Department of State
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
[Dollars in Thousands]

As of September 30,	1997 Audited	1996 Audited-Restated
ASSETS		
Entity Assets:		
Intragovernmental Assets -		
Fund Balances With Treasury (Note 2)	$2,435,277	$2,184,427
Investments (Note 4)	8,989,294	8,398,879
Accounts Receivable, Net	391,013	481,705
Interest Receivable	171,296	163,750
Advances and Prepayments	475	749
Governmental Assets -		
Accounts Receivable, Net	193,380	11,306
Credit Program Receivables (Note 5)	582	127
Advances and Prepayments	71,832	80,923
Cash and Other Monetary Assets (Note 3)	173	82
Inventory, Net (Note 6)	1,067	1,059
Property and Equipment, Net (Note 7)	4,399,532	4,571,585
Total Entity Assets	$16,653,921	$15,894,592
Non-Entity Assets:		
Cash and Other Monetary Assets (Note 3)	$110,308	$109,842
Total Non-Entity Assets	$110,308	$109,842
Total Assets	$16,764,229	$16,004,434

The accompanying notes are an integral part of the financial statements

Department of State

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

[Dollars in Thousands]

As of September 30,	1997 Audited	1996 Audited-Restated
LIABILITIES		
Liabilities Covered by Budgetary Resources:		
Intergovernmental Liabilities -		
Accounts Payable	$19,469	$33,114
Other Intragovernmental Liabilities	14,258	6,094
Governmental Liabilities -		
Accounts Payable	233,279	468,692
Pension Actuarial Liability (Note 9)	9,115,284	8,526,657
Accrued Salary and Benefits	100,158	103,200
Other Governmental Liabilities (Note 10)	269,653	25,935
Total Liabilities Covered by Budgetary Resources	$9,752,101	$9,163,692
Liabilities not Covered by Budgetary Resources:		
Intragovernmental Liabilities -		
Future Workers' Compensation Benefits	$43,706	$35,806
Other	-	521
Governmental Liabilities -		
Assessments from International Organizations (Note 11)	1,700,459	1,743,213
Pension Actuarial Liability (Note 9)	1,372,916	698,643
Capital Leases	81,683	70,279
Accrued Annual Leave	80,000	68,876
Funds Held in Trust (Note 3)	110,308	109,842
Other	125	15
Total Liabilities not Covered by Budgetary Resources	$3,389,197	$2,727,195
Total Liabilities	$13,141,298	$11,890,887
NET POSITION (Note 12)		
Unexpended Appropriations	$2,092,515	$1,873,319
Invested Capital	3,732,898	4,470,594
Cumulative Results of Operations	457,384	316,707
Donations	537,339	-
Future Funding Requirements	(3,197,205)	(2,547,073)
Total Net Position	$3,622,931	$4,113,547
Total Liabilities and Net Position	$16,764,229	$16,004,434

The accompanying notes are an integral part of the financial statements

Department of State

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

[Dollars in Thousands]

For the Period Ended September 30,	1997 Audited	1996 Unaudited
REVENUES AND FINANCING SOURCES:		
Appropriated Capital Used	$5,156,891	$4,995,927
Sales of Goods and Services -		
To the Public	639,715	577,945
Intragovernmental	521,475	491,720
Interest and Penalties, Non-Federal	24	122
Interest, Federal	675,351	641,134
Other Revenues and Financing Sources (Note 13)	260,867	144,033
Funds Transferred to Treasury	(469,129)	(428,784)
Total Revenues and Financing Sources	$6,785,194	$6,422,097
EXPENSES:		
Program or Operating Expenses (Note 14)	$5,754,252	$5,532,549
Unfunded Assessments from International Organizations	(42,754)	1,743,213
Change in Pension Actuarial Liability	222,500	359,400
Depreciation and Amortization	207,699	178,498
Other Expenses	44,000	-
Accrued Annual Leave	11,124	6,274
Future Worker's Compensation	7,898	798
Interest from Treasury Borrowing	9	9
Total Expenses	$6,204,728	$7,820,741
Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	$580,466	($1,398,644)
Net Position, Beginning Balance	$4,113,547	$8,454,051
Adjustments to Beginning Net Position (Note 15)	(241,885)	8,246
Cumulative Effect of Accounting Change (Note 16)	(1,040,400)	-
Net Position, Beginning Balance, Restated	$2,831,262	$8,462,297
Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	580,466	(1,398,644)
Non-Operating Changes (Note 17)	211,203	(2,950,106)
Net Position, Ending Balance	$3,622,931	$4,113,547

The accompanying notes are an integral part of the financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

ORGANIZATION

The U.S. Department of State, the senior executive department of the U.S. Government, was established by Congress in 1789, replacing the Department of Foreign Affairs established in 1781. The Department advises the President in the formulation and execution of foreign policy. As its head, the Secretary of State is the President's principal foreign affairs adviser. The Department's primary objective in the conduct of foreign relations is to promote U.S. security and well-being.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements reflect the financial position and results of operations for the Department. They have been prepared from the Department's books and records in accordance with its accounting policies which are summarized in this Note. These statements are presented in accordance with form and content requirements contained in Office of Management and Budget (OMB) Bulletin No. 94-01, *Form and Content of Agency Financial Statements*, and the Government Management Reform Act (GMRA) of 1994. The GMRA does not require the presentation of a Statement of Cash Flows nor a Statement of Budgetary Resources and Actual Expenses, and those statements are not presented. The statements presented herein are different from the financial reports prepared by the Department in accordance with OMB directives to monitor and control the status and use of budgetary resources.

The Department's accounting policies follow an "other comprehensive basis of accounting" as agreed to and published by the Director of OMB, the Secretary of the Treasury, and the Comptroller General. This basis consists of the following hierarchy.

1. Accounting standards and principles recommended by the Federal Accounting Standards Advisory Board (FASAB), and approved and issued by the above-named officials. These are known as Statements of Federal Financial Accounting Standards (SFFAS).
2. Form and content requirements in OMB Bulletin 94-01.
3. Accounting standards contained in the Department's accounting policy manuals and handbooks.
4. Accounting principles published by authoritative standard-setting bodies (e.g., Financial Accounting Standards Board (FASB)) and other authoritative sources (1) in the absence of other guidance in the first three parts of this hierarchy, and/or (2) if the use of such accounting standards improves the meaningfulness of these financial statements.

Reporting Entity and Basis of Consolidation

The accompanying financial statements reflect Department of State financial activity. The statements include accounts of all funds under Department control that have been established and maintained to account for resources of Department management, or for which the Department acts as a fiscal agent or custodian. The Department maintains 30 general funds, 4 special funds, 2 revolving funds, 4 trust funds, and 23 deposit funds.

