# Audit Report

OIG-07-010

Audit of the Department of the Treasury's Fiscal Years 2006 and 2005 Financial Statements

November 15, 2006

# Office of Inspector General

## Department of the Treasury

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

November 15, 2006

**MEMORANDUM FOR SECRETARY PAULSON**

**FROM:** Harold Damelin
Inspector General

**SUBJECT:** Audit of the Department of the Treasury's Financial Statements for Fiscal Years 2006 and 2005

**SUMMARY**

I am pleased to transmit the attached report presenting the results of the audit of the Department of the Treasury's (the Department) financial statements as of and for the fiscal years (FY) ending September 30, 2006 and 2005. The audit is required by the Chief Financial Officers Act of 1990, as expanded by the Government Management Reform Act of 1994.

**DISCUSSION**

We contracted with the independent certified public accounting firm KPMG LLP to audit the FY 2006 and 2005 financial statements. The contract required that the audit be performed in accordance with generally accepted government auditing standards; Office of Management and Budget Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*; and, the *GAO/PCIE Financial Audit Manual*.

In its audit of the Department of the Treasury, KPMG LLP:

- found that the financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles;

- reported that the four material weaknesses and one other reportable condition in financial management practices identified by the auditor of the Internal Revenue Service (IRS), collectively represent a material weakness for the Department as a whole;

- reported that weaknesses in 1) electronic data processing controls and information security programs over financial systems, and 2) controls over transactions and balances related to the International Assistance Programs, represent reportable conditions for the Department as a whole;

- reported that the Department's financial management systems did not substantially comply with the requirements of the *Federal Financial Management Improvement Act of 1996*;

- reported two instances of noncompliance with laws and regulations related to the *Internal Revenue Code* Section 6325 and the *Federal Information Security Management Act of 2002;* and

- reported two instances of possible *Anti-deficiency Act* violations related to transactions and activities of the Treasury Franchise Fund and the Departmental Offices.

In connection with the contract, we reviewed KPMG LLP's report and related documentation and inquired of its personnel. Our review, as differentiated from an audit in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the financial statements or conclusions about the effectiveness of internal control or on whether the Department of the Treasury's financial management systems substantially complied with the *Federal Financial Management Improvement Act of 1996*; or conclusions on compliance with laws and regulations. KPMG LLP is responsible for the attached auditor's report dated November 13, 2006, and the conclusions expressed in that report. However, our review disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

The IRS's pervasive internal control weaknesses have existed since audits of its financial statement were initiated in FY 1992. The Government Accountability Office (GAO), the auditor of the IRS's financial statements for the FYs ending September 30, 2006 and 2005, reported that the bureau continued to make great strides in addressing its financial management challenges and substantially mitigated several material weaknesses in its internal controls, particularly with respect to cost accounting and its property and equipment records. However, because of budgetary concerns and advances in automated financial management system technologies, the GAO reported that IRS is no longer committed to the future releases of its Integrated Financial System (IFS) that were once intended to resolve many of its most serious financial management issues, and is currently considering alternatives. IRS has not yet committed to an alternative approach nor has funding been appropriated. Additionally, IRS has not determined how to resolve issues related to the lack of integration between IFS and its tax processing systems. Consequently, it is unclear how or when these issues will be resolved. Continued involvement by IRS officials and the Department's senior leadership is essential to effectively address these matters.

Should you or your staff have questions, you may contact me at (202) 622-1090 or
Marla A. Freedman, Assistant Inspector General for Audit, at (202) 927-5400.

Attachment

cc: Sandra L. Pack
Assistant Secretary for Management
and Chief Financial Officer

# SECTION I –

# INDEPENDENT AUDITORS' REPORT, MANAGEMENT'S RESPONSE, AND REPORT DISTRIBUTION

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**KPMG LLP**
2001 M Street, NW
Washington, DC 20036

# Independent Auditors' Report

Inspector General
U.S. Department of the Treasury:

We have audited the accompanying consolidated balance sheets of the U.S. Department of the Treasury (the Department) as of September 30, 2006 and 2005, and the related consolidated statements of net cost, changes in net position, and financing, the combined statements of budgetary resources, and the statements of custodial activity (consolidated financial statements), for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these consolidated financial statements. These consolidated financial statements are incorporated in the accompanying *Department of the Treasury Fiscal Year 2006 Performance and Accountability Report (Performance and Accountability Report)*.

We did not audit the amounts included in the consolidated financial statements related to the Internal Revenue Service (IRS), a component entity of the Department. The financial statements of the IRS were audited by another auditor whose report has been provided to us. Our opinion, insofar as it relates to the amounts included for IRS's financial statements, is based solely on the report of the other auditor.

In connection with the fiscal year 2006 audits, we, and the other auditor, also considered the Department's internal controls over financial reporting and performance measures, and tested the Department's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on these consolidated financial statements.

## SUMMARY

As stated in our opinion below on the consolidated financial statements, based on our audits and the report of the other auditor, we concluded that the Department's consolidated financial statements as of and for the years ended September 30, 2006 and 2005, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles.

Also, as discussed in our opinion, in fiscal year 2006, the Department adopted new reporting requirements for earmarked funds.

Our, and the other auditor's consideration of internal controls over financial reporting and performance measures resulted in the following conditions being identified as reportable conditions:

- Financial Management Practices at the IRS (Repeat Condition);
- Electronic Data Processing (EDP) Controls and Information Security Programs Over Financial Systems (Repeat Condition); and
- Controls Over Transactions and Balances Related to the International Assistance Programs.

We consider the reportable condition related to financial management practices at the IRS noted above, to be a material weakness.

The results of our tests, and the tests performed by the other auditor, of compliance with certain provisions of laws, regulations, contracts, and grant agreements disclosed instances of noncompliance with *Internal Revenue Code* (IRC) Section 6325, and the *Federal Information Security Management Act of 2002* (FISMA), that are required to be reported under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements* (OMB Bulletin No. 06-03). In addition, the Department's financial management systems did not substantially comply with the *Federal Financial Management Improvement Act of 1996* (FFMIA) requirements related to compliance with Federal financial management system requirements (FFMSR), applicable Federal accounting standards, and the U.S. Government Standard General Ledger (SGL) at the transaction level.

As discussed in the Other Matters section of this report, the Department's Office of General Counsel has informed the Department of two instances of possible *Antideficiency Act* violations related to certain transactions and activities within the Treasury Franchise Fund and Departmental Offices. The facts surrounding these possible violations are currently under review by General Counsel and management.

The following sections discuss our opinion on the Department's consolidated financial statements, our, and the other auditor's consideration of the Department's internal control over financial reporting and performance measures, and tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, and management's and the auditors' responsibilities.

## OPINION ON THE FINANCIAL STATEMENTS

We have audited the accompanying consolidated balance sheets of the U.S. Department of the Treasury as of September 30, 2006 and 2005, and the related consolidated statements of net cost, changes in net position and financing, the combined statements of budgetary resources, and the statements of custodial activity for the years then ended. We did not audit the amounts included in the consolidated financial statements related to the financial statements of the IRS, a component entity of the Department, which reflects total assets of $26 billion and $27 billion, net costs of operations of $11.5 billion each year, and custodial revenues of $2.5 trillion and $2.3 trillion, as of and for the years ended September 30, 2006 and 2005, respectively. The financial statements of the IRS as of and for the years ended September 30, 2006 and 2005, were audited by another auditor whose report dated October 31, 2006, has been provided to us and our opinion, insofar as it relates to the amounts included for the IRS's financial statements, is based solely on the report of the other auditor.

In our opinion, based on our audits and the report of the other auditor, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Department of the Treasury as of September 30, 2006 and 2005, and its net costs, changes in net position, budgetary resources, reconciliation of net costs to budgetary obligations, and custodial activity, for the years then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, the Department changed its method of reporting earmarked funds in fiscal year 2006 to adopt the provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards No. 27, *Identifying and Reporting Earmarked Funds*.

The information in the *Performance and Accountability Report* in Part I – *Management's Discussion and Analysis,* and the Required Supplemental Information section of Part III – *Annual Financial Report,* is not a required part of the consolidated financial statements, but is supplementary information required by U.S. generally accepted accounting principles, and OMB Circular A-136, *Financial Reporting Requirements* (OMB Circular No. A-136). We, and the other auditor, have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audits, and the audits of the other auditor, were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The information in the *Performance and Accountability Report* in Part II – *Annual Performance Report*; the Other Accompanying Information in the Required Supplemental Information section of Part III – *Annual Financial Report*; and Part IV – *Appendices*, are presented for purposes of additional analysis and are not required as part of the consolidated financial statements. This information has not been subjected to auditing procedures, and, accordingly, we express no opinion on it.

## INTERNAL CONTROL OVER FINANCIAL REPORTING

Our, and the other auditor's consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our, and the other auditor's judgment, could adversely affect the Department's ability to record, process, summarize, and report financial data consistent with the assertions by management in the consolidated financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to the consolidated financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements, due to error or fraud, may nevertheless occur and not be detected.

In our fiscal year 2006 audit, we, and the other auditor, noted certain matters, summarized below, involving internal control over financial reporting and its operation that we consider to be reportable conditions.

## MATERIAL WEAKNESS

### Financial Management Practices at the IRS (Repeat Condition)

IRS has continued to make progress in addressing its financial management challenges and has resolved or substantially mitigated several material weaknesses and reportable conditions in its internal controls. However, serious internal control and financial management systems deficiencies still exist, and the IRS again had to rely extensively on resource-intensive compensating processes to prepare its financial statements.

Consequently, IRS personnel will continue to be challenged to sustain the level of effort needed to produce reliable financial statements timely until IRS successfully addresses the underlying systems and internal control weaknesses. These challenges affect IRS's ability to fulfill its responsibilities as the nation's tax collector because it is unable to obtain comprehensive, timely, useful information for day-to-day decision making.

The material weaknesses and the other reportable condition in internal control over financial reporting identified by the auditors of IRS's financial statements, all of which are repeat conditions, and collectively considered a material weakness for the Department as a whole, are summarized as follows:

- Weaknesses in controls over the financial reporting process, resulting in IRS (1) not being able to prepare reliable financial statements without extensive compensating procedures, and (2) not having current and reliable ongoing information to support management decision making and prepare cost-based performance measures;

- Weaknesses in controls over unpaid tax assessments, resulting in IRS's inability to properly manage unpaid assessments and leading to increased taxpayer burden;

- Weaknesses in controls over the identification and collection of tax revenues due the U.S. Government, and over the issuance of tax refunds, resulting in lost revenue to the U.S. Government, and allowing potentially billions of dollars in improper payments; and

- Weaknesses in information security controls, resulting in increased risk of unauthorized individuals being allowed to access, alter, or abuse proprietary IRS programs and electronic data and taxpayer information.

The material weaknesses in internal control noted above may adversely affect any decision by IRS's management that is based, in whole or in part, on information that is inaccurate because of these weaknesses.

One other reportable condition, a repeat condition, was identified that involved deficiencies in controls over hard-copy tax receipts and taxpayer data, which increase the U.S. government's and taxpayers' risk of loss or inappropriate disclosure of taxpayer data.

Additional details related to the material weaknesses and the reportable condition identified above have been provided to IRS management by the auditors of the IRS's financial statements.

**Recommendations**

Recommendations to address the material weaknesses and other reportable condition discussed above have been provided to IRS management by the auditors of the IRS's financial statements. We recommend that the Assistant Secretary for Management and Chief Financial Officer provide effective oversight to ensure that corrective actions are taken by the IRS to fully address these material weaknesses and the other reportable condition.

**OTHER REPORTABLE CONDITIONS**

**EDP Controls and Information Security Programs Over Financial Systems (Repeat Condition)**

Information controls and security programs at the Department require additional improvements. The weaknesses identified are summarized below.

***Financial Management Service (FMS)***

During fiscal year 2006, FMS continued to make progress in addressing information technology (IT) general controls weaknesses raised in prior years. However, current year tests conducted over IT general controls revealed the following weaknesses:

- **Entity-wide Security Management** – Although FMS has demonstrated its ability to remediate specific findings, current year security control deficiencies identified reveal inconsistencies in corrective actions taken, in that, while weaknesses were corrected in some systems and platforms, they continued to exist in others. An entity-wide program for security planning and management represents the foundation for an entity's security control structure and a reflection of senior management's commitment to addressing security risks. Without a well designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood, and improperly implemented; and controls may be inconsistently applied.

- **Access Controls** – Although prior access control findings have been substantially addressed, additional access control weaknesses were identified this year. Access controls are designed to limit or detect access to computer programs, data, equipment, and facilities to protect these resources from unauthorized modification, disclosure, loss, or impairment. Such controls include logical and physical security access controls. A comprehensive access control security program is needed to fully address the administration of access controls in order to increase the reliability of computerized data and decrease the risk of destruction or inappropriate disclosure of data.

- **Service Continuity** – Connectivity issues were noted during a disaster and system failover exercise related to the Treasury Check Information System (TCIS) application, a new system implemented this year. In addition, system unavailability and excessive downtime for extended periods of time were also noted. Contingency planning should address critical services to system resources to ensure that operations will continue in the event of a disaster or other service interruptions. Such plans and procedures should be a key part of business continuity plans.

The above issues collectively serve to weaken the IT general control environment at FMS.

***Departmental Bureaus and Offices***

During fiscal year 2006, the Department took various steps to improve its IT general control environment and to address prior year IT general control issues; however,  additional improvements are needed in the areas of certification and accreditation, security awareness, training employees with significant security responsibilities, tracking corrective actions, identifying and documenting system interfaces, security self-assessments, configuration management, and incident response, at various Departmental bureaus and offices.

The Department's Office of Inspector General report titled *Information Technology: 2006 Evaluation of Treasury's FISMA Implementation* dated September 29, 2006 (2006 FISMA Evaluation Report), which incorporated the results of the Treasury Inspector General for the Tax Administration's evaluation of IRS's systems, indicated that despite notable accomplishments to achieve compliance with FISMA, various security deficiencies identified throughout the Department, in the aggregate, constitute substantial noncompliance with FISMA. FISMA lays out a framework for required annual information security reviews, reporting, and remediation planning by Federal agencies. It is intended to strengthen information security by requiring agencies to develop, document, and implement agency-wide information security programs. The elements required by FISMA, as described below, also constitute an integral part of an effective internal control structure for information systems:

- Periodic testing and evaluation of the effectiveness of information security policies, procedures, and practices;

- Security awareness training for Department personnel, including contractors;

- A process for planning, implementing, evaluating, and documenting remedial action to address information security deficiencies; and

- Plans and procedures to ensure continuity of operations for information systems that support the operations and assets of the Department.

A key reason for the Department's information security weaknesses is that it has not yet fully implemented an agency-wide information security program to ensure that controls are effectively established and maintained to meet FISMA requirements.

**Recommendations**

Recommendations will be provided to FMS management in a separate letter. The fiscal year 2006 FISMA Evaluation Report has been provided to the Department's Chief Information Officer.

We recommend that the Department's Chief Information Officer provide effective oversight and the resources necessary to ensure that information security requirements over financial systems are implemented completely and timely throughout the Department.

**Controls Over Transactions and Balances Related to the International Assistance Programs**

Improvements in current accounting policies and procedures are needed for monthly reconciliations of transactions related to the *United States Quota, International Monetary Fund (IMF) Transfer to Treasury* account (fund) that is managed by the Department's Office of International Affairs (IA). The accounting and reporting of these transactions is performed by the Credit Accounting Branch (CAB) of Treasury's FMS. A review of proprietary-to-budgetary account relationships using IA's data applicable to this fund for the nine-month period ended June 30, 2006, revealed a proprietary-to-budgetary account relationship error in the net amount of approximately $1.4 billion. This was caused by a transaction posting logic error that we identified in August 2006. This error impacted various financial statement line items that are supported by these accounts. Because this was not identified in a timely manner, it also resulted in the submission of erroneous IA account balances for inclusion in Treasury's nine months' quarterly consolidated financial reporting submission to the OMB.

The *Federal Managers' Financial Integrity Act of 1982* (FMFIA) requires the establishment of internal accounting and administrative controls by each executive agency to be established that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.

This discrepancy occurred primarily because CAB's accounting procedures did not include a requirement to calculate certain proprietary-to-budgetary account relationship reconciliations during the year. These reconciliations were only performed at year-end. Since the IA's activities related to the IMF involve significant transaction amounts throughout the year, any error that occurs may have significant financial reporting impact. Corrective actions were taken as soon as the error was identified and procedures were revised to include appropriate monthly reconciliations.

**Recommendation**

We recommend that the Assistant Secretary for Management and Chief Financial Officer ensure that IA management continue to work with CAB to ensure that corrective actions taken remain in place so that monthly proprietary-to-budgetary account relationship reconciliations continue to be performed for the IMF account balances, and any differences are corrected in a timely manner.

**INTERNAL CONTROL OVER REQUIRED PERFORMANCE MEASURES**

Under OMB Bulletin No. 06-03, the definition of material weaknesses is extended to other controls as follows. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to a performance measure or aggregation of related performance measures, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.

Our, and the other auditor's consideration of the internal control over the design and operation of internal control over the existence and completeness assertions related to key performance measures would not necessarily disclose all matters involving the internal control and its operation related to the internal control over the existence and completeness assertions related to key performance measures that might be material weaknesses.

Further, in our fiscal year 2006 audit, we, and the other auditor, noted no matters involving the design and operation of the internal control over the existence and completeness assertions related to key performance measures that we considered to be material weaknesses as defined above.

* * * * * *

We also noted other matters involving internal control over financial reporting and its operation that we will report to the management of the Department in a separate letter dated November 13, 2006.

**COMPLIANCE AND OTHER MATTERS**

Our tests, and the tests performed by the other auditor, of compliance with certain provisions of laws, regulations, contracts, and grant agreements, as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed the following instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 06-03.

- ***Noncompliance with IRC Section 6325*** – The IRC grants IRS the power to file a lien against the property of any taxpayer who neglects or refuses to pay all assessed Federal taxes. Under IRC Section 6325, the IRS is required to release a Federal tax lien within 30 days after the date the tax liability is satisfied or has become legally unenforceable or the Secretary of the Treasury has accepted a bond for the assessed tax. The fiscal year 2006 audit identified instances in which the IRS did not release the applicable Federal tax lien within 30 days of the tax liability being either paid off or abated as required by the IRC (Repeat Condition).

- ***Noncompliance with FISMA*** – Information security weaknesses continue to exist throughout the Department, despite notable progress made in fiscal year 2006, as discussed in the Internal Control Over Financial Reporting section above. These deficiencies constitute substantial noncompliance with FISMA (Repeat Condition).

The results of our tests, and the tests performed by the other auditor, of compliance with certain provisions of other laws, regulations, contracts, and grant agreements as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 06-03.

The results of our tests and the tests performed by the other auditor, disclosed instances where the Department's financial management systems did not substantially comply with FFMIA Section 803(a) requirements related to compliance with FFMSR, applicable Federal accounting standards, and the SGL at the transaction level, as described below.

These instances of noncompliance with FFMSR are summarized below:

- IRS's financial management systems do not provide timely and reliable information for financial reporting and preparation of financial statements. IRS had to rely extensively on resource-intensive compensating procedures to generate reliable financial statements. IRS also lacks a subsidiary ledger for its unpaid assessments and lacks an effective audit trail from its general ledger back to subsidiary detailed records and transaction source documents for material balances such as tax revenues and tax refunds.

- Deficiencies identified in information security controls at the IRS, resulting in increased risk of unauthorized individuals being allowed to access, alter, or abuse proprietary IRS programs and electronic data and taxpayer information.

These instances of noncompliance with Federal accounting standards are summarized below:

- Material weaknesses at the IRS related to controls over unpaid tax assessments, tax revenue, and refunds.

- IRS's financial management system cannot routinely accumulate and report the full cost of its activities.

The instance of noncompliance with the SGL at the transaction level is summarized below:

- IRS's general ledger system lacks an effective audit trail to detailed records and transaction source documents for material balances such as tax revenues and tax refunds.

The Secretary of the Treasury also has stated in the Secretary's Letter of Assurance, included in Part I – *Management's Discussion and Analysis*, of the accompanying *Performance and Accountability Report*, that the Department cannot provide assurance that its financial management systems are in substantial compliance with FFMIA. The Department's remedial actions and related timeframes are presented in Appendix E of the *Performance and Accountability Report*.

FFMIA requires that if the head of an agency determines that its financial management systems do not substantially comply with FFMIA, a remediation plan must be developed, in consultation with OMB, that describes the resources, remedies, and intermediate target dates for achieving substantial compliance. FFMIA also requires OMB concurrence with any plan not expected to bring the agency's system into substantial compliance within three years after a determination of noncompliance is made.

IRS has established a remediation plan to address the conditions affecting its systems' inability to comply substantially with the requirements of FFMIA. This plan outlines the actions to be taken to resolve these issues, but many future corrective actions are on hold and currently unfunded. Because of the long-term nature of IRS's systems modernization efforts, which IRS expects will resolve many of its most serious issues, many of the planned time frames exceed the three-year resolution period specified in FFMIA. However, for these instances IRS has received a waiver from this requirement from OMB, as authorized by FFMIA.

**Recommendations**

We recommend that the Assistant Secretary for Management and Chief Financial Officer provide effective oversight to ensure that (1) IRS implements appropriate controls so that Federal tax liens are released in accordance with Section 6325 of the IRC; (2) information security programs are implemented throughout the Department in accordance with FISMA; and (3) IRS determines a plan of action to solve its financial management problems so as to enable resolving the identified instances of financial management systems noncompliance with the requirements of FFMIA.

**Other Matters**

The Department's Office of General Counsel has informed the Department of two instances of possible *Antideficiency Act* violations related to transactions and activities of the Treasury Franchise Fund (Fund) and Departmental Offices (DO). Specifically, contracting and budgetary control weaknesses existing within the Fund may have allowed a potential violation of both the *Competition in Contracting Act* and the *Antideficiency Act* for a contract whose ceiling was exceeded without proper competition. In addition, another possible *Antideficiency Act* violation may have occurred with respect to certain fiscal year 2006 classified apportionments for the National Intelligence Program funds included in a DO appropriation because reimbursable funds were received and obligated prior to apportionment. The facts surrounding these matters are currently under review by General Counsel and management and a determination of noncompliance has not yet been made.

**Management's Response to Internal Control and Compliance Findings**

The Department's management has indicated in a separate letter immediately following this report that it concurs with the findings presented in this section of our report. Further, it has responded that it will take corrective action as necessary to ensure the matters presented are addressed by the respective bureau management within the Department.

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**RESPONSIBILITIES**

**Management's Responsibilities.** The United States Code Title 31 Section 3515 and 9106 require agencies to report annually to Congress on their financial status and any other information needed to fairly present their financial position and results of operations. To meet these reporting requirements, the Department prepares and submits financial statements in accordance with OMB Circular No. A-136.

Management is responsible for the consolidated financial statements, including:

- Preparing the consolidated financial statements in conformity with U.S. generally accepted accounting principles;
- Preparing the Management Discussion and Analysis (including the performance measures), and Required Supplemental Information;
- Establishing and maintaining effective internal controls; and
- Complying with laws, regulations, contracts, and grant agreements applicable to the Department, including FFMIA.

In fulfilling this responsibility, management is required to make estimates and judgments to assess the expected benefits and related costs of internal control policies.

**Auditors' Responsibilities.** Our responsibility is to express an opinion on the fiscal year 2006 and 2005 consolidated financial statements of the Department based on our audits and the report of the other auditor. We, and the other auditor, conducted our audits in accordance with U.S. generally accepted auditing standards, the standards applicable to financial audits contained in *Government Auditing Standards*, and OMB Bulletin No. 06-03. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall consolidated financial statement presentation.

We believe that our audits, and the report of the other auditor, related to the amounts included for the IRS's financial statements, provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2006 audit, we considered the Department's internal control over financial reporting, exclusive of the internal control over financial reporting related to the IRS, by obtaining an understanding of the Department's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. Internal control over financial reporting related to the IRS was considered by the other auditor whose report thereon dated October 31, 2006 has been provided to us. We, and the other auditor, limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 06-03. We did not test all internal controls relevant to operating objectives as broadly defined by the FMFIA. The objective of our audit and the other auditor's audit was not to provide an opinion on the Department's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

As further required by OMB Bulletin No. 06-03, in our fiscal year 2006 audit, with respect to internal control related to performance measures determined by management to be key and reported in Part I – *Management's Discussion and Analysis* and Part II – *Annual Performance Report* sections of the *Performance and Accountability Report*, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, and determined whether these internal controls had been placed in operation, exclusive of those related to performance measures presented for the IRS. An understanding of the design of significant internal controls relating to the existence and completeness assertions and determination as to whether these internal controls had been placed in operation related to the IRS's performance measures was obtained by the other auditor whose report thereon was provided to us. We, and the other auditor, limited our testing to those controls necessary to test and report on the internal control over key performance measures in accordance with OMB Bulletin No. 06-03. Our, and the other auditor's procedures were not designed to provide an opinion on internal control over reported performance measures and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether the Department's fiscal year 2006 consolidated financial statements are free of material misstatement, we, and the other auditor, performed tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 06-03, including certain provisions referred to in FFMIA. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to the Department. However, providing an opinion on compliance with laws, regulations, contracts, and grant agreements was not an objective of our audit or the other auditor's audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 06-03 and FFMIA, we are required to report whether the Department's financial management systems substantially comply with (1) FFMSR, (2) applicable Federal accounting standards, and (3) the United States Government SGL at the transaction level. To meet this requirement, we, and the other auditor, performed tests of compliance with FFMIA requirements.

**RESTRICTED USE**

This report is intended for the information and use of the Department's management, the Department's Office of Inspector General, OMB, the Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 13, 2006

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DEPARTMENT OF THE TREASURY
WASHINGTON

November 13, 2006

ASSISTANT SECRETARY

KPMG LLP
2001 M Street, N.W.
Washington, D.C. 20036

Ladies and Gentlemen:

On behalf of Secretary Paulson, I am responding to your draft audit report on the Department of the Treasury's FY 2006 financial statements.

All of our bureaus and program offices can be proud of the Department's success in issuing its Performance and Accountability Report by November 15th, for the fifth consecutive year. Further, I congratulate them for overcoming many obstacles to achieve another unqualified opinion on the Department's financial statements. Without their collective dedicated efforts, our accelerated reporting would not be possible.

These successful results also are due in large part to the high level of professionalism, technical expertise, and commitment demonstrated by KPMG in conducting the audit. I appreciate your efforts during the audit process to provide timely, constructive advice on how to improve our financial reporting. I am equally appreciative of the equivalent expertise and commitment level demonstrated by the other organizations involved in the audit process – the Office of the Inspector General, the Government Accountability Office, and the firms that conducted the audits at several of our bureaus.

The Treasury Department continued to make progress during FY 2006 in addressing financial management and systems deficiencies. The Internal Revenue Service made considerable progress in enhancing its tax revenue accounting and the functionality of its administrative accounting system. The IRS also developed a new comprehensive systems security plan to address known shortcomings. The Department was able to finalize its systems inventory and to make considerable progress in certifying and accrediting its systems. We will continue our efforts to address longstanding financial management weaknesses. For example, we have initiated quarterly status briefings for our bureau heads and the inclusion of specific material weakness performance targets in senior managers' performance plans.

We concur with the Departmental level material weakness, the reportable conditions, and the instances of noncompliance with laws and regulations described in your report. Corrective actions are in place or underway to address each of these items.

We appreciate the continuing professional, cooperative relationship that exists with both KPMG and the Office of Inspector General.

Sincerely,

Sandra L. Pack

Sandra L. Pack
Assistant Secretary for Management
and Chief Financial Officer

# Report Distribution

**Office of Management and Budget**

Director, Office of Management and Budget

**United States Senate**

Chairman, Subcommittee on Transportation, Treasury, the Judiciary, and Housing and Urban Development, Committee on Appropriations
Ranking Minority Member, Subcommittee on Transportation, Treasury, the Judiciary, and Housing and Urban Development, Committee on Appropriations
Chairman, Committee on Homeland Security and Governmental Affairs
Ranking Minority Member, Committee on Homeland Security and Governmental Affairs

**United States House of Representatives**

Chairman, Subcommittee on Transportation, Treasury, and Housing and Urban Development, The Judiciary, District of Columbia, Committee on Appropriations
Ranking Minority Member, Subcommittee on Transportation, Treasury, Housing and Urban Development, The Judiciary, District of Columbia, Committee on Appropriations
Chairman, Committee on Government Reform
Ranking Minority Member, Committee on Government Reform

**United States Government Accountability Office**

Comptroller General of the United States

# SECTION II –

# DEPARTMENT OF THE TREASURY
# FISCAL YEAR 2006 PERFORMANCE
# & ACCOUNTABILITY REPORT

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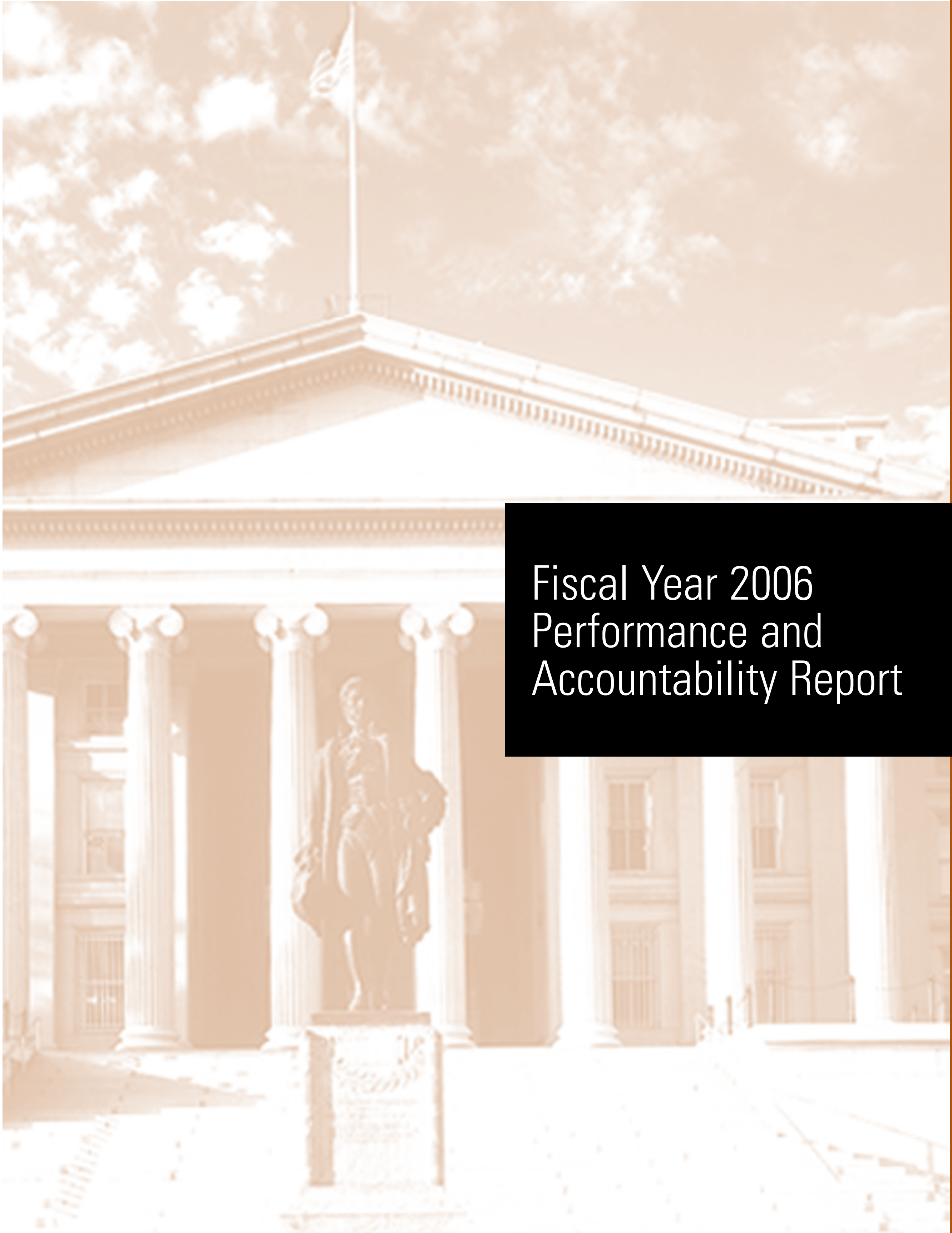
*The Department of the Treasury*



# Fiscal Year 2006 Performance and Accountability Report

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# Contents

## Major Sections

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# About this Report

## Purpose

The Department of the Treasury's Performance and Accountability Report (PAR) for FY 2006 provides information that enables Congress, the President and the public to assess the Department's performance relative to its mission and stewardship of the resources entrusted to it. The Treasury Department's report is designed around three areas of focus: Creating the Conditions for Prosperity (Economic), Financing the U.S. Government and Preserving the Integrity of Financial Systems (Financial), and Managing the Department's Operations (Management). Each of the three areas of focus has one or more strategic goals with supporting objectives and performance measures that outline the Treasury Department's approach and measure progress.

## How this Report is organized

### MESSAGE FROM THE SECRETARY

The Secretary's message includes an assessment of whether financial and performance data in the report is reliable and complete, and a statement of assurance as required by the Federal Managers' Financial Integrity Act (FMFIA) indicating whether management controls are in place and financial systems conform to government-wide standards. The Secretary's message sets the tone for conveying the Department's value to the public.

### MESSAGE FROM THE ASSISTANT SECRETARY FOR MANAGEMENT/ CHIEF FINANCIAL OFFICER

The Assistant Secretary's message describes progress and challenges pertaining to the Department's financial management, including integration of budget and performance, information on the Department's management controls program under FMFIA and financial management systems under the Federal Financial Management Improvement Act of 1996.

### MANAGEMENT'S DISCUSSION AND ANALYSIS

This Discussion and Analysis section provides a summary of the entire report. It includes a summary of the most important performance results and challenges for FY 2006; a brief analysis of financial performance; a description of systems, controls, and legal compliance; and information on the Department's progress in implementing the President's Management Agenda.

### PERFORMANCE SECTION

This section contains the annual program performance information required by the Government Performance and Results Act of 1993 (GPRA) and, combined with the Appendices, includes all of the required elements of an annual program performance report as specified in OMB Circular A-11, Preparing, Submitting and Executing the Budget.

### FINANCIAL SECTION

This section contains the Department's financial statements and related Independent Auditor's Report, and other information pertaining to the Department's financial management.

### APPENDICES

This section contains more detailed information on the Department's performance results, including information on program evaluations, revisions to indicators or targets, an organizational structure, in-depth information on the Improper Payments Information Act, Management Challenges and Responses, and information on the completeness and reliability of data.

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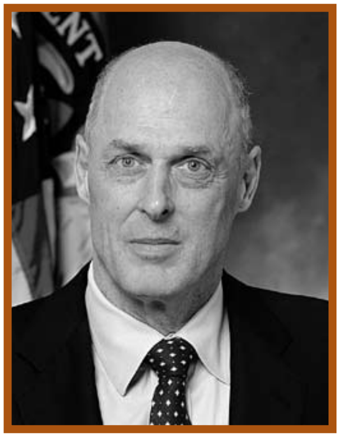
# Message from the Secretary



November 15, 2006

On behalf of the Department of the Treasury, I am submitting the Department's Performance and Accountability Report for Fiscal Year (FY) 2006. This report presents information on the Department's financial, management and programmatic results for the previous year and provides a transparent picture of the Department's successes and shortcomings.

The Treasury Department continues to focus on its core mission of promoting the conditions necessary for growth and stability in the U.S. and world economies. This mission highlights the Department's dedication to managing the government's finances, promoting economic opportunity at home and abroad through sound fiscal policy, and strengthening national security by combating the financial war on terror and safeguarding the U.S. financial system.

In executing our mission, and through sound stewardship and the increased use of new technologies, the Department improved efficiencies for collecting taxes and disbursing payments. In FY 2006 the Treasury Department continued to move toward an all-electronic environment and achieved record levels in electronically filed tax returns and revenue collection transactions. Education and outreach efforts resulted in more than 600,000 beneficiaries of Social Security and other federal payments enrolling in direct deposit, saving the government 77 cents per payment transaction, and providing improved security for these vital sources of income for our nation's citizens.

The senior managers at the Treasury Department and I are committed to efficient and effective management practices, and we continue to implement the principles of the President's Management Agenda. In FY 2006, the Treasury Department improved its score in Human Capital to the highest rating by implementing workforce management initiatives such as Senior Executive Service pay-for-performance and training and mentoring over 1,300 current and future managers Department-wide to strengthen leadership competencies. The Department expanded electronic government products and services, improved internal efficiency and effectiveness, and enhanced services to other governmental agencies and the public.

While the Treasury Department has made progress in addressing the management challenges identified by the Inspector General, we simply must do better. I recognize the need for continued improvement and the Department is implementing specific actions to build upon that progress. For example, we are strengthening policy guidance and instituting stronger oversight and accountability mechanisms for the management of information technology investments. The Department will also build upon the progress made in FY 2006 to bring its systems into compliance with federal IT security policies, standards, and guidelines. The Deputy Secretary and I are committed to regular engagement across the Department to ensure that we are focused on addressing these challenges.

In FY 2006, the Department improved the number of performance targets achieved, and significantly reduced the number of metrics lacking results from the previous year. In the coming year, the Department will continue to refine its set of performance measures to focus on important outcomes that generate value for the American people.

For the seventh consecutive year, the Department received an unqualified opinion on its financial statements, which speaks to the accuracy, completeness, and reliability of the financial data in this report. Likewise, the performance data presented herein are complete and reliable. The Department continued to make progress in reducing material management control weaknesses and has established corrective action plans to satisfy federal financial systems and control objectives.

The Treasury Department will continue to serve the American public by promoting the conditions that lead to economic growth, job creation for our citizens, and the safeguarding of our financial systems.

Sincerely,

Henry M. Paulson, Jr.
Secretary of the Treasury

# Message from the Assistant Secretary for Management and Chief Financial Officer

November 15, 2006

Secretary Paulson's message emphasizes the Treasury Department's core mission to promote the conditions necessary for growth and stability in the U.S. and world economies. The Office of Management supports this mission by securing the resources for the Department's $17 billion operating budget.

The Department of the Treasury not only is our nation's primary revenue collector but also manages the public debt on behalf of the Federal government. The results of these complex and enormous operations are reflected in the Department's financial statements: almost $9 trillion in assets and liabilities, net costs of $414 billion, budgetary resources of $503 billion, and gross revenues of $2.6 trillion. The American public entrust the Department with the stewardship of these resources.

In FY 2006, the Office of Management took Department-wide action to review and strengthen internal controls of financial reporting pursuant to new requirements established by the Office of Management and Budget (OMB). This significant effort was carried out through the dedicated efforts of the Department's Chief Financial Officers Council and many other employees across the Department. Internal controls not only apply to financial programs, but are a key factor in every Treasury Department program and activity. Consequently, we are taking steps to ensure that the performance plans of senior executives and their direct reports include specific elements and measures for correcting internal control weaknesses. Additionally, on a quarterly basis, Department bureau heads review and assess key internal control issues such as material weaknesses, reportable conditions, and key audit areas.

The Office of Management continued to provide timely and accurate financial information to the Department's managers through the 3-Day Close initiative, generating financial statements and budget execution data by the fourth day following the end of each month. Moreover, we made progress in information systems security, with 95% of the systems now fully certified and accredited, and with continued success in the Human Capital initiative under the President's Management Agenda.

The Department strengthened corporate management in FY 2006 by instituting the Executive Planning Board (EPB). The EPB is chaired by the Assistant Secretary for Management and Chief Financial Officer and includes several other senior Treasury leaders. The board reviews all bureau and policy office budget submissions and recommends funding levels to the Secretary. In FY

2006, the EPB identified critical Department-wide issues and challenges and found ways to optimize resources to benefit the Treasury Department as a whole.

As the Secretary noted, the Treasury Department again received an unqualified audit opinion on its financial statements, despite long-standing material weaknesses in financial systems. These weaknesses prevent the Department from achieving full compliance with Federal financial systems requirements and, along with weaknesses in non-financial areas, result in providing only qualified assurance that the Department is meeting Federal management control objectives. The Treasury Department eliminated one material weakness for FY 2006, with no new weaknesses identified, leaving six open material weaknesses. Several of these control weaknesses involve complex systems solutions that will require several years to mitigate.

The Office of the Assistant Secretary for Management and Chief Financial Officer is determined to address current and future challenges. For example, we are revising our Strategic Plan. The new strategic plan will use an integrated management system, based on the principles of continuous improvement, to achieve strategic goals, objectives and outcomes for a highly decentralized organization. We will continue the certification program for bureau Chief Information Officers and program managers in FY 2007, ensuring the accuracy of earned value management data provided on information technology investments. In addition, the Department will continue its program to review bureau information technology governance structures, capital planning processes, and select investments. Finally, the Department will maintain its emphasis on strong internal controls and corporate management, with the goal of closing two material weaknesses each year from FY 2007 to FY 2009.

These are only a few examples of the Treasury Department's commitment to improving service to the American public. Effective management not only is a priority, but it is an integral element of the Department's 217 year history and it is incumbent on us to continue this noble legacy.

