002, the reports have been combined to more effectively convey the financial outlook for the Medicare program as a whole.

2. Dollar amounts that are not adjusted for inflation or other factors are referred to as "nominal."

payments and administrative expenses. The estimates are for the "open group" population—all persons who will participate during the period as either taxpayers or beneficiaries, or both—and consist of payments from, and on behalf of, employees now in the workforce, as well as those who will enter the workforce over the next 30 years. The estimates also include expenditures attributable to these current and future workers, in addition to current beneficiaries.



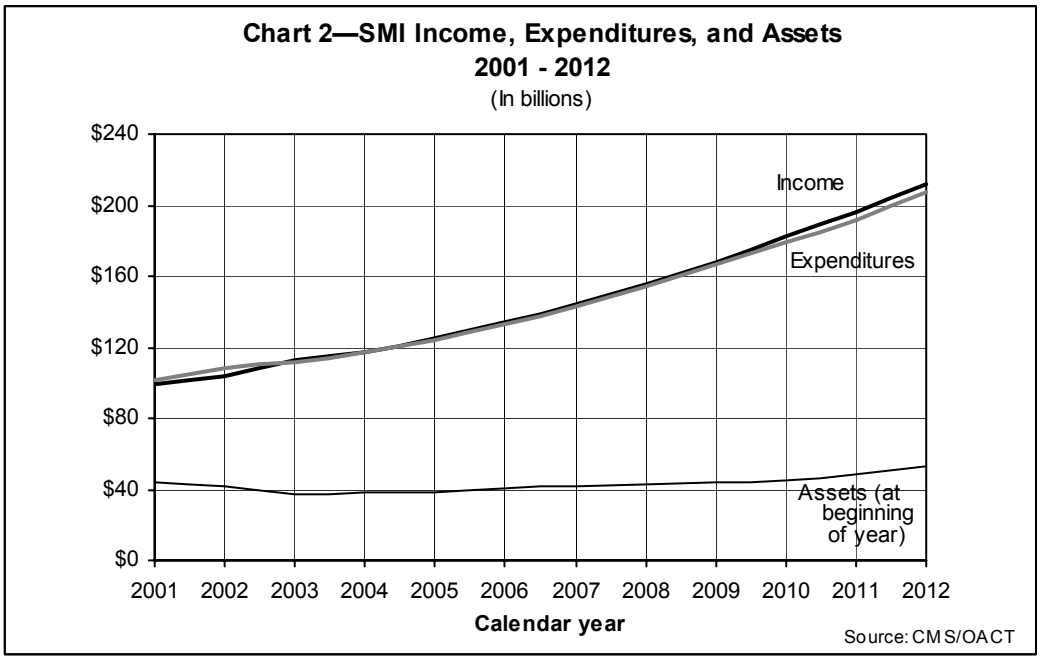
As chart 1 shows, under the intermediate assumptions HI expenditures would begin to exceed income including interest in 2022 and income excluding interest in 2016. This situation is due in part to the attainment of Medicare eligibility, starting in 2011, of those born during the 1946-1964 baby boom. It also arises as a result of health cost increases that are expected to continue to grow faster than workers' earnings. Beginning in 2022, the trust fund would start redeeming trust fund assets; in 2030, the assets would be depleted. The projected year of depletion of the trust fund is very sensitive to assumed future economic and other trends. Under less favorable conditions the cash flow could turn negative much earlier and thereby accelerate asset exhaustion.

By law, Medicare trust fund assets are invested in special U.S. Treasury Securities, which earn interest while Treasury uses those cash resources for other Federal purposes. During times of Federal "on-budget" surpluses, this process reduces the Federal debt held by the public. In times of Federal budget deficits, Medicare surpluses reduce the amount that must be borrowed from the public to finance those deficits. The trust fund assets are claims on the Treasury that, when redeemed, will have to be financed by raising taxes, borrowing from the public, or reducing other Federal expenditures. (When the assets are financed by borrowing, the effect is to defer today's costs to later generations who will ultimately repay the funds being borrowed for today's Medicare beneficiaries.) The existence of large trust fund balances, therefore, represents an important obligation of the Government to pay future Medicare benefits but does not necessarily make it easier for the Government to pay those benefits.

SMI

Chart 2 shows the actuarial estimates of SMI income, expenditures, and assets for each of the next 10 years, in nominal dollars. Whereas HI estimates are displayed through the year 2030, SMI estimates cover only the next 10 years, as SMI differs fundamentally from HI in regard to the way it is financed. In particular, SMI financing is not at all based on payroll taxes but instead on monthly premiums and income from the general fund of the U.S. Treasury—both of which are established annually to cover the following year's expenditures. Estimates of SMI income and expenditures, therefore, are virtually the same, as illustrated in chart 2, and so are not shown in nominal dollars separately beyond 10 years.

Income includes monthly premiums paid by, or on behalf of, beneficiaries, transfers from the general fund of the U.S. Treasury, and interest earned on the U.S. Treasury securities held by the trust fund.[3] Chart 2 displays only total income; it does not represent income excluding interest. The difference between the two is not visible graphically since interest is not a significant source of income.[4] Expenditures include benefit payments as well as administrative expenses.



3. In the financial statements, Medicare income and expenditures are shown from a "trust fund perspective." All sources of income to the trust funds are reflected, and the actuarial projections can be used to assess the financial status of each trust fund. Corresponding estimates for Medicare and other Federal social insurance programs are also shown in the annual *Financial Report of the United States Government*, also known as the consolidated financial statements. On a consolidated basis, the estimates are shown from a "Federal budget" perspective. In particular, certain categories of trust fund income—primarily interest payments and SMI general revenues—are excluded because they represent intragovernmental transfers, rather than revenues received from the public. Thus, the consolidated financial statements focus not on the financial status of individual trust funds, but on the overall balance between revenues and outlays for the federal budget. However, each perspective is appropriate and useful for its intended purpose.

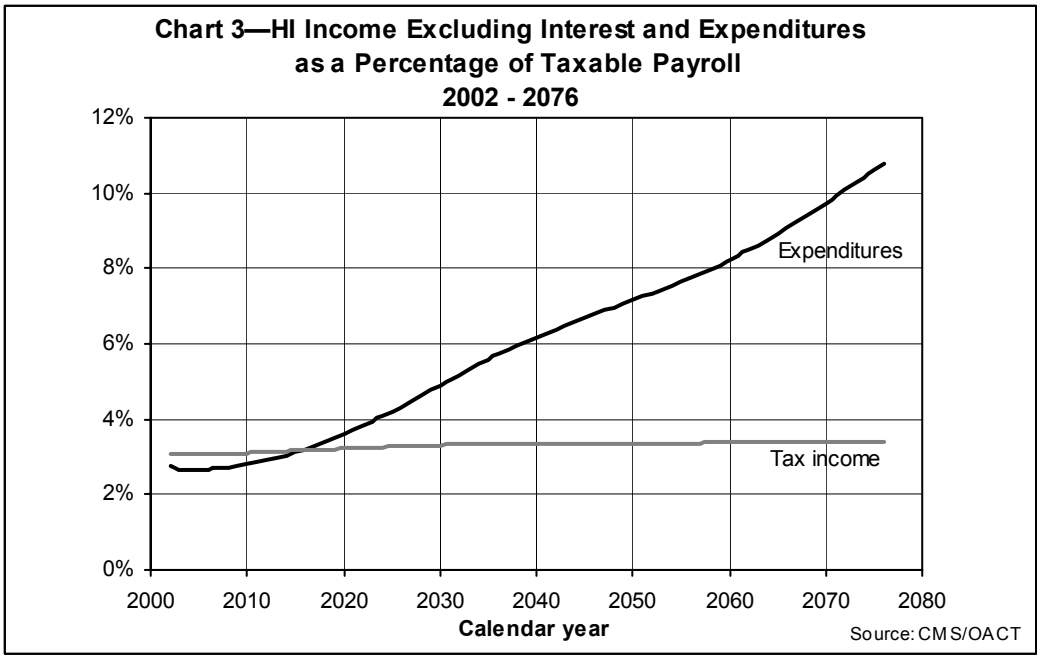
4. Interest income is generally about 4 percent of total SMI income.

As chart 2 indicates, SMI income is very close to expenditures. As noted earlier, this is due to SMI's financing mechanism. Under present law, SMI is automatically in financial balance every year, regardless of future economic and other conditions.

HI Cashflow as a Percentage of Taxable Payroll

Each year, estimates of the financial and actuarial status of the HI trust fund 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 HI (referred to as "taxable payroll").

Chart 3 illustrates income excluding interest and expenditures as a percentage of taxable payroll over the next 75 years. As it was in the 2001 report, the per beneficiary long-range growth in the 2002 report is assumed to be the level of per capita gross domestic product (GDP) growth plus 1 percentage point—reflecting an expectation that the impact of advances in medical technology on health care costs will continue, both in Medicare and in the health sector as a whole.



Since HI payroll tax rates are not scheduled to change in the future under present law, payroll tax income as a percentage of taxable payroll will remain constant at 2.90 percent. Income from taxation of benefits will increase only gradually as a greater proportion of Social Security beneficiaries become subject to such taxation over time. Thus, as chart 3 shows, the income rate is not expected to increase significantly over current levels. On the other hand, expenditures as a percentage of taxable payroll sharply escalate—in part due to health care cost increases that exceed wage growth, but also due to the attainment of Medicare eligibility of those born during the 1946-1964 baby boom.

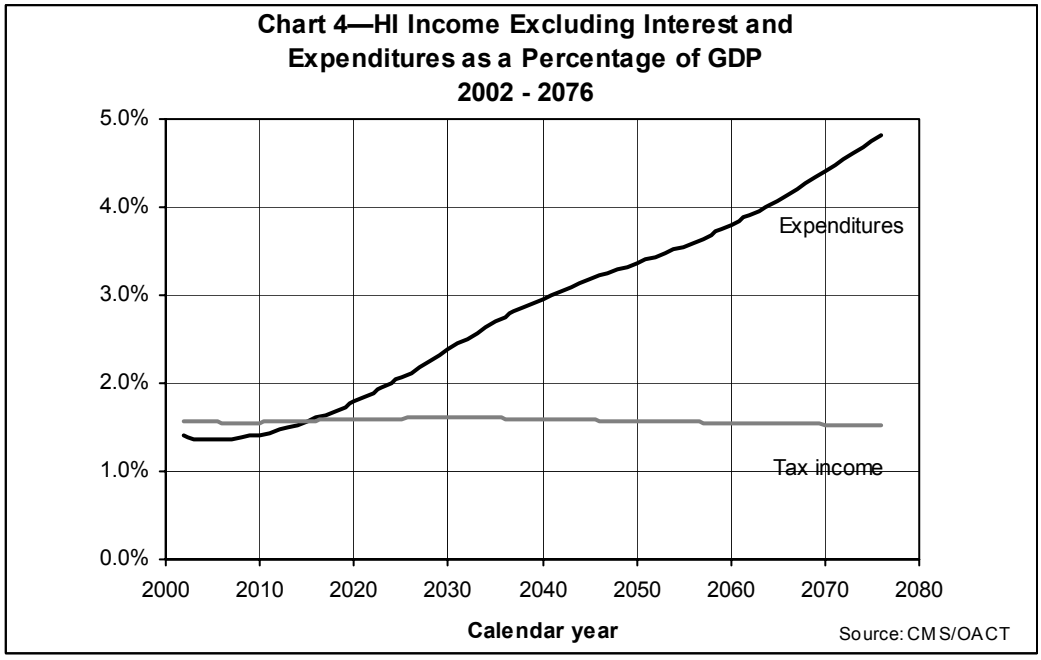
HI and SMI Cashflow as a Percentage of GDP

Expressing Medicare incurred expenditures as a percentage of the GDP gives a relative measure of the size of the Medicare program compared to the general economy. The 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.

