A MESSAGE FROM THE SECRETARY OF THE TREASURY

Attached is the fiscal year 1998 Financial Report of the United States Government, formerly known as the Consolidated Financial Statements of the U.S. Government. The Administration initiated the development of this financial report in order to create what we believe will be a useful management tool for policy-makers and a source of useful information for the public. Last year, for the first time, the United States Government prepared comprehensive financial statements covering all of its myriad activities and subjected them to audit. This year, for the second time, the Administration presents the Financial Report of the United States Government, including audited financial statements that cover the Executive Branch, as well as parts of the Legislative and Judicial branches of the United States Government.

The publication of this second annual financial report represents one component of the Clinton Administration's continuing efforts to improve the management and efficiency of the United States Government. In 1994, the Administration supported the Government Management Reform Act, which mandated the issuance of these audited financial statements. The Administration has supported the Federal Accounting Standards Advisory Board in creating the accounting standards that form the basis for the financial statements included in this financial report.

These accounting standards generally are based on the accrual basis of accounting, which differs from the cash basis of accounting used in the reporting of budget results. The principal differences between these two accounting methods pertain to the timing of the measurement and recognition of revenues and expenses and the inclusion of a presentation of assets and liabilities. Each method is a useful tool for looking at the government's operations for different purposes.

A great deal of work has been done, but the development of this new method of reporting is an immense task and a great deal of additional effort will be necessary to create and implement an entirely new system of reporting on the operations of the U.S. Government. We are working hard toward that goal to complement our existing budget reporting. The audit report from the General Accounting Office (GAO) discusses many areas in which the reliability of the current financial statements must be enhanced and improved. As a result, the GAO was unable to render an opinion on these statements. The Administration is committed to continuing its work with the GAO, Federal agencies, and other interested parties to achieve the President's goal of receiving an unqualified opinion from the GAO on the Financial Report of the United States Government. We believe that the publication of this financial report is an important step in providing the American public with useful information about their government's assets, liabilities and operations.

Robert E. Rubin

Robert E. Rubin

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Financial Report of the United States Government, Fiscal 1998

Management's Discussion and Analysis

Introduction

No other entity in the world compares in size and scope to the U.S. Government, which has continuing responsibilities for the general welfare of its citizens and for national defense. The U.S. Government's comprehensive financial report, prepared in accordance with Federal accounting standards, includes all of its activities.

Effective management of the U.S. Government has been hampered by a lack of comprehensive financial information. The Administration remains committed to providing reliable information about the financial position of the U.S. Government, the cost of its operations, and the financing sources used to fund operations. Such information will ultimately prove extremely helpful to policy-makers and the public.

To improve the quality of financial information, in 1990 the Office of Management and Budget (OMB), Treasury, and the U.S. General Accounting Office (GAO) established the Federal Accounting Standards Advisory Board (FASAB) to develop accounting standards for the U.S. Government. In 1994, the President signed the Government Management Reform Act, which requires annual financial statements for the 24 major agencies and for the U.S. Government as a whole.

The Administration appreciates the work of the GAO in subjecting these financial statements to audit and looks forward to working with the GAO, Federal agencies and other interested parties in its continuing effort to improve the reliability of Federal financial information. The effort to produce a comprehensive and reliable set of financial statements for the U.S. Government, which began in 1997, is ongoing and improvements are clearly necessary. Because of current limitations that are discussed in GAO's Report, the GAO is unable to render an opinion on these financial statements. The challenges involved in developing timely, reliable, and comprehensive financial information should not, however, obscure the progress that has been made or the insights provided by preparation and audit of these statements. The Administration's accomplishments are presented later in this discussion and analysis.

"The Administration is committed to improving the reliability of the financial information . . ."

The Administration is committed to improving the reliability of the financial information to achieve its goal of an unqualified opinion on the financial statements of individual agencies and the U.S. Government. The Administration's goals for individual agencies are reflected in the Federal Financial Management Status Report and Five-Year Plan issued by the OMB and the Governmentwide Chief Financial Officers (CFOs) Council. That document reflects the dates by which agencies are expected to achieve the Administration's objectives.

The accompanying Financial Report is required by 31 United States Code 331(e)(1) and consists of Management's Discussion and Analysis (MD&A), a Statement of Operations and Changes in Net Position, a Statement of Net Cost, a Balance Sheet, Stewardship Information, Notes to the Financial Statements, and Supplemental Information. Each section is preceded by a description of the section's contents. The Supplemental Information section describes the major functions of the U.S. Government.

Management's Discussion and Analysis, cont.

Reporting Entity and Basis of Accounting

The MD&A explains the Federal reporting entity, the basis of accounting used to prepare these financial statements, and presents selected financial and economic information intended to assist readers in their assessment of the U.S. Government's financial operations and status. It also summarizes financial management initiatives designed to continue improving the reliability of the financial statements and to address the issues identified in GAO's report on the U.S. Government's 1998 financial statements.