Sincerely,

Sandra L. Pack

Sandra L. Pack

# Part I: Management's Discussion and Analysis

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**Mission:** The mission of the Department of the Treasury is to promote the conditions for prosperity and stability in the United States and encourage prosperity and stability in the rest of the world.

**History:** On September 2, 1789, the First Congress of the United States created a permanent institution for the management of government finances. The Congress assembled the Department of the Treasury and named the following officers: a Secretary of the Treasury, a Comptroller, an Auditor, a Treasurer, a Register, and an Assistant to the Secretary.

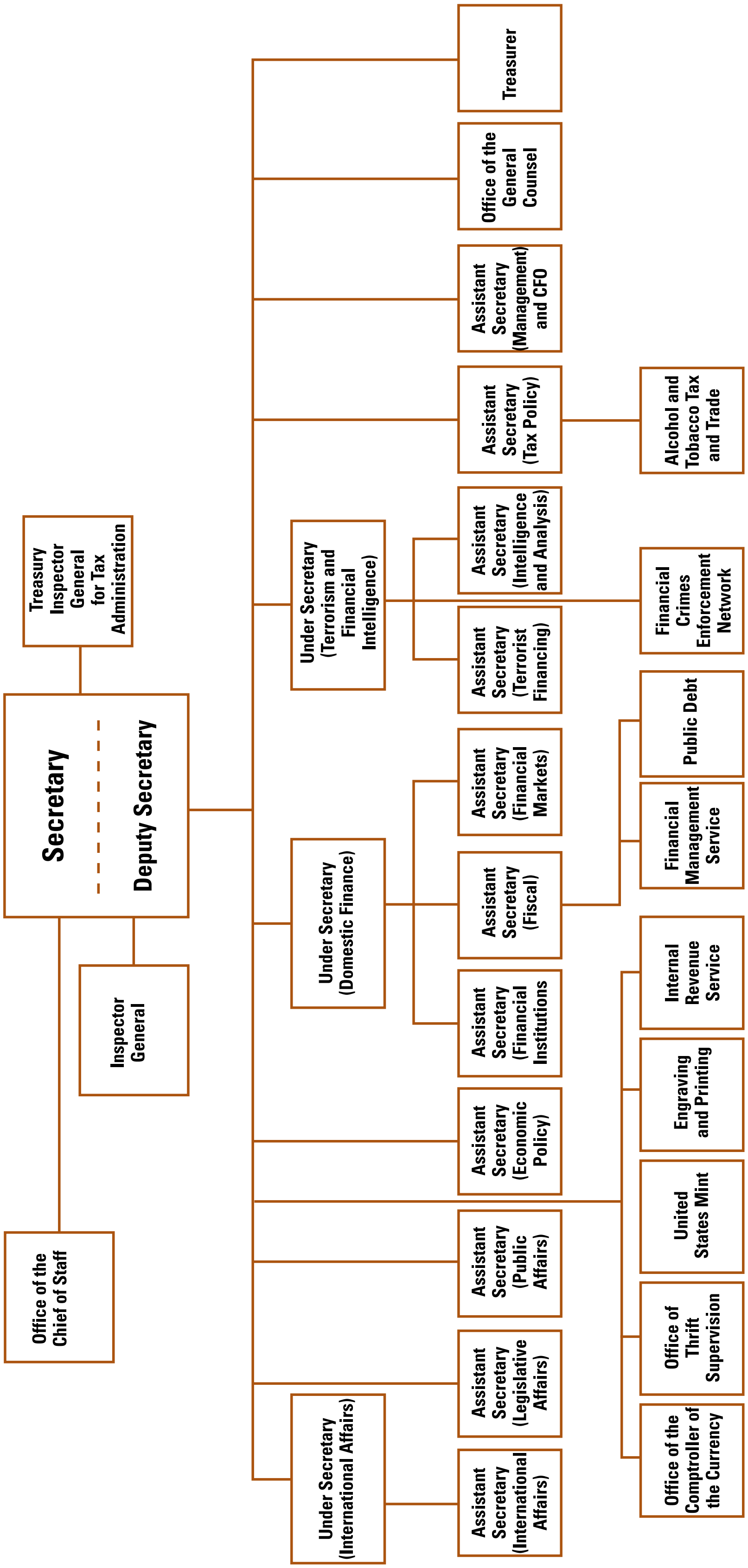
Alexander Hamilton took the oath of office as the first Secretary of the Treasury on September 11, 1789. Hamilton foresaw the development of industry and trade in the United States, and suggested that government revenues be based upon customs duties. His vision also inspired investment in the Bank of the United States, which acted as the government's fiscal agent. Throughout history, the Department of the Treasury has been a dynamic institution of the government's service to the people, expanding to accommodate a growing and ever-changing nation.

**Leadership Changes:** In FY 2006, the Department of the Treasury had some key leadership changes. During his tenure at the Department of the Treasury, Secretary John Snow worked closely with President Bush to strengthen economic growth and create jobs. In June 2006, Secretary Snow resigned as the Secretary of the Treasury and Henry Paulson was nominated by President Bush to succeed John Snow as the Treasury Secretary. On June 28, 2006, he was confirmed by the United States Senate to serve in the position. Secretary Paulson was officially sworn in at a ceremony held at the Treasury Department on the morning of July 10, 2006. Secretary Paulson previously served as the Chairman and Chief Executive Officer of Goldman Sachs & Company, one of the world's largest and most successful investment banks.

With the departure of Randal Quarles, Under Secretary for Domestic Finance, Robert K. Steel, was nominated by President Bush and confirmed by the United States Senate on September 29, 2006, for this post. The Under Secretary leads Department policy on issues of domestic finance, fiscal policy, fiscal operations, government assets, government liabilities and related economic and fiscal matters. Steel, a native of Durham, North Carolina, retired as vice chairman of Goldman Sachs & Company in New York City, in February 2004 and previously served as the advisory director for the firm.

James Wilkinson replaced Christopher A. Smith as the Chief of Staff to the Secretary of the Treasury. In his current position, Wilkinson is responsible for overseeing the day-to-day operations of the Department and coordinating policy development and review with other agencies and the White House, as well as assisting in setting the overall strategic direction of the Department. He is also responsible for advising the Secretary on a wide variety of policy and management issues on economic and market conditions.

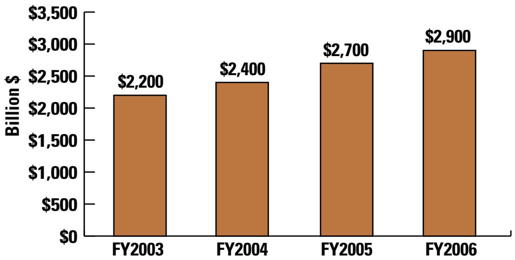
# DEPARTMENT OF THE TREASURY



# Operations Highlights

## In FY 2006 the Treasury Department…

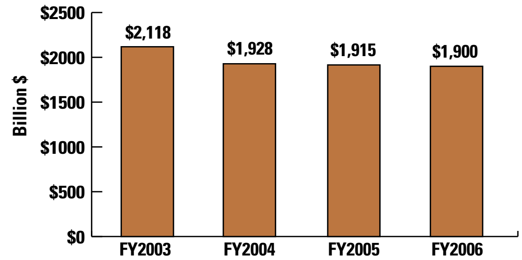
### Collected



Fiscal Year Total US Government Cash Collections

- US Government Receipts: $2.6 trillion
- Delinquent Debt Collected: $3.336 billion
- Collected through the Electronic Federal Tax Payment System: $1.9 trillion
- Enforcement revenue collected from all sources was at a record level of: $48.7 billion

### Disbursed

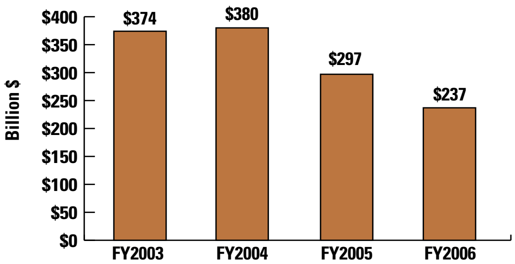


Fiscal Year Total Treasury Disbursements

- Total Treasury Disbursements: $1.9* Trillion
- Volume of electronic disbursements made through Treasury's Regional Finance Centers: 745 million
- Volume of check payments made through Treasury's Regional Finance Centers: 219 million

* Treasury Disbursements only

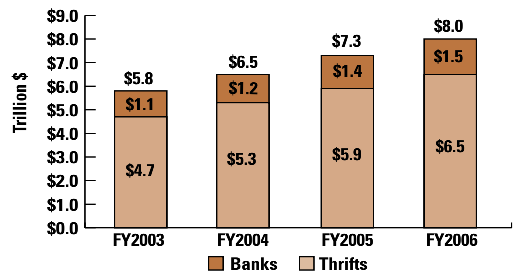
### Borrowed



Net Amount Borrowed from the Public

- Net Amount Borrowed from the Public: $237 billion
- Marketable Treasury Securities auctioned and issued: $4.4 trillion
- Non-Marketable Treasury Securities Issued to the public and government accounts: $32 trillion
- Number of Savings Bonds Issued: 32 million
- Interest Paid by Treasury (including interest credited to Trust Fund): $406 billion

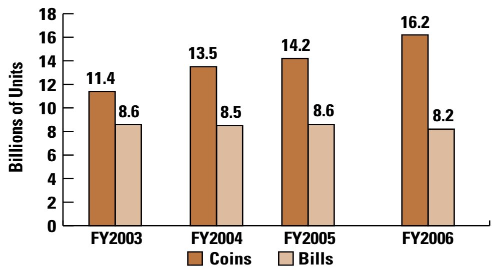
### Regulated



Total Assets Regulated

- Number of National Banks Regulated: 1852
- Number of Federal Branches Regulated: 49
- Number of Thrifts and Savings Associations Regulated: 854

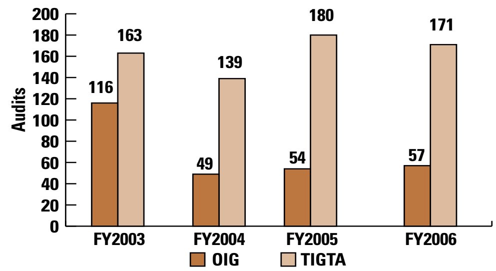
### Manufactured



Fiscal Year Total Current Production

- Produced 8.2 billion currency notes
- Produced 16.2 billion coins

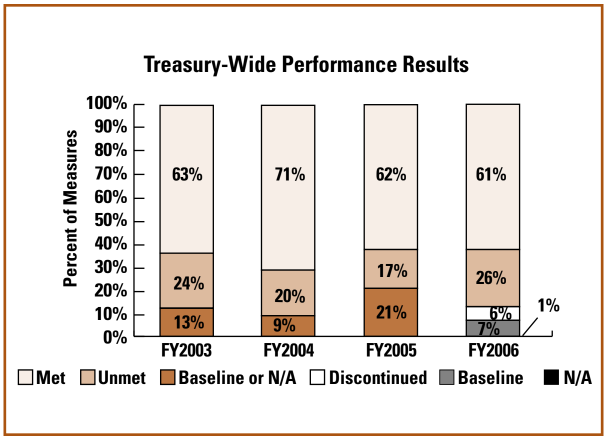
### Assured

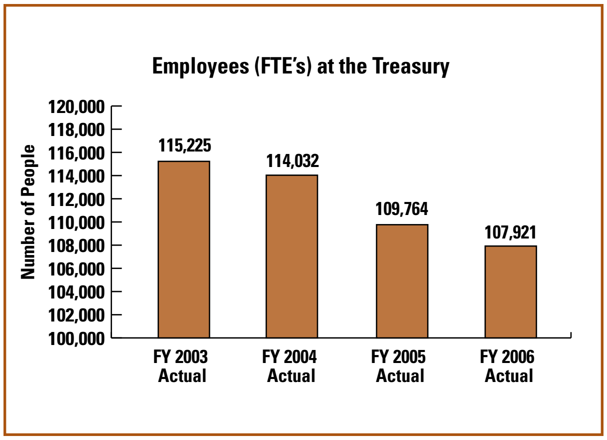


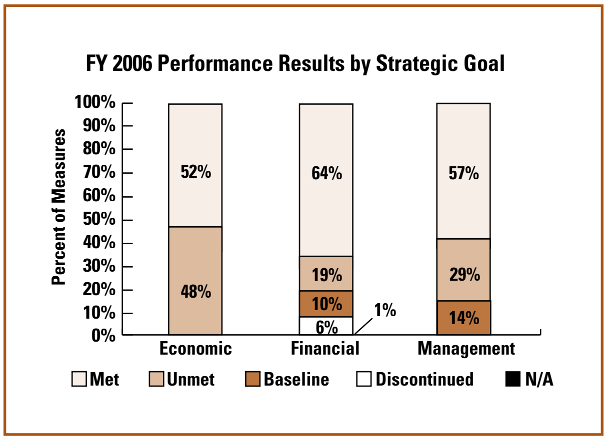
Number of IG Audits and Evaluations

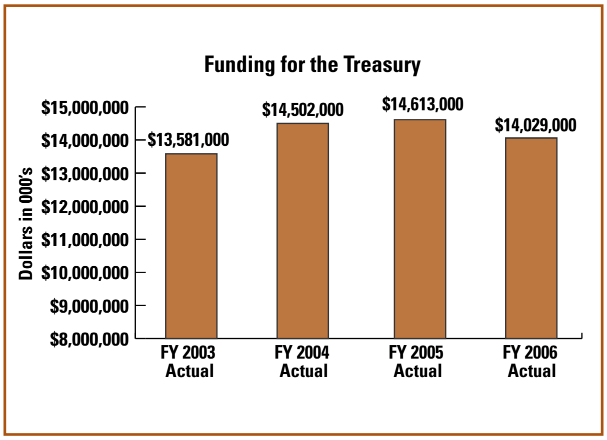
- Performed 228 audits and evaluations through the efforts of the Inspectors' General

# Performance Highlights



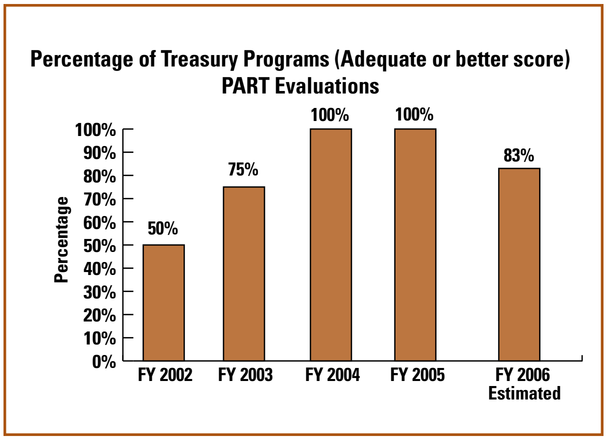



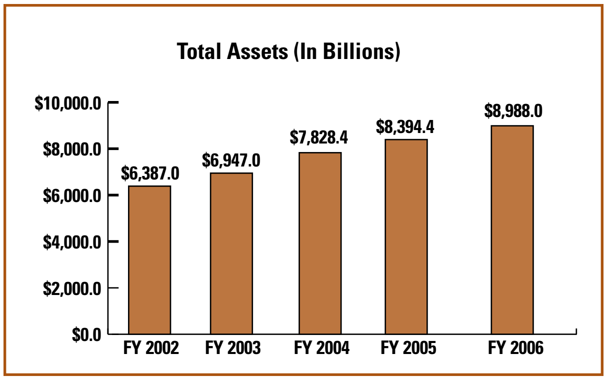

**President's Management Agenda**

| Initiative | Status | | FY 2006 Progress | | | |
|---|---|---|---|---|---|---|
| | FY 2005 | FY 2006 | Q1 | Q2 | Q3 | Q4 |
| Human Capital | Y | G | G | G | G | G |
| Competitive Sourcing | G | G | G | G | G | Y |
| Financial Performance | R | R | G | G | G | G |
| E-Government | R | Y | Y | G | Y | Y |
| Budget Performance Integration | Y | Y | G | G | Y | Y |
| Improper Payments | R | R | Y | Y | Y | Y |

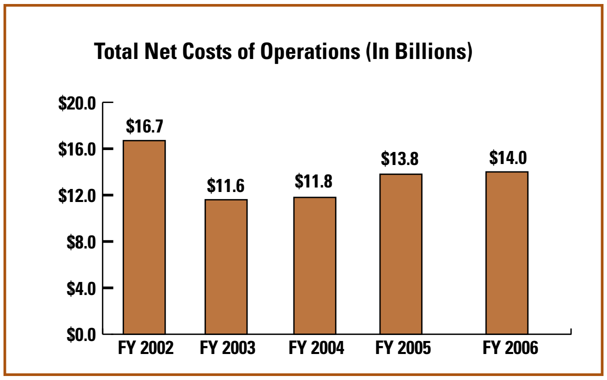
Green for Success Yellow for Mixed Results Red for Unsatisfactory



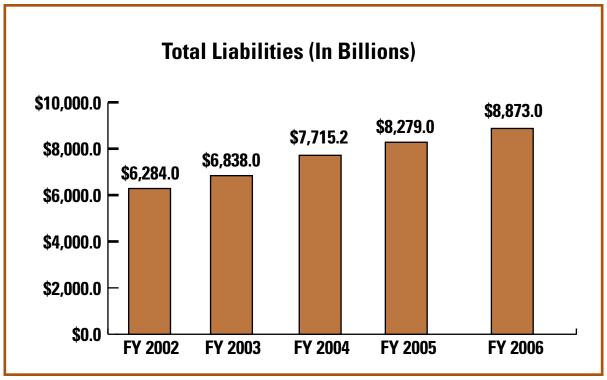
# Financial Highlights



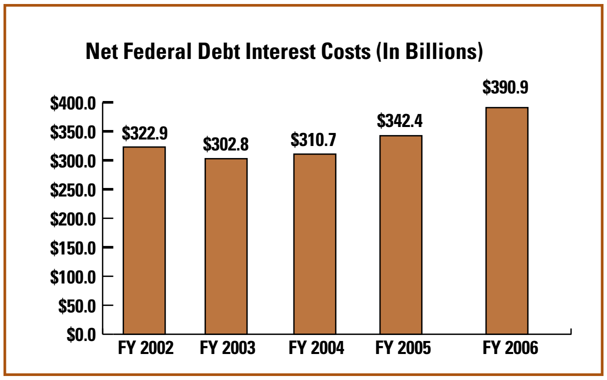

The increase in total assets from $8.4 trillion in FY 2005 to $9.0 trillion in FY 2006 is largely due to the increase in future funds required from the General Fund of the U.S. Government to pay for the federal debt.



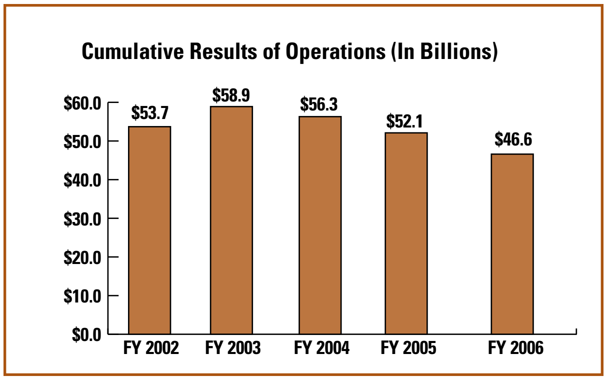

The increase of total net cost of operations from $13.8 billion in FY 2005 to $14.0 billion in FY 2006 is largely in the economic and financial programs and is primarily due to exchange rate fluctuations, reduced interest income, write offs of discontinued projects, and increased payments to financial agents.



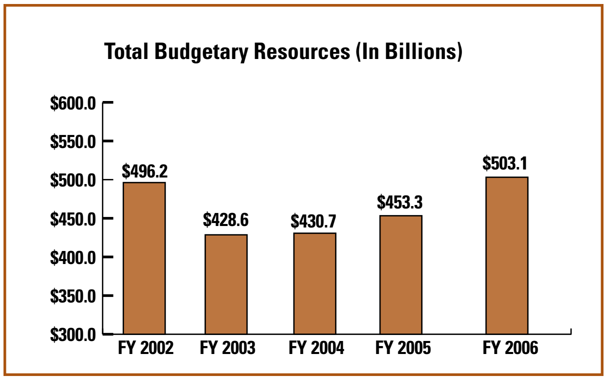

The borrowing from other federal agencies and debt issued to the public increased from $8.0 trillion in FY 2005 to $8.5 trillion in FY 2006.



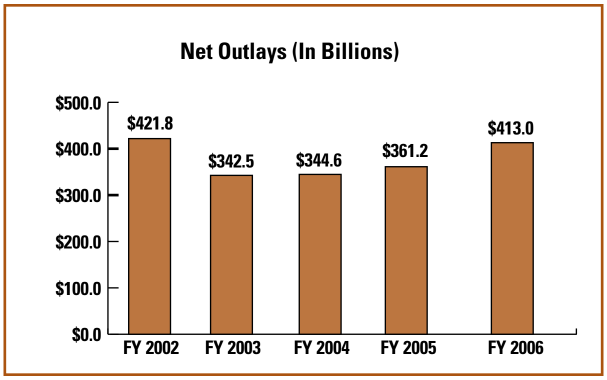

The net interest paid on the federal debt rose from $342.4 billion in FY 2005 to $390.9 billion in FY 2006 is due to the increase in the debt and higher interest rates.



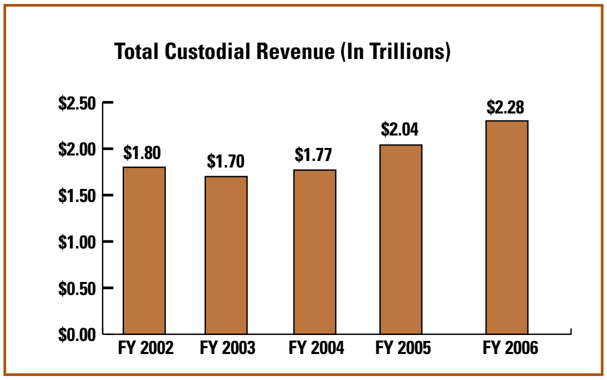

The net decrease of $5.5 billion in the cumulative results of operations from $52.1 billion in FY 2005 to $46.6 billion in FY 2006 was largely due to the decrease in Treasury's reserve position in the International Monetary Fund due to loan repayments by debtor countries.




The majority of the increase in total budgetary resources from $453.3 billion in FY 2005 to $503.1 billion in FY 2006 was due to the increase in funding to pay for the interest on the federal debt. The sharp increase in the budgetary resources for FY 2002 was the result of a restatement to reflect a change in accounting principles for the interest on public debt securities as directed by the Office of Management and Budget.




The majority of the increase in net outlays from $361.2 billion in FY 2005 to $413.0 billion in FY 2006 also was due to the increase in interest payments.




Total custodial revenue collected on behalf of the U.S. Government increased from $2.04 trillion in FY 2005 to $2.28 trillion in FY 2006. The majority of the increase is attributed to the rise in individual and corporate income taxes due to increased economic activity.

Note: Prior to March 1, 2003, Treasury bureaus also included Bureau of Alcohol, Tobacco and Firearms; Federal Law Enforcement Training Center; U.S. Customs Service; and U.S. Secret Service. These bureaus were divested to either the Department of Homeland Security or Department of Justice. FY 2003 and prior years include data for these bureaus.

# Management's Discussion and Analysis

## Executive Summary

The Department of the Treasury shoulders a great responsibility for the American people. While the Department performs a critical role in U.S. and global economies, it continually evolves to meet the ever changing needs of the nation. The Treasury Department provides cash management for the federal government, currency and coin production, administration of the tax code, oversight of the financial sector, and plays an integral role in stopping the financing of terrorism, and identifying and dismantling the support networks of terrorist organizations.

In fiscal year 2006, the Department's debt financing operations auctioned and issued more than $4 trillion in marketable securities, and $32 trillion in non-marketable securities, to the public and government. The Treasury Department also oversaw a daily cash flow of almost $60 billion, distributed 85 percent of federal payments worth $1.5 trillion, produced 8.2 billion currency notes, and 16.2 billion coins. The cost per 1,000 notes delivered was reduced by $1.34, while the cost of producing coins rose from $7.42, in FY 2005, to $7.55, in FY 2006, missing the very aggressive target of $6.62. The Department continued its efforts as the lead in the U.S. delegation to the Financial Action Task Force (FATF), the international standard setting body charged with safeguarding the global financial system against money-laundering and terrorist financing, yielding results, such as impeding access to funds and the financial system by terrorist groups such as al Qaida and Hamas and limiting North Korea's ability to abuse the international financial system to support its proliferation and illicit activities.

## Collecting Taxes

***"The tax gap represents, in dollar terms, the annual amount of noncompliance with our tax laws. It is the need to reduce that gap that drives much of what we do. This is true not only from a revenue standpoint, but also from a taxpayer fairness perspective. Our tax system is largely based on voluntary compliance and that compliance is enhanced if taxpayers believe that everyone is paying their fair share."***

Mark Everson
IRS Commissioner
April 6, 2006

Critical to managing the Federal Government's finances effectively is collecting federal tax revenue. The Department of the Treasury collected $2.5 trillion in federal tax revenue, with a record $48.7 billion collected through enforcement activities. Total collections of tax revenue increased 11 percent and enforcement revenue increased 3 percent over last year.

***Compliance:*** While most taxpayers voluntarily comply with their tax obligations, some do not; noncompliance results in a tax gap. In FY 2006, the IRS updated its tax gap estimates. New estimates show that underreporting of income taxes, employment taxes, and other taxes account for about 80 percent of the tax gap. The Treasury Department is focusing on corrosive activities of high-risk taxpayers including corporations, high-income taxpayers, and promoters of abusive tax avoidance transactions (ATAT) and other major violators of the tax code. Targeting high-risk taxpayers improves IRS efficiency, reduces the burden on compliant taxpayers, and concentrates enforcement presence where it is needed most.

**Free Tax Assistance For You by Volunteers.** For the past seven years, the IRS in Atlanta has partnered with Kroger grocery stores and the Georgia Department of Revenue to sponsor "Midnight Madness" on the last day of the tax filing season. IRS volunteers accept tax returns and extensions, provide tax forms, and answer tax questions at various Kroger store locations.

***Taxpayer Outreach:*** Expanding education and outreach helps the public understand their filing, tax reporting and payment obligations, and improves voluntary compliance. The Department continues to expand its outreach by relying on partner organizations such as state taxing authorities and a cadre of volunteer groups to serve taxpayer needs. Through its 12,300 Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) sites, the Department provided free tax assistance to the elderly, disabled, and limited English proficient individuals and families. The 69,000 volunteers located at the sites prepared approximately 2.3 million returns, a 7.3 percent increase over FY 2005.

***Taxpayer Burden Reduction:*** The taxpayer burden measures time and out-of-pocket expense taxpayers incur in meeting their tax responsibilities. The complexities of the tax laws and the taxpayer's familiarity and skills with tax return preparation (paper/electronic) have a significant impact on burden. Many taxpayers find it more convenient and beneficial to prepare tax returns electronically or use a tax preparer. The estimated FY 2006 burden was 6.7 billion hours, compared to 6.4 billion hours, in FY 2005, an increase of 251 million hours, resulting from changes to existing forms dictated by ten different laws enacted in 2005. The IRS continues to partner with external stakeholders including taxpayers, practitioners, citizens groups, software developers, and state/federal agencies to receive suggestions on reducing taxpayer burden while designing forms more suitable for computer usage.

***Tax Reform:*** The President's Advisory Panel on Federal Tax Reform issued its report in November 2005, entitled "Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System." The Panel recommended two options for fundamental reform of the Federal tax system. The Department of the Treasury is evaluating the Panel's report and is considering options for reform. In September 2006, the Department announced a comprehensive strategy for reducing the tax gap which includes the simplification and reform of the tax law to reduce unintentional errors caused by a lack of understanding, and to reduce opportunities for intentional evasion of tax liabilities. The Administration's FY 2007 budget included six proposals to simplify the tax treatment of savings and families by consolidating existing programs and clarifying eligibility requirements. The Office of Tax Policy is developing other simplification proposals for future consideration. These tax reform initiatives continue to be supplemented by IRS efforts to reduce taxpayer burden by simplifying forms and procedures.

## Managing U.S. Government Finances

In addition to collecting taxes, the Department of the Treasury oversees the daily cash flow of almost $60 billion and distributes 85 percent of all federal payments. Managing the government's finances also includes making payments, issuing debts, and preparing public financial statements.

***Federal Payments:*** The Treasury Department functions as the nation's disburser, manager, and accountant of public monies by distributing payments and financing public services. In FY 2006, the Treasury Department made 100 percent of its payments accurately and on-time, including income tax refunds, Social Security benefits, veterans' benefits, and other federal payments. The Department continued to transition from paper checks to electronic transactions issuing 77 percent of 964 million non-Defense payments electronically. In FY 2006, the Treasury Department continued to expand and market the use of electronic media to deliver federal payments, improve service to payment recipients, and reduce government program costs. These efforts helped to decrease the number of paper checks issued and minimize costs associated with postage on the re-issuance of lost, stolen or misplaced checks. Financial Management Service (FMS) issued over 8.5 million fewer checks than last year and through its Go-Direct campaign, converted over 600,000 individuals from checks to direct deposit in the first full year of the campaign. If the more than 154 million benefit checks issued in FY 2006 (142 million were Social Security and Supplemental Security Income payments) were converted to direct deposit, the savings to the American taxpayer would be $119 million.

> In FY 2006, FMS collected receipts totaling $2.9 trillion of which $1.8 trillion was collected through the Electronic Federal Tax Payment System. FMS has been working actively to reduce the unit cost of processing Federal revenue transactions. The overall cost efficiency of the collections business line has improved dramatically as a result of these efforts.

***Debt Management:*** The Treasury Department determines and executes the federal borrowing strategy to meet the monetary needs of the Government at the lowest possible cost. Each year, the Treasury Department borrows and accounts for trillions of dollars needed for the government to function. The Department conducts debt financing operations by issuing and servicing Treasury securities. In FY 2006, more than $4 trillion in marketable securities and $32 trillion in non-marketable securities were issued to the public and government accounts. The Department of the Treasury met its performance goal of announcing Treasury auction results within its target timeframe 100 percent of the time. The Department minimized the cost of borrowing; with a shorter release time, exposure to adverse market movements and the implicit market premium are reduced. The Department improved efficiency in the Government Agency Investment Services (GAIS) program. GAIS supports federal, state, and local government agency investments in non-marketable Treasury securities and manages over $3.7 trillion in customer assets. In FY 2006, over 97 percent of GAIS transactions were conducted online, as compared to 72.7 percent in FY 2005.

> **Treasury Hunt Expanded**
> Treasury Hunt is a tool available on Public Debt's website (*www.TreasuryDirect.gov*) that helps people determine if they have matured savings bonds that have stopped earning interest or if Public Debt is holding savings bonds or interest payments that were returned as undeliverable. Treasury Hunt encourages people to redeem their matured savings bonds and put their money back to work. Over the past year, Public Debt greatly expanded the number of matured savings bond records available for searching by taxpayer identification number to more than 12 million. Each month, bonds that have newly matured are added to the Treasury Hunt database, making it worthwhile for bond owners to visit the site often.

## Focusing Domestically

To achieve conditions promoting prosperity and stability in the U.S. and world economies we must stimulate economic growth. This is accomplished through the development of policies addressing overall economic development, implementing pro-growth tax programs, regulating banking and financial institutions, advocating for free and fair trade, promoting assistance programs in distressed communities, expanding opportunities for American businesses and workers in the global economy, creating good jobs with mobility and wage growth, averting or mitigating financial crises and, in general, accelerating and sustaining the economic performance of the nation. Modernizing entitlement programs before they destabilize the economy is a critically important aspect of this, as is keeping the economy performing at peak potential by encouraging and supporting American competitiveness through innovation.

Treasury supports trade liberalization and budget discipline through its role in negotiating and implementing international agreements pertaining to official export subsidies. The Treasury Department secured agreements in the Organization for Economic Cooperation and Development that reduced subsidies in export credits and tied aid flows valued at over $70 billion. These agreements open markets, leveled the playing field for U.S. exporters, and saved the U.S. taxpayer about $800 million. Cumulative budget savings from these agreements are estimated at over $11 billion since 1991.

***Economic Policies:*** The Department of the Treasury develops and implements economic policies to stimulate economic growth and job creation. While drawing a direct relationship between the Department's actions and economic indicators is difficult, the Department's policy makers have helped create an environment conducive to strong economic growth and a healthy labor market. In FY 2006, growth in the real Gross Domestic Product (GDP), the broadest measure of the economy's performance, was relatively unchanged from FY 2005, at 3.3 percent. The solid pace of expansion contributed to job creation and helped lower the unemployment rate from an average of 5.2 percent in FY 2005, to 4.8 percent in FY 2006.

***Capital Market Competitiveness:*** To ensure the American economy remains a model of strength, flexibility, and resiliency, it must grow and remain competitive. Strong capital markets play an important part in facilitating economic growth. The Department's efforts are aimed at preserving the integrity of the nation's markets while keeping pace with the dynamic U.S. economy and financial marketplace, which is increasingly competitive and integrated on a worldwide level. Capital markets competitiveness is influenced by many factors, some of which the Department will focus on, include regulatory, legal and accounting systems. In addition, the Treasury Department will address longer term issues that impact the economy including energy, entitlement reform, and trade.

***Free Trade and Investment:*** The United States seeks strong commitments from its trading partners to ensure their goods and services markets are available to the U.S. on an open basis under transparent and fair rules. The Department helps negotiate international agreements to remove trade and investment barriers, which enhance global market efficiency and increase job and business opportunities for Americans. The Department is responsible for the financial services negotiations on banking and securities issues. Once implemented these agreements serve as an element of our trading partners economic infrastructure that enhance international economic and financial stability. Negotiations are conducted through either the World Trade Organization or U.S.-initiated bilateral and regional Free Trade Agreements (FTA) and Bilateral Investment Treaties (BIT).

In FY 2006, the Department of the Treasury implemented FTAs and completed negotiations with nine countries in the Middle East and Latin America. The United States and Vietnam concluded their bilateral agreement on goods and services. FTA negotiations were launched with Malaysia and Korea. Each of the FTAs opened markets to U.S. goods and services, including financial services, and promoted open investment regimes.

BITs and the investment provisions in FTAs contain stipulations that help ensure the most efficient and effective use of capital and provide the legal framework to enhance investor confidence, economic growth and greater opportunities for American workers and employers. In its ongoing efforts to expand BITs with other nations, the Treasury Department continued to negotiate a formalized agreement with Pakistan based on the model developed in FY 2004. In addition, this year, Congress ratified a BIT with Uruguay.

The Free Trade Agreements (FTA) that were concluded since 2001, and combined with three earlier accords, now roughly cover $925 billion in two way trade – nearly 36 percent of the total U.S. trade with the world and 45 percent of our exports. Where we have a FTA, our exports are growing a healthy 20 percent per year on average, more than twice the rate of growth for our exports where we do not have a FTA.

***Supervising National Banks and Savings Associations:*** The Department of the Treasury is the primary regulator and supervisor of national banks, savings associations and savings and loan holding companies; and works to streamline licensing and supervisory procedures and keep regulations current. Effective supervision promotes competitive financial services, consistent with safety and soundness.

Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), federal bank and thrift regulations are reviewed at least once every ten years in an effort to eliminate any regulatory requirements that are outdated, unnecessary or unduly burdensome. As part of the EGRPRA, banking agencies continued their joint initiative to review and recommend the elimination of unnecessary regulations to Congress. Results of the initiative identified over 125 regulations and over 1,000 letters were received with suggested changes.

Congress passed and President Bush signed into law the "Financial Services Regulatory Relief Act of 2006", which provides regulatory burden relief for the financial services, and the banking and thrift industries. The law allows regulators to adjust exam cycles of healthy institutions for greater efficiency, modernizes record keeping requirements for regulators, and requires the federal banking agencies to propose within six months a simple, uniform privacy notice to comply with the Gramm-Leach-Bliley Act of 1999.

American homebuyers now have more financing options than ever before, with a menu of mortgage related products that offer a variety of maturities, interest rates and payment structures. In recent years, a combination of forces – especially the rapid increase in house prices – has led to the increased popularity of so-called non-traditional mortgage products. Understanding the tradeoffs of these products is essential if a borrower is to make an informed decision about one of their most important financial assets. To address these concerns, the OCC, OTS, the Federal Reserve Board, FDIC, and NCUA, published guidance on these nontraditional products. The guidance stresses the importance of carefully managing the risk associated with these loans, and clarifies how banks, thrifts, and credit unions can offer them in a safe and sound manner, with appropriate disclosure given to borrower. The Treasury Department continues to promote homeownership and healthy, stable communities by ensuring that financial institutions have the means to provide consistent, reliable housing financing to credit worthy borrowers.

***Creating Opportunity in Native Communities:*** The Treasury Department, through the Community Development Financial Institutions (CDFI) Fund, has a number of initiatives designed to overcome barriers preventing access to credit, capital and financial services in Native American communities. The Native Initiatives seek to increase the number and capacity of CDFIs serving Native communities. In FY 2006, the CDFI Fund issued $4.3 million in Native Initiative awards to 23 CDFIs, and Native CDFI awardees' reported asset growth of 182 percent, far exceeding the 33 percent projection. This asset growth represents required timely reporting of performance data to the Fund by 7 Native CDFI awardees. Most organizations experienced growth and one start-up CDFI had a ten-fold increase in its assets.

As an example, the Four Bands Community Fund, of Eagle Butte, South Dakota, is a certified Community Development Financial Institution serving the Cheyenne River Indian Reservation and a CDFI Fund awardee. In 2006, Four Bands received $618,000 from the CDFI Fund to continue to assist entrepreneurs on the Reservation with training, business incubation, and access to capital to encourage economic development for low-income residents. Four Bands recently introduced a new Credit Builder Loan to help new clients improve their credit worthiness and position themselves for the micro and small business loan products that Four Bands offers. With the Credit Builder Loan, clients are required to create and implement a Credit Builder Action Plan to repair their credit histories and develop a positive credit relationship with the organization. "Four Bands is not like a bank. They teach you the steps to succeed and then provide loan support," says Eva Gilbert, proud owner of Eva's Hair and Nails on the Reservation.

***Financial Assistance Awardees Exceed Leverage Goal:*** The CDFI Fund's Financial Assistance component gives financial awards to CDFIs that demonstrate the greatest ability to leverage non-federal dollars which support comprehensive business plans that create community development impact in underserved markets. In FY 2006, the Fund made $24 million in Financial Assistance awards to CDFIs that primarily serve rural and urban low-income communities. In addition, awardees leveraged the Fund's award dollars with $1.4 billion in private and non-CDFI Fund dollars, therefore significantly exceeding the $1.1 billion leveraging goal and marking this the second consecutive year the goal was surpassed. The leverage ratio of $27 of private and non-CDFI Fund dollars for every $1 of Financial Assistance awards held constant from FY 2005 to FY 2006.

***Bank Enterprise Award (BEA) Program:*** The BEA Program provides insured depository institutions with financial incentives to expand investments in CDFIs and increase direct lending, investment, and service activities in economically distressed communities. The BEA Program provided modest monetary awards for large increases in community development, thereby leveraging the CDFI Fund's dollars and putting more capital to work. BEA applicants showed an increase of over $318 million in community development activities from FY 2005 to FY 2006, surpassing the CDFI Fund's goal of $81 million by nearly 293 percent.

**ACCION**-New Mexico is a certified CDFI and CDFI Fund awardee whose mission is to break down barriers to credit for emerging entrepreneurs whose small capital needs, credit history, or lack of collateral may prevent them from qualifying for bank financing. ACCION-New Mexico has helped create or sustain more than 3,400 jobs by providing thousands of loans to small businesses and micro-enterprises in the state. Its average loan size is just $5,300. One borrower - the owner of Carniceria La Especial, a grocery and meat market in Albuquerque – put it this way: "ACCION-New Mexico believed in me when no one else would."

## Focusing Internationally

The Department of the Treasury plays an important role in the global economy, monitoring over 160 economies to help ensure stability and transparency in the global marketplace. The Department works with foreign governments, financial institutions and international organizations to promote free and fair trade practices, target development assistance, identify global financial trends, and expand prosperity in the United States and around the world.

***Multilateral Debt Relief Initiative (MDRI) for the Heavily Indebted Poor Countries:*** In July 2006, President Bush and other G8 leaders endorsed MDRI debt relief for Heavily Indebted Poor Countries. The Department of the Treasury developed and successfully negotiated the financial structure of an agreement which will result in 100 percent cancellation of debt obligations owed the International Development Association, African Development Fund, and International Monetary Fund by eligible countries. Under the agreement, 22 countries are currently eligible to receive $34 billion in relief, with an additional 16 countries eligible once they reach "Completion Point." Total relief provided is approximately $52 billion.

***Egypt:*** The Department of the Treasury, in cooperation with the State Department and U.S. Agency for International Development, negotiated an agreement with the Government of Egypt to tie the disbursement of U.S. foreign assistance to Egypt's implementation of a series of reforms designed to modernize its financial sector. As a result, Egypt began the process of privatizing state-owned banks, resolving bad loans, and increasing the efficiency of the foreign exchange market. These reforms boosted investor confidence in Egypt and contributed to strengthening economic growth - up from 4.1 percent in 2004 to 5.7 percent in the first half of 2006. If maintained, this growth will boost job creation and help protect Egypt against economic shocks as it opens its markets.

