Financial Section

MESSAGE FROM THE CHIEF FINANCIAL OFFICER

Accountability to the citizens of the United States, the President, Congress, our employees, as well as our customers and constituents is among the Department of State's highest priorities. The Annual Financial Report (Report) for Fiscal Year 2007 remains a cornerstone of our efforts to annually disclose the Department's successes and shortcomings. It is a comprehensive review of the Department's activities against the backdrop of the global challenges presented by a complex world. In the 2007 Report, as in past years, what remains apparent and should be inspirational to all Americans is the inextricable link between the Department's accomplishments and the unwavering commitment of our employees serving around the world, in turmoil as well as tranquility, dedicated to our mission and the very best interests of our nation.

For the past seven years, the President has challenged us to improve the management of key processes through the President's Management Agenda (PMA). The Department made a major commitment to achieving the goals of the PMA and currently has three "green" and two "yellow" status ratings for the five USG-wide Presidential initiatives and two "green" ratings for two other PMA initiatives. This is a significant accomplishment considering the challenging nature of conducting business in our global, foreign affairs environment. In addition, the Department has achieved the best record of all large agencies in evaluation of programs using the OMB-led Program Assessment Rating Tool evaluation process. The Department has a high number of programs rated Effective or Moderately Effective – the highest ratings – and no programs rated Ineffective or Results Not Demonstrated. In addition, the Department has demonstrated innovation and leadership in performance management by improving performance systems and coordinating strategic planning with other foreign affairs agencies.

Very few agencies or corporations have the level of complexity and variety of challenges that the men and women of the Department face daily. The Department operates in over 260 locations in 188 countries, frequently in hostile environments, while conducting business in 150 currencies and an even larger number of languages. Thousands of financial professionals around the globe plan, budget, allocate, obligate, disburse, and account for billions of dollars in annual resources. Despite our worldwide geographic dispersion, the Department operates as one team distinguished by its dedication to strong ethics and corporate governance.

Our strong commitment to corporate governance is evidenced by the priority we place on improving our internal controls. To that end, we continued to make considerable progress in 2007. One of our most important achievements this fiscal year was the implementation of our new core financial system – Global Financial Management System (GFMS). GFMS replaces our twenty year old legacy system with a state-of-the-art system that operates on the same platform as our overseas regional financial system. GFMS is also fully integrated with our procurement system. The next step will be to combine GFMS with our overseas system so that for the first time the Department will operate on one global integrated financial system. Although we experienced a few of the challenges normally associated with a conversion of such a massive scale, which resulted in a delay in submitting our financial statements to the Independent Auditor, we are confident that the Department now has a system that in addition to complying with regulatory requirements provides the accurate and timely data we need to manage the resources of the Department. We also continued our efforts on areas reported as material weaknesses in recent years and which were downgraded last year to significant deficiencies – IT Security, Accounting for Real Property, and Accounting for Personal Property. As a result of our efforts, the Independent Auditor further downgraded the IT Security and Accounting for Real Property to deficiencies (from a significant deficiency).

In summary, we have taken major steps to improve the Department's financial management in 2007, which we believe will provide significant dividends going forward. However we have had a set back with the material weakness with our handling of Unliquidated Obligations, and while not hampering the operations of the Department, no material weakness is acceptable, and we are committed to resolving this shortfall in the coming year along with the issues identified by the Independent Auditor. We also hope that the Independent Auditor will continue their review so that they will be able to reach a conclusion on the accuracy of our financial statements. We remain strong in our view that it is in the best interests of Congress and the American public to receive complete and accurate reports that they can rely on in contrast to a disclaimer.

Bradford R. Higgins
Assistant Secretary for Resource Management and Chief Financial Officer
November 15, 2007

Independent Auditor's Report

U.S. DEPARTMENT OF STATE

United States Department of State
and the Broadcasting Board of Governors

Inspector General

NOV 15 2007

UNCLASSIFIED

INFORMATION MEMO TO THE SECRETARY

FROM: OIG/AUD – Mark W. Duda

SUBJECT: Independent Auditor's Report on the U.S. Department of State's 2007 and 2006 Financial Statements (Report AUD/FM-08-05)

OIG contracted with the independent certified public accounting firm of Leonard G. Birnbaum and Company, LLP (LGB), to audit the financial statements of the Department of State as of September 30, 2007 and 2006, and for the years then ended. The contract required that the audit be performed in accordance with U.S. generally accepted government auditing standards; Office of Management and Budget (OMB) audit guidance; and the *Financial Audit Manual*, issued by the Government Accountability Office and the President's Council on Integrity and Efficiency.

Because the Department was unable to respond to requests for evidential material in a timely manner and LGB was not able to perform other auditing procedures to satisfy itself as to the accuracy of the 2007 financial statements in time to meet the November 15, 2007, deadline imposed by OMB for issuing the report, the scope of LGB's work was not sufficient to enable it to express, and it does not express, an opinion on the annual financial statements as of, and for the year ended, September 30, 2007.

LGB found:

- certain deficiencies in the Department's internal control that LGB considered to be significant deficiencies and other deficiencies that LGB considered to be material weaknesses,

- instances of noncompliance with selected provisions of applicable laws and regulations involving the Department's financial management system, and

- that the Department's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA).

UNCLASSIFIED

Address correspondence to: U.S. Department of State, Office of Inspector General, Washington, D.C. 20522–0308

UNCLASSIFIED

LGB is responsible for the auditor's report dated November 14, 2007, attached to this memorandum and the conclusions expressed in the report. OIG does not express an opinion on the Department's financial statements or conclusions on internal control and compliance with laws and regulations, including whether the Department's financial management systems complied with FFMIA.

Comments from the Bureau of Resource Management are included in the attached report in Appendix A.

OIG appreciates the cooperation extended to it and LGB by Department managers and staff during the conduct of this audit.

Attachment: As stated.

LEONARD G. BIRNBAUM AND COMPANY, LLP
CERTIFIED PUBLIC ACCOUNTANTS
WASHINGTON OFFICE
6285 FRANCONIA ROAD
ALEXANDRIA, VA 22310-2510

703-922-7622
FAX: 703-922-8256

LESLIE A. LEIPER
LEONARD G. BIRNBAUM
DAVID SAKOFS
CAROL A. SCHNEIDER
DORA M. CLARKE

WASHINGTON, DC
SUMMIT, NEW JERSEY
REDWOOD CITY, CALIFORNIA

INDEPENDENT AUDITOR'S REPORT

To the Secretary, Department of State:

We were engaged to audit the Department of State's (Department) Consolidated Balance Sheet, Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, and Combined Statement of Budgetary Resources (Annual Financial Statements) as of, and for the years ended, September 30, 2007 and 2006. We have considered internal control over financial reporting as of, and during the year ended, September 30, 2007, and we have tested compliance with selected laws and regulations.

Except as explained in the following paragraph, we conducted our audits in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits set forth in *Government Auditing Standards,* and Office of Management and Budget (OMB) Bulletin 07-04, *Audit Requirements for Federal Financial Statements.*

We are unable to express an opinion on the Department's annual financial statements as of, and for the year ended, September 30, 2007, because of limitations on the scope of our work. The Department was unable to respond to requests for evidential material in a timely manner, and we were not able to perform other auditing procedures to satisfy ourselves as to the accuracy of the financial statements in time to meet the November 15, 2007, deadline imposed by OMB for issuing our report. Therefore, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the 2007 financial statements.

In our opinion, the Department's 2006 annual financial statements, including the notes thereto, present fairly, in all material respects, the Department's financial position as of September 30, 2006, and its net cost of operations, changes in net position, and use of budgetary resources, for the year then ended, in accordance with accounting principles generally accepted in the United States of America. We issued our report thereon dated December 12, 2006.

We found the following:

- certain deficiencies in the Department's internal control that we considered to be significant deficiencies and other deficiencies that we considered to be material weaknesses,
- instances of noncompliance with selected provisions of applicable laws and regulations involving the Department's financial management systems, and
- that the Department's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act (FFMIA) of 1996.

Each of these conclusions is discussed in more detail below. This report also discusses the scope of our work.

ANNUAL FINANCIAL STATEMENTS

Because the Department was unable to respond to requests for evidential material in a timely manner and we were not able to perform other auditing procedures to satisfy ourselves as to the accuracy of the 2007 financial statements in time to meet the November 15, 2007, deadline imposed by OMB for issuing our report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the annual financial statements as of, and for the year ended, September 30, 2007.

In our opinion, the Department's 2006 annual financial statements, including the notes thereto, present fairly, in all material respects, the Department's financial position as of September 30, 2006, and the net cost of operations, the changes in net position, and the use of budgetary resources, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the annual financial statements, in 2006 the Department implemented new Statements of Federal Financial Auditing Standards related to earmarked funds and heritage assets. The Department also changed its treatment of major components installed on aircraft to the purchase method. In 2006 and 2007, the Department implemented new OMB reporting requirements. In addition, in 2007, the Department revised the presentation of the Statement of Net Cost to reflect the modification of the Department's strategic goals.

INTERNAL CONTROL

In planning and performing our audits of the Department's annual financial statements as of, and for the years ended, September 30, 2007 and 2006, in accordance with auditing standards generally accepted in the United States of America, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the annual financial statements but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control. We limited our consideration of internal control to those controls necessary to achieve the objectives described in OMB Bulletin 07-04. We did not consider all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations.

The purpose of internal control is to provide management with reasonable, but not absolute, assurance that the following objectives are met:

- transactions are properly recorded and accounted for to permit the preparation of reliable financial reports and to maintain accountability over assets;
- funds, property, and other assets are safeguarded against loss from unauthorized acquisition, use, or disposition;
- transactions, including those related to obligations and costs, are executed in compliance with laws and regulations that could have a direct and material effect on the financial statements and other laws and regulations that OMB, Department management, or the Office of Inspector General has identified as being significant for which compliance can be objectively measured and evaluated; and
- data that support reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.

Our consideration of the internal control over financial reporting would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. Under standards issued by the American Institute of Certified Public Accountants, a significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following four deficiencies to be significant deficiencies in internal control:

- The Department's financial and accounting system as of September 30, 2007, was inadequate. There is a risk of materially misstating financial information under the current conditions. This condition is a significant reason that the Department was unable to provide complete financial statements or respond to requests for evidential material in a timely manner, which led to our inability to express an opinion on the 2007 financial statements. The principal areas of inadequacy were the following:

- During 2007, the Department used several systems for the management of grants and other types of financial assistance. The systems lacked standard data classifications and common processes and were not integrated with the Department's core financial management system. Further, the Department could not produce reliable financial information that defined the universe of grants and other federal financial assistance. The Department has undertaken an initiative jointly with the United States Agency for International Development to establish a grants management system. Implementation of such a system was expected to begin in FY 2007, but as yet, it has not been funded.

- The Department is unable to produce year-end financial data to be included in its Agency Financial Report in a timely manner.

This deficiency was initially observed in our audit of the Department's 1997 financial statements and cited in subsequent audits.

- Although the Department complied with certain aspects of SFFAS Number 4, *Managerial Cost Accounting Standards* (for instance, it chose reasonable responsibility segments, recognized the cost of goods and services that it receives from other entities, and used an appropriate allocation methodology), it has not implemented an effective process to routinely collect managerial cost accounting information or establish outputs for each responsibility segment. Until this is done, we do not believe the information will be useful as a management decision-making tool. This condition was reported in our audit of the Department's 2000 financial statements and subsequent audits.

- The Department is unable to determine the extent of its unfunded actuarial liability accruing from defined benefit supplemental pension plans for locally employed staff.

- As discussed in this report, a number of significant deficiencies have been reported for several years. The Department has not taken appropriate action to either correct these significant deficiencies or conclude that they cannot be corrected.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following two deficiencies constitute material weaknesses:

- The Department's internal control process related to the management of undelivered orders was inadequate. The Department has made some improvements in this area over the past several years. The Bureau of Resource Management (RM) has actively worked with other Department bureaus to validate undelivered orders and has successfully cleared up a significant number of obligations that were outstanding from past years. The Department, however, needs to perform additional work to correct this condition. Our tests indicated that excess obligations as of September 30, 2007, were more than $550 million. Also, we noted that the Department's undelivered orders balance had grown to $13.4 billion as of September 30, 2007. The Budget and Accounting Procedures Act of 1950 requires that the Department's accounting system provide effective control over funds. Failure to deobligate funds in a timely manner may result in the loss of availability of those funds. The deficiencies in this process were cited in our report on the Department's 1997 financial statements and in subsequent reports.

- We have identified deficiencies related to the recording of personal property and related depreciation expense and accumulated depreciation. The Department's control over property in the hands of contractors, while improved, is still in development. Further, the Department's controls over vehicles and other personal property are less than fully effective. Our tests disclosed a continuation of assets acquired in prior years being reported as current year accessions and errors in depreciation resulting from incorrect in-service dates. This deficiency was initially observed in our audit of the Department's 2005 financial statements and cited again in our 2006 audit.

We are required to review the Department's current FMFIA report and disclose differences with the material weaknesses in our report. The Department's 2007 report did not identify control over personal property as a material weakness.

Finally, with respect to internal control related to performance measures reported in Management's Discussion and Analysis, we obtained an understanding of the design of significant controls relating to the existence and completeness assertions and determined whether those controls had been placed in operation as required by OMB Bulletin 07-04. Our procedures were not designed to provide assurance on internal control over reported performance measures, and accordingly, we do not provide an opinion on such controls.

We noted certain other internal control issues that we have reported to Department management in a separate letter dated November 14, 2007.

COMPLIANCE WITH LAWS AND REGULATIONS

Department management is responsible for complying with laws and regulations applicable to the Department. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Department's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin 07-04, including the requirements in FFMIA. We limited our tests of compliance to these provisions, and we did not test compliance with all laws and regulations applicable to the Department. The objective of our audit of the annual financial statements, including our tests of compliance with selected provisions of applicable laws and regulations, was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are failures to follow requirements or violations of prohibitions in statutes and regulations that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or that sensitivity warrants disclosure thereof.

The results of our tests of compliance with the laws and regulations described above, exclusive of FFMIA, disclosed the following instances of noncompliance with laws and regulations that are required to be reported under *Government Auditing Standards,* issued by the Comptroller General of the United States, and OMB Bulletin 07-04.

- *Budget and Accounting Procedures Act of 1950.* This act requires an accounting system to provide full disclosure of the results of financial operations; adequate financial information needed in the management of operations and the formulation and execution of the budget; and effective control over income, expenditures, funds, property, and other assets. However, we found that the Department's financial system (1) does not provide effective control over personal property, (2) does not manage undelivered orders effectively, and (3) is unable to issue year-end financial data in a timely manner.

- *Federal Managers' Financial Integrity Act of 1982.* This act requires the implementation of internal accounting and administrative controls that provide reasonable assurance that (1) obligations and costs are in compliance with applicable laws; (2) funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and (3) revenues and expenditures applicable to Department operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets. However, as discussed above, we found that the Department's financial system does not provide effective control over personal property and does not manage undelivered orders effectively. Hence, assets are not adequately protected from waste or loss.

- *Chief Financial Officers Act of 1990.* This act requires the development and maintenance of an integrated accounting and financial management system that (1) complies with applicable accounting principles, standards and requirements, and internal control standards; (2) complies with such policies and requirements as may be prescribed by the Director of OMB; (3) complies with any other requirements applicable to such systems; and (4) provides for (i) complete, reliable, consistent, and timely information that is prepared on a uniform basis and that is responsive to the financial information needs of agency management; (ii) the development and reporting of cost information; (iii) the integration of accounting and budgeting information; and (iv) the systematic measurement of performance. However, we found that the Department's financial system does not produce year-end financial data in a timely manner.

- *OMB Circular A-127, Financial Management Systems.* This circular requires the Department to establish and maintain an accounting system that provides for (1) complete disclosure of the financial results of the activities of the Department; (2) adequate financial information for Department management and for formulation and execution of the budget; and (3) effective control over revenue, expenditure, funds, property, and other assets. However, we found again that the financial system did not maintain effective control over personal property and undelivered orders. Further, the Department's failure to implement an effective managerial cost accounting system precludes effective control over revenues and expenditures.

The above areas of noncompliance were cited in our audit of the Department's 1997 financial statements and subsequent audits.

The results of our tests of compliance with other laws and regulations disclosed no material instances of noncompliance. Compliance with FFMIA is discussed below.

Under FFMIA, we are required to report whether the Department's financial management systems substantially comply with federal financial management system requirements, applicable accounting standards, and the U.S. Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance using the implementation guidance for FFMIA issued by OMB on January 4, 2001. OMB implementation guidance states that, to be in substantial compliance with this requirement, the Department must adhere to all applicable SFFASs; meet specific requirements of OMB Circular A-127, including the computer security controls required by OMB Circular A-130, *Management of Federal Information Resources;* and receive an unqualified opinion on its financial statements that discloses no material weaknesses in internal control that affect the Department's ability to prepare financial statements and related disclosures.

The results of our tests disclosed instances, described below, where the Department's financial management systems did not, in our view, substantially comply with the requirement to follow the federal financial management system requirements, nor did it comply with applicable accounting standards.

- SFFAS No. 4, as noted above, requires implementation of an effective process to routinely collect managerial cost accounting information and establish outputs for each responsibility segment. We found, as discussed above, that the Department had not met this requirement.

- Circular A-127 requires that the Department's systems support management's fiduciary role by providing complete, reliable, consistent, timely, and useful financial management information. Based on the deficiencies related to financial management systems discussed in the report on internal controls and the preceding paragraphs in the report on compliance with laws and regulations, we determined that the Department was not substantially in compliance with this standard.

In addition, we were unable to express an opinion on the annual financial statements as of, and for the year ended, September 30, 2007, because of limitations on the scope of our work. The Department was unable to respond to requests for evidential material in a timely manner, and we were not able to satisfy ourselves as to the accuracy of the 2007 financial statements in time to meet the November 15, 2007, deadline imposed by OMB for issuing our report.

RM has overall responsibility for the Department's financial management systems. The foregoing noncompliance has its roots in the lack of organization and integration of the Department's financial management systems. In our audits of the Department's financial statements since 1997, we observed that the Department's financial management systems were not in compliance with FFMIA and recommended, in connection with our audits of the Department's 1997 and 1998 Principal Financial Statements, that a remediation plan be prepared. RM submitted its plan to remediate noncompliance with FFMIA to OMB on March 16, 2000. Although RM has made significant progress in completing several phases of its plan, the plan has not effectively dealt with the issues related to managerial cost accounting.

We noted certain other instances of noncompliance that we reported to the Department's management in a separate letter dated November 14, 2007.

RESPONSIBILITIES AND METHODOLOGY

Department management has responsibility for the following:

- preparing the annual financial statements, required supplementary information, and other accompanying information in conformity with accounting principles generally accepted in the United States of America,
- establishing and maintaining effective internal control, and
- complying with applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether management maintained effective internal control. We are also responsible for testing compliance with selected provisions of applicable laws and regulations that may materially affect the financial statements.

In order to fulfill these responsibilities, we took the following actions:

- We examined, on a test basis, evidence supporting the amounts on the annual financial statements and related disclosures.
- We assessed the accounting principles used and significant estimates made by management.
- We evaluated the overall presentation of the annual financial statements.
- With respect to the Department's internal control over financial reporting, we obtained an understanding of the design effectiveness of internal controls, determined whether they had been placed in operation, assessed control risk, and performed tests of controls.
- With respect to performance measures included in Management's Discussion and Analysis, we obtained an understanding of the design of internal controls relating to the existence and completeness assertions and determined whether they had been placed in operation.
- We obtained an understanding of the process by which the agency identifies and evaluates weaknesses required to be reported under FMFIA and related agency implementing procedures.
- We tested compliance with selected provisions of laws and regulations that may have a direct and material effect on the financial statements.
- We obtained written representations from management.
- We performed other procedures as we considered appropriate under the circumstances.

We performed our work in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in the *Government Auditing Standards,* and the provisions of OMB Bulletin 07-04. We considered the limitations on the scope of our work in forming our conclusions.

The Management's Discussion and Analysis and Required Supplementary Information are supplementary information required by OMB Circular A-136, *Financial Reporting Requirements,* and the Federal Accounting Standards Advisory Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

This report is intended solely for the information and use of Department management, the Inspector General of the U.S. Department of State and Broadcasting Board of Governors, OMB, the Government Accountability Office, the Department of the Treasury, and the Congress and is not intended to be and should not be used by anyone other than those specified parties. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Comments by Department management on this report are presented as Appendix A to this report. The written response by Department management to the material weaknesses and significant deficiencies identified in our report has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion on these comments.

Leonard G. Birnbaum and Company, LLP
Alexandria, Virginia

November 14, 2007

APPENDIX A

United States Department of State

Washington, D.C. 20520

November 15, 2007

MEMORANDUM

TO: OIG – Mr. Howard J. Krongard

FROM: RM – Bradford R. Higgins BRH

SUBJECT: Draft Audit Report on the Department of State's 2007 and 2006 Financial Statements

This is in response to your request for comments on the draft report titled "Audit of the U.S. Department of State's 2007 and 2006 Financial Statements" (Report).

The Department operates in over 260 locations in 172 countries, while conducting business in 150 currencies and an even larger number of languages. Thousands of talented financial professionals around the world plan, budget, allocate, obligate, disburse, and account for billions of dollars in annual resources. Very few agencies or corporations have the depth and variety of challenges that the men and women of the Department of State (Department) face daily. Despite these complexities, the Department pursues a commitment to financial integrity, transparency, and accountability that is the equal of any multi-national corporation.

Given the breadth, depth and complexity of our financial operations, it will always be a challenge for the Department to meet OMB's November 15 deadline. In addition, each year will bring new challenges (such as accounting for contractor held property in Iraq/Afghanistan, increased spending through allocations to other agencies such as for HIV/AIDS, etc). Adding to that complexity this year, the Department implemented the new Global Financial Management System (GFMS) as the next step in our multiyear effort to establish a single global financial system. GFMS replaces the Department's 20 year old Central Financial Management System (our core accounting system) and centrally accounts for the Department's billions of dollars of finances through millions of annual transactions by 1,000 users and over 25 "handshakes" with other internal and external systems. As part of this implementation, the Department also installed integrated acquisitions and fixed assets modules, a managerial cost allocation module, and a new data warehouse. Upgrading a financial system of this size and complexity is a large and challenging undertaking.

Working closely with the Independent Auditor and your office, the Department has a proud tradition of unqualified opinions on our financial statements for the past decade. Due to the complexity of the matters involved with installing a new core financial system, it took the Department slightly longer to close our books this year. Consequently, the Department was unable to provide financial statements and certain evidential documentation in a timely fashion, and the Independent Auditor issued a disclaimer of opinion on our FY 2007 financial statements.

In addition to accomplishing the upgrade of our core financial system, we continued our efforts to resolve significant internal control weaknesses. Our priority was on those items that were reported as material weaknesses in recent years and that were downgraded last year to significant deficiencies (formerly reportable conditions) – IT Security, Accounting for Real Property, and Accounting for Personal Property. As a result of our efforts, the Independent Auditor downgraded the IT Security and Accounting for Real Property to deficiencies (from a significant deficiency). With the introduction of new definitions by SAS 112, which in effect "raises the bar" on moving items down in terms of severity, we think this is a significant achievement.

With respect to the Independent Auditor reporting the Accounting for Personal Property as a material weakness, we respectfully disagree with this determination. Our continuing progress to address the many causes of this weakness for our multitude of global assets (aircraft, vehicles, security equipment) is perhaps not as fast as we would like. However, we believe our actions have improved our controls from a year ago (when it was downgraded to a significant deficiency). As a result of the improved status by September 30, 2007, the Department's Management Control Steering Committee (MCSC) voted to downgrade this item from a significant deficiency to a deficiency. In FY 2007, management did complete its assessment of the controls over personal property, noting additional improvements in conducting inventories of vehicles, both held by the Department and by contractors; the successful implementation of tools in ILMS to manage its vehicle fleet; and improvements in guidance and policy. Further corrective actions are planned for FY 2008, including expanding the capabilities for overseas posts to report acquisitions and disposals in the Integrated Logistics Management System. In 2008, the MCSC will ensure that efforts continue to further strengthen the controls over the accounting for personal property.

The Report cites a new material weakness for the management of unliquidated obligations, and notes that there have been improvements in this area. We are already refocusing our efforts to establish adequate processes and controls. Improvements in the management of unliquidated obligations is a priority for the Department in FY 2008, and corrective actions are already underway including the distribution of aging reports, and using recently developed enhancements to our Global Financial Management System's capabilities to automate deobligations. In addition, actions to improve contract closeout procedures relative to unliquidated obligations will be established, and the Senior Assessment Team will be actively engaged with the implementation and oversight of these corrective actions.

Significant improvements in the Department's management of Federal financial assistance were made in 2007. To address the need for increased training, two new FSI courses, quarterly assistance meetings, an annual symposium, and periodic audio-conferences on financial management issues have been established. Outreach efforts include the creation of a new "Ask

APPENDIX A

Grants" electronic bulletin board, as well as continued updates of three linked websites that offer comprehensive information on assistance. Key achievements in the standardization of policies have been the issuance of sixteen updated and four new Grant Policy Directives and a Payment Management System (PMS) User Handbook; newly-standardized Terms & Conditions have been finalized. A new Grants Officer's Handbook and FAM/FAH updates are being circulated for clearance. The existing Grants Database Management System (GDMS) was upgraded to accommodate the data reporting requirements of the Federal Funding Accountability & Transparency Act (FFATA). In addition, all domestic offices completed the transition to using the HHS *Payment Management System* (PMS) for all assistance disbursements (one-time payments are exempt from mandatory use) and an automated system to apply for and receive grants warrants was implemented. Development of an automated assistance management system that will track assistance activities from solicitation to post-award monitoring and closeout continues; configuration is approximately 80% complete.