Coverage

The financial statements cover the executive branch, as well as parts of the legislative and judicial branches of the U.S. Government. A list of the significant entities included in these financial statements is included in the Appendix. Information from the legislative and judicial branches is limited because those entities are not required to prepare comprehensive financial statements. In addition, Government-sponsored enterprises (such as Federal Home Loan Banks and the Federal National Mortgage Association) are excluded because they are privately owned. The Federal Reserve System is also excluded because monetary policy is conducted separately from and independently of the other central Government functions.

Accounting Standards

The accounting standards used in the preparation of the accompanying financial statements were developed by the Federal Accounting Standards Advisory Board (FASAB); approved by Treasury, OMB and GAO as the FASAB principals; and issued by OMB and GAO. The standards are tailored to the U.S. Government's unique characteristics and special needs. For example, land not used in U.S. Government operations (stewardship land) and weapon systems and support property used in the performance of military missions and vessels held as part of the National Defense Reserve Fleet (national defense assets) are reported in the Stewardship Information section rather than on the Balance Sheet.

The financial statements of the U.S. Government are prepared generally on the accrual basis of accounting. Under the accrual basis, transactions are reported when the events giving rise to the transactions occur, rather than when cash is received or paid (cash basis). By contrast, Federal budgetary reporting is generally on the cash basis in accordance with accepted budget concepts and policies.

The most significant difference between these two bases involves the timing of recognition and measurement of revenues and costs. For example, Federal accounting standards require recognition of liabilities for costs related to environmental cleanup when the events resulting in such costs occur. By contrast, budget concepts and policies require the recognition of such costs at the time payment is made. The effects of these differences are reflected in the "Reconciliation of the Excess of Net Cost Over Revenue to the Unified Budget Surplus," which is presented in the Supplemental Information section of this Financial Report.

In fiscal 1998, there was a budget surplus of $69.2 billion. The excess of net cost over revenue figure contained in these financial statements for fiscal 1998 is $133.8 billion. This difference is attributable to factors discussed immediately above. The primary components of the difference that have been identified are increases in accrued veteran compensation benefits, $109.4 billion; increases in actuarial expenses for Federal employees and military pensions and health benefits, $39.8 billion; and an increase in environmental liabilities, $12.8 billion.

This Financial Report does not include information on natural resources (depletable resources, such as mineral deposits and petroleum or renewable resources, such as timber) because standards have not yet been developed for recognizing and measuring these assets.

Finally, a thorough assessment of the U.S. Government's financial status should recognize its sovereign powers to raise revenue and regulate commerce. These powers are not reflected in the accompanying statements, but should be considered in a comprehensive assessment of the U.S. Government's overall financial condition.

Implementation of New Accounting Standards

While the FASAB completed work on a basic set of accounting standards in 1996, some standards did not become effective until fiscal 1998. Standards becoming effective in fiscal 1998 require that the value of national defense assets be removed from the Balance Sheet and that information about these assets be reported in the Stewardship Information section of the Financial Report. These assets were valued at $655.2 billion when reported on the fiscal 1997 Balance Sheet. FASAB has initiated a project to identify and research user information needs for national defense assets.

In addition, standards effective for the first time in 1998 require current services assessment information showing both the short-term and medium-term direction of current programs. The current services assessment presents actual receipt and outlay data for all programs for the year for which the financial statements are prepared (the base year) and estimates for 6 years subsequent to the base year. This assessment will thus facilitate evaluation of the sufficiency of future resources to sustain public services and to meet current and future obligations as they become due.

Standards becoming effective in future years require reporting of annual Federal expenses for stewardship investments, which include:

- Non-Federal physical property: the Federal investment in properties owned by State and local governments (e.g., highways and airports).
- Human capital: investments in education and training programs financed by the U.S. Government for the benefit of the public.
- Research and development: the U.S. Government's investments in basic and applied research and development.

The annual expense related to these investments included in the Statement of Net Cost will be separately

Economic and Budgetary Results

Very strong economic growth continued through fiscal 1998. The Asian financial crisis and weakness abroad had some negative impacts on the U.S. economy, chiefly through exports and volatility in financial markets, but the domestic economy surged forward. Job gains were very solid over the year ending in September and the unemployment rate held near 28-year lows. At the same time, inflation was very well contained, with the rate of inflation dropping to levels not seen since the mid-1960's. Strong growth in incomes and a rising stock market led to a boost in Federal tax receipts in fiscal 1998, contributing to the first Federal unified budget surplus in 29 years.