***Brazil:*** The largest economy in Latin America continued a strong recovery from the financial crisis of 2002, during which the United States supported International Monetary Fund assistance to stabilize Brazil's economy. From August 2005 through July 2006, Brazil's economy created 413,000 new jobs. During the Treasury Department's consultations with Brazil, in July 2006, discussions focused on the global outlook, the benefits of increased trade openness, strategies to increase investment in productive infrastructure, and policies promoting research and innovation.

**Secretary Paulson in China**

Secretary Paulson visited China in September 2006. The Strategic Economic Dialogue that was established through this meeting will to ensure the two countries can address future critical economic challenges, including: building innovative societies, seizing the opportunities for global economic integration to assure sustained growth, and the economics of energy and conservation. The United States will also support China in its goal of building a consumer-driven economy rooted in open markets.

## Fighting Terrorism and Financial Crime

The Department of the Treasury is a key player in the Government's efforts to track and cut off the flow of funds to terrorists and other national security threats. In strong partnership with the Departments of Justice, State, and Homeland Security, as well as the Intelligence Community, the Department utilizes a range of financial intelligence and enforcement authorities to prevent the flow of funds to terrorist organizations.

The Office of Terrorism and Financial Intelligence (TFI), created in 2004, align the Department's national security resources and authorities, and deploy them in a coordinated and focused manner against security threats. TFI unifies leadership for the functions of:

- The Office of Intelligence and Analysis (OIA)
- The Office of Terrorist Financing and Financial Crimes (TFFC)
- The Financial Crimes Enforcement Network (FinCEN)
- The Office of Foreign Assets Control (OFAC)
- The Treasury Executive Office for Asset Forfeiture (TEOAF).

The Department's range of activities against national security threats include: (1) intelligence analysis on the financial and other support networks for terrorist groups, weapons of mass destruction (WMD) proliferators, and other serious national security threats, (2) promoting international cooperation to attack the financial foundation of national security threats, (3) improving the transparency and safeguards of financial systems, and (4) targeting and sanctioning supporters of terrorism, WMD proliferators, narcotics traffickers, and other threats.

***Safeguarding the nation's financial system through Bank Secrecy Act:*** The Department of the Treasury effectively administers and enforces the Bank Secrecy Act (BSA), an important weapon in combating anti-money laundering. The BSA requires financial institutions to make reports of suspicious activities available to law enforcement, keep records, and establish appropriate internal controls to guard against financial crime. As administrator of the BSA, the Department oversees and coordinates the sharing of financial intelligence and analysis with its stakeholders, and works closely with regulatory partners to take action against violating institutions, such as imposing stiff monetary penalties.

> FinCEN has completed three major geographic threat assessments of financial activity in states along the U.S. southwest border, to support federal and state drug and cash interdiction efforts. These assessments, which are based on analysis of more than 400,000 BSA reports filed in border counties, identified potential money laundering hotspots and significant changes in financial activity to help federal and state authorities allocate resources on the southwest border.

***Enforcing Sanctions:*** The Office of Foreign Assets Control (OFAC) administers and enforces economic and trade sanctions against targeted foreign countries, terrorists, international narcotics traffickers and those engaged in activities related to the proliferation of weapons of mass destruction. In FY 2006, OFAC, in response to the Administration's policies, pursued designations of entities engaged in the proliferation of weapons of mass destruction, continued their efforts to expose terrorist networks, and built on their success in dismantling networks associated with drug cartels. OFAC worked with the Office of Intelligence and Analysis to pursue designations targeting terrorist groups and their supporters. In addition, OFAC worked closely with the Departments of State and Justice to identify targets for four newly established sanctions programs, including Sudan's Darfur region, Côte d'Ivoire, Belarus, and the Democratic Republic of Congo.

## Producing Coins and Currency

The Treasury Department ensures the U.S. financial system's reliability and security through the production of the nation's coins and currency. The Department manufactures circulating coinage and popular numismatic products, and the nation's paper currency. The Department of the Treasury also engages in research and development to design next generation currency that guards against counterfeiting.

The Department had revenue and other financing sources of $2.3 billion for FY 2006, for both circulating and numismatic coin products, a 31 percent increase over FY 2005. As a result of operations, $750 million was returned to the Treasury General Fund, compared to $775 million in FY 2005. This reduction in transfer was due primarily to significant increases in the price of metal used for coin fabrication.

In FY 2006, the cost per 1,000 coin equivalents increased about two percent to $7.55, from $7.42 in FY 2005, missing the aggressive target of $6.62. Cycle time increased slightly from 69 days, in 2005, to 72 days, in 2006. This increase had no effect on the overall program or activity performance. Rising metal prices had a significant impact on production cost, causing the penny and the nickel to cost more than their face value. The Treasury Department is working with Congress to evaluate alternative materials to reduce production cost.

The Mint's numismatic and bullion sales increased from $588.2 million in FY 2005, to $1.03 billion in FY 2006. Particularly noteworthy was the introduction of the first ever U.S. Government issued 24-karat gold coin.

In FY 2006, the Department streamlined its operations to reduce the cost of producing currency notes. Manufacturing costs per 1,000 notes produced decreased from $28.83, in FY 2005, to $27.49, in FY 2006; and security costs were favorable at $6.00 per thousand notes produced, against a performance target of $6.25 per thousand notes delivered. In FY 2006, the currency program was completed below standard costs.

The currency production program specifically addresses the nation's need for counterfeit-deterrent currency by applying the latest technologies in security printing and processing. This fiscal year, the Treasury Department introduced the redesigned $10 note which followed the successful introductions of the redesigned $20 and $50 notes in 2003 and 2004, respectively; redesigns of the $5 and $100 notes are scheduled for circulation in 2008 and 2009. The new notes are part of the current multi-year initiative to implement the most ambitious currency redesign in U.S. history. Due to the Department's consistent automated inspection equipment, more than 99 percent of all notes delivered to the Federal Reserve met or exceeded their exacting quality standards.

## Improving Management Efficiency and Effectiveness

The Treasury Department ensures that taxpayers receive the most efficient and effective use of their tax dollars by building a strong institution that is citizen-centered, results-oriented, and actively implements the principles of the President's Management Agenda (PMA).

***PMA:*** The PMA is designed to improve management practices across the federal government and transform government into a results-oriented, efficient and citizens-centered enterprise. Implementing the PMA involves: (1) lowering the cost of doing business through competition; (2) strengthening the Department's workforce; (3) improving financial performance; (4) increasing the use of information technology and e-government capabilities; and (5) integrating budget decisions with performance data.

The Office of Management and Budget assesses each agency's status and progress for the PMA initiatives on a quarterly basis. Initiative "status" describes overall success, and "progress" describes ongoing efforts to meet PMA goals.

In FY 2006, the Department continued to be successful in two initiatives, Competitive Sourcing and Human Capital; in the E-Government initiative, the status score went up; while Budget Performance, Improper Payments, and Financial Performance initiatives remained unchanged. Some initiatives showed progress by increasing the score one level for the quarterly rating.

**President's Management Agenda**

| Initiative | Status | | FY 2006 Progress | | | |
|---|---|---|---|---|---|---|
| | FY 2005 | FY 2006 | Q1 | Q2 | Q3 | Q4 |
| Human Capital | Y | G | G | G | G | G |
| Competitive Sourcing | G | G | G | G | G | Y |
| Financial Performance | R | R | G | G | G | G |
| E-Government | R | Y | Y | G | Y | Y |
| Budget Performance Integration | Y | Y | G | G | Y | Y |
| Improper Payments | R | R | Y | Y | Y | Y |

Green for Success  Yellow for Mixed Results  Red for Unsatisfactory

***Program Assessment Rating Tool (PART):*** Like the PMA, the PART process gives the Department of the Treasury a framework for assessing performance in its major programs. Through the use of in-depth performance questions, PART allows the Department leadership to evaluate how well a program is meeting its intended objectives, how effectively and efficiently it is managed, the extent to which the program supports the Department's overarching strategic goals and how well the program achieves results.

The Treasury Department continues to work towards achieving strong PART scores by: (1) improving goals and measures; (2) providing a training session that includes an exchange of lessons learned across bureaus; and (3) solid evidentiary procedures. We estimate that 83 percent of the Department's PART evaluations will score "adequate" or better in FY 2006. Additional details of OMB recommendations and actions planned or underway for each program can be found in the appendix of this report. Scores are still pending for the programs PARTed for the FY 2007 (2008 budget year) and will be reported in the FY 2007 Performance and Accountability Report.

***Revision of the Strategic Plan:*** In FY 2006, the Treasury Department embarked on a total revision of its Strategic Plan. This new plan more clearly defines the strategic priorities and better articulates outcome-oriented goals and objectives. The Department tested its mission, goals and strategies against a set of future possibilities to ensure they are robust. Outcomes that the Department wants to achieve were identified, recognizing that outcomes connect us across different programs and organizations. A new vision statement and a set of core values were added, both of which serve to integrate and draw the Department toward a compelling picture of its future. In addition, this strategic plan establishes the structure by which the Treasury Department will link budget and cost to outcomes, and quantify the value the Department produces for the American people.

### *Summary of Management Challenges and High Risk Area*

The Department's Inspectors General and the Government Accountability Office (GAO) have identified the following areas as being the Department's most significant challenges and having high-risk:

- Corporate Management
- Management of Capital Investment
- Information Security
- Linking Resources to Results
- Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement
- Modernization of the Internal Revenue Service
- Tax Compliance Initiatives
  - Business and Individual
  - Tax-Exempt Entities
- Security of the Internal Revenue Service
- Providing Quality Taxpayer Service Operations
- Complexity of the Tax Law
- Using Performance and Financial Information for Program and Budget Decisions
- Erroneous and Improper Payments
- Taxpayer Protection and Rights
- Processing Returns and Implementing Tax Law Changes During the Tax Filing Season
- Human Capital

# Analysis of Financial Statements

The following are the condensed financial statements of the Department as of and for the years ended September 30, 2006 and 2005. The complete financial statements and auditors' report are in Part III of this report.

**Condensed Balance Sheets**
**As of September 30, 2006 and 2005**
**(In Millions)**

| | 2006 | 2005 |
|---|---|---|
| **ASSETS** | | |
| **Intra-governmental Assets** | | |
| Due From the General Fund | $ 8,540,195 | $ 7,978,081 |
| Other Intra-governmental Assets | 326,552 | 304,677 |
| **Total Intra-governmental Assets** | **8,866,747** | **8,282,758** |
| Cash, Foreign Currency, and Other Monetary Assets | 63,892 | 47,578 |
| Investments and Related Interest | 9,325 | 9,404 |
| Tax, Other and Related Interest Receivables, Net | 21,962 | 21,430 |
| Other Assets | 26,052 | 33,202 |
| **Total Assets** | **$ 8,987,978** | **$ 8,394,372** |
| **LIABILITIES** | | |
| **Intra-governmental Liabilities** | | |
| Federal Debt and Interest Payable | $ 3,673,117 | $ 3,354,905 |
| Other Intra-governmental Liabilities | 320,817 | 288,137 |
| **Total Intra-governmental Liabilities** | **3,993,934** | **3,643,042** |
| Federal Debt and Interest Payable | 4,844,074 | 4,600,668 |
| Other Liabilities | 35,056 | 35,354 |
| **Total Liabilities** | **$8,873,064** | **$8,279,064** |
| **NET POSITION** | | |
| Unexpended Appropriations | 68,270 | 63,182 |
| Cumulative Results of Operations | 46,644 | 52,126 |
| **Total Net Position** | **$ 114,914** | **$ 115,308** |
| **Total Liabilities and Net Position** | **$ 8,987,978** | **$ 8,394,372** |

## Condensed Statements of Net Cost
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Cost of Treasury Operations:** | | |
| Net Economic Program Cost | $ 1,188 | $ 2,284 |
| Net Financial Program Cost | 12,413 | 11,093 |
| Net Management Program Cost | 428 | 417 |
| **Total Net Cost of Operations** | **$ 14,029** | **$ 13,794** |
| Net Federal Costs | 399,806 | 351,075 |
| **Net Cost of Operations, Federal Debt Interest, and Other Federal Costs** | **$ 413,835** | **$ 364,869** |

## Condensed Statement of Changes in Net Position
## For the Year Ended September 30, 2006 and 2005
## (In Millions)

| | FY 2006 | | | | FY 2005 |
|---|---|---|---|---|---|
| | Combined Earmarked Funds | Combined All Other Funds | Eliminations | Consolidated Total | Consolidated Total |
| **CUMULATIVE RESULTS OF OPERATIONS** | | | | | |
| Beginning Balance, as Adjusted | $ 30,817 | $ 21,309 | $ 0 | $ 52,126 | $ 56,308 |
| Budgetary Financing Sources | 441 | 412,061 | (30) | 412,472 | 362,272 |
| Other Financing Sources | 4 | (3,653) | (470) | (4,119) | (1,585) |
| Total Financing Sources | 445 | 408,408 | (500) | 408,353 | 360,687 |
| Net Cost of Operations | 352 | (414,687) | 500 | (413,835) | (364,869) |
| Net Change | 797 | (6,279) | 0 | (5,482) | (4,182) |
| **Cumulative Results of Operations** | **$ 31,614** | **$ 15,030** | **$ 0** | **$ 46,644** | **$ 52,126** |
| **UNEXPENDED APPROPRIATIONS** | | | | | |
| Beginning Balance, as Adjusted | 202 | 62,980 | | 63,182 | 56,850 |
| Total Budgetary Financing Sources | 0 | 5,088 | | 5,088 | 6,332 |
| Total Unexpended Appropriations | 202 | 68,068 | | 68,270 | 63,182 |
| **Net Position** | **$ 31,816** | **$ 83,098** | | **$ 114,914** | **$ 115,308** |

## Condensed Statements of Budgetary Resources
## For the Years Ended September 30, 2006
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Budgetary Resources:** | | |
| Unobligated Balance, Brought Forward | $ 64,670 | $ 69,912 |
| Recoveries of Prior Year Unpaid Obligations | 380 | 1,286 |
| Budget Authority | 446,742 | 386,110 |
| Other Budget Authority | (8,701) | (3,976) |
| **Total Budgetary Resources** | **$ 503,091** | **$ 453,332** |
| **Status of Budgetary Resources:** | | |
| Obligations Incurred | 445,551 | 388,662 |
| Unobligated Balance | 47,093 | 54,656 |
| Unobligated Balance Not Available | 10,447 | 10,014 |
| **Total Status of Budgetary Resources** | **$ 503,091** | **$ 453,332** |
| **Change in Obligated Balance** | | |
| Total Unpaid Obligated Balances, Net | $ 45,738 | $ 41,446 |
| Obligations Incurred, Net | 445,551 | 388,662 |
| Gross Outlays | (438,494) | (383,128) |
| Recoveries of Prior Year Unpaid Obligations, Actual | (380) | (1,286) |
| Changes in Uncollected Customer Payments from Federal Sources | 33 | 46 |
| Total Unpaid Obligated Balance, net, End of Period | 52,448 | 45,738 |
| **Net Outlays** | | |
| Gross Outlays | $ 438,494 | $ 383,128 |
| Offsetting Collections and Distributed Offsetting Receipts | (25,467) | (21,907) |
| **Net Outlays** | **$ 413,027** | **$ 361,221** |

## Condensed Statements of Financing
## For the Years Ended September 30, 2006, and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Resources Used to Finance Activities:** | | |
| Net Obligations | $ 419,300 | $ 365,515 |
| Net Other Resources Used to Finance Activities | (4,119) | (1,585) |
| **Total Resources Used to Finance Activities** | **415,181** | **363,930** |
| Total Resources Used to Finance Items Not Part of the Net Cost of Operations | 2,438 | (973) |
| **Total Resources Used to Finance the Net Cost of Operations** | **$ 412,743** | **$ 364,903** |
| Total Components of Net Cost of Operations That Will not Require or Generate Resources in the Current Period | 1,092 | (34) |
| **Net Cost of Operations** | **$ 413,835** | **$ 364,869** |

## Condensed Statements of Custodial Activity
## For the Years Ended September 30, 2006, and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Sources of Custodial Revenue** | | |
| **Revenue Received** | | |
| Individual Income and FICA Taxes | $ 2,034,209 | $ 1,864,687 |
| Corporate Income Taxes | 380,426 | 306,869 |
| Other Revenues | 146,937 | 131,911 |
| **Total Revenue Received** | **2,561,572** | **2,303,467** |
| Less Refunds | (277,778) | (267,114) |
| **Net Revenue Received** | **2,283,794** | **2,036,353** |
| Accrual Adjustment | 554 | 643 |
| **Total Custodial Revenue** | **2,284,348** | **2,036,996** |
| | | |
| **Disposition of Custodial Revenue:** | | |
| Amounts Provided to Fund the Federal Government | 2,283,420 | 2,035,899 |
| Other | 928 | 1,097 |
| **Total Disposition of Custodial Revenue** | **2,284,348** | **2,036,996** |
| **Net Custodial Revenue Activity** | **$ 0** | **$ 0** |

### Auditors' Report on the Treasury Department's Financial Statements

The Department received an unqualified audit opinion on its FY 2006 financial statements. The auditor reported a material weakness and two other reportable conditions.

### Limitations on the Principal Financial Statements

These statements have been prepared from Treasury's accounting records in conformity with the accounting principles generally accepted in the United States, and the form and content of entity financial statements specified by OMB Circular A-136, *Financial Reporting Requirements*, as amended. These principles are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB), which is designated the official accounting standards setting body of the Federal government by the American Institute of Certified Public Accountants.

While the financial statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by OMB, they are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

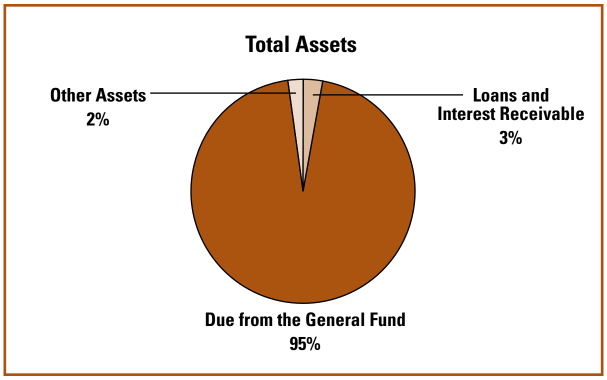
The financial statements should be read with the realization that they are for a component of a sovereign entity, that liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

## Financial Highlights

The following provides the highlights of Treasury's financial position and results of operations for FY 2006.

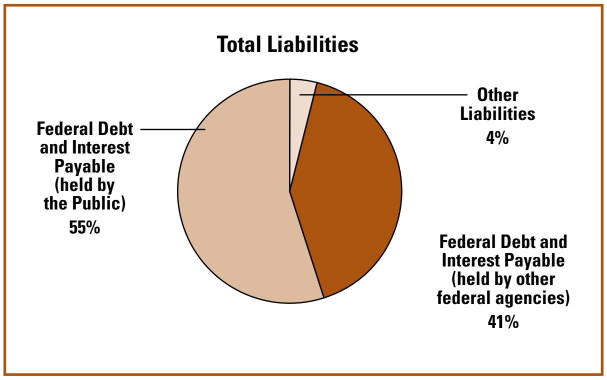
***Assets.*** Total assets increased from $8.4 trillion at September 30, 2005 to $9.0 trillion at September 30, 2006. The primary reason for the increase is the rise in the federal debt, which causes a corresponding rise in the "Due from the General Fund of the U.S. Government" account ($8.5 trillion.) This account represents future funds due from the General Fund of the U.S. Government to pay borrowings from the public and other federal agencies.

The majority of loans and interest receivable ($245.2 billion) included in "Other Intra-governmental Assets" are the loans issued by the Bureau of the Public Debt to other federal agencies for their own use or to private sector borrowers, whose loans are guaranteed by the federal agencies. In addition, $288 million are loans and credits issued by the United States to various foreign governments. These loans are due and payable in U.S. denominations.

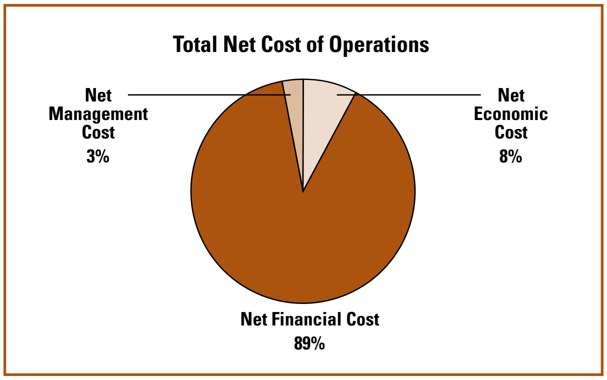



***Liabilities.*** Intra-governmental liabilities totaled $4.0 trillion, and include $3.7 trillion of principal and interest payable to various Federal agencies such as the Social Security Trust Fund. These borrowings do not include debt issued separately by other governmental agencies, such as the Tennessee Valley Authority or the Department of Housing and Urban Development.

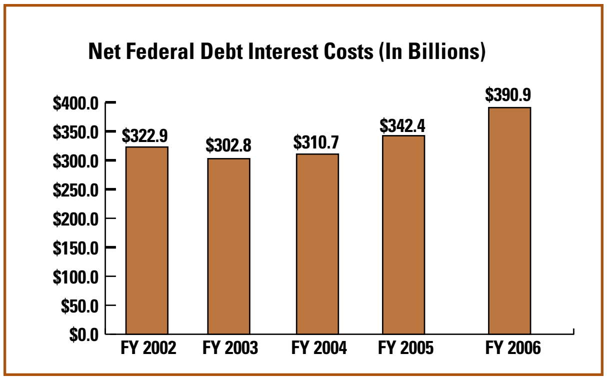
Liabilities also include federal debt held by the public, including interest, of $4.8 trillion; the majority of this debt was issued as Treasury Notes. The increase in total liabilities in FY 2006 over FY 2005 ($594 billion and 7.2%), is the result of increases in borrowings from various federal agencies ($318 billion), and federal debt held by the public, including interest, ($243 billion). Debt held by the public increased primarily because of the need to finance budget deficits.



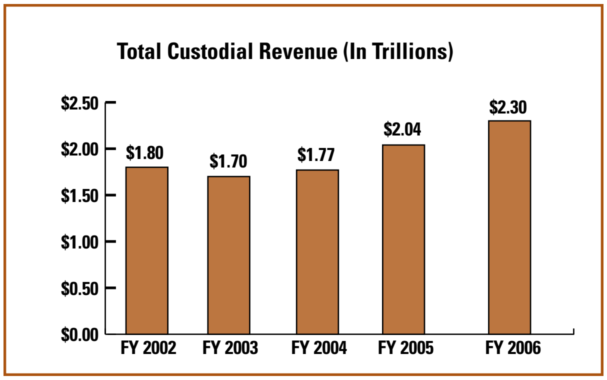

***Net Cost of Treasury Operations.*** The Consolidated Statement of Net Cost presents the Department's gross and net cost for its three strategic missions: economic program, financial program, and management program. The majority of the net cost of Treasury operations is in the financial mission area, which the cost increased in FY 2006 by $1.3 billion. Treasury is the primary fiscal agent for the Federal government in managing the Nation's finances by collecting revenue, making Federal payments, managing Federal borrowing, performing central accounting functions, and producing coins and currency sufficient to meet the demand.

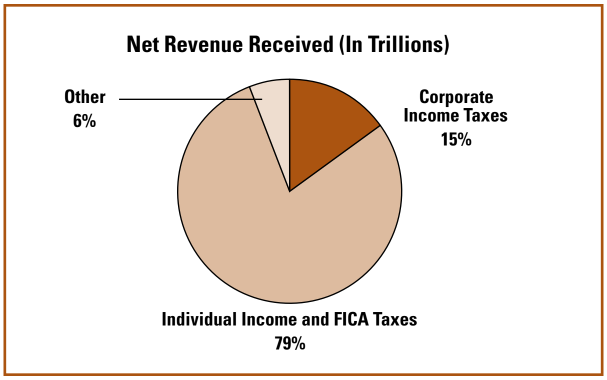



***Net Federal Debt Interest Costs.*** Interest costs have increased significantly ($48.5 billion in FY 2006 and $31.8 billion in FY 2005) over the past two years due to the increase in the federal debt.




***Custodial Revenue.*** Total net revenue collected by Treasury on behalf of the federal government includes various taxes, primarily income taxes, user fees, fines and penalties, and other revenue. Over 93 percent of the revenues are from income and social security taxes. Following a 15% ($260.8 billion) increase in FY 2005, net revenue increased by 12% ($247.4 billion) in FY 2006, due to a continuing high level of economic activity. The majority of increase in revenue was from the individual income and FICA taxes, which was primarily attributed to the growth in wages and overall taxable income.


Total Custodial Revenue (In Trillions)
$2.50
$2.00
$1.50
$1.00
$0.50
$0.00
$1.80
$1.70
$1.77
$2.04
$2.30
FY 2002
FY 2003
FY 2004
FY 2005
FY 2006


Net Revenue Received (In Trillions)
Other
6%
Corporate
Income Taxes
15%
Individual Income and FICA Taxes
79%

# Improper Payments Information Act and Recovery Act

## Summary of FY 2006 Activities

### Improper Payments Information Act

#### *Background*

The Improper Payments Information Act of 2002 (IPIA) requires agencies to review their programs and activities annually to identify those that are susceptible to significant erroneous payments. According to OMB Circular A-123, Appendix C, "Management's Responsibility for Internal Controls", "Significant" means that an estimated error rate and a dollar amount exceed the threshold of 2.5% and $10 million of total program funding. OMB Circular A-123, Appendix C also requires the agency to implement a corrective action plan that includes improper payment reduction and recovery targets.

Some Federal programs are so complex that developing an annual error rate is not feasible. The government-wide Chief Financial Officers Council developed an alternative for such programs to assist them in meeting the IPIA requirements. Agencies may establish an annual estimate for a high-risk component of a complex program (e.g., a specific program population) with the Office of Management and Budget (OMB) approval. Agencies also must perform trend analyses to update the program's baseline error rate in the interim years between detailed program studies. When development of a statistically valid error rate is possible, the reduction targets are revised and become the basis for future trend analyses.

#### *Treasury's Risk Assessment Methodology and Results for FY 2006*

Each year, the Department develops a comprehensive inventory of all funding sources and conducts a risk assessment for improper payments on all of its programs and activities. The risk assessment performed on all of Treasury's programs and activities resulted in low and medium risk susceptibility for improper payments except for the Internal Revenue Service's (IRS) Earned Income Tax Credit (EITC) program. The high-risk status of this program is well-documented and has been deemed a complex program for the purposes of the Improper Payments Information Act.

#### *Earned Income Tax Credit*

The Earned Income Tax Credit is a refundable tax credit that offsets income tax owed by low-income taxpayers and, if the credit exceeds the amount of taxes due, provides a lump-sum payment in the form of a refund to those who qualify. The FY 2006 estimate is that a maximum of 28% ($11.6 billion) and a minimum of 23% ($9.8 billion) of the EITC total program payments are overclaims.

Since June 2003, IRS has focused on reducing EITC overclaims through a five-point initiative designed to:

- Reduce the backlog of pending EITC examinations
- Minimize the burden and enhance the quality of communications with taxpayers
- Encourage eligible taxpayers to claim the EITC
- Ensure fairness by refocusing compliance efforts on income-ineligible taxpayers
- Pilot a certification effort to substantiate qualifying child residency eligibility

The Department continues to work with OMB to establish viable error rate measurements while working toward the development of a Corrective Action Plan.

### Recovery Audit Act

#### *Background*

The Recovery Audit Act requires agencies issuing in excess of $500 million in contracts to establish and maintain recovery auditing activities and report on the results of those recovery efforts annually. Recovery auditing activities include the use of (1) contract audits, in which an examination of contracts pursuant to the audit and records clause incorporated in the contract is performed, (2) contingency contracts for recovery services in which the contractor is paid a percentage of the recoveries, and (3) internal review and analysis in which payment controls are employed to ensure that contract payments are accurate.

### *Results for FY 2006*

During FY 2006, $4.6 billion in contracts (defined as issued and obligated contracts, modifications, task orders, and delivery orders) were issued. Improper payments in the amount of $2,305,424 were identified from recovery auditing efforts and, of this amount, $1,442,708 has been recovered with $862,716 outstanding as accounts receivable on September 30, 2006.

# Management Assurances

## The Secretary's Letter of Assurance

Management is responsible for establishing and maintaining internal controls, and the Department has evaluated its management controls, internal controls over financial reporting, and compliance with Federal financial systems standards. As part of the Department's evaluation process, the results of extensive testing, assessment, and independent audits were considered.

The Department can provide reasonable assurance that the objectives of the Federal Managers' Financial Integrity Act have been achieved, as a result of our evaluations, except for the material weaknesses noted below. We can provide qualified assurance that internal controls over financial reporting are effective as of June 30, 2006. Our assessment was conducted in accordance with the Office of Management and Budget Circular A-123, Appendix A. The Department is not in substantial compliance with the Federal Financial Management Improvement Act, however, because of its material weaknesses involving revenue accounting systems. The revenue accounting system weakness is the only weakness that affected our overall assurance level for A-123, Appendix A, for internal controls over financial reporting.

The Department retains six remaining material weaknesses as of September 30, 2006. The weaknesses are in the following areas:

Internal Revenue Service
- Resolving weaknesses in revenue accounting systems
- Improving systems modernization management and controls
- Reducing overclaims in the Earned Income Tax Credit program
- Improving systems security controls

Financial Management Service
- Improving systems, controls, and procedures to prepare the Government-wide financial statements

Departmental Offices
- Improving systems security

The Department began the year with seven material weaknesses. During FY 2006 no new material weaknesses were identified and one weakness was closed. Detailed information on our material weaknesses is provided in Appendix E. We continually are achieving positive results through:
- Emphasizing internal control program responsibilities throughout the Department.
- Ensuring senior management attention to management controls.
- Developing and implementing capital planning investment control processes.
- Focusing on developing and carrying out responsible plans for resolving weaknesses.

The progress we have achieved over the past few years will continue in FY 2007.

Sincerely,

Henry M. Paulson, Jr.

# Material Weaknesses, Audit Follow-up, and Financial Systems

### Federal Managers' Financial Integrity Act (FMFIA)

The management control objectives under FMFIA are to reasonably ensure that:

- programs achieve their intended results.
- resources are used consistent with overall mission.
- programs and resources are free from waste, fraud and mismanagement.
- laws and regulations are followed.
- controls are sufficient to minimize any improper or erroneous payments.
- performance information is reliable.
- system security is in substantial compliance with all relevant requirements.
- continuity of operations planning in critical areas is sufficient to reduce risk to reasonable levels.
- financial management systems are in compliance with Federal financial systems standards.

Deficiencies that seriously affect an agency's ability to meet these objectives are deemed "material weaknesses." The Department can provide reasonable assurance that the objectives of FMFIA have been achieved, except for the remaining material weaknesses noted in the Secretary's Letter of Assurance above. During FY 2006, the Department had a decrease of one material weakness. The reduction came as a result of the downgrade of the IRS material weakness "Collection of Unpaid Taxes" to a reportable condition. Six material weaknesses are outstanding as of September 30, 2006. Four of the remaining six are complex systems development or systems security weaknesses, and will require a more protracted timeframe to resolve. The last currently identified material weakness is targeted to be closed in FY 2009. See Appendix E for additional information on FMFIA material weaknesses.

Material weaknesses, both the resolution of existing ones and the prevention of new ones, received special attention during FY 2006. Over the past five years, we have made great progress in reducing the number of material weaknesses Treasury-wide. For FY 2007, we have made material weakness resolution a performance requirement for every executive, manager, and supervisor to continue our path of resolving the current material weaknesses and preventing new ones before they occur.

### Office of Management and Budget Circular A-123, Appendix A

The Department continues to strengthen and improve the execution of our mission through the application of sound internal controls over financial reporting. In response to Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Controls*, Appendix A, the Department developed and implemented an extensive testing and assessment methodology that identified and documented internal controls over financial reporting at the transaction level integrated with the Government Accountability Office's Standards for Internal Control. The testing and assessment was completed across all material Department bureaus and offices by June 30, 2006. The Department provides qualified reasonable assurance that internal controls over financial reporting are effective as of June 30, 2006 due to the revenue accounting system weaknesses at the Internal Revenue Service.

### Federal Financial Management Improvement Act (FFMIA)

FFMIA mandates that agencies "... implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level." FFMIA also requires that remediation plans be developed for any entity that is unable to report substantial compliance with these requirements.

As of September 30, 2006, the Department is not in substantial compliance with these requirements due to the revenue accounting system weaknesses at the

Internal Revenue Service. The Department continues to make progress with the implementation of the IRS remediation plan. For additional information on FFMIA non-compliance, see Appendix E.

### Audit Follow-Up

During FY 2006, Treasury continued its efforts to improve both the general administration of management control issues throughout the Department and the timeliness of the resolution of all findings and recommendations identified by the Office of the Inspector General (OIG), the Treasury Inspector General for Tax Administration (TIGTA), the Government Accountability Office, and external auditors.

The Department management at every level will maintain the momentum on accomplishing Planned Corrective Actions (PCAs) to resolve and implement sound solutions for all audit recommendations, and, although we have made great progress, we have considerably more work to do. Specifically, we must provide timely and accurate performance in addressing PCA schedules and implementation and integrate the effects of those actions more fully into our management decision-making processes. We need to identify more precisely what it costs to accomplish our varied missions and develop ways to improve overall performance. This will entail building upon the progress we have made in expanding the communication and coordination among offices variously involved in strategic planning, budget formulation, budget execution, performance management and financial management.

### Financial Management Systems Framework

The Department's overall financial management systems framework consists of a Treasury-wide financial data warehouse, supported by a financial reporting tool and separate bureau financial systems. Bureaus submit monthly financial data to the data warehouse within three business days. The Department produces monthly financial statements and reports for financial analysis. This framework satisfies both the bureaus' diverse financial operational and reporting needs as well as the Department's internal and external reporting requirements. The financial data warehouse is part of the overarching Treasury-wide Financial Analysis and Reporting System (FARS), which also includes applications for bureaus to report the status of their performance measures and the status of their planned audit corrective actions. Additional FARS applications are being planned to improve the Department's financial management and operations. This includes asset management, budget formulation and execution, and enhanced reporting functionality.

The Department continues to enhance its financial management systems. As of September 30, 2006, the number of financial management systems increased to 69, up from 68 at the end of fiscal year 2005.

The Bureau of Public Debt's Administrative Resource Center (ARC) has been selected by the Office of Management and Budget as a Financial Management Line of Business Shared Service Provider. ARC currently services 28 Federal entities for core financial systems, including eleven Treasury bureaus and reporting entities. Over the next two years, two additional Treasury bureaus will migrate to ARC for core financial systems support.

ARC also provides systems and service support to eleven Department bureaus in the processing of their travel needs as part of the Department's e-Travel initiative. Of the three remaining bureaus, one is currently conducting a pilot review. The two remaining bureaus are working with the Department to finalize plans for e-Travel implementation.

The Department's FARS applications are also used to support other Federal agencies. The Department currently hosts two agencies for consolidated financial processing and reporting. In addition, the Department has demonstrated various FARS applications to other agencies to operate within their own computer centers. The Department continues to demonstrate FARS applications to other agencies as requested.

# Part II: Annual Performance Report

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## Performance Scorecard

The following scorecard indicates the FY 2006 results for a selection of key Treasury Department performance measures. For a complete list of official performance measures see Appendix A.

| Measure | FY 2006 Planned | FY 2006 Actual | Target Met? | FY 2007 Planned |
|---|---|---|---|---|
| **Financial** | | | | |
| Cost to Process a Federal Revenue Collection Transaction | 1.37 | 1.1* | ✓ | 1.33 |
| Unit Cost for Federal Government Payments | .35 | .37 | | .35 |
| Percent of Payments Made Electronically | 78 | 77 | | 79 |
| Percent of Payments Made Accurately and On-time | 100 | 100 | ✓ | 100 |
| Percent of Debt Auction Results Released in Two Minutes +/- 30 Seconds | 95 | 100 | ✓ | 95 |
| Percent of Retail Customer Service Transactions Completed Within Thirteen Business Days | 90 | 98 | ✓ | 90 |
| Cost Per Federal Funds Investment Transaction | 90.15 | 55.06 | ✓ | 64.5 |
| Percentage of Government-wide Accounting Reports Issued Accurately | 100 | 100 | ✓ | 100 |
| Variance Between Estimated and Actual Receipts | 5 | 3.9 | ✓ | 5 |
| Percent of Thrifts That Are Well Capitalized | 95 | 99.9 | ✓ | 95 |
| Percent of Banks That Are Well Capitalized | 95 | 99 | ✓ | 95 |
| Average Time to Process Enforcement Matters (in years) | 1 | 1 | ✓ | 1 |
| Percentage of customers satisfied with BSA Direct E-filing component | Baseline | 92 | ✓ | 90 |
| Increase the Number of Outreach Engagements With the Charitable and International Financial Communities | 105 | 45 | | 70 |
| Number of Countries Assessed for Financial Action Task Force Compliance | 45 | 5 | | 12 |
| Cost Per 1,000 Currency Notes | 28.5 | 27.49 | ✓ | 32.5 |
| Cost Per 1,000 Coin Equivalents | 6.62 | 7.55 | | 6.96 |
| **Economic** | | | | |
| Number of full-time equivalent jobs created or maintained in underserved communities by businesses financed by CDFI Program Awardees and New Markets Tax Credit (NMTC) Allocatees (Actual relate to those CDFI awardees and NMTC allocates that submitted required annual performance data, for relevant reporting period, timely to the Fund). | 29,158 | 22,329 | | 34,009 |
| Administrative costs per number of Bank Enterprise Award (BEA) Applications processed | 1,280 | 1,630 | | 1,455 |
| Improve International Monetary Fund (IMF) Effectiveness and Quality Through Periodic Review of IMF Programs | 90 | 100 | ✓ | 90 |
| Level of MDB grant financing and satisfactory results measurements (Grants as a % of IDA FY Commitment) | 30.4 | 25 | | 30 |
| Number of New FTA and BIT Negotiations Underway or Completed | 9 | 12 | ✓ | 7 |
| **Management** | | | | |
| Percent of Statutory IG Audits Completed By the Required Date | 100 | 100 | ✓ | 100 |
| Average Calendar Days for TIGTA to Issue Final Audit Report | 325 | 334 | | 325 |
| Number of Open Material Weaknesses | 2 | 1 | ✓ | 1 |
| Management Cost Per Treasury Employee | 40.27 | 40.59 | | 38.21 |

## Internal Revenue Service Performance Scorecard

| Measure | FY 2006 Planned | FY 2006 Actual | Target Met? | FY 2007 Planned |
|---|---|---|---|---|
| Customer Service Representative (CSR) Level of Service | 82% | 82% | ✓ | 82% |
| Customer Contacts Resolved per Staff Year | 7,477 | 7,414 | | 7,555 |
| Percent of Eligible Taxpayers Who file for EITC | 80% | TBD | * | TBD |
| Customer Accuracy – Tax Law (Phones) | 90% | 90.9% | ✓ | 90.5% |
| Customer Accuracy – Accounts (Phones) | 92% | 93.2% | ✓ | 92.6% |
| Timeliness of Critical Filing Season Tax Products to the Public | 92% | 83% | | 93% |
| Timeliness of Critical Other Tax Products to the Public | 85% | 61.2% | | 86% |
| Percent of Individual Returns Processed Electronically | 55% | 54.1% | | 58.8% |
| Percent of Business Returns Processed Electronically | 18.6% | 16.6% | | 20.6% |
| Refund Timeliness – Individual (Paper) | 99.2% | 99.3% | ✓ | 99.2% |
| Taxpayer Self Assistance Rate | 45.7% | 46.8% | ✓ | 47.5% |
| Examination Coverage – Individual | 0.9% | 1.0% | ✓ | 1.0% |
| Field Examination – Embedded Quality [1] | Baseline | * | Baseline | TBD |
| Office Examination – Embedded Quality [1] | Baseline | * | Baseline | TBD |
| Examination Quality – Industry | 80% | 85% | ✓ | 84% |
| Examination Quality – Coordinated Industry | 92% | 96% | ✓ | 93% |
| Examination Coverage – Business | 7.5% | 7.4% | | 8.4% |
| Examination Efficiency – Individual | 121 | 128 | ✓ | 128 |
| Automated Underreporter Efficiency | 1,759 | 1,832 | ✓ | 1,834 |
| Automated Underreporter Coverage | 2.30% | 2.40% | ✓ | 2.30% |
| Collection Coverage – Units | 52% | 54% | ✓ | 52% |
| Collection Efficiency – Units | 1,650 | 1,677 | ✓ | 1,717 |
| Field Collection Embedded Quality [1] | Baseline | 84.2% | Baseline | TBD |
| Automated Collection System (ACS) Accuracy | 88% | 91% | ✓ | 89% |
| Criminal Investigations Completed | 3,945 | 4,157 | ✓ | 3,960 |
| TEGE Determination Case Closure | 112,400 | 107,761 | | 112400+ |
| BSM Project Cost Variance by Release/Sub-release [1] | Baseline | ** | Baseline | 10% |
| BSM Project Schedule Variance by Release/Sub-release [1] | Baseline | ** | Baseline | 10% |

**KEY:**

- * Performance reported after close of calendar year
- ** Cost and Schedule variance is based on +/- 10% and is reported on several project releases/sub-releases (See Appendix A for full results on these measures).
- [1] These measures were not reported in the FY 2005 PAR and are baseline in FY 2006
- \+ The target was revised based on the implementation of a new staggered amendment filing process.