- General and special fund accounts are used to record financial transactions under congressional appropriations or other authorization to spend general revenues.

- Revolving fund accounts are established by law to finance a continuing cycle of operations, with receipts derived from such operations usually available in their entirety for use by the fund without further action by Congress.

- Trust fund accounts are credited with receipts generated by the terms of a trust agreement or statute. At the point of collection, these receipts are available immediately or unavailable depending upon statutory requirements.

- Deposit fund accounts are established for: (1) amounts received for which the Department is acting as a fiscal agent or custodian, (2) unidentified remittances, (3) monies withheld from payments for goods and services received, and (4) monies held awaiting distribution on the basis of a legal determination.

Except for the Foreign Service Retirement and Disability Fund (FSRDF), the financial activities of these funds have been classified into functional areas in the consolidating statements presented as supplemental data. This classification is consistent with their presentation in the *Budget of the United States Government* – Administration of Foreign Affairs, International Organizations and Conferences, International Commissions, Foreign Assistance, and Other Funds. The FSRDF, the Department's largest fund in terms of total assets, is reported in the *Budget of the United States Government* under the Administration of Foreign Affairs, but is displayed separately in the consolidating statements. The funds in each functional area are as follows.

- Administration of Foreign Affairs
  - Diplomatic and Consular Programs (D&CP)
  - Salaries and Expenses (S&E)
  - Security and Maintenance of U.S. Missions
  - Working Capital Fund (WCF)
  - Repatriation Loans
  - Foreign Service National Separation Liability Trust Fund (FSNSLTF)
  - Gift Funds
  - Capital Investment Fund
  - Emergencies in the Diplomatic and Consular Service
  - Payments to the American Institute in Taiwan
  - Office of Inspector General
  - Representation Allowances
  - Payment to the Foreign Service Retirement and Disability Fund

- International Organizations and Conferences
  - International Peacekeeping Activities
  - Contributions to International Organizations
  - International Conferences and Contingencies

- International Commissions
  - International Boundary and Water Commission (IBWC)
  - International Commissions
  - International Fisheries Commission

- Foreign Assistance
  - Migration and Refugee Assistance
  - Emergency Refugee and Migration Assistance
  - International Narcotics Control
  - Anti-Terrorism Assistance
  - Special Assistance to Cuban and Haitian Entrants

- Other Funds
  - International Center
  - Asia Foundation
  - Nonproliferation and Disarmament Fund
  - Fisherman's Protective and Special Funds
  - International Litigation Fund
  - Soviet-East European Research and Training
  - Promotion of Stability and Security in Central America
  - Various Deposit and Clearing Accounts

For 1996, the Department did not include the Bosnia Federation Defense Fund in the consolidated financial statements. This Fund is a depository account in the U.S. Treasury (Treasury) that contains monies contributed by governments to assist Bosnia-Herzegovina in establishing a military balance to promote lasting peace in the region. The Fund was excluded because the Department acts solely as a fiscal agent, makes disbursements and handles record-keeping for the account as instructed by the donor governments and the Federation, and has no title to nor control of any monies in the Fund. For 1997, the Department included this account so that amounts reported would encompass every Deposit Fund carried by the Treasury for the Department, and thereby provide for a better Government-wide reconciliation and reporting. Since the Department has no title to these monies, they are reported as Non-Entity Assets and a corresponding amount is reported as Governmental Liabilities (**see** Note 3). The 1996 totals have been restated to reflect the inclusion of this fund. The effect of these changes increased Non-Entity Assets and Governmental Liabilities by $99.8 million in the Statement of Financial Position. This change had no effect on the 1996 Statement of Operations and Changes in Net Position.

All significant interfund balances and transactions within the Department have been eliminated in consolidation.

Basis of Accounting

Transactions are recorded on both an accrual and budgetary basis. Under the accrual method, reimbursements are recognized when earned and expenses are recognized when a liability is incurred. Budgetary accounting facilitates compliance with legal constraints and controls over the use of Federal resources.

Budgets and Budgetary Accounting

Congress generally enacts one-year appropriations that provide the Department with authority to obligate funds within the fiscal year cited for necessary expenses to carry out mandated program activities. In addition, Congress also enacts multi-year appropriations and appropriations that are available until expended (e.g., Capital Investment Fund, Emergencies in the Diplomatic and Consular Service, Security and Maintenance of U.S. Missions). The Funds appropriated are subject to OMB apportionment of funds in addition to congressional restrictions on the expenditure of funds. Also, the Department places internal restrictions to ensure the efficient and proper use of all funds. One-year and multi-year fixed appropriations are canceled and cannot be used for disbursements after 5 years have elapsed since the appropriation was last available for obligation.

Revenues and Other Financing Sources

Department operations are financed through appropriations, reimbursements for the provision of goods or services, proceeds of sales of property, certain consular-related and other fees, and donations. In addition, the Department collects, but does not retain, passport, visa, and other consular fees. These passport and visa fees are deposited directly to a U.S. Treasury receipt account and reported as Sales of Goods and Services to the Public and Funds Transferred to Treasury in the Statement of Operations and Changes in Net Position.

For financial statement purposes, appropriations are reported as a financing source, i.e., Appropriated Capital Used, at the time they are recognized as an expense. Appropriations expended for capitalized property and equipment are recognized as expenses when the asset is consumed in operations and the applicable depreciation expenses recorded.

Work performed for other Federal agencies is initially financed through the account providing the service (e.g., D&CP, S&E, and WCF) and subsequently reimbursed from other agencies or funds. Reimbursements are recognized as revenues when earned, i.e., goods have been delivered or services rendered, and the associated costs incurred. Administrative support services at overseas posts are provided to other Federal agencies through the International Cooperative Administrative

Support Services Fund (ICASS). ICASS charges for the services used by the agencies at overseas posts. These charges become revenue to ICASS and must be sufficient to cover all overhead and operating expenses and provide enough profit to replace capital assets necessary to carry on the operation. Revenue is recognized when billed. Agencies are billed at the beginning of each fiscal year for their estimated use of ICASS services. At midyear, a second billing is made to adjust for changes based on actual usage through the first half of the year.

Proceeds of sales of real property, vehicles, and other personal property are recognized as revenues when the proceeds of sales are credited to the account from which the asset was funded. For noncapitalized property, the full amount realized is recognized as revenue. For capitalized property, gain or loss is recognized based on whether the proceeds received were greater or less than the net book value of the asset sold. The funds received are available for purchase of the same or similar category of property.