HI

Chart 4 shows HI income excluding interest and expenditures over the next 75 years expressed as a percentage of GDP. In 2001, the expenditures were $143.4 billion, which was 1.4 percent of GDP. Following slight reductions in 2003 and 2004, this percentage is projected to increase steadily throughout the remainder of the 75-year period.



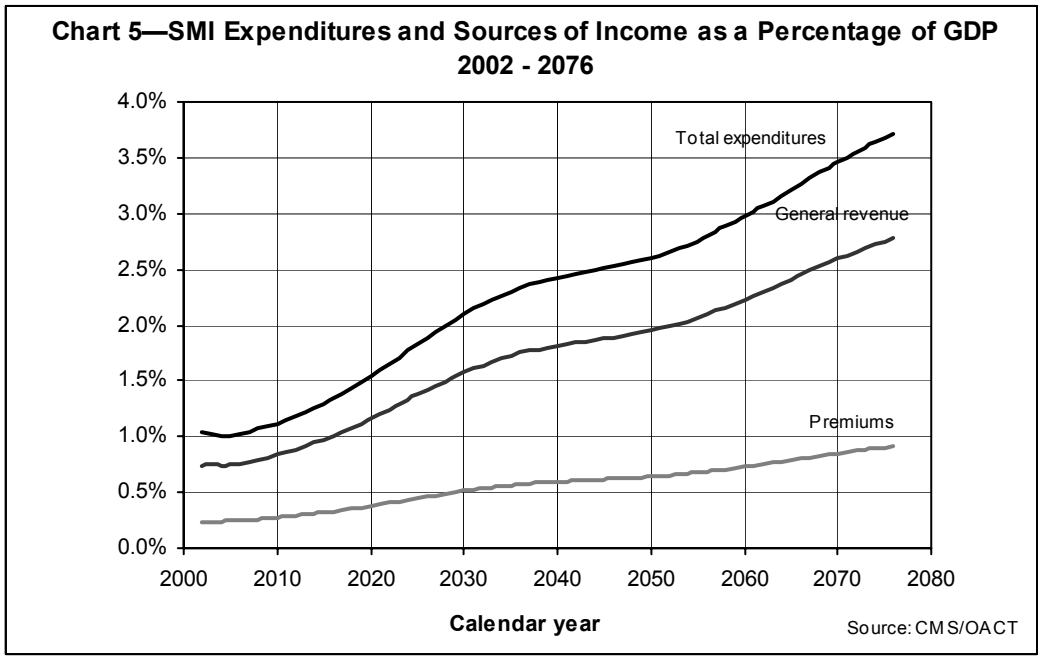
SMI

As noted earlier, because of the SMI financing mechanism in which income mirrors expenditures, it is not necessary to test for imbalances between income and expenditures. Rather, it is more important to examine the projected rise in expenditures and the implications for beneficiary premiums and Federal general revenue payments.

Chart 5 shows SMI expenditures over the next 75 years expressed as a percentage of GDP. In 2001, SMI expenditures were $101.4 billion, which was 1.0 percent of GDP. After 2005, this percentage is projected to increase steadily, reflecting growth in the volume and intensity of services provided per beneficiary throughout the projection period, together with the effects of the baby boom eligibility for retirement.

In the SMI expenditure projections, as in those for HI, the per beneficiary long-range growth rate is assumed to equal per capita GDP growth plus 1 percentage point. The growth rates are estimated year by year for the next 12 years, reflecting the impact of specific statutory provisions. Expenditure growth for years 13 to 25 is assumed to grade smoothly into the long-range assumptions.

Also shown in chart 5 are SMI general revenue transfers and premium income expressed as a percentage of GDP.[5] Under present law, premiums will cover roughly 25 percent of total expenditures. As indicated, both sources of revenue would increase more rapidly than the GDP over time, to match the faster growth rates for SMI expenditures.

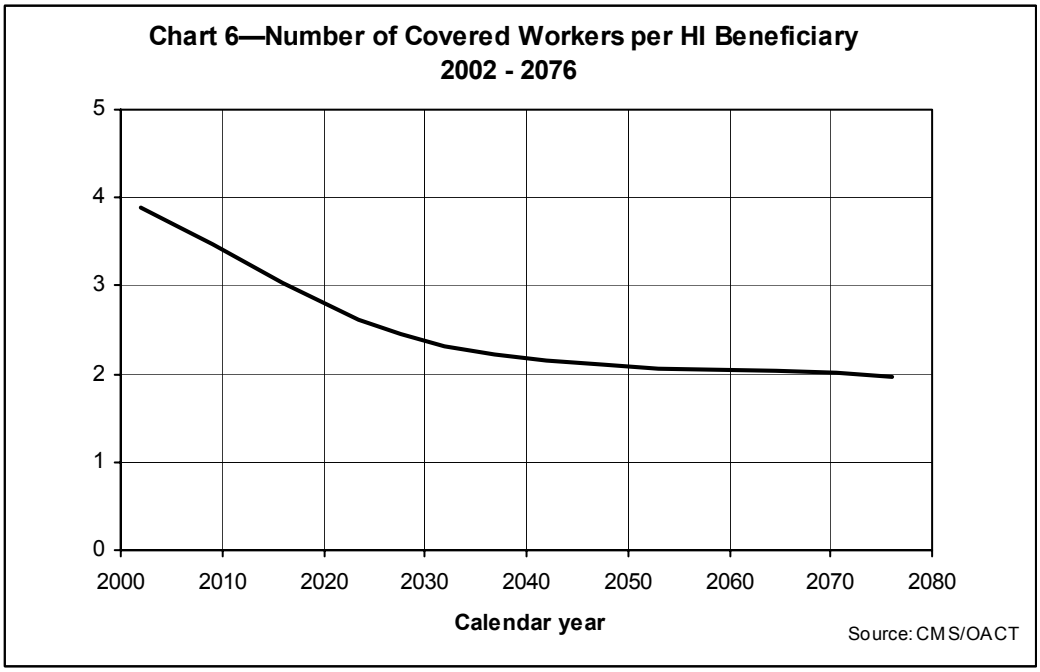


Worker-to-Beneficiary Ratio

HI

Another way to evaluate the long-range outlook of the HI trust fund is to examine the projected number of workers per HI beneficiary. Chart 6 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 2001, every beneficiary had almost 4.0 workers to pay for his or her benefit. In 2030, however, after the last baby boomer turns 65, there will be only about 2.4 workers per beneficiary. The projected ratio continues to decline until there are just 2.0 workers per beneficiary in 2076.

5. See footnote 3 regarding the treatment of SMI general revenue income in the consolidated financial statement of the U.S. Government.



Actuarial Present Values

Projected future expenditures can be summarized by computing an "actuarial present value." This value represents the lump-sum amount that, if invested today in trust fund securities, would be just sufficient to pay each year's expenditures over the next 75 years, with the fund being drawn down to zero at the end of the period. Similarly, future revenues (excluding interest) can be summarized as a single, equivalent amount as of the current year.

Actuarial present values are calculated by discounting the future annual amounts of non-interest income and expenditures at the assumed rates of interest credited to the HI and SMI trust funds. Present values are computed as of the beginning of the 75-year projection period for three different groups of participants: current workers and other individuals who have not yet attained eligibility age; current beneficiaries who have attained eligibility age; and new entrants, or those who are expected to become participants in the future.

Table 1 sets forth, for each of these three groups, the actuarial present values of all future HI and SMI expenditures and all future non-interest income for the next 75 years. Also shown is the net present value of cashflow, which is calculated by subtracting the actuarial present value of future expenditures from the actuarial present value of future income.

Table 1—Actuarial Present Values of Hospital Insurance and Supplementary Medical Insurance Revenues and Expenditures: 75-year Projection as of January 1, 2002

(In billions)

	HI			SMI		
	2002	2001	2000	2002	2001	2000
Actuarial present value[1] of estimated future income (excluding interest) received from or on behalf of:						
Current participants[3] who, at start of projection period:						
Have not yet attained eligibility age (ages 15-64)	$4,408	$4,136	$3,757	$7,423	$7,378	$6,109
Have attained eligibility age (age 65 and over)	125	113	97	1,008	1,032	934
Those expected to become participants (under age 15)	3,753	3,507	3,179	2,402	2,370	1,616
All current and future participants	8,286	7,757	7,033	10,833	10,780	8,659
Actuarial present value[1] of estimated future expenditures[4] paid to or on behalf of:						
Current participants[3] who, at start of projection period:						
Have not yet attained eligibility age (ages 15-64)	9,195	8,568	6,702	7,463	7,415	6,094
Have attained eligibility age (age 65 and over)	1,747	1,693	1,681	1,132	1,159	1,051
Those expected to become participants (under age 15)	2,470	2,225	1,349	2,238	2,206	1,514
All current and future participants	13,412	12,487	9,732	10,833	10,780	8,659
Actuarial present value[1] of estimated future income (excluding interest) less expenditures	-5,126	-4,730	-2,700	0	0	0
Trust fund assets at start of period	209	177	141	41	44	45
Assets at start of period plus actuarial present value[1] of estimated future income (excluding interest) less expenditures	-4,917	-4,553	-2,558	41	44	45

[1] Present values are computed on the basis of the intermediate set of economic and demographic assumptions specified in the Report of the Boards of Trustees for the year shown and over the 75-year projection period beginning January 1 of that year.

[2] SMI income includes premiums paid by beneficiaries and general revenue contributions made on behalf of beneficiaries. See footnote 3 on page 40 concerning treatment of SMI general revenues in the consolidated financial statement of the U.S. Government.

[3] Current participants are the "closed group" of individuals age 15 and over at the start of the period. The projection period for these current participants would theoretically cover all of their working and retirement years, a period that could be greater than 75 years in some instances. As a practical matter, the present values of future income and expenditures from/for current participants beyond 75 years are not material. The projection period for new entrants covers the next 75 years.

[4] Expenditures include benefit payments and administrative expenses.

Note: Totals do not necessarily equal the sums of rounded components.

As shown in table 1, the HI trust fund has an actuarial deficit of more than $4.9 trillion over the 75-year projection period, as compared to more than $4.5 trillion in the 2001 financial report. SMI, on the other hand, does not have similar problems because it is automatically in financial balance every year due to its financing mechanism.