# Treasury Strategic Goals and Objectives

Below is a crosswalk that links the Department's focus areas, goals and objectives. The Department's goals and objectives fall into three focus areas: Economic, Financial and Management. The goals and objectives describe how the Treasury Department will (1) promote prosperous and stable U.S. and world economies; (2) preserve the integrity of financial systems; (3) manage the U.S. Government's finances effectively; and (4) ensure sound and professional internal operations of the Department.

| | Strategic Goals | Strategic Objectives |
|---|---|---|
| **Economic** | **Promote Prosperous U.S. and World Economies** | Stimulate Economic Growth and Job Creation<br>Improve and Simplify the Tax Code<br>Provide a Flexible Legal and Regulatory Framework |
| | **Promote Stable U.S. and World Economies** | Increase Citizens' Economic Security<br>Improve the Stability of the International Financial System |
| **Financial** | **Preserve the Integrity of Financial Systems** | Disrupt and Dismantle Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate Their Support Networks<br>Execute the Nation's Financial Sanctions Policies<br>Increase the Reliability of the U.S. Financial System |
| | **Manage the U.S. Government's Finances Effectively** | Collect Federal Revenue When Due, Through a Fair and Uniform Application of the Law<br>Manage Federal Debt Effectively and Efficiently<br>Make Collections and Payments on Time and Accurately, Optimizing Use of Electronic Mechanisms<br>Optimize Cash Management and Effectively Administer the Government's Financial System |
| **Management** | **Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of Treasury** | Protect the Integrity of the Department of Treasury<br>Manage Treasury Resources Effectively to Accomplish the Mission and Provide Quality Customer Service |

** NOTE: When costing our strategic objectives - All funding charts presented in this section are estimated costs based on allocating the Department's net cost of operations by strategic objective.

# E Creating the Conditions for Economic Prosperity

| Strategic Goals | Strategic Objectives |
|---|---|
| **Promote Prosperous U.S. and World Economies** | Stimulate Economic Growth and Job Creation |
| | Provide a Flexible Legal and Regulatory Framework |
| | Improve and Simplify the Tax Code |
| **Promote Stable U.S. and World Economies** | Increase Citizens' Economic Security |
| | Improve the Stability of the International Financial System |

## Promote Prosperous U.S. and World Economies

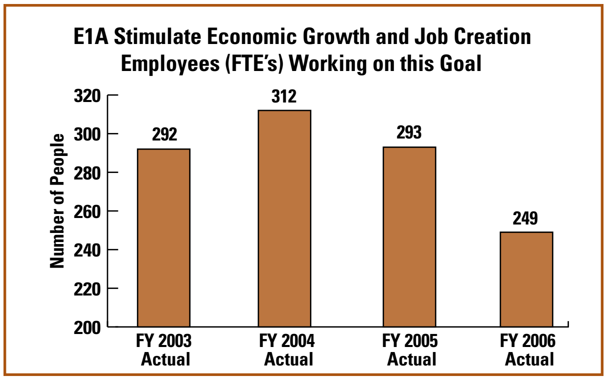
### *Stimulate Economic Growth and Job Creation*

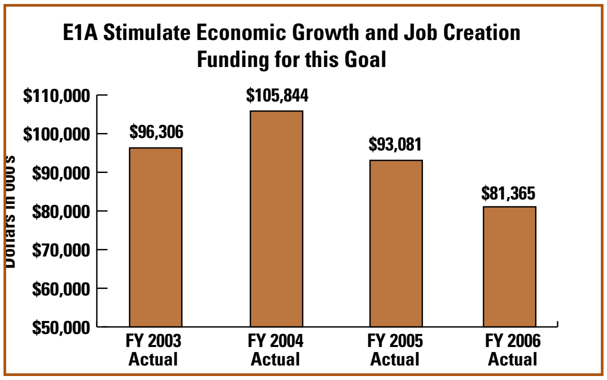
The Department of the Treasury, with other agencies and organizations, works to stimulate economic growth and raise living standards in the United States and abroad.

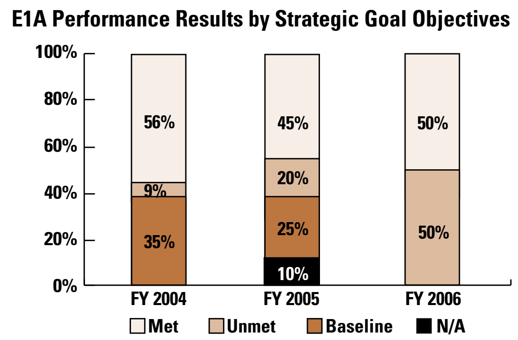
To achieve conditions promoting prosperity and stability in the U.S. and world economies, we must stimulate economic growth. This is accomplished through policies addressing overall economic development, implementing pro-growth tax programs, regulating banking and financial institutions, advocating for free trade, promoting assistance programs in distressed communities, expanding opportunities for American businesses and workers in the global economy, creating good jobs with mobility and wage growth, averting or mitigating financial crises and, in general, accelerating and sustaining the economic performance of the nation. Modernizing entitlement programs before they destabilize the economy is a critically important aspect of this, as is keeping the economy performing at peak potential by encouraging and supporting American competitiveness through innovation.

### Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $81.36 million with a workforce of 249 employees to stimulate economic growth and job creation. The Department of the Treasury met 50 percent of its performance measures for this objective.

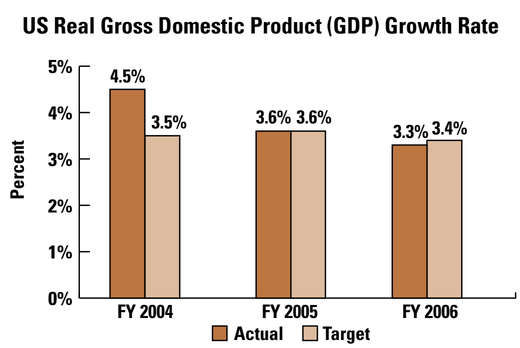


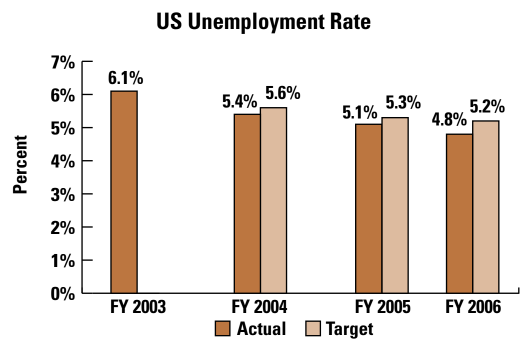



## Discussion and Analysis

***Economic Policies:*** The Department of the Treasury develops and implements economic policies to stimulate economic growth and job creation. While drawing a direct relationship between the Department's actions and economic indicators is difficult, policy makers help to create an environment conducive to strong economic growth and a healthy labor market. In FY 2006, growth in the real Gross Domestic Product (GDP), the broadest measure of the economy's performance, was 3.3 percent, slightly below that of FY 2005, at 3.6 percent. The solid pace of expansion contributed to job creation and helped lower the unemployment rate from an average of 5.1 percent, in FY 2005, to 4.8 percent in FY 2006.

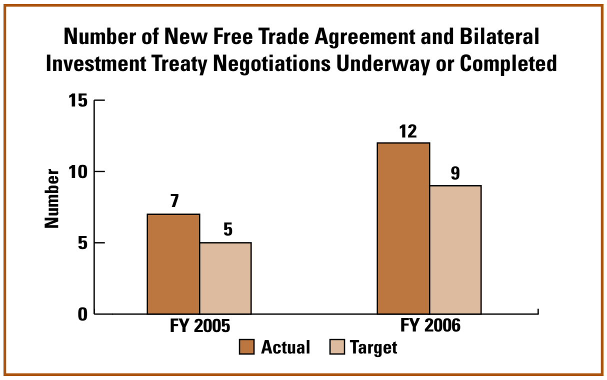



Each year, the Department's Office of Economic Policy participates in an interagency working group which is responsible for developing the economic assumptions that serve as the foundation for the Administration's budget forecast. In FY 2006, the Department of the Treasury made several important contributions to this effort, including a detailed presentation on the components of potential GDP. Economic Policy's work in this area was used to develop the forecast for economic growth and estimated tax receipts in formulating the President's overall financial plan for the federal government.




***Removing International Barriers to Trade and Investment:*** The Treasury Department participates in the negotiation of international agreements that remove trade and investment barriers. These agreements lead to enhanced global market efficiency, and increased job and business opportunities for Americans. The U.S. seek strong commitments from its trading partners to ensure those markets are available to the U.S. on a fair and open basis. Once implemented, these agreements serve as a core element of our trading partner's economic infrastructure, enhancing international economic and financial stability. The Department participates actively in these negotiations, which are facilitated through the World Trade Organization or through U.S.-initiated bilateral and regional Free Trade Agreements (FTAs) and Bilateral Investment Treaties (BITs).

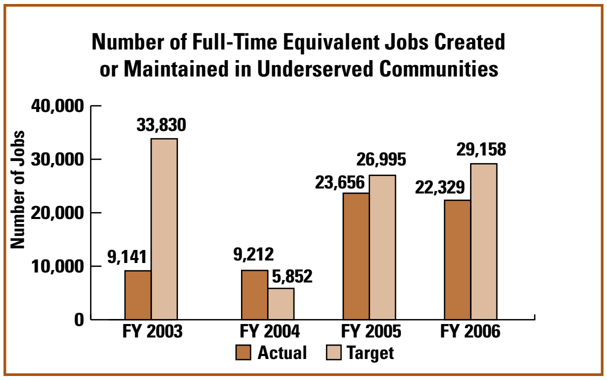
In July 2005, the U.S. Congress passed the Central American – Dominican Republic Free Trade Agreement (CAFTA-DR) and to date, the agreement was implemented by El Salvador, Honduras, Nicaragua, and Guatemala. The Treasury Department co-led the financial services negotiations and was a significant participant in negotiations of the investment provisions. Once fully implemented, CAFTA-DR will end most tariffs on more than $32 billion of two-way trade between the United States and Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras and Nicaragua.




In FY 2006, negotiations were concluded on three FTAs – Oman, Peru, and Colombia. Open FTA negotiations launched earlier include Panama, Thailand, Ecuador and the United Arab Emirates (UAE). In addition, FTA negotiations were launched with Korea and Malaysia.

BITs contain provisions that help ensure efficient and effective use of capital, and provide a legal framework to enhance investor confidence, economic growth, and greater opportunities for American workers and employers. Building on the model BIT developed last year, the Department conducts on-going negotiations with Pakistan. In addition, Congress ratified a FY 2006 BIT with Uruguay.

***Creating Opportunity in Economically Distressed Communities:*** The Community Development Financial Institutions (CDFI) Fund's CDFI Program awardees and New Markets Tax Credit (NMTC) allocatees create jobs in economically distressed communities, by lending to and investing in business and real estate projects. In FY 2006, the CDFI Fund reported 22,329 jobs created or maintained by awardees and allocatees.




***Financial Assistance Awardees Exceed Leverage Goal:*** The CDFI Fund's Financial Assistance component gives financial awards to CDFIs that demonstrate the greatest ability to leverage non-federal dollars which support comprehensive business plans that create community development impact in underserved markets. In FY 2006, the Fund made $24 million in Financial Assistance awards to CDFIs that primarily serve rural and urban low-income communities. In addition, awardees leveraged the Fund's award dollars with $1.4 billion in private and non-CDFI Fund dollars, therefore significantly exceeding the $1.1 billion leveraging goal and marking this the second consecutive year the goal was surpassed. The leverage ratio of $27 of private and non-CDFI Fund dollars for every $1 of Financial Assistance awards held constant from FY 2005 to FY 2006.

***Native Initiatives Awardees Surpass Growth Expectations:*** The CDFI Fund's Native Initiatives are designed to overcome barriers preventing access to credit, capital and financial services in Native American Communities. Through these initiatives, the CDFI Fund provides monetary awards and training aimed at increasing the number and capacity of existing or new CDFIs serving Native Communities. In FY 2006, the CDFI Fund issued $4.3 million in Native Initiative awards to 23 CDFIs, and Native CDFI awardees' reported asset growth of 182 percent, far exceeding the 33 percent projection. This asset growth represent required timely reporting of performance data to the Fund by 7 Native CDFI awardees. Most organizations experienced growth and one start-up CDFI had a ten-fold increase in its assets.

***Bank Enterprise Award (BEA) Program:*** The BEA Program provides insured depository institutions with financial incentives to expand investments in CDFIs and increase direct lending, investment, and service activities in economically distressed communities. The BEA Program provided modest monetary awards for large increases in community development, thereby leveraging the CDFI Fund's dollars and putting more capital to work. BEA applicants showed an increase of over $318 million in community development activities from FY 2005 to FY 2006, surpassing the CDFI Fund's goal of $81 million by nearly 293 percent.

***New Markets Tax Credit (NMTC) Program:*** The NMTC Program allows taxpayers a federal income tax credit for making qualified equity investments in designated Community Development Entities (CDEs), which must utilize the investment in low-income communities. In FY 2006, the CDFI Fund and the IRS made $3.5 billion in tax credit allocations providing recipients the ability to raise capital and invest. The CDEs, in FY 2006, made $2 billion in loans and investments exceeding the $1.6 billion projection. The CDEs used NMTC proceeds to finance a variety of community activities throughout the United States, many of which would not have been undertaken without the benefit of this tax credit.

In an effort to improve service to the American public, the CDFI Fund began two independent program evaluations in FY 2006. The first was a review of the NMTC Program; the second was a review of the CDFI and Training Programs. Evaluation results, including recommendations for program improvements, are expected in FY 2007.

### Moving Forward

In FY 2007, the Office of Economic Policy will continue to advance its analytical and forecasting capabilities. Special emphasis will be placed on streamlining and improving analyses and the flow of information to policy makers.

While the CDFI Fund did not achieve its jobs goal for FY 2006, it will continually make changes to programs to help communities in need. The shortfall was driven by an overestimation of the number of jobs that the NMTC Program would create or maintain per year. The CDFI Fund developed the jobs target based on the only actual data available for this relatively young program – 8 FY 2003 allocatees' performance data on 28 transactions. The Fund is currently reviewing the most recent performance data, which includes data on hundreds of transactions financed by more than 50 allocatees, and will revise future year's performance targets based on these.

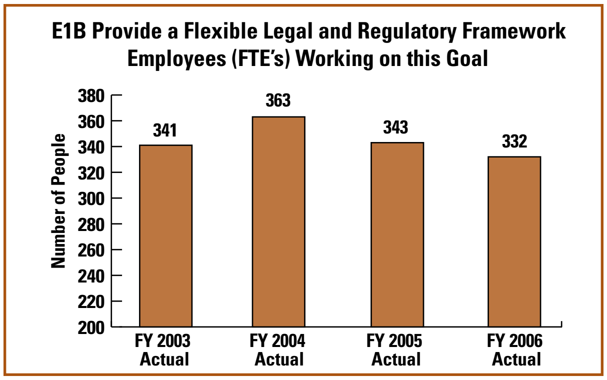
BITs and the investment provisions in FTAs contain stipulations that help ensure the most efficient and effective use of capital, and provide the legal framework to enhance investor confidence, economic growth, and greater opportunities for American workers and employers. In its ongoing efforts to expand BITs with other nations, the Treasury Department will continue to negotiate a formalized agreement with Pakistan based on the model developed last year.

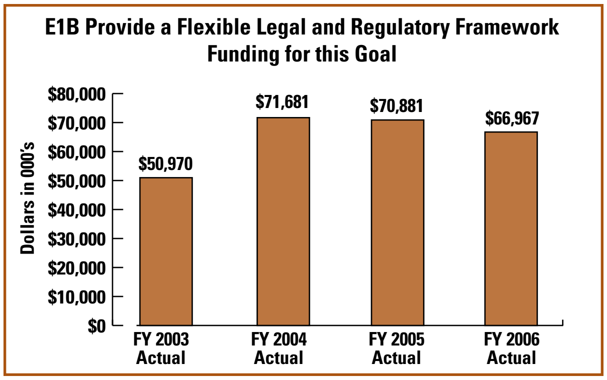
### *Provide a Flexible Legal and Regulatory Framework*

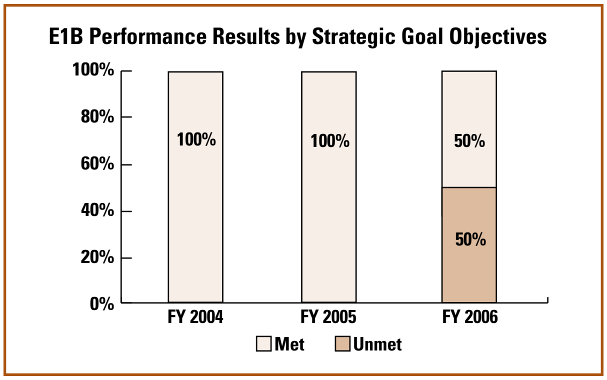
The Department of the Treasury is the primary regulator and supervisor of national banks, savings associations, and savings and loan holding companies. The Treasury Department's regulation efforts are performed through the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS). OCC and OTS work to streamline their licensing and supervisory procedures, and to keep regulations current, clearly written and supportive of an effective process to promote competitive financial services, consistent with safety and soundness.

## Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $66.96 million with a workforce of 332 to provide a flexible legal and regulatory framework, and met 50 percent of its performance measures for this objective.




## Discussion and Analysis

The OCC evaluates the suitability of banks and their subsidiary structures and activities. A responsive and efficient licensing operation is essential to meet the needs of banks that seek to become or are part of the national banking system. In FY 2006, the OCC received approximately 3,760 corporate applications and notices. Of the 2,425 decisions issued on applications, 94 percent were completed within the established timeframe, while providing a consistently high level of services as rated by applicants. In addition, the OCC received 1,367 applications and notices electronically, an increase of 8.8 percent over the 1,256 received in FY 2005. Electronic filing reached 36 percent of all applications and notices received in FY 2006. This activity promotes safety and soundness of these institutions.

In FY 2006, OCC issued 78 legal opinions on significant topics which include permissible bank premises, trust company involvement in closed-end investment funds, and use of cash-settled derivative transactions. Of the opinions subject to the established processing time frame, 90 percent were issued on time, slightly higher than the target of 86 percent.

Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), federal bank and thrift regulations are reviewed at least once every ten years in an effort to eliminate burdensome, unnecessary and outdated regulatory requirements. During FY 2006, the OCC, the OTS, and the federal banking agencies conducted this review process. The federal banking agencies sponsored numerous banker outreach events across the country to gain insight into issues the industry considers burdensome. Congress passed and President Bush signed into law the "Financial Services Regulatory Relief Act of 2006" which provides regulatory burden relief for the financial services, and banking and thrift industries. The law allows regulators to adjust exam cycles of healthy institutions for greater efficiency; modernizes record keeping requirements for regulators, and requires the federal banking agencies to propose within six months a simple, uniform privacy notice to comply with the Gramm-Leach-Bliley Act of 1999.

During FY 2006, the OCC, the OTS, and the federal bank regulators, issued final risk management guidance on non-traditional mortgage products, concentrating in commercial real estate lending and financial transactions with a complex structure. In addition, the guidance addressed the importance of managing potentially heightened risk levels to ensure that consumers have sufficient information to clearly understand loan terms and make the best decision. The guidance "Interagency Questions and Answers Regarding Community Reinvestment," was published in the March 2006 *Federal Register* and implements recent changes to the Community Reinvestment Act (CRA) regulations, as well as, addressing changes dealing with CRA consideration available for bank activities that revitalize or stabilize designated disaster areas and underserved or distressed middle-income rural areas, and the new community development test for banks with assets between $250 million and $1 billion.

The OTS, like the OCC, charters, examines, supervises, and regulates federal savings associations, in addition to their holding companies. The OTS strives to reduce regulatory burden on savings associations while maintaining effective supervision. To achieve this goal, the OTS is improving the application process, limiting assessment rate increases, and reviewing and making suggested improvements to burdensome statutes and regulations. The OTS tailors examinations based on savings association's risk profile; smaller savings associations undergo streamlined exams, while larger and more complex savings associations are comprehensively reviewed.

In 2006, the OTS continued to combine examinations for safety and soundness and compliance in order to attain greater efficiencies, improve its assessment of risk, reduce regulatory burden, and provide examiners with broader developmental opportunities. For the fourth consecutive year, the OTS managed its operations to ensure that assessment rate increases did not exceed the inflation rate.

### Moving Forward

The OCC legal opinions and corporate decisions will enable national bank activities to continue to evolve, consistent with safety and soundness. The OCC will continue to support the national banks' ability to operate under uniform national standards. In FY 2007, the OCC will propose a notice of proposed rulemaking to eliminate or streamline existing requirements or procedures, and enhance national banks' flexibility in conducting authorized activities, either by revising provisions currently contained in OCC regulations, or by codifying, and thus making generally applicable, conclusions that the OCC has reached in case-by-case determinations. The OTS will work with Congress in 2007 to further reduce regulatory burden for all insured depository institutions.

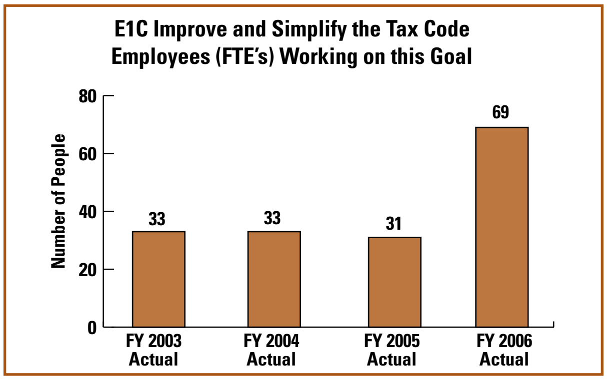
The OCC and the OTS will continue to monitor their performance to efficiently control cost, while ensuring the safety and soundness of the national bank and thrift industry. Both organizations use the performance measure of total cost per $100,000 of assets regulated to track their success in achieving their targets. Improvements in processes and procedures will continue to be implemented to improve efficiency.

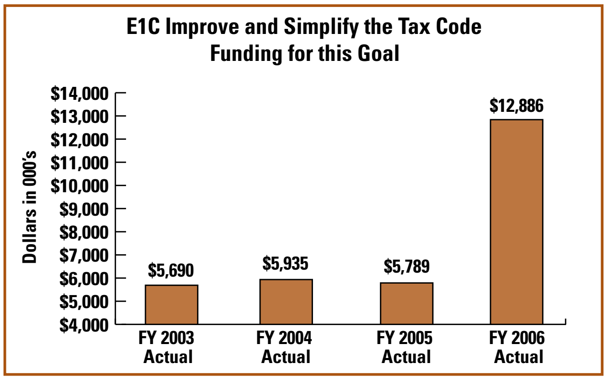
## *Improve and Simplify the Tax Code*

The Treasury Department is focused on simplifying and reforming the tax code, which will reduce the cost of compliance and contribute to economic growth. The Department's Office of Tax Policy conducts this analysis.

### Performance Summary and Resources Invested

In FY 2006, the Department of the Treasury spent $12.88 million with a workforce of 69 employees committed to the analysis and development of proposals to improve and simplify the tax code. Performance measure data was not available for this objective due to revisions or discontinuance of measures.




**New performance measures are being developed for this activity**

## Discussion and Analysis

In FY 2006, the Department's Office of Tax Policy and the IRS continued to work together with the President's Advisory Panel on Federal Tax Reform. In November 2005, the Panel issued a report entitled "Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System" which recommends two options for fundamental reform of the federal tax system. The Department of the Treasury is evaluating the Panel's report and considering options for reform.

## Moving Forward

In September 2006, the Department announced a comprehensive strategy for reducing the tax gap in FY 2007 and beyond. The strategy builds upon the current efforts of the Treasury Department, working with the Office of Management and Budget, to improve compliance. Four key principles guided the development of this strategy:

- Unintentional taxpayer errors and intentional taxpayer evasion should both be addressed
- Sources of noncompliance should be targeted with specificity
- Enforcement activities should be combined with a commitment to taxpayer service
- Policy positions and compliance proposals should be sensitive to taxpayer rights and maintain an appropriate balance between enforcement activity and imposition of taxpayer burden

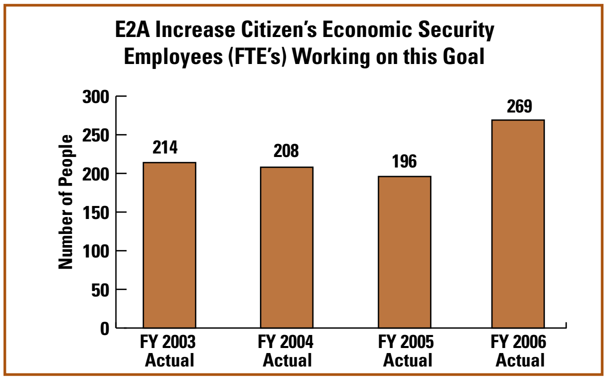
## Promote Stable U.S. and World Economies

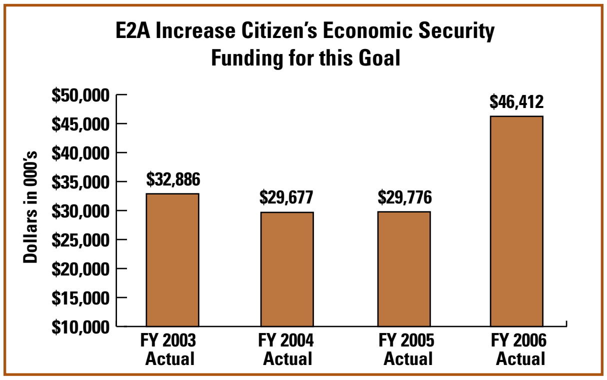
### *Increase Citizens Economic Security*

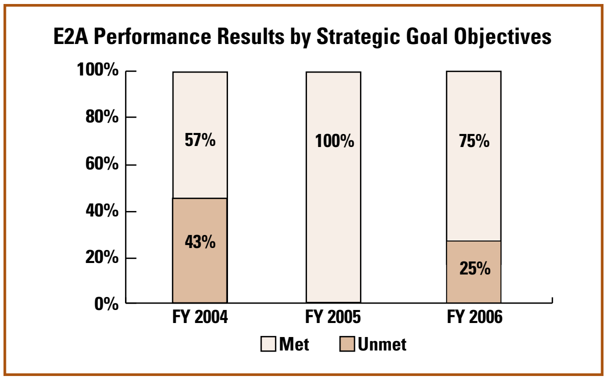
The Treasury Department promotes a stable U.S. economy by encouraging personal savings, protecting the security of pensions, ensuring the privacy of personal information in financial transactions, and protecting consumers from fraud and deception. The Office of International Affairs (IA), the Office of Financial Education, the Office of Economic Policy (EP), and the Alcohol and Tobacco Tax and Trade Bureau (TTB) work to further these ends.

### Performance Summary and Resources Invested

In FY 2006, the Department of the Treasury spent $46.41 million with a workforce of 269 employees to increase citizens' economic security. The Department met 75 percent of its performance measures for this objective.



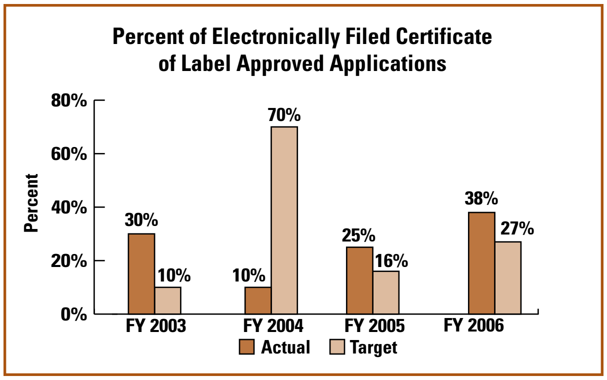

### Discussion and Analysis

***Pensions:*** The Treasury Department's Office of Economic Policy (EP) supported the Administration's initiative to ensure secure pensions for citizens through fundamental reform of the defined-benefit pension system.

***Gulf Coast Redevelopment and Flood Insurance Reform:*** EP provided analysis and developed options in support of the Administration's initiatives to encourage post-Katrina Gulf Coast redevelopment and to reform the flood insurance system.

***Avian Influenza:*** EP helped create coordinated epidemiological and economic models to evaluate policy options in the event of an influenza pandemic.

***Regulation:*** TTB uses business regulation to protect alcohol consumers from fraud and deception. Prior to introducing most alcoholic beverages into interstate commerce, TTB requires that importers and bottlers obtain either a Certificate of Label Approval (COLA) or an exemption from such. Personal and financial background investigations, as well as inspections of operations are conducted. In FY 2006, the Department approved 80,000 of the 111,000 COLA applications received.




***Monitoring the Economy:*** The Department of the Treasury promotes a stable economy by conducting timely, in-depth analysis of economic developments and emerging trends. In FY 2006, the Treasury Department prepared over 400 updates on breaking economic news and more than two dozen studies for the Secretary. By sharing these materials with key policy makers at other agencies, economic stability is enhanced and relevant economic issues are properly understood.

***Improving Receipts Forecasting Capabilities:*** EP participated in the Revenue Forecasting Workgroup to identify recent trends in tax receipts based on monthly budget reporting and daily cash flows, and recent changes in key macroeconomic indicators, which could result in a re-estimate of the major budget receipt categories. The work of this group, which also includes representatives from Tax Policy and Domestic Finance, helps improve the accuracy of the Department's annual forecast of the variance between estimated and actual tax receipts.

***Entitlement Reform:*** EP supported the important goal of entitlement reform, and developed a comprehensive framework for evaluating and understanding Social Security reform. This framework is instrumental in educating policymakers about Social Security reform, and as a communication tool to discuss reform. In FY 2006, the Department's primary focus of the health care work was to study, in a variety of contexts, the causes and consequences of high health care spending, which is critical to stimulating economic growth and job creation over the long-term.

***Financial and Currency Education:*** The U.S. Treasurer's Office is the only office in the Treasury Department older than the Department itself. The Treasurer advises the Directors of the BEP and the Mint on various collaborative outreach and educational efforts, as well as serves as an advisor to the Secretary and Deputy Secretary of the Department on matters relating to coinage, currency, and the production of other items by the Treasury Department, and improving currency and financial education.

In FY 2006, the Treasurer played an instrumental role in an educational campaign for public awareness on the newly designed $10 bill, by participating in numerous events both domestically and internationally. In addition, the Treasurer served as a key member of the Anti-counterfeit Deterrence Committee, which coordinates with the Treasury Department, the Federal Reserve, and the U.S. Secret Service in analyzing threats, monitoring counterfeit activity, evaluating deterrence tools, and implementing design changes.

During FY 2006, the Treasurer underscored the success of the U.S. economy and promoted financial education for all Americans, particularly advocating establishing a relationship with a traditional financial institution, and planning and saving for the future. The Treasurer is committed to educating the public on the many federal resources available on personal finance topics, through keynote remarks at conferences across the country, interviews, and the Department public service announcements. The Treasurer is a key spokesperson for Treasury's Go Direct campaign, an effort to educate federal benefit payment recipients of the advantages, safety, and security of receiving their payments by direct deposit rather than by paper check.

In addition, the Treasurer initiated coordination activities within the Department to address special challenges faced by the estimated 10 million American households currently considered "unbanked," or who do not have an established relationship with a traditional financial institution. This ongoing effort continues to focus on developing possible approaches to encourage this portion of the U.S. population to become "banked" and save for the future.

### Moving Forward

In FY 2007, the Revenue Forecasting Workgroup will help the Department of the Treasury again meet its forecast target for the annual variance between estimated and actual tax receipts. The Workgroup will continue to improve the forecasting process.

The Office of Economic Policy will continue to support the important goal of entitlement reform, with the goal of providing timely, usable, and comprehensive analyses to advance the policy process.

For FY 2007, the Treasurer will continue the efforts to focus on possible approaches to encourage American households to establish a relationship with a traditional financial institution and save for the future.

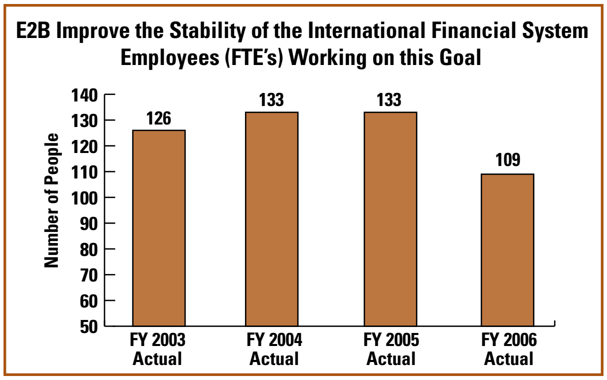
## *Improve the Stability of the International Financial System*

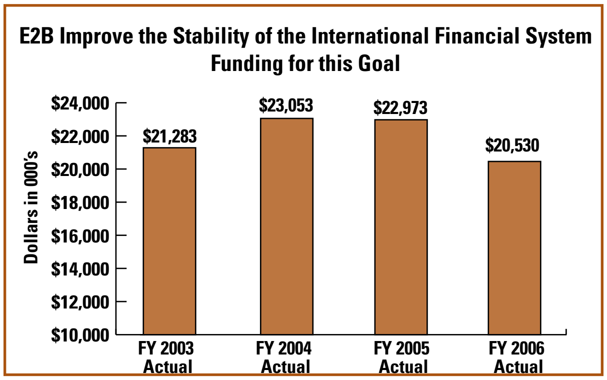
The Treasury Department plays an important role in the global economy, monitoring over 160 economies to ensure stability and transparency in the global marketplace. The Department works with foreign governments, financial institutions and international organizations to promote free and fair trade practices, target development assistance, identify global financial trends, and expand prosperity in the United States and around the world.

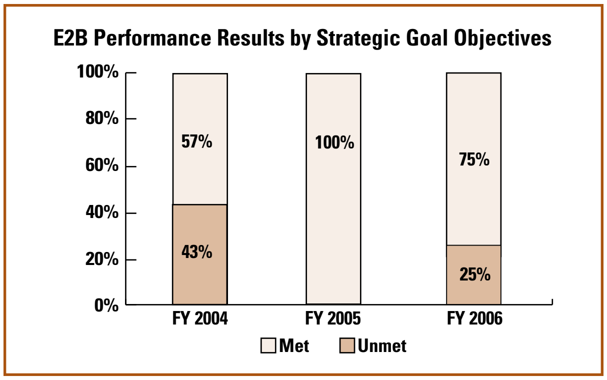
The Department seeks to stimulate international economic growth and job creation through the Office of International Affairs (IA) by working to open markets for increased trade and investment, encourage growth in developing countries, and promote responsible international debt, finance, and economic policies.

### Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $20.53 million with a workforce of 109 employees to improve the stability of the international financial system. The Department met 75 percent of its performance measures for this objective.



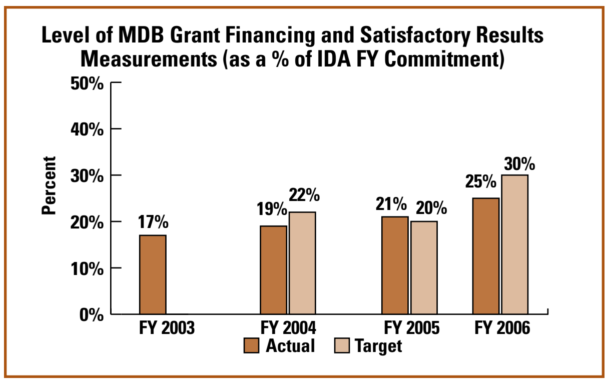
## Discussion and Analysis

***Promoting Free Trade and Budget Savings:*** The Treasury Department supports trade liberalization and budget discipline through its role in negotiating and implementing international agreements pertaining to official export subsidies. The Department secured agreements in the Organization for Economic Cooperation and Development (OECD) that reduced subsidies in export credits and tied aid flows valued at over $70 billion annually. These agreements open markets, level the playing field for U.S. exporters, and save the U.S. taxpayer about $800 million annually. Cumulative budget savings from these agreements are estimated at over $11 billion since 1991.

In addition, the Department, with the support of a Congressional mandate and using the G7 forum (United States, Canada, United Kingdom, Japan, France, Germany, and Italy) and the OECD, negotiated and reached an agreement to subject untied aid financing to new OECD rules. Under this agreement, bidding information for untied aid financed projects must now be publicly available in advance of bidding to facilitate effective competition by U.S. and other exporters. U.S. exporters could average as much as $1 billion of new capital goods export contracts annually at no cost to U.S. taxpayers; untied aid financing has averaged over $8 billion annually since 1993.

***G8-Broader Middle East and North Africa (BMENA) Initiative:*** Across the Middle East, countries lack the strong, well-regulated, efficient financial systems that allocate resources to productive activities which provide employment, goods, and services for a rapidly growing population. The multilateral G8 (U.S. Canada, United Kingdom, Japan, France, Germany, Italy, and Russia)-BMENA initiative addresses this deficiency by providing training, technical assistance, and policy advice. The Department's goal is to secure a more prosperous Middle East by influencing development of the financial sector, which will create jobs and opportunities for the region, and allow it to become an increasingly important U.S. trading partner.

***Egypt:*** The Treasury Department, in cooperation with the State Department and U.S. Agency for International Development, negotiated an agreement with the Government of Egypt to tie the disbursement of U.S. foreign assistance to Egypt's implementation of a series of reforms designed to modernize its financial sector. As a result, Egypt began the process of privatizing state-owned banks, resolving bad loans, and increasing the efficiency of the foreign exchange market. These reforms boosted investor confidence in Egypt and contributed to strengthening economic growth - up from 4.1 percent in 2004, to 5.7 percent in the first half of 2006. If maintained, this growth will boost job creation and help protect Egypt against economic shocks as it opens its markets.




***Brazil:*** From August 2005 through July 2006, Brazil's economy created 413,000 new jobs. During the Department's consultations with Brazil, in July 2006, discussions focused on the global outlook, the benefits of increased trade openness, strategies to increase investment in productive infrastructure, and policies promoting research and innovation.

***China:*** During FY2006, the Department of the Treasury continued to promote greater exchange rate flexibility, a more balanced economy, and the modernization of China's financial system. In addition to holding bilateral and multilateral discussions with the Chinese leadership, the Department established a permanent, full-time Financial Attaché office in Beijing to significantly bolster its engagement with China. The Department established a financial regulator Working Group with the Chinese to discuss key regulatory issues and held the first two meetings of this group. These efforts helped bring about Chinese President Hu Jintao's April 2006 public statement that, "China will continue to develop the foreign exchange market [and] increase the flexibility of the exchange rate." Between October 2005 and October 2006, the Renminbi (RMB) fluctuated between 8.092 and 7.8965 to the dollar and appreciated by 2.32 percent. In FY 2006, China introduced inter-bank foreign currency trading, reaching an agreement with the Chicago Mercantile Exchange to develop and trade currency futures allowing the RMB hedging, and undertook steps to further reduce capital flow restrictions.

***Multilateral Debt Relief Initiative (MDRI) for the Heavily Indebted Poor Countries (HIPC):*** In July 2006, President Bush and other G8 leaders endorsed MDRI debt relief for Heavily Indebted Poor Countries (HIPC). The Department of the Treasury developed and successfully negotiated the financial structure of an agreement which will result in 100 percent cancellation of debt obligations owed the International Development Association (IDA), African Development Fund (AfDF), and International Monetary Fund (IMF) by eligible countries. Under the agreement, 22 countries are currently eligible to receive $34 billion in relief, with an additional 16 countries eligible once they reach "Completion Point". Total relief provided is approximately $52 billion.

This unprecedented initiative will improve debt sustainability and balance of payments positions, contribute to economic growth and job creation, and end the destabilizing lend-and-forgive approach to development assistance. Furthermore, the removal of unsustainable debt combined with additional development resources, largely provided on grant terms, will deliver significant support for countries' efforts to reach their development goals.

***Afghanistan:*** The Department of the Treasury has taken a number of steps to support Afghanistan's economic growth and development. The Department worked closely with Afghanistan and its major creditors, particularly Russia, to provide significant debt relief. The Paris Clubs debt relief process will take a few years to complete, ultimately leaving Afghanistan with a much more sustainable foreign debt level. In addition, the Department provided Afghanistan important technical assistance on debt, banking, and financial enforcement issues, and assisted them with putting in place procedures that will help prevent their financial system from being used for illicit purposes. The Treasury Department works closely with the IMF, World Bank, and Asian Development Bank on programs to strengthen Afghanistan's economy.

***India:*** The Treasury Department's international efforts include ongoing dialogue with Indian financial sector officials to achieve further liberalization of India's economy. These efforts involved discussions with senior policy officials from regulatory agencies on both sides. Although India continues to gradually liberalize its economy by cutting tariff rates each year, the pace of liberalization should be accelerated to benefit India and the rest of the world. In addition, the Department continues working through bilateral and multilateral channels to assist India in strengthening its efforts to stop illicit financial flows.