The Department is authorized to collect and retain for specific uses, fees for machine-readable visas, expedited passport processing, and fingerprint checks on immigrant visa applicants. These revenues are recognized in the D&CP account when the fees are collected. The Department is also authorized to credit to the respective appropriations fees for the use of Blair House, lease payments and transfers from the International Center Chancery Fees held in Trust to the International Center Project, registration fees for the Office of Defense Trade Controls, reimbursements for international litigation related expenses, and reimbursement for training of foreign government officials at the National Foreign Affairs Training Center.

Generally, contributions (i.e., gifts) received, including unconditional promises to give, are recognized as revenues at their fair values in the period received. Contributions of services are recognized if the services received: (1) create or enhance nonfinancial assets, or (2) require specialized skills provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. Contributions of works of art, historical treasures, and similar assets that are added to collections are not recognized at time of donation. If subsequently sold, proceeds from the sale of these collection items are recognized in the year of sale.

The Department receives the majority of the funding needed to support the Repatriation Loan Program through an annual appropriation and permanent, indefinite borrowing authority. The appropriation has two components: (1) the subsidy portion for the present value of long-term cash flows, and (2) estimated expenses to administer the program. Appropriations are recognized as appropriated capital used at the time the loans are obligated and administrative expenses are incurred.

Fund Balances with Treasury

The Fund Balances with Treasury are resources available to pay accrued liabilities and finance authorized commitments relative to goods, services, and benefits. The Department does not maintain cash in commercial bank accounts for the resources reported in its financial statements, except for the Office of Foreign Missions and the International Center, which maintain a commercial account for lease fees held in trust. Domestic receipts and disbursements are processed by the U.S. Treasury. The Department operates three Financial Service Centers at Paris, France; Bangkok, Thailand; and Charleston, South Carolina; that provide financial support for the Department of State and other agencies' overseas operations. There is a U.S. Disbursing Officer (USDO) at each Center, who is empowered to disburse funds on behalf of Treasury.

Accounts Receivable

Intragovernmental accounts receivable are due principally from other Federal entities for reimbursable and WCF services. Governmental accounts receivable are due primarily for sales of real property overseas. There are also governmental accounts receivable from current and former employees and vendors. Governmental accounts receivable from current and former employees and vendors are subject to the full debt collection cycle, e.g., salary offset, referral to collection agents, and Internal Revenue Service offset. Uncollectible amounts are not formally closed out but are written off and become inactive.

Credit Program Receivables

The Department provides repatriation loans for destitute American citizens overseas. These loans provide assistance to pay for return transportation, food and lodging, or medical expenses. The application process requires that relatives and friends are the primary source of funding, but when that fails, the Department become the lender of last resort. A promissory note is executed by the borrower without collateral. Consequently, loans are made anticipating a low recovery rate.

Loans are accounted for as credit program receivables from the time of disbursement. For loans made prior to October 1, 1991, loan principal, interest receivable, penalties, and fees are reduced by an allowance for estimated uncollectible amounts. The allowance is based on historical experience and an analysis of outstanding balances. Loans made on or after October 1, 1991, are reduced by an allowance equal to the present value of the subsidy costs associated with these loans.

Loans are due and payable 60 days after disbursement. After 60 days, they are considered delinquent, and interest is accrued at the current Treasury rate from the original disbursement date. After 60 days, a 6% penalty and a $50 handling fee are added to the outstanding principal balance.

After collection procedures have been exhausted, delinquent loans become inactive. Inactive loans are nonperforming and therefore do not accrue interest and penalties. Inactive loans meeting specific criteria remain on the books and are referred to the Department of the Treasury for tax refund offset. Other loans that are deemed uncollectible or not of economic value to continue collection efforts are closed out.

Advances and Prepayments

Payments in advance of the receipt of goods and services are recorded as advances or prepayments and recognized as expenses when the related goods and services are received. Governmental advances are principally advances to Department employees for official travel, prepayments and advances to other entities for future services, and salary advances to employees transferring to overseas assignments.

Valuation of Investments

FSRDF investments consist solely of special issues of U.S. Government securities, which are redeemable on demand, at par. Therefore, for financial statement purposes, the investments are valued at par. Interest on the investments is paid semiannually, on June 30 and December 31.

The Gift Funds investments consist of U.S. guaranteed securities. These investments are reported at the acquisition cost, which equals the security's face value plus or minus the unamortized premium or discount. Premiums and discounts are amortized over the life of the security using the effective interest method.

Works of Art and High-Value Furnishings

The Department of State's Gift Funds acquire collections of works of art and antique furnishings through purchase with donated funds or by in-kind donation. Collections are held for public exhibition, education, or official entertainment of visiting Chiefs of State, Heads of Government, Foreign Ministers, and other distinguished foreign and American guests. The Department provides protection and preservation services for these collections. The Office of Foreign Buildings Operations (A/FBO) manages the curatorial services and Art-in-Embassies programs, which provides high value furnishings and American art at embassies worldwide. Most of the artworks in the Art-in-Embassies program are on loan to the Department.

In accordance with accounting policies followed by museums, no value is assigned to the collections on the Statements of Financial Position. Purchases of items for collections are recorded as an expense in the year of purchase. Proceeds from disposals are recognized as other revenue in the year of sale and are designated for future collection acquisitions. As of September 30, 1997, there were 4,794 owned items in the Gift Funds' collection with a total estimated fair market value of $55.6 million and 189 loaned items with a total estimated fair market value of $7.8 million. Under the Curatorial Services Program, the Department owns fine and decorative art at 126 posts. The collections in Brussels, Lisbon, London, Madrid, Prague, Rome, and Paris are significant in number and intrinsic value. The estimated total value of the collection managed by the Art-in-Embassies program was $76.1 million as of September 30, 1997. Of this amount, $70.0 million is on loan to the Department, and $6.1 million is owned by the Department.

Inventories

Inventories are held by the WCF Publishing Services and Supply Services Center and Stock Account and the IBWC. The WCF inventory primarily consists of paper and inks used in the printing and reproduction services and furniture held for sale to bureaus within the Department. A central inventory of expendable supplies is maintained for use by the operations and maintenance program and administrative operations of the IBWC.

Publishing Services inventory on hand is valued at the latest acquisition cost. The Supply Services Center and Stock Account inventory is valued monthly using a weighted moving average. Recorded values are adjusted for the results of physical inventories taken periodically. IBWC's inventory is valued using the weighted average balance method.

Property and Equipment - Real Property

Real property assets primarily consist of facilities used for U.S. diplomatic missions abroad and capital improvements to these facilities. They include unimproved land, residential and functional use buildings, such as embassy/consulate office buildings, office annexes and support facilities, and construction in progress. These properties are managed by the Chiefs of Mission of U.S. Embassies under the policy direction and guidance of the Office of Foreign Buildings Operations. Title to these properties are held under various conditions, including fee simple, restricted use, crown lease, and deed of use agreement.