The existence of a large actuarial deficit for the HI trust fund indicates that, under reasonable assumptions as to economic, demographic, and health cost trends for the future, HI income is expected to fall substantially short of expenditures in the long range. Although the deficits are not anticipated in the immediate future, as indicated by the preceding cashflow projections, they nonetheless pose a serious financial problem for the HI trust fund.

It is important to note that no liability has been recognized on the balance sheet for future payments to be made to current and future program participants beyond the existing "incurred but not reported" Medicare claim amounts as of September 30, 2002. This is because Medicare is accounted for as a social insurance program rather than a pension program. Accounting for a social insurance program recognizes the expense of benefits when they are actually paid, or are due to be paid, because benefit payments are primarily nonexchange transactions and, unlike employer-sponsored pension benefits for employees, are not considered deferred compensation. Accrual accounting

for a pension program, by contrast, recognizes retirement benefit expenses as they are earned so that the full actuarial present value of the worker's expected retirement benefits has been recognized by the time the worker retires.

Actuarial Assumptions and Sensitivity Analysis

In order to make projections regarding the future financial status of the HI and SMI trust funds, various assumptions have to be made. First and foremost, the estimates presented here are based on the assumption that the trust funds will continue under present law. In addition, the estimates depend on many economic and demographic assumptions, including changes in wages and the consumer price index (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.

Table 2 shows some of the underlying assumptions used in the projections of Medicare spending displayed in this section. Further details on these assumptions are available in the OASDI and Medicare Trustees Reports for 2002. In practice, a number of specific assumptions are made for each of the different types of service provided by the Medicare program (for example, hospital care and physician services). These assumptions include changes in the utilization, volume, and intensity of each type of service. The per beneficiary cost increases displayed in table 2 reflect the overall impact of these more detailed assumptions.

Table 2—Medicare Assumptions

				Annual percentage change in:					
							Per beneficiary cost[3]		Real-
	Fertility rate[1]	Net immigration	Real-wage differential[2]	Wages	CPI	Real GDP	HI	SMI	interest rate[4]
2002	2.13	900,000	1.8	3.1	1.3	0.7	3.5	4.2	3.6
2005	2.10	900,000	1.2	4.1	2.9	3.2	4.5	5.2	3.5
2010	2.07	900,000	1.0	4.1	3.0	2.2	4.4	5.5	3.0
2020	1.99	900,000	1.1	4.1	3.0	1.8	4.4	5.2	3.0
2030	1.95	900,000	1.1	4.1	3.0	1.8	5.9	5.6	3.0
2040	1.95	900,000	1.1	4.1	3.0	1.8	6.1	5.3	3.0
2050	1.95	900,000	1.1	4.1	3.0	1.7	5.2	4.9	3.0
2060	1.95	900,000	1.1	4.1	3.0	1.7	5.3	5.4	3.0
2070	1.95	900,000	1.1	4.1	3.0	1.7	5.5	5.2	3.0
2076	1.95	900,000	1.1	4.1	3.0	1.6	5.4	5.1	3.0

[1]Average number of children per woman.
[2]Difference between percentage increases in wages and the CPI.
[3]See text for nature of this assumption.
[4]Average rate of interest earned on new trust fund securities, above and beyond rate of inflation.

Estimates made in prior years have sometimes changed substantially 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, six of the key

assumptions were varied individually to determine the impact on the HI actuarial present values and net cashflows.[6] The assumptions varied are the fertility rate, net immigration, real-wage differential, CPI, real-interest rate, and health care cost factors.[7]

For this analysis, the intermediate economic and demographic assumptions in the *2002 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Fund*s 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, 2002 and are based on estimates of income and expenditures during the 75-year projection period.

Charts 7 through 12 show the net annual HI cashflow in nominal dollars and the present value of this net cashflow for each assumption varied. In most instances, the charts depicting the estimated net cashflow indicate that, after increasing in the early years, net cashflow decreases steadily through 2030 under all three scenarios displayed.

On the present value charts, the same pattern is evident, though the magnitudes are lower because of the discounting process used for computing present values.

Fertility Rate

Table 3 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.

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6. As noted in footnote 3 on page 40, the actuarial deficit is calculated from a *trust fund perspective*, reflecting all sources of income and expenditures to or from the HI and SMI trust funds. If, instead, a *budget perspective* is considered, as used in the consolidated financial statement, one would compare Medicare outlays to the public with revenues received directly from the public. On this basis, transfers to the SMI trust fund from the general fund of the Treasury would be excluded, with the result that the present value of projected SMI expenditures through 2076 would exceed the present value of projected SMI premium revenue alone by $8.1 trillion. When added to the corresponding differential for HI, the present value of expenditures for the Medicare program overall is projected to exceed receipts from the public by $13.3 trillion. This *budget impact* reflects both (i) the cost to the Federal budget of SMI general revenues provided under current law and (ii) the amount that HI revenues would have to be increased to enable HI benefits to be paid at their currently scheduled level-for which there is no provision in current law.

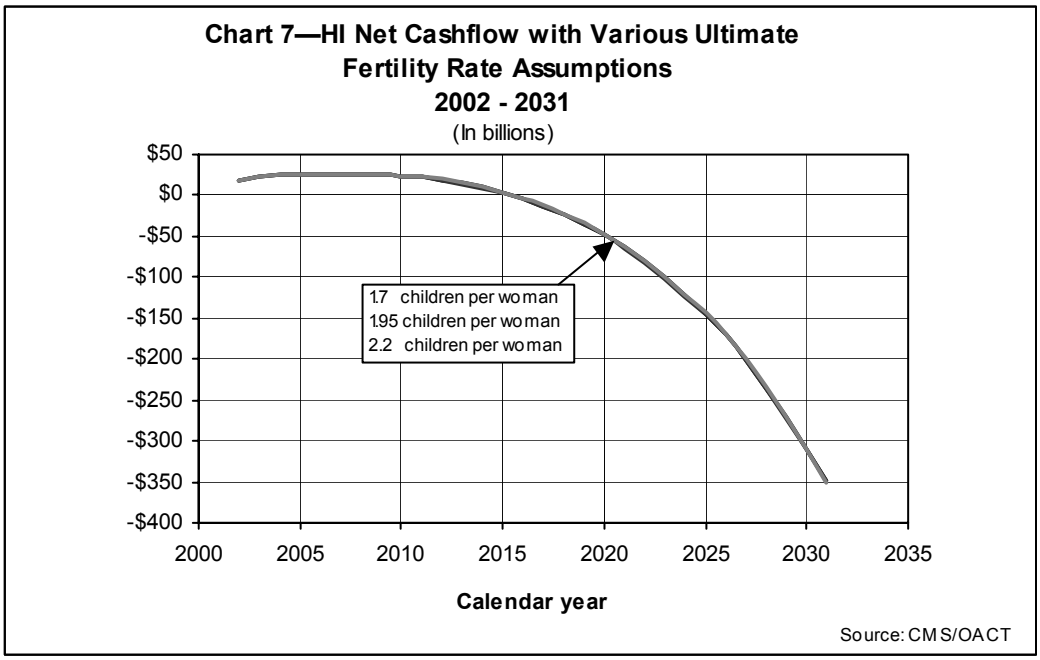
7. The sensitivity of the projected HI net cash flow to variations in future mortality rates is also of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per beneficiary health expenditures.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

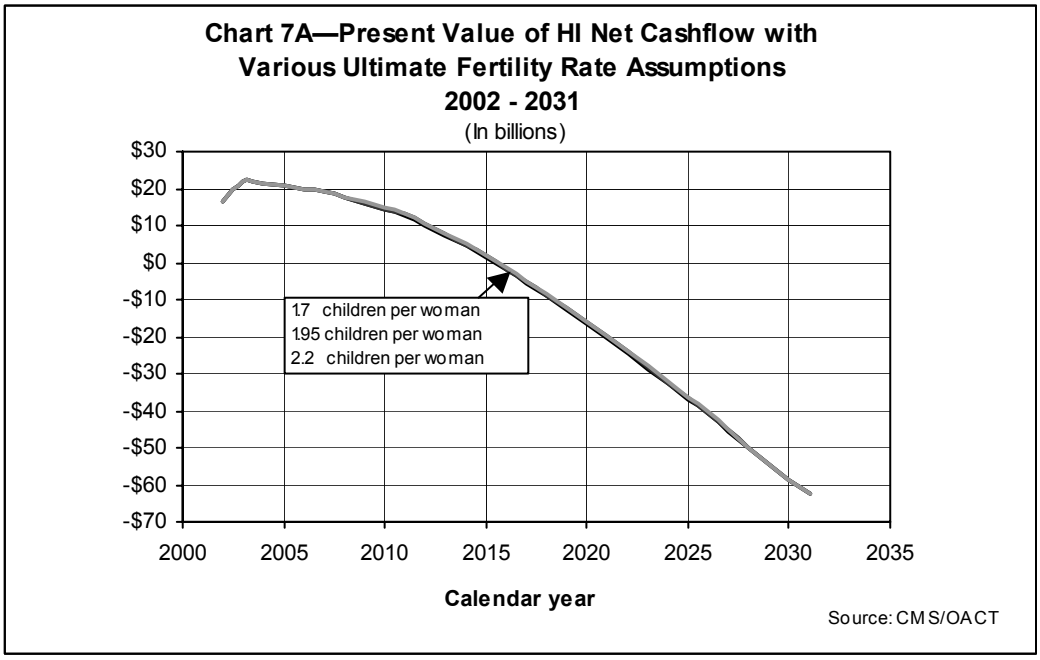
Table 3—Present Value of Estimated HI Income Less Expenditures under Various Fertility Rate Assumptions			
Ultimate fertility rate[1]	1.7	1.95	2.2
Income minus expenditures (in billions)	-$5,266	-$5,126	-$4,989

[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.

Table 3 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 $5,126 billion to $5,266 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 $4,989 billion.

Charts 7 and 7A show projections of the net cashflow under the three alternative fertility rate assumptions presented in table 3.





As charts 7 and 7A indicate, the fertility rate assumption has only a negligible impact on projected HI cashflows over the next 30 years. This is because higher fertility in the first year does not affect the labor force until roughly 20 years have passed (increasing HI payroll taxes slightly) and has virtually no impact on the number of beneficiaries within this period. Over the full 75-year period, the changes are somewhat greater, as illustrated by the present values in table 3.