***Southeast Asia:*** Collectively, the Southeast Asia region is now one of the most active trading partners of the United States. In FY 2006, to further enhance this important relationship, the Department provided aid in:

- Crafting the economic dimension of the United States-Association of Southeast Asian Nations (ASEAN) Enhanced Partnership. Under this partnership, the U.S. and the ten ASEAN countries negotiated a new Trade and Investment Framework Agreement.
- Promoting free flow of capital and goods in the region, and leading the financial services aspects

of free trade agreement negotiations with Thailand and Malaysia.

- Engaging in bilateral dialogue with Southeast Asian finance ministries and central banks to focus on fiscal responsibility, currency flexibility, financial sector modernization, infrastructure development, regional financial arrangements (such as the Chiang Mai swap arrangements), and preparation for a possible avian influenza pandemic.
- Working with Southeast Asia countries to stop illicit financial flow and develop stronger domestic controls through bilateral engagement and multilateral forums like the Asia-Pacific Group on Money Laundering.

***Jordan:*** In FY 2006, the United States provided Jordan with almost $297.5 million in Economic Support Fund (ESF) assistance. The goal is for Jordan to become economically self-sufficient and no longer dependent on United States' assistance. The Treasury Department worked closely with Jordanian financial authorities providing policy advice and support. The Department continued to press Jordanian authorities for the removal of inefficient and costly fuel subsidies which has become an enormous drain on the government's resources. With Jordan's implementation of fuel price increases, the final stage scheduled for March 2007, combined with fiscal discipline, will foster economic stability while supporting continued private sector job growth, and allow for a reduction in U.S. foreign aid as the Jordanian economy adjusts to these various shocks.

***Iraq:*** One of the United States' primary goals in Iraq is to help the newly established unity government function effectively, while rebuilding its security infrastructure. Once accomplished, the U.S. can reduce its presence by shifting responsibility to the Iraqi Government.

Real success can only happen with a rejuvenated Iraqi economy, and meaningful employment opportunities will help restore a flourishing middle class and weakening support for insurgents and militias. A credible, sustainable budget is the first step in Iraq's return to the international financial system. A restored oil sector will provide Iraq with the resources to finance its own reconstruction and security. The Department's staff works closely with Iraqi officials providing policy advice and assistance. Key to this effort is the Treasury Department's Financial Attaché in Baghdad, who serves as the head of the Fiscal and Financial Affairs Office of the Iraq Reconstruction Management Office, and supervises the Deputy Financial Attaché.

In FY2006, the Department helped Iraq secure the second portion of an historic debt reduction deal under the Paris Club, negotiate a Stand-by Arrangement with the IMF following the successful conclusion of an Emergency Post-Conflict Assistance program, and strengthen financial management and budget execution capabilities. In addition, the Treasury Department began leading U.S. outreach to negotiate an international agreement, through which Iraq will commit to a series of economic, political, and security reforms, and in exchange, receive increased donor support.

***Turkey:*** The Department continued to work closely with Turkish authorities to support an extremely successful economic stability program. Turkey has a large, fast-growing economy with a major emerging market, and its economic stability is critical to the United States' interests in the region. Its stability is also important to the financial health of the International Monetary Fund (IMF), as Turkey is the IMF's debtor. In FY 2006, Turkey's economy was strong enough to weather sharp currency depreciation; validation of its stability is demonstrated through Turkey's formal negotiations to join the European Union (EU).

***Encouraging Small Business Growth in Eurasia:*** Established in 2000, the Small and Medium Enterprise (SME) Fund leverages capital from the European Bank for Reconstruction and Development (EBRD) to lend to SMEs through local banking systems in 15 Southeast European and former Eastern Bloc countries. As in the U.S., SMEs generate the bulk of growth and job creation. As of July 2006, more than 1.1 million loans were provided to entrepreneurs and the total loan volume exceeded $7.7 billion with a total U.S. share of contributions as $39.1 million. Each $1 of U.S. funding leverages $199 of new lending.

### Moving Forward

The Treasury Department will continue to study, recommend, and support Administration policy initiatives which strengthen the U.S. economy, create more jobs for Americans, and enhance citizens' economic security. The Department will actively work to improve the U.S. pension system, reform social security, and improve the federal income tax system.

In FY 2007, the Department will continue measuring IMF programs to ensure efficiency and effectiveness while striving to meet performance targets. Last year was the first year IMF programs were measured and the targets were not met.

In addition, the Department of the Treasury will continue to support the broader Middle East and North Africa to build strong, well regulated, and efficient financial systems, which allocate resources to productive activities that provide employment, goods, and services for rapidly growing populations. The Department will continue dialogue with China, including through the U.S. – China Strategic Economic Dialogue that is co-chaired by Secretary Paulson, to address global and current account trade imbalances, and increase exchange rate flexibility.

# F Managing the U.S. Government's Finances Effectively

| Strategic Goals | Strategic Objectives |
|---|---|
| Preserve the Integrity of Financial Systems | Disrupt and Dismantle Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate Their Support Networks |
| | Execute the Nation's Financial Sanctions Policies |
| | Increase the Reliability of the U.S. Financial System |
| Manage the U.S. Government's Finances Effectively | Collect Federal Revenue When Due, Through a Fair and Uniform Application of the Law |
| | Manage Federal Debt Effectively and Efficiently |
| | Make Collections and Payments on Time and Accurately, Optimizing Use of Electronic Mechanisms |
| | Optimize Cash Management and Effectively Administer the Government's Financial Systems |

## Preserving the Integrity of Financial Systems

### *Disrupt and Dismantle Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate Their Support Networks*

### *Execute the Nation's Financial Sanctions Policies*

The Treasury Department's Office of Terrorism and Financial Intelligence (TFI) is a key player in the Government's efforts to track and cut off the flow of funds to terrorists and other national security threats. Created in 2004, TFI marshals all of the Department's intelligence and enforcement functions with the twin aim of safeguarding the financial system against illicit use, and combating rogue nations, terrorist facilitators, weapons of mass destruction (WMD) proliferators, money launderers, drug kingpins, and other national security threats.

In strong partnership with the Departments of Justice, State, and Homeland Security, as well as the Intelligence Community, TFI utilizes a range of financial authorities to prevent the flow of funds to terrorist organizations, WMD proliferators, narcotic traffickers and other threats. These efforts are beginning to yield encouraging results. For example, this partnership had success impeding access to funds and the financial system by terrorist groups such as al Qaida and Hamas. In addition, TFI, working with the international community, was successful limiting North Korea's ability to abuse the global financial system to support its proliferation and illicit activities.

TFI unifies leadership for the functions of:

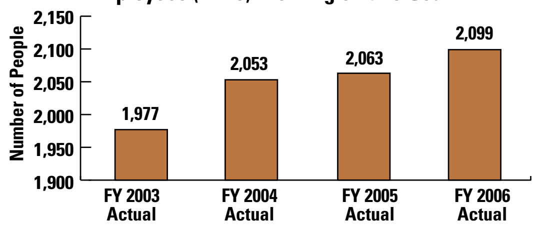
- The Office of Intelligence and Analysis (OIA)
- The Office of Terrorist Financing and Financial Crimes (TFFC)
- The Financial Crimes Enforcement Network (FinCEN)
- The Office of Foreign Assets Control (OFAC)
- Internal Revenue Service – Criminal Investigation Division (IRS-CI)
- The Treasury Executive Office for Asset Forfeiture (TEOAF)

The Department's range of activities against national security threats include: (1) intelligence analysis on the financial and other support networks for terrorist groups, WMD proliferators, and other serious national security threats, (2) promoting international cooperation to attack the financial underpinnings of national security threats, (3) improving the transparency and safeguards of financial systems, and (4) targeting and sanctioning supporters of terrorism, proliferators of weapons of mass destruction, narcotics traffickers and other threats.

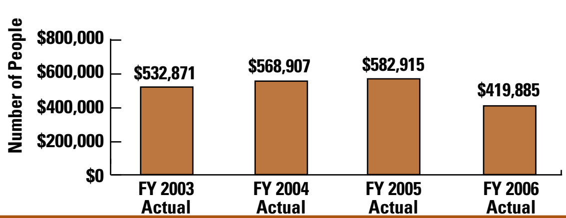
### Performance Summary and Resources Invested

In FY 2006, the Department of the Treasury spent $419.88 million with a workforce of 2,099 employees to fight the financial war on terror. The Treasury Department met 20 percent of its targets for this objective, did not meet 27 percent and designated 7 percent as baseline to assess the data and set appropriate targets for next year; and 46 percent were unavailable due to revisions or discontinuance of the measures.

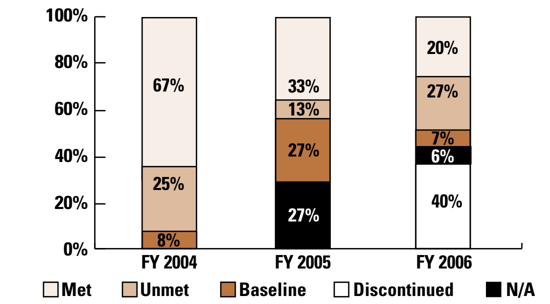
**F3A and F3B Disrupt and Dismantle the Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate their Support Networks and Execute the Nations Financial Sanctions Policies**
**Employees (FTE's) Working on this Goal**




**F3A and F3B Disrupt and Dismantle the Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate their Support Networks and Execute the Nations Financial Sanctions Policies**
**Funding for these Goals**




**F3A & F3B Performance Results by Strategic Objectives**




### Discussion and Analysis

***Developing an Increased Role in the Intelligence Community:*** TFI's policy actions to combat the financial and other support networks for terrorist groups, WMD proliferators, and other key national security threats are driven by the analytic efforts of the Office of Intelligence and Analysis (OIA). In 2004, Congress created the OIA, TFI's in-house intelligence component, to improve the Department's intelligence and analytic capabilities. OIA's responsibilities include the receipt, analysis, collation, and dissemination of foreign intelligence and foreign counterintelligence information related to the operation and responsibilities of the Department of the Treasury.

Their mission is to support the formulation of policy and execution of the Department authorities by providing:

- Expert analysis and intelligence production on financial and other support networks for terrorist groups, proliferators, and other key national security threats
- Timely, accurate, and focused intelligence support on the full range of economic, political, and security issues

In 2005, OIA began weekly meetings to review potential targets, assess the full range of possibilities, and assign follow-up action. Intelligence information and analyses are incorporated into all aspects of policy deliberations.

Through OIA, TFI is better integrated into the intelligence community. OIA analysts work closely with their intelligence community counterparts, and have begun to collaborate more frequently on intelligence analytic products. In addition, OIA hired a Requirements Officer, in 2005, who is focused on working with the U.S. Intelligence Community to tailor its intelligence collection specifically to the Department's needs. In FY 2006, the Treasury Department played a lead role in the Baghdad-based Iraq Threat Finance Cell (ITFC), an inter-agency effort to enhance the collection, analysis, and dissemination of intelligence to combat the Iraqi insurgency. OIA analysts served at the ITFC on a rotational basis.

TFI components are involved in:

- Freezing the assets of terrorists, proliferators, drug kingpins and support networks
- Cutting off corrupt foreign jurisdictions and financial institutions from the U.S. financial system
- Tracing and repatriating assets looted by corrupt foreign officials
- Promoting a meaningful exchange of information with the private financial sector to help detect and address threats to the financial system.

***Enforcing Sanctions:*** The Office of Foreign Assets Control (OFAC) administers and enforces economic and trade sanctions against targeted foreign countries, terrorists, international narcotics traffickers and those engaged in activities related to the proliferation of WMD. OFAC acts under the President's wartime and national emergency powers, and under authority granted by specific legislation, to impose controls on transactions and assets subject to U.S. jurisdiction. Many of the sanctions are based on United Nations and other international mandates, are multilateral in scope, and involve close cooperation with allied governments.

In FY 2006, OFAC, in support of U.S. policy objectives, pursued designations of entities engaged in the proliferation of WMD, continued its efforts to expose terrorist networks, and built on its success of dismantling networks associated with drug cartels. In addition, OFAC worked closely with the Departments of State and Justice to help establish and identify targets for four new sanction programs, which include Sudan's Darfur region, Côte d'Ivoire, Belarus, and the Democratic Republic of Congo.

Underscoring the importance of complying with sanctions, in December 2005, OFAC and the Federal Reserve Board, jointly, assessed total monetary penalties of $80 million against ABN-AMRO, a large Dutch bank with U.S. operations, in connection with violations of the Iran and Libya sanction programs.

***Implementing Tools to Prevent the Spread of Weapons of Mass Destruction:*** OFAC, under TFI's leadership, plays a significant role in disrupting and dismantling proliferators of WMD. In FY 2006, OFAC continued to implement Executive Order 13382, Blocking Property of Weapons of Mass Destruction Proliferators and Their Supporters. OIA provided vital intelligence support to OFAC in this critical area. Executive Order 13382 enables the Treasury and State Departments to designate WMD proliferators and their supporters, freezing their U.S. assets and prohibiting U.S. persons from doing business with them. In the last year, OFAC designated 19 proliferation entities and one individual.

Notable targets designated in FY 2006, under the WMD program, included Iranian and Chinese companies that supplied Iran's military and Iranian proliferators with missile-related and dual-use components; and a Swiss company that acted as a technology broker for North Korean military goods with weapons-related applications.

TFI works closely with its international partners to encourage other countries to develop authorities similar to Executive Order 13382. Aggressive outreach strategy is occurring bilaterally, as well as through international organizations and activities, such as the Proliferation Security Initiative (PSI) and the G7. Both of these groups released high level statements this year referencing the importance in combating proliferation financing.

***Denying Terrorists' Access to Funds:*** Combating terrorism continued to be a top priority for all TFI components. Supported by information gathered and prepared by OIA, OFAC's actions continued to expose the financial networks of terrorist groups including al Qaida, Hizballah, Hamas, Jemaah Islamiyah, and the GSPC (Salafist Group for Preaching and Combat), and designated financiers and companies in Southeast Asia, the Persian Gulf, the Horn of Africa, South America's Tri-Border Area, Europe, and the United States. Recent targets included:

- Two overseas branches of the International Islamic Relief Organization (IIRO), which is headquartered in Saudi Arabia, as well as Abd al Hamid Sulaiman Al-Mujil, the head of IIRO's branch in the Eastern Province of Saudi Arabia. These branch offices, while holding themselves out as purely charitable organizations, were bankrolling the al Qaida network in Southeast Asia
- Several individuals and entities known for their role in financing the Libyan Islamic Fighting Group, an al Qaida affiliate
- Four top leaders of the al Qaida linked to Southeast Asian Terrorist Organization "Jemaah Islamiyah."

Ongoing efforts to disrupt Hizballah's financial network were highlighted by a regulatory action, taken by OFAC, to cut off Iran's Bank Saderat from even indirect access to the U.S. financial system. Bank Saderat was a significant facilitator of Hizballah's financial activities and served as a conduit between the Government of Iran and a range of terrorist groups, including Hizballah, Hamas, the Popular Front for the Liberation of Palestine-General Command (PFLP-GC), and the Palestinian Islamic Jihad (PIJ). Other designation actions directed at Hizballah included:

- The Islamic Resistance Support Organization (ISRO), a so-called "charity" operated by Hizballah;
- Bayt al-Mal and the associated Yousser Company, which together functioned as Hizballah's unofficial treasury, holding and investing its assets and serving as intermediaries between Hizballah and the mainstream banks.

In addition to designations, TFI develops and implements domestic and international policies, strategies, and initiatives to identify and address vulnerabilities in the U.S. and international financial system.

***Countering Money Laundering:*** The Department of the Treasury continues to promote anti-money laundering as a key to attacking terrorist financing and criminal activity, including narcotics trafficking, white-collar crime, organized crime, and public corruption. Resources devoted to fighting money laundering and financial crimes reap benefits beyond addressing the financial crimes they directly target. Financial investigations expose the infrastructure of criminal organizations. They provide investigators a roadmap to the activities of those who would facilitate criminal activity; lead to the recovery and forfeiture of illegally obtained assets; and create broad deterrence against criminal activity.

International cooperation is a critical element in this fight. The Treasury Department leads the U.S. delegation to the Financial Action Task Force (FATF), the international standard setting body charged with safeguarding the global financial system against money laundering and terrorist financing. In FY 2006, as a member of the FATF, the Department:

- Actively participated in and led numerous FATF initiatives, including efforts to strengthen international counter terrorist financing standards

- Influenced the creation of an initiative within the FATF to strengthen the world's defenses of counter-terrorist financing
- Coordinated the adoption of a new international standard through the FATF, *Special Recommendation IX*, calling on governments to establish regimes to address cross border movement of illicit currency and bearer negotiable instruments
- Coordinated research and published the FATF typologies Report on "Money Laundering and Terrorist Financing Trends and Indicators;"
- Responded to Questionnaires and defended the U.S. position in face-to-face meetings with FATF Assessors
- Collaborated with the Department of Homeland Security's Immigration and Customs Enforcement (ICE) to produce a comprehensive report on trade-based money laundering

In addition, TFFC worked closely with representatives from 16 federal bureaus and offices across law enforcement, regulatory, and policy communities to produce the U.S. Government's first-ever Money Laundering Threat Assessment report. For this assessment, the working group used arrest and forfeiture statistics, case studies, regulatory filings, private sector and government reports, and field observations. The report analyzes more than a dozen money laundering methods and serves as a first step in a government-wide process to develop strategies to counteract vulnerabilities identified.

***Safeguarding the nation's financial system through administration of the Bank Secrecy Act (BSA) and analysis, collection and dissemination of BSA information:*** TFI, through the Financial Crimes Enforcement Network (FinCEN), effectively administers and enforces the Bank Secrecy Act (BSA), another important weapon in combating money laundering and illicit finance. The BSA requires financial institutions to make reports of suspicious activities available to law enforcement, keep records, and establish appropriate internal controls to guard against financial crime. As administrator of the BSA, FinCEN oversees and coordinates the sharing of financial intelligence and analysis with its law enforcement and regulatory partners.

FinCEN works closely with its regulatory partners to take action against institutions that violate the compliance and enforcement provisions of the BSA; an example of an action taken includes the imposition of stiff monetary penalties as appropriate. Timely enforcement action communicates urgency to financial institutions, and is paramount to deterring noncompliance. In FY 2006, FinCEN met their target measure of 1.0 years average time to process cases. The year-to-date actual result of 1.0 years reflects effective use of resources.

By the close of FY 2006, FinCEN had executed memoranda of understanding (MOU) governing the exchange of information with 48 federal and state regulatory agencies, surpassing its projected target of 45. These agreements provide a solid foundation for FinCEN to improve upon its ability to monitor industry compliance by providing vital data on various industry segments. FinCEN will be in a position to extend the reach of its compliance efforts even further as it completes MOUs with additional agencies and increases the resources available to make effective use of the data.

In addition, FinCEN provides authorized law enforcement, regulatory and intelligence agencies direct access to BSA data. Several of FinCEN's ongoing efforts will continue to improve its systems for analyzing and disseminating information. During FY 2006, FinCEN, in partnership with the IRS, provided its partners access to BSA data through the WebCBRS system, a new, easier to use web-based interface, through which BSA data can be accessed. FinCEN also conducted a baseline survey of their users of the BSA Direct E-Filing system to determine overall satisfaction level and identify where improvements are needed. In FY 2006, 92 percent of respondents were satisfied with the BSA Direct E-Filing system.

FinCEN supports law enforcement and its regulatory industry partners by facilitating information sharing and providing analyses of BSA data. In FY 2006, a survey of FinCEN's customers found that 69 percent rated FinCEN's analytic products as valuable, not meeting its annual target. FinCEN's original target of 75 percent respondents rating their analytic product as valuable, was established in FY 2005, and based on one year of data. This measure is currently being revised through the FY 2006 Program Assessment Rating Tool (PART) process.

FinCEN issues regulations and guidance for implementing and integrating BSA compliance programs within different segments of the financial services industry. In FY 2006, FinCEN issued the following proposed and final rulings:

- Requiring financial institutions doing business with foreign entities to implement appropriate due diligence policies, procedures, and controls with correspondent accounts established or maintained for certain foreign financial institutions, in accordance with Section 312 of the USA PATRIOT Act
- Requiring mutual funds to report suspicious activity
- Requiring certain insurance companies to establish anti-money laundering programs and report suspicious activity
- Proposing special measures against foreign financial institutions deemed to be of primary money laundering concern, in accordance with Section 311 of the USA PATRIOT Act

FinCEN enhanced its outreach program by increasing the amount of written guidance provided to the regulated industries concerning Bank Secrecy Act compliance.

FinCEN continued to support anti-money laundering policy initiatives and investigations at the federal and state level by producing advanced BSA data analyses tailored to law enforcement and other partner agencies needs. Examples of the analytical products that were valuable to FinCEN's customers include:

- Three assessments, using the analysis of all BSA reports, identified potential money laundering hotspots and significant changes in financial activity. The report helped federal and state authorities to allocate drug and cash interdiction resources along the southwest border. The recipients of these reports were the Texas Department of Public Safety, the Arizona Attorney General's office, the El Paso Intelligence Center, the Office of National Drug Control Policy and the National Drug Intelligence Center
- An assessment of vulnerabilities in the limited liability corporation (LLC) structure and formation process, which could be exploited by illicit international transactions, formed the basis for FinCEN recommendations to increase regulation of state business incorporation practices, and contributed to coordination among federal agencies investigating abuse of LLCs

FinCEN, as the financial intelligence unit (FIU) for the United States, plays a leadership role in Egmont Group, a cooperative network of 101 FIUs from around the globe. In FY 2006, FinCEN supported cooperative efforts to combat money-laundering, terrorist financing and other financial crimes by:

- Enhancing reciprocal international sharing of financial intelligence information
- Providing training to personnel from foreign FIUs
- Facilitating efficient and secure communication among FIUs through the Egmont Secure Web system
- Promoting the establishment or strengthening of FIUs in jurisdictions lacking one, and

assisting in the enhancement of anti-money laundering and counter-terrorist financing programs within existing FIUs

FinCEN led international efforts by hosting a meeting to counter terrorist financing activities in the tri-border area of Argentina, Brazil, and Paraguay. The FIUs from these three countries and the United States, known as the 3 + 1 Group, compared data, examined common trends and developed strategies to address the situation.

***Supporting Criminal Investigations:*** In addition to ensuring taxpayers comply with tax laws, Internal Revenue Service (IRS) enforcement actions contribute to national security. Terrorists and their supporters use the cover of humanitarian, religious, or charitable work performed by tax-exempt non-profit organizations to raise funds. Funding also comes from more conventional criminal activities, such as property theft, insurance fraud, smuggling, and narcotics trafficking. Some of these terrorist activities occur within the United States and adversely impact tax administration, uniquely positioning the IRS to fight such abuses. TFI provides policy guidance to the IRS' Criminal Investigation Division (CI) in such cases. The IRS works closely with TFI and OFAC to investigate and freeze accounts controlled by individuals and alleged charitable organizations suspected of moving funds used to support terrorism.

The IRS provides financial investigation expertise to the FBI's Joint Terrorism Task Force and the U.S. Attorneys' Anti-Terrorism Advisory Council, as well as IRS-CI supports FinCEN by conducting BSA investigations, and provides a detailee to OFAC.

During FY 2006, IRS' CI had:

- 212 terrorism related investigations, a 31 percent increase over FY 2005
- 52 terrorism cases were recommended for prosecution, resulting in 44 indictments
- Over 34 percent of the prosecution recommendations included tax violations; CI maintained a conviction rate of 92 percent in these cases

***Outreach to the International Banking Community:*** In accordance with its international private sector outreach strategy, TFI initiated private sector anti-money laundering/counter terror-finance (AML/CFT) dialogues, linking the U.S. banking sector with those from the Middle East/North Africa (MENA) region and the Latin American region, to the support of relevant financial and regulatory authorities.

In collaboration with its interagency and regional partners, TFI successfully facilitated the launch of the U.S.-MENA Private Sector Dialogue on AML/CFT, through the initial AML/CFT Conference in Cairo, in March 2006. Bankers and financial and regulatory authorities, from the U.S. and the region, discussed a range of challenges associated with the development and implementation of effective AML/CFT jurisdictional and institutional measures. In June, TFI initiated a similar dialogue with the Latin American banking community, and hosted at the Department a roundtable discussion of U.S. and regional interests, to help frame this initiative.

***Outreach to the Charitable Sector:*** Outreach to the charitable sector represents a fundamental objective for the Department of the Treasury in its broader campaign to combat terrorist financing. The Department's ongoing engagement with the charitable community strives to protect charities from terrorist abuse and empower them to adopt and implement effective safeguards against terrorist exploitation.

At the close of the fiscal year, TFFC published, in December 2005, the revised version of its Anti-Terrorist Financing Guidelines: Best Practices for U.S.-Based Charities. In addition, the Treasury Department continued to provide information on the risks and typologies of terrorist abuse, such as those discussed in the Department's paper on risks associated with terrorist exploitation of post-earthquake relief efforts in Pakistan.

***Countering Narcotics:*** In FY 2006, TFI worked closely with law enforcement, bank regulators, and other appropriate parties to identify evolving trends in drug proceeds money-laundering, and then communicate these to the U.S. financial industry.

In addition, OFAC's Specialty Designated Narcotics Traffickers (SDNT) Program continued to see significant activity. OFAC targeted the North Valle drug cartel in four separate actions which resulted in the designation of 22 individuals and 29 companies. Designations under this program included individuals involved with managing a large Colombian department store chain on behalf of two previously designated leaders of the North Valle drug cartel. Shortly after these designations, Colombian authorities seized the department store chain, along with other companies and properties. These four actions also targeted companies in Colombia, the British Virgin Islands, Mexico, Panama, and the United States.

In September 2006, OFAC's success in exposing the two notorious Cali cartel leaders, Miguel and Gilbert Rodriguez Orejuela, culminated with guilty pleas. The Rodriguez Orejuela brothers not only admitted to over two decades of drug trafficking, but also confessed to laundering the proceeds through the network of companies that OFAC targeted in over a dozen investigations in the past decade. An agreement was reached for the forfeiture of $2.1 billion in assets levied against personal and business entities worldwide. These entities are comprised of the 246 front companies that were already designated by OFAC, in the last 11 years and under at least 12 separate OFAC designation actions.

The Kingpin program targets narcotics traffickers and money laundering organizations worldwide. In FY 2006, OFAC targeted groups in Southeast Asia, Mexico, and Colombia, designating several individuals and companies that are part of the network of previously designated Wei Hsueh-kang and the United Wa State Army (UWSA); the UWSA is the largest and most powerful drug trafficking organization in Southeast Asia. In FY 2006, OFAC designated 21 individuals and 19 companies from Mexico, to include money service businesses, which form part of the Arellano Felix Organization (AFO); and five individuals of the Arriola Marquez Organization (AMO). In addition, OFAC used the Kingpin program to target the FARC, a Colombian rebel group known by its Spanish acronym, which is heavily involved in narcotics trafficking activities. OFAC designated nine FARC leaders, including the organization's international representative.

### Moving Forward

Although the Treasury Department is making progress in combating financing of terrorists and other national security threats, quantifying these results is challenging. Given the clandestine nature of the activities of terrorists and proliferators of weapons of mass destruction, it is impossible to estimate what portion of the money intended for their support was blocked, and the Department relied on proxy indicators to estimate the effectiveness of its actions; more refined measures to assess performance will be implemented in the future.

In FY 2007, TFI will continue to work to further safeguard the financial system by enhancing its abilities to isolate, disrupt and dismantle the financial infrastructure of national security threats, such as terrorists, proliferators of weapons of mass destruction, narcotics traffickers, and other criminals. In addition, TFI plans to:

- Continue to develop and expand intelligence analytic capabilities, policy strategies, and enforcement efforts to combat the financial support networks for terrorist groups, WMD proliferators, and other key national security threats

- Cover and address the most pressing and emerging national security issues in support of senior leadership and policymakers
- Continue efforts to establish the Department as a fully integrated member of the IC (OIA)
- Monitor, update and extend existing designations to counter the evasive tactics of Specifically Designated Global Terrorists and their support networks (OIA, OFAC)
- Monitor, update and extend existing designations to counter the evasive tactics of proliferators of weapons of mass destruction (OFAC, OIA)
- Continue to build OIA as a center of analytic expertise on the financial and other support networks for terrorists groups, WMD proliferators and other key national security threats (OIA)
- Continue to work with foreign governments and international organizations to encourage the development in other countries of authorities to identify, track, and freeze proliferators' assets (TFFC, OFAC)
- Continue to engage in outreach and develop guidance to the charitable community about appropriate protective measures against terrorist abuse (TFFC)
- Discuss in the FATF how existing AML/CFT international standards should be supplemented, amended, or applied to address the vulnerabilities associated with trade-based money laundering (TFFC)
- Organize a follow-up conference for the US-MENA private sector dialogue in December 2006, and an AML/CFT conference in the Latin American region for early 2007 (TFFC)
- Increase global capacity in AML/CFT efforts by continuing bilateral and multilateral engagements with international partners (TFFC, OFAC, FinCEN)
- Improve outreach to state governments and financial industries newly covered by BSA regulations (FinCEN)
- Strengthen oversight and compliance examination (FinCEN)
- Continue to revise anti-money laundering regulations (FinCEN)
- Continue major enforcement actions for systemic non-compliance of BSA requirements (FinCEN)
- Improve coordination with other agencies to identify and educate unregistered money services businesses (FinCEN)
- Use advanced analytical tools to improve geographic and industry threat assessments (FinCEN)
- Continue facilitating efficient and secure communication among FIUs through the Egmont Secure Web application (FinCEN)
- Improve outreach to U.S. law enforcement and regulatory agencies on the benefits of connecting to the Egmont Group's global network of FIUs (FinCEN)
- Upgrade information technology to improve retrieval and sharing of BSA data with a growing user population (FinCEN)
- Use BSA data analysis to identify regulatory issues within the financial industries (FinCEN)
- Evaluate reducing the current $3,000 recordkeeping and travel rule threshold (FinCEN)
- Collaborate with the Electronic Payments Association regarding automated clearinghouse wire transfer information (FinCEN, OFAC)
- Collaborate with law enforcement, federal banking agencies and industry to address potential abuse of cover payments (FinCEN, OFAC)

### *Increase the Reliability of the U.S. Financial Systems*

The Department of the Treasury ensures the U.S. financial system's reliability and security through the production of the nation's coins and currency and supervision of national banks and savings associations. Two bureaus share the responsibility of producing the world's most accepted coins and currency. The United States Mint manufactures circulating coinage and popular numismatic products; the Bureau of Engraving and Printing (BEP) designs next generation currency to guard against counterfeiting and manufactures the nation's paper currency. The Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) promote the increased reliability of the U.S. financial system by supervising national banks, savings associations, and savings and loan holding companies, thereby ensuring adherence to applicable laws, rules, and regulations and providing a safe and sound financial system.

In FY 2006, the Mint and BEP:

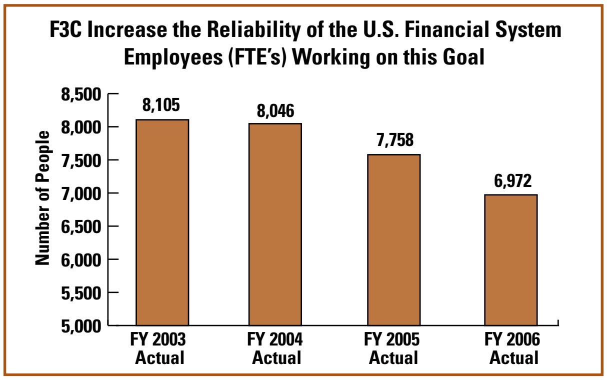
- Produced 16.2 billion coins – 2 billion more than FY 2005
- Produced 8.2 billion paper currency notes – 400 million less than FY 2005
- Reduced currency production costs by $1.34 per one thousand notes delivered

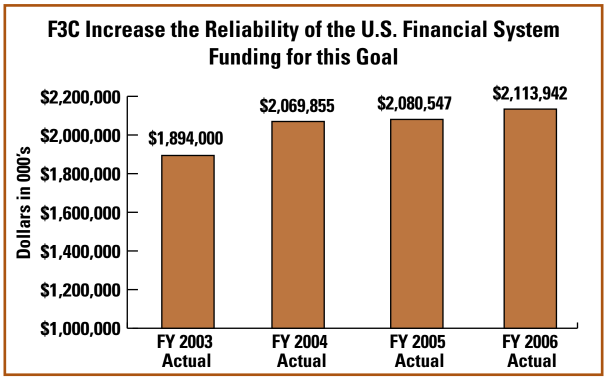
The OCC and OTS:

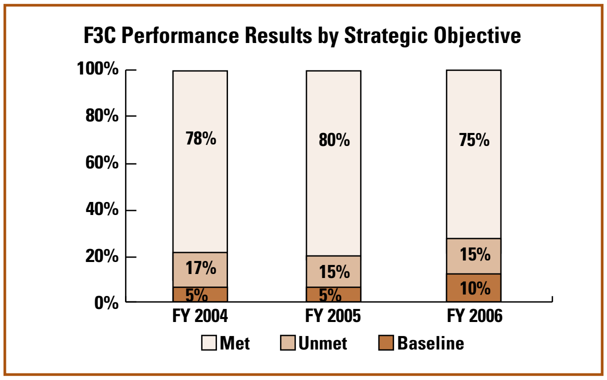
- Supervised 1,852 institutions with national bank charters and 49 federal branches, with assets totaling approximately $6.5 trillion.
- Supervised 854 savings associations with $1.53 trillion in total assets and 480 holding company enterprises with approximately $7.5 trillion in consolidated assets

### Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $2.113 billion with a workforce of 6,972 employees to sustain reliable financial systems. The Department met 75 percent of its performance measures for this objective, did not meet 15 percent and designated the remaining 10 percent as baseline to assess the data and set appropriate targets for next year.



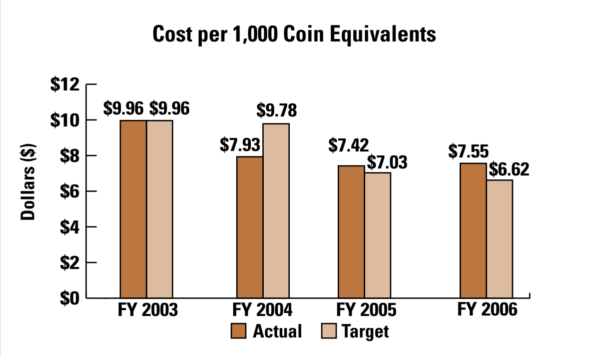



## Discussion and Analysis

The Mint and BEP streamlined processes and utilized technology to produce the nation's coin and currency at significant cost savings providing additional value to the American people.

***Producing Coins:*** In FY 2006, the Mint had revenue and other financing sources of $2.3 billion, a 31 percent increase from $1.7 billion in FY 2005. These results reflect an increase in demand for both circulating and numismatic products. The Mint returned $750 million to the Treasury General Fund as a result of operations, compared to $775 million in FY 2005. Despite an increase in demand, this reduction in funds returned was due primarily to much higher costs for metal used to fabricate coins.

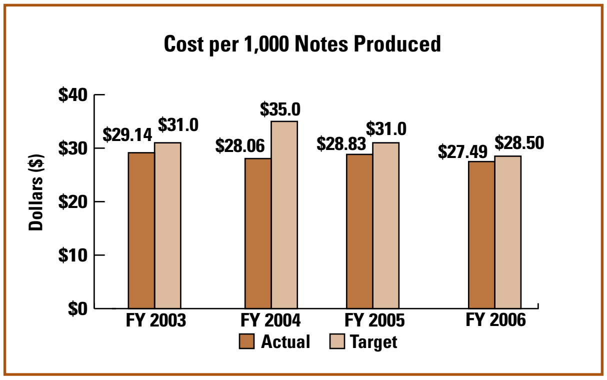
The cost per 1,000 coin equivalents increased two percent to $7.55 in FY 2006, from $7.42 in FY 2005, missing the very aggressive target of $6.62. The increase in conversion cost was the result of rising energy costs, replenishment of shipping and packaging supplies, overtime to support new numismatic products, and an increase in depreciation expense. Cycle time increased slightly from 69 days, in 2005, to 72 days, in 2006, having no effect on the overall program or activity performance. Rising metal prices had a significant impact on production cost, causing the penny and the nickel to cost more than their face value. The Mint is working with Congress to evaluate alternative materials and other opportunities to reduce production cost.




The Mint's numismatic and bullion sales increased from $588.2 million in FY 2005, to $1.03 billion in FY 2006. Particularly noteworthy was the introduction of the first ever U.S. Government issued 24-karat gold coin.

***Producing Currency:*** In FY 2006, BEP streamlined its operations to reduce the cost of producing notes. BEP uses two performance measures to assess production and delivery efficiency: manufacturing costs per 1,000 notes produced and security costs per 1,000 notes delivered.

Cost per 1,000 notes produced decreased from $28.83, in FY 2005, to $27.49, in FY 2006; and security cost were favorable at $6.00 per thousand notes produced against a performance target of $6.25 per thousand notes delivered. In FY 2006, the currency program was completed below standard costs.



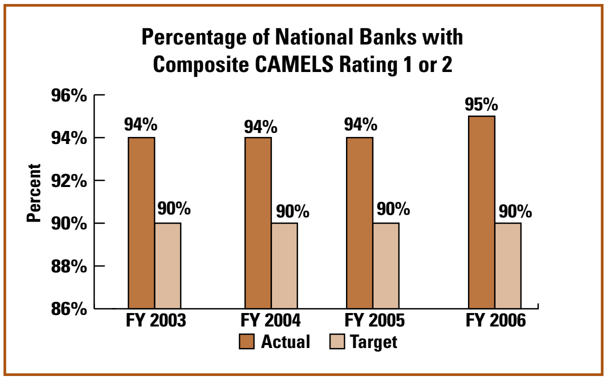

BEP's currency production program specifically addresses the nation's need for counterfeit-deterrent currency by applying the latest technologies in security printing and processing. In FY 2006, the Treasury Department introduced the redesigned $10 note which followed successful introductions of the redesigned $20 and $50 notes in 2003 and 2004, respectively. Redesign of the $5 and $100 notes is scheduled for circulation in 2008 and 2009. The new notes are part of the current multi-year initiative which implemented the most ambitious currency redesign in U.S. history. Due to BEP's consistent automated inspection equipment, more than 99 percent of all notes delivered to the Federal Reserve met or exceeded exacting quality standards.

Analysis and reporting of production and cost data gives managers feedback used to fine-tune production processes. For example, currency shipment discrepancies are prevented by a series of automated quality and accountability checks performed throughout the entire production process, as well a final verification prior to shipment.

***Regulating National Banks and Savings Associations:*** The Treasury Department continually enhances the reliability of the U.S. financial system by administering supervision programs over national bank and saving associations to ensure that the industry operates in a manner consistent with safety and soundness principles, and complies with applicable laws, rules, and regulations.

The Department of the Treasury, through the Office of the Comptroller of the Currency (OCC), supervised 1,852 institutions with national bank charters and 49 federal branches, with assets totaling approximately $6.5 trillion. OCC supervision ensures the safe and sound operation of the national banking system. In FY 2006, 99 percent of all national banks were well capitalized relative to their risks. OCC examiners concluded that 95 percent of national banks earned the highest composite ratings of 1 or 2 according to standard evaluation methods. These evaluations assess capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk (CAMELS). In FY 2006, those national banks, which had problems in the prior year, 46 percent improved their composite CAMELS rating to either 1 or 2.

To ensure fair access and treatment for all bank customers, banks are evaluated on compliance with consumer protection laws and regulations. In FY 2006, 94 percent of national banks earned the highest consumer compliance ratings of 1 or 2, thereby meeting the FY 2006 target.




In FY 2006, the OCC implemented a new efficiency measure, OCC costs relative to every $100,000 in bank assets regulated. The baseline for this year is $8.84 and the OCC is in the process of establishing future targets.

Bank Secrecy Act (BSA) supervision remained a high priority for OCC in FY 2006. The OIG identified industry compliance of BSA as a significant challenge. To address this, comprehensive initiatives to strengthen BSA and AML compliance were implemented. Highlights include:

- Completed 90 percent of compliance reviews of non-high risk community banks and mid-size banks, in accordance with the USA PATRIOT Act
- Developed national pool of BSA examiners who have attained Anti-Money Laundering (AML) Specialist certification
- Delivered BSA training to Large Bank Examiners-in-Charge and compliance specialists
- Increased the number of AML training sites from 4 in 2005, to 8 in 2006

In FY 2006, the FFIEC released the revised BSA/AML Examination Manual, reflecting an ongoing commitment of federal banking agencies and FinCEN, to provide current and consistent guidance, and safeguard operations from money laundering and terrorist financing. The update further clarifies supervisory expectations and incorporates regulatory changes since the previous year's release; revisions to the manual were a collaborative effort of the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, OCC, OTS and FinCEN. The Conference of State Bank Supervisors served in a consultative role while OFAC collaborated on revisions to the section that addresses compliance with regulations they enforce.

The Treasury Department, through OTS, supervises savings associations and their holding companies to ensure compliance with consumer laws, and encourage a competitive industry. The OTS regulated 854 savings associations with total assets of $1.53 trillion. These savings associations operated in a manner consistent with safety and soundness, and with 93 percent achieving an overall composite CAMELS rating of 1 or 2. The industry's capital position remains strong with over 99 percent of savings associations meeting the well-capitalized standards. The OTS regulates 480 holding company enterprises with approximately $7.5 trillion in consolidated assets. Over half of all savings associations and 79 percent of total savings association assets are owned by OTS-regulated holding companies. From January 2005 through June 2006, OTS conducted 1,069 BSA examinations, initiating 37 enforcement actions to address significant violations of applicable laws and regulations.