For 1997, additions to asset accounts for acquisitions, construction of new buildings, and capital improvements are based on historical costs. Construction-in-progress as of September 30, 1997, represents costs incurred for new facilities, major rehabilitations, or other improvements that are in the design or construction stage. When these projects are completed, the costs will be transferred to the appropriate property account. The capitalized costs for 1997 include both direct and indirect costs associated with the project.

Prior to 1997, historical cost information for most of the Department's overseas properties was either unavailable or incomplete. For 1996 statements, the Department estimated a value for worldwide real property assets through other means. These Assets valued through the estimation technique comprise nearly all assets as of September 30, 1997.

The estimation method applied for 1996 involved the use of appraisal estimates adjusted back to the year of acquisition or construction to approximate historical cost. The appraisal estimates were restated from the date of the appraisal estimate back to the date of acquisition, using local general inflation factors (e.g., consumer price index) and currency exchange rate fluctuations. In cases where the property cost was not separately allocated between land and buildings, the estimated cost was divided evenly between land and buildings.

If an estimated appraisal value was unavailable for a property, a value was determined by using a substitution method, that compared the asset without an appraisal estimate to similar properties in the same or proximate geographic location. If no comparable values were available to use in substitution and the property was recently constructed or acquired, the available cost information in the property accountability records was used. Available cost information was also used for properties in the 20 countries where the consumer price index or foreign currency exchange rate was so volatile that the standard valuation method was determined to be inaccurate.

The total value for worldwide real property prior to 1997 also includes a total for capital improvements for 1987 through 1996. This amount is included because the valuation method used did not reflect capital improvements that occurred since the property appraisal date. Since it was not possible to identify these improvements on a specific property basis, the amount was recorded in aggregate based on the total obligations for applicable program categories during the last 10 years. The aggregate capital improvement amount is being depreciated on a straight-line basis over 10 years.

Accumulated depreciation of buildings and other structures is computed on a straight-line basis. Buildings and other facilities are estimated to have a useful life of 30 years.

The Department also owns several domestic real properties, including the National Foreign Affairs Training Center, the International Center, the Charleston Financial Services Center, the Beltsville Information Management Center, the Florida Regional Center, and the Portsmouth, NH Consular Center. Except for the International Center, these properties have been recorded at their estimated actual cost, based on available information maintained by the Department's Office of Real Property Management. The value for the International Center is reconstructed historical cost. In addition, the IBWC has buildings and structures related to boundary preservation, flood control, and sanitation. Its buildings and structures are capitalized at cost.

For valuation purposes, as of September 30, 1997, all Department real property has been treated as general purpose property.

Property and Equipment - Personal Property

In general, personal property and equipment with an acquisition cost of $25,000 or more and a useful life of two years or more is capitalized at cost. However, some items are capitalized using different amounts. All vehicles are capitalized. In addition, COTS software costing more than $100,000, and ADP software developed internally costing more than $250,000 are capitalized. Depreciation of property and equipment is calculated on a straight-line basis over the asset's estimated life with a 5% salvage value. Depreciation is not recorded until the fiscal year after the item is put into service. Vehicles are depreciated over periods ranging from three to six years. Other personal property and equipment is depreciated over periods ranging from five to eight years. Telecommunication equipment is depreciated over 20 years.

Capital Leases

Leases are accounted for as capital leases if they meet one of the criteria: (1) the lease transfers ownership of the property by the end of the lease term, (2) the lease contained an option to purchase the property at a bargain price, (3) the lease term is equal to or greater than 75 percent of the estimated useful life of the property, or (4) the present value of the minimum lease payments equals or exceeds 90% of the fair value of the leased property. The initial recording of the value of a lease (with a corresponding liability) is the lesser of the net present value of the lease payments or the fair value of the leased property. Capital leases are amortized over the term of the lease.

Accrued Salaries and Benefits, Accounts Payable, and Other Accrued Liabilities

Accrued salaries and benefits, accounts payable, and other accrued liabilities represent amounts owed for employee salaries, Foreign Service annuity benefits, and contracts for goods and services received, but unpaid, as of the end of the fiscal year.

Annual, Sick, and Other Leave

Annual leave is accrued as the accrual is earned and is reduced as it is taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick leave and other types of leave, which are not vested, are expensed when paid.

Borrowings Payable to Treasury

Borrowings payable to Treasury result from that portion of repatriation loans provided for under the Department's permanent, indefinite borrowing authority with Treasury. Periodic principal payments to Treasury are required based on the collection of loans receivable.

Interest Payable to Treasury

The Repatriation Loan Program accrues interest payable on the borrowings payable to Treasury. The Department is required to make periodic interest payments to Treasury based on its debt.

Retirement Plans

Department Civil Service employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Members of the Foreign Service participate in either the Foreign Service Retirement and Disability System (FSRDS) or the Foreign Service Pension System (FSPS).

Employees covered under CSRS make contributions of 7% with the Department making matching contributions. Employees covered under CSRS also contribute to Medicare insurance for which the Department makes a matching contribution of 1.45% of pay. On January 1, 1987, FERS went into effect pursuant to Public Law 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984, were allowed to join FERS or remain in CSRS. Employees participating in FERS contribute 0.8% of pay, and the Department contributes 12.9% of pay. In addition, FERS employees contribute 6.2% to Social Security and 1.45% to Medicare insurance; the Department makes matching contributions to both. A primary feature of FERS is that it offers a Thrift Savings Plan (TSP) into which the Department automatically contributes 1 percent of pay and matches employee contributions up to an additional 4% of pay.

Foreign Service employees hired prior to January 1, 1984, participate in the FSRDS with certain exceptions. FSPS was established pursuant to Public Law 99-335. Foreign Service employees hired after December 31, 1983, participate in FSPS with certain exceptions. FSRDS employees contribute 7% of pay and the Department makes a matching contribution. FSPS employees contribute a percentage of pay equal to 7.5% of pay minus a percentage for Old Age, Survivor, and Disability Insurance (OASDI). For 1997, the OASDI rate was 6.2%. Consequently, FSPS employees contributed 1.3% of pay. The Department makes a 23.04% contribution for FSPS employees. A primary feature of FSPS is that it offers a TSP identical to the FERS TSP.

FSNs and Third Country Nationals at worldwide posts who were hired prior to January 1, 1984, are covered under CSRS. Employees hired after that date are covered under a variety of local governmental plans in compliance with host-country laws and regulations. In a limited number of cases where no plans are regulated by the host country or such plans are inadequate, the employees are covered by a privately managed pension plan to conform with prevailing practices by comparable employers in those countries.