The Department continues to make progress in implementing Managerial Cost Accounting Standards (MCAS). In 2005, the Department established a project team, which includes consultants with experience implementing Cost Accounting Systems. In 2006, the team surveyed other agencies and organizations for lessons learned and best practices; conducted an assessment of offices to determine business needs for cost information, current cost accounting practices, outputs and outcomes, and unmet needs; evaluated a managerial cost software module and confirmed usability; and developed a strategic approach and implementation strategy. In 2007, the Department implemented CGI's Momentum Cost Allocation module, and an initial cost model was developed that assigns costs to bureaus. The MCA model contains three cost components: 1) central payroll, 2) bureau managed funds, and 3) overhead/support. This model was run for each quarter of FY 2007. The next phase in FY 2008 will be to incorporate bureaus' specific cost allocations. The Department's new data warehouse will be used to generate all managerial cost reports.

With respect to the significant deficiency for defined benefit supplemental pension plans for locally employed staff, the Department will undertake efforts in FY 2008 to establish an accurate inventory of these plans. This will serve as a basis to work and establish an appropriate approach to determining any unfunded actuarial amounts.

We thank you for the opportunity to comment on the draft report. Our work with the Independent Auditor and your office over the past 10 years has been collaborative, productive, and a catalyst for positive change. We would like to extend our appreciation to Leonard G. Birmbaum and Company, LLP, for their dedicated efforts on this year's audit. We believe, as detailed above, that considerable progress on a number of matters has been made over the years, and the Department remains committed to improving the management of its programs and the quality of its financial reporting.

Financial Statements

INTRODUCTION TO PRINCIPAL FINANCIAL STATEMENTS

The Principal Financial Statements (Statements) have been prepared to report the financial position and results of operations of the U.S. Department of State (Department). The Statements have been prepared from the books and records of the Department in accordance with formats prescribed by the Office of Management and Budget (OMB) in OMB Circular A-136, *Financial Reporting Requirements.* The Statements are in addition to financial reports prepared by the Department in accordance with OMB and U.S. Department of the Treasury (Treasury) directives to monitor and control the status and use of budgetary resources, which are prepared from the same books and records. The Statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity. The Department has no authority to pay liabilities not covered by budgetary resources. Liquidation of such liabilities requires enactment of an appropriation. Comparative data for 2006 are included.

The **Consolidated Balance Sheet** provides information on assets, liabilities, and net position similar to balance sheets reported in the private sector. Intra-departmental balances have been eliminated from the amounts presented.

The **Consolidated Statement of Net Cost** reports the components of the net costs of the Department's operations for the period. The net cost of operations consists of the gross cost incurred by the Department less any exchange (i.e., earned) revenue from our activities. Intra-departmental balances have been eliminated from the amounts presented.

The **Consolidated Statement of Changes in Net Position** reports the beginning net position, the transactions that affect net position for the period, and the ending net position. Intra-departmental transactions have been eliminated from the amounts presented.

The **Combined Statement of Budgetary Resources** provides information on how budgetary resources were made available and their status at the end of the year. Information in this statement is reported on the budgetary basis of accounting. Intra-departmental transactions have not been eliminated from the amounts presented.

Required Supplementary Information contains a Combining Schedule of Budgetary Resources that provides additional information on amounts presented in the **Combined Statement of Budgetary Resources,** and information on Stewardship Plant, Property and Equipment.

PRINCIPAL FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEET

(Dollars in Thousands)

As of September 30,	**Notes**	**2007**	**2006**
ASSETS	3		
Intragovernmental Assets:			
Fund Balances With Treasury	4	$ 19,778,998	$ 16,170,761
Investments, Net	5	14,412,447	13,909,584
Interest Receivable		194,705	192,181
Accounts Receivable, Net	6	391,560	344,038
Total Intragovernmental Assets		34,777,710	30,616,564
Accounts and Loans Receivable, Net	6	32,534	34,319
Cash and Other Monetary Assets	7	60,382	48,666
Property and Equipment, Net	8	10,198,455	9,175,917
Other Assets	9	164,748	82,488
Total Assets		$ 45,233,829	$ 39,957,954
Stewardship PP&E	8		
LIABILITIES	10		
Intragovernmental Liabilities:			
Accounts Payable		$ 4,853	$ 3,473
Other Liabilities		658,225	316,271
Total Intragovernmental Liabilities		663,078	319,744
Accounts Payable		1,945,071	1,250,204
Foreign Service Retirement Actuarial Liability	11	14,728,700	14,215,300
Liability to International Organizations	12	1,476,596	1,155,344
Environmental Liabilities	10	392,300	392,300
Other Liabilities	10,13	687,378	560,155
Total Liabilities		19,893,123	17,893,047
Commitments and Contingencies	14		
NET POSITION			
Unexpended Appropriations		14,553,330	13,095,268
Cumulative Results of Operations—Earmarked Funds	15	(27,893)	(19,824)
Cumulative Results of Operations—Other Funds		10,815,269	8,989,463
Total Net Position		25,340,706	22,064,907
Total Liabilities and Net Position		$ 45,233,829	$ 39,957,954

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

CONSOLIDATED STATEMENT OF NET COST (NOTE 16)

(Dollars in Thousands)

As of September 30,	**2007**	**2006**
Achieve Peace and Security		
Total Cost	$ 5,761,110	$ 5,663,920
Earned Revenue	(849,177)	(694,911)
Net Program Costs	4,911,933	4,969,009
Governing Justly and Democratically		
Total Cost	696,812	631,846
Earned Revenue	(46,704)	(55,020)
Net Program Costs	650,108	576,826
Investing in People		
Total Cost	2,321,731	1,328,527
Earned Revenue	(21,083)	(24,791)
Net Program Costs	2,300,648	1,303,736
Promoting Economic Growth and Prosperity		
Total Cost	1,138,891	1,032,707
Earned Revenue	(76,335)	(89,926)
Net Program Costs	1,062,556	942,781
Providing Humanitarian Assistance		
Total Cost	1,099,132	924,589
Earned Revenue	(31)	(122)
Net Program Costs	1,099,101	924,467
Promoting International Understanding		
Total Cost	1,925,025	1,638,788
Earned Revenue	(151,451)	(165,591)
Net Program Costs	1,773,574	1,473,197
Strengthening Consular and Management Capabilities		
Total Cost	2,609,552	2,380,822
Earned Revenue	(2,661,992)	(2,332,238)
Net Program Costs	(52,440)	48,584
Executive Direction and Other Costs Not Assigned		
Total Cost	3,472,286	3,481,740
Earned Revenue	(1,581,683)	(1,227,677)
Net Program Costs	1,890,603	2,254,063
Total Cost	**19,024,539**	**17,082,939**
Total Revenue	**(5,388,456)**	**(4,590,276)**
Total Net Cost	$ **13,636,083**	**$ 12,492,663**

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

(Dollars in Thousands)

For the Year Ended September 30	2007			2006
	Earmarked Funds	**All Other Funds**	**Consolidated Total**	**Consolidated Total**
Cumulative Results of Operations				
Beginning Balances	$ (19,824)	$ 8,989,463	$ 8,969,639	$ 7,844,356
Budgetary Financing Sources:				
Other Adjustments	–	–	–	555
Appropriations Used	–	16,372,544	16,372,544	14,370,657
Non-exchange Revenue	1,505	19,502	21,007	27,730
Donations and Forfeitures of Cash and Cash Equivalents	10,506	163	10,669	7,819
Transfers in(out) without Reimbursement	–	(1,074,773)	(1,074,773)	(905,379)
Other	–	–	–	–
Other Financing Sources (Non-Exchange):				
Imputed Financing From Costs Absorbed by Others	–	124,373	124,373	116,564
Total Financing Sources	12,011	15,441,809	15,453,820	13,617,946
Net Cost of Operations	(20,080)	(13,616,003)	(13,636,083)	(12,492,663)
Net Change	(8,069)	1,825,806	1,817,737	1,125,283
Cumulative Results of Operations	**(27,893)**	**10,815,269**	**10,787,376**	**8,969,639**
Unexpended Appropriations:				
Beginning Balances	–	13,095,268	13,095,268	11,430,639
Budgetary Financing Sources:				
Appropriations Received	–	17,719,856	17,719,856	16,129,704
Appropriations transferred in(out)	–	239,823	239,823	191,963
Other Adjustments	–	(129,073)	(129,073)	(286,381)
Appropriations Used	–	(16,372,544)	(16,372,544)	(14,370,657)
Total Budgetary Financing Sources	–	1,458,062	1,458,062	1,664,629
Total Unexpended Appropriations	–	14,553,330	14,553,330	13,095,268
Net Position	**$ (27,893)**	**$ 25,368,599**	**$ 25,340,706**	**$ 22,064,907**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES (NOTE 17)

(Dollars in Thousands)

For the Year Ended September 30,	**2007**	**2006**
Budgetary Resources:		
Unobligated Balance, brought forward, October 1:	$ 5,287,148	$ 4,271,107
Recoveries of Prior Year Unpaid Obligations	193,629	834,868
Budget Authority:		
Appropriations	19,021,844	17,370,186
Borrowing Authority	–	378
Spending authority from offsetting collections (gross):		
Earned		
Collected	6,781,787	4,693,095
Change in receivable from Federal sources	(9,575)	(521,627)
Change in unfilled customer orders:		
Advance received	104,611	264,239
Without Advance from Federal Sources	1,360	(750)
Nonexpenditure transfers, net, anticipated and actual	205,315	191,226
Temporarily not available pursuant to Public Law	(500,027)	(376,869)
Permanently not available	(131,792)	(292,892)
Total Budgetary Resources	**$ 30,954,300**	**$ 26,432,961**
Status of Budgetary Resources:		
Obligations Incurred:		
Direct	$ 18,701,403	$ 16,095,192
Reimbursable	6,500,348	5,050,621
Unobligated balance		
Apportioned	5,438,660	4,762,140
Exempt from apportionment	23,596	40,863
Unobligated balance not available	290,293	484,145
Total Status of Budgetary Resources	**$ 30,954,300**	**$ 26,432,961**
Change in Obligated Balance:		
Obligated Balance, net		
Unpaid Obligations, brought forward, October 1	11,195,023	10,279,062
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(416,192)	(938,570)
Obligations incurred, net	25,201,751	21,145,813
Less: Gross Outlays	(21,879,678)	(19,394,984)
Obligated balance transfers, net		
Actual transfers, unpaid obligations	-	-
Actual transfers, uncollected customer payments from Federal sources	-	-
Less: Recoveries of prior-year unpaid obligations, actual	(193,629)	(834,868)
Change in uncollected customer payments from Federal sources	8,215	522,378
Obligated balance, net, end of period:		
Unpaid obligations	14,542,794	11,195,023
Less: Uncollected customer payments from Federal sources	(627,306)	(416,192)
Net Outlays		
Gross outlays	21,879,678	19,394,984
Less: Offsetting collections	(6,886,399)	(4,957,334)
Less: Distributed Offsetting receipts	(260,419)	(250,820)
Net Outlays	**$ 14,732,860**	**$ 14,186,830**

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

NOTES TO PRINCIPAL FINANCIAL STATEMENTS

ORGANIZATION

Congress established the U.S. Department of State ("Department of State" or "Department"), the senior executive department of the United States Government in 1789, replacing the Department of Foreign Affairs, which was established in 1781. The Department advises the President in the formulation and execution of foreign policy. As head of the Department, the Secretary of State is the President's principal advisor on foreign affairs.

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity and Basis of Consolidation

The accompanying principal financial statements (statements) present the financial activity for the Department of State. The statements include the accounts of all funds under Department control that have been established and maintained to account for the resources entrusted to Department management, or for which the Department acts as a fiscal agent or custodian.

Basis of Presentation and Accounting

The accompanying statements are prepared as required by the Government Management and Reform Act (GMRA) of 1994 and presented in accordance with form and content requirements contained in Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, as amended.

The statements have been prepared from the Department's books and records, and are in accordance with the Department's accounting policies (the significant policies are summarized below in this Note). The Department's accounting policies follow accounting principles generally accepted in the United States of America (GAAP). GAAP for Federal entities is the hierarchy of accounting principles prescribed in the American Institute of Certified Public Accountants' Statement of Auditing Standards No. 91, Federal GAAP Hierarchy, which is also incorporated in OMB Circular A-136.

Transactions are recorded on both an accrual and budgetary basis. Budgetary accounting facilitates compliance with legal constraints

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions, and exercise judgment that affects the reported amounts of assets, liabilities and net position and disclosure of contingent liabilities as the date of the financial statements, and the reported amounts of revenues, financing sources, expenses and obligations incurred during the reporting period. These estimates are based on management's best knowledge of current events, historical experience, actions the Department may take in the future, and on various other assumptions that are believed to be reasonable under the circumstances. Due to the size and complexity of many of the Department's programs, the estimates are subject to a wide range of variables, including assumptions on future economic and financial events. Accordingly, actual results could differ from those estimates.

Revenues and Other Financing Sources

Department operations are financed through appropriations, reimbursement for the provision of goods or services to other Federal agencies, proceeds from the sale of property, certain consular-related and other fees, and donations. In addition, the Department collects passport, visa, and other consular fees that are not retained by the Department but are deposited directly to a Treasury account. The passport and visa fees are reported as earned revenues on the Statement of Net Cost and as a transfer-out of financing sources on the Statement of Changes in Net Position.

Congress annually enacts one-year and multi-year appropriations that provide the Department with the authority to obligate funds within the respective fiscal years for necessary expenses to carry out mandated program activities. In addition, Congress enacts appropriations that are available until expended. All appropriations are subject to OMB apportionment as well as Congressional restrictions. For financial statement purposes, appropriations are recorded as a financing source (i.e., Appropriations Used) and reported on the Statement of Changes in Net Position at the time they are recognized as expenditures. Appropriations expended for capitalized property and equipment are recognized when the asset is purchased.

Work performed for other Federal agencies under reimbursable agreements is financed through the account providing the service and reimbursements are recognized as revenue when earned. Administrative support services at overseas posts are provided to other Federal agencies through the International Cooperative Administrative Support Services (ICASS). ICASS bills for the services it provides to agencies at overseas posts. These billings are recorded as revenue to ICASS and must cover overhead costs, operating expenses, and replacement costs for capital assets needed to carry on the operation. Proceeds from the sale of real property, vehicles, and other personal property are recognized as revenue when the proceeds are credited to the account from which the asset was funded. For non-capitalized property, the full amount realized is recognized as revenue. For capitalized property, revenue or loss is determined by whether the proceeds received were more or less than the net book value of the asset sold. The Department retains proceeds of sale, which are available for purchase of the same or similar category of property.

The Department is authorized to collect and retain certain user fees for machine-readable visas, expedited passport processing, and fingerprint checks on immigrant visa applicants. The Department is also authorized to credit the respective appropriations with (1) fees for the use of Blair House; (2) lease payments and transfers from the International Center Chancery Fees held in Trust to the International Center Project; (3) registration fees for the Office of Defense Trade Controls; (4) reimbursement for international litigation expenses; and (5) reimbursement for training foreign government officials at the Foreign Service Institute.

Generally, donations received in the form of cash or financial instruments are recognized as revenue at their fair value in the period received. Contributions of services are recognized if the services received (a) create or enhance non-financial assets, or (b) require specialized skills that are provided by individuals possessing those skills, which would typically need to be purchased if not donated. Works of art, historical treasures, and similar assets that are added to collections are not recognized at the time of donation. If subsequently sold, proceeds from the sale of these items are recognized in the year of sale.

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

Allocation Transfers

Allocation transfers are legal delegations by one federal agency of its authority to obligate budget authority and outlay funds to another agency. The Department processes allocation transfers with other federal agencies as both a "parent" agency transferring budget authority to a receiving (child) entity and as a receiving (child) agency of budget authority from another transferring (parent) entity. A separate fund account (allocation account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. Subsequent obligations and outlays incurred by the child agency are charged to this allocation account as they execute the delegated activity on behalf of the parent agency.

Generally, all financial activities related to allocation transfers (i.e., budget authority, obligations, outlays) are reported in the financial statements of the parent agency. An exception to this rule is for transfers from the Executive Office of the President for whom the Department is the receiving agency. Per OMB guidance, State reports all activity relative to these allocation transfers in the Department's financial statements. In addition to these funds the Department receives allocation transfers, as the child, from USAID. The Department allocates funds, as the parent, to Department of Defense, Department of Labor, Treasury, Health and Human Services, PeaceCorp, and the U.S. Agency for International Development.

Fund Balances with Treasury

The Fund Balances with Treasury are 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 funds reported in the Consolidated Balance Sheet, except for the Emergencies in the Diplomatic and Consular Services, Office of Foreign Missions, Foreign Service National Defined Contributions Retirement Fund, and the International Center. Treasury processes domestic receipts and disbursements. The Department operates two Financial Service Centers, which are located in Bangkok, and Charleston, South Carolina, and provide financial support for the Department and other Federal agencies' operations overseas. The U.S. Disbursing Officer at each Center has the delegated authority to disburse funds on behalf of the Treasury.

Accounts and Loans Receivable

Intragovernmental Accounts Receivable are due principally from other Federal agencies for ICASS services, reimbursable agreements, and Working Capital Fund (WCF) services. Accounts and Loans Receivable fr om non-Federal entities are primarily the result of International Boundary and Water Commission (IBWC) receivables for Mexico's share of IBWC activities and Repatriation Loans.

The Department provides Repatriation Loans for destitute American citizens overseas whereby the Department becomes the lender of last resort. These loans provide assistance to pay for return transportation, food and lodging, or medical expenses. The borrower executes a promissory note without collateral. Consequently, the loans are made anticipating a low rate of recovery. Interest, penalties, and administrative fees are assessed if the loan becomes delinquent.

Accounts and Loans Receivable from non-Federal entities are subject to the full debt collection cycle and mechanisms, e.g., salary offset, referral to collection agents, and Treasury offset. In addition, Accounts Receivable from non-Federal entities are assessed interest, penalties and administrative fees if they become delinquent. Interest and penalties are assessed at the Current Value of Funds Rate established by Treasury. Accounts Receivable is reduced to net realizable value by an Allowance for Uncollectable Accounts.

Interest Receivable

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

Advances and Prepayments

Payments made 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. Advances are made principally to Department employees for official travel, miscellaneous prepayments and advances to other entities for future services, and salary advances to Department employees transferring to overseas assignments. Advances and prepayments are reported as Other Assets on the Balance Sheet.

Valuation of Investments

The Department has several accounts that have the authority to invest cash resources (see Note 5 "Investments"). For these accounts, the cash resources not required to meet current expenditures are invested in interest-bearing obligations of the U.S. Government. These investments consist of U.S. Treasury special issues and securities. Special issues are unique public debt obligations for purchase exclusively by the Foreign Service Retirement and Disability Fund and for which interest is computed and paid semi-annually on June 30 and December 31. They are purchased and redeemed at par which is their carrying value on the Consolidated Balance Sheet.

Investments by the Department's Gift, Israeli-Arab Scholarship, Eisenhower Exchange Fellowship and Middle-Eastern-Western Dialogue accounts are in U.S. Treasury securities. Interest on these investments I s paid semi-annually at various rates. These investments are reported at acquisition cost, which equals the face value net of unamortized discounts or premiums. Discounts and premiums are amortized over the life of the security using the straight-line method for Gift Funds investments, and effective interest method for the other accounts.

Inventories

Inventories are reported as Other Assets on the Department's Consolidated Balance Sheet and include inventories held by WCF's Publishing Services, and the Supply Services Center and Stock Account. The WCF inventory consists primarily of paper and ink used for printing and reproduction services (Publishing Services), furniture held for sale to bureaus in the Department (Supply Services Center and Stock Account), and publications held for sale.

The WCF's Publishing Services inventory is valued at the latest acquisition cost. The Supply Services Center and Stock Account inventory is valued monthly using a weighted moving average. The inventory value of the publications held for sale is based on the cost of production. Recorded values are adjusted for the results of periodic physical inventories.

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, including unimproved land; residential and functional-use buildings such as embassy/consulate office buildings; office annexes and support facilities; and construction-in-progress. Title to these properties is held under various conditions including fee simple, restricted use, crown lease, and deed of use agreement. Some of these properties are considered historical treasures and are considered multi-use heritage assets. These items are reported on the Balance Sheet, in Note 8 (Stewardship PP&E) to the financial statements, and included in the Required Supplementary Information—Heritage Assets.

The Tangier Old Legation, the first property that the United States Government acquired for a diplomatic mission, was presented as a gift to the American people by Sultan Moulay Suliman in 1821.

The Department also owns several domestic real properties, including the National Foreign Affairs Training Center (Arlington, VA); the International Center (Washington, D.C.); the Charleston Financial Services Center (S.C.); the Beltsville Information Management Center (Md.); the Florida Regional Center (Ft. Lauderdale); and consular centers in Charleston (S.C.); Portsmouth (N.H.) and Williamsburg (K.Y.). The International Boundary and Water Commission (IBWC) has buildings and structures related to its boundary preservation, flood control, and sanitation programs.

Buildings and structures are carried at either actual or estimated historical cost. The Department capitalizes all costs for constructing new buildings and building acquisitions regardless of cost, and capitalizes all other improvements greater than $250,000. Costs incurred for constructing new facilities, major rehabilitations, or other improvements in the design or construction stage are recorded as Construction-in-Progress. After these projects are completed, costs are transferred to Buildings and Structures or Leasehold Improvements as appropriate. Depreciation of buildings and other structures is computed on a straightline basis, principally over a 30-year period.

Personal Property

Personal property consists of several asset categories including aircraft, vehicles, security equipment, communication equipment, ADP equipment, reproduction equipment, and software. The Department holds title to these assets, some of which are operated in unusual conditions as described below.

The Department's Bureau of International Narcotics and Law Enforcement (INL) uses aircraft to help eradicate and stop the flow of illegal drugs. To accomplish its mission, INL maintains an aircraft fleet that is the third largest federal, nonmilitary fleet. Most of the aircraft are under direct INL airwing management. However, a number of aircraft are managed by host-countries. The Department owns title to the aircraft under these programs and is prohibited from giving title for any aircraft to foreign governments without

Congressional approval. As such, these host-country managed aircraft are, for the most part, no-cost, long-term leases. INL contracts with firms to provide maintenance support depending on whether the aircraft are INL airwing or host-country managed. INL airwing managed aircraft are maintained to FAA standards that involves routine inspect, replace as necessary activity as well as scheduled maintenance and replacement of certain parts after given hours of use. Host-country managed aircraft are maintained to host country requirements, which are less than FAA standards.

The Department maintains a large vehicle fleet that operates overseas. Many vehicles require armoring for security reasons, and for some locations large utility vehicles are used instead of conventional sedans. In addition, the Department contracts with firms to provide support in strife-torn areas such as Iraq, Afghanistan and Darfur. The contractor support includes the purchase and operation of armored vehicles. Under the terms of the contracts, the Department has title to the contractor-held vehicles.

Personal property and equipment with an acquisition cost of $25,000 or more, and a useful life of two or more years, is capitalized at cost. However, there are exceptions to this capitalization policy. All vehicles are capitalized, as well as ADP software costing over $500,000. Except for contractor-held vehicles in Iraq and Afghanistan, depreciation is calculated on a straight-line basis over the asset's estimated life and begins when the property is put into service. Contractor-held vehicles in Iraq and Afghanistan, due to the harsh operating conditions, are depreciated on a double-declining balance basis. The estimated useful lives are as follows:

Asset Category	Estimated Useful Life
Aircraft:	
INL airwing managed	10 years
Host-country managed	5 years
Vehicles:	
Department managed	3 to 6 years
Contractor-held in Iraq and Afghanistan	2 1/2 years
Security Equipment	3 to 15 years
Communication Equipment	3 to 20 years
ADP Equipment	3 to 6 years
Reproduction Equipment	3 to 15 years
Software	Lesser of estimated useful life or 7 years

Capital Leases

Leases are accounted for as capital leases if they meet one of the following criteria: (1) the lease transfers ownership of the property by the end of the lease term; (2) the lease contains an option to purchase the property at a bargain price; (3) the lease term is equal to or greater than 75% of the estimated useful life of the property; or (4) the present value of the minimum lease payment equals or exceeds 90% of the fair value of the leased property. The initial recording of the lease's value (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.

Works of Art and High Value Furnishings

See Note 8 "Property and Equipment – Stewardship PP&E," on page 66 for the Department's policy for works of art and high value furnishings.

Grants

The Department awards educational, cultural exchange, and refugee assistance grants to various individuals, universities, and not-for-profit organizations. Budgetary obligations are recorded when grants are awarded. Grant funds are disbursed in two ways: grantees draw funds commensurate with their immediate cash needs via the Department of Health and Human Services (HHS) Payments Management System (PMS); or grantees submit invoices. In both cases, the expense is recorded upon disbursement.

Accounts Payable

Accounts payable represent the amounts accrued for contracts for goods and services received but unpaid at the end of the fiscal year and unreimbursed grant expenditures. In addition to accounts payables recorded through the Department's normal business activities, domestic accounts payable also includes an estimate of unbilled payables existing at year end for which payment will be made in the subsequent period based on an average of actual disbursements over a four-year period. The Department also includes an estimate of unbilled overseas accounts payable at year end, based on analysis of past payment trends applied towards current expenses.

Annual, Sick and Other Leave

Annual leave is accrued as it is earned, and the accrual is reduced as leave is taken. Throughout the year the balance in the accrued annual leave liability account is adjusted to reflect current pay rates. The amount of the adjustment is recorded as an expense. Current or prior year appropriations are not available to fund annual leave earned but not taken. Funding occurs in the year the leave is taken and payment is made. Sick leave and other types of non-vested leave are expensed as taken.