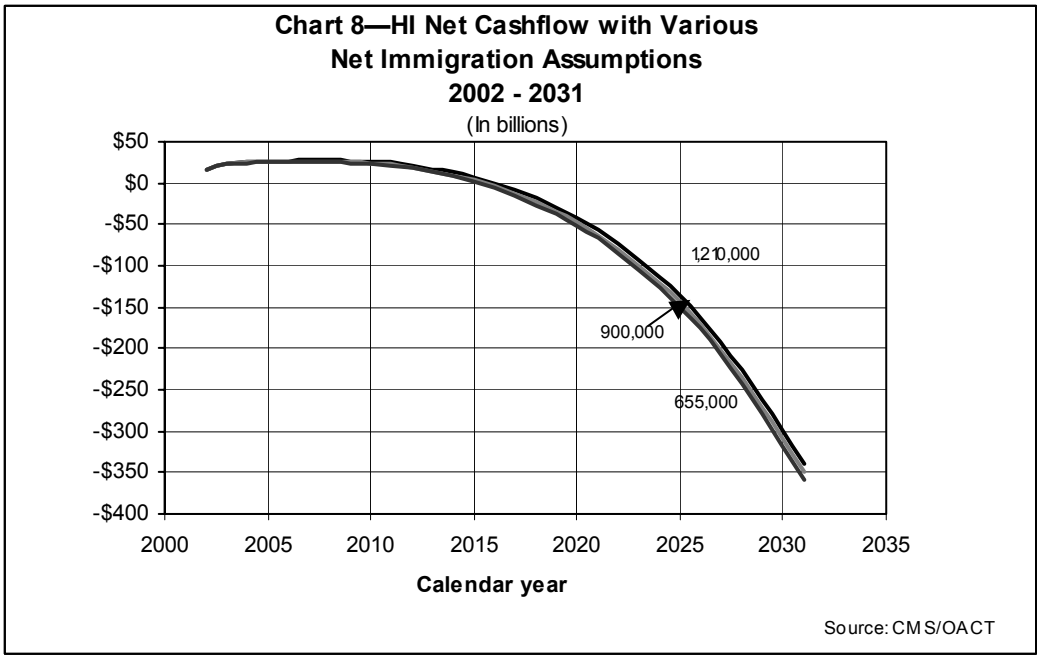
Net Immigration

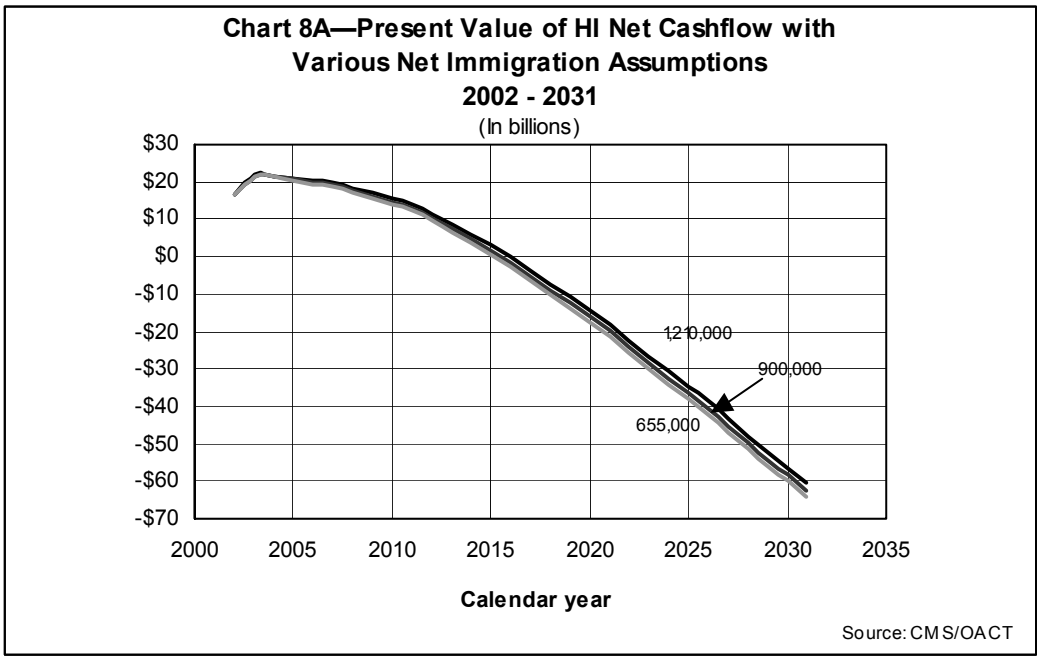
Table 4 shows the net present value of cashflow during the 75-year projection period under three alternative net immigration assumptions: 655,000 persons, 900,000 persons, and 1,210,000 persons per year.

Table 4—Present Value of Estimated HI Income Less Expenditures under Various Net Immigration Assumptions			
Ultimate net immigration	655,000	900,000	1,210,000
Income minus expenditures (in billions)	-$5,094	-$5,126	-$5,156

Table 4 demonstrates that if the ultimate net immigration assumption is decreased from 900,000 to 655,000 persons, the deficit of income over expenditures decreases from $5,126 billion to $5,094 billion. On the other hand, if the ultimate net immigration assumption is increased from 900,000 to 1,210,000 persons, the deficit increases to $5,156 billion.

Charts 8 and 8A show projections of the net cashflow under the three alternative net immigration assumptions presented in table 4.





As charts 8 and 8A indicate, this assumption has an impact on projected HI cashflow starting almost immediately. Because immigration tends to occur among younger individuals, the number of covered workers is affected immediately, while the number of beneficiaries is affected much less quickly. Nonetheless, variations in net immigration result in fairly small differences in cashflow.

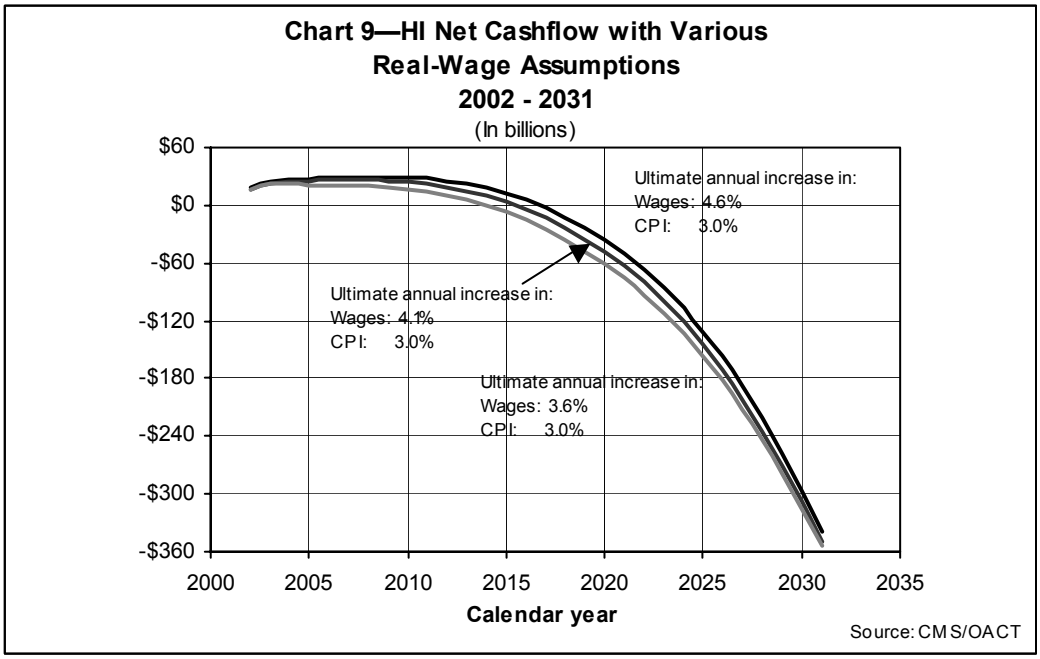
Real-Wage Differential

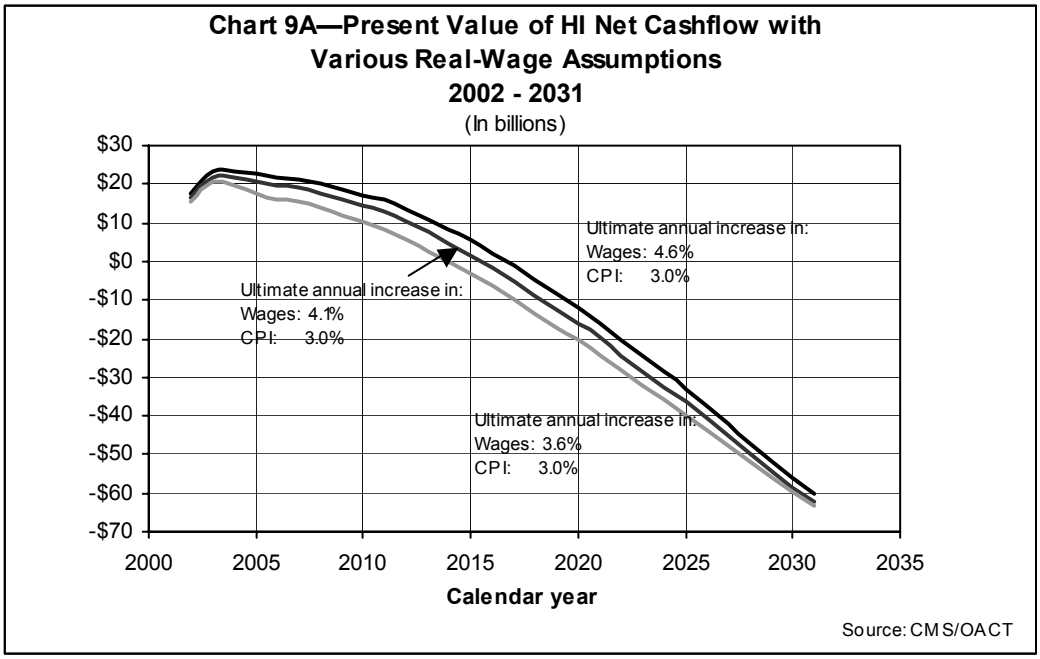
Table 5 shows the net present value of cashflow during the 75-year projection period under three alternative ultimate real-wage differential assumptions: 0.6, 1.1, and 1.6 percentage points. In each case, the CPI is assumed to be 3.0 percent, yielding ultimate percentage increases in average annual wages in covered employment of 3.6, 4.1, and 4.6 percent, respectively.

Table 5—Present Value of Estimated HI Income Less Expenditures under Various Real-Wage Assumptions			
Ultimate percentage increase in wages - CPI	3.6 - 3.0	4.1 - 3.0	4.6 - 3.0
Ultimate percentage increase in real-wage differential	0.6	1.1	1.6
Income minus expenditures (in billions)	-$5,361	-$5,126	-$4,812

Table 5 demonstrates that if the ultimate real-wage differential assumption is decreased from 1.1 percentage points to 0.6 percentage point, the deficit of income over expenditures increases from $5,126 billion to $5,361 billion. On the other hand, if the ultimate real-wage differential assumption is increased from 1.1 percentage points to 1.6 percentage points, the deficit decreases to $4,812 billion.

Charts 9 and 9A show projections of the net cashflow under the three alternative real-wage differential assumptions presented in table 5.





As charts 9 and 9A indicate, this assumption has a fairly large impact on projected HI cashflow very early in the projection period. Higher real-wage differential assumptions immediately increase both HI expenditures for health care and wages for all workers. Though there is a full effect on wages and payroll taxes, the effect on benefits is only partial, since not all health care costs are wage-related.