The Department does not report CSRS or FERS assets, accumulated plan benefits, or unfunded liabilities applicable to its employees. This information is reported by the Office of Personnel Management (OPM) on the Civil Service Retirement and Disability Fund (CSRDF). As described in

Note 16, the Department is required, beginning in 1997, to recognize an expense and imputed financing source for the unfunded portion of CSRDF pensions, post-retirement health benefits, and life insurance for Department employees reported by OPM.

Future Workers' Compensation Benefits

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to cover Federal employees injured on the job or who have incurred a work-related occupational disease and beneficiaries of employees whose death is attributable to job-related injury or occupational disease. FECA is administered by the U.S. Department of Labor (DOL). DOL initially pays valid claims and is subsequently reimbursed by the Department. The Department of Labor calculates the actuarial liability for claims outstanding at the end of the fiscal year. In 1997, the actuarial model was revised to provide for a more accurate estimate of the liability.

The present value of the liability estimates for 1997 was computed using a discount rate of 6.24% for the first year, 5.82% for the second year, 5.6% for the third year, 5.45% for the fourth year, and 5.4% for years thereafter. In 1997, the Department's actuarial liability increased by approximately $7.9 million. The total actuarial liability for which the Department is responsible totaled $43.7 million as of September 30, 1997. This liability will be paid when due from future appropriations.

Other Liabilities Not Covered by Budgetary Resources

These liabilities result from the receipt of goods and services in the current or prior periods, or occurrence of eligible events in the current or prior periods, for which revenues or other sources of funds to pay the liabilities have not been made available through appropriations or current Department earnings. Major liabilities in this category include assessments from international organizations, an unfunded actuarial liability for FSRDF, future workers' compensation benefits, and accrued annual leave (see additional explanation in Notes 1, 9, and 11).

Valuation of FSN Separation Liability

Separation payments are made to eligible FSN employees who voluntarily resign, retire, or lose their jobs due to a reduction in force and are in countries that require a voluntary separation payment. The amount required to finance the current and future costs of FSN separation pay are determined annually. To determine the annual adjustment, an amount is determined for the current year accrued annual adjustment based on current salary. In addition, an adjustment to prior years' accruals for current-year wage increases is determined. The amount of the increase in separation liability that becomes due from the Department's operating accounts comprises these two amounts added together.

Interest Receivable

Interest earned on investments, but not received as of September 30, 1997, is recognized as interest receivable.

Actuarial Present Value of Projected Plan Benefits

The Department's 1997 financial statements reflect the Pension Actuarial Liability of the Foreign Service Retirement and Disability Fund (the Plan) as the actuarial present value of projected plan benefits, as required by the SFFAS No. 5. The Pension Actuarial Liability represents those future periodic payments allocated for current employee and retired Plan participants, less future employee and Department contributions, stated in current dollars. Future periodic payments include expected benefits paid to (1) retired or terminated employees or their beneficiaries, (2) beneficiaries of employees who have died, and (3) present employees or their beneficiaries, including refunds of employee contributions as specified by Plan provisions. Total projected service is used to determine eligibility for retirement benefits. The value of voluntary, involuntary, and deferred retirement benefits is based on projected service and assumed salary increases. The value of benefits for disabled employees or survivors is determined by multiplying the benefit the employee or survivor would receive on the date of disability or death, by a ratio of service at the valuation date to projected service at the time of disability or death.

The Pension Actuarial Liability is determined by an actuary from Treasury. It is the amount that results from applying actuarial assumptions to adjust the projected Plan benefits to reflect the time value of money (discounts of interest) and the probability of payment (by means of decrements, such as death, disability, withdrawal or retirement) between the valuation date and the expected date of payment. For 1997, the valuation included assumed average rates of return on investments of 7%, inflation of 4%, and salary increases of 4.25%. The Plan uses an actuarial cost method known as aggregate entry age normal. The aggregate entry age normal is a method whereby the present value of projected benefits of each employee is allocated on a level basis (such as a constant percentage of salary) over the service of the employee between entry age and assumed exit age. The portion of the present value allocated to each year is referred to as the normal cost.

In February 1997, Treasury's Board of Actuaries announced a change in the dynamic economic assumptions used to calculate actuarial liability. The economic assumptions reflect predictions regarding long-term relationships among inflation, interest on investments, and salary adjustments. The new assumptions reflect recent financial experience and indicate a more optimistic view on the part of the Board regarding long-term interest earnings in relation to the other two factors.

The calculation of normal cost considers both the economic and demographic assumptions. Based on the new economic assumptions, the Plan actuary revised the normal cost percentages. The table below reflects the assumptions and normal costs for 1997 and 1996.

	1997	1996
Assumptions:		
Inflation	4%	4.5%
Interest	7%	7%
Salary increase	4.25%	4.5%
Normal Cost:		
FSRDS	28.31%	30.69%
FSPS	21.64%	24.34%

Actuarial assumptions are based on the presumption that the Plan continues. If the Plan terminates, different actuarial assumptions and other factors might be applicable in determining the actuarial present value of accumulated Plan benefits.

Net Position

The Department's Net Position is comprised of the following components.

1. *Unexpended Appropriations* represents unobligated and unexpended budget authority. Unobligated balances are the amount of appropriations or other authority remaining after deducting cumulative obligations from the amount available for obligation. Undelivered orders are the amount of goods or services ordered, but not yet received, from the public or other Federal entities.

2. *Invested Capital* represents U.S. Government resources invested in the Department's property and equipment. The account balance includes: (1) the acquisition cost of Capitalized Property and Equipment financed by appropriations or acquired through donation or exchange, and (2) the investment in a revolving fund to commence operations or begin a new activity. Increases to invested capital are recorded when assets are acquired, and decreases are recorded as a result of the depreciation or the disposition of capital assets.

3. *Cumulative Results of Operations* represents the net difference between expenses and revenues and financing sources since inception.

4. *Donated Capital* represents the value (as determined by the estimation technique described earlier in this Note) of overseas real property that was obtained by the Department as a gift.

5. *Future Funding Requirements* represents the liabilities reported in the Statement of Financial Position that are not covered by available budgetary resources. These include, among other things, liability for assessments from international organizations, unfunded actuarial liability for FSRDF, liability for accrued annual leave, and actuarial liability for future workers' compensation benefits.

Foreign Currency

Accounting records for the Department are maintained in U.S. dollars. Although many of the Department's overseas expenditures are made in foreign currencies, the obligations and disbursements are recorded in U.S. dollars based on the rate of exchange as of the date of the transaction. The foreign currency payments are made by the USDO's located at the Department's Financial Service Centers. The USDO's purchase foreign currencies using Treasury funds, which are maintained in more than 240 bank accounts worldwide until disbursed. Gains and losses in the foreign currency accounts are reflected in Treasury's accounts.