Employee Benefit Plans

Retirement Plans: Civil Service employees participate in either 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 contribute 7% of their salary; the Department contributes 7%. Employees covered under CSRS also contribute 1.45% of their salary to Medicare insurance; the Department makes a matching contribution. 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 0.80% of their salary, with the Department making contributions of 11.20%. FERS employees also contribute 6.20% 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% of pay and matches employee contributions up to an additional 4%.

Foreign Service employees hired prior to January 1, 1984, participate in FSRDS with certain exceptions. FSPS was established pursuant to Section 415 of Public Law 99-335, which became effective June 6, 1986. Foreign Service employees hired after December 31, 1983, participate in FSPS with certain exceptions. FSRDS employees contribute 7.25% of their salary; the Department contributes 7.25%. FSPS employees contribute 1.35% of their salary; the Department contributes 20.22%. Both FSRDS and FSPS employees contribute 1.45% of their salary to Medicare; the Department matches their contributions. Similar to FERS, FSPS also offers the TSP described above.

Foreign Service Nationals (FSNs) and Third Country Nationals (TCNs) at overseas posts who were hired prior to January 1, 1984, are covered under CSRS. FSNs and TCNs hired after that date are covered under a variety of local government plans in compliance with the host country's laws and regulations. In cases where the host country does not mandate plans or the plans are inadequate, employees are covered by a privately managed pension plan that conforms to the prevailing practices of comparable employers.

Health Insurance: Most American employees participate in the Federal Employees Health Benefits Program (FEHBP), a voluntary program that provides protection for enrollees and eligible family members in case of illness and/or accident. Under FEHBP, the Department contributes the employer's share of the premium as determined by the U.S. Office of Personnel Management (OPM).

Life Insurance: Unless specifically waived, employees are covered by the Federal Employees Group Life Insurance Program (FEGLIP). FEGLIP automatically covers eligible employees for basic life insurance in amounts equivalent to an employee's annual pay, rounded up to the next thousand dollars plus $2,000. The Department pays one-third and employees pay two-thirds of the premium. Enrollees and their family members are eligible for additional insurance coverage but the enrollee is responsible for the cost of the additional coverage.

Other Post Employment Benefits: The Department does not report CSRS, FERS, FEHBP or FEGLIP assets, accumulated plan benefits, or unfunded liabilities applicable to its employees; OPM reports this information. As required by SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, the Department reports the full cost of employee benefits for the programs that OPM administers. The Department recognizes an expense and imputed financing source for the annualized unfunded portion of CSRS, post-retirement health benefits, and life insurance for employees covered by these programs. The Department recognized $124.4 and $116.6 million in 2007 and 2006, respectively, for unfunded pension and post-retirement benefits. The additional costs are not actually owed or paid to OPM, and thus are not reported on the Balance Sheet as a liability, but instead are reported as an imputed financing source from costs absorbed from others on the Statement of Changes in Net Position.

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. The U.S. Department of Labor (DOL) administers the FECA program. DOL initially pays valid claims and bills the employing Federal agency. DOL calculates the actuarial liability for future workers' compensation benefits and reports to each agency its share of the liability.

The total actuarial liability for which the Department is responsible totaled $68.1 million and $62.7 million as of September 30, 2007 and September 30, 2006 respectively.

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 is determined annually.

Actuarial Present Value of Projected Plan Benefits for the Foreign Service Retirement and Disability Program

See Note 11 "Foreign Service Retirement Actuarial Liability," on pages 69 to 70 for the Department's accounting policy for Foreign Service retirement-related benefits.

Net Position

The Department's net position contains the following components. Amounts attributable to earmarked funds are separately disclosed. See Note 15 "Earmarked Funds" on page 75 for a description of and the Department's accounting policy for earmarked funds.

1. **Unexpended Appropriations** — the sum of undelivered orders and unobligated balances. Undelivered orders represent the amount of obligations incurred for goods or services ordered, but not yet received. An unobligated balance is the amount available after deducting cumulative obligations from total budgetary resources. As obligations for goods or services are incurred, the available balance is reduced.

2. **Cumulative Results of Operations** — include (1) the accumulated difference between revenues and financing sources less expenses since inception; (2) the Department's investment in capitalized assets financed by appropriation; (3) donations; and (4) unfunded liabilities, whose liquidation may require future Congressional appropriations or other budgetary resources.

Foreign Currency

Accounting records for the Department are maintained in U.S. dollars, while a significant amount of the Department's overseas expenditures are in foreign currencies. For accounting purposes, overseas obligations and disbursements are recorded in U.S. dollars based on the rate of exchange as of the date of the transaction. Foreign currency payments are made by the U.S. Disbursing Office.

2 ACCOUNTING CHANGES

Standards Implemented

In 2007 and 2006, the Department implemented revised financial statement reporting requirements and new Statements of Federal Financial Accounting Standards (SFFAS). The changes did not have a material effect on the Department's financial position or results of operations. The new reporting requirements and SFFASs primarily affect the manner in which the Department reports on its programs.

On June 29, 2007, OMB issued A-136 Revised, Financial Reporting Requirements, which provides guidance for preparing agency financial statements. It supersedes OMB Circular A-136, dated July 24, 2006. The requirements contained in A-136 are effective for the preparation of financial statements for fiscal years beginning with FY 2007.

As prescribed by OMB Circular A-136, the Department implements financial statement reporting requirements and new SFFASs when they become effective and if they apply to the Department's operations. The following SFFASs were implemented for FY 2006:

- SFFAS 27, Identifying and Reporting Earmarked Funds, dated December 28, 2004, requires separate reporting of earmarked funds on the Balance sheet and Statement of Changes in Net Position along with other disclosure requirements.

- SFFAS29, Heritage Assets and Stewardship Land, dated July 7, 2005, reclassifies heritage assets and stewardship land information phasing in their requirements starting in FY 2006 through FY 2009.

There were no new SFFASs required to be implemented in FY 2007 that apply to the Department. The following reporting requirements were implemented for FYs 2007 and 2006:

NEW FY 2007 OMB REPORTING REQUIREMENTS	
OMB GUIDANCE	**DESCRIPTION OF CHANGE**
A-136 *Balance Sheet*	A-136 clarifies reporting of Fund Balance with Treasury to include "Other Fund Types."
A-136 *Statement of Financing*	A-136 reclassifies the Statement of Financing from a principal statement to a display in the footnotes.
A-136 *Notes to the Financial Statements*	A-136 adds a new disclosure requirement to Note 1 for Parent/child reporting (allocation transfers)
	New disclosure requirement on earmarked funds for which more than one component entity is responsible for a program financed with earmarked revenues.
	A-136 adds a new note to replace the Statement of Financing titled "Reconciliation of Net Cost of Operations to Budget."
	A-136 expands the information to be included in Restatement Note.

NEW FY 2006 OMB REPORTING REQUIREMENTS AND SFFASs	
OMB GUIDANCE	**DESCRIPTION OF CHANGE**
A-136 *Statement of Net Cost*	A-136 requires separate disclosure of Intragovernmental and public costs and revenues which is moved from the face of the Consolidated Statement of Net Cost to the footnote.
A-136 *Statement of Changes in Net Position*	A-136 changes the statement format, adding columns for earmarked funds and eliminations between earmarked funds and other reporting entity funds with disclosure in the Earmarked Funds footnote. Lines added to the statement for changes in accounting principles and corrections of errors per SFFAS 21.
A-136 *Statement of Custodial Activity*	Exchange revenue requirements added per SFFAS 7. Requirements for accrual adjustments for nonexchange revenue clarified.
A-136 *Notes to the Financial Statements*	Disclosure required for changes in GAAP that affect the financial statements, to include explanation of concepts that are unique to Federal financial statements. Modified the provisions for restatement to comply with paragraphs 20 and 26 of SFFAS 21. Modified the Fund Balance with Treasury footnote to include non-budgetary FBWT in section B, Status of Fund Balance with Treasury (FY 2005). Added earmarked funds to note on investments and added note for earmarked funds per SFFAS 27, replacing the note on Dedicated Collections.
A-136 *RSI*	Removed intragovernmental amounts and segment information sections. Risk assumed information removed from RSSI and included in RSI per SFFAS 5. Stewardship PP&E condition information may be moved from the RSI and reported with deferred maintenance. Deferred maintenance additional guidance added from SFFAS 6.
A-136 *RSSI*	Removed all sections on heritage assets and stewardship land to be reclassified as basic information in the RSI, except for condition information.
SFFAS	**DESCRIPTION OF CHANGE**
SFFAS 27 Earmarked Funds	**Balance Sheet:** Separate lines added for Cumulative Results of Operations and Unexpended Appropriations for earmarked funds. As directed by SFFAS 27, the Department did not restate prior periods of the principal financial statements and related disclosures. **Statement of Changes in Net Position:** Separate display and lines added for earmarked funds. **Footnotes:** Information on earmarked funds added to Investments footnote (sample footnote provided in SFFAS 27). Disclosure required of all earmarked funds for which the reporting entity has program management responsibility.
SFFAS 29 *Heritage Assets and Stewardship Land*	**Balance Sheet:** Line added for Stewardship PP&E without an asset dollar amount and with footnote disclosure. **Footnotes:** New footnote added with requirements phased in starting with FY 2006. Disclosure explains how these assets relate to the entity's mission and a description of the entity's stewardship policies. In FY 2008, footnote will include a description of the major categories of heritage assets and physical unit information. In FY 2009, disclosure will include physical units added and withdrawn during the year and a description of methods of acquisition and withdrawal. **Cost of Stewardship PP&E:** The cost of acquiring, constructing, improving, reconstructing, or renovating heritage assets (other than multi-use heritage assets), and the cost of acquiring stewardship land and any costs to prepare stewardship land for its intended use, recognized as a cost in the Statement of Net Cost in the period in which it is incurred, reported separately on the face of the statement or in the footnotes.

Change in Accounting Estimate

The Department's Bureau of International Narcotics and Law Enforcement (INL) operates aircraft used to carry out INL's mission worldwide (see Note 1 Property and Equipment – Personal Property). As part of these activities, in 2005, the Department determined that major aircraft components – high dollar value items (replacement cost in excess of $50,000) that are repairable (e.g., engines) and in serviceable condition (ready for use) – should be treated as general property and equipment and as such capitalized and depreciated over the life of the asset once installed on an aircraft. In 2006, the Department conducted additional analysis to determine the actual useful life of the major components once installed on the aircraft. The analysis determined that the actual useful life is less than two years, and as such does not meet the definition of general property and equipment as provided for in SFFAS No. 6, *Accounting for Property, Plant and Equipment,* paragraph 17. Nor do these major components meet the definition of inventory as provided for in SFFAS No. 3, *Accounting for Inventory and Related Property,* paragraph 17. Consequently, for 2006, the Department changed the treatment of the major components to the purchase method. The estimated historical cost for the major components was $13.2 million at September 30, 2005, which was recorded to expense during 2006.

Change in Reporting of Program Costs on the Consolidated Statement of Net Cost

The Departments strategic goals were changed effective FY 2007 to align them in conformance with the five objectives of foreign assistance reform. The seven strategic goals, as provided in the DOS/USAID Joint Strategic Plan covering Fiscal Years 2007 thru 2012, constitute the strategic planning framework for the Department. This framework, and the Foreign Assistance Strategic Framework with which it is consistent, serves as the basis for the Department's annual performance plans. Accordingly, amounts reported in the Consolidated Statement of Net cost for FY 2007 reflects the implementation of the new strategic goals. Amounts for FY 2006 have been reclassified to align with the new strategic goals.

3 ASSETS

The Department's assets are classified as entity assets and non-entity assets. Entity assets are those assets that the Department has authority to use for its operations. Non-entity assets are those held by the Department but are not available for use in its operations. The vast majority of the Department's assets are entity assets. Total non-entity assets at September 30, 2007and 2006 were $13.8 million and $12.7 million, respectively, for amounts in the Chancery Development Trust Account. These items are included in amounts reported as Cash and Other Monetary Assets (See Note 7, " Cash and Other Monetary Assets " for further information).

4 FUND BALANCES WITH TREASURY

Fund Balances with Treasury at September 30, 2007 and 2006, are summarized below (Dollars in Thousands).

Fund Balances	2007	2006
Appropriated Funds	$ 19,220,025	$ 15,573,572
Revolving Funds	388,106	490,436
Trust Funds	99,177	105,135
Special Funds	10,518	13,173
Deposit & Receipt Accounts	61,172	(11,555)
Total	$ 19,778,998	$ 16,170,761

Status of Fund Balance	2007	2006
Unobligated Balances		
Available	$ 5,462,256	$ 4,803,003
Unavailable	290,293	484,145
Obligated Balances not yet Disbursed	$ 13,965,277	10,895,168
Total Unobligated and Obligated	$ 19,717,826	$ 16,182,316
Deposit & Receipt Accounts	61,172	(11,555)
Total	$ 19,778,998	$ 16,170,761

5 INVESTMENTS

Summary of Investments

Investments at September 30, 2007 and 2006 are summarized below (Dollars in Thousands). All investments are classified as Intragovernmental.

At September 30, 2007:	Par	Unamortized Premium (Discount)	Investments (Net)	Market Value	Maturity Dates	Interest Rates Range	Interest Receivable
Non-Marketable, Par Value:							
Special Issue Securities	$ 14,377,713	$ —	$ 14,377,713	$ 14,377,713	2008-2022	3.50%-7.25%	$ 194,371
Subtotal	$ 14,377,713	$ —	$ 14,377,713	$ 14,377,713			$ 194,371
Non-Marketable, Market Based:							
Israeli-Arab Scholarship, Notes	4,723	(1)	4,722	4,753	2008	4.75%-5.00%	64
Eisenhower Exchange Fellowship, Notes	7,567	(12)	7,555	7,593	2008-2015	3.25%-6.00%	43
Middle Eastern–Western Dialogue, Note	17,100	396	17,496	17,464	2008-2010	3.375%-6.50%	227
Gift Funds, Bills	5,005	(44)	4,961	4,972	2007	1.93%	—
Subtotal	$ 34,395	$ 339	$ 34,734	$ 34,782			$ 334
Total Investments	$ 14,412,108	$ 339	$ 14,412,447	$ 14,412,495			$ 194,705

At September 30, 2006:	Par	Unamortized Premium (Discount)	Investments (Net)	Market Value	Maturity Dates	Interest Rates Range	Interest Receivable
Non-Marketable, Par Value:							
Special Issue Securities	$ 13,875,717	$ —	$ 13,875,717	$ 13,875,717	2007-2021	3.50%-7.375%	$ 191,762
Subtotal	$ 13,875,717	$ —	$ 13,875,717	$ 13,875,717			$ 191,762
Non-Marketable, Market Based:							
Israeli-Arab Scholarship, Notes	4,723	11	4,734	4,732	2006-2008	3.125%-6.625%	80
Eisenhower Exchange Fellowship, Notes	7,521	(8)	7,513	7,505	2007-2014	3.25%-6.25%	45
Middle Eastern–Western Dialogue, Note	17,096	556	17,652	17,406	2006-2010	2.25%-6.625%	294
Gift Funds, Bills	4,005	(37)	3,968	3,970	2006	2.41%	—
Subtotal	$ 33,345	$ 522	$ 33,867	$ 33,613			$ 419
Total Investments	$ 13,909,062	$ 522	$ 13,909,584	$ 13,909,330			$ 192,181

The Department's activities that have the authority to invest cash resources are earmarked funds (see Note 15 "Earmarked Funds"). The Federal Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash receipts collected from the public for an earmarked fund are deposited in the U.S. Treasury, which uses the cash for general Government purposes. Treasury securities are issued to the Department as evidence of its receipts. Treasury securities are an asset to the Department and a liability to the U.S. Treasury. Because the Department and the U.S. Treasury are both parts of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Government-wide financial statements.

Treasury securities provide the (component entity) with authority to draw upon the U.S. Treasury to make future benefit payments or other expenditures. When the Department requires redemption of these securities to make expenditures, the Government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the Government finances all other expenditures.

Although funds in the Chancery Development Trust Account and the Bosnia Federation Defense Fund are invested, because they are considered non-entity assets the investments for these funds are not shown in this section, but are described in Note 7, " Cash and Other Monetary Assets."

6 ACCOUNTS AND LOANS RECEIVABLE, NET

The Department's Accounts Receivable and Loans Receivable at September 30, 2007and 2006 are summarized here (Dollars in Thousands). All are entity receivables.

	2007			2006		
	Entity Receivables	**Allowance for Uncollectible**	**Net Receivables**	**Entity Receivables**	**Allowance for Uncollectible**	**Net Receivables**
Intragovernmental Accounts Receivable	$ 407,521	$ (15,961)	$ 391,560	$ 359,998	$ (15,960)	$ 344,038
Non-Intragovernmental Accounts and Loans Receivable	43,132	(10,598)	32,534	42,726	(8,407)	34,319
Total Receivables	$ 450,653	$ (26,559)	$ 424,094	$ 402,724	$ (24,367)	$ 378,357

Included in Non-Intragovernmental Accounts and Loans Receivable are approximately $551 thousand and ($123) thousand, in 2007 and 2006, respectively, of Repatriation Loans administered by the Department. Repatriation Loans enable destitute American citizens overseas to return to the United States. Repatriation loans made prior to 1992 are reported net of an allowance for uncollectible loans based upon historical experience. The Federal Credit Reform Act of 1990 (the Act), as amended, governs Repatriation loan obligations made after 1991, and the resulting direct loans. The Act requires that the present value of all direct costs (i.e., interest rate differentials, estimated delinquencies and defaults) associated with a loan be recognized and funded completely in the year the loan is disbursed. This value is termed the "subsidy cost" for the year, and is expressed as a percentage of the total face amount of loans disbursed that year. Funding for subsidy costs for loans made after 1991 establishes the subsidy allowance against which future collections and future loan write-offs are netted. In FY 2006, the subsidy was greater than the loans outstanding. Per the provisions of the Act, the Department borrows from Treasury the difference between the face value of loans disbursed and their calculated subsidy costs. The administrative costs associated with loan administration are separately budgeted and funded.

7 CASH AND OTHER MONETARY ASSETS

The Cash and Other Monetary Assets at September 30, 2007 and 2006, are summarized below (Dollars in Thousands). There are no restrictions on entity cash. Non-Entity cash is restricted as discussed below.

	2007			2006		
	Entity Assets	Non-Entity Assets	Total	Entity Assets	Non-Entity Assets	Total
Hurricane Katrina Relief Efforts	$ —	$ —	$ —	$ —	$ —	$ —
Chancery Development						
Trust Account:						
Treasury Bills, at par	—	$13,785	$13,785	—	12,905	12,905
Unamortized Discount	—	(18)	(18)	—	(205)	(205)
Cash-Imprest and Other Funds	46,615	—	46,615	35,966	—	35,966
Total	$ 46,615	$ 13,767	$ 60,382	$ 35,966	$ 12,700	$ 48,666

Lease fees collected from foreign governments by the Department for the International Chancery Center are deposited into an escrow account called the Chancery Development Trust Account. The funds are unavailable to the Department at time of deposit, and do not constitute expendable resources until funds are necessary for additional work on the Center project. The Chancery Development Trust account invests in six-month marketable Treasury bills issued at discount and redeemable for par at maturity. A corresponding liability for these amounts is reflected as Funds Held in Trust and Deposit Accounts.

8 PROPERTY AND EQUIPMENT, NET

Property and equipment balances at September 30, 2007 and 2006, are shown in the following table (Dollars in Thousands):

	2007			2006		
Major Classes	Cost	Accumulated Depreciation	Net Value	Cost	Accumulated Depreciation	Net Value
Real Property:						
Overseas —						
Land and Land Improvements	$ 2,107,572	$ (7,435)	$ 2,100,137	$ 2,013,634	$ (1,650)	$ 2,011,984
Buildings and Structures	7,891,766	(3,309,772)	4,581,994	6,849,444	(3,080,559)	3,768,885
Construction-in-Progress	2,076,123	—	2,076,123	1,940,647	—	1,940,647
Assets Under Capital Lease	77,194	(31,195)	45,999	76,503	(29,704)	46,799
Leasehold Improvements	347,142	(153,606)	193,536	306,367	(88,323)	218,044
Domestic —						
Structures, Facilities and Leaseholds	590,308	(246,818)	343,490	586,352	(232,387)	353,965
Construction-in-Progress	18,362	—	18,362	21,007	—	21,007
Land and Land Improvements	80,967	(5,399)	75,568	80,782	(5,086)	75,696
Subtotal — Real Property	$ 13,189,434	$ (3,754,225)	$ 9,435,209	$ 11,874,736	$ (3,437,709)	$ 8,437,027
Personal Property:						
Aircraft	$ 643,342	$ (343,935)	$ 299,407	$ 624,452	$ (297,018)	$ 327,434
Vehicles	401,645	(241,930)	159,715	334,095	(192,692)	141,403
Communication Equipment	53,452	(45,170)	8,282	52,158	(42,959)	9,199
ADP Equipment	63,567	(45,739)	17,828	59,585	(42,321)	17,264
Reproduction Equipment	12,883	(10,376)	2,507	13,218	(10,005)	3,213
Security	90,927	(55,134)	35,793	92,770	(52,037)	40,733
Software	287,319	(164,207)	123,112	199,558	(123,402)	76,156
Software-in-Development	53,973	—	53,973	121,468	—	121,468
Other Equipment	222,077	(159,448)	62,629	212,187	(210,167)	2,020
Subtotal — Personal Property	$ 1,829,185	$ (1,065,939)	$ 763,246	$ 1,709,491	$ (970,601)	$ 738,890
Total	$ 15,018,619	$ (4,820,164)	$ 10,198,455	$ 13,584,227	$ (4,408,310)	$ 9,175,917

Stewardship PP&E

The Department has collections of art, furnishings and real property (Culturally Significant Property) that are held for public exhibition, education, and official entertainment for visiting Chiefs of State, Heads of Government, Foreign Ministers, and other distinguished foreign and American guests. As the lead institution in the conduct of American diplomacy, this property is used to promote national pride and the distinct cultural diversity of American artists and to recognize the historical, architectural and cultural significance of the Department's overseas operations.

The Department has six separate collections of art and furnishings: the Diplomatic Reception Rooms, the Art Bank, Art in Embassies, Curatorial Services Program, the Library Rare and Special Book Collection, and the Secretary of State's Register of Culturally Significant Property. The collections, described in the Required Supplementary Information (RSI) section of this report, consist of items that were donated, purchased using donated or appropriated funds, or are on loan from individuals, organizations, or museums. The Department provides protection and preservation services for these collections.

The stewardship PP&E items that the Department owns are considered heritage assets (see "Required Supplementary Information — Heritage Assets"). In accordance with SFFAS No. 29, *Heritage Assets and Stewardship Land,* no value is assigned to these assets in the Consolidated Balance Sheet. Purchases of items for collections are recorded as an expense in the year of purchase. Proceeds from disposals are recognized as revenue in the year of sale and are designated for future collection acquisitions.

9 OTHER ASSETS

The Department's other assets at September 30, 2007 and 2006, are summarized below (Dollars in Thousands).

	2007	2006
Salary Advances to Employees	$ 9,126	$ 9,536
Travel Advances to Employees	10,807	12,566
Other Advances and Prepayments	138,442	52,897
Inventory Held for Current Sale	6,373	7,489
Total Other Assets	$ 164,748	$ 82,488

10 LIABILITIES

The Environmental Liabilities on the Balance Sheet at September 30, 2007 and 2006 were $392.3 million, and represent the estimated cost of upgrades, constructions, and projected operation and maintenance costs of wastewater treatment plants owned and operated by IBWC. Other Liabilities on the Balance Sheet at September 30, 2007 and 2006 were $1,345.6 million and $876.4 million, respectively, and consist of the following.

	2007	2006
Accrued Annual Leave	254,093	237,949
Funds Held in Trust and Deposit Accounts	13,767	12,700
Accrued Salaries Payable	124,503	112,856
Federal Employees Compensation Act Benefits	68,078	62,669
Pension Benefits Payable	50,455	48,164
Capital Lease Liability	60,384	59,466
Deferred Revenues	657,223	288,061
Other	117,100	54,561
Total Other Liabilities	$ 1,345,603	$ 876,426

The Department's liabilities are classified as covered by budgetary resources or not covered by budgetary resources. Liabilities not covered by budgetary resources result from the receipt of goods and services, or occurrence of eligible events in the current or prior periods, for which revenue or other funds to pay the liabilities have not been made available through appropriations or current earnings of the Department. The liabilities in this category at September 30, 2007 and 2006, are summarized below (Dollars in Thousands).

	2007	2006
Liability to International Organizations	1,476,596	1,155,344
Environmental Liabilities	392,300	392,300
Foreign Service Retirement Actuarial Liability	208,982	193,430
Other Liabilities:		
Accrued Annual Leave	254,093	237,949
Funds Held in Trust and Deposit Accounts	13,767	12,700
Federal Employees Compensation Act Benefits	68,078	62,669
Capital Lease Liability	60,384	59,466
Intragovernmental Other	17,637	14,541
Total Liabilities Not Covered By Budgetary Resources	$ 2,491,837	$ 2,128,399
Total Liabilities Covered By Budgetary Resources	$ 17,401,286	$ 15,764,648
Total Liabilities	$ 19,893,123	$ 17,893,047

11 FOREIGN SERVICE RETIREMENT ACTUARIAL LIABILITY

The Foreign Service Retirement and Disability Fund finances the operations of the FSRDS and the FSPS. The FSRDS and the FSPS are defined-benefit single-employer plans. FSRDS was originally established in 1924; FSPS in 1986.The 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 the Thrift Savings Plan.