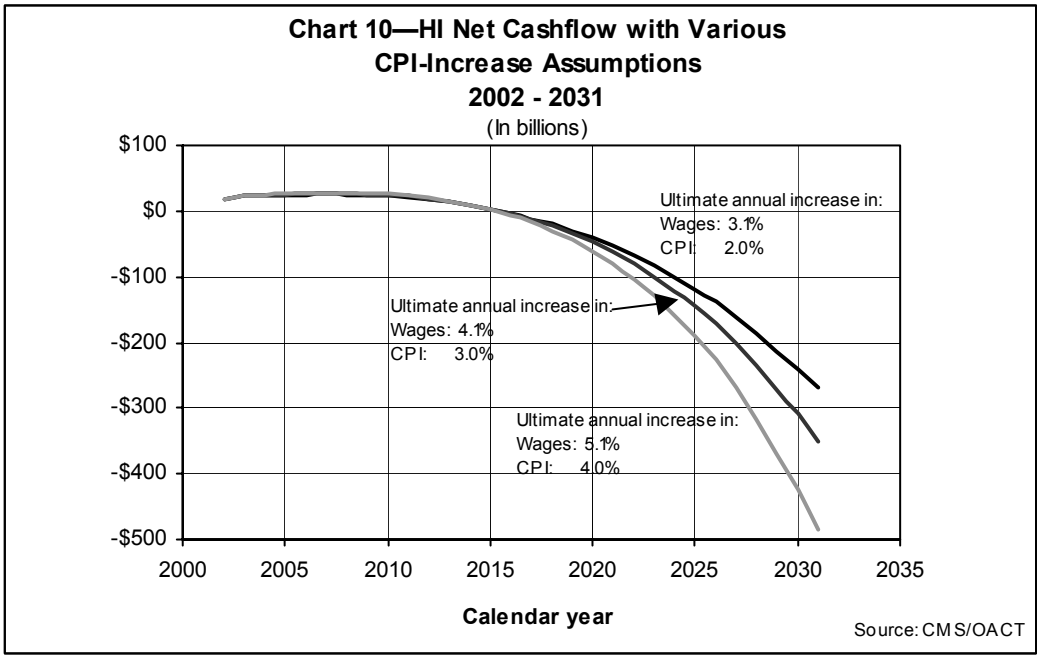
Consumer Price Index

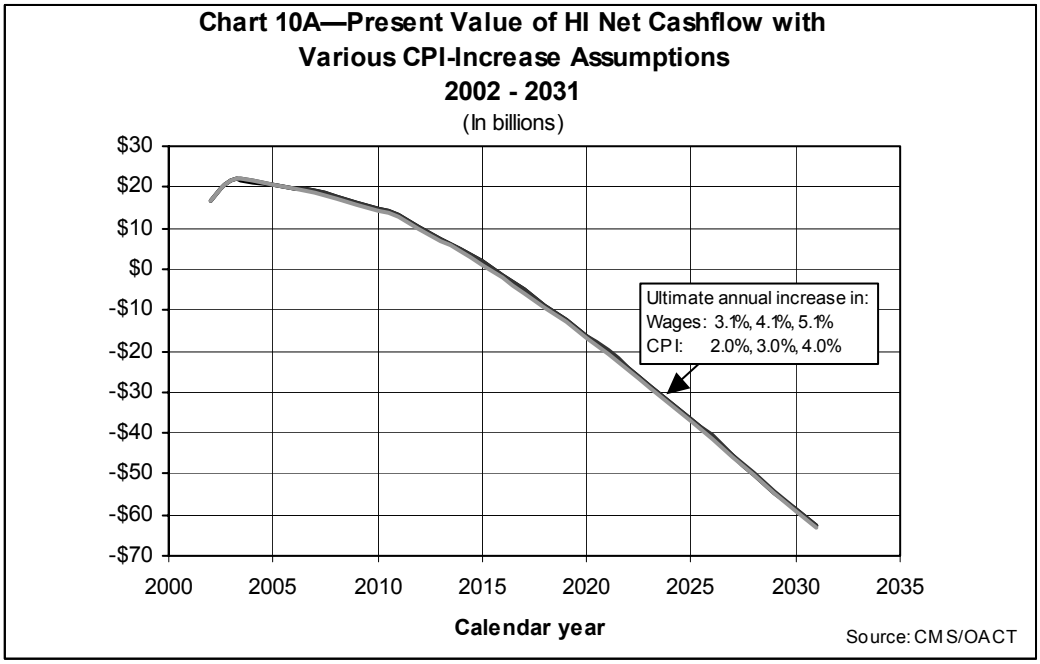
Table 6 shows the net present value of cashflow during the 75-year projection period under three alternative ultimate CPI rate-of-increase assumptions: 2.0, 3.0, and 4.0 percent. In each case, the ultimate real-wage differential is assumed to be 1.1 percent, yielding ultimate percentage increases in average annual wages in covered employment of 3.1, 4.1, and 5.1 percent, respectively.

Table 6—Present Value of Estimated HI Income Less Expenditures under Various CPI-Increase Assumptions			
Ultimate percentage increase in wages - CPI	3.1 - 2.0	4.1 - 3.0	5.1 - 4.0
Income minus expenditures (in billions)	-$5,149	-$5,126	-$5,148

Table 6 demonstrates that if the ultimate CPI increase assumption is decreased from 3.0 percent to 2.0 percent, the deficit of income over expenditures increases from $5,126 billion to $5,149 billion. Furthermore, if the ultimate CPI increase assumption is increased from 3.0 percent to 4.0 percent, the deficit increases to $5,148 billion.

Charts 10 and 10A show projections of the net cashflow under the three alternative CPI rate-of-increase assumptions presented in table 6.





As charts 10 and 10A indicate, this assumption has a large impact on projected HI cashflow in nominal dollars but only a negligible impact when the cashflow is expressed as present values. The relative insensitivity of the projected present values of HI cashflow to different levels of general inflation occurs because inflation tends to affect both income and costs equally. In nominal dollars, however, a given deficit "looks bigger" under high-inflation conditions but is not significantly different when it is expressed as a present value or relative to taxable payroll. This sensitivity test serves as a useful example of the limitations of nominal-dollar projections over long periods.

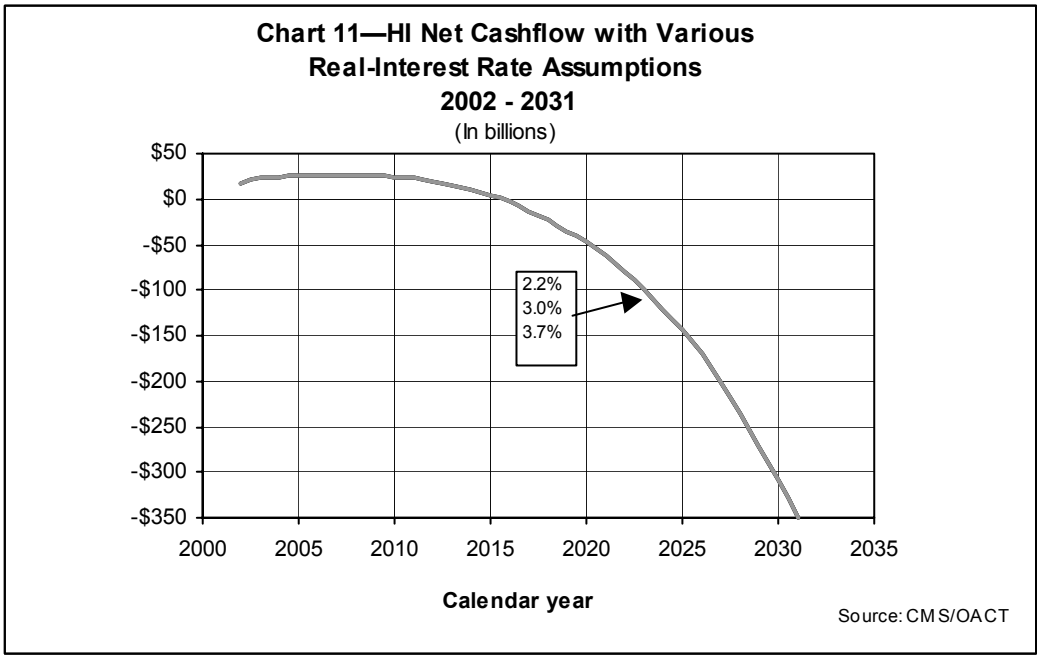
Real-Interest Rate

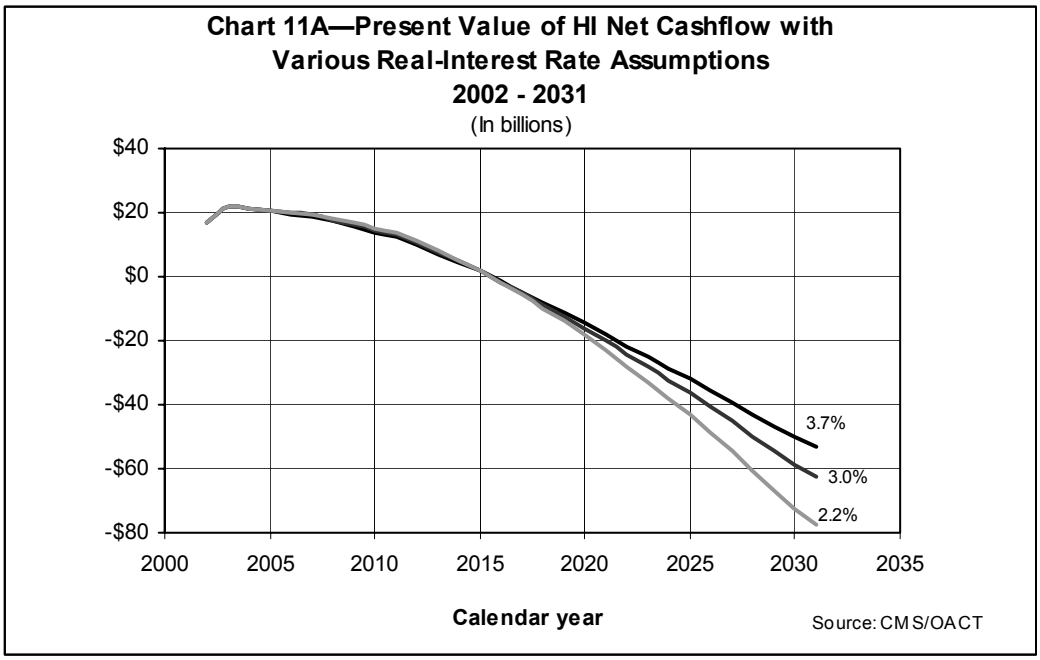
Table 7 shows the net present value of cashflow during the 75-year projection period under three alternative ultimate real-interest assumptions: 2.2, 3.0, and 3.7 percent. In each case, the ultimate annual increase in the CPI is assumed to be 3.0 percent, resulting in ultimate annual yields of 5.2, 6.0, and 6.7 percent, respectively.

Present Value of Estimated HI Income Less Expenditures under Various Real-Interest Assumptions			
Ultimate real-interest rate	2.2 percent	3.0 percent	3.7 percent
Income minus expenditures (in billions)	-$7,892	-$5,126	-$3,812

Table 7 demonstrates that if the ultimate real-interest rate percentage is decreased from 3.0 percent to 2.2 percent, the deficit of income over expenditures increases from $5,126 billion to $7,892 billion. On the other hand, if the ultimate real-interest rate assumption is increased from 3.0 percent to 3.7 percent, the deficit decreases to $3,812 billion.