Comparative Data

Comparative data for 1996 are presented for both the Statement of Financial Position and the Statement of Operations and Net Position. The 1996 Statement of Financial Position has been restated to include the Bosnia Federation Trust Fund discussed in Note 1 - **Reporting Entity and Basis of Consolidation**. The Department received a qualified opinion on its 1996 Statement of Financial Position relative to the $1.4 billion reported in undelivered orders under Unexpended Appropriations. The 1996 Statement of Operations and Net Position was not audited and its data are presented as unaudited.

2. FUND BALANCES WITH TREASURY

Fund balances with Treasury are summarized below [dollars in thousands].

		Unobligated Balances		
Balance as of September 30,1997	Obligated Balances, Net	Available for Obligation	Unavailable for Obllgation	Total Fund Balances with Treasury
Administration of Foreign Affairs	$1,181,225	$275,373	$110,866	$1,567,464
Foreign Service Retirement and Disability Fund	110	-	-	110
Intemational Commissions	13,005	12,204	1,710	26,919
Intemational Organizations and Conferences	172,595	2,427	4,703	179,725
Foreign Assistance	508,559	69,130	13,721	591,410
Other Funds	59,692	9,957	-	69,649
			Total Funds	$2,435,277

As of September 30,1997, $38.7 million in Fund Balances with Treasury, excluded from the above, was no longer available for expenditure and was returned to Treasury in accordance with cancellation of the appropriations as outlined in 31 U.S.C. 1552 (Closing Accounts).

3. CASH AND OTHER MONETARY ASSETS

Cash and other monetary assets are summarized below [dollars in thousands].

Balance as of September 30, 1997	Entity Assets	Nonentity Assets
Cash - Imprest Funds	$173	$ -
Bosnia Federation Defense Fund		99,845
International Chancery Center Fees Held in Trust	-	10,463
Totals	$173	$110,308

Lease fees collected for the International Chancery Center are deposited into an escrow account. The funds are unavailable to the Department at time of deposit and do not constitute proceeds until certifications are made that funds are necessary for additional work performed on the project. Until such certifications are made, the Department is precluded from asserting any right, title, or interest in or to such deposits. For 1997, Center funds were held in the form of cash ($1,709) or investments ($10,461,217). The Chancery Development Trust account invests in one-year, marketable Treasury bills issued at discount and redeemable for par at maturity. As of September 30, 1997, the investments had a par value of $10,870,000 and an unamortized discount of $408,783. A corresponding liability for these amounts is reflected as a Governmental Liability - Fees Held in Trust.

The Bosnia Federation Defense Fund is a depository account containing funds donated by various governments to assist the Federation of Bosnia and Herzegovina in establishing a military balance to promote lasting peace in the region. Funds not required for immediate disbursement needs are invested in short-term, marketable Treasury bills issued at discount and redeemable for par at maturity. As of September 30, 1997, there was a cash balance of $19,548,280, and the investments had a par value of $80,315,000 and an unamortized discount of $17,714. A corresponding liability for these amounts is reflected as a Governmental Liability - Fees Held in Trust.

4. INVESTMENTS

The Department has two activities that have the authority to invest funds. A description of the investments made and a list of the outstanding investments are described below. Although funds in the Chancery Development Trust Fund and the Bosnia Federation Fund are invested, because they are considered nonentity assets, investments for these funds are not included in the table below, but are described in Note 3.

Foreign Service Retirement and Disability Fund

All receipts are invested in special issues of U.S. Government nonmarketable securities redeemable, on demand, at par. Maturity dates on these securities range from 1998 through 2012.

Gift Funds

The Gift Funds invest in U.S. Government nonmarketable, market-based securities, issued at either a premium or a discount and redeemable for par at maturity. As of September 30, 1997, investments with a par value of $11,320,000 had an unamortized discount of $260,079. The discounts on these investments are amortized over the life of the security using the effective interest method [dollars in thousands].

Balance as of September 30,1997

Type of Security	Interest Range	FSRDF	Gift Funds	Total
Certificates	6.250 - 6.875%	$ 57,272	$ -	$ 57,272
Bonds	6.25 -1 3.75%	8,920,962		8,920,962
Notes	3.78- 5.64%	-	11,320 *	11,320*
Totals		$8,978,234	$11,320 *	$8,989,554*

* This amount excludes an unamortized discount of $260.

5. LOANS, NON-FEDERAL BORROWERS

Repatriation Direct Loan Program

Repatriation loan obligations made prior to 1992, and the resulting direct loans, are reported net of an allowance for estimated uncollectible loans or estimated losses. Loss allowances are estimates of amounts the Department does not expect to recover on its loans receivable obligated prior to 1992. These allowances are based upon historical experience.

Repatriation loan obligations made after 1991, and the resulting direct loan, are governed by the Federal Credit Reform Act. The Act provides that the present value of the subsidy costs (i.e., interest rate differentials, interest subsidies, estimated delinquencies, defaults, fee offsets, and other cash flows) associated with the loans be recognized as a cost in the year the loan is disbursed.

An analysis of loans receivable as of September 30, 1997, and the nature and amounts of the subsidy and administrative costs associated with the loans is provided below.

Repatriation Loans Obligated Prior to 1992

Loans and Interest Receivable, Gross	Allowance for Est. Uncoll. Loans and Interest	Loans and Interest Receivable, Net
$1,191,983	$1,180,817	$11,166

Repatriation Loans Obligated after 1991

Loans and Interest Receivable, Gross	Allowance for Subsidy Cost (Present Value)	Net Present Value of Direct Loans
$1,448,445	$877,996	$570,449

Subsidy and Administrative Expenses

In 1997 total subsidy expense for the Repatriation Loan Program was $656,000, and total administrative expense was $663,000.

6. INVENTORY

Inventory is summarized below [dollars in thousands].

Working Capital Fund:		
Multi-Media Services	$	160
Supply Services Center and Stock Account		725
International Boundary and Water Commission		180
Other		2
Total Inventory as of September 30, 1997	$	1,067

7. PROPERTY AND EQUIPMENT, NET

Property and equipment balances as of September 30, 1997 are shown in the following table. The overseas real property amounts are based on a combination of estimated value and historical cost as explained in Note 1 [dollars in thousands].