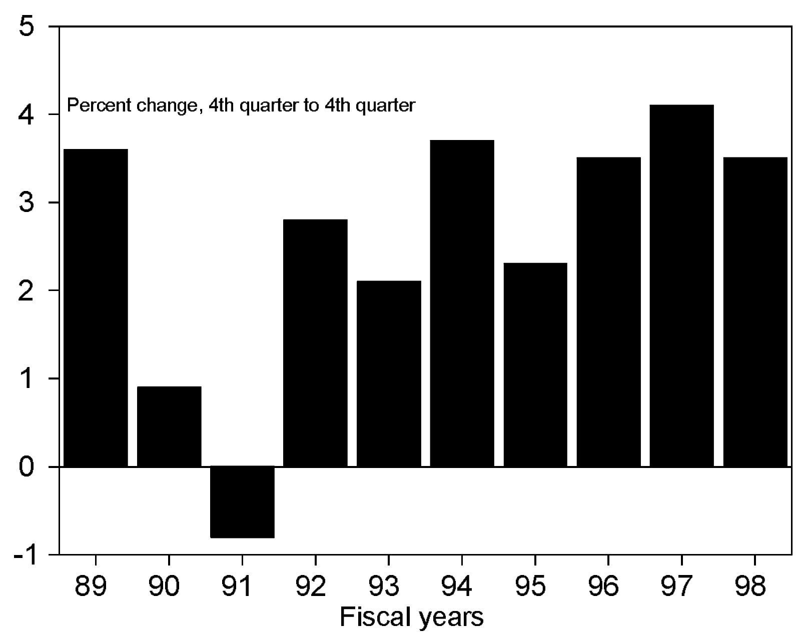
The Economy in Fiscal 1998

Real gross domestic product (GDP) grew by 3.5 percent across the four quarters of fiscal 1998 (which encompasses the fourth quarter of calendar 1997 through the third quarter of calendar 1998). Over the past 3 fiscal years, real growth averaged a robust 3.7 percent.

The household sector accounted for much of the gain in 1998, with consumer spending and residential investment growing very rapidly. Consumer purchases swelled by 4.7 percent over the fiscal year, the most rapid rate of advance in 15 years. Investment in new housing jumped by 12 percent and the home ownership rate hit an all-time high. The gains in spending were fueled by rising employment and income and by the wealth effects of the rapid increases in stock prices over the past few years.

Partly offsetting strength in the domestic economy was a sizable deteri-

Growth of Real GDP



oration in the foreign trade balance due to weakening global financial and economic conditions. U.S. exports in real terms fell by 2.3 percent over the fiscal year, while imports grew by 8.3 percent. The widening trade deficit acted as a considerable drag on real GDP growth, particularly in the first half of calendar 1998 when it subtracted more than 2 percentage points from growth. U.S. agricultural and manufacturing industries were most affected by the loss of exports and other consequences of the global situation. Manufacturing production and capacity utilization slowed over the year, and factory employment declined by 137,000 from March through September.

Employment growth in other sectors of the economy was very strong in fiscal 1998, and labor markets continued to be very tight. About 3.1 million jobs were added during the year, the same as in the previous fiscal year. The unemployment rate held between 4.3 and 4.7 percent throughout the fiscal year, the lowest readings in 28 years. The share of the working-age population with a job averaged 64 percent, a new fiscal-year record, and long-term unemployment fell. Workers enjoyed an acceleration in wage and salary growth, which increased by 4 percent over the fiscal year. This was considerably faster than the rate of inflation and resulted in solid gains in real wages and salaries.

Despite strong economic growth and very low rates of unemployment, price pressures did not build up during the year. Falling prices for imported goods, energy and food held down growth in commodity prices and the overall rate of inflation as well. Consumer prices edged up just 1.4 percent over the fiscal year, the smallest inflation rate since the mid-1960's. Excluding the food and energy components, the underlying "core" rate of consumer price inflation was 2.4 percent, up a bit from 2.2 percent in the previous fiscal year, which had been the lowest core rate since the mid-1960's.

Budget Results

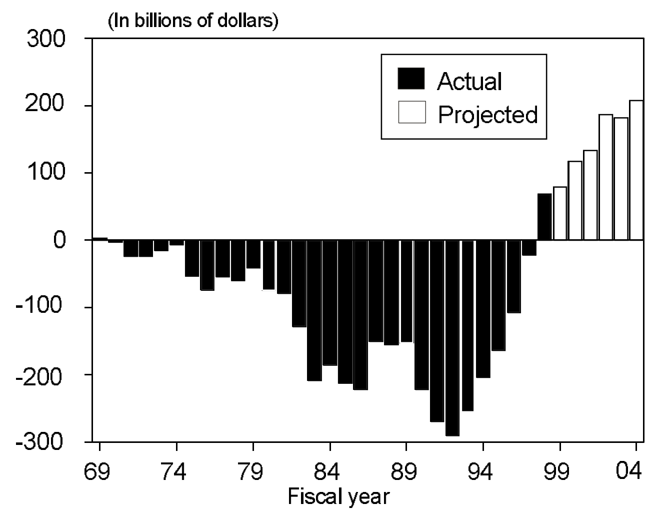
The unified Federal budget was in surplus by $69.2 billion in fiscal 1998, the first Federal surplus since 1969. This represented 0.8 percent of GDP, the highest share of GDP for a surplus in more than 40 years, and resulted in a reduction in the level of Federal debt held by the public for the first time in 29 years. Passage of deficit reduction programs in conjunction with strong economic growth placed the budget on its path toward surplus after the annual deficit reached an all-time high of $290 billion in fiscal 1992.