Charts 11 and 11A show projections of the net cashflow under the three alternative real-interest assumptions presented in table 7.





As shown in charts 11 and 11A, the present values of the net cashflow are more sensitive to the interest assumption than is the nominal net cashflow. This is not an indication of the actual role that interest plays in HI financing. In actuality, interest finances very little of the cost of the HI trust fund because, under the intermediate assumptions, the fund is projected to be relatively low and exhausted by 2030. These results illustrate the substantial sensitivity of present value measures to different interest rate assumptions. With higher assumed interest, the very large deficits in the more distant future are discounted more heavily (that is, are given less weight), and the overall net present value is smaller.

Health Care Cost Factors

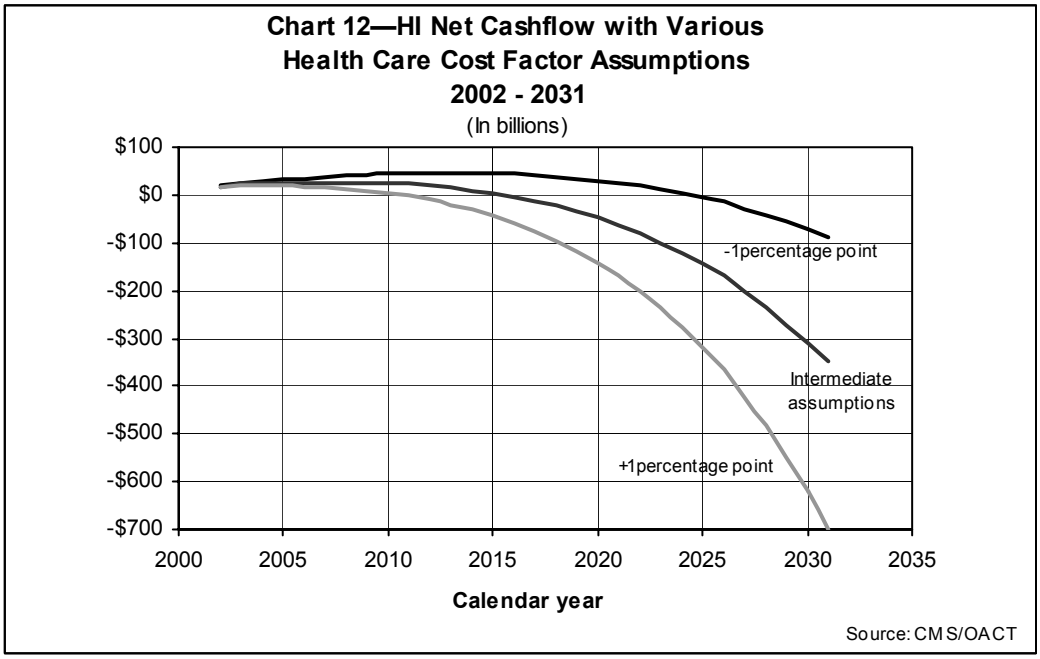
Table 8 shows the net present value of cashflow during the 75-year projection period under three alternative assumptions of the annual growth rate in the aggregate cost of providing covered health care services to beneficiaries. These assumptions are that the ultimate annual growth rate in such costs, 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

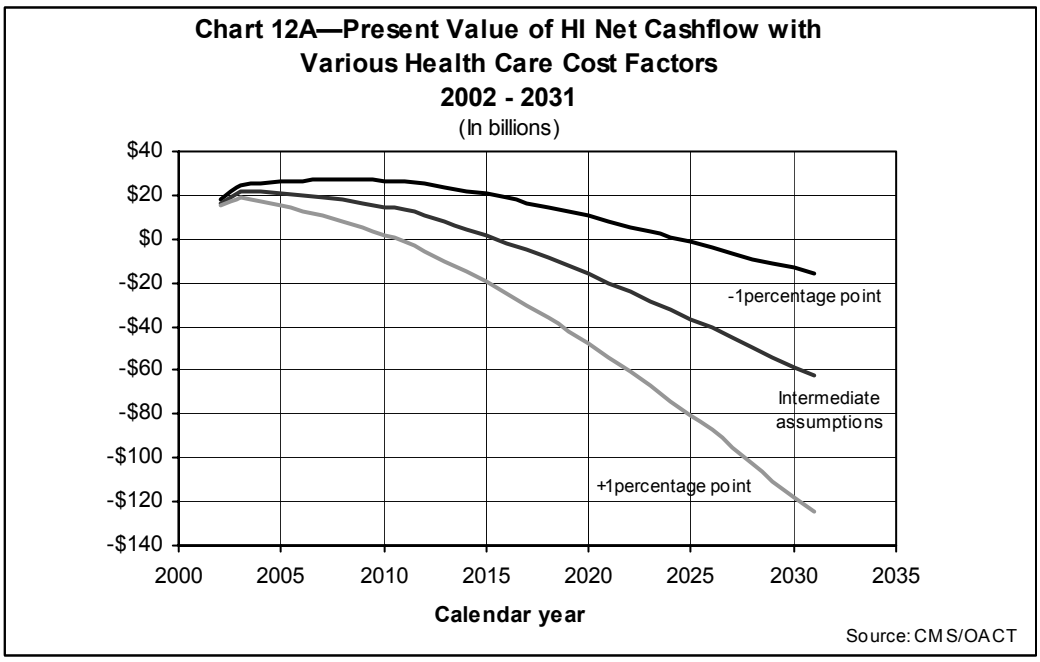
Table 8—Present Value of Estimated HI Income Less Expenditures under Various Health Care Cost Growth Rate Assumptions

Annual cost/payroll relative growth rate	-1 percentage point	Intermediate assumptions	+1 percentage point
Income minus expenditures (in billions)	-$906	-$5,126	-$12,047

Table 8 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 $5,126 billion to $906 billion. On the other hand, if the ultimate growth rate assumption is 1 percentage point higher than the intermediate assumptions, the deficit increases substantially to $12,047 billion.

Charts 12 and 12A show projections of the net cashflow under the three alternative annual growth rate assumptions presented in table 8.





This assumption has a dramatic impact on projected HI cashflow. The assumptions analyzed thus far have affected HI income and costs simultaneously. However, several factors, such as the utilization of services by beneficiaries or the relative complexity of services provided, can affect costs without affecting tax income. As charts 12 and 12A indicate, the financial status of the HI trust fund is extremely sensitive to the relative growth rates for health care service costs versus taxable payroll.

Trust Fund Finances and Sustainability

HI

The HI trust fund is substantially out of financial balance in the long range. Under the Medicare Trustees' intermediate assumptions, income is projected to continue to moderately exceed expenditures for the next 20 years but to fall short by steadily increasing amounts in 2022 and later. These shortfalls can be met by redeeming trust fund assets, but only until 2030.

To bring the HI trust fund into actuarial balance over the next 75 years under the intermediate assumptions, either outlays would have to be reduced by 38 percent or income increased by 60 percent (or some combination of the two) throughout the 75-year period. These substantial changes in income and/or outlays are needed in part as a result of the impending retirement of the baby boom generation.

The projections presented here 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.

SMI

The financing established for the SMI trust fund for calendar year 2002 is estimated to be sufficient to cover expenditures for that year and to preserve an adequate contingency reserve in the fund. Moreover, for all future years, trust fund income is projected to equal expenditures—but only because beneficiary premiums and government general revenue contributions are set to meet expected costs each year.

The SMI trust fund's automatic financing provisions prevent crises such as those faced in recent years by the HI trust fund, the assets of which were projected to be exhausted in the near future. As a result, there has been substantially less attention directed toward the financial status of the SMI trust fund than to the HI trust fund—even though SMI expenditures have increased faster than HI expenditures in most years and are expected to continue to do so for a number of years in the future.

SMI costs have generally grown faster than the GDP, and this trend is expected to continue under present law. The projected increases are initially attributable in part to assumed continuing growth in the volume and intensity of services provided per beneficiary. Starting in 2011, the attainment of Medicare eligibility of the post-World War II baby boom generation will also have a major influence on the growth in SMI costs. This growth in SMI expenditures relative to GDP is a matter of great concern.

Medicare Overall

The projections shown in this section continue to demonstrate the need for the Administration and the Congress to address the financial challenges facing Medicare—both the remaining financial imbalance facing the HI trust fund and the continuing problem of rapid growth in SMI expenditures. In their 2002 annual report to Congress, the Medicare Boards of Trustees emphasize the seriousness of these concerns and urge the nation's policy makers to take "effective and decisive action…to build upon the strong steps taken in recent reforms." They also state: "Consideration of further reforms should occur in the relatively near future."

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U.S. Department of Health and Human Services
Combining Statement of Budgetary Resources
For the Fiscal Year Ended September 30, 2002
(in millions)

	CMS			Other	
	Medicare HI	Medicare SMI	Medicaid	OPDIV Budgetary Accounts[1]	OPDIV Combined Totals
Budgetary Resources:					
1. Budget Authority	$ 178,744	$ 105,679	$ 147,111	$ 195,124	$ 626,658
2. Unobligated Balances	-	-	110	4,550	4,660
3. Spending Authority from Offsetting Collections	-	-	2	7,101	7,103
4. Recoveries of prior year obligations	-	-	4,198	3,425	7,623
5. Temporarily not available pursuant to Public Law	(31,543)	3,512	-	(2,879)	(30,910)
6. Permanently not available (-)	-	-	(760)	(3,337)	(4,097)
7. Total Budgetary Resources	$ 147,201	$ 109,191	$ 150,661	$ 203,984	$ 611,037
Status of Budgetary Resources:					
8. Obligations Incurred	$ 147,201	$ 109,191	$ 150,661	$ 195,542	$ 602,595
9. Unobligated Balances - Available	-	-	-	5,842	5,842
10. Unobligated Balances - Not Available	-	-	-	2,600	2,600
11. Total Status of Budgetary Resources	$ 147,201	$ 109,191	$ 150,661	$ 203,984	$ 611,037
Relationship of Obligations to Outlays:					
12. Obligated Balance, Net – Beginning of Period	$ 818	$ 556	$ 5,332	$ 65,488	$ 72,194
13. Obligated Balance Transferred, Net (+/-)	-	-	-	-	-
14. Obligated Balance, Net – End of Period	968	922	5,049	69,441	76,380
15. Outlays	147,051	108,825	146,744	181,063	583,683
16. Less: Offsetting receipts	1,524	24,427	-	14	25,965
17. Net Outlays	$ 145,527	$ 84,398	$ 146,744	$ 181,049	$ 557,718

[1] "Other OPDIV Budgetary Accounts" includes the budgetary accounts of the eleven HHS OPDIVs other than CMS, as well as the remaining budgetary accounts not reported by CMS under Medicare and Medicaid. Information on each of the major budgetary accounts for individual OPDIVs can be found in each OPDIVs' own annual report. OPDIVs reports can be accessed via the Department of Health and Human Services website at: www.hhs.gov.