The Department's financial statements present the Pension Actuarial Liability of the Foreign Service Retirement and Disability Program (the "Plan") as the actuarial present value of projected plan benefits, as required by the SFFAS No. 5, *Accounting for Liabilities of the Federal Government.* The Pension Actuarial Liability represents the future periodic payments provided for current employee and retired Plan participants, less the future employee and employing Federal agency contributions, stated in current dollars.

Future periodic payments include benefits expected to be 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 of employees 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 calculated by applying actuarial assumptions to adjust the projected plan benefits to reflect the discounted time value of money 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. The economic assumptions used for the valuation (other than the assumed merit salary increases) match the economic assumptions approved by the Board of Actuaries of the Civil Service Retirement and Disability Fund for use in performing the dynamic actuarial valuations of CSRS and FERS. All the other assumptions used for the valuation are based upon the actual past experience of the covered lives under the two retirement systems. . The Plan uses the aggregate entry age normal actuarial cost method, whereby the present value of projected benefits for each employee is allocated on a level basis (such as a constant percentage of salary) over the employee's service between entry age and assumed exit age. The portion of the present value allocated to each year is referred to as the normal cost.

The Board of Actuaries economic assumptions since the last valuation did not change. The general salary increase remained at 4.25% and the inflation rate stayed at 3.50%. Based on the economic assumptions, the plan actuary kept the normal cost percentages the same. The table below presents the normal costs for FY 2007 and FY 2006.

	FY 2007	FY 2006
Normal Cost:		
FSRDS	30.35%	30.35%
FSPS	25.38%	25.38%

Actuarial assumptions are based on the presumption that the Plan will continue. If the Plan terminates, different actuarial assumptions and other factors might be applicable for determining the actuarial present value of accumulated plan benefits. The following table presents the calculation of the combined FSRDS and FSPS Pension Actuarial Liability and the assumptions used in computing it for the years ended September 30, 2007 and 2006 (Dollars in Thousands).

For the Year Ended September 30,	2007	2006
Pension Actuarial Liability, Beginning of Year	$ 14,215,300	$ 13,429,300
Add Pension Expense:		
Normal Cost	298,900	274,800
Interest on Pension Liability	874,400	826,000
Prior Service Costs	—	—
Actuarial Losses/(Gains)	93,300	386,100
Total Pension Expense	1,266,600	1,486,900
Less Payments to Beneficiaries (annuities and refunds)	(753,200)	(700,900)
Pension Actuarial Liability, End of Year	14,728,700	14,215,300
Less: Net Assets Available for Benefits	(14,519,718)	(14,021,870)
Actuarial Unfunded Pension Liability for Projected Plan Benefits	$ 208,982	$ 193,430
Actuarial Assumptions:		
Rate of Return on Investments	6.25%	6.25%
Rate of Inflation	3.50%	3.50%
Salary Increase	4.25%	4.25%

Net Assets Available for Benefits at September 30, 2007 and 2006, consist of the following (Dollars in Thousands):

	2007	2006
Fund Balances with Treasury	$ 467	$ 2,070
Receivables	9,683	9,552
Interest Receivable	194,371	191,762
Investments in USG Securities	14,377,713	13,875,717
Total Assets	14,582,234	14,079,101
Less: FSRDF Liabilities	(62,516)	(57,231)
Net Assets Available for Benefits	$ 14,519,718	$ 14,021,870

12 LIABILITIES TO INTERNATIONAL ORGANIZATIONS

The Department reports an unfunded liability for the accumulated arrears assessed by the United Nations (UN), its affiliated agencies, and other international organizations in the amount of $60.0 million for both 2007 and 2006 for regular budget assessments and international peacekeeping. These financial commitments mature into obligations (as that term is used in domestic law) only when funds are authorized and appropriated by Congress.

The financial statements also report an unfunded liability of $ 1.417 billion and $1.095 billion at September 30, 2007 and 2006, respectively, for the current year 2007 and 2006 unfunded or restricted annual assessments from the United Nations, its affiliated agencies and several other international organizations, as well as for peacekeeping. It has been the Department's policy to pay annual assessments for the UN and certain international organizations out of the following fiscal year's appropriation, usually in the last quarter of the calendar year (i.e., the 2007 calendar year assessment is paid from the Department's 2008 appropriation). The Liability to International Organizations at September 30, 2007 and 2006 is summarized below (Dollars in Thousands).

	2007	2006
Accumulated Arrears	$ 60,029	$ 60,029
Unfunded Annual Assessments	1,416,567	1,095,315
Liability to International Organizations	$ 1,476,596	$ 1,155,344

13 LEASES

The Department is committed to over 13,000 leases, which cover office and functional properties, and residential units at diplomatic missions overseas. The majority of these leases are short-term operating leases. In most cases, management expects that the leases will be renewed or replaced by other leases. Personnel from other US Government agencies occupy some of the leased facilities (both residential and non-residential). These agencies reimburse the Department for the use of the properties. Reimbursements are received for approximately $68.1m 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 in accordance with SFFAS No. 6, *Accounting for Property, Plant, and Equipment*. Assets that meet the definition of a capital lease and their related lease liability are initially recorded at the present value of the future minimum lease payments or fair market value, whichever is less. In general, capital asses are depreciated over the estimated remaining life of the asset, and the related liability is amortized over the term of the lease, which can result in a different value in the asset versus the liability.

The following is a summary of Net Assets under Capital Leases and Future Minimum Lease payments as of September 30, 2007 (Dollars in Thousands).

	2007	2006
Net Assets Under Capital Leases:		
Land and Buildings	$ 77,194	$ 76,503
Accumulated Depreciation	(31,195)	(29,704)
Net Assets under Capital Leases	$ 45,999	$ 46,799

Future Minimum Lease Payments:

	2007		2006	
	Fiscal Year	Lease Payments	Fiscal Year	Lease Payments
	2008	$ 3,685	2007	$ 3,636
	2009	4,065	2008	3,685
	2010	3,738	2009	4,065
	2011	4,218	2010	3,738
	2012	3,842	2011	4,218
	2013 and thereafter	143,584	2012 and thereafter	147,426
Total Minimum Lease Payments		$ 163,132		$ 166,768
Less: Amount Representing Interest		(102,748)		(107,302)
Obligations under Capital Leases		$ 60,384		$ 59,466

Operating Leases

The Department leases real property in overseas locations under operating leases. These leases expire in various years. Minimum future rental payments under operating leases have remaining terms in excess of one year as of September 30, 2007 for each of the next 5 years and in aggregate are as follows (Dollars in Thousands).

Year Ended September 30	Operating Lease Amounts
2008	$ 591,314
2009	448,839
2010	273,010
2011	170,809
2012	82,421
2013 and thereafter	184,118
Total Minimum Future Lease Payments	$ 1,750,511

14 COMMITMENTS AND CONTINGENCIES

Commitments

In addition to the future lease commitments discussed in Note 13, "Leases," the Department is committed under obligations for goods and services which have been ordered but not yet received (undelivered orders — see Note 17, "Statement of Budgetary Resources") at fiscal year end. In FY 2005 appropriations, the Department of State received $6 million to subsidize the cost of a direct loan of up to $1.2 billion to the United Nations to cover the cost of renovating its headquarters in New York City. As of the date of this Report, the loan agreement had not been ratified.

Contingencies

Counter-Terrorism Rewards (a.k.a. Rewards for Justice), Narcotics Rewards and War Crimes Rewards Programs. The Department operates rewards programs for information critical to combating international terrorism, narcotics trafficking, and war crimes. The Rewards for Justice Program can offer rewards [we recommend deleting references to limitations on the amount of funds because there is no statutory cap; instead, by regulation, the Secretary has to approve awards above a certain amount] for information leading to: the arrest or conviction in any country of persons committing (or conspiring or attempting to commit, or aiding or abetting the commission of) acts of international terrorism against United States persons or property; the prevention, frustration or favorable resolution of such acts; the identification or location of key leaders of a terrorist organization; or the disruption of financial mechanisms of a foreign terrorist organization. The Narcotics Rewards Program has the authority under 22 U.S.C. 2708 to offer rewards for information leading to: the arrest or conviction in any country of persons committing (or conspiring or attempting to commit, or aiding and abetting the commission of) major foreign violations of U.S. narcotics laws or the killing or kidnapping of U.S. narcotics law enforcement officers or their family members; or the prevention, frustration or favorable resolution of such criminal acts. The War Crimes Information Rewards Program currently offers rewards for information leading to the arrest, transfer, or conviction of persons indicted by the International Criminal Tribunal for the Former Yugoslavia or the International Criminal Tribunal for Rwanda for serious violations of international humanitarian law, or their arrest or conviction in any country for such violations. Authority exists to create a similar war crimes program for information related to indictees of the Special Court of Sierra Leone.

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

Claims Filed in Response to Embassy Bombings: Nearly 4,000 Kenyan nationals filed administrative tort claims against the Department alleging that Department negligence was responsible for the damages they suffered when terrorists bombed the American Embassy in Nairobi, Kenya on August 7, 1998. These claims are for sums ranging from $150 to $10,000,000 and total approximately $1.5 billion. Two lawsuits, in the amounts of $1 billion and $500 million, arising from these tort claims were dismissed this year by the Federal District Court in Washington, D.C. Both of the cases have been appealed to the D.C. Circuit Court of Appeals. After that court affirmed the District Court's dismissal of the $1 billion action in July 2003, the plaintiffs in the other, almost identical, suit abandoned their appeal. The plaintiffs in the first case have petitioned the Supreme Court for certiorari, which was denied.

In addition, the families of eleven of the twelve Americans killed in the bombing also filed administrative tort claims with the Department alleging that Department negligence led to the death of their family members in Nairobi. These claims, including those by the estates of the deceased, are for a total of $117 million. Recent Supreme Court jurisprudence has ruled out liability under the Act for injuries or deaths suffered abroad. We are reviewing the claims under the Secretary's discretion as authorized by the Basic Authorities Act and in conjunction with proposed litigation for compensation to victims of terrorism. Any settlements made under the Secretary's discretionary authority in excess of $2,500 would be funded and paid from the Judgment Fund maintained by the Treasury.

North American Free Trade Agreement (NAFTA) Arbitrations: The United States is currently defending itself against more than one hundred claims submitted to arbitration – and facing approximately $1.1 billion in potential liability – under chapter Eleven (investment) of the North American Free trade Agreement (NAFTA). The United States also has received two notices of intent to submit claims to arbitration, in the amounts of $513 million and $8 million, respectively. The United States has successfully defended itself against four individual claims and one consolidated claim (involving three claimants) submitted to arbitrations. Any adverse award in any of these cases would be paid out of the Judgment Fund.

Fluor Intercontinental Inc. (Astana Embassy Project): The claimant has asserted three claims, totaling $36,032,537, for work on one contract in building the new embassy compound in Astana, Kazakhstan related to the installation of piles for the foundation, the perimeter wall, and the impact of the alleged delay in the construction of the infrastructure. The Contracting Officer has denied the claims, and the Department awaits appeal of the denial. Claimant is unlikely to be able to provide its claims, which appear to be very inflated. It is not possible at this time to accurately access within a predictable range the estimated amount of losses which would be probable or reasonably possible.

Fluor Intercontinental Inc. (Kingston Embassy Project): Claimant is seeking return of $12.2 million in two separate claims for alleged Government delay in the construction of the new embassy compound in Kingston, Jamaica. The Contracting Officer has denied the claims, and the claimant has appealed to the Civilian Board of Contract Appeals. Because the issues are complex and depend in part on schedule analysis, it is not possible at this time to assess within a predictable range the estimated amount of losses which would be probable or reasonably possible.

Fluor Intercontinental Inc. (Frankfurt Project): Flour Intercontinental has asserted numerous discrete claims pertaining to renovation of Air Force Hospital in Frankfurt for use as the Consulate General, plus large delay and constructive acceleration claims said to arise from impact of the discrete claims on the construction schedule. The total amount of the global claim is anticipated to be approximately $18.4 million. This claim has now been settled for $4.2 million, plus interest, to be paid from the Judgment Fund.

Inversa, S.A. (Leases): Claimant has asserted $45 million in claims arising out of the lease of the Embassy Panama office building annex between 1990 and 2004 and a claimed breach of a letter of intent to lease housing units. The untimely termination claim (approximately $275,000) decided in favor of the lessor by the Court of Federal Claims will be paid from the Judgment Fund ($241, 000 plus interest) when the quantum is agreed upon or determined by the Court of Federal Claims. The Civilian Board of Contract Appeals granted summary judgment in favor of the Government on Inversa's $30 million claim for breach of the letter of intent. The remaining claims, which amount to just under $10 million, are currently scheduled to go to trial in the Civilian Board of Contract Appeals next February. The claimant's appeals of claims denied by the court of Federal Claims are likely to fail.

Zachry Caddell Joint Venture (Beijing Embassy Project): Claimant has asserted two overarching claims and one Request for Equitable Adjustment, totaling $35,202,899, concerning multiple aspects of the new embassy compound in Beijing, China. The two claims are in litigation at the Board of Contract Appeals, but that litigation has been stayed pending action on the Request for Equitable Adjustment. The contracting officer has settled a number of the direct cost claims, but about $30 million in claims remain outstanding. The Department received the Request for Equitable Adjustment in July 2007 and is preparing a response. It is not possible at this stage to assess within a predictable range the estimated amount of losses that would be probable or reasonably possible.

Chattler et al. v. United States of America: Plaintiffs filed a class action complaint against the United State and the Department on August 7, 2007. The putative plaintiff class seeks a refund of expedite fees, along with damages, prejudgment interest, and attorneys' fees arising from the Department's alleged failure to process within three days, and/or return within two weeks, passport applications for which an expedite fee was paid. The U.S. Government filed a motion to dismiss the complaint on October 9, 2007, and plans to contest the claims vigorously. The estimated amount or range of potential loss may be $50 million to $70 million.

Certain legal matters to which the Department is a party are administered and, in some instances, litigated and paid by other U.S. Government agencies. Generally, amounts to be paid under any decision, settlement, or award pertaining to these legal matters are funded from the Judgment Fund. None of the amounts paid under the Judgment Fund on behalf of the Department in 2006 and 2005 had a material effect on the financial position or results of operations of the Department.

15 EARMARKED FUNDS

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits or purposes, and accounted for separately from the Government's general revenues. See Note 5 "Investments" for further information on investments in U.S. Treasury securities for earmarked funds. There are no intradepartmental transactions between the various earmarked funds.

The Department administers thirteen earmarked funds as listed below. A brief description of the individually reported earmark funds and their purpose follows.

Treasury Fund Symbol	Description	Statute
19X5497	Foreign Service National Defined Contribution Fund	22 USC 3968(a)(1)
19X8166	American Studies Endowment Fund	108 Stat. 425
19X8167	Trust Funds	22 USC 1479
19X8186	Foreign Service Retirement and Disability Fund	22 USC 4042-4065
19X8271	Israeli Arab Scholarship Programs	105 Stat. 696, 697
19X8272	Eastern Europe Student Exchange Endowment Fund	105 Stat. 699
19X8340	Foreign Service National Liability Trust Fund	105 Stat. 672
19X8341	Foreign Service National Liability Trust Fund	105 Stat. 672
19X8812	Gifts and Bequests, National Commission on Educational, Scientific, and Cultural Cooperation	22 USC 287q
19X8813	Center for Middle Eastern-Western Dialogue Trust Fund	118 Stat. 84
19X8821	Unconditional Gift Fund	22 USC 809, 1046
19X8822	Conditional Gift Fund	22 809, 1046
95X8276	Eisenhower Exchange Fellowship Program Trust Fund	PL 101-454

Foreign Service National Defined Contributions Retirement Fund (FSNDCF) (19X5497)

The Foreign Service National Defined Contributions Retirement Fund is a retirement savings program designed to provide benefits upon separation to locally employed staff under local compensation plans at overseas U.S. diplomatic or consular missions or establishments. Contributions are made to the FSNDCF by the Department's appropriations from which the benefits are paid.

Foreign Service Retirement and Disability Fund (19X8186)

The Foreign Service Retirement and Disability Fund (FSRDF) was established in 1924 to provide pensions to retired and disabled members of the Foreign Service. The FSRDF's revenues consist of contributions from active participants and their U.S. Government agency employers; appropriations; and interest on investments. Monthly annuity payments are made to eligible retired employees or their survivors. Separated employees without title to an annuity may take a refund of their contributions. P.L. 96-465 limits the amount of administrative expense that can be charged to the fund to $5,000. The total cost for administering FSRDF was $4.3 million in both 2006 and 2005, respectively. Cash is invested in U.S. Treasury securities until it is needed for disbursement. The Department also issues separate annual financial statements for the FSRDF.

Foreign Service National Separation Liability Trust Funds (FSNSLTF) (19X8340 and 19X8341)

FSNSLTF funds separation liabilities to foreign service national (FSNs) and personal service contractor (PSCs) employees who voluntarily resign, retire, or lose their jobs due to a reduction in force. The liability is applicable only in those countries that, due to local law, require a lump-sum voluntary separation payment based on years of service. The FSNSLTF was authorized in 1991 and initially capitalized with a transfer from the Department. Contributions are made to the FSNSLTF by the Department's appropriations, from which the FSNs and PSCs are paid. Once the liability to the separating FSN or PSC is computed in accordance with the local compensation plan, the actual disbursement is made from the FSNSLTF.

Conditional and Unconditional Gift Funds (19X8821 and 19X8822)

The Department maintains two Trust Funds for receiving and disbursing donations. It is authorized to accept gifts from private organizations and individuals in the form of cash, gifts-in-kind, and securities. Gifts are classified as Restricted or Unrestricted Gifts.

Restricted Gifts must be used in the manner specified by the donor. Unrestricted Gifts can be used for any expense normally covered by an appropriation, such as representational purposes or embassy refurbishment.

(Dollars in Thousands)	FSRDF	FSNSLTF	FSNDCF	GIFT	Total - Other Earmarked	Total Earmarked Funds
Balance Sheet As of September 30, 2007:						
Assets:						
Fund Balances with Treasury	$ 467	$ 81,458	$ 55	$ 14,622	$ 2,630	$ 99,232
Investments	14,377,713	—	—	4,961	29,774	14,412,448
Taxes and Interest Receivable	194,371	—	—	—	334	194,705
Other Assets	9,683	—	45,247	1,864	—	56,794
Total Assets	**$ 14,582,234**	**$ 81,458**	**$ 45,302**	**$ 21,447**	**$ 32,738**	**$ 14,763,179**
Liabilities						
Actuarial Liability	$ 14,728,700	$ —	$ —	$ —	$ —	$ 14,728,700
Other Liabilities	62,515	—	61	(213)	9	62,372
Total Liabilities:	**$ 14,791,215**	**$ —**	**$ 61**	**$ (213)**	**$ 9**	**$ 14,791,072**
Net Position						
Unexpended Appropriations	$ —	$ —	$ —	$ —	$ —	$ —
Cumulative Results of Operations	(208,981)	81,458	45,241	21,660	32,729	(27,893)
Total Liabilities and Net Position	**$ 14,582,234**	**$ 81,458**	**$ 45,302**	**$ 21,447**	**$ 32,738**	**$ 14,763,179**
Statement of Net Cost for the Period Ended September 30:						
Gross Program Costs	$ —	$ 16,951	$ 3,894	$ 6,645	$ 2,251	$ 29,741
Less Earned Revenues	1,251,011	10,641	14,571	—	—	1,276,223
Net Program Costs	(1,251,011)	6,310	(10,677)	6,645	2,251	(1,246,482)
Costs Not Attributable to Program Costs	1,266,562	—	—	—	—	1,266,562
Less Earmed Revenues Not Attributable to Program Costs	—	—	—	—	—	—
Net Cost of Operations	$ 15,551	$ 6,310	$ (10,677)	$ 6,645	$ 2,251	$ 20,080
Statement of Changes in Net Position for the Period Ended September 30:						
Net Position Beginning of Period	$ (193,430)	$ 87,768	$ 34,564	$ 17,587	$ 33,687	$ (19,824)
Non-Exchange Revenue	$ —	$ —	$ —	$ 10,718	$ 1,293	$ 12,011
Other Financing Sources	—	—	—	—	—	—
Net Cost of Operations	(15,551)	(6,310)	10,677	(6,645)	(2,251)	(20,080)
Taxes and Other Nonexchange Revenue	—	—	—	—	—	—
Change in Net Position	$ (15,551)	$ (6,310)	$ 10,677	$ 4,073	$ (958)	$ (8,069)
Net Position End of Period	**$ (208,981)**	**$ 81,458**	**$ 45,241**	**$ 21,660**	**$ 32,729**	**$ (27,893)**

(Dollars in Thousands)	FSRDF	FSNSLTF	FSNDCF	GIFT	Total - Other Earmarked	Total Earmarked Funds
Balance Sheet As of September 30, 2006:						
Assets:						
Fund Balances with Treasury	$ 2,070	$ 87,768	$ 49	$ 11,925	$ 3,373	$ 105,185
Investments	13,875,717	—	—	3,968	29,899	13,909,584
Taxes and Interest Receivable	191,762	—	—	—	419	192,181
Other Assets	9,552	—	34,564	1,695	4	45,815
Total Assets	$ 14,079,101	$ 87,768	$ 34,613	$ 17,588	$ 33,695	$ 14,252,765
Actuarial Liability	$ 14,215,300	$ —	$ —	$ —	$ —	$ 14,215,300
Other Liabilities	57,231	—	49	1	8	57,289
Total Liabilities:	$ 14,272,531	$ —	$ 49	$ 1	$ 8	$ 14,272,589
Unexpended Appropriations	$ —	$ —	$ —	$ —	$ —	$ —
Cumulative Results of Operations	(193,430)	87,768	34,564	17,587	33,687	(19,824)
Total Liabilities and Net Position	$ 14,079,101	$ 87,768	$ 34,613	$ 17,588	$ 33,695	$ 14,252,765
Statement of Net Cost for the Period Ended September 30:						
Gross Program Costs	$ —	$ 12,491	$ 1,716	$ 4,155	$ 878	$ 19,240
Less Earned Revenues	1,220,904	10,464	8,539	—	—	1,239,907
Net Program Costs	(1,220,904)	2,027	(6,823)	4,155	878	(1,220,667)
Costs Not Attributable to Program Costs	1,486,862	—	—	—	—	1,486,862
Less Earmed Revenues Not Attributable to Program Costs	—	—	—	—	—	—
Net Cost of Operations	$ 265,958	$ 2,027	$ (6,823)	$ 4,155	$ 878	$ 266,195
Statement of Changes in Net Position for the Period Ended September 30:						
Net Position Beginning of Period	$ 72,528	$ 89,795	$ 27,741	$ 13,758	$ 28,440	$ 232,262
Non-Exchange Revenue	$ —	$ —	$ —	$ 7,984	$ 1,189	$ 9,173
Other Financing Sources	—	—	—	—	4,936	4,936
Net Cost of Operations	(265,958)	(2,027)	6,823	(4,155)	(878)	(266,195)
Taxes and Other Nonexchange Revenue	—	—	—	—	—	—
Change in Net Position	$ (265,958)	$ (2,027)	$ 6,823	$ 3,829	$ 5,247	$ (252,086)
Net Position End of Period	$ (193,430)	$ 87,768	$ 34,564	$ 17,587	$ 33,687	$ (19,824)

16 STATEMENT OF NET COST

The Consolidated Statement of Net Cost reports the Department's gross and net cost for its strategic objectives and strategic goals. The net cost of operations is the gross (i.e., total) cost incurred by the Department, less any exchange (i.e., earned) revenue.

The Consolidating Schedule of Net Cost categorizes costs and revenues by strategic goal and responsibility segment. A responsibility segment is the component that carries out a mission or major line of activity, and whose managers report directly to top management. For the Department, a Bureau (e.g., Bureau of African Affairs) is considered a responsibility segment. For presentation purposes, Bureaus have been summarized and reported at the Under Secretary level (e.g., Under Secretary for Political Affairs).

The presentation of program results by strategic objectives and strategic goals is based on the Department's current Strategic Plan established pursuant to the Government Performance and Results Act of 1993. The Department's strategic goals and strategic priorities are defined in Management 's Discussion and Analysis section of this report.

The Management and Organizational Excellence strategic goal relates to the Department's responsibilities for managing infrastructure, information, and human resources. The ability of the Department to advance national and foreign policy interests depends on the quality of these items — the two largest and most visible of which are Diplomatic Security and Overseas Buildings Operations.