"The expanding economy over the course of the year brought a surge in tax revenue in 1998, which far outpaced modest gains in Federal outlays."

The expanding economy over the course of the year brought a surge in tax revenue in 1998, which far outpaced modest gains in Federal outlays. Receipts increased by 9.0 percent in fiscal 1998 to $1,722 billion, faster than gains over the previous several years. Growth was led by a more than 12 percent increase in individual income tax payments, reflecting rapid job and income growth as well as high levels of capital gains from the rising stock market. That was more than enough to offset a slowdown in corporate profits tax receipts, which grew by 3-1/2 percent in fiscal 1998 compared with 6 percent in the prior year. Corporate profits weakened a bit over the year primarily due to the impacts of the global situation on earnings, particularly among manufacturing firms.

Growth of outlays was held to just 3.2 percent in fiscal 1998, with outlays rising to $1,653 billion. Outlays in relation to GDP were the smallest since 1974, dipping to a 19.7 percent share from 20.0 percent in fiscal 1997. The underlying improvement over the year was even greater than the

Unified Federal Budget Moves from Deficit to Surplus



Budget, cont.

summary figure suggests, as outlays in fiscal 1997 were held down by large inflows to the deposit insurance account which were not repeated in fiscal 1998. (These inflows are treated as negative outlays in budget accounting.) Excluding the deposit insurance account and other similar factors, outlays increased by less than 2-1/2 percent in fiscal 1998.

Defense spending dipped slightly in fiscal year 1998 after increasing by $4.8 billion in the prior year. That increase followed 4 years of reductions in defense spending. Outlays for income support (excluding Federal retirement payments) were smaller than a year ago, reflecting the expansion of employment and rising income in 1998. Net interest payments declined by $0.7 billion. Growth in Medicare slowed sharply compared with previous years due in part to slower processing of payments, but expanded use of managed care plans and lower-than-expected payments for inpatient hospital services also contributed.

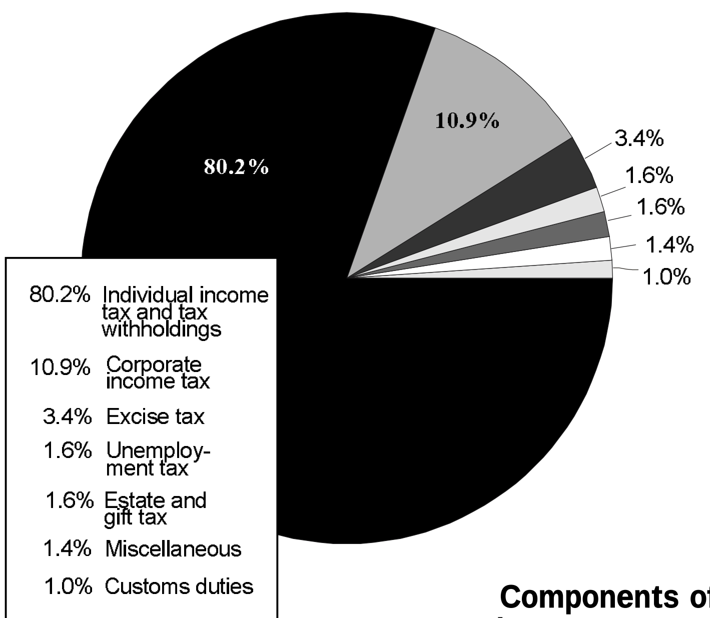
The unified budget in fiscal 1999 is expected to post a slightly larger surplus than the $69.2 billion recorded in fiscal 1998. New projections from the Fiscal Year 2000 Budget show surpluses growing throughout the forecast horizon, accumulating to $2.4 trillion over the period 2000-2009. These results are similar to the forecasts of the Congressional Budget Office, which yield an even larger cumulative surplus of $2.6 trillion over that 10-year span.

Revenue and Expense Summary

Revenue

Non-exchange revenue is the U.S. Government's primary source of revenue, and totaled $1,712.8 billion in 1998. More than 95 percent of this total came from tax receipts, with the remainder coming from customs duties and other miscellaneous receipts.

Earned revenues are inflows of resources that arise from exchange transactions. Exchange transactions occur when each party to the transaction sacrifices value and receives value in return -- for example, when the U.S. Government sells goods or services to the public. During 1998, the U.S. Government earned $168.9 billion in exchange revenue including $2.8 billion from the sale of the Elk Hills Naval Petroleum Reserve by the Department of Energy. Of these revenues, $161.5 billion are offset against the gross cost of the related functions to arrive at the function's net cost. The U.S. Government also earned $7.4 billion that was not offset against the cost of any function, e.g., royalties on the Outer Continental Shelf lands.