Balance as of September 30,1997	Cost	Accumulated Depreciation	Net Value
Real Property:			
Overseas -			
Land	$1,852,529	$ -	$1,852,529
Buildings and Structures	3,057,096	1,411,407	1,645,689
Construction-in-Progress	176,549		176,549
Assets under Capital Lease	128,545	46,862	81,683
Leasehold Improvements	3,005	317	2,688
Domestic -			
Structures, Facilities and Leaseholds	363,498	103,951	259,547
Land Improvements	9,378	2,273	7,105
Land	69,708	-	69,708
Construction in Progress	156,590	-	156,590
Subtotal - Real Property	$5,816,898	$1,564,810	$4,252,088
Personal Property:			
Communication Equipment	$88,789	$43,711	$45,078
Vehicles	98,753	65,752	33,001
ADP Equipment	48,431	30,662	17,769
Reproduction Equipment	9,061	5,449	3,612
Other Equipment	83,886	35,902	47,984
Subtotal - Personal Property	$328,920	$181,476	$147,444
Total	$6,145,818	$1,746,286	$4,399,532

8. LEASES

The Department was committed to more than 9,000 leases covering office and functional properties and residential units at diplomatic missions overseas. Most of these leases are short-term, operating leases. In most cases, management expects that they will be renewed or replaced by other leases.

Some leased buildings (both residential and nonresidential) are occupied by personnel from other Federal foreign affairs agencies. These agencies reimburse the Department for use of the properties. Such reimbursements are received for more than 25% of the lease costs.

Capital Leases

The Department has various long-term leases (more than 10 years) for overseas real property that meet the criteria as a capital lease for accounting purposes. Following is a schedule of capital leases and future minimum lease payments [dollars in thousands].

Summary of Assets Under Capital Leases

Land and Buildings	$128,545
Accumulated Depreciation	46,862
Net	$ 81,683

Future Minimum Lease Payments

Fiscal Year	Lease Payments
1998	$ 9,886
1999	9,631
2000	9,169
2001	9,002
2002	7,172
2003 and thereafter	164,697
Total Minimum Lease Payments	$209,557
Less: Amount Representing Interest	127,874
Obligations under Capital Leases	$81,683

Operating Leases

The following chart reflects the estimated operating lease obligations for the next 5 fiscal years for overseas real property based on total estimated lease costs. Operating lease costs are recognized as expenses when paid [dollars in thousands].

Fiscal Year	Estimated Operating Lease Payments
1998	$154,231
1999	157,094
2000	162,558
2001	167,876
2002	175,013

9. PENSION ACTUARIAL LIABILITY

The FSRDF finances the operations of the FSRDS and the FSPS. FSRDS and FSPS are defined-benefit, single-employer plans. FSRDS was originally established in 1924. FSPS was established in 1986. FSRDS and FSPS are excluded from major provisions of Public Law 93-406, the Employee Retirement Income Security Act of 1974 (ERISA) relating to reporting, disclosure, fiduciary, and vesting standards. However, the status of FSRDS and FSPS is reported annually under provisions of Public Law 95-595 which requires Federal pension plans to report under ERISA standards in such form as prescribed by the President, in consultation with the Comptroller General. The actuarial present value of projected plan benefits shown is consistent with amounts reported in the Public Law 95-595 report.

FSRDS is a single-benefit retirement plan. Retirees receive a monthly annuity from FSRDS for the rest of their lives. FSPS provides benefits from three sources: a basic benefit (annuity) from FSPS, Social Security, and TSP.
The following table presents the Pension Actuarial Liability and the assumptions used in computing it for 1997 and 1996 [dollars in millions].

	1997	1996
Amount of Pension Actuarial Liability before change in Accounting Principles	-	$ 9,225.3
Cumulative Effect of Accounting Change (Note 16)	-	1,040.4
Amount of Pension Actuarial Liability	$10,488.2	$10,265.7
Actuarial Assumptions:		
Rate of Return on Investments	7%	7%
Inflation Rate	4%	4.5%
Pay Increases	4.25%	4.5%

The table below presents the calculation of the Pension Actuarial Liability for 1997 [dollars in millions].

Pension Actuarial Liability as of September 30, 1996		$10,265.7
Add Pension Expense:		
Normal Cost	$183.7	
Interest on Pension Liability	707.5	
Actuarial Gains (Losses)	(168.6)	
Total Pension Expense		722.6
Less: Payments to Retirees		(500.1)
Pension Actuarial Liability, 9/30/97		$10,488.2
Less: Plan Net Assets Available		(9,115.3)
Unfunded Pension Actuarial Liability as of September 30, 1997		$ 1,372.9

10. OTHER GOVERNMENTAL LIABILITIES

Other Governmental Liabilities primarily includes unearned revenue from sales of real property. It also includes other items such as advances for work from other entities, funds awaiting distribution on the basis of a legal or other determination, and funds received for which the Department is acting as a fiscal agent or custodian. Real property sales are considered unearned because the proceeds are paid in installments (current versus noncurrent amounts) and title and possession of the property have not passed from the Department to the buyer [dollars in thousands].

	Current	Noncurrent	Total
Unearned Revenue from Sale of Real Property	$114,187	$75,000	$189,187
Other	80,466	-	80,466
	$194,653	$75,000	$269,653

11. ASSESSMENTS FROM INTERNATIONAL ORGANIZATIONS

The Department has recognized as a liability the amount of accumulated arrears assessed by the United Nations, its affiliated agencies, and other international organizations in the amount of $1,020.8 million for regular budget assessments and international peacekeeping. In 1998, $100 million has been appropriated to pay a portion of the arrears, subject to enactment of applicable authorizing legislation. The Administration has proposed to Congress a supplemental request to make advance appropriations totaling $921 million for 1999 and 2000 to pay the remainder of the arrears. The financial statements also report a liability for the current annual assessments from the United Nations and several other international organizations of $679.6 million. It has been the Departmentís policy to pay the annual assessments for these organizations out of the following fiscal year's appropriation (i.e., the 1997 calendar year assessment is paid from the 1998 appropriation).

12. SUMMARY NET POSITION

Details of the Department's Net Position are summarized below [dollars in thousands].

Balances as of September 30,1997	Administration of Foreign Affairs	FSRDF	International Commissions	International Organizations	Foreign Assistance	Other	Total
Unexpended Appropriations:							
Unobligated:							
Available	$275,373	$ -	$12,204	$2,427	$69,130	$9,957	$369,091
Unavailable	110,866	-	1,710	4,703	13,721		131,000
Undelivered Orders	946,138	-	13,104	127,988	481,512	23,682	1,592,424
Total Unexpended Appropriations	$1,332,377	$ -	$27,018	$135,118	$564,363	$33,639	$2,092,515
Invested Capital	3,392,499	-	327,611	-	26	12,762	3,732,898
Donated Capital	537,339	-	-	-	-	-	537,339
Cumulative Results of Operations	450,690	-	828	-	-	5,866	457,384
Future Funding Requirements	(120,746)	(1,372,916)	(1,269)	(1,700,487)	(1,787)	-	($3,197,205)
Total Net Position	$5,592,159	($1,372,916)	$354,188	($1,565,369)	$562,602	$52,267	$3,622,931

13. OTHER REVENUES AND FINANCING SOURCES

Other Revenues and Financing sources are summarized below [dollars in thousands].