DEPARTMENT OF STATE
CONSOLIDATING SCHEDULE OF NET COST

For the year ended September 30, 2007

(Dollars in Thousands)

STRATEGIC GOAL	Under Secretary for: Arms Control, Int'l Security	Economic, Business and Agriculture	Global Affairs	Political Affairs	Public Diplomacy and Public Affairs	Management-Consular Affairs	Eliminations	Total
Achieving Peace and Security								
Total Cost	$ 579,272	$ 16,915	$ 2,114,664	$ 3,338,226	$ 1,296	$ 83	$ (289,346)	$ 5,761,110
Earned Revenue	(100,753)	(2,883)	(621,803)	(413,043)	(28)	(13)	289,346	(849,177)
Net Program Costs	478,519	14,032	1,492,861	2,925,183	1,268	70	–	4,911,933
Governing Justly and Democratically								
Total Cost	104,085	3,039	43,469	595,897	–	15	(49,693)	696,812
Earned Revenue	(18,104)	(518)	(4,515)	(73,258)	–	(2)	49,693	(46,704)
Net Program Costs	85,981	2,521	38,954	522,639	–	13	–	650,108
Investing in People								
Total Cost	618,141	18,443	120,452	1,586,997	–	89	(22,391)	2,321,731
Earned Revenue	(8,168)	(233)	(2,037)	(33,035)	–	(1)	22,391	(21,083)
Net Program Costs	609,973	18,210	118,415	1,553,962	–	88	–	2,300,648
Promoting Economic Growth and Prosperity								
Total Cost	170,120	4,967	71,047	973,953	–	24	(81,220)	1,138,891
Earned Revenue	(29,589)	(847)	(7,380)	(119,735)	–	(4)	81,220	(76,335)
Net Program Costs	140,531	4,120	63,667	854,218	–	20	–	1,062,556
Providing Humanitarian Assistance								
Total Cost	–	–	1,102,220	(1,410)	294	–	(1,972)	1,099,132
Earned Revenue	–	–	(2,001)	0	(2)	–	1,972	(31)
Net Program Costs	–	–	1,100,219	(1,410)	292	–	–	1,099,101
Promoting International Understanding								
Total Cost	205,737	6,007	85,921	1,177,863	547,693	29	(98,225)	1,925,025
Earned Revenue	(35,784)	(1,024)	(8,925)	(144,802)	(59,136)	(5)	98,225	(151,451)
Net Program Costs	169,953	4,983	76,996	1,033,061	488,557	24	–	1,773,574
Strengthening Consular and Management Capabilities								
Total Cost	–	–	–	773,763	300,743	1,913,421	(378,375)	2,609,552
Earned Revenue	–	–	–	(167,666)	(46,501)	(2,826,200)	378,375	(2,661,992)
Net Program Costs	–	–	–	606,097	254,242	(912,779)	–	(52,440)
Executive Direction and Other Costs Not Assigned								
Total Cost	2,721	2,506	73,592	4,735,798	524,003	2,596	(1,868,930)	3,472,286
Earned Revenue	(1,674)	(1,541)	(45,267)	(3,056,791)	(325,328)	(1,570)	1,850,488	(1,581,683)
Net Program Costs	1,047	965	28,325	1,679,007	198,675	1,026	(18,442)	1,890,603
Total Cost	1,680,076	51,877	3,611,365	13,181,087	1,374,029	1,916,257	(2,790,152)	19,024,539
Total Revenue	(194,072)	(7,046)	(691,928)	(4,008,330)	(430,995)	(2,827,795)	2,771,710	(5,388,456)
Total Net Cost	$ 1,486,004	$ 44,831	$ 2,919,437	$ 9,172,757	$ 943,034	$ (911,538)	$ (18,442)	$13,636,083

Executive Direction and Other Costs Not Assigned relate to high-level executive direction (e.g., Office of the Secretary, Office of the Legal Adviser), international commissions, general management, and certain administrative support costs that cannot be directly traced or reasonably allocated to a particular program. For the year ended September 30, 2007 and 2006, these consist of costs and earned revenue summarized below (Dollars in Thousands).

	2007			2006		
Program	**Total Prior to Eliminations**	**Intra-Departmental Eliminations**	**Total**	**Total Prior to Eliminations**	**Intra-Departmental Eliminations**	**Total**
Costs:						
Executive Direction	$ 2,647,830	$ 466,418	$ 2,181,412	$ 2,591,920	$ 588,788	$ 2,003,132
FSRDF	1,266,562	440,746	825,816	1,486,863	397,920	1,088,943
ICASS	1,323,061	959,423	363,638	1,196,669	894,766	301,903
International Commissions	103,763	2,343	101,420	89,860	2,098	87,762
Total Costs	$ 5,341,216	$ 1,868,930	$ 3,472,286	$ 5,365,312	$ 1,883,572	$ 3,481,740
Earned Revenue:						
Executive Direction	$ 877,698	$ 466,418	$ 411,280	$ 632,366	$ 588,788	$ 43,578
FSRDF	1,251,011	422,304	828,707	1,220,904	372,407	848,497
ICASS	1,295,229	959,423	335,806	1,222,128	894,766	327,362
International Commissions	8,233	2,343	5,890	10,338	2,098	8,240
Total Earned Revenue	$ 3,432,171	$ 1,850,488	$ 1,581,683	$ 3,085,736	$ 1,858,059	$ 1,227,677
Total Net Cost for Executive Direction and Other Costs Not Assigned	$ 1,909,045	$ 18,442	$ 1,890,603	$ 2,279,576	$ 25,513	$ 2,254,063

Program Costs

These costs include the full cost of resources consumed by a program, both direct and indirect, to carry out its activities. Direct costs can be specifically identified with a program. Indirect costs include resources that are commonly used to support two or more programs, and are not specifically identified with any program. Indirect costs are assigned to programs through allocations. Full costs also include the costs of goods or services received from other Federal entities (referred to as inter-entity costs), whether or not the Department reimburses that entity.

Indirect Costs: Indirect costs consist primarily of Management and Organizational Excellence charges for central support functions performed in 2007 and 2006 under the Under Secretary for Management by the following organizations (Dollars in Thousands):

Bureau (or equivalent)	**2007**	**2006**
Bureau of Diplomatic Security	$ 1,484,899	$ 1,282,989
Office of Overseas Buildings Operations	339,466	776,887
Bureau of Administration	880,256	650,511
Bureau of Information Resource Management	283,728	358,036
Bureau of Personnel	279,752	465,596
Bureau of Resource Management	1,179,615	497,586
Foreign Service Institute	101,267	128,670
Medical Services and Other	229,418	168,849
Total Central Support Costs	$ 4,778,401	$ 4,329,124

These support costs were distributed to programs on the basis of a program's total base salaries for its full-time employees, as a percentage of total base salaries for all full-time employees, except for the Office of Overseas Buildings Operations. Since the Office of Overseas Buildings Operations supports overseas operations, its costs were allocated based on the percentage of budgeted cost by program for the regional bureaus. The distribution of support costs to programs in 2007 and 2006 was as follows (Dollars in Thousands):

Program Receiving Allocation	**2007**	**2006**
Achieving Peace and Security	$ 1,144,577	$ 1,056,117
Governing Justly and Democratically	198,737	181,166
Investing in People	89,548	81,631
Promoting Economic Growth and Prosperity	324,822	296,104
Providing Humanitarian Assistance	27	21
Promoting International Understanding	392,828	358,097
Strengthening Consular and Management Capabilities	1,079,557	999,480
Executive Direction and Other Costs Not Assigned	1,548,305	1,356,508
Total	$ 4,778,401	$ 4,329,124

Since the cost incurred by the Under Secretary for Management and the Secretariat are primarily support costs, these costs were distributed to the other Under Secretaries to show the full costs under the responsibility segments that have direct control over the Department's programs. One exception within the Under Secretary for Management is the Bureau of Consular Affairs, which is responsible for the American Citizens program. As a result, these costs were not allocated and continue to be reported as the Under Secretary for Management.

The Under Secretary for Management/Secretariat costs (except for the Bureau of Consular Affairs) were allocated to the other Department responsibility segments based on the percentage of total costs by organization for each program. The allocation of these costs to the other Under Secretaries and to the Bureau of Consular Affairs was as follows (Dollars in Thousands):

Under Secretary	**2007**	**2006**
Political Affairs	$ 6,342,670	$ 5,112,736
Public Diplomacy	825,582	710,975
Management (Consular Affairs)	973,493	696,395
Arms Control, International Security Affairs	1,084,311	336,902
Global Affairs	314,825	1,337,724
Economic, Business and Agriculture Affairs	33,897	29,092
Total	$ 9,574,778	$ 8,223,824

Inter-Entity Costs and Imputed Financing: To measure the full cost of activities, SFFAS No. 4, *Managerial Cost Accounting,* requires that total costs of programs include costs that are paid by other U.S. Government entities, if material. As provided by SFFAS No. 4, OMB issued a Memorandum in April 1998, entitled "Technical Guidance on the Implementation of Managerial Cost Accounting Standards for the Government." In that Memorandum, OMB established that reporting entities should recognize inter-entity costs for (1) employees' pension benefits; (2) health insurance, life insurance, and other benefits for retired employees; (3) other post-retirement benefits for retired, terminated and inactive employees, including severance payments, training and counseling, continued health care, and unemployment and workers' compensation under the *Federal Employees' Compensation Act;* and (4) payments made in litigation proceedings.

The Department recognizes an imputed financing source on the Statement of Changes in Net Position for the value of inter-entity costs paid by other U.S. Government entities. This consists of all inter-entity amounts as reported below except for the Federal Workers' Compensation Benefits (FWCB). For FWCB, the Department recognizes its share of the change in the actuarial liability for FWCB as determined by the Department of Labor (DoL). The Department reimburses DoL for FWCB paid to current and former Department employees.

The following inter-entity costs and imputed financing sources were recognized in the Statement of Net Cost and Statement of Changes in Net Position, respectively, for the years ended September 30, 2007 and 2006 (Dollars in Thousands):

Inter-Entity Cost	**2007**	**2006**
Other Post-Employment Benefits:		
Civil Service Retirement Program	$ 25,639	$ 24,867
Federal Employees Health Benefits Program	98,435	91,410
Federal Employees Group Life Insurance Program	299	287
Litigation funded by Treasury Judgment Fund	—	—
Subtotal – Imputed Financing Source	$ 124,373	$ 116,564
Future Workers' Compensation Benefits	17,637	16,873
Total Inter-Entity Costs	$ 142,010	$ 133,437

Intra-departmental Eliminations. Intra-departmental eliminations of cost and revenue were recorded against the program that provided the service. Therefore the full program cost was reported by leaving the reporting of cost with the program that received the service.

Earned Revenues

Earned revenues occur when the Department provides goods or services to the public or another Federal entity. Earned revenues are reported regardless of whether the Department is permitted to retain all or part of the revenue. Specifically, the Department collects but does not retain passport, visa, and certain other consular fees. Earned revenues for the year ended September 30, 2007 and 2006, consist of the following (Dollars in Thousands):

	2007			2006		
Program	**Total Prior to Eliminations**	**Intra-Departmental Eliminations**	**Total**	**Total Prior to Eliminations**	**Intra-Departmental Eliminations**	**Total**
Consular Fees:						
Passport, Visa and Other Consular Fees	$ 1,092,382	$ –	$ 1,092,382	$ 882,160	$ —	$ 882,160
Machine Readable Visa	740,458	–	740,458	693,051	—	693,051
Expedited Passport	314,677	–	314,677	177,853	—	177,853
Passport, Visa and other Surcharges	386,373	–	386,373	188,137	—	188,137
Fingerprint Processing, Diversity Lottery, and Affadavit of Support	24,258	–	24,258	28,414	—	28,414
Subtotal – Consular Fees	$ 2,558,148	$ –	$ 2,558,148	$ 1,969,615	$ —	$ 1,969,615
FSRDF	$ 1,251,011	$ 422,305	$ 828,706	$ 1,220,904	$ 361,943	$ 858,961
ICASS	1,295,229	959,424	335,805	1,222,128	894,766	327,362
Other Reimbursable Agreements	2,204,564	720,807	1,483,757	1,879,580	673,332	1,206,248
Working Capital Fund	744,284	643,408	100,876	524,274	377,520	146,754
Other	106,931	25,767	81,164	93,568	12,232	81,336
Total	$ 8,160,167	$ 2,771,711	$ 5,388,456	$ 6,910,069	$ 2,319,793	$ 4,590,276

Pricing Policies

Generally, a Federal agency may not earn revenue from outside sources unless it obtains specific statutory authority. Accordingly, the pricing policy for any earned revenue depends on the revenue's nature, and the statutory authority under which the Department is allowed to earn and retain (or not retain) the revenue. Earned revenue that the Department is not authorized to retain is deposited into the Treasury's General Fund.

The FSRDF finances the operations of the Foreign Service Retirement and Disability System (FSRDS) and the Foreign Service Pension System (FSPS). The FSRDF receives revenue from employee/employer contributions, a U.S. Government contribution, and interest on investments. By law, FSRDS participants contribute 7.25% of their base salary, and each employing agency contributes 7.25%; FSPS participants contribute 1.35% of their base salary and each employing agency contributes 20.22%. Employing agencies report employee/employer contributions biweekly. Total employee/employer contributions for 2007 and 2006 were $233.5 million and $224.0 million, respectively.

The FSRDF also receives a U.S. Government contribution to finance (1) FSRDS benefits not funded by employee/employer contributions; (2) interest on FSRDS unfunded liability; and (3) FSRDS disbursements attributable to military service. The U.S. Government contributions for 2007 and 2006 were $241.4 million and $231.3 million, respectively. FSRDF cash resources are invested in special non-marketable securities issued by the Treasury. Total interest earned on these investments in 2007 and 2006 was $776.1 million and $765.6 million, respectively.

Consular Fees are established primarily on a cost recovery basis and are determined by periodic cost studies. Reimbursable Agreements with Federal agencies are established and billed on a cost-recovery basis. ICASS billings are computed on a cost- recovery basis; billings are calculated to cover all operating, overhead, and replacement of capital assets, based on budget submissions, budget updates, and other factors. In addition to services covered under ICASS, the Department provides administrative support to other agencies overseas for which the Department does not charge. Areas of support primarily include buildings and facilities, diplomatic security (other than the local guard program), overseas employment, communications, diplomatic pouch, receptionist and selected information management activities. The Department receives direct appropriations to provide this support.

17 STATEMENT OF BUDGETARY RESOURCES

The Statement of Budgetary Resources reports information on how budgetary resources were made available and their status as of and for the years ended September 30, 2007 and 2006. Intra-departmental transactions have not been eliminated in the amounts presented.

The Budgetary Resources section presents the total budgetary resources available to the Department. For 2007 and 2006, the Department received approximately $31.0 billion and $26.4 billion in budgetary resources, respectively, primarily consisting of the following:

Source of Budgetary Resources	2007	2006
Budget Authority:		
Direct or related appropriations	$ 17.7 billion	$ 16.1 billion
Authority financed from Trust Funds	1.3 billion	1.3 billion
Spending authority from providing goods and services	6.8 billion	4.4 billion
Unobligated Balances – Beginning of Year	5.2 billion	4.3 billion
Other	—	0.3 billion
Total Budgetary Resources	$ 31.0 billion	$ 26.4 billion

The Department received permanent indefinite appropriations of $41.4 million and $42.5 million for 2007 and 2006, respectively. The permanent indefinite appropriation provides payments to the Foreign Service Retirement and Disability Fund to finance the interest on the unfunded pension liability for the year and disbursements attributable to military service. The amount of budgetary resources obligated for undelivered orders for all activities as of September 30, 2007 and 2006 was approximately $13.4 billion and $10.2 billion, respectively. This includes amounts of $419 million for September 30, 2007 and $396 million for September 30, 2006, pertaining to revolving funds, trust funds, and substantial commercial activities.

Information on U.S. Government agencies' budgets is reported in the *Budget of the United States Government, Fiscal Year 2009 – Appendix* (Appendix). The Appendix includes for each agency (including the Department), among other things, budget schedules for the agency's accounts. Information on budgetary resources and their status will be displayed in the *Program and Financing* (P&F) Schedule under each account. Amounts presented in the P&F Schedules are in millions of dollars. Each agency is responsible for submitting the data presented in the *P&F Schedules*. Amounts shown on the 2007 Statement of Budgetary Resources will differ from "2007 Actual" reported in the *P&F Schedules* for the Department's accounts as detailed in the schedule on the next page.

The *Appendix* is organized by major subordinate organizations or program areas within the agency, and then by the nature of account(s) (e.g., general, special, revolving, trust) within organization or program area. The Department's section consists of the following areas: Administration of Foreign Affairs, International Organizations and Conferences, International Commissions, Foreign Assistance, and Other. The Combining Schedule of Budgetary Resources appearing as Required Supplementary Information presents amounts in the Combined Statement of Budgetary Resources by these areas.

(Dollars in Millions):

	Budget Authority	Unobligated Balance Beginning of Year	Unobligated Balance End of Year	Obligations Incurred	Obligated Balance Beginning of Year	Obligated Balance End of Year	Net Outlays	Offsetting Receipts
FY 2007:								
International Security Assistance Programs	1,186	273	402	1,194	837	992	969	—
Undelivered Orders Adjustment	—	—	—	—	—	—	—	—
Expired Accounts Unobligated Balances	—	363	287	118	2,778	946	1,760	—
Undistributed Offsetting Receipts	—	—	—	—	—	—	—	1,069
Total FY 2007 Differences	1,186	636	689	1,312	3,615	1,938	2,729	1,069
FY 2006:								
International Security Assistance Programs	1,211	446	356	1,442	854	860	1,321	—
Undelivered Orders Adjustment	—	—	397	(187)	—	(397)	—	—
Expired Accounts Unobligated Balances	—	232	291	262	1,475	600	703	—
Undistributed Offsetting Receipts	—	—	—	—	—	—	—	861
Total FY 2006 Differences	1,211	678	1,044	1,517	2,329	1,063	2,024	861

The Statement of Budgetary Resources includes amounts the Department received in 2006 and 2005 to administer programs related to International Security Assistance. Amounts for these programs are not directly presented under the Department in the Appendix, but are reported in the Appendix under the section titled International Assistance Programs. In addition, the Statement of Budgetary Resources includes amounts of unavailable unobligated and obligated balances (primarily for expired annual accounts) that will not be reported in the Appendix. These unavailable unobligated balances in expired accounts (2005 and prior) remain available for adjustment, liquidation of obligations and other purposes authorized by law, until such accounts are closed as required by law and any remaining amounts will be returned to the General Fund of the U.S. Treasury. However, they are not available to incur new obligations since their period of availability to do such has expired.

18 CUSTODIAL ACTIVITY

The Department administers certain activities associated with the collection of non-exchange revenues, which are deposited and recorded directly to the General Fund of the Treasury. The Department does not retain the amounts collected. Accordingly, these amounts are not considered or reported as financial or budgetary resources for the Department. At the end of each fiscal year, the accounts are closed and the balances are brought to zero by Treasury. Specifically, the Department collects interest, penalties and handling fees on accounts receivable; fines, civil penalties and forfeitures; and other miscellaneous receipts. In 2007 and 2006, the Department collected $19.3 million and $37.2 million, respectively, in custodial revenues that were transferred to the Treasury.

19 RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

The Reconciliation of Net Cost of Operations to Budget reports the relationship between budgetary transactions and financial transactions.

(Dollars in Thousands) **For the Year Ended September 30,**	**2007**	**2006**
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 25,201,751	$ 21,145,813
Less: Spending Authority from offsetting collections and recoveries	(7,071,812)	(5,269,825)
Obligations net of offsetting collections and recoveries	18,129,939	15,875,988
Less: Offsetting receipts	(260,419)	(250,820)
Net obligations	17,869,520	15,625,168
Other Resources		
Donations and forfietures of property	10,669	7,819
Transfers in/out without reimbursement	(1,074,773)	(905,379)
Imputed financing from costs absorbed by others	124,373	116,564
Net other resources used to finance activities	(939,731)	(780,996)
Total Resources used to Finance Activities	**$ 16,929,789**	**$ 14,844,172**
Resources Used to Finance Items not Part of Net Cost of Operations:		
Change in budgetary resources obligated for goods, services, and benefits ordered but not yet received	3,029,996	1,295,410
Resources that fund expenses recognized in prior periods	246	56,908
Budgetary offsetting collections and receipts that do not affect net cost of operations		
Credit program collections which increase liabilities for loan guarantees or allowances for subsidy	1,453	1,480
Other	25	7,842
Resources that finance the acquisition of assets	1,021,848	1,775,898
Other resources or adjustments to net obligated resources that do not affect net cost of operations	–	384
Total Resources used to Finance Items not Part of the Net Cost of Operations	**4,053,568**	**3,137,922**
Total Resources Used to Finance the Net Cost of Operations	**$ 12,876,221**	**$ 11,706,250**
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components requiring or generating resources in future periods		
Increase in annual leave liability	$ 16,143	$ 13,548
Increase in actuarial liability	513,400	786,007
Other	327,455	1,070
Total components of Net Cost of Operations that will require or generate resources in future periods	856,998	800,625
Components not Requiring or Generating Resources:		
Depreciation and Amortization	478,357	584,732
Revaluation of assets or liabilities	40,823	30,350
Other	(616,316)	(629,294)
Total components of Net Cost of Operations that will not require or generate resources	(97,136)	(14,212)
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period	**759,862**	**786,413**
Net Cost of Operations	**$ 13,636,083**	**$ 12,492,663**

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

REQUIRED SUPPLEMENTARY INFORMATION

DEPARTMENT OF STATE
COMBINING SCHEDULE OF BUDGETARY RESOURCES
For the Year Ended September 30, 2007
(Dollars in Thousands)

	Administration of Foreign Affairs	International Organizations	International Commissions	Foreign Assistance	Other	Total
Budgetary Resources:						
Unobligated Balance, brought forward, October 1:	$ 3,938,875	$ 129,868	$ 7,095	$ 356,018	$ 855,292	$ 5,287,148
Recoveries of Prior Year Unpaid Obligations	89,356	10,565	1,481	(56,112)	148,339	193,629
Budget Authority:						
Appropriations	8,850,849	2,619,592	67,256	1,185,412	6,298,735	19,021,844
Borrowing Authority	—	—	—	—	—	—
Contract Authority	—	—	—	—	—	—
Spending authority from offsetting collections (gross):						
Earned						
Collected	5,818,609	143	6,756	47,181	909,098	6,781,787
Change in receivable from Federal sources	21,434	—	187	(1,430)	(29,766)	(9,575)
Change in unfilled customer orders:						
Advance received	—	—	(17)	(4,842)	109,470	104,611
Without Advance from Federal Sources	—	—	1,361	—	(1)	1,360
Anticipated for rest of year, without advance	—	—	—	—	—	—
Previously unavailable	—	—	—	—	—	—
Expenditure transfers from trust funds:	—	—	—	—	—	—
Nonexpenditure transfers, net, anticipated and actual	(471)	—	—	75,662	130,124	205,315
Temporarily not available pursuant to Public Law	(500,027)	—	—	—	—	(500,027)
Permanently not available	(115,009)	(2,653)	(660)	(9,311)	(4,159)	(131,792)
Total Budgetary Resources	**18,103,616**	**2,757,515**	**83,459**	**1,592,578**	**8,417,132**	**30,954,300**
Status of Budgetary Resources:						
Obligations Incurred:						
Direct	9,325,715	2,666,778	65,194	1,187,078	5,456,638	18,701,403
Reimbursable	5,510,662	—	6,579	6,447	976,660	6,500,348
Unobligated balance						
Apportioned	3,067,775	89,208	10,276	354,603	1,916,798	5,438,660
Exempt from appotionment	(1,309)	—	—	—	24,905	23,596
Unobligated balance not available	200,773	1,529	1,410	44,450	42,131	290,293
Total Status of Budgetary Resources	**$ 18,103,616**	**$ 2,757,515**	**$ 83,459**	**$ 1,592,578**	**$ 8,417,132**	**$ 30,954,300**

DEPARTMENT OF STATE

COMBINING SCHEDULE OF BUDGETARY RESOURCES *continued*

For the Year Ended September 30, 2007
(Dollars in Thousands)

	Administration of Foreign Affairs	International Organizations	International Commissions	Foreign Assistance	Other	Total
Change in Obligated Balance:						
Obligated Balance, net						
Unpaid Obligations, brought forward, October 1	5,371,948	217,895	22,046	848,286	4,734,848	11,195,023
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(366,249)	67	(3,545)	(3,000)	(43,465)	(416,192)
Obligations incurred, net	14,836,377	2,666,778	71,773	1,193,525	6,433,298	25,201,751
Less: Gross Outlays	(13,439,467)	(2,118,682)	(77,327)	(1,009,265)	(5,234,937)	(21,879,678)
Obligated balance transfers, net						
Actual transfers, unpaid obligations	—	—	—	—	—	—
Actual transfers, uncollected customer payments from Federal sources	—	—	—	—	—	—
Less: Recoveries of prior-year unpaid obligations, actual	(89,356)	(10,565)	(1,481)	56,112	(148,339)	(193,629)
Change in uncollected customer payments from Federal sources	(21,434)	—	(1,548)	1,430	29,767	8,215
Obligated balance, net, end of period:						
Unpaid obligations	6,898,831	755,426	15,009	1,088,658	5,784,870	14,542,794
Less: Uncollected customer payments from Federal sources	(607,013)	67	(5,092)	(1,570)	(13,698)	(627,306)
Net Outlays						
Gross outlays	13,439,467	2,118,682	77,327	1,009,265	5,234,937	21,879,678
Less: Offsetting collections	(5,818,609)	(143)	(6,739)	(42,339)	(1,018,569)	(6,886,399)
Less: Distributed Offsetting receipts	(260,419)	—	—	—	—	(260,419)
Net Outlays	**$ 7,360,439**	**$ 2,118,539**	**$ 70,588**	**$ 966,926**	**$ 4,216,368**	**$ 14,732,860**

HERITAGE ASSETS

FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 2007 AND 2006

The Department has collections of art objects, furnishings, books, and buildings that are considered heritage or multi-use heritage assets. These collections are housed in the Diplomatic Reception Rooms, senior staff offices in the Secretary's suite, offices, reception areas, conference rooms, the cafeteria and related areas, and embassies throughout the world. The items have been acquired as donations, are on loan from the owners, or were purchased using gift and appropriated funds. The assets are classified into six categories: the Diplomatic Reception Rooms, Art Bank, Art in Embassies, Curatorial Services Program, Library Rare & Special Book Collection, and Secretary of State's Register of Culturally Significant Property. Items in the Register of Culturally Significant Property category are classified as multi-use heritage assets due to their use in general government operations.