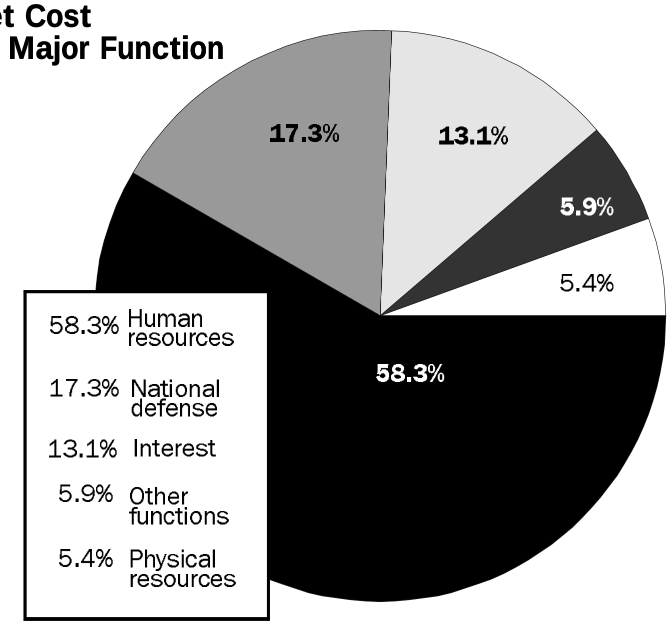
Components of Non-exchange Revenue by Major Source

Detail may not add to totals due to rounding.

Expenses by Function

The net cost of U.S. Government operations was $1,854 billion for 1998. Net cost represents the gross cost of operations less attributable earned revenues. The Statement of Net Cost reflects the cost incurred to carry out the national priorities identified by the President and the Congress and how the net cost was financed. The functions and subfunctions used to accumulate costs associated with the national priorities are identified in the President's budget and described in detail in the Supplemental Information section of this report. The accompanying chart presents the percentage of the net cost of U.S. Government operations represented by each of the U.S. Government's major functions.

Net Cost by Major Function



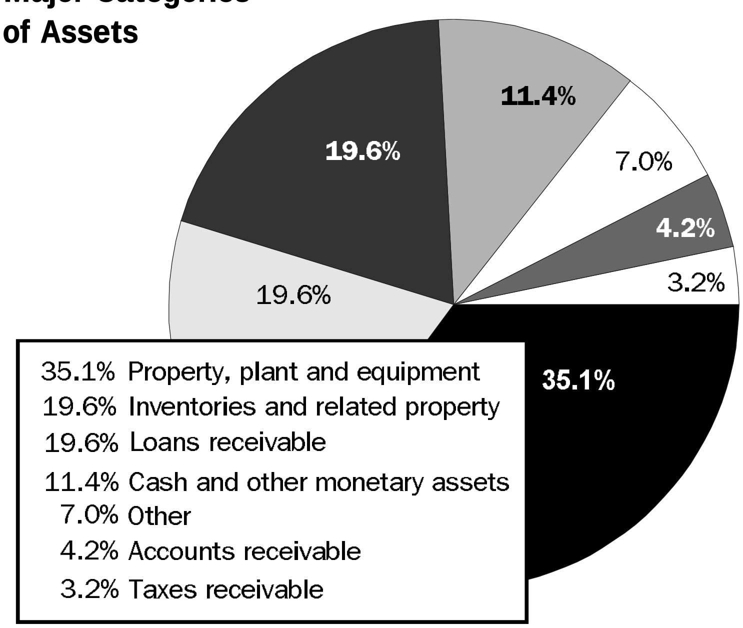
Detail may not add to totals due to rounding.

Asset and Liability Summary

Assets

The assets of the U.S. Government are the resources available to pay liabilities or to satisfy future service needs. The accompanying chart depicts the major categories of reported assets as of September 30, 1998 as a percentage of reported total assets. Detailed information about the components of these asset categories can be found in the notes to the financial statements. The assets presented on the Balance Sheet are not a comprehensive list of Federal resources. For example, the U.S. Government's most important financial resource, its ability to tax and regulate commerce, cannot be quantified and is not reflected. Natural resources, stewardship land (national parks, forests and grazing lands), national defense assets and heritage assets are other examples of resources that are not included in the $852.8 billion of Federal assets reported on the Balance Sheet at the end of fiscal 1998.

Major Categories of Assets



Detail may not add to totals due to rounding.