For the Year Ended September 30	1997 Audited	1996 Unaudited
Proceeds of Sale - Foreign Buildings Operations	$ 102,393	$ 21,050
Program Benefit Revenue - FSRDF	97,298	99,720
Imputed Financing - Post Retirement Benefit (Note 16)	42,858	-
Contributions to Gift Funds	1,384	1,007
Other	16,934	22,256
Total Other Revenues	$ 260,867	$ 144,033

14. PROGRAM OR OPERATING EXPENSES

The components of Program and Opertaing Expenses are summarized below [dollars in thousands].

For the Year Ended September 30	1997 Audited	1996 Unaudited
Object of Expenditure:		
Grants, Subsidies and Contributions	$2,095,965	$2,038,894
Personnel Compensation	1,433,536	1,436,609
Contractual Services	728,060	699,893
Insurance Claims and Indemnities	498,267	462,900
Rent, Communications and Utilities	407,355	412,500
Travel and Transportation	242,781	231,363
Supplies and Materials	114,225	96,714
Equipment Not Capitalized	200,686	91,975
Printing and Reproduction	24,194	42,919
Refunds	8,435	9,399
Other	748	9,383
Total	$5,754,252	$5,532,549

15. ADJUSTMENTS TO BEGINNING NET POSITION

Several adjustments made to beginning Net Position in 1997 related to prior fiscal years. The principal adjustment was a decrease of $279.5 million to reflect changes to the valuation recorded for overseas real property in 1996. In addition, a $38 million increase in beginning Net Position was made to reverse an adjustment to Appropriated Capital Used and Operating Expenses reported in the 1996 financial statements.

16. CUMULATIVE EFFECT OF ACCOUNTING CHANGE

In December 1995, the FASAB issued SFFAS No. 5, *Accounting for Liabilities of the Federal Government*. SFFAS No. 5 establishes accounting standards to recognize and measure liabilities resulting from contingencies, capital leases, pensions and other retirement benefits, and is effective for 1997 financial reporting. Except as noted below, the Department's implementation of SFFAS 5 had no material effect on the financial position or results of operations of Department operations.

As FSRDF administrator, the Department reports assets of FSRDS and FSPS, accumulated plan benefits and any unfunded liability (see Note 9). SFFAS No. 5 requires Federal pension plans to report the Pension Actuarial Liability as the actuarial present value of all future benefits, based on projected salaries and total projected service, less the actuarial present value of future normal cost contributions that would be made for and by employees under the Plan. Prior to 1997, the Department reported the FSRDF's actuarial liability on an accumulated benefit basis, as specified by FASB No. 35. The Pension Actuarial Liability computed and reported under SFFAS No. 5 uses the same inflation and return on investments assumptions, but, unlike the accumulated benefit basis under FASB No. 35, considers future service and salary changes, including an estimate of future changes attributable to seniority, promotions and COLA's. The cumulative effect of adopting SFFAS No. 5 as of October 1, 1996, is a reduction of Net Position of $1.04 billion. 1996 consolidated financial statements have not been restated and the reduction in net position is reflected in the line titled "Cumulative Effect of Accounting Change" on the 1997 Statement of Operations and Change in Net Position.

Prior to SFFAS No. 5, Federal agencies recognized as costs in their financial statements only the contributions they made to the various Federal pension plans, such as Civil Service Retirement and Disability Fund (CSRDF) and the FSRDF, as well as for other post-retirement benefits administered by the OPM. SFFAS No. 5 requires Federal agencies to recognize the full cost for these items for the reporting period. Unlike FSRDF, the Department does not report CSRDF assets, accumulated plan benefits, or unfunded liabilities applicable to its employees. This information is reported by OPM. Accordingly, under SFFAS No. 5, the Department is required, in 1997, to recognize an expense and imputed financing source for the unfunded portion of CSRDF pensions, post-retirement health benefits and life insurance for Department employees that were funded by OPM during the fiscal year. The Department's 1997 Operating Expenses and Other Revenues and Financing Sources on the Consolidated Statement of Operations and Changes in Net Position include $42.9 million for these post-retirement benefits. These imputed costs are not actually owed or paid to OPM and, thus, are not reported on the 1997 Statement of Financial Position as a liability.

17. NONOPERATING CHANGES

Nonoperating changes consist of changes in Net Position that are not reported on the Statement of Operations. These changes primarily consist of changes in the balances of Unexpended Appropriations for S&E, D&CP, and A/FBO as well as changes in Invested Capital.

Changes in Invested Capital reflect the adjustment made to the property account for the value of overseas real property discussed in Note 1. The 1996 Invested Capital was adjusted to record the change in capitalization threshold for personal property from $5,000 to $25,000.

18. COMMITMENTS AND CONTINGENCIES

Commitments

In addition to the future lease commitments discussed in Note 8, the Department is committed under obligations for goods and services which have been ordered but not yet received (undelivered orders) at fiscal year-end. Undelivered orders for all activities was approximately $1.6 billion as of September 30, 1997.

Contingencies

The Department is a party in various administrative proceedings, legal actions, environmental suits, and claims brought by and against it. Some of these actions are not related directly to Department programs, but the Department is involved because of its status as the foreign policy agency. In the Department's opinion, the ultimate resolution of these proceedings, actions, and claims should not materially affect the financial position or results of Department operations.

Certain legal matters to which the Department is a party are administered and, in some instances litigated and paid by other Federal agencies. Generally, amounts to be paid under any decision, settlement, or award pertaining to such litigation are funded from a special appropriation called the Judgment Fund maintained by Treasury. None of the amounts paid from the Judgment Fund had a material effect on the financial position or results of Department operations.

19. SUBSEQUENT EVENTS

On August 6, 1998, the embassies in Nairobi, Kenya, and Dar Es Salaam, Tanzania, were subjected to terrorist bombings. Substantial loss of life and property and personal injuries occurred in both incidents. On September 22, 1998, a request for an emergency supplemental appropriation of $1.398 billion for the Department was submitted to Congress for reconstitution of embassy activities and facilities in those countries, and security improvements to U.S. facilities worldwide. The supplemental appropriation request is still under consideration. The Department expects to make funding requests for subsequent fiscal years for additional security improvements.