Diplomatic Reception Rooms

Under the management of the Curator's Office, the Diplomatic Reception Room collection is comprised of museum-caliber American furnishings from the 1750 to 1825 period. These items are used to decorate the Diplomatic Reception Rooms located on the 8th floor of the Department of State, as well as 19 offices on the 7th floor used by the Secretary of State and the Secretary's senior staff. These items have been acquired through donations or purchases funded through gifts from private citizens, foundations, and corporations. Tax dollars have not been used to acquire or maintain the collection.

Philadelphia mahogany table-desk on which Thomas Jefferson drafted the Declaration of Independence.

Photo: Richard Cheek

Thomas Jefferson State Reception Room.

The Benjamin Franklin State Dining Room.

Photo: Richard Cheek

Art Bank

The Art Bank was established in 1984 to acquire artworks that could be displayed throughout the Department's offices and annexes. The works of art are displayed in staff offices, reception areas, conference rooms, the cafeteria, and related public areas. The collection consists of original works on paper (watercolors and pastels) as well as limited edition prints, such as lithographs, woodcuts, intaglios, and silk-screens. These items are acquired through purchases funded by contributions from each participating bureau.




Volkmar Wentzel
(clockwise from top left)
U.S. Capitol
The Washington Monument
Q Street Bridge
Pennsylvania Avenue

Rare & Special Book Collection

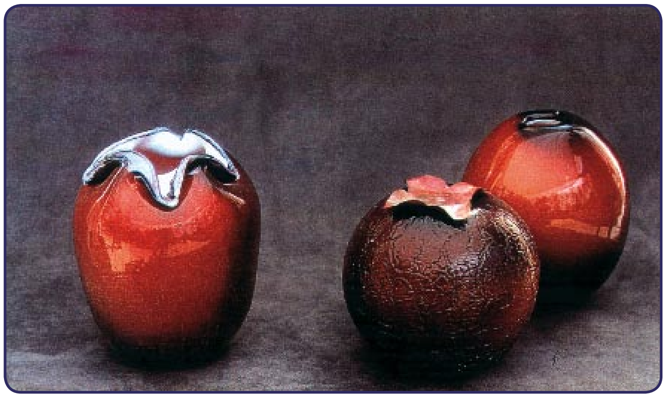
In recent years, the Library has identified books that require special care or preservation. Many of these publications have been placed in the Rare Books and Special Collections Room, which is located adjacent to the Reading Room. Among the treasures is a copy of the Nuremberg Chronicles, which was printed in 1493; volumes signed by Thomas Jefferson; and books written by Foreign Service authors.

Curatorial Services Program

The Curatorial Services Program, which is managed by Overseas Buildings Operations, Interiors & Furnishings Division, Program Management Branch, is responsible for identifying and maintaining cultural objects owned by the Department of State in its properties abroad. The collections are identified based upon their historic importance, antiquity, or intrinsic value.

Art in Embassies

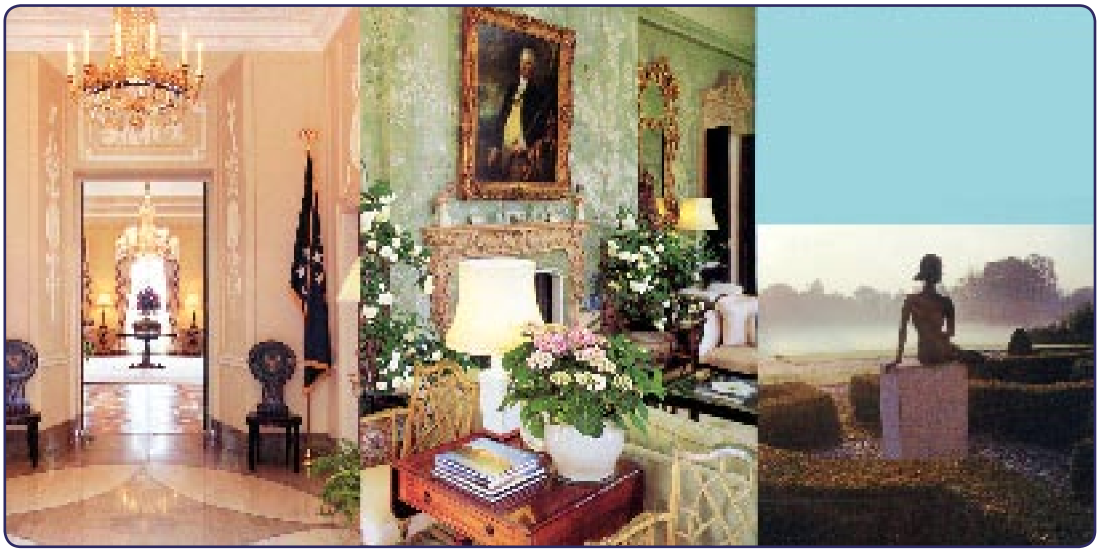
The Art in Embassies Program was established in 1964 to promote national pride and the distinct cultural identity of America's arts and its artists. The program, which is managed by the Bureau of Overseas Buildings Operations, provides original U.S. works of art for the representational rooms of United States ambassadorial residences worldwide. The works of art were purchased or are on loan from individuals, organizations, or museums.



1. Jerry Hovanec, Persimmon with Pulled Stem-Cap 1998, Persimmon with Copper Stem-Cap 1997, and Untitled/Persimmon Vessel 1997, (17 x 13 x 13 cm) blown glass. Courtesy of the artist, Lusby, Maryland

Secretary of State's Register of Culturally Significant Property

The Secretary of State's Register of Culturally Significant Property was established in January 2001 to recognize the Department's owned properties overseas, which have historical, architectural, or cultural significance. Properties in this category include chanceries, consulates, and residences. All these properties are used predominantly in general government operations and are thus classified as multi-use heritage assets. Financial information for multi-use heritage assets is presented in the principal statements.



Situated adjacent to Regent's Park in London, England, Winfield House is the residence of the U.S. Ambassador to the Court of St. James. Heiress Barbara Hutton built this country manor in 1936, and named it after her grandfather F.W. (Winfield) Woolworth, who had founded the famous Woolworth stores where any item could be purchased for five or ten cents. After World War II, Hutton offered the building to the United States Government to use as the ambassador's residence for the price of one American dollar.

HERITAGE ASSETS
For Years Ended September 30, 2005 through 2007

	Diplomatic Reception Rooms Collection	Art Bank	Art in Embassies Program	Curatorial Services Program	Library Rare & Special Book Collection	Secretary of State's Register of Culturally Significant Property
Description	Collectibles – Art and furnishings from the period 1750 to 1825	Collectibles – American works of art	Collectibles – American works of art	Collections include fine and decorative arts and other cultural objects.	Collectibles – Rare books and other publications of historic value	Noncollection – Buildings of historic, cultural, or architectural significance
Acquisition and Withdrawal	Acquired through donation or purchase using donated funds. Excess items are sold.	Acquired through purchase. Excess items are sold.	Acquired through purchase or donation. Excess items are sold.	The program provides assessment, preservation, and restoration as needed.	Acquired through purchase or donation. Excess items are sold.	Acquired through purchase. Excess items are sold.
Condition	Good to excellent	Good to excellent	Good to excellent	Good to excellent	Good to excellent	Poor to Excellent
Number of Items – 09/30/2005	3,413	2,143	979	4,475	1,033	8
Acquisitions	8	22	—	74	—	—
Adjustments	—	—	—	—	—	9
Disposals	—	—	—	8	—	—
Number of Items – 09/30/2006	3,421	2,165	979	4,541	1,033	17
Deferred Maintenance – 09/30/2006	N/A	N/A	N/A	N/A	N/A	$2,716,714
Acquisitions	5	38	—	272	—	—
Adjustments	43	—	—	9	—	—
Disposals	29	—	—	3	—	—
Number of Items – 09/30/2007	3,440	2,203	979	4,819	1,033	17
Deferred Maintenance – 09/30/2007	N/A	N/A	N/A	N/A	N/A	$6,000

DEFERRED MAINTENANCE FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2007

The Department occupies more than 3,000 government-owned or long-term leased real properties at more than 260 overseas locations. It uses a condition assessment survey method to evaluate the asset's condition, and determine the repair and maintenance requirements for its overseas buildings.

SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, requires that deferred maintenance (measured using the condition survey method) and the description of the requirements or standards for acceptable operating condition be disclosed. Fundamentally, the Department considers all of its overseas facilities to be in an "acceptable condition" in that they serve their required mission. Adopting standard criteria for a classification of acceptable condition is difficult due to the complex environment in which the Department operates.

From a budgetary perspective, funding for maintenance and repair has been insufficient in the past. As a result, the Department has identified current maintenance and repair backlog of $151.8 million for buildings and facilities-related equipment and heritage assets that have not been funded. This figure is less than the $325.8 million reported for 2006 as a result of removing function codes (7344, 7357, 7563, 7581, and 7667) which do not incur or pertain to deferred maintenance. The current estimate is a more realistic measure of maintenance and repair work that must be done to buildings and equipment to bring them up to where the Department believes they should be.

MILESTONES OF AMERICAN DIPLOMACY

1778: Treaty of Alliance with France, engineered by Benjamin Franklin, enabled the fledgling republic to continue its struggle for independence.

1783: Treaty of Paris-Great Britain recognized American independence and control over western lands as far as the Mississippi.

1795: Jay's Treaty required Great Britain to remove troops from northwestern frontier; Pinckney's Treaty with Spain opened mouth of Mississippi River to U.S. navigation.

1803: Louisiana Purchase removed foreign control of Mississippi's mouth and doubled U.S. territory.

1819: Adams-Onis Treaty with Spain, transferring Florida, extended the U.S. to present boundaries in southeast.

1823: Monroe Doctrine established U.S. policy of opposing European intervention or new colonization in Western Hemisphere.

1842: Webster-Ashburton Treaty with Great Britain delimited northeastern U.S. (Maine) boundary.

1846: Oregon Treaty with Great Britain extended U.S. sole dominion to the Pacific.

1848: Treaty of Guadalupe-Hidalgo, ending 1846-48 war with Mexico, confirmed U.S. claim to Texas and completed U.S. expansion to Pacific.

1867: Alaska purchase ended Russian territorial presence and completed U.S. expansion on North American mainland.

1898: Treaty of Paris, at end of Spanish-American War, transferred to the United States Puerto Rico, Guam, and the Philippines, expanding U.S. power into the Pacific.

1918: Allies and Germany accepted Wilson's 14 points as basis for just and lasting peace ending World War I.

1945: U.S. and 50 other countries founded the United Nations.

1947: Truman Doctrine asserted U.S. policy of containing Soviet expansion through economic and military aid to threatened countries.

1947: Marshall plan of aid to Europe set foundation for economic cooperation among industrial democracies.

1948: Ninth International Conference of American States created the Organization of American States (OAS) to intensify U.S. and Latin American collaboration in all fields.

1948: NATO, first U.S. alliance concluded in peacetime, provided integrated force for defense of Western Europe and North America.

1963: Limited Nuclear Test Ban Treaty, first major-power agreement regulating atomic weapons testing, banned explosions in the atmosphere, in outer space and under water.

1967: Nonproliferation Treaty, now signed by 110 governments, banned the spread of atomic weapons.

1972: Strategic Arms Limitation Talks (SALT) agreements with U.S.S.R. prescribed mutual limitations on defensive and offensive weapons and established SALT as a continuing process.

1972: President Nixon's February visit to China followed Secretary Kissinger's earlier negotiations in Peking, marking first important step in the process of normalizing relations with the People's Republic of China.

1979: U.S. established diplomatic relations with the People's Republic of China ending 30 years of nonrecognition.

1979: Israel-Egypt Peace Treaty (Camp David Accords) ended 30 years of conflict between the two countries and provided possible framework for comprehensive peace in the Middle East.

1986: The U.S. Congress implemented strong economic sanctions against South Africa, which helped to bring an end to apartheid in 1991.

1989-1991: As President George H.W. Bush stated a desire to integrate the Soviet Union into the community of nations, the Cold War ended when communist regimes collapsed across Eastern Europe and the Soviet Union disintegrated.

1990-1991: In response to the Iraqi invasion of Kuwait, the United States built an international coalition to defend Saudi Arabia and, after United Nations approval, to eject Iraq from Kuwait through Operation Desert Storm.

1992: Representatives of more than 175 nations, including the United States, met at the Earth Summit in Rio de Janeiro, which produced a treaty on climate change and was the largest international meeting on the environment ever convened.

1994: The North American Free Trade Agreement (NAFTA) between the United States, Canada, and Mexico took effect and the United States joined another structure that promoted global free trade, the World Trade Organization.

1995: The General Framework Agreement for Peace in Bosnia and Herzegovina ended the Bosnian civil war by providing for NATO troops to serve as peacekeepers.

2001: The United States led a global coalition that fought a war against terrorism in the wake of the September 11 terrorist attacks in New York and Washington D.C.

2003: After Iraq's repeated refusals to comply with UN resolutions, the United States led a coalition to depose the regime of Saddam Hussein.

2005: General elections held in Iraq to form a new government. Iraqis vote to elect a 275-member National Assembly, provincial councils and a Kurdish regional assembly.

Other Accompanying Information

FINANCIAL MANAGEMENT PLANS AND REPORTS

OVERVIEW

INTRODUCTION

The Department's Bureau of Resource Management (RM), headed by the Assistant Secretary for Resource Management and Chief Financial Officer (CFO), employs over 500 people around the globe--in Washington, Charleston, South Carolina, and Bangkok, Thailand. With five major operating units, the CFO oversees all strategic and performance planning, State operations budgeting and resource management, global accounting, disbursing and payroll, financial systems, financial policies, internal controls and issuance of the financial statements and "annual report" of the Department. The CFO also coordinates and leads the remediation of vulnerabilities within the Department's global critical infrastructure. RM produces a number of essential documents including the Joint State/USAID Strategic Plan, Department Performance Plan, Agency Financial Report, Budget-in-Brief, and the Congressional Budget Justification Document.

RM's customers are all embassies, consulates, and missions overseas, nearly 40 other U.S. Government organizations overseas, all domestic bureaus and employees of the State Department, and the Broadcasting Board of Governors. RM's services to its customers are critical in order that they can do their job to create a more secure, democratic, and prosperous world.

MISSION

"To integrate strategy, budgeting, and performance management, and secure and manage the resources necessary to accomplish the Department of State's mission."

The CFO's mission statement is incorporated into the Department's strategic goal for Strengthening Consular and Management Capabilities.

IMPROVED FINANCIAL PERFORMANCE

GOALS AND STRATEGIES

INITIATIVE GOAL STATEMENT

Provide world-class financial services that support strategic decision-making, mission performance, the President's Management Agenda, and improved accountability to the American people.

Improving financial performance means that the Department knows where every dollar comes from and where every dollar goes in a timely and accurate manner. Accurate and timely information is critical to managing our programs on a day-to-day basis, obtaining the best performance, and ensuring accountability to the American public. It is also a core competency of world–class organizations.

To do this, RM will:

- Produce on-time, accurate and useful financial statements on a routine basis.
- Obtain an unqualified ("clean") opinion on annual Departmentwide financial statements.
- Implement financial systems and processes that meet Federal and Department requirements.
- Ensure effective internal controls are in place and functioning.
- Consolidate and standardize financial operations.
- Leverage best business practices and electronic technologies (E-Gov).
- Build a top-notch finance team.
- Undertake other value-added activities that support strategic decision-making and mission performance.

Key measures of our success in this area are aligned with how OMB scores financial management related to achieving a "green" status rating on the President's Management Agenda (PMA). Other measures of success include:

- Are we implementing the President's mandate to effectively adopt E-Gov solutions, especially in the areas of payroll, travel and grants?
- Are we adequately investing in our greatest asset – our people?

Customer Service

Customer service is the hallmark of the Bureau of Resource Management. As the Department moves to a single world-class financial system, RM has redoubled its emphasis on customer service and support. The Overseas Post Support Desk, in addition to helping posts with implementation of financial systems and changes, has been expanded to become a state-of-the-art help desk for financial management professionals in the Department and in other agencies we service. As part of this effort, RM is moving the customer support function towards a 24/7 operation, leveraging our presence in time zones roughly equidistant around the globe (Charleston, Bangkok and Paris), and integrating former Washington-based operations into our customer support regime.

Building a Top-Notch Finance Team

Establishing a worldwide cadre of qualified financial managers presents a difficult challenge to the CFO. Unlike most other Government agencies, the CFO must manage the dynamics of three personnel systems that include financial management personnel: Foreign Service, Civil Service and Foreign Service Nationals (FSNs). Our primary strategy is to maintain a vigorous and active training program for financial management practitioners. We view the training program as critical — in implementing new systems, establishing RM as the lead bureau within the Department on financial management issues, and also in ensuring that information in the field is current and authoritative. In 2007, the training program was strengthened to provide overseas customers a full line-up of training opportunities. Our training program enjoys customer approval ratings in excess of 90 percent.

THE ROAD AHEAD

Looking ahead, State will continue to achieve fundamental "compliance" results. Moving beyond compliance-based results, State management is making decisions based on meaningful financial information to achieve better performance results in the form of lower costs, improved efficiencies and/or improved outcomes for agency mission.

State will also undertake other value added activities that support effective strategic decision-making and mission performance. These activities include:

- **Enhancing management and internal controls.** The Department maintains a robust system of management controls overseen by senior leadership and administered by RM. The Department's strong commitment to management controls has served as a positive catalyst for change and there are no material weaknesses reported under FMFIA. Recent events in the private sector have increased concerns related to financial management, and in particular on internal controls. To address these concerns, Congress passed the Sarbanes-Oxley Act of 2002, which establishes new demands for corporate accountability and includes several important sections related to internal controls for public companies. In December 2004, OMB revised Circular A-123, *Management's Responsibility for Internal Control*, to strengthen internal control in the Federal government. The Department fully implemented the requirements of revised circular A-123 in FY 2006, as required, and has continued to strengthen and expand the program in FY 2007, including establishing a new Office of Management Controls.

- **Streamlining and consolidating global financial operations.** In FY 2005, State completed a multi-year effort to consolidate and streamline our worldwide financial operations in our Charleston, South Carolina and Bangkok, Thailand locations. Building on this success, RM is expanding our Post Support Unit (PSU) in Charleston, SC to take on more of the burden of repetitive, standardized financial processing from the posts and perform those tasks centrally at a substantially lower cost. We will work with offices throughout the Department to seek additional opportunities to reduce costs by moving processing to the PSU. This will not only significantly reduce processing costs, but more importantly free up financial staff for higher value, active financial management at our Missions and offices worldwide, which is critical to better managing our rising costs.

- **Leveraging best business practices and electronic technologies (E-Gov).** The President's Management Agenda includes an aggressive strategy to secure better services at lower cost through electronic government (E-government). In the Department, we are advancing this E-Government strategy through projects that offer performance gains, such as E-Travel. E-Travel uses a web-based travel system solution (E^2 Solutions) that provides electronic authorizations and vouchers, as well as on-line booking and ticketing, for temporary-duty (TDY) travel to minimize cost and improve customer satisfaction. E^2 Solutions will replace the hundreds of stand-alone, stove-piped instances of our existing Travel Manager (TM+) System operating throughout the world. E^2 pilots were conducted overseas and domestically in FY 2007, and user feedback has been positive. The E2 rollout will occur in phases, continuing throughout FY 2008 and concluding in FY 2009. The current plan is to deploy E^2 at 60 posts in FY 2008. When fully deployed by the end of FY 2009, we will have a single worldwide TDY travel management process, fully integrated with the Department's financial systems.

FINANCIAL MANAGEMENT SYSTEMS

IMPLEMENT A GLOBAL FINANCIAL MANAGEMENT SYSTEM (GFMS)

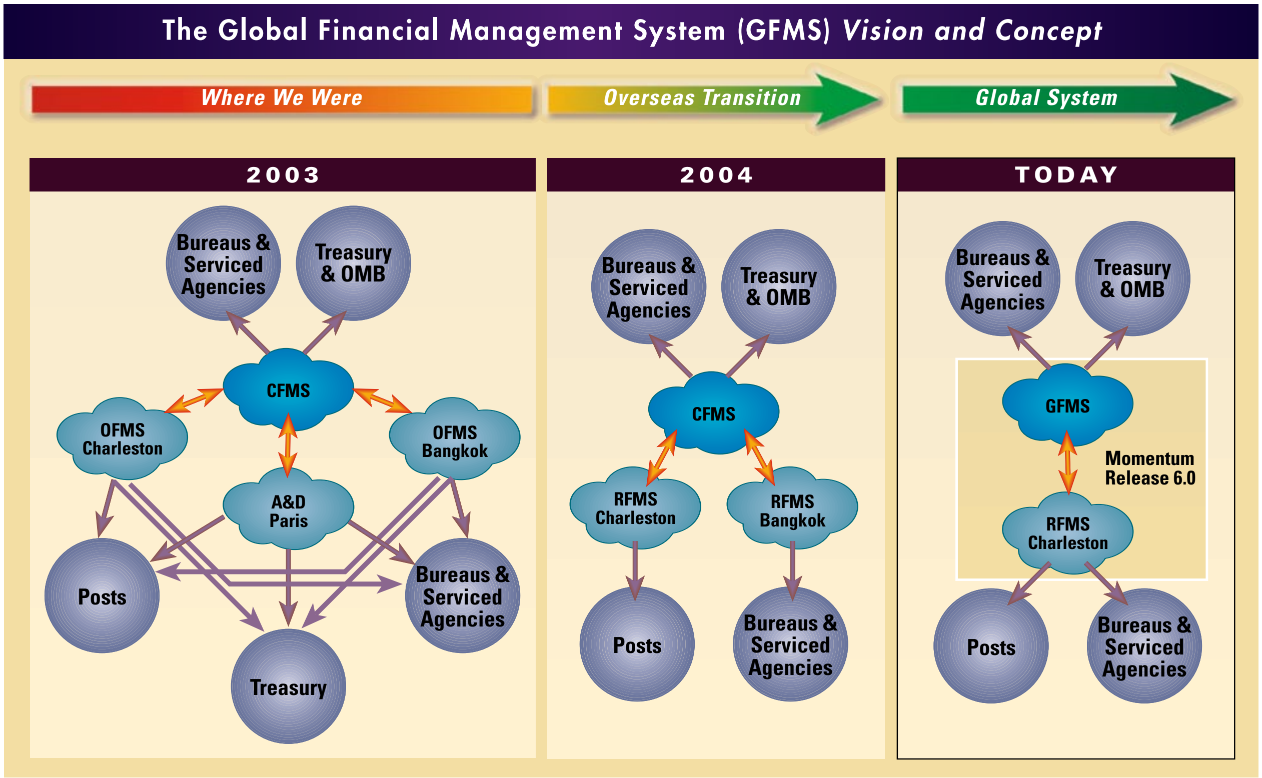
For the past two decades, the Department accounted for its resources through multiple outdated and disjointed legacy financial systems. Some posts effectively conducted operations through the integration of little more than a collection of Excel spreadsheets. Often, it could take up to 45 days after a financial event occurred for overseas financial data to update the Department's Central Financial Management System (CFMS).

The Global Financial Management System (GFMS) project integrates the Department's overseas and domestic financial operations onto common financial management software platform in Charleston. This provides a single integrated view of financial data through data standardization, common business processes, and the seamless exchange of information through the Department's financial and administrative sectors. This will dramatically improve operations and reduce costs by eliminating system redundancies and replacing obsolete and unsupported financial systems. It will also provide the infrastructure for integrating other administrative activities within the Department, such as the Integrated Logistics Management System (ILMS).

In FY 2007, State implemented the Global Financial Management System (GFMS) as the next step in our multiyear effort to establish a single global financial system. GFMS replaces the Department's 20 year old Central Financial Management System (our core accounting system) and centrally accounts for State's billions of dollars of finances through over 5 million annual transactions by 1,000 users and over 25 "handshakes" with other internal and external systems. Upgrading a financial system of this size and complexity is a large and challenging undertaking.

GFMS is based on the CGI Federal's Momentum financial management system. Momentum is a certified Federal financial system used widely in the Federal market place. GFMS uses the same software (CGI Momentum) and technical platform used by the Regional Financial Management System (RFMS) overseas and the Joint Financial Management System of USAID. As part of the implementation, GFMS integrates, for the first time, the Acquisition and Fixed Asset systems into a single software application. Also, a data warehouse and cost allocation module (for managerial cost accounting) were installed. GFMS will align our domestic financial management systems environment with the Department's enterprise architecture. By July 2008, we will have stabilized GFMS and established plans for our final step in establishing a single global financial system – combining GFMS and RFMS. By July 2009, we will be in the final stages of combining GFMS and RFMS, and together with our efforts on Global Direct Connect (detailed below), will begin FY 2010 with a virtual single global financial management system.

The diagram on the following page depicts the state of our financial systems at the beginning of FY 2003 and the end state of our global vision for the beginning of FY 2008 and beyond.



Regional Financial Management System (RFMS)

RFMS is the global accounting and disbursing system that has been implemented for posts around the world, and the building block of GFMS. RFMS is comprised of a commercial-off-the-shelf, accounting system for funds management, obligation, and voucher processing, and the RFMS/D disbursing system developed by the Department for disbursing services. The successful worldwide implementation of RFMS replaced the obsolete Paris Accounting and Disbursing system (mainframe-based) used at FSC Paris and the Overseas Financial Management System (Wang-based) used at FSCs Charleston and Bangkok. RFMS incorporates State's standard account structure and improves transaction standardization and timeliness between RFMS and GFMS, which results in the consistent, timely processing and recording of financial data on a worldwide basis. In addition, the overseas interface was reengineered for RFMS and provides daily updates of overseas financial transactions to GFMS. These daily updates allow headquarters managers to ascertain the worldwide balance of our accounts on a daily basis, something never before possible.