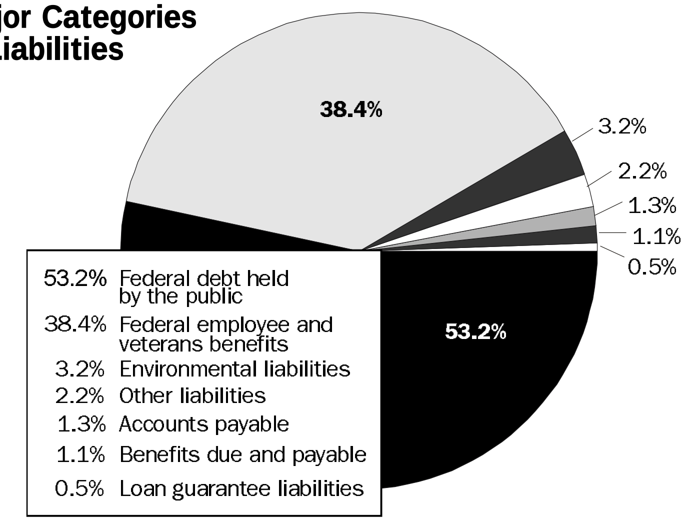
Liabilities

At the end of fiscal 1998, the U.S. Government reported liabilities of $6,987.2 billion. These liabilities are probable and measurable future outflows of resources arising out of past transactions or events. The largest component of these liabilities ($3,717.7 billion) is represented by Federal debt securities held by the public. The next largest component ($2,685.1 billion) relates to pension, disability and health care costs for veterans, and Federal civilian and military employees. Included in this component is a Department of Veterans Affairs program whereby veterans or their dependents receive compensation benefits if the veteran was disabled or died from military service-connected causes. Changes in the actuarial methodology and the interest rate assumption resulted in a liability increase of $381 billion. This liability increase coupled with the removal from the Balance Sheet of $655.2 billion in national defense assets were the major factors in causing the net position of the U.S. Government to decrease by $1.1 trillion in fiscal 1998. The national defense assets were removed from the Balance Sheet as a result of implementing a new accounting standard.

"Another liability, which will likely require substantial future budgetary resources to liquidate, is related to environmental cleanup costs."

Another liability, which will likely require substantial future budgetary resources to liquidate, is related to environmental cleanup costs. As of September 30, 1998, the cost of cleaning up environmental contamination was estimated to be $224.5 billion. The accompanying chart presents the percentage of total Federal liabilities represented by each of the categories of liabilities reported on the Balance Sheet. Additional details about the U.S. Government's reported liabilities can be found in the notes to the financial statements.

Major Categories of Liabilities



Detail may not add to totals due to rounding.

Future Commitments

The U.S. Government has substantial future commitments to its citizens, including the provision of social insurance through the Social Security and Medicare programs. The FASAB continues to discuss the content and format for reporting of these commitments.

Financial Condition of the Social Security Trust Funds

Two trust funds have been established by law to finance the Social Security program (OASDI): Federal Old-Age and Survivors Insurance (OASI) and Federal Disability Insurance (DI). OASI pays retirement and survivors benefits , and DI pays benefits after a worker becomes disabled. OASDI revenues consist primarily of taxes on earnings that are paid by employees, their employers, and the self-employed. OASDI also receives revenue from taxation of part of Social Security benefits. Revenues that are not needed to pay current benefits or administrative expenses are invested in Treasury securities to earn interest for the trust funds. The securities issued to the trust funds are guaranteed as to both principal and interest and backed

"The Administration intends to work with Congress on a bipartisan basis to enact long-term Social Security solvency and reform in 1999."

Social Security, cont.

by the full faith and credit of the U.S. Government.

The Board of Trustees of the OASI and DI Trust Funds provides the President and the Congress with short-range (10 years) and long-range (75 years) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for as long as 75 years into the future, the Social Security Trustees use three alternative sets of economic and demographic assumptions to show a range of possibilities. Most analysts use the Trustees' intermediate or "best estimate" set of assumptions to evaluate the financial condition of the Social Security program.

The 75-year estimates assume that future workers (except for those working in types of employment not mandatorily covered by the program) are covered by Social Security once they enter the labor force. The estimates reflect the impact of the retirement of the baby boomers, as well as changing demographics (e.g., an increase in life expectancy and a decline in the birth rate). For example, in 1960, 5.1 workers paid for every beneficiary. Today, the ratio of workers to beneficiary is 3.4 to 1 and 32 years from now, when all of the baby boom generation has retired, the ratio will drop to approximately 2 to 1. The retirement component of the program is financed largely on a "pay-as-you-go" basis, i.e., current retirement benefits are largely financed by current payroll contributions.

"With no change in the program, in 2013 the trust funds are expected to begin using interest on their investments to cover the cash shortfall and to pay benefits."