In FY 2006, the OTS hosted an outreach event for the industry on BSA/AML compliance issues, providing informative briefings by OTS senior staff on topics of BSA/AML best practices, avoiding common violations, and the consequences of noncompliance. This event provided a valuable opportunity for over 1,400 compliance officers, risk managers, auditors, attorneys and senior bank and thrift managers to interact directly with OTS experts.

In FY 2006, 63 percent of thrifts had assets of less than $250 million and as community-based lenders, the majority of savings associations' loans are made to consumers. Direct loans to consumers make up 62 percent of aggregate savings association assets. Savings associations' asset quality is strong, but quality is dependent on stable real estate values, a favorable employment environment, and consumers' continued ability to service debt. OTS maintains an interest rate risk sensitivity model that evaluates potential exposure to changing interest rates. OTS remains cautious of the potential impact of a rapid increase in market interest rates and real estate market volatility that could affect the safety and soundness of the industry and have a profound economic impact.

The federal banking agencies are continuing efforts to implement the international Basel II risk-based capital framework. The OTS is supportive of the Basel IA efforts to increase risk sensitivity in the existing Basel I capital rules and to mitigate competitive inequities that may arise with the implementation of Basel II. The OTS believes that Basel II warrants close scrutiny and refinement as the process continues. OTS is a leader among the four Federal banking agencies in developing capital modifications to Basel I for the considerable majority of financial institutions that will not adopt Basel II. Domestically, OCC and OTS, along with the other Federal Banking Agencies (FBA) are evaluating issues to ensure that the new framework results in safe and sound capital allocation and fair competition among all financial institutions.

**Moving Forward**

In FY 2007, monitoring the potential impact of a sudden and sustained rise in interest rates on banks' and savings associations', real estate portfolios, and the potential effects to other consumer lending portfolios will be a critical issue for the supervision of banks and thrifts. The OTS will pay close attention to underwriting standards and lending practices of savings associations. Expanding transparency in the financial sector will also continue to be an important goal. By ensuring that banks and thrifts have adequate and effective BSA/AML programs in place, and by exercising balanced discretion and judgment in supervisory actions, OCC and OTS will continue to enhance transparency and combat money-laundering. During

FY 2007, the OCC and OTS will continue the Basel II implementation process.

In FY 2007, the United States Mint will continue efforts to modernize coin production materials and technology, increase the flexibility and future capability of the workforce, and respond to the opportunities presented to meet the demand for numismatic products. In addition, the Mint will introduce five new 50 State quarter-dollar coins, and commemorative coins honoring the San Francisco Old Mint, the Jamestown 400th Anniversary, and the Little Rock Central High School Desegregation 50th Anniversary. New products authorized by the Presidential $1 Coin Act include circulating $1 coins honoring Presidents of the United States, featuring four coins each year minted in order of their periods of service. FY 2007 will feature Presidents Washington, Adams, Jefferson and Madison. The Act also authorizes the mintage of complementary gold bullion coins and bronze medals honoring the spouses of the presidents.

During FY 2007, BEP will continue the research and development of new counterfeit deterrent features for possible use in future currency note designs, which will further protect our nation's currency. The redesigned $5 note will begin circulating in spring 2008 and a new $100 note is scheduled for circulation in 2009. In addition, BEP plans to attain ISO 14001 certification for its environmental management systems to demonstrate its commitment to sound environmental stewardship. BEP will seek designation as an Occupational Safety and Health Administration (OSHA) Voluntary Protection Program (VPP) site. In the VPP, management, labor, and OSHA establish cooperative relationships at workplaces that have implemented a comprehensive safety and health management system. VPP designation is OSHA's official recognition of the outstanding efforts of employers and employees who have achieved exemplary occupational safety and health.

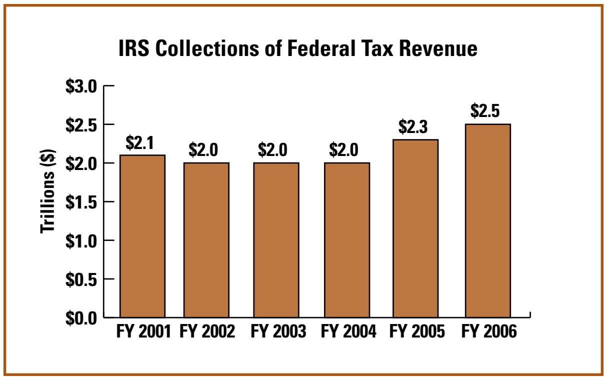
## Manage the U.S. Government's Finances Effectively

### *Collect Federal Tax Revenue When Due Through A Fair and Uniform Application of the Law*

Collecting federal taxes and other revenue is integral to the Department of the Treasury's core mission of effectively managing the federal government's finances. The Department dedicates the largest percentage of its resources to this mission. Three Department bureaus process and collect federal tax revenue: the Internal Revenue Service (IRS), the Alcohol and Tobacco Tax and Trade Bureau (TTB) and Financial Management Services (FMS).

FMS manages the collection of federal revenues such as individual and corporate income tax deposits. The most important program that supports electronic collections is the Electronic Federal Tax Payment System (EFTPS). EFTPS is a tax payment system that offers all business and individuals the convenience of making their federal tax payments electronically 24 hours, 7 days a week, instead of using checks. In FY 2006, collections through EFTPS totaled $1.9 trillion with EFTPS-Online collections totaling $283.63 billion on volume of 15.6 million transactions. This represented an increase of 35.93 percent in dollar collections, and 38.36 percent in transaction volume, over FY 2005. Approximately 5.2 million taxpayers actively enrolled and paid through EFTPS; nearly 1.297 million of whom have enrolled through EFTPS-Online.

In FY 2006, the IRS, through FMS, collected 2.5 trillion dollars in revenue, with a record $48.7 billion collected through IRS enforcement activities. Total IRS collections of tax revenue increased 11 percent and enforcement revenue increased 3 percent over last year.

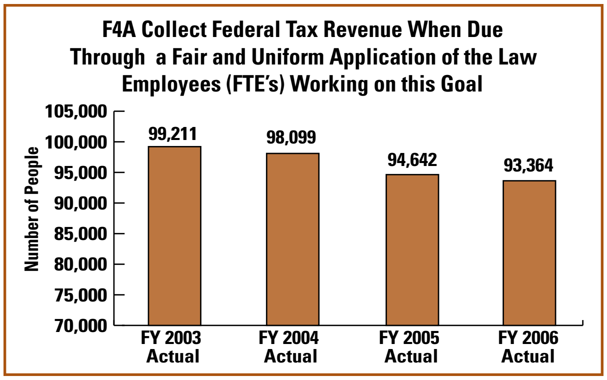


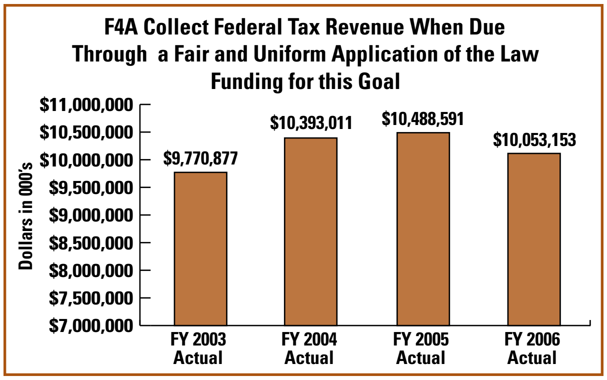

TTB collected an additional $14.786 billion in excise taxes from producers and sellers of alcohol, tobacco, firearms and ammunition.

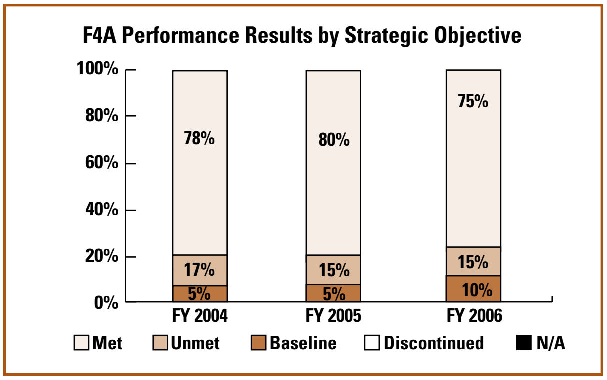
## Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $10.05 billion with a workforce of 93,364 employees to collect federal tax revenue. For this objective, the Treasury Department met 75 percent of its targets, did not meet 15 percent, and designated 10 percent as baseline to assess the data and set appropriate targets for next year.

Of the above totals, TTB spent approximately $45.75 million with 282 employees. TTB provided reimbursable services in its Puerto Rico operations and spend approximately $1,700,000 with a workforce of 15 employees. TTB met all five of their Collect the Revenue measures, with one new measure being a baseline.



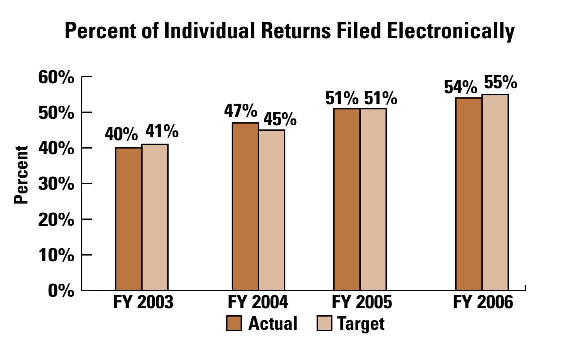

## Discussion and Analysis

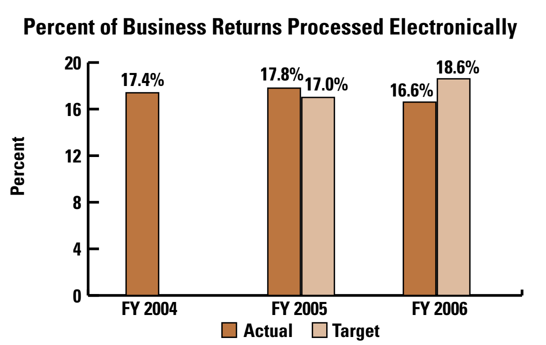
The IRS met 15 of 22 performance measures, achieving an overall success rate of more than 68 percent. The seven measures for which IRS did not meet its performance targets related to electronic filing, delivery of tax products, determination case closures, customer contacts and examination coverage for businesses. The target for this last measure, examination coverage for businesses, was missed by only 1 percent due to the IRS being prevented from taking enforcement action on a significant number of partnership return examinations involving a tax shelter promoter.

## Collection of Tax Revenue/ Processing Efficiency

For FY 2006, despite not meeting its aggressive individual electronic filing target, the IRS set another record for the number of returns filed electronically. More than half or 72.8 million individual returns were filed through electronic means representing a 6.6 percent increase over FY 2005. Highlights of IRS' electronic filing:

- Home computer filing increased 18.5 percent or 20.2 million returns, the most significant increase in electronic filing.
- Professional tax preparation use of e-file increased 9.4 percent or 52.1 million returns
- The Free File Alliance, the partnership between IRS and a consortium of tax preparation software companies, had 4 million use the free service, a 22.6 percent decrease from 2005, due to a change in eligibility requirements
- Customer use of on-line services increased
  - More than 1.3 billion web pages were viewed on IRS.gov, an increase of 4 percent over 2005
  - More than 24.7 million taxpayers used "Where's My Refund?", an increase of 11.8 percent over 2005

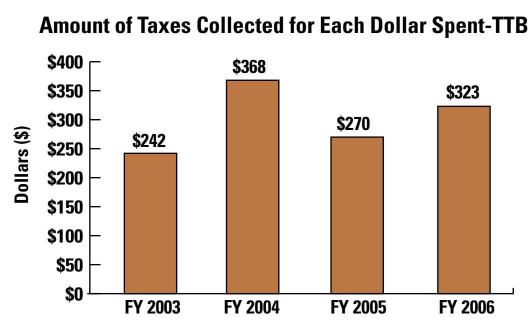



For FY 2006, the IRS did not meet its business electronic filing target primarily due to the elimination of Telefile, resulting in an increase of 3 million paper employment returns while there were 325,000 fewer electronic employment returns.

Electronic filing provides numerous benefits such as eliminating manual sorting of paper returns, batching, and the assignment of document locator numbers while providing efficiencies like data transcription, error correction, and refund issuance. Increased electronic filing reduces the need for processing centers and in FY 2006 the IRS completed the remaining actions for the closure of the Memphis Submission Processing Center, and continues planning efforts to phase out its Philadelphia Submission Processing Center.

TTB administers federal taxes on tobacco, alcohol, firearms and ammunition; collecting revenue from more than 7,500 organizations. Approximately 200 of the largest taxpaying organizations account for 98 percent of all excise tax collections annually. To collect revenues owed the federal government and achieve high levels of voluntary compliance, a field approach is used to target non-compliant industry members and a risk model is used to evaluate and select the audit targets. In FY 2006, TTB completed more than 128 audits of alcohol and tobacco companies, up from 110 audits in FY 2005.

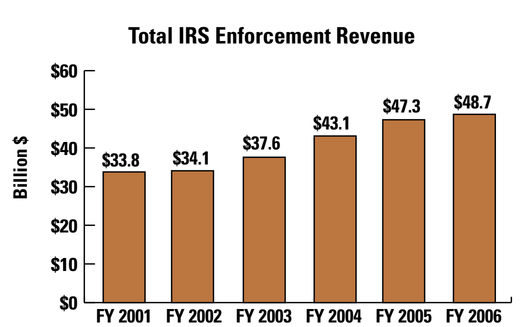


In FY 2006, TTB collected $323 in alcohol and tobacco excise taxes for every dollar spent. TTB benchmarks its performance by comparing its operations to those of similar entities in other countries, and found that it excels in terms of resources used as a percentage of taxes collected.

### Compliance/Reducing the Tax Gap

In FY 2006, the IRS updated its estimate of the tax gap which is the difference between what taxpayers should pay and what they actually pay. A tax gap results from taxpayers not filing tax returns, not paying reported tax liabilities on time, or failing to report the correct tax liabilities. New estimates show that underreporting of income taxes, employment taxes, and other taxes account for about 80 percent of the tax gap. The largest percentage of underreporting is by individuals understating their income, taking improper deductions, overstating business expenses, or erroneously claiming credits. The majority of understated income is related to business activities as opposed to wages or investment income.

The IRS focused on combating corrosive activities of major tax code violators, including delinquent corporations and high income individuals in FY 2006. These efforts are having a positive impact on collecting additional tax revenue; enforcement revenue collected from all sources was at a record level of $48.7 billion in FY 2006. In addition, targeting high-risk taxpayers improves IRS efficiency, reduces burden on compliant taxpayers, and concentrates enforcement presence where it is most needed.




In FY 2006, as a result of audit findings, TTB collected $4.4 million and identified $8.1 million in taxes, penalties, and interest potentially due.

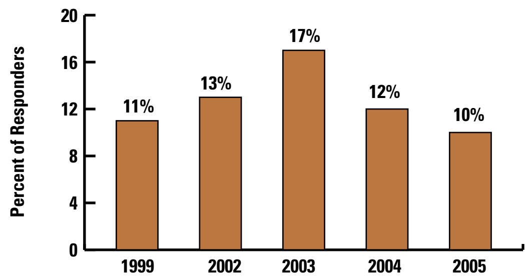
The IRS continues to focus its enforcement efforts on improving taxpayer compliance while ensuring taxpayer confidence. For FY 2006, the IRS met 83 percent of its enforcement targets. Focusing on limited scope examinations, productivity enhancements, improved analytics, improved workload identification, and selection systems that target high-risk cases resulted in:

- 7 percent improvement in individual audits
- 18 percent increase in high income audits
- 8 percent increase in small-business audits
- 10 percent increase in automated underreporter closures
- 15 percent increase in collection case closures
- 9 percent increase in revenue received from collection activities

In addition, in FY 2006, the IRS met its coverage, efficiency and embedded quality annual targets. Improvements in pipeline inventory management, decreased cycle time, and targeted training all contributed to improved productivity; improved quality controls for examinations and a reinforced focus on case quality improved performance.

In FY 2006, the IRS continued to streamline and improve its examination process by focusing on high risk issues, resulting in shortened cycle time for large corporations. In FY 2006, the time from assigning a large corporate return to a revenue agent until the final closing decreased 18 percent, from 17.5 months in FY 2005, to 14.3 months in FY 2006. The improvements to the examination process ultimately increased inventory turnover and closures.

A heightened focus by the IRS on publicizing high profile enforcement cases increased taxpayer awareness on the importance of voluntary compliance. Indicators of taxpayer attitudes toward compliance rebounded in 2004 and 2005, with more than seven out of ten taxpayers agreeing it is everyone's duty to pay their fair share of taxes. In 2005, over 30 percent of Americans, as compared to 24 percent in 2004, agreed that it is everyone's responsibility to report anyone who cheats on their taxes.




Enforcement of criminal statutes is an integral component of the IRS' efforts to enhance voluntary compliance of the tax laws. Criminal investigations completed exceeded FY 2005 performance and the FY 2006 target by more than 212 cases. The referral acceptance rate, 71.8 percent, and the total number of referrals accepted, 445, were both higher than FY 2005. In FY 2006, the proliferation of abusive tax schemes presented a significant risk to the integrity of the nation's tax system. Fraudulent and abusive financial schemes are characterized by the use of trusts; limited liability companies; limited liability corporations; foreign accounts; foreign credit and debit cards; and complex, multi-layered transactions designed to facilitate income tax evasion. The IRS used parallel proceedings, one of its most effective tools to combat abusive tax schemes. This tool enables the IRS to prevent promoters of abusive schemes from engaging in further promotional activities while a criminal investigation is in progress.

In FY 2006, the IRS upgraded its BSA database to provide an improved management information system for an intensified campaign that will focus on combating money laundering and high risk money service businesses.

In addition, the IRS participated on the Joint International Tax Shelter Taskforce, with other officials from the U.S., United Kingdom, Canada and Australia, tasked with scrutinizing tax arbitrage by multi-national corporations. A Joint International Tax Shelter Information Centre, through its advanced detection analytical capabilities, will improve the IRS' and other participating tax agencies abilities to take action against those who go abroad to plan, facilitate, or engage in abusive tax transactions.

In FY 2006, the IRS continued to research ways to reduce Earned Income Tax Credit (EITC) erroneous payments, as well as identify trends in the diverse EITC taxpayer population. The IRS launched the second year of its EITC return preparer study, which emphasizes tracking, researching and monitoring preparers' behavior.

The IRS provided assistance to taxpayers in identifying and resolving disputes earlier in the examination process, through its Pre-filing Agreement (PFA) and Industry Issue Resolution (IIR) programs. These new programs are beneficial to the taxpayer and the IRS, enabling both parties to reach agreement on contentious issues through a cooperative effort and before filing the return, therefore reducing costs, burden and further delays. In FY 2006, the IRS received over 230 PFA requests, accepting 152; of those, 55 percent were closed with an agreement and 20 percent were withdrawn. On a five point scale, taxpayers reported an overall program satisfaction level of 4.7 on the PFA, and 4.6 on the IIR programs.

## Taxpayer Service

Helping the public understand tax reporting and payment obligations is the cornerstone of taxpayer compliance. Expanding education, outreach, and service options offered to taxpayers encourages greater voluntary compliance, thus reducing the tax gap. In FY 2006, the IRS continued to improve service to taxpayers in telephone assistance, tax return processing, and electronic filing.

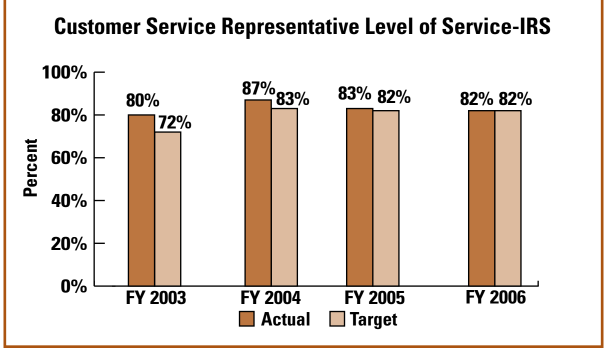
The IRS delivered a successful 2006 filing season in the midst of a very challenging year. Despite natural disasters that impacted a large number of taxpayers and required an unprecedented response from the agency, the IRS met or exceeded 50 percent of its performance targets related to taxpayer service. The following highlight IRS' performance:

- Processed more than 134.7 million individual returns, compared to 128.6 million last year, and issued more than 100 million refunds totaling $226 billion, compared to 97.1 million refunds totaling $205.1 billion
- Achieved an 82 percent level of service for toll-free calls, meeting the FY 2006 target
- Answered 32.7 million assistor telephone calls and completed nearly 24.3 million automated calls
- Correctly responded to more than 91 percent of tax law questions and 93 percent of account questions received via the telephone

More taxpayers are interacting with the IRS through various electronic media such as the Internet, e-filing and payment, e-services, and the IRS' website. In FY 2006, the IRS redesigned its website to improve search and navigation capabilities, and received the Annual Government Solutions Center Pioneer Award for Innovative Use of Technology in a Government Program. This award recognizes government agencies that make substantial progress in adding or improving electronic solutions under the President's Management Agenda.

In FY 2006, FMS continued to work with IRS on a number of initiatives to further expand the use of the Electronic Federal Tax Payment System (EFTPS) and reduce the number of paper coupons.

All 400 Taxpayer Assistance Centers (TACs) remained open and services were consistent with the 2005 filing season. In addition, wait time at the TACs was minimized with more than 80 percent of customers being served in 30 minutes or less. The accuracy of response to tax law questions increased to 83 percent, compared to 75 percent in FY 2005. With the availability of improved online service options to taxpayers, visits to the TACs were down 10 percent from FY 2005, while usage of the IRS.gov website increased nearly 10 percent. "Where's My Refund?" an online application which allows the user to check the status of a tax return, experienced almost a 12 percent increase in usage over last year. Telephone assistance calls decreased as more taxpayers opted to use automated phone and Internet services. Productivity improvements resulted in fewer resources expended in addressing account workload and taxpayer correspondence cases.




As a result of the hurricanes in 2005, legislation was passed requiring over 230 changes to 78 tax products. Despite late passage of the legislation, 83 percent of the filing season tax products deemed critical and over 61 percent of other tax products were delivered to the public on time. The IRS will continue its efforts to simplify tax forms and publications making them more user-friendly with the ultimate goal of providing all of its published products in electronic format.

## Taxpayer Outreach

Improved service options for the taxpaying public and simplifying the tax process are essential strategies supporting the IRS strategic goal to improve taxpayer service. Helping the public to understand their tax reporting and payment obligations remains a vital part of maintaining public confidence in administering the tax laws. The IRS expanded its outreach by relying on partner organizations such as state taxing authorities and a cadre of volunteer groups to serve taxpayer needs. Through its 12,300 Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) sites the IRS provided free tax assistance to the elderly, disabled, and limited English proficient individuals and families. The 69,000 volunteers located at the sites filed approximately 2.3 million returns, a 7 percent increase over FY 2005.

In addition to conducting its own outreach and education activities, the IRS partnered with private education and outreach programs. During FY 2006, the IRS provided resources and support for over 290 Partner Coalitions, resulting in the electronic filing of 1.9 million returns. Partner Coalitions or Community-based Coalitions are groups of community organizations with common interests and a shared commitment of helping working families. Benefits of these partnerships include the ability to coordinate existing activities of multiple organizations and the ability to share ideas and resources to reach a common goal. One of the larger partnerships, Connect America, provides free tax assistance to disabled veterans and free tax preparation and asset building strategies for low-income families. In 2006, the IRS was the first federal agency to receive an award as Connect America's Partner of the Year for 2005, for its efforts to provide free tax assistance to disadvantaged groups.

The 2006 filing season nationwide marketing and education campaign, aimed at reducing EITC error, reached a wide audience of taxpayers, tax practitioners, members of the media, and partner organizations. The IRS held grassroots events in New Orleans and Houston to focus on hurricane victims; and in Denver and New York for certain limited English proficiency communities. These events provided information and free tax preparation to over 1,000 people and, through the help of volunteers, nearly 300 returns were prepared. Over 1.5 million viewed the EITC pages on IRS.gov and a million used the EITC Assistant, a web-based application to help taxpayers determine eligibility, filing status, and estimated EITC amount. In addition, the IRS provided answers to more than 160,000 EITC questions through telephone assistance.

In FY 2006, the IRS played a significant role supporting the government's emergency response to the record 2005 hurricane season. Within days of the storms, the IRS provided the Federal Emergency Management Agency (FEMA) 2,500 telephone operators who answered nearly one million disaster related calls. In addition, the IRS provided assistance to the Small Business Administration (SBA) and the Department of Labor to expedite income verification for disaster loans and unemployment benefits. The IRS processed more than 1.3 million requests for tax information from the SBA, expediting the disaster claims process.

During FY 2006, the IRS answered over 288,000 taxpayer questions, on the toll-free telephone lines, relating to tax matters such as claiming property and personal losses, applying for filing extensions, and requesting extensions on existing tax liabilities due to financial hardships resulting from the hurricane. In addition, the IRS secured agreements with several tax professional and practitioner organizations to provide assistance at local disaster relief centers and free casualty loss tax return preparation for low income taxpayers. Many VITA sites remained open after April 17, 2006, to help disaster impacted taxpayers.

In FY 2006, the IRS' Identity Theft Program Office and Communications and Liaison organization implemented a communication strategy to educate taxpayers and employees about significant identity theft issues. Outreach channels included DVDs, public service announcements, and presentations at the IRS' Tax Forums to educate tax professionals on requirements to secure taxpayer data. The IRS also provided similar educational services to persons with limited English proficiency.

## Taxpayer Burden Reduction

The complexities of the tax laws and the taxpayer's familiarity and skills with tax return preparation (paper/electronic) have a significant impact on burden. As a result, many taxpayers find it more convenient and beneficial to prepare tax returns electronically or use a tax preparer. The IRS is addressing the taxpayer burden through its strategic objective of simplifying the tax process.

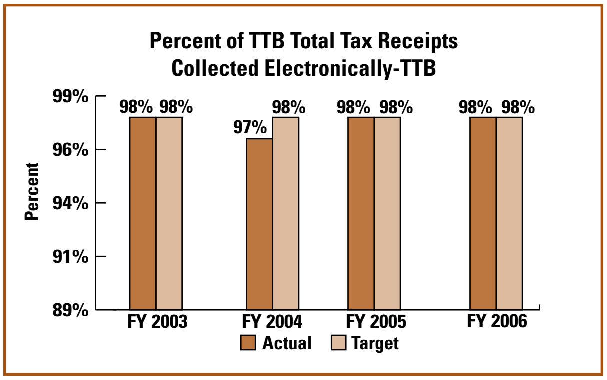
The taxpayer burden measures time and out-of-pocket expense taxpayers incur in meeting their tax responsibilities. The estimated FY 2006 burden was 6.7 billion hours, compared with 6.4 billion hours in FY 2005, an increase of 251 million hours. The increase in burden was a result of new forms and changes to existing forms dictated by the 10 different laws enacted in 2005. To help taxpayers file accurately and timely tax returns that are less burdensome, the IRS simplified the forms and instructions, to a more computer friendly format.

As in previous years, the IRS partnered with external stakeholders including taxpayers, practitioners, citizen groups, industry groups, software developers, and state and federal agencies to receive suggestions for reducing taxpayer burden. As a result, in FY 2006, the IRS launched a number of new forms and procedures designed to reduce burden without compromising tax administration objectives. The following highlight some of these:

- Unemployment tax returns redesigned to reduce filing burden for 950,000 small business owners and governmental entities. The new Form 940 and 944 allow certain employment tax filers to file annually rather than quarterly and make a single payment with the annual return.
- Revised Schedule K-1 for Form 1041 provides streamlined instructions for beneficiaries and is capable of being scanned to reduce the number of transcription errors. The new Schedule K-1 is expected to reduce 4.27 million hours of burden for 3.5 million taxpayers.
- Implementation of Alternative Minimum Tax (AMT) Calculator to assist taxpayers in determining if they are subject to the AMT and need to complete tax Form 6251. The alternative minimum tax is figured separately and eliminates many deductions and credits, thus increasing the tax liability for individuals who would otherwise pay less tax.
- Simplification of the process for requesting a filing extension for individual returns, Form 4868, which now automatically grants an additional six month extension to file. The redesign of the extension process allowed an additional 2 million taxpayers the ability to e-file/e-pay and eliminated 5 million duplicate filings. Similar changes were made to the extension process for corporate taxpayers. Automating the process affected 15.5 million submissions, reducing taxpayer burden by 9 million hours, and processing costs by 50 percent.

In addition, the IRS provided assistance to taxpayers by identifying and resolving disputes that might become controversial earlier in the examination process through its Pre-filing Agreement (PFA) and the Industry Issue Resolution programs. These programs reduce costs, burden, and delays for the taxpayer, enabling businesses and the IRS to reach agreement on contentious issues through cooperative efforts before a return is filed. In FY 2006, the IRS received over 230 PFA requests, accepting 152; of these, 55 percent were closed with an agreement, and 20 percent were withdrawn, either by the taxpayer or the IRS. On a five point scale, taxpayers reported an overall program satisfaction level of 4.7 on PFA and 4.6 for the IIR programs.

TTB, like the IRS, strives to reduce taxpaying burden on the industries of alcohol, tobacco, firearms and ammunitions. TTB uses technology to reduce paperwork burden and recently expanded the use of the Pay.gov program, allowing all excise taxpayers to file and pay electronically.




FY 2006 was the first full year the TTB infrastructure operated separately from the Department of Alcohol, Tobacco and Firearms' (ATF) IT infrastructure. (ATF is now part of the Department of Homeland Security). TTB's IT team developed and implemented the Electronic Forms Acceptance and Processing System (EFAPS), which electronically automates the entire filing process and has disaster recovery and security features.

### Business Systems Modernization (BSM)

The BSM program combines industry best practices and government expertise in business and technology solutions to develop a modernized tax administration system that meets taxpayer needs and fulfills revenue collection requirements.

Over the last two years, BSM established a foundation of disciplined project delivery and accomplishment. The program achieved its targets for both cost and schedule components while transitioning from a contractor-led program to an IRS-led program, achieving a degree of success not seen since the program's inception.

In FY 2006, the IRS implemented an updated release of it modernized e-File project, which expands taxpayer base served through combined federal and state processing of corporate and tax-exempt organizations income tax returns. For certain corporations, it is mandatory to file by this means because corporate returns typically include hundreds, or even thousands, of pages of information and are very complex; by receiving the data electronically it precludes the IRS from having to convert the data for use in an examination. Electronic capture of return information allows the IRS to quickly deliver the data to analysts and agents for compliance risk assessment and action. Modernized e-file processed 375,000 corporate returns for the 2006 filing season.

The IRS introduced their new Customer Account Data Engine (CADE) capabilities for the 2006 filing season, supporting faster refunds to taxpayers than previously possible with legacy systems. For example, direct deposit refunds were issued up to seven days faster while paper refunds were issued up to 13 days faster. With this system 7.3 million returns were processed, an increase of more than a 400 percent over the prior year; and 7 million refunds were issued totaling in excess of $3.4 billion. CADE improved taxpayer service by allowing access to current information up to seven days sooner, increasing the likelihood of single telephone call resolution, and allowed for faster issue detection and more timely account settlement. CADE is expected to process an estimated 33 million returns in 2007.

The IRS delivered release functionality for Filing & Payment Compliance, which provides for the identification of cases to be issued to Private Collection Agencies (PCAs). The system identified and delivered the first 12,500 cases to three PCAs in September 2006.

### Moving Forward

The Internal Revenue Service supports the Administration's goals to reduce the federal deficit by increasing tax receipts collected through taxpayer service and enforcement compliance. The IRS collects 97 percent of the revenues that fund the United States government.

***Enhance Enforcement of the Tax Law:*** The most recent estimate of the tax gap was $345 billion in Tax Year 2001. The need to address this gap is one of the primary forces driving all IRS activity from enforcement to taxpayer activities service.

The IRS enforcement programs yield a return on investment; each dollar invested yields at least four dollars in revenue. The complexity of the nation's current tax system is a significant reason for the tax gap and helping taxpayers understand their obligations under tax law is critical to addressing this gap. The IRS remains committed to helping taxpayers understand the tax laws and the remittance of proper tax amounts. Future efforts to reduce the tax gap include developing and implementing corporate strategies to ensure optimum, balanced audit coverage and improved resource allocation.

The IRS has a robust, balanced, and comprehensive plan to help reduce improper payments, which include base compliance activities and redesign efforts. In FY 2006, the IRS opened over 520,000 examinations of EITC returns, for tax year 2005, based on enhanced scoring and selection methodology, completed more than 515,000 examinations, uncovered 315,000 misreported income cases, issued over 650,000 math error notices, developed and implemented an enterprise research strategy in partnership with internal and external organizations to better focus EITC compliance and outreach activities, and continued the third year of the Qualifying Child test to better understand the effect of certification on EITC participation, claim accuracy, and burden. Analyzing the final results of these tests will be imperative to assessing their effectiveness in reducing erroneous EITC over claims while maintaining high participation rates by eligible taxpayers. Collectively, these enforcement efforts prevented nearly $2 billion in erroneous payments. Redesign efforts include a process to score and select amended returns for examination; a risk-based scoring strategy to identify and select cases for examination that ensures the IRS works the most egregious and productive examination cases; systemic assignment of examination cases to campuses using new data such as capacity and risk-based scores; and, integration of a decision support tool which automates issue identification, increases consistency in case documentation and, eliminates duplicative data entry when the case is closed.

Refund fraud increased significantly since 2001 and is constantly evolving and becoming more complex and sophisticated. Through the Questionable Refund Program (QRP) and the Return Preparer Program (RPP), the IRS will continue to combat this growing problem by identifying and stopping the payment of fraudulent refund claims. The IRS will also persist in identifying and investigating unscrupulous return preparers and their clients.

***Improved Taxpayer Services:*** Providing taxpayer service over multiple channels to align content, delivery, and resources with taxpayer and partner expectations will be achieved by the implementation of the Taxpayer Assistance Blueprint (TAB). Elements of the TAB are designed to reduce taxpayer burden, increase voluntary compliance, and improve workforce performance by establishing a credible taxpayer-partner baseline of needs, preferences, and behaviors. Institutionalizing key research, operational, and assessment activities will help the IRS manage and improve service delivery.

***Modernize the IRS through its People, Processes, and Technology:*** The IRS will continue to use the latest technology to optimize both taxpayer service and enforcement programs. The IRS will continue to implement its revised BSM strategy, emphasizing the incremental release of projects to deliver value sooner with less risk. Modernization efforts will continue to focus on three key tax administration systems that provide additional benefits to taxpayers and the IRS employees: Customer Account Data Engine (CADE) project, Modernized e-file (MeF), and Filing and Payment Compliance (F&PC). An example of continued modernization efforts is the expansion of the MeF taxpayer base, to include the automation of Partnership Income tax returns, which will enable nearly 2.7 million small business and self-employed taxpayers to benefit from modernized electronic filing.

Recognizing the responsibility for safeguarding Americans' most sensitive financial information, the IRS will continue taking significant steps to deploy its three-fold strategy focusing on technological solutions (encryption), employee education and awareness, and critical analysis of IRS policies and procedures.

Targeted training, activities to promote retention, and engagement of employees are important elements of the IRS Strategic Plan, and necessary to sustain an engaged and productive workforce. To meet changing business and technological demands, the IRS will focus on implementing a retention program that identifies targeted occupations, skill sets, and hard to fill positions. The program will feature integration of all recruitment, hiring, and compensation efforts; along with the development of new and improved methods of predicting future attrition through retirements. Developing activities specifically targeted toward mitigating the impact of retirements and those necessary to attract and retain new hires with advanced skills, will continue to be critical to IRS' business goals.

TTB will continue to hire CPAs as a significant portion of its workforce, and in addition to the pilot program for Pay Demo, which provides pay banding for mission critical occupations, TTB has implemented the Telework/Flexiplace program to help maintain a viable workforce.

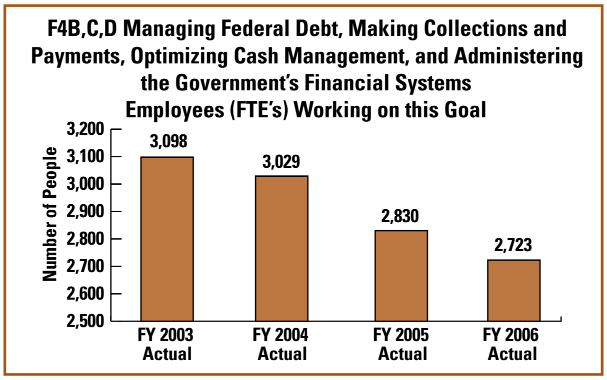
## *Manage Federal Debt Effectively and Efficiently*

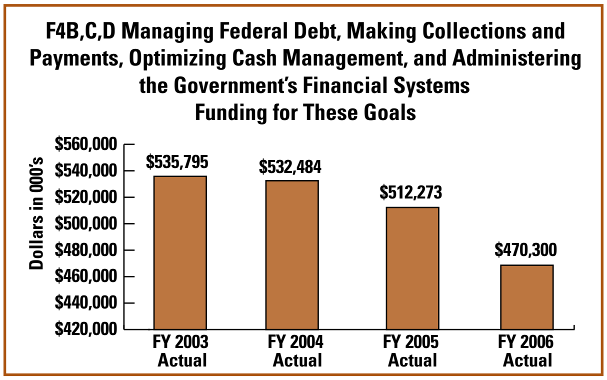
The Department determines and executes the federal borrowing strategy to meet the monetary needs of the government at the lowest possible cost. Each year, the Treasury Department borrows and accounts for trillions of dollars necessary for the government to function. Moreover, as the government's money manager, the Department provides centralized payment, collection, and reporting services for the government.

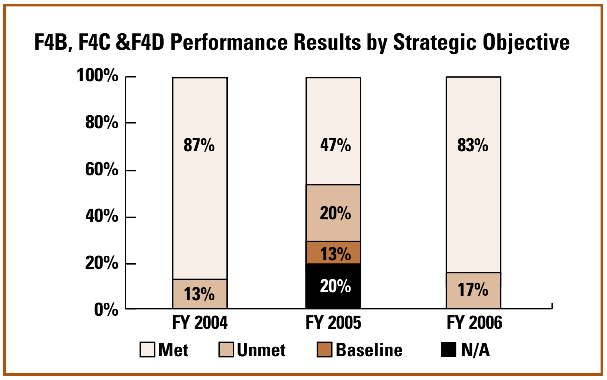
The Bureau of the Public Debt (BPD) conducts the Department's debt financing operations by issuing and servicing Treasury securities. Debt is held by individuals, corporations, state and local governments, federal agencies, and foreign governments. In FY 2006, more than $4 trillion in marketable securities were auctioned and issued and $32 trillion in non-marketable securities were issued to the public and government accounts.

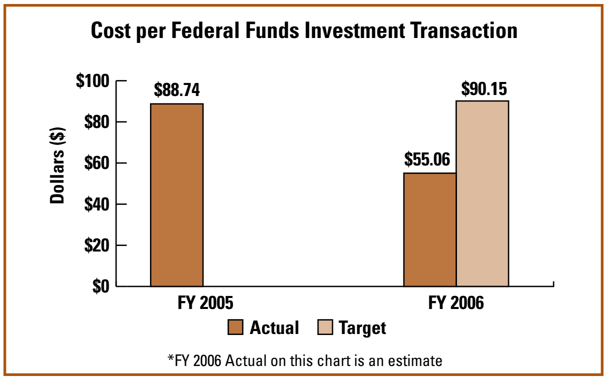
### Performance Summary and Resources Invested

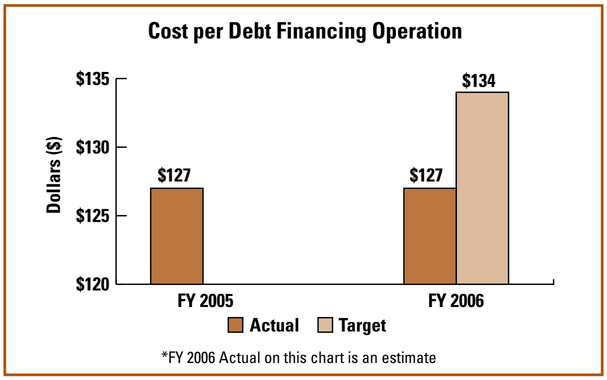
In FY 2006, the Department spent $470.3 million with a workforce of 2,723 employees to manage the federal debt. In addition, the Treasury Department met 83 percent of its performance measures for this objective.





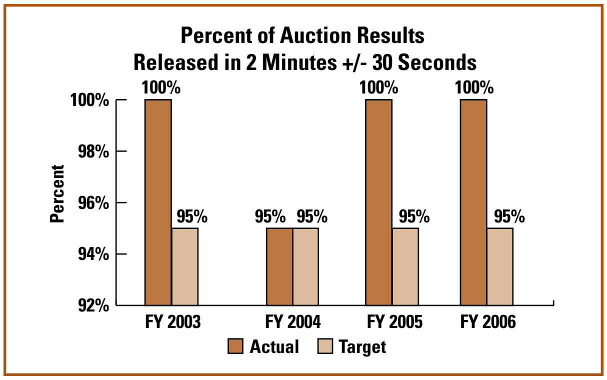




## Discussion and Analysis

In FY 2006, BPD met its performance goal of announcing Treasury auction results within its target timeframe 100 percent of the time. The Department minimized the cost of borrowing; with a shorter release time, exposure to adverse market movements and the implicit market premium are reduced. Due to ongoing improvement in work processes and efficient use of resources, BPD met its goal of processing 90 percent of retail customer service transactions within 13 business days.