Summary of Other OPDIV Budgetary Accounts

	Budgetary Resources	Status of Budgetary Resources	Net Outlays
ACF	$ 47,341	$ 47,341	$ 45,671
AoA	1,206	1,206	1,106
AHRQ	343	343	(67)
CDC	5,726	5,726	4,402
CMS	103,004	103,004	95,049
FDA	1,753	1,753	1,125
HRSA	7,081	7,081	5,735
IHS	4,096	4,096	2,817
NIH	25,517	25,517	20,456
OS	3,788	3,788	1,578
PSC	807	807	296
SAMHSA	3,322	3,322	2,881
	$ 203,984	$ 203,984	$ 181,049

U.S. Department of Health and Human Services
Condensed Balance Sheet
Franchise and Intra-Governmental Support Revolving Funds
As of September 30, 2002
(in millions)

	HHS Service and Supply Fund	NIH Service and Supply Fund	Combined Totals
Assets			
Fund Balance with Treasury	$ 41	$ 195	$ 236
Accounts Receivable, Net	116	13	129
Property, Plant and Equip, Net	12	69	81
Other Assets	16	17	33
Total Assets	$ 185	$ 294	$ 479
Liabilities			
Accounts Payable	$ 45	$ 55	$ 100
Other Liabilities	18	146	164
Total Liabilities	$ 63	$ 201	$ 264
Net Position			
Cumulative Results of Operations	$ 122	$ 93	$ 215
Total Liabilities and Net Position	$ 185	$ 294	$ 479

U.S. Department of Health and Human Services
Condensed Statement of Net Cost
Franchise and Intra-Governmental Support Revolving Funds
For the Fiscal Year Ended September 30, 2002
(in millions)

Program/Business Line	Gross Costs	Less: Earned Revenue	Net Costs
HHS Service and Supply Fund			
Administrative Operations Services	$ 173	$ 164	$ 9
Financial Management Service	51	52	(1)
Human Resources Service	59	61	(2)
Federal Occupational Health	110	113	(3)
Total	$ 393	$ 390	$ 3
NIH Service and Supply Fund			
Administrative Services	$ 373	$ 409	$ (36)
Information Technology	148	156	(8)
Instrumentation Services	10	10	0
Animal Services	41	43	(2)
Total	$ 572	$ 618	$ (46)

The Program Support Center (PSC), a component of the Office of the Secretary, manages the HHS Service and Supply Fund. The PSC provides support services to federal agencies on a competitive, "service-for-fee" basis. Services and products are available in the areas of Acquisitions, Computer and Information Technology, Finance, Medical Supply Operation, Health Services, Personnel and Payroll and Support Services. Major customers are other HHS Operating Divisions and components of many federal agencies including Departments of Defense, Education, Housing and Urban Development, Interior, Energy, Labor, State, Transportation, Treasury and other independent federal organizations.

NIH provides administrative services, which include facilities management, supply stores, printing and reproduction, medical arts and photography, procurement, and a wide range of other research support services. The information Technology includes the regional data processing center, which sells computing services and programming services and enterprise IT software development. Instrumentation Services include biomedical fabrication and instrumentation activities, which entails creating highly technical bioengineering structures. The Animal Services entails purchasing, housing and feeding animals used in research. NIH's major customers are the NIH Research Institutes and Centers and for computer services, the Department of Defense.

U.S. Department of Health and Human Services
Deferred Maintenance
For the Fiscal Years Ended September 30, 2002 and 2001

Deferred maintenance is maintenance that was not performed when it should have been, was scheduled and not performed, or was delayed for a future period. Maintenance is the act of keeping fixed assets in acceptable condition, including preventive maintenance, normal repairs, replacement of parts and structural components and other activities needed to preserve the asset so that it continues to provide acceptable services and achieves its expected life. Maintenance does not include activities aimed at expanding the capacity of an asset or otherwise upgrading it to serve needs different from, or significantly greater than, those originally intended. Maintenance expense is recognized as incurred. The Centers for Disease Control and Prevention, the National Institutes of Health, and the Food and Drug Administration all use the condition assessment survey for all classes of property. The Indian Health Service uses two types of surveys to assess installations – annual general inspections and deep look surveys.

Category of Asset	Condition	Cost to Return to Acceptable Condition 2002	2001 Restated
General PP&E			
Buildings	3 – 4	$ 718	$ 690
Equipment	4	5	7
Other Structures	4	11	13
Total		$ 734	$ 710

Asset Condition is assessed on a scale of 1-5 as follows: Excellent-1; Good-2; Fair-3; Poor-4; Very Poor-5. A "fair" or 3 rating is considered acceptable operating condition. Although PP&E categories may be rated as acceptable, individual assets within a category may require maintenance work to return them to acceptable operating condition. Therefore, asset categories with an overall rating of "fair" or above may still report necessary costs to return them to acceptable condition.

U.S. Department of Health and Human Services
Intragovernmental Transactions – Assets
For the Fiscal Year Ended September 30, 2002
(in millions)

Agency	TFM Dept Code	Fund Bal. w/ Treasury	Investments	Accounts Receivable	Other [1]
Dept of Agriculture	12	$ -	$ -	$ 5	$ -
Dept of Commerce	13	-	-	3	7
Dept of Defense	17,21,57,97	-	-	138	1
Dept of Education	91	-	-	2	-
Dept of Energy	89	-	-	6	-
Dept of Housing & Urban Development	86	-	-	13	-
Dept of the Interior	14	-	-	1	-
Dept of Justice	15	-	-	8	-
Dept of Labor	16	-	-	5	-
Dept of State	19	-	-	3	-
Dept of Transportation	69	-	-	2	-
Dept of the Treasury	20	84,772	273,867	44	10,410
Dept of Veterans Affairs	36	-	-	5	-
Agency for International Development	72	-	-	14	-
Environmental Protection Agency	68	-	-	44	-
Federal Emergency Mgmt Agency	58	-	-	26	131
General Services Admin	47	-	-	3	-
National Aeronautics & Space Admin	80	-	-	1	-
National Science Foundation	49	-	-	3	-
Nuclear Regulatory Commission	31	-	-	-	-
Office of Personnel Mgmt	24	-	-	-	-
Small Business Admin	73	-	-	-	-
Social Security Admin	28	-	-	2	-
RRB	60	-	-	412	-
All other Federal agencies		-	-	103	-
Total		$ 84,772	$ 273,867	$ 843	$ 10,549

[1] Includes Anticipated Congressional Appropriation of $10,399.

U.S. Department of Health and Human Services
Intragovernmental Transactions – Liabilities
For the Fiscal Year Ended September 30, 2002
(in millions)

Agency	TFM Dept Code	Accounts Payable	Accrued Payroll & Benefits	Other
Dept of Agriculture	12	$ -	$ -	$ -
Dept of Commerce	13	-	-	-
Dept of Defense	17,21,57,97	6	-	4
Dept of Education	91	-	-	-
Dept of Energy	89	3	-	5
Dept of Housing & Urban Development	86	-	-	57
Dept of the Interior	14	9	-	-
Dept of Justice	15	-	-	28
Dept of Labor	16	-	15	4
Dept of State	19	-	-	-
Dept of Transportation	69	-	-	-
Dept of the Treasury	20	-	34	654
Dept of Veterans Affairs	36	4	-	2
Agency for International Development	72	-	-	-
Environmental Protection Agency	68	-	-	54
Federal Emergency Mgmt Agency	58	-	-	76
General Services Admin	47	23	-	68
National Aeronautics & Space Admin	80	-	-	1
National Science Foundation	49	-	-	-
Nuclear Regulatory Commission	31	-	-	-
Office of Personnel Mgmt	24	1	27	-
Small Business Admin	73	-	-	-
Social Security Admin	28	224	-	-
RRB	60	-	-	-
All other Federal agencies		-	-	14
Total		$ 270	$ 76	$ 967

U.S. Department of Health and Human Services
Intragovernmental Transactions – Revenues and Expenses
For the Fiscal Year Ended September 30, 2002
(in millions)

Agency	TFM Dept Code	Earned Revenue	Gross Cost	Non-exchange Revenue Transfers-In	Non-exchange Revenue Transfers-Out
Dept of Agriculture	12	$ 10	$ (5)	$ -	$ -
Dept of Commerce	13	7	(44)	-	-
Dept of Defense	17,21,57,97	63	(35)	81	-
Dept of Education	91	10	(4)	-	-
Dept of Energy	89	33	(49)	-	-
Dept of Housing & Urban Development	86	7	-	-	-
Dept of the Interior	14	5	(58)	-	-
Dept of Justice	15	94	(112)	-	-
Dept of Labor	16	10	(28)	-	-
Dept of State	19	5	(49)	-	-
Dept of Transportation	69	5	(18)	-	-
Dept of the Treasury	20	32	(42)	-	-
Dept of Veterans Affairs	36	42	(37)	-	-
Agency for International Development	72	43	(9)	-	-
Environmental Protection Agency	68	37	(5)	78	-
Federal Emergency Mgmt Agency	58	13	(238)	-	-
General Services Admin	47	9	(659)	-	-
National Aeronautics & Space Admin	80	3	(1)	-	-
National Science Foundation	49	3	(15)	-	-
Nuclear Regulatory Commission	31	1	-	-	-
Office of Personnel Mgmt	24	-	(2,124)	-	-
Small Business Admin	73	3	-	-	-
Social Security Admin	28	10	(6)	2	(1,405)
RRB	60	-	-	373	(5)
All other Federal agencies		33	(85)	-	(8)
Total		$ 478	$ (3,623)	$ 534	$ (1,418)

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U.S. Department of Health and Human Services
Consolidating Balance Sheet by Budget Function
As of September 30, 2002
(in millions)