In addition, RM enhanced its reporting tool called COAST which provides daily updates on all financial transactions to 168 posts overseas and domestic bureaus, allowing them to analyze, and "slice and dice" their financial data for local reporting purposes using modern reporting and query tools on their local workstation.

Global Direct Connect

Our Global Direct Connect initiative moves posts that have operationally practical and reliable network connections (estimated at over 85 percent of our embassies) from their current batch processing environment to a real-time, on-line connection. As a result of our efforts to date, there are now over 100 (out of a possible 180) posts using Global Direct Connect. Our plan is to implement another 25 posts to Global Direct Connect by July 2008. By July 2009, we will convert all remaining posts (with reliable networks) to Global Direct Connect.

Joint Assistance Management System (JAMS)

The Department of State is implementing a Joint Assistance Management System (JAMS). The system will collect assistance information and will interface with the Global Financial Management System. JAMS will be based on a commercial product called "Grantium." Grantium was selected from a field of commercial products because of its ability to be easily configured for assistance processes. Other features include a robust reporting capability.

During FY 2006 significant progress was made on JAMS, and a proof of concept was conducted with support from both domestic and field users of Grantium. FY 2007 saw a second proof of concept to evaluate changes and upgrades resulting from the suggestions in the first session. Pilot deployments will begin in FY 2008, setting the stage for domestic rollout in FY 2009.

MANAGEMENT OF OBLIGATIONS TO THE DEPARTMENT

FEDERAL CIVIL PENALTIES INFLATION ADJUSTMENT ACT

The Federal Civil Penalties Inflation Adjustment Act of 1990 established annual reporting requirements for civil monetary penalties assessed and collected by Federal agencies. Civil penalties are defined as any non-criminal penalty, fine or other sanction for which a given dollar amount or maximum amount is specified by Federal law, and which is assessed or enforced by an agency as a result of an administrative proceeding or civil action in the Federal courts. The Department has assessed fines on individuals and companies for exporting defense materials without required approvals and for misrepresenting facts on an export application.

COMPANY NAME	VIOLATION	DATE ASSESSED	AMOUNT ASSESSED
SPACE SYSTEM/LORAL, INC.	Violating the express terms and conditions of the Department's munitions licenses and exporting defense services without a munitions license or other authorization to the People's Republic of China.	1/9/2002	$ 14,000,000
HUGHES ELECTRONICS CORP. & BOEING SATELITE SYSTEMS	Violating the terms and conditions of the Department's munitions licenses and exporting defense services without munitions licenses or other authorizations (and conduct relating to two failed launches of rockets carrying spacecraft) to the People's Republic of China.	3/4/2003	12,000,000
EDO CORPORATION	Violations incurred by Condor Systems, Inc. prior to the acquisition of business assets by EDO that included the terms and conditions of the Department's munitions license and exporting defense services without munitions license or other authorizations.	11/24/2003	1,750,000
ITT CORPORATION	Exporting defense articles and services (night vision products and space remote sensing technical data and defense services) in violation of the terms or conditions of other approvals that were provided by the Department.	11/1/2004	3,000,000
GENERAL MOTORS CORPORATION	Exporting defense articles and services (to foreign person employees of proscribed countries) in violation of the terms or conditions of other approvals that were provided by the Department.	11/1/2004	8,000,000
ORBIT ADVANCED TECHNOLOGIES INC.	Violating the terms and conditions of the Department's munitions and licenses by agreeing to sell defense articles (Radome Measurement System – AL8098/AL8099) to the People's Republic of China	8/29/2005	500,000
THE BOEING COMPANY	Exporting unauthorized defense articles and services (to foreign person employees of proscribed countries) in violation of the terms and conditions of the Department's International Traffic in Arms Regulations (ITAR).	3/28/2006	15,000,000
GOODRICH CORPORATION	Exporting unauthorized defense articles and services (to foreign person employees of proscribed countries) in violation of the terms and conditions of the Department's International Traffic in Arms Regulations (ITAR).	3/28/2006	1,250,000
L-3 COMMIUNICATIONS	Exporting unauthorized defense articles and services (to foreign person employees of proscribed countries) in violation of the terms and conditions of the Department's International Traffic in Arms Regulations (ITAR).	2/28/2006	2,000,000
THE DIRECTTV GROUP INC. & HUGHES NETWORK SYSTEMS INC.	Exporting unauthorized defense articles and services (to foreign person employees of proscribed countries) in violation of the terms and conditions of the Department's International Traffic in Arms Regulations (ITAR).	1/26/2005	5,000,000
LOCKHEED MARTIN (SIPPICAN) CORPORATION	Exporting unauthorized classified and unclassified technical data and defense articles and services in violation of the terms and conditions of the Department's International Traffic in Arms Regulations (ITAR).	12/12/06	3,000,000
SECURITY ASSISTANCE INTERNATIONAL, INC. & HENERY L. LAVERY III	Violating the terms and conditions of the Department's munitions licenses and exporting defense services without munitions licenses or other authorizations to the People's Republic of China.	12/12/2006	75,000
TOTAL			**$65,575,000**

COMPANY NAME	BALANCE OUTSTANDING SEPTEMBER 30, 2006	FISCAL YEAR 2007 ASSESSMENTS	FISCAL YEAR 2007 COLLECTIONS	BALANCE OUTSTANDING SEPTEMBER 30, 2007
SPACE SYSTEM/LORAL, INC.	$ 5,057,142	$ —	$ 1,685,714	$3,371,428
HUGHES ELECTRONICS CORP. & BOEING SATELITE SYSTEMS	1,500,000	—	—	1,500,000
EDO CORPORATION	—	—	—	—
ITT CORPORATION	1,000,000	—	1,000,000	—
GENERAL MOTORS CORPORATION	4,500,000	—	1,500,000	3,000,000
ORBIT ADVANCED TECHNOLOGIES INC.	233,333	—	66,667	166,666
THE BOEING COMPANY	—	—	—	—
GOODRICH CORPORATION	750,000	—	250,000	500,000
L-3 COMMIUNICATIONS	1,500,000	—	1,500,000	—
THE DIRECTTV GROUP INC. & HUGHES NETWORK SYSTEMS INC.	—	5,000,000	3,500,000	1,500,000
LOCKHEED MARTIN (SIPPICAN) CORPORATION	—	3,000,000	1,000,000	2,000,000
SECURITY ASSISTANCE INTERNATIONAL, INC. & HENERY L. LAVERY III	—	75,000	—	75,000
TOTAL	**$14,540,475**	**$ 8,075,000**	**$10,502,381**	**$12,113,094**

DEBT MANAGEMENT

Outstanding debt from non-federal sources (net of allowance) decreased from $34.3 million in 2006 to $32.5 million in 2007.

Non-federal receivables consist of debts owed to the International Boundary and Water Commission, Civil Monetary Fund, and amounts owed for Repatriation Loans, medical costs, travel advances, and other miscellaneous receivables.

Of the delinquent receivables over 365 days old, the majority ($5.6 million) is for the Repatriation Loan Program. These are loans given to destitute American citizens stranded overseas to allow them to return to the United States. The loans are given only if the individual cannot obtain funds from relatives, friends, employers, or another source. The Department acts as the lender of last resort. The loan becomes delinquent 60 days after repatriation to the United States. Due to their poor economic situation, most of these individuals are unable to repay the loans on time.

The Department uses installment agreements, salary offset, and restrictions on passports as tools to collect its receivables. It also receives collections through its cross-servicing agreement with the Department of the Treasury. In 1998, the Department entered into a cross-servicing agreement with the Department of the Treasury for collections of delinquent receivables. In accordance with the agreement and the Debt Collection Improvement Act of 1996 (Public Law 104-134), the Department referred $1,444,897 to Treasury for cross-servicing in 2007. Of the current and past debts referred to Treasury, $385,867 was collected in 2007.

Receivables Referred to the Department of the Treasury for Cross-Servicing

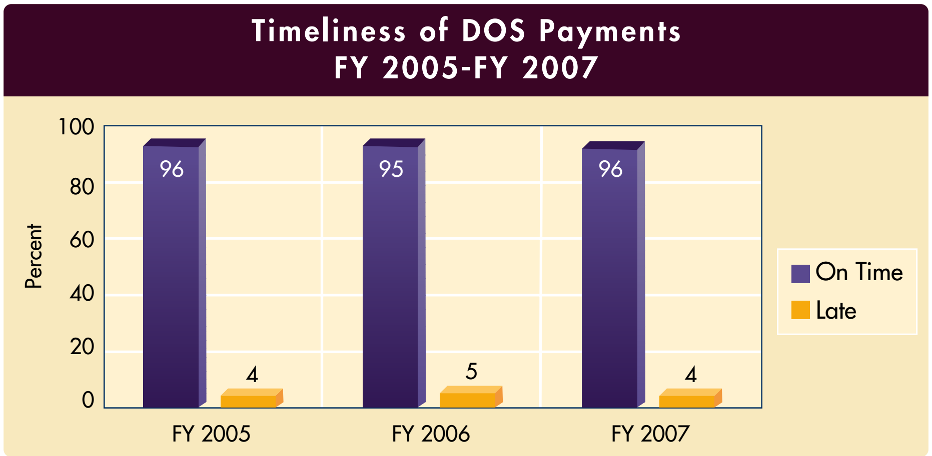
	FY 2007	FY 2006	FY 2005	FY 2004
Number of Accounts	884	1,044	772	253
Amounts Referred (In Thousands)	$1,445	$ 1,673	$ 401	$ 261

MANAGEMENT OF PAYMENTS

PROMPT PAYMENT ACT

TIMELINESS OF PAYMENTS

The Prompt Payment Act (PPA) requires Federal agencies to pay their bills on time or an interest penalty must be paid to vendors. During FY 2007, the Department made 731,830 payments subject to prompt payment of which 704,583 or 96% were paid on time. Presented below is a chart that reflects the timeliness of the Department's payments from FY 2005 through FY 2007.



During FY 2007, The Department realized an increase in interest penalties paid (4 percent), when compared to one percent or $405 K in FY 2006. The increase in Prompt Payment penalties was primary due domestic payment delays caused by the transition to a new accounting system in FY 2007. Also, the effects of the system transition were seen in the percentage domestic invoices paying penalties against the total amount of domestic payments paid (FY 2007 - 0.031 percent vs. FY 2005 - 0.013 percent and FY 2006 - 0.009 percent).

SELECTED PAYMENT DATA

	2007	2005	2005
Interest Paid ($000)	1,420	405	557
Interest Under $1 Not Due ($000)	—	—	—
Interest Due But Not Paid ($000)	—	—	—
Number of Procurement Card Transactions			
Domestic	41,524	45,804	54,061
Overseas	93,480	82,023	75,407

ELECTRONIC PAYMENTS

Payments made through Electronic Funds Transfer (EFT) were 90 percent of the total payments made for domestic and overseas payments. This is an increase of 3 percent over the fiscal year 2006 rate. EFT payments made for the Domestic operations were 97 percent of the total domestic payments. EFT payments made through the USDO for overseas operations was 85 percent of the total number of overseas payments. This is an increase of over 4 percent of the fiscal year 2006 rate. Payments made for overseas operations will not have the same rate as the domestic payments due to the result of complexities of banking operations in some of the countries where payments are made by the Department of State.

EFT and Check Payment Volumes

	2007		2006		2005	
Payment Type	**Number**	**Percent**	**Number**	**Percent**	**Number**	**Percent**
EFT:						
Domestic	1,263,429	97	1,095,691	98	1,120,735	98
Overseas	1,586,790	85	1,455,055	81	1,309,530	77
EFT Subtotal	2,850,219	90	2,550,746	87	2,430,265	85
Checks:						
Domestic	39,924	3	26,869	2	23,539	2
Overseas	289,585	15	352,092	19	400,985	23
Checks Subtotal	329,509	10	378,961	13	424,524	15
Total Domestic	1,303,353	41	1,122,560	38	1,144,274	40
Total Overseas	1,876,375	59	1,807,147	62	1,710,515	60
Total Payments	**3,179,728**	**100**	**2,929,707**	**100**	**2,854,789**	**100**

IMPROPER PAYMENTS INFORMATION ACT

The Improper Payments Information Act of 2002 (IPIA), Public Law No. 107-300, requires agencies to annually review their programs and activities to identify those susceptible to significant improper payments. OMB Circular A-123, Appendix C, defines significant improper payments as annual improper payments in a program that exceed both 2.5 percent of program annual payments and $10 million. Once those highly susceptible programs and activities are identified, agencies are required to estimate and report the annual amount of improper payments. Generally, an improper payment is any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, and administrative or other legally applicable requirement. Summarized below are the Department's IPIA accomplishments and future plans for identifying improper payments as provided for in OMB Circular A-136, Financial Reporting Requirements.

Statistical Sampling Process

Records of payments were provided to the statistician for sample selection. The statistician randomly selected the records and the required number of samples for analysis of accuracy. The number selected was the minimum required to yield an estimate with a 90 percent confidence level and a confidence interval of plus or minus 2.5 percent.

INTERNATIONAL INFORMATION PROGRAMS (IIP) –U.S. SPEAKER PROGRAM

In FY 2003, the Department of State began to institute an effort that would identify programs that were susceptible to significant improper payments in accordance with the Improper Payments Information Act (IPIA) of 2002 (Public Law No. 107-300). All of the Department's expenditures for FY 2002 were classified into three categories: employee pay, vendor payments, and federal financial assistance. A risk assessment was performed based on a number of factors such as dollar volume, number of recipients, internal controls and the audit reports of the programs. As a result of this risk assessment, International Information Program (IIP), U.S. Speaker and Specialist program was classified as high-risk.

In FY 2004, a statistical sample was selected for IIP and detailed evaluations were performed. The improper payments projected error rate over the entire population was 81.18 percent or $1.4 million. The findings related to insufficient supporting documentation being provided and an incorrect financial assistance award instrument being used to obligate the award. In FY 2005, there were no detailed evaluations for improper payments performed for IIP. As a result, the program was reviewed during FY 2006.

In FY 2006, a statistical sample was selected for IIP and detailed evaluations were performed. The detailed evaluations resulted in 30 improper payments and several internal control findings. The projected error rate and dollar amount of improper payments in the population sampled was 23.81 percent or $348,567.

In FY 2007, a statistical sampling was conducted for IIP and a comprehensive assessment was performed. The assessment resulted in four improper payments and three internal control findings. The projected error rate and dollar amount of improper payments shows significant improvement with an error rate of only 4 percent or $17,038. The findings related to insufficient documentation (Bio or Resume) to support whether the grantee was eligible for the award. In no instance was evidence found that a payment was erroneous and needed to be recovered.

Last Quarter FY 2006 and First Three Quarters FY 2007-International Information Programs-US Speaker Program (IIP)

Program	Transactions in		Dollars in		Projected	
	Population	Sample	Population	Sample	Error Rate	Improper Payments
International Information Programs-U.S. Speaker and Specialist Program	1,061	126	$23,747,609	$388,693	4%	$17,038

Corrective Action Plans

During our review of the International Information Program -U.S. Speaker and Specialist Program, four improper payments were found where there was insufficient documentation provided to support the grantee eligibility for the award (i.e. biographical information or resumes). To address these issues, the program officers will periodically check project tracker for each respective grantee to ensure that the documentation required to validate and support the eligibility of each grantee is supported.

IPIA REPORTING FY 2007-BUSINESS CLASS TRAVEL

In March 2006, GAO issued a report that identified shortcomings in the Department of State's authorization and administration of business class travel. In April 2006, in response to the report, the Department instituted additional measures to tighten internal controls over the approval and use of business class travel. The GAO report also recommended that the Secretary of State conduct regular reviews of the Department's use of business class travel and report the findings to senior management. Specifically, the reviews would determine whether the Travel Management Centers, bureaus and travelers adhered to government-wide and Department regulations for premium class travel.

In response to this recommendation, the Department incorporated the audits of premium class travel into the ongoing reviews conducted in accordance with the IPIA, the GAO guide, and other guidelines for evaluating and testing controls over sensitive payments. Grant Thornton was tasked with testing the controls for authorization and issuance of Business Class Travel for FY 2006 and FY 2007.

The first review was conducted for the first and second quarters of FY 2006. Results generally supported the findings end of the GAO report. The second review, covering the second and third quarters of FY 2007, was conducted after the new management controls were implemented in April 2006. The improvements were significant. In particular, there were no instances where the travelers flying business class were found to be ineligible.

Errors that were found stemmed from weaknesses in administrative procedures and instances where supporting documentation was not readily available. These can be projected to an overall error rate of 3.97% or $21,594. In no instance was evidence found that a business class travel payment was erroneous and needed to be recovered.

Second and Third Quarters FY 2007-Business Class Travel and Sensitive Payments

Program	Transactions in		Dollars in		Projected	
	Population	Sample	Population	Sample	Error Rate	Improper Payments
Business Class Travel and Sensitive Payments	3,808	126	$16,568,322	$649,697	3.974%	$21,594

Corrective Action Plans

- For Blanket Authorizations, one instance was found where it was not possible to verify that the appropriate justification for business class travel was properly authorized and approved. The requirement for the DS 4087 became effective in April 2006, when 14 FAM 567.2-2 (b) was revised to establish the requirement for use of DS 4087 to document the justification for authorizing business class travel, including travel over 14 hours.

  To address this problem, a Business Class Travel Department Notice will be issued to re-emphasize the business class travel regulations as cited in 14 FAM 567.2-4 and the Disposition Authorization Number, GRS 9 that provides travelers with specific instructions on what documents are to be retained for travel relating to routine and operational aspects of travel.

- Three instances were identified where full supporting documentation was missing (travel voucher, DS-4087 and itinerary) in order to verify compliance in accordance with 14FAM 567.2-2 (A) and (B).

  The correction action plan provides that the Department will issue a Business Class Travel directive that states that all travel documentation (travel orders, travel vouchers, receipts related to a reimbursable expense, DS 4087 and the government travel agency issued itinerary) be retained for not less than seven years.

- One instance was found during the review where full supporting travel voucher documentation did not provide the appropriate signature (electronic) by the designated approving official.

  As a corrective measure, the Department will require that the voucher be sent back to the person aware of the travel for proper approval before the voucher can be funded.

Results Summary

The following table summarizes the results of the International Information Programs (IIP), Business Class Travel Improper Payment Review, and the projected improper payment percentage and outlay estimates for the next three years.

The Improper Payment dollar amounts in the table represents the estimated value of errors in the entire population based upon the samples average dollar amount per improper payment times the prospected number of improper payment transactions in the population.

Program	PY Outlays	PY%	PY$ (in dollars)	CY Outlays (dollars in millions)	CY IP%	CY IP $ (in dollars)	CY+1 Est Outlays (dollars in millions)	CY+1 IP%	CY+1 IP$ (in dollars)
IPIA									
FY 2006-2007 International Information Programs	28	23.81%	$348,567	23	4%	$180,794	24	<1%	$182,602
Sensitive Payments									
FY 2007 Business Class Travel	NA	NA	NA	16	4%	$652,603	17	>1%	$659,129

Program	CY+2 Est Outlays (dollars in millions)	CY+2 IP%	CY+2 IP$ (in dollars)	CY+3 Est Outlays (dollars in millions)	CY+3 IP%	CY+3 IP$ (in dollars)
IPIA						
FY 2006-2007 International Information Programs	25	<1%	$184,428	26	<1%	$186,272
Sensitive Payments						
FY 2007 Business Class Travel	18	<1%	$665,720	19	<1%	$672,377

RECOVERY AUDIT PROGRAM RESULTS

Currently the Department of State, Bureau of Resource Management has established a two-tiered erroneous payment monitoring and review program, which supplements the formal account receivable process. The Global Financial Services (GFS), Office of Claims, has integrated erroneous payment identification and collection as key functions of the accounts payable process and the paying office's operations. The claims office has established an internal debt management unit, whose primary mission is the identification and collection of erroneous payments, coordinating with the Accounts Receivable Division (ARD) as necessary. In addition, the GFS Office of Oversight Management & Analysis conducts a monthly query of all domestic payments, focusing on identifying potential erroneous and duplicate payments. The GFS approach has incorporated various manual and automated data analysis techniques and processes to identify, validate and collect erroneous payments, including use of data mining software, manual sampling of internal payment records, U.S. Treasury TIN matching, sampling of vendors etc.

In FY 2007, the GFS domestic claims debt management process identified and validated 214 actual duplicate/erroneous payments, totaling $5.3 million, out of 551,149 total payments, totaling $23.2 billion. The claims office has collected or recovered 198 of the 214 validated erroneous payment debts (93 percent), totaling $4.9 million (92 percent). While the transition to a new financial system in 2007 has increased the number of incidents and expanded the debt collection timeline, the primary reasons for these improper payments and debts continues to be the use the wrong vendor payment record in the funding of the awards and/or authorization of payment on submitted claims.

The GFS duplicate or erroneous payment program has proven to be a cost effective tool (the program's annual $100 thousand operating costs) to supplement the ARD domestic commercial debt management and recovery. Identified debts not collected by the office of claims are transferred to ARD for follow-up collection. Since FY 2005, this GFS program has identified 736 duplicate/erroneous payments ($13.1 million), and collected 673 identified debts ($12.6 million or a collection rate of 96.2 percent).

RECOVERY AUDIT PROGRAM RESULTS

Agency Component	Amount Subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amounts Identified for Recovery CY	Amounts Recovered CY	Amounts Identified for Recovery PY's	Cumulative Amounts Identified for Recovery (CY + PY's)	Cumulative Amounts Recovered (CY + PY's)	Outstanding
Number	551,149	551,149	214	198	522	736	673	63
Amount	$ 23.2 billion	$ 23.2 billion	$ 5,353,615	$ 4,900,338	$ 7,765,452	$ 13,119,067	$ 12,627,827	$ 491,240

ACCOUNTABILITY

The Department is committed to reducing erroneous payments issued domestically and overseas. Programs and procedures have been instituted that will strengthen agency management and internal control procedures for prevention, detection and recovery of erroneous payments. The following improvements are being undertaken:

- Issue updated guidance for performing program reviews and risk assessments
- Strengthen policies and procedures with regard to proper documentation requirements for payments
- Provide training to affected staff regarding proper payment requirements and documentation
- Strengthen payment and debt management programs policies and practices that will improve detection, referral and recovery efforts
- Report information on improper payments in the annual *Agency Financial Report.*

INFORMATION SYSTEMS

Based on the improper payment reviews conducted in FY 2005 and FY 2006, the improper payments identified did not result from the lack of proper information systems. Although the Department transitioned to a new global financial management system in FY 2007, the current financial management system did not have an impact on the level of improper payments identified.

ISSUES

As previously mentioned, one of the challenges the Department faced in FY 2007 was determining to what extent federal financial assistance should be tested to obtain reasonable assurance that improper payments are not occurring at the grantee level. The Department performed limited procedures to test for improper payments that did not involve reviewing payments at the grantee level. However, to supplement the test work performed, the Department relied on monitoring procedures performed at the program offices, the A-133 reports of grantees, and the results of OIG reviews. In FY 2008, the Department will consider establishing procedures in the Bureau of Resource Management to monitor financial transactions. The Department will also seek guidance from OMB in FY 2008 to determine the most feasible way to test federal financial assistance for compliance with the IPIA. The Department will also review best practices to follow in FY 2008.

FY 2007 MANAGEMENT AND PERFORMANCE CHALLENGES

The *Reports Consolidation Act of 2000* requires that the Department's *Performance and Accountability Report* include a statement by the Inspector General that summarizes the most serious management and performance challenges facing the Department and briefly assesses the progress in addressing those challenges. The Office of Inspector General (OIG) considers the most serious management and performance challenges for the Department to be in the following areas:

- Protection of People and Facilities
- Information Security
- Financial Management
- Human Resources
- Counterterrorism and Border Security
- Public Diplomacy
- Post-Conflict Reconstruction and Stabilization

PROTECTION OF PEOPLE AND FACILITIES

Making its people, facilities, and information more secure continues to be one of the Department's highest priorities and greatest challenges. In FY 2007, the Department had success in addressing security vulnerabilities at a number of overseas posts through its new construction and security upgrade programs. However, the Department remains challenged to identify and fund interim solutions to address security vulnerabilities at facilities awaiting long-term new construction or the completion of major security upgrades. Additionally, as the number of American Presence Posts increases, the Department will need funding to complete required security upgrades for these facilities.

The Department has continued to make progress in strengthening its domestic protection program during FY 2007, especially through its emergency preparedness program. As stated in the FY 2006 letter, the Department has strengthened its domestic emergency program through more frequent emergency drills, employee forums, and by providing proactive guidance to improve employee preparedness at work and home. In FY 2007, the Department opened a new Domestic Emergency Command Center to handle emergencies such as Hurricane Katrina and other events that threaten the safety of the people working at State Department facilities. Additionally, the Department implemented a new Warden Program. These wardens have been trained to assist employees in evacuating a building or to direct the employees to designated shelter-in-place areas or assembly points. While the Department has made significant progress in its domestic emergency program, more still needs to be done. The Department needs to continue the work it has started in developing new Facility Emergency Action Plans (FEAP) for all Washington area facilities. The Department also needs to finalize the development and implementation of domestic emergency policies and procedures.

INFORMATION SECURITY

The Department continues to make progress in strengthening its information security programs and practices, while realizing that more must be done to effectively administer and manage its information security programs per statutory requirements. Improvements have been made by the Department in its governance structures for information security over the last year with the creation of the Information Security Steering Committee, which has helped resolve differences between components involved in the information security process. Training and awareness, contingency planning, and incident response are among the strongest and most mature areas in terms of operational development within the Department. There has been high level support from the Secretary and Under Secretary for Management for the protection of privacy information with positive steps, such as the creation of the Privacy Protection Governance Board, already completed.