Under current legislation and using intermediate assumptions, the Trustees estimated in their 1998 report that by 2013 cash disbursements for the programs will exceed cash receipts and by 2032 the combined trust fund assets, primarily investments in Treasury securities, will be exhausted. With no change in the program, in 2013 the trust funds are expected to begin using interest on their investments to cover the cash shortfall and to pay benefits. Starting in 2021, they would begin redeeming their investments in Treasury securities to provide the needed funding. In 2032 trust fund assets would be exhausted; at that time, dedicated tax revenues would be sufficient to pay approximately 75 percent of the benefits due.

The Administration intends to work with Congress on a bipartisan basis to enact long-term Social Security solvency and reform in 1999. Acting sooner rather than later to address the long-term financing needs of the program will make the required changes less severe and disruptive and ensure that Social Security works as well for future generations as it has for past generations. Additional information about the Social Security program can be found in the Stewardship Information section of this Financial Report.

Financial Condition of the Medicare Trust Funds

Two trust funds have been established to finance the Medicare program. The Medicare Part A Hospital Insurance (HI) Trust Fund is financed by a 2.9 percent tax on wages and salaries required to be paid equally by employees and employers. The Medicare Part B Supplementary Medical Insurance (SMI) Trust Fund receives premium payments on behalf of Medicare beneficiaries who have elected coverage. The Balanced Budget Act of 1997 provides that the SMI premium is set at 25 percent of program costs. The remainder of the costs is funded by Congressional appropriations.

The 1998 trustees' report projects that the HI trust fund's assets will be depleted by 2008 using intermediate or "best estimate" assumptions. Additional information about the Medicare program can be found in the Stewardship Information section of this Financial Report.

Accomplishments and Actions Taken to Address Financial Reporting Issues

The Administration's Priority Management Objectives included in the fiscal 1999 and 2000 Budgets of the U.S. Government include improving financial management information as part of its plan for strengthening Governmentwide management. Audits of agency financial statements disclose that agencies have made substantial progress in correcting financial management deficiencies that impede compliance with Federal accounting standards and, accordingly, improved financial management. The following exhibit illustrates agency progress as measured by the increasing number of unqualified audit opinions on their financial statements. (Audits for all of the 24 major agencies were not required until fiscal 1996.)

While progress has been made, recent audits disclosed that major agencies continue to have serious financial management problems, which preclude compliance with numerous Federal accounting standards. These agencies must satisfactorily address these problems in order to receive an unqualified opinion on their financial statements and for the U.S. Government to receive an unqualified opinion on its financial statements. The exhibit on the following page correlates the most critical problem areas with the agencies responsible for taking corrective action. The exhibit also highlights that the Department of Defense has serious deficiencies in all but one issue area and all agencies have problems with accounting for intragovernmental transactions.

"Audits of agency financial statements disclose that agencies have made substantial progress in correcting financial management deficiencies . . ."

With respect to intragovernmental transactions, the problem pertains to identifying and eliminating transactions between agencies. The audit of the U.S. Government's financial statements for fiscal 1997 disclosed that agencies cannot effectively identify transactions with other agencies so they can be eliminated for governmentwide reporting. If these transactions are not properly eliminated, total U.S. Government assets, liabilities, revenues and expenses will be misstated by the amount of these transactions.

The U.S. Government's ability to correctly identify these items improved in fiscal 1998. In addition, the Administration has organized a task force to address the intragovernmental transactions issue. The task force expects to complete its work in the near future.

In addition to the foregoing obstacles, because the U.S. Government calculates the budget surplus on the basis of cash receipts and disbursements and calculates operating results for financial statement purposes on the accrual basis of accounting, Treasury must, but currently cannot, reconcile these two amounts in order to fully explain to readers why the reported amounts differ.

Number of Agencies with or Anticipating Unqualified Audit Opinions for the Fiscal Years Indicated

(Of 24 agencies covered)

1991	1993	1996	1997	1998*	1999*	2000*
1	1	6	11	13	20	23**

* Anticipated results
** DOD does not anticipate an unqualified opinion on its financial statements before the year 2003.

Obstacles to an Unqualified Opinion of the Financial Statements of the U.S. Government

Entity	Property, Plant and Equipment	Inventory	Loans, Accounts Receivable and Loan Guarantees	Environ-mental Liabilities	Pension, Health and Other Liabilities	Unrecon-ciled Dis-bursements	Intragovern-mental Transac-tions
USDA	X		X				X
DOD	X	X		X	X	X	X
Education			X				X
HHS			X				X
HUD			X				X
Transportation (FAA)	X						X
VA			X				X
OPM							X
All other							X

President's Goal and Direction to Agencies

The President's Budget for fiscal 1999 set as a goal an unqualified opinion on the U.S. Government's financial statements. The President issued a Memorandum to the Heads of Federal Agencies on May 26, 1998, advising them of the Administration's goal and directing them to develop corrective action plans for addressing obstacles to achieving the goal and to submit quarterly progress reports. All named agencies submitted the required plans and progress reports.