	Education, Training & Social Services	Health	Medicare	Income Security	Admin. of Justice	Natural Resources & Environ	OPDIV Combined Totals	Intra-HHS Eliminations	HHS Consolidated Totals
Assets (Note 2)									
Intragovernmental									
Fund Balance with Treasury (Note 3)	$ 8,979	$ 56,831	$ 2,925	$ 16,002	$ 16	$ 19	$ 84,772	$ -	$ 84,772
Investments, Net (Note 5)	-	1,934	271,933	-	-	-	273,867	-	273,867
Accounts Receivable, Net (Note 6)	3	471	2,369	-	-	-	2,843	(2,000)	843
Anticipated Congressional Appropriation - CMS (Note 7)	-	10,399	-	-	-	-	10,399	-	10,399
Other (Note 11)	-	430	-	-	-	-	430	(280)	150
Total Intragovernmental	$ 8,982	$ 70,065	$ 277,227	$ 16,002	$ 16	$ 19	$ 372,311	$ (2,280)	$ 370,031
Accounts Receivable, Net (Note 6)	-	1,437	2,669	44	-	-	4,150		4,150
Loans Receivable and Foreclosed Property (Note 8)	-	370	-	-	-	-	370		370
Cash and Other Monetary Assets (Note 4)	-	-	375	-	-	-	375		375
Inventory and Related Property, Net (Note 9)	-	165	-	-	-	-	165		165
General Property, Plant & Equipment, Net (Note 10)	-	2,746	9	-	-	1	2,756		2,756
Other (Note 11)	-	18	43	-	-	-	61		61
Total Assets	**$ 8,982**	**$ 74,801**	**$ 280,323**	**$ 16,046**	**$ 16**	**$ 20**	**$ 380,188**	**$ (2,280)**	**$ 377,908**
Liabilities (Note 12)									
Intragovernmental									
Accounts Payable	$ 9	$ 119	$ 2,090	$ 1	$ -	$ -	$ 2,219	$ (1,949)	$ 270
Accrued Payroll and Benefits	2	70	4	-	-	-	76	-	76
Other (Note 17)	-	1,056	242	-	-	-	1,298	(331)	967
Total Intragovernmental	$ 11	$ 1,245	$ 2,336	$ 1	$ -	$ -	$ 3,593	$ (2,280)	$ 1,313
Accounts Payable	13	753	-	9	-	-	775		775
Entitlement Benefits Due and Payable (Note 13)	-	16,340	28,236	-	-	-	44,576		44,576
Environmental and Disposal Costs (Note 15)	-	15	-	-	-	-	15		15
Accrued Grant Liability (Note 16)	885	1,629	-	913	50	3	3,480		3,480
Loan Guarantees Liability (Note 8)	-	276	-	-	-	-	276		276
Federal Employee and Veterans Benefits (Note 14)	5	8,158	10	-	-	1	8,174		8,174
Accrued Payroll and Benefits	19	720	53	-	-	-	792		792
Other (Note 17)	(2)	650	201	12	-	1	862		862
Total Liabilities	**$ 931**	**$ 29,786**	**$ 30,836**	**$ 935**	**$ 50**	**$ 5**	**$ 62,543**	**$ (2,280)**	**$ 60,263**
Net Position									
Unexpended Appropriations	8,022	47,635	3,017	15,112	-	-	73,786		73,786
Cumulative Results of Operations	29	(2,620)	246,470	(1)	(34)	15	243,859	-	243,859
Total Net Position	$ 8,051	$ 45,015	$ 249,487	$ 15,111	$ (34)	$ 15	$ 317,645	$ -	$ 317,645
Total Liabilities and Net Position	**$ 8,982**	**$ 74,801**	**$ 280,323**	**$ 16,046**	**$ 16**	**$ 20**	**$ 380,188**	**$ (2,280)**	**$ 377,908**

In addition to this schedule, more detailed information on individual operating divisions (OPDIVs) can be found in the OPDIVs' audited financial statement. OPDIV financial statements can be accessed on the Internet at: ***www.hhs.gov***

U.S. Department of Health and Human Services
Consolidating Balance Sheet by Operating Division
As of September 30, 2002
(in millions)

	ACF	AoA	AHRQ	CDC	CMS	FDA	HRSA	IHS	NIH	OS	PSC	SAMHSA	OPDIV Consolidated Totals	Inter-OPDIV Eliminations	HHS Consolidated Totals
Assets (Note 2)															
Intragovernmental															
Fund Balance with Treasury (Note 3)	$ 24,443	$ 553	$ 356	$ 4,607	$ 19,182	$ 711	$ 5,581	$ 1,426	$ 22,455	$ 2,922	$ 94	$ 2,442	$ 84,772	$ -	$ 84,772
Investments, Net (Note 5)	-	-	-	-	271,933	-	1,907	-	27	-	-	-	273,867	-	273,867
Accounts Receivable, Net (Note 6)	3	-	1	83	634	11	-	21	52	67	96	-	968	(125)	843
Anticipated Congressional Appropriation - CMS (Note 7)	-	-	-	-	10,399	-	-	-	-	-	-	-	10,399	-	10,399
Other (Note 11)	-	-	-	10	-	-	-	-	11	131	1	-	153	(3)	150
Total Intragovernmental	24,446	553	357	4,700	302,148	722	7,488	1,447	22,545	3,120	191	2,442	370,159	(128)	370,031
Accounts Receivable, Net (Note 6)	44	-	-	8	3,612	379	1	82	14	-	7	3	4,150	-	4,150
Loans Receivable and Foreclosed Property (Note 8)	-	-	-	-	-	$ -	370	-	-	-	-	-	370	-	370
Cash and Other Monetary Assets (Note 4)	-	-	-	-	375	-	-	-	-	-	-	-	375	-	375
Inventory and Related Property, Net (Note 9)	-	-	-	30	-	-	-	12	13	94	16	-	165	-	165
General Property, Plant & Equipment, Net (Note 10)	-	-	-	313	9	261	1	760	1,378	21	13	-	2,756	-	2,756
Other (Note 11)	-	-	-	2	54	-	-	1	2	-	2	-	61	-	61
Total Assets	**$ 24,490**	**$ 553**	**$ 357**	**$ 5,053**	**$ 306,198**	**$ 1,362**	**$ 7,860**	**$ 2,302**	**$ 23,952**	**$ 3,235**	**$ 229**	**$ 2,445**	**$ 378,036**	**$ (128)**	**$ 377,908**
Liabilities (Note 12)															
Intragovernmental															
Accounts Payable	$ 10	$ -	$ 2	$ -	$ 224	$ 13	$ 11	$ 1	$ 47	$ 32	$ 1	$ 3	$ 344	$ (74)	$ 270
Accrued Payroll and Benefits	2	-	-	5	5	12	3	13	26	4	5	1	76	-	76
Other (Note 17)	-	-	-	81	312	374	59	107	11	-	1	76	1,021	(54)	967
Total Intragovernmental	12	-	2	86	541	399	73	121	84	36	7	80	1,441	$ (128)	1,313
Accounts Payable	21	1	12	258	-	80	38	56	204	39	43	23	775	-	775
Entitlement Benefits Due and Payable (Note 13)	-	-	-	-	44,576	-	-	-	-	-	-	-	44,576	-	44,576
Environmental and Disposal Costs (Note 15)	-	-	-	3	-	4	-	-	8	-	-	-	15	-	15
Accrued Grant Liability (Note 16)	1,770	78	7	230	-	-	343	14	1,083	(30)	-	(15)	3,480	-	3,480
Loan Guarantees Liability (Note 8)	-	-	-	-	-	-	276	-	-	-	-	-	276	-	276
Federal Employee and Veterans Benefits (Note 14)	5	-	1	18	10	21	35	79	61	22	7,900	22	8,174	-	8,174
Accrued Payroll and Benefits	18	1	3	97	56	110	30	130	268	44	27	8	792	-	792
Other (Note 17)	9	1	1	37	212	129	347	39	83	3	2	(1)	862	-	862
Total Liabilities	**$ 1,835**	**$ 81**	**$ 26**	**$ 729**	**$ 45,395**	**$ 743**	**$ 1,142**	**$ 439**	**$ 1,791**	**$ 114**	**$ 7,979**	**$ 117**	**$ 60,391**	**$ (128)**	**$ 60,263**
Net Position															
Unexpended Appropriations	22,661	473	35	4,038	14,096	414	4,639	1,226	20,764	3,051	34	2,355	73,786	-	73,786
Cumulative Results of Operations	(6)	(1)	296	286	246,707	205	2,079	637	1,397	70	(7,784)	(27)	243,859	-	243,859
Total Net Position	$ 22,655	$ 472	$ 331	$ 4,324	$ 260,803	$ 619	$ 6,718	$ 1,863	$ 22,161	$ 3,121	$ (7,750)	$ 2,328	$ 317,645	$ -	$ 317,645
Total Liabilities and Net Position	**$ 24,490**	**$ 553**	**$ 357**	**$ 5,053**	**$ 306,198**	**$ 1,362**	**$ 7,860**	**$ 2,302**	**$ 23,952**	**$ 3,235**	**$ 229**	**$ 2,445**	**$ 378,036**	**$ (128)**	**$ 377,908**

In addition to this schedule, more detailed information on individual operating divisions (OPDIVs) can be found in the OPDIVs' audited financial statement. OPDIV financial statements can be accessed on the Internet at: ***www.hhs.gov***

Department of Health and Human Services
Consolidating Statement of Net Cost By Budget Function
For the Fiscal Year Ended September 30, 2002
(in millions)

Operating Division:	Education, Training, & Social Services	Health	Medicare	Income Security	Admin of Justice	Natural Resources & Environment	OPDIV Combined Totals	Intra-HHS Eliminations Cost (-)	Intra-HHS Eliminations Revenue	HHS Consolidated Totals
ACF	$ 16,139	$ -	$ -	$ 29,792	$ 28	$ -	$ 45,959	$ (27)	$ 4	$ 45,936
AoA	1,104	-	-	-	-	-	1,104	(2)	-	1,102
AHRQ	-	276	-	-	-	-	276	(5)	-	271
CDC	-	4,542	-	-	-	11	4,553	(113)	93	4,533
CMS	-	153,792	231,132	-	-	-	384,924	(46)	1	384,879
FDA	-	1,298	-	-	-	-	1,298	(78)	19	1,239
HRSA	-	5,794	-	-	-	-	5,794	(102)	27	5,719
IHS	-	2,857	-	-	-	-	2,857	(29)	20	2,848
NIH	-	20,575	-	-	-	-	20,575	(438)	93	20,230
OS	-	1,285	-	-	-	-	1,285	(73)	115	1,327
PSC	-	946	-	-	-	-	946	(22)	208	1,132
SAMHSA	-	2,883	-	-	-	-	2,883	(34)	9	2,858
Net Cost of Operations	**$ 17,243**	**$ 194,248**	**$ 231,132**	**$ 29,792**	**$ 28**	**$ 11**	**$ 472,454**	**$ (969)**	**$ 589**	**$ 472,074**

U.S. Department of Health and Human Services
Gross Cost and Exchange Revenue
For the Fiscal Year Ended September 30, 2002
(in millions)

Operating Division	Intragovernmental						With the Public		HHS Consolidated Net Cost of Operations
	Gross Cost			Less: Exchange Revenue					
	Combined	Eliminations	Consolidated	Combined	Eliminations	Consolidated	Gross Cost	Less: Exchange Revenue	
ACF	$ 128	$ (45)	$ 83	$ 26	$ (22)	$ 4	$ 45,857	$ -	$ 45,936
AoA	9	(2)	7	-	-	-	1,095	-	1,102
AHRQ	29	(5)	24	-	-	-	247	-	271
CDC	517	(120)	397	166	(100)	66	4,205	3	4,533
CMS	279	(46)	233	1	(1)	-	410,663	26,017	384,879
FDA	366	(78)	288	23	(19)	4	1,121	166	1,239
HRSA	219	(108)	111	110	(33)	77	5,771	86	5,719
IHS	258	(29)	229	21	(20)	1	3,361	741	2,848
NIH	2,453	(1,811)	642	1,537	(1,466)	71	19,733	74	20,230
OS	452	(76)	376	173	(118)	55	1,006	-	1,327
PSC	1,226	(27)	1,199	398	(213)	185	118	-	1,132
SAMHSA	68	(34)	34	24	(9)	15	2,839	-	2,858
Totals	**$ 6,004**	**$ (2,381)**	**$ 3,623**	**$ 2,479**	**$ (2,001)**	**$ 478**	**$ 496,016**	**$ 27,087**	**$ 472,074**