In FY 2006, Domestic Finance's Office of Financial Markets continued to offer 5 year and 20 year Treasury's Inflation-Protected Securities (TIPS). TIPS are auctioned to the public, and help to diversify Treasury's investor base, lessen operational risks, and lower borrowing costs. The offerings, coupled with outreach efforts, have improved liquidity and increased investor interest and demand.




In FY 2006, after a four year absence, the Department reintroduced regular issuance of the 30-year bond to diversify funding options and stabilize the average maturity of the public debt. Previously, 20-year TIPS were the longest dated marketable securities issued by the Department of the Treasury.

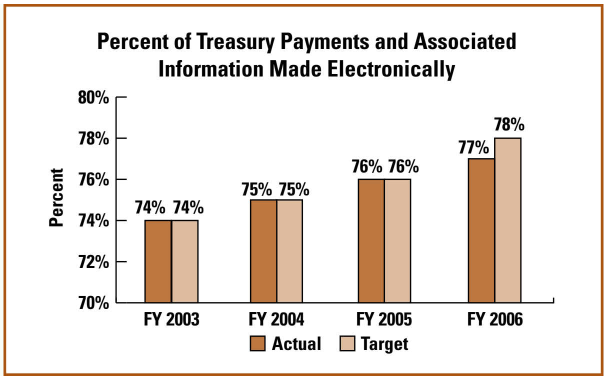
The Treasury Department improved efficiency in the Government Agency Investment Services (GAIS) program. GAIS supports federal, state, and local government agency investments in non marketable Treasury securities and manages over $3.7 trillion in customer assets. In FY 2006, over 97 percent of GAIS transactions were conducted online, as compared to 72.7 percent in FY 2005.

This increase in online GAIS transactions resulted from three factors: (1) all loans receivable transactions were conducted using the Government-Wide Accounting application, (2) regulatory changes effective in August 2005 required investors in state and local government securities to perform all investment transactions online using the SLGSafe internet application, and (3) the Federal Investments Program made a comprehensive effort to convert and train its user community to conduct investment transactions through the FedInvest internet application.

### *Make Collections and Payments on Time and Accurate*

The Treasury Department functions as the nation's disburser, manager and accountant of public monies by distributing payments, financing public services, and balancing the government's books.

The Financial Management Service (FMS) administers the government's payments, collections, and debt collections systems. FMS oversees a daily cash flow of almost $60 billion, and distributes 85 percent of federal payments each year worth close to $1.9 trillion timely and accurately. In FY 2006, FMS made 100 percent of its payments accurately and on-time, including income tax refunds, Social Security benefits, veterans' benefits, and other federal payments. FMS continued to transition from paper checks to electronic transactions issuing 77 percent of over 964 million non-Defense payments electronically. In FY 2006, FMS continued to expand and market the use of electronic media to deliver federal payments, improve service to payment recipients, and reduce government program costs. These efforts helped to decrease the number of paper checks issued and minimize costs associated with postage on the re-issuance of lost, stolen or misplaced checks.



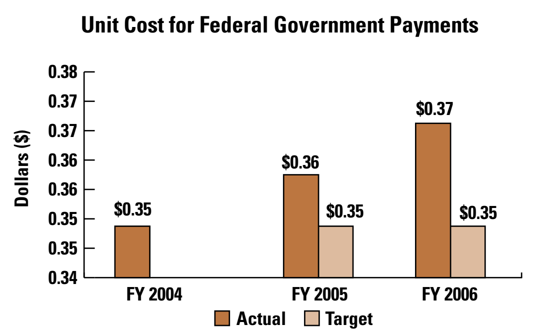

In FY 2006, FMS issued over 8.5 million fewer checks than FY 2005, continuing to face obstacles to increase the growth of electronic payments. EFT payments are less costly and more secure for the taxpayers. The direct deposit growth rate for federal benefit payments leveled off from the increases of the late 1990's. To increase the use of direct deposit for federal benefit payments, FMS began a nationwide campaign called "Go Direct," which encourages check recipients to switch from paper checks to direct deposit; saving 77 cents per transaction. During the first full year of the campaign, over 600,000 check recipients converted to direct deposit, saving millions of dollars for taxpayers.

FMS collected $2.9 trillion in FY 2006 which was an increase of 10.1 percent over FY 2005. FMS develops and operates a variety of collection mechanisms and systems to promote the use of electronics in the collections process, and assist agencies in converting collections from paper to electronic media programs such as Electronic Federal Tax Payment System (EFTPS). EFTPS is an accurate, secure and convenient way to make all federal tax payments, including corporate, excise, and employment taxes, and 1040 quarterly estimated taxes via the internet or a telephone voice response system. EFTPS processes 95 percent of U.S. tax dollars and is required to be used by businesses with annual federal tax obligations above $200,000.

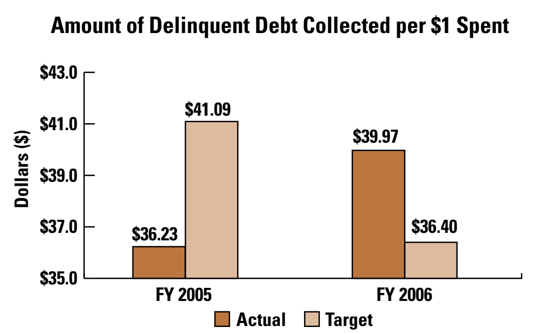
In FY 2006, to further expand the use of EFTPS, FMS conducted a marketing effort to encourage tax preparers and small businesses to pay federal taxes electronically through this system. The campaign was successful in reducing the number of Federal Tax Deposit (FTD) coupons by 8.1% or 3.4 million over last year.

In addition, FMS assisted government agencies to convert collections, at the point of receipt, from paper to electronic media receipt, including imaging paper remittances and invoices. Services such as the Paper Check Conversion Over-the-Counter System

(PCC-OTC) and Electronic Check Processing (ECP) facilitate the conversion to electronic media.




In FY 2006, FMS collected a record of $3.336 billion of delinquent government and child support debt; approximately $40 of delinquent debt is collected per $1 of program costs. Collection amounts have increased steadily since the inception of the program.




### *Optimize Cash Management and Effectively Administer the Government's Financial Systems*

The Department must manage the government's cash position to ensure that funds are available for payment, and monitor the government's receipts and payments to accurately forecast the government's current and future daily cash requirements.

Domestic Finance's Office of Fiscal Projections (OFP), BPD, and FMS are involved in cash management and administering the government's financial systems. OFP ensures that funds are available on a daily basis to cover federal payments and maximize investment earnings while minimizing borrowing costs. The OFP continually implements new and improved methods for forecasting receipts, outlays and debt. The OFP monitors its forecasting process by measuring the variance between forecasted and actual budget receipts. In FY 2006, forecasted receipts were within 3.9 percent of actual – a 20 percent improvement over the goal, which was established in FY 2005, and was to be no more than a 5 percent variance between forecasted and actual receipts.

In addition to meet its performance measure Domestic Finance expanded its monthly meetings to include representatives from Economic Policy and the revenue estimating staff of Tax Policy. These meetings focused on identifying revisions to key macro-economic indicators and the impact that revisions, both retrospective and prospective, had on current receipt projections. The success of this process was evident by the annual performance, which exceeded the tolerance for FY 2006 and resulted in a reduction of the forecast variance from FY 2005.

In FY 2006, BPD received an unqualified audit opinion on its *FY 2005 and FY 2004 Schedules of Federal Debt*, representing the largest single liability on the government-wide financial statement. In addition, BPD successfully introduced monthly financial statements in FY 2006, providing more timely financial information.

FMS maintains the federal government's books and accounts of monetary assets and liabilities, by operating and overseeing the government's central accounting and reporting system. In FY 2006, FMS was successful in publishing all government-wide financial data relating to U.S. Treasury cash-based accounting reports (i.e., the Daily Treasury Statement, the Monthly Treasury Statement, and the Annual Combined Report) with 100 percent accuracy and timeliness. For the second consecutive year, FMS released the Financial Report of the United States Government 75 days after the close of the fiscal year.

## Moving Forward

The Treasury Department will annually review its operations to utilize advancements in technology and business processes, and will continue to apply best practices to its analysis. Improvements in forecast accuracy will have a direct impact on reducing borrowing costs and increasing the return on investment.

Over the past several years, the Fiscal Service has been exploring new and innovative ways to invest excess cash, including the implementation of a program to auction off excess cash at competitive market rates. More recently, Fiscal has initiated a pilot program to invest a small portion of the Department's cash balances in reverse repurchase transactions. The pilot will be evaluated in FY 2007.

The Department of the Treasury is committed to financing the Federal Government at the lowest possible cost. BPD will continue to meet its target timeframe for auctions, and will replace the auction system to ensure it continues to meet business and contingency needs. In addition, BPD will continue to progress towards a paperless environment for savings bonds. BPD's goal in FY 2007 is to complete 90 percent of retail customer service transactions within 12 business days and by FY 2010 within 10 business days.

The Treasury Department will continue to accurately account for and report on federal debt. To improve the availability and usefulness of financial information, BPD will begin producing daily financial statements by year-end FY 2007.

In order to focus directly on mission-related activities, the Office of Management and Budget encourages federal agencies to use Shared Service Providers (SSP) for administrative services. The Department of the Treasury plans to leverage BPD's designated SSP, Administrative Resource Center (ARC), to reduce costs by improving the delivery of services in human capital, financial management, and procurement.

The Department continues to work towards an "all-electronic Treasury," integrating e-commerce technologies. FMS will continue to streamline payments and collections processes and invest in state-of-the-art technology. This is an integral part in processing payments and collections accurately and timely, and safely and securely for the taxpayer. These efforts will decrease costs and increase efficiencies.

In FY 2007, FMS will continue to increase the percentage of government receipts collected electronically to 81 percent. FMS will continue working towards their goal of converting more checks to electronic collections at the various collection lockboxes, expanding *Pay.gov* to other federal agencies. In addition, FMS will continue to expand EFTPS for taxpayers.

To increase the amount of delinquent debt collected, FMS will focus on incorporating all non-Treasury disbursed salary and vendor payments, as well as other payment types into its offset program. These efforts will allow increased debt collection from delinquent government contractors and vendors.

In October 2005, the current debt program Cross-Servicing system was replaced with *FedDebt*, a system which provides a single point of entry for agencies to refer their debts to FMS for collection. FMS will continue to roll out *Debt Check*, a program to help agencies bar delinquent debtors from obtaining new loans or loan guarantees.

In FY 2007, FMS will continue to revamp government-wide accounting processes to provide more useful and reliable financial information on a regular basis through the new government-wide accounting system, which will significantly reduce agency reporting and reconciliation requirements. As part of the system redesign, FMS will provide agencies with a web-based account statement that resembles a bank statement that summarizing Treasury fund account balance activity. Agencies will have daily access to critical data for reconciliation and fund reclassification. As a result, fund balance information will be available to agencies on a one-day turnaround. The new accounting processes will be rolled out to agencies by major transaction type with full implementation occurring over the next few years.

# M Managing the Treasury

| Strategic Goals | Strategic Objectives |
|---|---|
| Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of Treasury | Protect the Integrity of the Department of Treasury |
| | Manage the Department Resources Effectively to Accomplish the Mission and Provide Quality Customer Service |

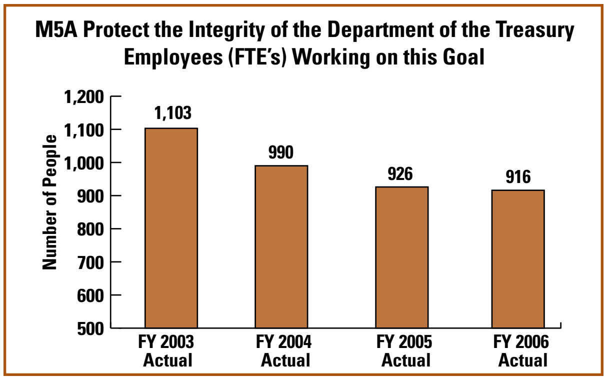
## Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of the Treasury

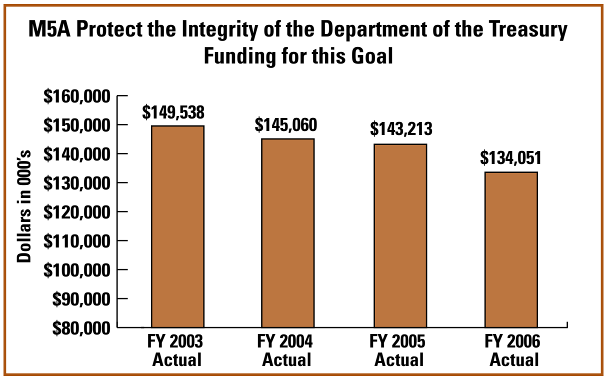
### *Protecting the Integrity of the Department of Treasury*

The Treasury Department has two Inspectors General (IGs) that provide independent oversight of the Department's activities: the Office of Inspector General (OIG) and the Treasury Inspector General for Tax Administration (TIGTA). The OIG has audit and investigative responsibilities for all non-IRS organizations within the Department (eight bureaus and all departmental offices). The TIGTA's audit and investigative services protect and promote the fair administration of the tax system and ensure that the IRS is accountable in its administration of the internal revenue laws. Both Inspectors General keep the Congress, the Secretary of the Treasury, and bureau and departmental management informed on issues, problems, and deficiencies in administering Department programs and operations, and any necessary corrective actions.

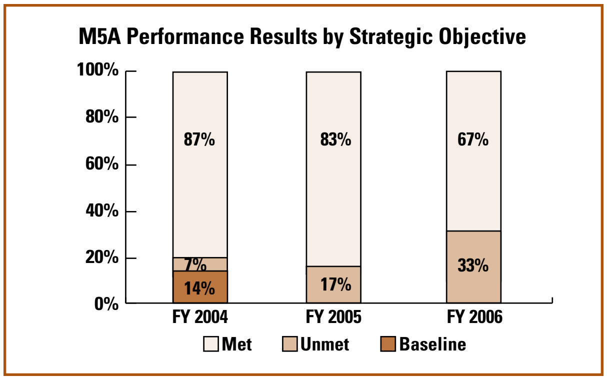
### Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $134.05 million with a workforce of 916 employees to conduct audits and investigations. The Department met 67 percent of its performance measures for this objective.




Note: OIG expended $16,830 and with a workforce of 115 FTEs. TIGTA expended $131,953 and with a workforce of 850 FTEs.



**Discussion and Analysis**

In FY 2006, the OIG issued 57 audit products, completed 100 percent of all statutory requirements, and met all required professional standards for sampled audits. FY 2006 audits identified $35 million in potential monetary benefits or cost savings, and focused on a number of the Department's most serious management challenges identified by the Inspector General. Most notably, completed audits identified weaknesses in: (1) Treasury Communications Enterprise procurement, (2) information security at several bureaus, (3) OCC and OTS examinations for compliance with Office of Foreign Assets Control (OFAC) sanctions, and (4) OCC's enforcement action against Wells Fargo Bank for Bank Secrecy Act (BSA) deficiencies. The audit of the Department's FY 2005 financial statements resulted in an unqualified or clean opinion, however one material weakness related to IRS financial management was reported.

The OIG completed its FY 2005 and FY 2006 independent evaluations of the Department's information security policies and practices pursuant to the Federal Information Security and Management Act (FISMA). The FY 2006 evaluation found that while the Department made progress in accounting for its inventory of systems, it remained in non-compliant with FISMA. In addition, the IG issued its annual management and performance challenges memorandum to the Secretary citing five challenges which are: (1) corporate management, (2) management of capital investments, (3) information security, (4) linking resources to results, and (5) anti-money laundering and terrorist financing/Bank Secrecy Act enforcement.

The OIG has criminal, civil, and administrative investigative responsibilities for all Department programs and operations excluding the IRS. In FY 2006, the OIG reviewed 488 complaints for potential investigation or inquiry, opened 129 new investigations, referred 61 for criminal prosecution and had administrative corrective action taken on 29. All investigations sampled met applicable standards set by President's Council for Integrity and Efficiency.

The OIG prevented, detected, and investigated a variety of crimes which include: identity theft, forged and stolen treasury checks, fraud involving disaster recovery funds, and other crimes. Examples of OIG investigations include:

- Banking officials who perpetrated a multi-million dollar bank fraud, thereby jeopardizing the safety and soundness of their institutions.
- An individual who schemed to defraud the Federal Emergency Management Agency (FEMA) of more than $100,000 in relief funds intended for victims of Hurricanes Katrina and Rita by employing the stolen identities of others.
- A Department employee who falsely reported the theft of Privacy Act protected information. This case highlighted information security weaknesses and identity theft vulnerabilities.
- A Department employee who was arrested pursuant to a plea agreement, pled guilty to one charge of 18 USC 642, possession of tools and materials for counterfeiting purposes, in connection with his theft of a number of partially printed sheets of $100 bills from BEP.

In FY 2006, the OIG auditors and investigators, working collaboratively with Department program managers, began a proactive initiative to identify potentially fraudulent Federal Employee Compensation Act (FECA) claims, as well as opportunities to improve internal program controls. These investigations led to the arrest and indictment of a former employee who received $270,000 in FECA benefits over 4 years. Similar initiatives are being undertaken by OIGs at other federal agencies.

The TIGTA's audit and investigative services protect and promote the fair administration of the tax system, and ensure the IRS is accountable in its administration of the internal revenue laws.

The TIGTA issued 171 audit reports, in FY 2006, resulting in potential financial accomplishments of $ 1.8 billion and potentially impacting 1,798,152 million taxpayer accounts in areas such as taxpayer burden and taxpayer rights. Audit recommendations lead to improvements in systems modernization, tax compliance, tax return processing, and the implementation of tax law changes. Results include:

- Identifying data discrepancies in the IRS' Taxpayer Assistance Center Closure Model that affect the IRS' ability to accurately determine cost savings.
- Recommending the IRS' Commissioner of the Small Business/Self-Employed Division, convene a study group to develop a business case for filers of Form 5471 (Information Return of U.S. Persons with Respect to Certain Foreign Corporations) and Form 5472 (Information Return of a 25 percent. Foreign Owned U.S. Corporation or a Foreign Corporation Engaged in U.S. Trade or Business).
- Estimating there are approximately 22,500 licensed tax practitioners not compliant with their individual tax obligations, necessitating identification and referral to the IRS' Office of Professional Responsibility.

Investigative work by the TIGTA is designed to protect the integrity of tax administration, which includes investigating allegations of bribery, threats, and external attempts of tax administration corruption. In FY 2006, the TIGTA achieved a 79 percent positive results ratio from its investigations, more than 8,772 complaints of alleged criminal wrongdoing or administrative misconduct, and closing 3,412 cases.

As of April 2006, an investigation of reported tax payment thefts from a Lockbox, operated by the Bank of America, revealed 54 remittance checks were identified as stolen. (Payment checks of taxes are made out to the Department of Treasury, not the IRS). The TIGTA estimates the cumulative value of stolen checks was approximately $2.8 million; to date, the TIGTA's investigation resulted in the court ordered seizure and recovery of $500,293.67. In May 2006, another TIGTA investigation revealed a temporary employee of the Bank of America altered 15 stolen checks totaling $330,009.04.

**Moving Forward:**

In FY 2007, the OIG will increase oversight of the Department's BSA and intelligence systems development efforts, as well as other high risk capital investments. In addition, the OIG will:

- Increase audit coverage of programs designed to counter money-laundering and terrorist financing
- Complete 100 percent of statutory audits on time
- Timely investigate complaints of fraud, waste, and abuse in non-IRS programs
- Continue the proactive integrity program

In FY 2007, the TIGTA will ensure that audit recommendations continue to improve by:

- Addressing major management challenges such as computer security, taxpayer rights and protection, and ensuring quality taxpayer services
- Monitoring the IRS' modernization efforts to identify problems encountered in the implementation of new programs and information systems
- Monitoring IRS' efforts to achieve its strategic goals, eliminating identified material weaknesses and achieving the President's Management Agenda initiatives

In addition, the TIGTA will ensure that investigative programs continue to improve by:

- Investigating complaints of wrongdoing that may impact the integrity of tax administration
- Conducting investigations that concentrate on three core areas: employee integrity, external

attempts to corrupt tax administration, and employee and infrastructure security

- Heightening integrity awareness through the regular delivery of presentations to IRS employees, law enforcement agencies, tax practitioners and community groups

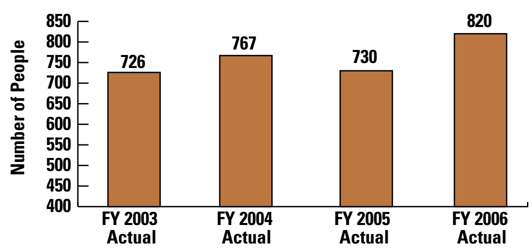
## *Managing Treasury Resources Effectively to Accomplish the Mission and Provide Quality Customer Service*

The Treasury Department ensures that taxpayers receive the most efficient and effective use of their tax dollars by building a strong institution that is citizen-centered, results-oriented, and actively implements the principles of the President's Management Agenda (PMA).

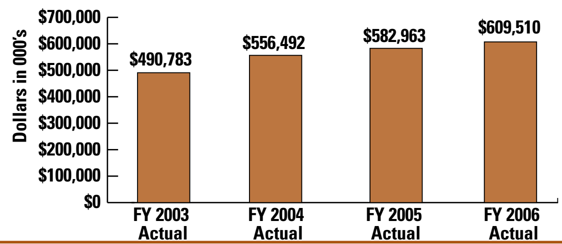
### Performance Summary and Resources Invested

In FY 2006, the Treasury Department spent $609.5 million with a workforce of 820 employees to manage Department-wide policies and programs. In addition, the Department of the Treasury met 53 percent of its performance measures for this objective, did not meet 27 percent, and the remaining 20 percent was unavailable due to the discontinuance of the measure.

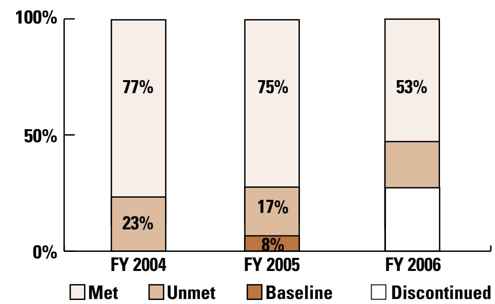
M5B Manage Treasury Resources Effectively to Accomplish the Mission and Provide Quality Customer Service Employees (FTEs) Working on This Goal




M5B Manage Treasury Resources Effectively to Accomplish the Mission and Provide Quality Customer Service Funding for This Goal




M5B Performance Results by Strategic Objective




### Discussion and Analysis

The Department of the Treasury works to manage the Department effectively through the principles of the President's Management Agenda (PMA). In 2001, the President challenged the Federal Government to become more efficient, effective, results-oriented and accountable. Over the past five years, the PMA has become the framework for organizing the efforts cited by the President and for focusing on results. This agenda reflects the President's commitment to achieve immediate, concrete and measurable results that matter to the American people.

The President holds each agency accountable for its performance in carrying out the PMA. This is done through quarterly scorecards issued by OMB. Two rating categories are used – one for "status," which assesses whether an agency has satisfied the overall goals or long-term criteria to accomplish an initiative and the other for "progress," which measures the extent to which the agency has followed its plan. To convey an agency's performance, the Administration developed a simple grading system of red, yellow and green.

In FY 2006, the Department continued to be successful in two initiatives, Competitive Sourcing and Human Capital; in the E-Government initiative the status score went up; while the Budget Performance, Improper Payments, and Financial Performance initiatives remained unchanged. Some initiatives showed progress by increasing the score one level for the quarterly rating.

The Department of the Treasury is responsible for six initiatives identified by the PMA, five standard initiatives that are government-wide and one that is limited to the Department.

**President's Management Agenda**

| Initiative | Status | | FY 2006 Progress | | | |
|---|---|---|---|---|---|---|
| | FY 2005 | FY 2006 | Q1 | Q2 | Q3 | Q4 |
| Human Capital | Y | G | G | G | G | G |
| Competitive Sourcing | G | G | G | G | G | Y |
| Financial Performance | R | R | G | G | G | G |
| E-Government | R | Y | Y | G | Y | Y |
| Budget Performance Integration | Y | Y | G | G | Y | Y |
| Improper Payments | R | R | Y | Y | Y | Y |

G Green for Success   Y Yellow for Mixed Results   R Red for Unsatisfactory

***Human Capital:*** In FY 2006, during a year of challenges, the Treasury Department's Human Capital initiative was successful by continuing to align its workforce with its human capital goals and objectives. Consistent with its human capital vision, the Department used strategic workforce planning and flexible tools to recruit, retain, and reward employees, fostering a diverse and high-performing workforce.

In FY 2006, the Department's human capital activities focused on results-oriented performance, leadership succession planning, and accountability. The Office of Personnel Management approved the Treasury Department's program for succession planning and accountability, a condition for remaining successful in the PMA Human Capital initiative. This program ensures that future management acquires appropriate skills to enable them to lead the Department in an ever-changing environment.

FY 2006 human capital successes include:

- Achieving a goal of 100% of supervisors', managers', and executives' performance plans that contain elements directly linked to the Department's mission
- Training over 1,300 current and future managers in leadership competencies
- Strengthening the accountability system through Department-wide policy which emphasizes compliance with federal laws and regulations, and merit system principles.

In FY 2007, human capital strategies are aimed at reducing under representation in mission-critical occupations and the Department's leadership ranks. Continued emphasis will be on expanding pay-for-performance systems throughout the Department, and conducting accountability and compliance reviews, ensuring that improvement action is taken where needed.

***Competitive Sourcing:*** Through Competitive Sourcing, the Treasury Department utilizes public-private competition to effectively deliver services at the lowest possible cost to the American taxpayer. Competitive Sourcing allows the Department to look internally and externally for the most efficient ways to achieve its mission.

In FY 2006, the Department of the Treasury remained successful in the Competitive Sourcing initiative. The Competitive Sourcing team accomplished this by:

- Migrating and conducting the Federal Activities Inventory Reform (FAIR) Act in

HR Connect, the Department's on-line human capital system

- Creating a Shared Services concept to optimize existing competitive sourcing expertise
- Developing a demand analysis system for conducting potential studies
- Improving coordination of competitive sourcing activities Department-wide

In FY 2006, the Treasury Department continued to oversee A-76 competitions by issuing appropriate guidance and coordinating reporting efforts to the OMB and Congress on the FAIR Act and Congressional mandates. Significant results of the Department's activities this fiscal year include:

- Realizing over $10 million in cost savings and avoidance from Competitive Sourcing
- Continued oversight of competitive sourcing actions covering 2,700 FTE

In FY 2007, the Department will complete studies on time, establish the process, procedures, and framework for Most Efficient Organization (MEO) use of sub-contracts, and manage and monitor post-implementation of competitive sourcing studies.

***Improved Financial Performance:*** The Treasury Department continued to work toward full compliance with the Federal Managers Financial Improvement Act (FMFIA) and improved financial management processes to produce accurate and timely information that supports operating, budget and policy decisions.

In FY 2006, the Department of the Treasury accounted for public funds accurately and timely through a successful three day closing process at the end of each month. The Department's Financial Performance team met its reporting deadlines and was provided a clean annual audit.

In addition, the Treasury Department continued emphasis on reducing material weaknesses during the year resulting in a reduction from seven to six material weaknesses.

In FY 2007, the Department will continue to implement its corrective action plan to address material weaknesses.

***Expanded E-government:*** Expanding electronic government products and services department-wide improve internal efficiency and effectiveness, and enhanced service to the public. In FY 2006, the Treasury Department continued to improve its enterprise architecture, information technology (IT) capital planning processes, and cyber security practices department-wide. The Department managed projects to meet cost, schedule and performance goals, certified and accredited Treasury systems to protect information from unauthorized access and theft, and fully participated in all applicable Presidential E-Government Initiatives.

During FY 2006, accomplishments include:

- Improving Treasury-wide Capital Planning and Investment Control policies and processes, including executive certification of quarterly project performance reporting
- Applying standard definitions for systems under the Federal Information Security Management Act (FISMA) and establishing a new system inventory to improve future management and reporting
- Integrating Treasury Enterprise Architecture (EA) and IT Capital Planning processes
- Completing all required E-Government initiative implementation milestones

In FY 2007, the Department will continue to improve its compliance with FISMA, and strengthen the oversight and management of Treasury IT investments using the Treasury Enterprise Architecture.

***Budget and Performance Integration:*** In FY 2006, the Treasury Department embarked on revising its Strategic Plan. This plan clearly defines the strategic priorities and articulates outcome-oriented goals and objectives. The Department's senior leadership sponsored the effort and served as champions for the teams developing outcomes, strategies and measures.

The Treasury Department tested its mission, goals and strategies against a set of future possibilities to ensure their robustness. The Department identified 10 value chains, groups of programs with a common purpose, recognizing that outcomes connect us across different programs and organizations. The new Treasury Strategic Plan will add a vision statement, and a set of core values, both of which serve to integrate and draw the Department toward a compelling picture of its future. Finally, the strategic plan will establish an integrated management system that links budget and cost to outcomes, enabling the Department to measure the value it produces for the American people.

***Eliminating Improper Payments:*** : The score for this initiative remained unchanged. The Department continuously works with the Office of Management and Budget (OMB) to develop improved error measurement methodology for the Internal Revenue Service (IRS) Earned Income Tax Credit (EITC) program. EITC, due to erroneous payments, is the only high-risk program in the Treasury Department.

In FY 2007, the IRS has committed to providing a corrective action plan to OMB, which includes aggressive reduction targets, for EITC's erroneous payments, that will produce effective results. Additional information on this PMA initiative and the Department's plan to address the Act can be found in Part IV of this report.

### The Program Assessment Rating Tool (PART)

Program evaluation is a core management tool used to allocate resources and promote efficiency and effectiveness. In addition to regular independent program evaluations conducted by the Treasury Department's bureaus, the Department works with OMB to select programs each year that will be evaluated through the PART process. Programs are evaluated through this process by OMB every five years.

All programs that undergo a PART evaluation receive weighted scores in four categories: program purpose and design, strategic planning, program management and program results and accountability. The weights are as follows:

| Categories | Weight |
|---|---|
| Program Purpose and Design | 20% |
| Strategic Planning | 10% |
| Program Management | 20% |
| Program Results/Accountability | 50% |

PART scores are summarized by OMB as a qualitative rating of "Effective," "Moderately Effective," "Adequate," "Results Not Demonstrated" or "Ineffective."

Like the PMA, the PART process gives the Treasury Department a framework for assessing performance in its major programs. Through the use of in-depth performance questions, PART allows the leadership to evaluate how well a program is meeting its intended objectives, how effectively and efficiently it is managed, the extent to which the program supports the Department's overarching strategic goals and how well the program achieves results.

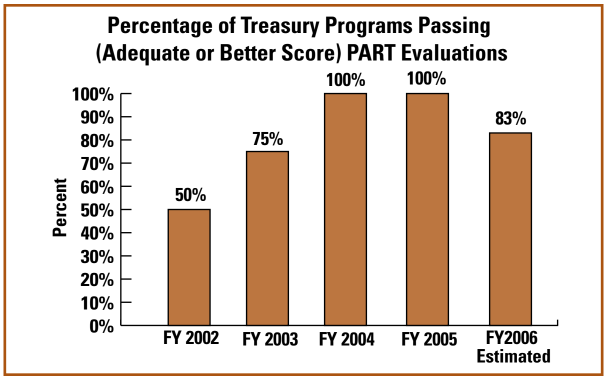
The Table below details all of the Treasury Department programs that have received OMB PART evaluations thus far. For a full list of PART evaluations see the appendix. (FY 2006 PART scores not final at time of publication).

| Program | Bureau | Year PART Conducted | Rating |
|---|---|---|---|
| Bank Enterprise Award | CDFI | 2002 | Results Not Demonstrated |
| Office of Foreign Assets Control | DO | 2002 | Results Not Demonstrated |
| Earned Income Tax Credit | IRS | 2002 | Ineffective |
| Tax Collection | IRS | 2002 | Results Not Demonstrated |
| Consumer Product Safety Commission | TTB | 2002 | Adequate |
| International Development Association | DO | 2002 | Adequate |
| Bank Supervision | OCC | 2002 | Effective |
| Thrift Supervision | OTS | 2002 | Effective |
| Coin Production | Mint | 2002 | Effective |
| African Development Fund | DO | 2003 | Results Not Demonstrated |
| Administering the Public Debt | BPD | 2003 | Effective |
| Debt Collection | FMS | 2003 | Effective |
| New Currency Manufacturing | DO | 2003 | Effective |
| Office of Technical Assistance | DO | 2003 | Adequate |
| Global Environment Facility | DO | 2004 | Results Not Demonstrated |
| Tropical Forest Conservation Act | DO | 2004 | Results Not Demonstrated |
| Financial and Technical Assistance | CDFI | 2004 | Adequate |
| FMS Collections | FMS | 2004 | Effective |
| IRS Taxpayer Advocate Service | IRS | 2004 | Moderately Effective |
| IRS Taxpayer Service | IRS | 2004 | Adequate |
| New Markets Tax Credit | CDFI | 2004 | Adequate |
| Mint Numismatic | Mint | 2004 | Effective |
| Asian Development Fund | DO | 2005 | Results Not Demonstrated |
| Collect the Revenue Program | TTB | 2005 | Effective |
| BSA Data Collection, Retrieval and Sharing | FinCEN | 2005 | Moderately Effective |
| FMS Payments | FMS | 2005 | Effective |
| IRS Criminal Investigations | IRS | 2005 | Moderately Effective |
| IRS Examinations | IRS | 2005 | Moderately Effective |
| IRS Submission Processing | IRS | 2005 | Moderately Effective |
| U.S. Mint Protection Program | Mint | 2005 | Effective |
| Protection | BEP | 2006 | Rating Pending |
| Bank Secrecy Act Administration | FinCEN | 2006 | Rating Pending |
| Bank Secrecy Act Analysis | FinCEN | 2006 | Rating Pending |
| Government Wide Accounting and Reporting | FMS | 2006 | Rating Pending |
| Health Care Tax Credit Administration | IRS | 2006 | Rating Pending |
| IRS Retirement Savings Regulatory Program | IRS | 2006 | Rating Pending |

The Treasury Department continues to work towards achieving strong PART scores by: (1) improving goals and measures; (2) providing a training session that includes an exchange of lessons learned across bureaus; and (3) solid evidentiary procedures. Additional details of OMB recommendations and actions planned or underway for each program can be found in appendix of this report.

Scores are pending for the programs that were evaluated through the PART process for the FY 2007 (2008 budget year) and will be reported in the FY 2007 Performance and Accountability Report.

The Department's progress in program performance is indicated in the chart below:




Additional details of OMB recommendations and actions planned or underway for each program can be found in appendix of this report.