Discussion with Agency Officials

A team of senior managers from the OMB, the Treasury, and the GAO met with senior agency officials to discuss agency plans and prospects for successfully meeting planned goals. The conclusion of the team is that, while progress has been made since the March 1998 release of the report on audit of the fiscal 1997 financial statements of the U.S. Government, much remains to be done in the areas presented in the aforementioned exhibit.

Ongoing Monitoring and Assistance Activities

The OMB, the Treasury, and the GAO are monitoring agencies' progress by (1) reviewing quarterly progress reports from all the agencies listed in the aforementioned exhibit on their progress in meeting the goals and milestones set out in the action plans required by the President's May 26, 1998, Memorandum; (2) meeting regularly with officials of those agencies with the most formidable obstacles to their progress in achieving planned goals; and, (3) providing necessary advice and assistance.

Management Initiatives

Manage the Year 2000 (Y2K) Computer Problem

There is no more immediate management challenge facing the U.S. Government and industry worldwide than the impending shift of dates from the year 1999 to the year 2000. The Administration is committed to ensuring that Federal agencies meet the challenges posed by the Year 2000 (Y2K) computer problem. Since November, the U.S. Government has made substantial progress toward fixing the problem. As of February 12, 1999:

- Of the 6,399 mission critical systems, 79 percent are now fully compliant, up from 61 percent in December. These compliant systems include systems that have been repaired or replaced as well as those that were already compliant.
- Of the remaining 1,354 mission critical systems that are not yet compliant, 966 (71 percent) are being repaired, 270 (20 percent) are being replaced, and 118 (9 percent) will be retired.
- Of the 4,130 mission critical systems being repaired, 96 percent have completed renovation, 87 percent have completed validation and 76 percent have completed implementation and are fully compliant.

OMB, in cooperation with the President's Council on Year 2000 Conversion, continues to work closely with individual agencies. Since December, most agencies have made significant progress toward meeting the governmentwide goals, although several agencies remain behind schedule. As of February 12, 1999:

- Five agencies (the Environmental Protection Agency, National Science Foundation, Nuclear Regulatory Commission, Small Business Administration and Social Security Administration) report that their mission critical systems are now 100 percent compliant.
- Three agencies (the U.S. Agency for International Development, Department of Health and Human Services and Department of Transportation) are not making adequate progress and have been rated in Tier I.

Year 2000 Status Mission Critical Systems

	All Systems	Systems Being Repaired			
Agency Status	Y2K Compliant	Assessment Complete	Renovation Complete	Validation Complete	Implementation Complete
Tier III: NASA, FEMA, Education, OMB, HUD, Interior, GSA, VA, SBA, EPA, NSF, NRC, SSA	96%	100%	100%	99%	96%
Tier II: Agriculture, Commerce, Defense, Energy, Justice, Labor, State, Treasury	77%	100%	94%	83%	74%
Tier I: U.S. Agency for International Development, Health and Human Services, Transportation	63%	100%	98%	79%	42%
All agencies	79%	100%	96%	87%	76%

Agencies now estimate that, from Fiscal 1996 through Fiscal 2000, they will spend $6.8 billion fixing the problem, an increase from the February estimate of $6.4 billion. This increase is not unexpected, and OMB and the Congress continue to work closely with the agencies to ensure that they have adequate funding through allocations from the supplemental contingent emergency reserve.

While agencies expect that their mission critical systems will be ready by December 31, they also are developing business continuity and contingency plans (BCCPs) to ensure program delivery in the event of a system failure or malfunction, whether within or outside the agency. Additionally, those agencies that are behind schedule are emphasizing completion of their remaining mission critical systems.

As agencies complete work on fixing their mission critical systems, they are now focusing on demonstrating that programs and services, especially those critical to public safety, health and well-being, will be operational. In addition, new guidance from OMB will direct agencies to work with other Federal agencies, State and local governments, the private sector, and others to assure the readiness of 40 high-impact public programs.

Use Results to Improve Program Management

The Government Performance and Results Act (GPRA) makes U.S. Government agencies more accountable by focusing managers and policy makers on agency performance. GPRA can fundamentally change how the U.S. Government carries out its programs and makes funding decisions. GPRA requires Federal agencies to periodically develop long-range strategic plans and annually prepare performance plans and performance reports. The annual plans set specific performance targets for an agency's programs and activities. The combination of GPRA plans and reports introduces an unprecedented degree of managerial and institutional accountability for accomplishing program goals. Key to achieving success is making the plans useful to Congress, the President, and agency management.

In fiscal 2000, agencies will submit to Congress and the President the first of their annual reports on program performance. These reports, covering fiscal 1999, will compare actual performance to the performance target levels in the annual plans for that year, and provide an explanation for any goal not met. With these reports, the first phase of GPRA implementation will be complete.

During fiscal 2000, agencies will also be revising and updating strategic plans for submission to Congress and OMB by September 2000. All GPRA plans and reports are publicly available, and can often be found on individual agency web sites.

Additional Information

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