There are several areas that require additional attention from the Department in order to ensure an overall effective information security program. There is an ad hoc nature to the Department's program with operational elements stronger than the program planning elements. For example, the information security program plan for the Department, submitted to the Office of Management and Budget in late August, does not fully meet statutory requirements. Further, the Department's inventory management policy does not address roles and responsibilities for overall inventory management nor does it establish accountability for the maintenance of accurate inventory records. The Federal Enterprise Architecture, System Development Life Cycle, and Capital Planning and Investment Control processes are not integrated within the Department and, as a result, the ability to address information security through the planning process is hampered. Finally, the Office of Information Programs and Services' ability to implement privacy requirements has been limited due to insufficient funding to support a multitude of new tasks.

Given the increasing use and reliance on cellular telephones (both official and non-official) in the work place domestically, the Department is also faced with reevaluating its existing, but relatively unenforced, restrictive policies. The Department's challenge is balancing users' perceived needs against known threats and the cellular telephone's potential for being exploited as a means to clandestinely access sensitive or classified information.

FINANCIAL MANAGEMENT

Financial management continues to be a major challenge within the Department. During FY 2006, the Department became aware of potentially material amounts of real property that had not been properly reported in its financial statements. Because of the effort to address the real property issue, the Department was unable to provide complete financial statements or certain evidential material in a timely manner. Therefore, the independent external auditor was unable to express an opinion on the Department's financial statements by the November 15, 2006, deadline imposed by the Office of Management and Budget.

The Department thereafter completed its work on real property and restated the FY 2005 financial statements to correct the errors. The Department also restated its FY 2006 financial statements to correct an error related to funds provided to another agency. The Department provided completed financial statements and supporting documentation to the independent external auditor, who issued an unqualified opinion on the financial statements on December 12, 2006.

In its findings, the independent external auditor identified a weakness related to real property and again noted concerns that had been identified in prior reports relating to the recording of personal property and related depreciation expenses, information systems security, the adequacy of the financial and accounting systems, management of undelivered orders, and the lack of a managerial cost accounting system. The independent external auditor also again noted that the Department continues to have difficulty producing year-end financial data in a timely manner.

During FY 2007, the Department has taken steps to address some of these weaknesses. For example, the Department developed detailed guidance to ensure construction costs are properly capitalized, and implemented processes to monitor both project establishment and completion. The Department also created a committee to address weaknesses related to personal property. This committee has implemented improvements in the methods used to identify and report vehicle costs, aircraft, and property held by contractors. For computer security, the Department has made progress in its certification and accreditation processes, and is working to develop an accurate inventory of systems, address new security requirements, and improve patch management. The Department has also implemented a new domestic financial and accounting system, and is automatically deobligating certain undelivered orders. In addition, the Department is working to implement a managerial cost accounting system.

HUMAN RESOURCES

The Director General of the Foreign Service (DG) and the Bureau of Human Resources (HR) face significant challenges in implementing the Secretary of State's vision of transformational diplomacy and ensuring the availability of a dynamic diplomatic corps that has a broad range of knowledge, skills, and capabilities. In responding to these challenges, the DG and his team must balance high-stakes problems in international relations with a series of major personnel-related initiatives.

The bureau has redesigned the assignment system to fill key overseas positions, changed the Foreign Service examination process, taken steps to strengthen the retirement office, and launched a shared services structure for certain human resources functions.

A controversial new assignment system successfully met its short-term goal of filling Foreign Service vacancies in critical hardship posts. However, despite this, it is unclear whether the Department will continue to be able to staff Iraq on a voluntary basis or will have to move to directed reassignments.

The Department's efforts to establish shared services (Centers of Excellence) for certain HR functions must be put on a rational implementation schedule if it is to succeed. The Department should also explore consolidation of certain HR functions in a single center.

A Global Repositioning Program moved 200 Foreign Service jobs from Washington, Europe, and elsewhere to India, China and other countries to support transformational diplomacy. Before proceeding with additional rounds of this program, the Department should undertake more rigorous planning and analysis to lay out clear objectives and develop the most cost-effective means of achieving them.

A 15-percent deficit in mid-ranked Foreign Service positions due to decreased hiring in the 1990s continues to hamper staffing for key positions worldwide. The Department could only overcome this problem before 2010 through an extraordinary intervention in the hiring and promotion process for Foreign Service officers. The Civil Service fills some key policy jobs in Washington, provides crucial administrative support to the Department, and increasingly provides support in critical posts overseas, but it also faces increasing retirements and recruiting challenges.

Over 38,000 locally employed (LE) staff also work for the Department at overseas posts. The Department needs to codify and strengthen its commitment to LE staff.

The Department needs an effective program for returning to work those employees who have been injured on the job and are receiving benefits under the Federal Employees Compensation Act. A systematic effort to contact and encourage injured employees to return to work as soon as medically feasible is an industry and government best practice, and a key to reduced claimant fraud. However, although officials in HR had drafted a policy paper for such a program, no program has been established because HR said there were uncertainties regarding which bureau within the Department should develop and manage the program.

COUNTERTERRORISM AND BORDER SECURITY

Cross-border problems, which have a direct impact on U.S. business interests, environmental safety, quality of life, and border security, continue to challenge the Department. The U.S. Embassy in Mexico and the Bureau of Western Hemisphere Affairs emphasize border issues in their strategic plans. However, neither has dedicated sufficient staff or attention to the coordination of those issues. Border posts need additional positions to allow them to focus on solving the problems.

With looming increases in consular workload and in demands on consular resources over the next five years, there is also a need to address non-consular issues and their priority in the operations of the border posts. If non-consular issues are not properly managed now, it will be impossible to do so once the wave of U.S. passport and nonimmigrant visa applications hits the border. The decision to assign regional security officers to each border consulate has improved the security of the consulates and enhanced the coordination of cross-border law enforcement issues that in turn affect bilateral commercial development.

PUBLIC DIPLOMACY

The Under Secretary for Public Diplomacy and Public Affairs has made a personal priority of improving public diplomacy coordination within the Department and in the interagency process, and has made important progress in this area, including implementing recommendations of the OIG and the Government Accountability Office. Public diplomacy strategic planning has improved, but could be stronger, especially at the mission level.

The Department has also made important, promising progress in the difficult task of measuring the impact and outcomes of public diplomacy efforts rather than just totaling public diplomacy activities undertaken, as had primarily been done in the past. The prospects for further progress are encouraging. The need to increase public diplomacy officers' foreign language capabilities is a long-term challenge.

POST-CONFLICT STABILIZATION AND RECONSTRUCTION

Despite its broad mandate, the Office of the Coordinator for Reconstruction and Stabilization (S/CRS) has not yet carved out a leadership role in the management of reconstruction and stabilization crises. It has remained on the periphery in the interagency handling of such crises, playing only an incremental role.

At present, S/CRS has four central issues on its agenda that will determine whether it will expand significantly the parameters of its present responsibilities and establish for itself a viable institutional role. These issues are: a new relationship with the Director of Foreign Assistance, a major role in implementing the S/CRS charter in National Security Presidential Directive-44, a lead role in developing the Civilian Reserve Corps, and management of the Department of Defense's FY 2007 $100-million transfer authority.

Although S/CRS has not played the role its proponents had hoped, the S/CRS divisions have continued to develop doctrine, manage exercises, and provide useful, albeit limited, assistance to embassies through the Active Response Corps. S/CRS has excellent leadership, an able committed staff, and surprisingly high morale; however, it needs to restructure. Its current organizational pattern does not adequately reflect the actual delineation of responsibilities within the office and inhibits coordination and communication.

SUMMARY OF FINANCIAL STATEMENT AUDIT AND MANAGEMENT ASSURANCES

SUMMARY OF FINANCIAL STATEMENT AUDIT

Audit Opinion:	**Disclaimer**
Restatement:	**No**

MATERIAL WEAKNESSES	BEGINNING BALANCE	NEW	RESOLVED	ENDING BALANCE
Management of Unliquidated Obligations	0	1	0	1
Accounting for Personal Property	0	1	0	1
Total Material Weaknesses	0	2	0	2

SUMMARY OF MANAGEMENT ASSURANCES

EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING (FMFIA § 2)						
Statement of Assurance:	qualified					
MATERIAL WEAKNESSES	BEGINNING BALANCE	NEW	RESOLVED	CONSOLIDATED	REASSESSED	ENDING BALANCE
Management of Unliquidated Obligations	0	1	0	0	0	1
Total Material Weaknesses	0	1	0	0	0	1
EFFECTIVENESS OF INTERNAL CONTROL OVER OPERATIONS (FMFIA § 2)						
Statement of Assurance:	qualified					
MATERIAL WEAKNESSES	BEGINNING BALANCE	NEW	RESOLVED	CONSOLIDATED	REASSESSED	ENDING BALANCE
Management of Unliquidated Obligations	0	1	0	0	0	1
Total Material Weaknesses	0	1	0	0	0	1
CONFORMANCE WITH FINANCIAL MANAGEMENT SYSTEM REQUIREMENTS (FMFIA § 4)						
Statement of Assurance:	qualified					

COMPLIANCE WITH FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT (FFMIA)		
	AGENCY	AUDITOR
Overall Substantial Compliance	Yes	No
1. System Requirements	Yes	No
2. Accounting Standards	Yes	No
3. USSGL at Transaction Level	Yes	Yes

FINANCIAL PERFORMANCE METRICS

Below is a year-end summary provided to senior managers of the Department's performance relative to the Chief Financial Officers (CFO) Council financial metrics. Because of the unique aspects of operating in both a domestic and overseas environment, the Department adjusts these metrics were appropriate to reflect a measure for domestic operations and a separate indicator for overseas performance. A good example of this would be *Percent of Vendor Payments Made by EFT* where the domestic percentage target would be higher than the overseas target to convey the differences in the overseas banking systems inability to handle EFT transactions.

For FY 2007, the Department's financial metrics improved to green in two categories, fell to red in one category, and remained constant in the others. The Government-wide metrics are as of May 2007.

Measure and Frequency	Why Is It Important	State Sept 2007		State Sept 2006		Governmentwide Performance Standards			Governmentwide May 2007	
		Actual	Rating	Actual	Rating	Fully Successful	Minimally Successful	Unsuccessful	Actual	Rating
Fund Balance With Treasury - Net Percent Unreconciled [Monthly]	Smaller reconciliation differences translate to greater integrity of financial reports and budget results.	1%		0.90%		< = 2%	> 2% to < = 10%	> 10%	0%	
Percent of Amount in Suspense (Absolute) Greater than 60 Days Old [Quarterly]	Timely reconciliation supports clean audits and accurate financial information.	15%		90.00%		< = 10%	> 10% to < = 20%	> 20%	24%	
Percent of Accounts Receivable from Public Delinquent Over 180 Days [Quarterly]	Actively collecting debt improves management accountability and reduces Treasury borrowing.	53%		40.70%		< = 10%	> 10% to < = 20%	> 20%	14%	
Percent of Vendor Payments made Electronically [Monthly]	Use of electronic funds transfer saves money, reduces paperwork, and improves cash management.	97%		95.40%		> = 96%	> = 90% to < 96%	< 90%	96%	
Percent Non-Credit Card Invoices Paid On-Time [Monthly]	Timely payment reduces interest charges and reflects a high degree of accountability and integrity.	84%		79.40%		> = 98%	> = 97% to < 98%	< 97%	100%	
Interest Penalties Paid as a Percent of Total Payments [Monthly]	Smaller percentages of interest paid shows that an agency is paying its bills on time which saves money and allows funds to be used for their intended purpose.	0.08%		0.0100%		> = .02%	> .02 to < = .03%	> .03%	0.03%	
Travel Card Delinquency Rates - Individually Billed Accounts [Monthly]	Reducing outstanding travel card balances helps increase rebates to agencies.	2%		2.30%		> = 2%	> 2% to < = 4%	> 4%	3%	
Travel Card Delinquency Rates - Centrally Billed Account [Monthly]	Reducing outstanding travel card balances helps increase rebates to agencies.	0.0%		0.90%		>= 0%	> 0% to < = 1.5%	> 1.5%	9.4%	
Purchase Card Delinquency Rate [Monthly]	Reducing outstanding purchase card balances helps increase rebates to agencies and reduces interest payments.	0.1%		0.88%		>= 0%	> 0% to < = 1.5%	> 1.5%	3.6%	

WOMEN IN DIPLOMACY*

Ever since women were permitted to join the U.S. diplomatic corps in 1922, they have slowly but surely made their way to the highest leadership positions in the State Department. In 1933, Ruth Bryan Owen was appointed as the first female chief of mission as head of the U.S. embassy for Denmark and Iceland. The first woman appointed chief of mission at the ambassador level, Helen Eugenie Moore Anderson, was named ambassador to Denmark in 1949.

In the first 42 years following Ruth Owen's appointment as chief of mission (1933-1976), the number of female appointments as chief of mission or assistant secretaries of State stayed well within the single digits. The Ford administration broke this barrier, appointing seven female chiefs of mission and three women to senior positions. With the Carter administration, rapid progress began: 18 women were made chiefs of mission and 10 were appointed to other senior positions. Presidents Ronald Reagan and George H.W. Bush continued the trend, with 33 and 37 female appointments, respectively. The Clinton administration made a larger leap, appointing 116 women to the senior-most diplomatic posts. In his first term, President George W. Bush named 69 women to the highest diplomatic posts.

Since 2001, several women have been named ambassadors to Arab countries. Maureen Quinn was ambassador to Qatar from 2001 to 2004. During the same period, Marcelle Wahba was ambassador to the United Arab Emirates, and was succeeded by Michelle Sison, who had been the deputy chief of mission in Pakistan from 2000 to 2002. In 2003, Margaret Scobey was appointed ambassador to Syria. The rapid gains of the past decade are the culmination of over 70 years of incremental advances for women in U.S. diplomacy, and position women for new breakthroughs in leadership in the months and years ahead.

Firsts for Female Diplomats

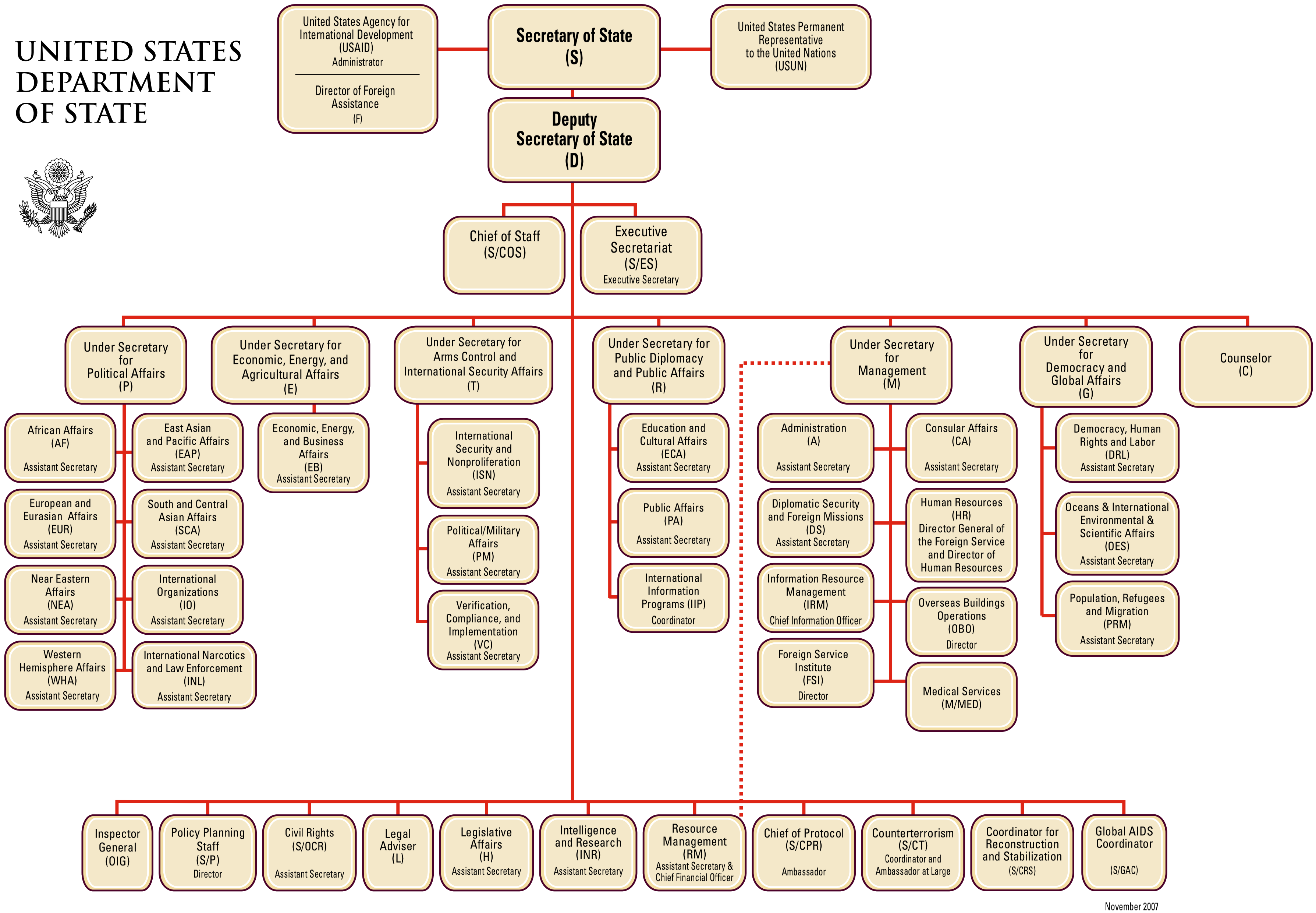
1922	First woman admitted to the U.S. Foreign Service: Lucile Atcherson (FSO).*
1933	First female chief of mission at the minister rank: Ruth Bryan Owen, Denmark and Iceland.
1949	First woman chief of mission at the ambassador rank: Helen Eugenie Moore Anderson, Denmark.
1953	First female career diplomat chief of mission: Frances Willis (FSO), Switzerland. She was the third woman to be admitted to the Foreign Service.
1961	First female chief of mission outside of Europe and first to South Asia: Frances Willis (FSO), Ceylon.
1962	First woman to attain the rank of career ambassador: Frances Willis (FSO).
1965	First female African-American ambassador: Patricia Harris, Luxembourg.
1969	First female ambassador to a Caribbean country: Eileen Roberts Donovan (FSO), Barbados.
1971	First woman appointed to an international organization: Betty Dillon, representative to the International Civil Aviation Organization.
1972	First female ambassador to an African country: Jean Wilkowski (FSO), Zambia.
1973	First female assistant secretary of State: Carol Laise Bunker (FSO), Public Affairs.
1975	First female ambassador to a Pacific island nation: Mary Olmsted (FSO), Papua New Guinea and the Solomon Islands.
1977	First female Hispanic-American ambassador and first female ambassador to a Central American country: Mari-Luci Jarimillo, Honduras.
1977	First female Asian-American assistant secretary of State: Patsy Takemoto Mink, Oceans and International Environmental and Scientific Affairs.
1977	First female under secretary of State: Lucy Benson, Security Assistance, Science and Technology.
1978	First female ambassador to a South American country: Nancy Ostrander (FSO), Suriname.
1979	First female ambassador to an Asian country: Patricia Byrne (FSO), Burma.
1981	First female U.S. Permanent Representative to the United Nations: Jeane Kirkpatrick. In 1993, Madeleine Albright became the second woman appointed as U.S. Permanent Representative to the U.N.
1985	First woman to head a geographic bureau: Rozanne Ridgway (FSO), Assistant Secretary for European and Canadian Affairs.
1988	First female ambassador to a Middle Eastern country: April Catherine Glaspie (FSO), Iraq.
1994	First female Asian-American ambassador: March Fong Eu, Micronesia.
1997	First female Secretary of State: Madeleine Albright.
2005	First female African-American Secretary of State: Condoleezza Rice.

**(FSO) Foreign Service officer. All others are non-career, political appointees.*

* This article and the accompanying chart are excerpted from Ann Wright's article, "Breaking Through Diplomacy's Glass Ceiling," published in the October 2005 issue of *Foreign Service Journal*. The complete article can be found at the American Foreign Service Association's website at www.afsa.org.

Appendices

UNITED STATES DEPARTMENT OF STATE



GLOSSARY OF ACRONYMS

AFR	Agency Financial Report
Appendix A	(Refers to) OMB Circular A-136, Appendix A
CFMS	Central Financial Management System
CFO	Chief Financial Officer
CIF	Capital Investment Fund
COTS	Commercial Off-The-Shelf
CSRS	Civil Service Retirement System
D&CP	Diplomatic and Consular Programs
DG	Director General of the Foreign Service
DOD	Department of Defense
DOL	Department of Labor
DOS	U.S. Department of State
ECE	Economic Commission for Europe
EFT	Electronic Funds Transfer
ESCM	Embassy Security, Construction, Maintenance Appropriation
FAA	Federal Aviation Agency
FASAB	Federal Accounting Standards Advisory Board
FECA	Federal Employees Compensation Act
FEGLIP	Federal Employees Life Insurance Program
FEHB	Federal Employees Health Benefits Program
FERS	Federal Employees Retirement System
FFMIA	Federal Financial Management Improvement Act
FISMA	Federal Information Security Act
FMFIA	Federal Managers' Financial Integrity Act
FSC	Financial Services Center
FSN	Foreign Service Nationals
FSNDCF	Foreign Service National Defined Contributions Retirement Fund
FSNSLTF	Foreign Service National Separation
FSRDF	Foreign Service Retirement and Disability Fund
FSRDS	Foreign Service Retirement and Disability System
FSPS	Foreign Service Pension System
FTE	Full Time Employee
FWCB	Federal Workers Compensation Benefits
G-8	Group of Eight (major industrialized nations)
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GFMS	Global Financial Management System
GFS	Global Financial Services
GMRA	Government Management Reform Act
GPRA	Government Performance and Results Act
HHS	Department of Health and Human Services
HR	Bureau of Human Resources (DoS)
IBWC	International Boundary and Water Commission
ICASS	International Cooperative Administrative Support Services (DoS)
ICOFR	Internal Control Over Financial Reporting

IG	Inspector General
IIP	Bureau of International Information Programs (DoS)
ILMS	Integrated Logistics Management System
INL	Bureau of International Narcotics and Law Enforcement Affairs (DoS)
IPIA	Improper Payments Information Act
ISP	Information Security Program
IT	Information Technology
JAMS	Joint Assistance Management System
LE	Locally Employed
MCA	Managerial Cost Accounting
MCSC	Management Control Steering Committee
OIG	Office of Inspector General
OMB	Office of Management and Budget
OPM	Office of Personnel Management
P&F	Program and Financing Schedule
PART	Program Assessment Rating Tool
PEPFAR	President's Emergency Plan for AIDS Relief
PMA	President's Management Agenda
PMS	Payment Management System (HHS)
PP&E	Property, Plant and Equipment
PSC	Personal Service Contractor
PSU	Post Support Unit
RCSO	Regional Computer Security Officer
RM	Bureau of Resource Management (DoS)
RSI	Required Supplementary Information
SAT	Senior Assessment Team (FMFIA)
S/CRS	Office of the Coordinator for Reconstruction and Stabilization (DoS)
SFFAS	Statements of Federal Financial Accounting Standards
UDO	Undelivered Orders
UN	United Nations
USAID	United States Agency of International Development
USG	U.S. Government
WCF	Working Capital Fund

ACKNOWLEDGMENTS

This Financial Report was produced with the energies and talents of Department of State staff in Washington, D.C., and our offices and posts around the world. To these dedicated individuals we offer our sincerest thanks and acknowledgment. In particular, we recognize the following individuals and organizations for their contributions:

The AFR Core Team: *Stephanie Cabell, Kevin Covert, and Frank Sullivan.*

Staff from the Office of the Deputy Chief Financial Officer: *Eileen Angle, Anthony Belliotti, Steven Chu, Melissa Clarke, Melinda DeCorte, Tynesha Douglass, Bill French, Carol Gower, Michelle Green, Shelly Harvey, Don Hunter, Sherril Hyson, Matthew Johnson, Ola Kalpazzi, Yen Le, Jeffrey Long, Irwin Mazin, Doris Perry, Marshelle Richardson, Troy Scaptura, Sanjay Shah, Merredith Shears, Catherine Smith, Mark Terman, Richard Thompson, Dan Tonzi, Peter Vieira, Lisa Wyffels.*

Global Financial Services *personnel in Charleston, Bangkok, Paris and Washington.*

We would also like to acknowledge the ***Office of Inspector General*** *for their objective review of the Department's performance and* ***Leonard G. Birnbaum and Company*** *for the professional manner in which they conducted the audit of the FY 2007 financial statements.*

We offer our special thanks to ***The DesignPond****, in particular Michael James, Sheri Beauregard, and Don James for their outstanding contributions to the design of this report.*

FY 2007 PHOTO CREDITS

Associated Press: I **Department of State:** II

The Financial Report for Fiscal Year 2007 is published by the

U.S. Department of State

Bureau of Resource Management
Office of Financial Policy, Reporting and Analysis

An electronic version is available on the World Wide Web at

http://www.state.gov/s/d/rm/rls/perfrpt/

Please call (202) 261-8620 with comments, suggestions, or requests.

U.S. Department of State Publication No. 11475

Bureau of Public Affairs
November 2007

Note: The Bureau of Public Affairs, Office of Electronic Information (PA/EI) assisted the Bureau of Resource Management with the production of the FY 2007 Financial Report, including photos from AP/Wide World.

2201 C Street, N.W.
Washington, D.C. 20520
(202) 647-4000

www.state.gov