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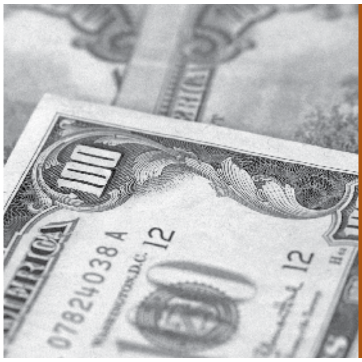

# Part III: Annual Financial Report

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## Consolidated Balance Sheets
### As of September 30, 2006 and 2005
### (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **ASSETS** | | |
| **Intra-governmental Assets** | | |
| Fund Balance (Note 2) | $ 71,153 | $ 66,334 |
| Loans and Interest Receivable (Note 3) | 245,206 | 228,491 |
| Advances to the Black Lung Trust Fund (Note 4) | 9,632 | 9,186 |
| Due From the General Fund (Note 4) | 8,540,195 | 7,978,081 |
| Accounts Receivable and Related Interest (Note 10) | 483 | 626 |
| Other Intra-governmental Assets | 78 | 40 |
| **Total Intra-governmental Assets** | **8,866,747** | **8,282,758** |
| Cash, Foreign Currency, and Other Monetary Assets (Note 5) | 63,892 | 47,578 |
| Gold and Silver Reserves (Note 6) | 11,062 | 10,933 |
| Loans and Interest Receivable (Note 3) | 288 | 670 |
| Investments and Related Interest (Note 7) | 9,325 | 9,404 |
| Reserve Position in the International Monetary Fund (Note 8) | 6,621 | 13,247 |
| Investments in International Financial Institutions (Note 9) | 5,488 | 5,464 |
| Tax, Other and Related Interest Receivables, Net (Note 10) | 21,962 | 21,430 |
| Inventory and Related Property, Net (Note 11) | 389 | 468 |
| Property, Plant, and Equipment, Net (Note 12) | 2,182 | 2,398 |
| Other Assets | 22 | 22 |
| **Total Assets (Note 13)** | **$ 8,987,978** | **$ 8,394,372** |
| Stewardship Property (Note 12) | | |
| **LIABILITIES** | | |
| **Intra-governmental Liabilities** | | |
| Federal Debt and Interest Payable (Notes 4 & 14) | 3,673,117 | $3,354,905 |
| Other Debt and Interest Payable (Note 14) | 14,164 | 14,164 |
| Due to the General Fund (Note 4) | 306,352 | 273,551 |
| Other Intra-governmental Liabilities (Note 18) | 301 | 422 |
| **Total Intra-governmental Liabilities** | **3,993,934** | **3,643,042** |
| Federal Debt and Interest Payable (Notes 4 & 14) | 4,844,074 | 4,600,668 |
| Certificates Issued to Federal Reserve Banks (Notes 5) | 2,200 | 2,200 |
| Allocation of Special Drawing Rights (Note 5) | 7,234 | 7,102 |
| Gold Certificates Issued to Federal Reserve Banks (Note 6) | 11,037 | 10,924 |
| Refunds Payable (Notes 4 & 22) | 1,701 | 1,952 |
| D.C. Pensions Actuarial Liability (Note 16) | 9,068 | 8,511 |
| Other Liabilities (Note 18) | 3,816 | 4,665 |
| **Total Liabilities (Note 18)** | **8,873,064** | **8,279,064** |
| Commitments & Contingencies (Notes 3, 5, 12, 15, 16 & 17) | | |
| **NET POSITION** | | |
| Unexpended Appropriations: | | 63,182 |
| Earmarked funds (Note 23) | 202 | — |
| Other funds | 68,068 | — |
| Subtotal | 68,270 | 63,182 |
| Cumulative Results of Operations: | | 52,126 |
| Earmarked funds (Note 23) | 31,614 | — |
| Other funds | 15,030 | — |
| Subtotal | 46,644 | 52,126 |
| **Total Net Position (Note 19)** | **$114,914** | **115,308** |
| **Total Liabilities and Net Position** | **$ 8,987,978** | **$ 8,394,372** |

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

## Consolidated Statements of Net Cost
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Cost of Treasury Operations:** | | |
| Economic Program: | | |
| Gross Cost | $ 2,339 | $ 3,066 |
| Less Earned Revenue | (1,151) | (782) |
| **Net Program Cost** | **$ 1,188** | **$ 2,284** |
| **Financial Program:** | | |
| Gross Cost | $ 17,496 | $ 15,580 |
| Less Earned Revenue | (5,083) | (4,487) |
| **Net Program Cost** | **$ 12,413** | **$ 11,093** |
| **Management Program:** | | |
| Gross Cost | $ 987 | $ 1,156 |
| Less Earned Revenue | (559) | (739) |
| **Net Program Cost** | **$ 428** | **$ 417** |
| Total Program Gross Costs | 20,822 | 19,802 |
| Total Program Gross Earned Revenues | (6,793) | (6,008) |
| **Total Net Cost of Operations (Note 20)** | **$ 14,029** | **$ 13,794** |
| **Federal Costs:** | | |
| Federal Debt Interest | $ 403,459 | $ 354,386 |
| Less Interest Revenue from Loans (Note 19) | (12,593) | (11,984) |
| **Net Federal Debt Interest Costs (Note 20)** | **$ 390,866** | **$ 342,402** |
| Other Federal Costs (Note 20) | $ 8,940 | $ 8,673 |
| **Net Federal Costs** | **$ 399,806** | **$ 351,075** |
| **Net Cost of Operations, Federal Debt Interest, and Other Federal Costs** | **$ 413,835** | **$ 364,869** |

*The accompanying notes are an integral part of these financial statements.*
*See Note 20 for Net Cost Schedule by Sub-organizations.*

## Consolidated Statements of Changes in Net Position
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | | | | 2005 |
|---|---|---|---|---|---|
| | Combined Earmarked Funds | Combined All Other Funds | Eliminations | Consolidated Total | Consolidated Total |
| **CUMULATIVE RESULTS OF OPERATIONS** | | | | | |
| Beginning Balances | $ $30,817 | $ 21,309 | $ 0 | $ 52,126 | $ 56,308 |
| **Budgetary Financing Sources:** | | | | | |
| Appropriations Used | 298 | 412,116 | 0 | 412,414 | 362,067 |
| Non-exchange Revenue | 76 | 10 | (30) | 56 | 36 |
| Donations and Forfeitures of Cash/Equivalent | 79 | 0 | 0 | 79 | 169 |
| Transfers In/Out without Reimbursement | 0 | (28) | 0 | (28) | 0 |
| Other | (12) | (37) | 0 | (49) | 0 |
| **Other Financing Sources** | | | | | |
| Donation/Forfeiture of Property | 61 | 0 | 0 | 61 | 51 |
| Accrued Interest & Disc. on Debt | 0 | 8,991 | 0 | 8,991 | 9,879 |
| Transfers In/out Without Reimbursement | (45) | 21 | 0 | (24) | (133) |
| Imputed Financing Sources | 57 | 1,145 | (470) | 732 | 722 |
| Transfers to the General Fund and Other (Note 19) | (69) | (13,810) | 0 | (13,879) | (12,104) |
| **Total Financing Sources** | **445** | **408,408** | **(500)** | **408,353** | **360,687** |
| Net Cost of Operations | 352 | (414,687) | 500 | (413,835) | (364,869) |
| Net Change | 797 | (6,279) | 0 | (5,482) | (4,182) |
| **Cumulative Results of Operations** | **$ 31,614** | **$ 15,030** | **$ 0** | **$ 46,644** | **$ 52,126** |
| **UNEXPENDED APPROPRIATIONS** | | | | | |
| Beginning Balance | $ 202 | $ 62,980 | | $ 63,182 | $ 56,850 |
| **Budgetary Financing Sources:** | | | | | |
| Appropriation Received (Note 19) | 298 | 417,468 | | 417,766 | 369,312 |
| Appropriations Transferred in/out | 0 | 14 | | 14 | (594) |
| Other Adjustments | 0 | (278) | | (278) | (319) |
| Appropriations Used | (298) | (412,116) | | (412,414) | (362,067) |
| **Total Budgetary Financing Sources** | **0** | **5,088** | | **5,088** | **6,332** |
| **Total Unexpended Appropriations** | **202** | **68,068** | | **68,270** | **63,182** |
| **Net Position** | **$ 31,816** | **$ 83,098** | | **$ 114,914** | **$ 115,308** |

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

## Combined Statements of Budgetary Resources
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **BUDGETARY RESOURCES** | | |
| Unobligated balance, brought forward | $ 64,670 | $ 69,912 |
| Recoveries of prior year unpaid obligations | 380 | 1,286 |
| Budget authority: | | |
| Appropriations (Note 19) | 437,427 | 379,567 |
| Borrowing authority | 12 | 331 |
| Spending authority from offsetting collections: | | |
| Earned: | | |
| Collected | 9,310 | 6,286 |
| Change in receivables from Federal sources | 19 | 36 |
| Change in unfilled customer orders: | | |
| Advance received | 25 | (29) |
| Without advance from Federal sources | (51) | (81) |
| Subtotal | 446,742 | 386,110 |
| Non-expenditure transfers, net | 134 | (530) |
| Temporarily not available pursuant to Public Law | (3,671) | 1,957 |
| Permanently not available | (5,164) | (5,403) |
| **Total Budgetary Resources** | **$ 503,091** | **$ 453,332** |
| **STATUS OF BUDGETARY RESOURCES** | | |
| Obligations incurred: | | |
| Direct | $ 440,798 | $ 384,853 |
| Reimbursable | 4,753 | 3,809 |
| Subtotal | 445,551 | 388,662 |
| Unobligated Balance: | | |
| Apportioned | 14,309 | 14,572 |
| Exempt from apportionment | 32,784 | 40,084 |
| Subtotal | 47,093 | 54,656 |
| Unobligated balance not available | 10,447 | 10,014 |
| **Total Status of Budgetary Resources** | **$ 503,091** | **$ 453,332** |

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

## Combined Statements of Budgetary Resources
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **CHANGE IN OBLIGATED BALANCE** | | |
| Obligated balance, net: | | |
| Unpaid obligations brought forward, Oct. 1 | $ 46,381 | $ 42,133 |
| Uncollected customer payments from Federal sources, brought forward | (643) | (687) |
| Total unpaid obligated balance, net | 45,738 | 41,446 |
| Obligations incurred, net | 445,551 | 388,662 |
| Gross outlays | (438,494) | (383,128) |
| Recoveries of prior year unpaid obligations, actual | (380) | (1,286) |
| Change in uncollected customer payments from Federal sources | 33 | 46 |
| Obligated balance, net, end of period: | | |
| Unpaid obligations | 53,057 | 46,381 |
| Uncollected customer payments from Federal sources | (609) | (643) |
| **Total, unpaid obligated balance, net, end of period** | **52,448** | **45,738** |
| **Net Outlays** | | |
| Gross outlays | 438,494 | 383,128 |
| Offsetting collections | (8,899) | (6,258) |
| Distributed offsetting receipts | (16,568) | (15,649) |
| **Net Outlays** | **$ 413,027** | **$ 361,221** |

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

## Consolidated Statements of Financing
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **RESOURCES USED TO FINANCE ACTIVITIES:** | | |
| **Budgetary Resources Obligated:** | | |
| Obligations Incurred | $ 445,551 | $ 388,662 |
| Less: Spending Authority from Offsetting Collections and Recoveries | (9,683) | (7,498) |
| **Obligations Net of Offsetting Collections and Recoveries** | **435,868** | **381,164** |
| Less: Offsetting Receipts | (16,568) | (15,649) |
| **Net Obligations** | **419,300** | **365,515** |
| **Other Resources:** | | |
| Donations and Forfeitures of Property | 61 | 51 |
| Accrued Interest & Discount on the Debt | 8,991 | 9,879 |
| Transfers In/Out Without Reimbursement | (24) | (133) |
| Imputed Financing Sources | 732 | 722 |
| Transfers to the General Fund and Other (Note 19) | (13,879) | (12,104) |
| **Net Other Resources Used to Finance Activities** | **(4,119)** | **(1,585)** |
| **Total Resources Used to Finance Activities** | **415,181** | **363,930** |
| **RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS:** | | |
| Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered but not yet Provided | 6,690 | 4,384 |
| Resources that Fund Expenses Recognized in Prior Periods | 117 | 432 |
| Budgetary Offsetting Collections and Receipts that do not Affect Net Cost of Operations: | | |
| Credit Program Collections that Increase Liabilities for Loan Guarantees or Allowances for Subsidy | (37) | (7) |
| Other (primarily non-exchange portion of offsetting receipts) | (15,515) | (15,677) |
| Resources that Finance the Acquisition of Assets or Liquidation of Liabilities | 1,013 | 522 |
| Adjustment to Accrued Interest & Discount on the Debt | 10,496 | 7,313 |
| Other Resources or Adjustments to Net Obligated Resources that do not Affect Net Cost of Operations | (326) | 2,060 |
| **Total Resources Used to Finance Items Not Part of the Net Cost of Operations** | **2,438** | **(973)** |
| **Total Resources Used to Finance the Net Cost of Operations** | **$ 412,743** | **$ 364,903** |

## Consolidated Statements of Financing
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Periods** | | |
| **Components of Net Cost of Operations Requiring or Generating Resources in Future Periods** | | |
| Increase in Annual Leave Liability | $ 20 | $ 9 |
| Upward Reestimates of Credit Subsidy Expense | (1) | 1 |
| Increase in Exchange Revenue Receivable from the Public | (2) | (2) |
| Other | 547 | 141 |
| **Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods** | **564** | **149** |
| **Components of Net Cost of Operations That Will Not Require or Generate Resources in the Current Periods** | | |
| Depreciation and Amortization | 554 | 612 |
| Revaluation of Assets or Liabilities | (51) | (714) |
| Other | 25 | (81) |
| **Total components of Net Cost of Operations that will not Require or Generate Resources** | **528** | **(183)** |
| **Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period** | **1,092** | **(34)** |
| **Net Cost of Operations** | **$ 413,835** | **$ 364,869** |

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

## Statements of Custodial Activity
## For the Years Ended September 30, 2006 and 2005
## (In Millions)

| | 2006 | 2005 |
|---|---|---|
| **SOURCES OF CUSTODIAL REVENUE (NOTE 22)** | | |
| **Revenue Received** | | |
| Individual Income and FICA Taxes | $2,034,209 | $1,864,687 |
| Corporate Income Taxes | 380,426 | 306,869 |
| Estate and Gift Taxes | 28,688 | 25,605 |
| Excise Taxes | 72,774 | 71,970 |
| Railroad Retirement Taxes | 4,673 | 4,539 |
| Unemployment Taxes | 7,533 | 6,948 |
| Deposit of Earnings, Federal Reserve System | 29,945 | 19,297 |
| Fines, Penalties, Interest & Other Revenue | 3,324 | 3,552 |
| **Total Revenue Received** | **2,561,572** | **2,303,467** |
| Less Refunds | (277,778) | (267,114) |
| **Net Revenue Received** | **2,283,794** | **2,036,353** |
| Accrual Adjustment | 554 | 643 |
| **Total Custodial Revenue** | **2,284,348** | **2,036,996** |
| **DISPOSITION OF CUSTODIAL REVENUE:** | | |
| Amounts Provided to Fund Non-Federal Entities | 374 | 454 |
| Amounts Provided to Fund the Federal Government (Note 22) | 2,283,420 | 2,035,899 |
| Accrual Adjustment | 554 | 643 |
| **Total Disposition of Custodial Revenue** | **2,284,348** | **2,036,996** |
| **Net Custodial Revenue** | **$ 0** | **$ 0** |

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

# Notes to the Financial Statements

## 1. Summary of Significant Accounting Policies

### *A. Reporting Entity*

The accompanying financial statements include the operations of the U.S. Department of the Treasury (Treasury Department), one of 25 Cabinet level agencies of the Executive Branch of the United States Government, and certain custodial activities managed on behalf of the entire U.S. Government. The following paragraphs describe the activities of the reporting entity.

The Treasury Department was created by Act (1 Stat. 65) on September 2, 1789. Many subsequent acts have affected the development of Treasury, delegating new duties to its charge and establishing the numerous bureaus and divisions that now comprise the Treasury Department. As a major policy advisor to the President, the Secretary has primary responsibility for formulating and managing the domestic and international tax and financial policies of the U.S. Government.

Further, the Secretary is responsible for recommending and implementing United States domestic and international economic and fiscal policy; governing the fiscal operations of the government; maintaining foreign assets control; managing the federal debt; collection of income and excise taxes; representing the United States on international monetary, trade and investment issues; overseeing Departmental overseas operations; and directing the activities of the Treasury Department in manufacturing coins, currency, and other products for customer agencies and the public.

The Treasury Department includes Departmental Offices (DO) and nine operating bureaus. For financial reporting purposes, DO is comprised of: International Assistance Programs (IAP), Office of Inspector General (OIG), Treasury Forfeiture Fund, Treasury Franchise Fund, Exchange Stabilization Fund (ESF), Community Development Financial Institutions Fund (CDFI), Office of D.C. Pensions (DCP), Treasury Inspector General for Tax Administration (TIGTA), the Federal Financing Bank (FFB) and the Air Transportation Stabilization Board (ATSB).

The Treasury Department's nine operating bureaus are: Office of the Comptroller of the Currency (OCC); Bureau of Engraving and Printing (BEP); Financial Crimes Enforcement Network (FinCEN); Financial Management Service (FMS); Internal Revenue Service (IRS); U.S. Mint (Mint); Bureau of the Public Debt (BPD); Office of Thrift Supervision (OTS), and the Alcohol and Tobacco Tax & Trade Bureau (TTB).

The Treasury Department's financial statements reflect the reporting of its own entity activities, which include appropriations it receives to conduct its operations and revenue generated from those operations. They also reflect the reporting of certain non-entity (custodial) functions it performs on behalf of the U.S. government and others. Non-entity activities include the collection of federal revenue, servicing the federal debt, disbursing certain federal funds, and maintaining certain assets and liabilities for the U.S. government as well as for others. The Treasury Department's reporting entity does not include the "General Fund" of the U.S. government, which maintains receipt, disbursement and appropriation accounts for all federal agencies.

Transactions and balances among the Treasury Department's entities have been eliminated from the Consolidated Balance Sheets, the Consolidated Statements of Net Cost, the Consolidated Statements of Changes in Net Position, and the Consolidated Statements of Financing.

### *B. Basis of Accounting & Presentation*

The financial statements have been prepared from the accounting records of the Treasury Department in conformity with accounting principles generally accepted in the United States, and the Office of Management and

Budget (OMB) Circular A-136, *"Financial Reporting Requirements,"* as amended. Accounting principles generally accepted for federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB). FASAB is recognized by the American Institute of Certified Public Accountants as the official accounting standards-setting body of the U.S. government.

These financial statements are provided to meet the requirements of the Government Management Reform Act of 1994. They consist of the consolidated Balance Sheets, the consolidated Statements of Net Cost, the consolidated Statements of Changes in Net Position, the combined Statements of Budgetary Resources, the consolidated Statements of Financing, and the Statement of Custodial Activity. The statements and the related notes are prepared in a comparative form to present both FY 2006 and FY 2005 information.

While these financial statements have been prepared from the books and records of the Treasury Department in accordance with the formats prescribed by OMB, these financial statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

Throughout these financial statements, intra-governmental assets, liabilities, earned revenues, and costs have been classified according to the entity for these transactions. Intra-governmental assets and liabilities are those from or to other federal entities. Intra-governmental earned revenues are collections or accruals of revenue from other federal entities, and intra-governmental costs are payments or accruals of expenditure to other federal entities.

The financial statements should be read with the realization that they are for a component of a sovereign entity, that liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

### *C. Tax and Other Non-Entity Receivables*

Tax receivables are not accrued until related tax returns are filed or assessments are made. Prepayments of taxes are netted against liabilities. Accruals are made to reflect penalties and interest on tax receivables through the balance sheet date. Tax receivables consist of unpaid assessments (taxes and associated penalties and interest) due from taxpayers for which the Treasury Department can support the existence of a receivable through taxpayer agreement, such as filing a tax return without sufficient payment, or a court ruling in favor of Treasury. Tax receivables are shown on the balance sheet net of an allowance for doubtful accounts and abatements. The allowance for doubtful accounts reflects an estimate of the portion deemed to be uncollectible based on historical experience of similar taxes receivable.

### *D. Inventory and Related Property*

Inventories and related property include inventory, operating materials and supplies, and forfeited property. The Treasury Department values inventories at either standard cost or lower of cost or market, except for finished goods inventories, which are valued at weighted average unit cost. All operating materials and supplies are recorded as an expense when consumed in operations.

Forfeited property is recorded at estimated fair market value at the time of seizure as deferred revenue, and may be adjusted to reflect the current fair market value at the end of the fiscal year. Property forfeited in satisfaction of a taxpayers liability is recorded when title to the property passes to the U.S. Government and a corresponding credit is made to the related taxes receivable. Direct and indirect holding costs are not capitalized for individual forfeited assets.

Mortgages and claims on forfeited assets are recognized as a valuation allowance and a reduction of deferred revenue from forfeited assets when the asset is forfeited. The allowance includes mortgages and claims on forfeited property held for sale and a minimal amount of claims on forfeited property previously sold.

Revenue from the forfeiture of property is deferred until the property is sold or transferred to a state, local or federal agency. Revenue is not recorded if the forfeited property is ultimately destroyed or cannot be legally sold.

### *E. Loans and Interest Receivable - from Other Federal Agencies*

Intra-governmental entity Loans and Interest Receivable from other federal agencies represent loans and interest receivable held by the Treasury Department. No subsidy costs were recorded for loans purchased from federal agencies or for guaranteed loans made to non-federal borrowers, because these are guaranteed (interest and principal) by those agencies.

Intra-governmental non-entity Loans and Interest Receivable from other federal agencies represent loans issued by Treasury to federal agencies on behalf of the U.S. government. The Treasury Department acts as an intermediary issuing these loans, because the agencies receiving these loans will lend these funds to others to carry out various programs of the Federal Government. Because of the Treasury Department's intermediary role in issuing these loans, the Treasury Department does not record an allowance or subsidy costs related to these loans. Instead, loan loss allowances and subsidy costs are recognized by the ultimate lender, the federal agency that issued the loans.

### *F. Advances to the Black Lung Trust Fund*

Advances have been provided to the Department of Labor's Black Lung Trust Fund from the General Fund of the U.S. Government. The Bureau of Public Debt accounts for the advances on behalf of the General Fund of the U.S. government. Advances to the Black Lung Trust Fund are being accounted for pursuant to the Benefits Revenue Act which states: In the event that fund resources are not adequate to meet fund obligations, then, Advances interest and principal are paid to the General Fund of the U.S. government when the Secretary of the Treasury determines that funds are available in the trust fund for such purposes. The Black Lung Trust Funds are repayable with interest at a rate determined by the Secretary of the Treasury to be equal to the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the anticipated period during which the advance will be outstanding. Advances made prior to 1982 carried rates of interest equal to the average rate borne by all marketable interest-bearing obligations of the United States then forming a part of the public debt.

### *G. Property, Plant, and Equipment*

The Treasury Department's property, plant, and equipment (PP&E) is recorded at cost and depreciated using the straight line method over the estimated useful lives of the assets. Major alterations and renovations are capitalized, while maintenance and repair costs are charged to expense as incurred. The Treasury Department owns the Treasury building — a multi-use heritage asset. Multi-use heritage assets are assets of historical significance for which the predominant use is general government operations. All acquisition, reconstruction, and betterment costs for the Treasury Department building are capitalized as general PP&E and depreciated over their service life.

The Treasury Department's bureaus are diverse both in size and in operating environment. Accordingly, Treasury's capitalization policy thresholds range from $25,000 to $50,000. Treasury also uses a capitalization threshold range for bulk purchases: $250,000 to $500,000 for non-manufacturing bureaus and $25,000 to $50,000 for manufacturing bureaus. Bureaus determine the individual items that comprised bulk purchases. In addition, the Treasury

Department's bureaus may expense bulk purchases if they conclude that total period costs would not be materially distorted and the cost of capitalization is not economically feasible.

### *H. Federal Debt*

Debt and associated interest are reported on the accrual basis of accounting. Certain debt securities are issued at a discount or premium. Discounts and premiums are amortized over the term of the security using the effective interest rate method.

### *I. Pension Costs, Other Retirement Benefits, and Other Post Employment Benefits*

The Treasury Department recognizes the full costs of its employees' pension benefits. However, the liabilities associated with these costs are recognized by the Office of Personnel Management (OPM) rather than Treasury.

Most employees of the Treasury Department hired prior to January 1, 1984, participate in the Civil Service Retirement System (CSRS), to which the Treasury Department contributes 8.51 % of salaries for regular CSRS employees.

On January 1, 1987, the Federal Employees' Retirement System (FERS) went into effect pursuant to Public Law 99-335. Employees hired after December 31, 1983, are automatically covered by FERS and Social Security. A primary feature of FERS is that it offers a savings plan to which the Treasury Department automatically contributes 1 % of base pay and matches any employee contributions up to an additional 4 % of base pay. For most employees hired after December 31, 1983, the Treasury Department also contributes the employer's matching share for Social Security. For the FERS basic benefit the Treasury Department contributes 10.7 % for regular FERS employees.

Similar to federal retirement plans, OPM, rather than the Treasury Department, reports the liability for future payments to retired employees who participate in the Federal Employees Health Benefits Program (FEHBP) and Federal Employees Group Life Insurance (FEGLI) Program. The Treasury Department reports the full cost of providing other retirement benefits (ORB). The Treasury Department also recognizes an expense and liability for other post employment benefits (OPEB), which includes all types of benefits provided to former or inactive (but not retired) employees, their beneficiaries, and covered dependents. Additionally, the Treasury Department's Office of the Comptroller of the Currency (OCC) and Office of Thrift Supervision (OTS) separately sponsor certain benefit plans for their employees. OCC sponsors a defined life insurance benefit plan for current and retired employees. Additionally, OTS provides certain health and life benefits for all retired employees that meet eligibility requirements.

### *J. Special Drawing Rights (SDRs) Certificates Issued to Federal Reserve Banks*

The Special Drawing Rights Act of 1968 authorized the Secretary of the Treasury to issue certificates, not to exceed the value of SDRs holdings, to the Federal Reserve Banks in return for interest free dollar amounts equal to the face value of certificates issued. The certificates may be issued to finance the acquisition of SDRs from other countries or to provide resources for financing other Exchange Stabilization Fund operations. Certificates issued are to be redeemed by the Treasury Department at such times and in such amounts as the Secretary of the Treasury may determine. Certificates issued to Federal Reserve Banks are stated at their face value. It is not practical to estimate the fair value of Certificates Issued to Federal Reserve Banks since these certificates contain no specific terms of repayment.

### *K. Federal Employee Benefits Payable - FECA Actuarial Liability*

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered Federal civilian employees injured on the job, and employees who have incurred a work-related injury or occupational disease. These future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases.

### *L. Revenue and Financing Sources*

The Treasury Department activities are financed either through exchange revenue it receives from others or through non-exchange revenue and financing sources (such as appropriations provided by the Congress and penalties, fines, and certain user fees collected). User fees primarily include Internal Revenue Service reimbursable costs to process installment agreements and accompanying photocopy and reproduction charges. Exchange revenues are recognized when earned; i.e. goods have been delivered or services have been rendered. Non-exchange revenues are recognized when received by the respective Treasury Department collecting bureau. Appropriations used are recognized as financing sources when related expenses are incurred or assets are purchased. Revenue from reimbursable agreements is recognized when the services are provided. The Treasury Department also incurs certain costs that are paid in total or in part by other federal entities, such as pension costs. These subsidized costs are recognized on the Consolidated Statement of Net Cost, and the imputed financing for these costs is recognized on the Consolidated Statement of Changes in Net Position. As a result, there is no effect on net position. Other non-exchange financing sources such as donations and transfers of assets without reimbursements also are recognized for the period in which they occurred on the Consolidated Statement of Changes in Net Position.

The Treasury Department recognizes revenue it receives from disposition of forfeited property as non-exchange revenue on the Consolidated Statement of Changes in Net Position. The costs related to the forfeiture fund program are reported on the Consolidated Statement of Net Cost.

### *M. Custodial Revenues and Collections*

Non-entity revenue reported on the Treasury Department's Statement of Custodial Activity includes cash collected and received by the Treasury Department, primarily taxes. It does not include revenue collected by other Federal agencies, such as user fees and other receipts, which are remitted for general operating purposes of the U.S. government or are earmarked for certain trust funds. The Statement of Custodial Activity is presented on the "modified accrual basis." Revenues are recognized as cash is collected. The Balance Sheets include an estimated amount for taxes receivable and payable to the General Fund of the U.S. government at September 30, 2006 and 2005.

### *N. Tax Assessments and Abatements*

Under Internal Revenue Code Section 6201, the Treasury Department is authorized and required to make inquiries, determinations, and assessments of all taxes which have not been duly paid (including interest, additions to the tax, and assessable penalties) under the law. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as from tax compliance programs, such as examination, under-reporter, substitute for return, and combined annual wage reporting. The Treasury Department also has authority to abate the paid or unpaid portion of an assessed tax, interest, and penalty. Abatements occur for a number of reasons and are a normal part of the tax administration process. Abatements may result in claims for refunds or a reduction of the unpaid assessed amount.

### *O. Permanent and Indefinite Appropriations*

Permanent and indefinite appropriations are used to disburse tax refunds, income tax credits, and child tax credits. These appropriations are not subject to budgetary ceilings established by Congress. Therefore, refunds payable at year end are not subject to funding restrictions. Refund payment funding is recognized as appropriations are used. Permanent indefinite authority for refund activity is not stated as a specific amount and is available for an indefinite period of time. Although funded through appropriations, refund activity, in most instances, is reported as a custodial activity of the Treasury Department, since refunds are, in substance, a custodial revenue-related activity resulting from taxpayer overpayments of their tax liabilities.

The Treasury Department also receives two permanent and indefinite appropriations related to debt activity. One is used to pay interest on the public debt securities; the other is used to redeem securities that have matured, been called, or are eligible for early redemption. These accounts are not annual appropriations; and do not have refunds. Debt activity appropriations are related to the Treasury Department's liability and would be reported on the Treasury Department's balance sheet. Permanent indefinite authority for debt activity is available for an indefinite period of time.

Additionally, the Treasury Department receives other permanent and indefinite appropriations to make certain payments on behalf of the U.S. government. These appropriations are provided to make payments to the Federal Reserve for services provided. They also include appropriations provided to make other disbursements on behalf of the U.S. government, including payments made to various individuals as the result of certain claims and judgments rendered against the United States.

### *P. Imputed Costs/Financing Sources*

U.S. government entities often receive goods and services from other U.S. government entities without reimbursing the providing entity for all the related costs. These constitute subsidized costs which are recognized by the receiving entity. An offsetting imputed financing source is also recognized by the receiving entity. The Treasury Department recognized imputed costs and financing sources in fiscal years 2006 and 2005 to the extent directed by the OMB, such as: employees' pension, post-retirement health and life insurance benefits; other post-employment benefits for retired, terminated, and inactive employees, which includes unemployment and workers compensation under the Federal Employee's Compensation Act; and losses in litigation proceedings.

### *Q. Reclassifications*

Certain 2005 balances have been reclassified to conform to the 2006 presentation. Beginning with fiscal year 2006, OMB revised its' format of the SF-133 as described in OMB Circular No. A-11 (as amended). In addition, the format of the Statement of Budgetary Resources (SBR) is based on the SF-133. The comparative fiscal year 2006 SBR includes fiscal year 2005 data that has been reclassified into the new fiscal year 2006 format.

### *R. Income Taxes*

As an agency of the Federal government, the Treasury Department is exempt from all income taxes imposed by any governing body, whether it is a federal, state, commonwealth, local, or foreign government.

### *S. Use of Estimates*

The Treasury Department has made certain estimates and assumptions relating to the reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent liabilities to prepare these financial statements. Actual results could differ from these estimates. Financial statement line items subject to estimates include tax receivables; depreciation; imputed costs; cost and earned revenue allocations; and, credit reform subsidy costs.

### *T . Credit Risk*

Credit risk is the potential, no matter how remote, for financial loss from a failure of a borrower or a counter party to perform in accordance with underlying contractual obligations. The Treasury Department takes on possible credit risk when it makes direct loans or credits to foreign entities or becomes exposed to institutions which engage in financial transactions with foreign countries. Given the history of the Treasury Department with respect to such exposure and the financial policies in place in the U. S. government and other institutions in which the United States participates, the Treasury Department has no expectation that credit losses will be incurred in the foreseeable future. The Treasury Department also takes on credit risk related to loan guarantees, committed but undisbursed direct loans and its Terrorism Risk Insurance Program. The extent of the risk assumed by the Treasury Department is described in more detail in the notes to the financial statements.

### *U. Liability for Loan Guarantees*

The Treasury Department operates a loan guarantee program administered by the Air Transportation Stabilization Board. The purpose of the program is to assist air carriers that suffered losses as a result of the terrorist attacks on the United States that occurred on September 11, 2001. The program is accounted for in accordance with the provisions of the Federal Credit Reform Act of 1990, as amended. The authority to issue loan guarantees expired on September 30, 2004. The Liability for Loan Guarantees represents the present value of future projected cash outflows from the Treasury Department, net of inflows, such as fees, and other collections. A subsidy cost for the liability for loan guarantees is recognized as a cost in the year the guaranteed loan is disbursed. Subsidy costs are an estimate of the long-term cost to the U.S. Government. The subsidy costs represent the calculation of the present value of the estimated cash outflows over the life of the loan guarantee minus the present value of the estimated cash inflows, discounted at the applicable Treasury Department interest rate. The subsidy cost is reestimated on an annual basis. Administrative costs such as salaries and contractual fees are not included in the subsidy cost.

Each air carrier has material cash flows that are not considered appropriate to average with those of other air carriers, with the result that each air carrier guarantee has its own subsidy rate. The fluctuations in subsidy rates for the respective air carriers depend upon several risk factors, including current credit rating and default rates. Other factors that may affect the estimated subsidy rates include changes in loan terms (modifications, prepayments, etc), appraised collateral/liquidation values, interest payments, outstanding balances and other economic, legal and financial conditions specific to each individual air carrier (see Note 15).

### *V. Earmarked Funds*

In 2006, Treasury has accounted for revenues and other financing sources for earmarked funds separately from other funds. This new method was adopted in accordance with the provisions of the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards (SFFAS) No. 27, *Identifying and Reporting Earmarked Funds*, which became effective October 1, 2006. This new standard amended SFFAS No. 7, *Revenue and Other Financing Sources*, by:

- elaborating the special accountability needs associated with dedicated collections;
- separating dedicated collections into two categories – earmarked funds and fiduciary activity; and
- defining and providing accounting and reporting guidance for earmarked funds.

In accordance with SFFAS No. 27, Treasury did not restate the FY 2005 columns for the Consolidated Balance Sheet, Statement of Changes in Net Position, and the related note disclosures. See Note 23 for the specific required disclosures related to Treasury's earmarked funds.

## 2. Fund Balance

Fund Balance with Treasury is the aggregate amount of the Treasury Department's accounts with the U.S. government's central accounts from which the Treasury Department is authorized to make expenditures and pay liabilities. It is an asset because it represents the Treasury Department's claim to the U.S. Government's resources. Fund balance with Treasury is not equivalent to unexpended appropriations, because it also includes non-appropriated revolving and enterprise funds, suspense accounts, and custodial funds such as deposit funds, special funds, and trust funds.

### *Fund Balances:*

As of September 30, 2006 and September 30, 2005, fund balances consisted of the following (in millions):

| | | 2006 | | 2005 |
|---|---|---|---|---|
| Appropriated Funds | $ | 68,748 | $ | 63,793 |
| Revolving Funds | | 1,539 | | 1,761 |
| Trust Funds | | 10 | | 0 |
| Clearing Funds | | 13 | | 0 |
| Deposit Funds | | 511 | | 457 |
| Special Funds | | 332 | | 315 |
| Other Funds | | 0 | | 8 |
| **Total Fund Balances** | **$** | **71,153** | **$** | **66,334** |

As of September 30, 2006 and September 30, 2005, the status of fund balances consisted of the following (in millions):

| Status of Fund Balance with Treasury | | 2006 | | 2005 |
|---|---|---|---|---|
| Unobligated Balance – Available | $ | 21,606 | $ | 30,479 |
| Unobligated Balance – Unavailable | | 10,447 | | 10,014 |
| Obligated Balance not yet Disbursed | | 52,369 | | 45,704 |
| **Subtotal** | | **84,422** | | **86,197** |
| Adjustment for Non-Budgetary Funds | | 525 | | 462 |
| Adjustment for Borrowing Authority | | (5,716) | | (5,720) |
| Adjustment for Intra-Treasury Investments | | (4,963) | | (4,732) |
| Adjustment for Imprest Funds | | (4) | | (4) |
| Adjustment for Other Budgetary Resources Not in Fund Balance - Cash & Other Assets | | (6,756) | | (13,427) |
| Authority Unavailable for Obligation | | 3,645 | | 3,558 |
| **Total Status of Fund Balance** | **$** | **71,153** | **$** | **66,334** |

The above balances do not include unobligated balances related to the Exchange Stabilization Fund (ESF). Accordingly, while ESF balances are included on the Statement of Budgetary Resources (SBR), they are not a component of the Fund Balance with the Treasury. The ESF balances displayed on the SBR includes components of cash, foreign currency, and other monetary assets (see Note 5).

At September 30, 2006 and September 30, 2005, the Treasury Department did not have any budgetary authority in fund balance that was specifically withheld from apportionment by OMB. The balances in non-entity funds, such as deposit funds, are being held in a fiduciary capacity by the Treasury Department for the public or for another federal entity, such as the General Fund of the U.S. government. Such funds have an offsetting liability equal to fund balance. See Note 8 regarding restrictions related to the International Monetary Fund. Restrictions on Funds related to the line of credit held on the U.S. Quota in the International Monetary Fund.

## 3. Loans and Interest Receivable

***Entity Intra-governmental:***

As of September 30, 2006 and September 30, 2005, intra-governmental loans (issued by the Federal Financing Bank) and interest receivable consisted of the following (in millions):

| | Loans Receivable | Interest Receivable | 2006 Total | Loans Receivable | Interest Receivable | 2005 Total |
|---|---|---|---|---|---|---|
| Executive Office of the President | $ 1,024 | $ 13 | $ 1,037 | $ 1,244 | $ 17 | $ 1,261 |
| Department of Agriculture | 25,283 | 281 | 25,564 | 22,806 | 1 | 22,807 |
| United States Postal Service | 2,100 | 0 | 2,100 | 0 | 0 | 0 |
| General Services Administration | 2,192 | 39 | 2,231 | 2,201 | 39 | 2,240 |
| Department of Housing & Urban Development | 884 | 107 | 991 | 972 | 118 | 1,090 |
| Department of Education | 155 | 2 | 157 | 126 | 1 | 127 |
| Department of Defense | 171 | 3 | 174 | 376 | 6 | 382 |
| Other agencies | 34 | 1 | 35 | 49 | 1 | 50 |
| **Subtotal – Entity** | **$ 31,843** | **$ 446** | **$ 32,289** | **$ 27,774** | **$ 183** | **$ 27,957** |

The Federal Financing Bank (Bank) issues the above loans to federal agencies for their own use or to private sector borrowers, whose loans are guaranteed by the federal agencies. When a federal agency has to honor its guarantee because a private sector borrower defaults, the federal agency that guaranteed the loan must obtain an appropriation or use other resources to repay the Bank. Loan principal and interest are backed by the full faith and credit of the U.S. government, except for loans to the U.S. Postal Service. The Bank has not incurred and does not expect to incur any credit-related losses on its loans and accordingly, has not recorded an allowance for uncollectible intra-governmental loans.

### *Non-Entity Intra-governmental*

| | Loans Receivable | Interest Receivable | 2006 Total | Loans Receivable | Interest Receivable | 2005 Total |
|---|---|---|---|---|---|---|
| Department of Agriculture | $ 57,760 | $ 427 | $ 58,187 | $ 60,385 | $ 323 | $ 60,708 |
| Department of Interior | 391 | 663 | 1,054 | 392 | 823 | 1,215 |
| Federal Communications Commission | 449 | 0 | 449 | 1,274 | 0 | 1,274 |
| Department of Veterans Affairs | 980 | 0 | 980 | 2,193 | (3) | 2,190 |
| Railroad Retirement Board | 2,958 | 72 | 3,030 | 2,973 | 69 | 3,042 |
| Small Business Administration | 9,303 | 0 | 9,303 | 7,695 | 0 | 7,695 |
| Department of Housing & Urban Development | 6,258 | 0 | 6,258 | 7,787 | 45 | 7,832 |
| Department of Energy | 2,482 | 3 | 2,485 | 2,777 | 13 | 2,790 |
| Department of Education | 105,522 | 0 | 105,522 | 104,471 | 2 | 104,473 |
| Export Import Bank of the U. S. | 4,911 | 0 | 4,911 | 5,848 | 0 | 5,848 |
| Other agencies | 20,379 | 359 | 20,738 | 3,459 | 8 | 3,467 |
| **Subtotal – Non-Entity** | **$ 211,393** | **$ 1,524** | **$ 212,917** | **$ 199,254** | **$ 1,280** | **$ 200,534** |
| **Total Intra-governmental Loans and Interest Receivable – Entity and Non-Entity** | | | **$ 245,206** | | | **$ 228,491** |

### *Entity and Non-Entity Non-Federal:*

As of September 30, 2006 and September 30, 2005, loans and interest receivable from non-federal entities consisted of the following (in millions):

| | Entity | Non-entity | 2006 Total | Entity | Non-entity | 2005 Total |
|---|---|---|---|---|---|---|
| Direct Loans | $ 142 | $ 133 | $ 275 | $ 187 | $ 464 | $ 651 |
| Interest Receivable | 0 | 87 | 87 | 0 | 142 | 142 |
| Less: Allowance and Subsidy Cost | (74) | 0 | (74) | (123) | 0 | (123) |
| **Total Non-Federal Loans and Related Interest Receivable** | **$ 68** | **$ 220** | **$ 288** | **$ 64** | **$ 606** | **$ 670** |

These amounts include certain loans and credits issued by the United States to various foreign governments. The agreements with each debtor government vary as to dates, interest rates, method of payment, and billing procedures. All such loans and credits represent legally valid and outstanding obligations of foreign governments, and the U.S. government has not waived or renounced its rights with respect to any of them. The loans are due and payable in U.S. denominations.

## 4. Due from the General Fund and Due to the General Fund

The Treasury Department is responsible for managing various assets and liabilities on behalf of the U.S. government as a whole. Due from the General Fund represents amounts required to fund liabilities managed by Treasury on behalf of the U.S. government. Liabilities managed by the Treasury Department are comprised primarily of the federal debt. Due to the General Fund represents assets held for the General Fund of the U.S. government.

As of September 30, 2006 and September 30, 2005, Due from and Due to the General Fund, included the following non-entity assets and liabilities (in millions):

| | | 2006 | | 2005 |
|---|---|---|---|---|
| **Liabilities Requiring Funding from the General Fund:** | | | | |
| Federal Debt and Interest Payable | $ | 4,844,074 | $ | 4,600,668 |
| Federal Debt and Interest Payable - Intra-governmental | | 3,673,117 | | 3,354,905 |
| Refunds Payable | | 1,701 | | 1,952 |
| Adjustment for Eliminated Liabilities | | 21,303 | | 20,556 |
| **Total Due From the General Fund** | **$** | **8,540,195** | **$** | **7,978,081** |
| **Assets to be Distributed to the General Fund:** | | | | |
| Fund Balance | $ | 224 | $ | 170 |
| Advances to the Black Lung Trust Fund | | 9,632 | | 9,186 |
| Cash Held by the Treasury for Government-wide Operations | | 44,090 | | 28,344 |
| Cash, Foreign Currency and Other Monetary Assets | | 68 | | 39 |
| Custodial Silver and Gold held by the U.S. Mint without certificates | | 25 | | 9 |
| Loans and Interest Receivable - Intra-governmental | | 212,917 | | 200,534 |
| Loans and Interest Receivable | | 220 | | 606 |
| Accounts Receivable - Intragovernmental | | 373 | | 501 |
| Tax and Other Non-Entity Receivables | | 21,819 | | 21,331 |
| Miscellaneous Assets | | 24 | | 162 |
| Adjustment for Eliminated Assets | | 16,960 | | 12,669 |
| **Total Due to the General Fund** | **$** | **306,352** | **$** | **273,551** |

The Adjustment for Eliminated Intra-Treasury liabilities mainly represents investments in U.S. Government securities held by Treasury reporting entities that were eliminated against Federal Debt and Interest Payable. The Adjustment for Eliminated Intra-Treasury assets mainly represents loans and interest payable owed by reporting entities that are consolidated with Treasury, which were eliminated against Loans and Interest Receivable held by the Bureau of the Public Debt.

On the Balance Sheet, Treasury reported $21,962 million in Tax, Other, and Related Interest Receivables as of September 30, 2006 ($21,430 million as of September 30, 2005). However, only $21,819 million is reported as due to the General Fund of the U.S. government ($21,331 million as of September 30, 2005). The difference is attributable to the exclusion of amounts which will be paid to others outside the U.S. Government, and miscellaneous entity receivables (see Note 10).

## 5. Cash, Foreign Currency, and Other Monetary Assets

Cash, foreign currency, and other monetary assets held as of September 30, 2006 and September 30, 2005 were as follows (in millions):

| | 2006 | 2005 |
|---|---|---|
| **Entity:** | | |
| Cash | $ 24 | $ 4 |
| Foreign Currency: | | |
| Japanese Yen | 2,622 | 2,719 |
| European Euro | 8,042 | 7,413 |
| Other | 0 | 14 |
| Other Monetary Assets: | | |
| Special Drawing Rights | 8,710 | 8,245 |
| Other | 135 | 227 |
| **Subtotal – Entity** | **19,533** | **18,622** |
| **Non-Entity:** | | |
| Operating Cash of the Federal Government | 43,587 | 27,857 |
| Foreign Currency | 68 | 89 |
| Other | 704 | 1,010 |
| **Subtotal - Non-Entity** | **44,359** | **28,956** |
| **Total Cash, Foreign Currency, and Other Monetary Assets** | **$ 63,892** | **$ 47,578** |

Non-entity Operating Cash & Other Cash of the U.S. Government held by Treasury disclosed above consisted of the following (in millions):

| | 2006 | 2005 |
|---|---|---|
| Operating Cash of the U.S. Government | $ 46,676 | $ 31,299 |
| Operating Cash - Federal Reserve Account | 5,569 | 4,509 |
| **Subtotal** | **52,245** | **35,808** |
| Outstanding Checks | (8,658) | (7,951) |
| **Total Operating Cash of the U.S. Government** | **43,587** | **27,857** |
| Other Miscellaneous Items | 503 | 487 |
| **Total Cash Held by the Treasury for Government-wide Operations (See Note 4)** | **$ 44,090** | **$ 28,344** |

### *Entity*

Entity cash, foreign currency, and other monetary assets primarily include Foreign Currency Denominated Assets (FCDA), Special Drawing Rights (SDRs), and forfeited cash. SDRs and FCDAs are valued as of September 30, 2006 and September 30, 2005, using current exchange rates plus accrued interest, at September 30, 2006 and 2005. "Other" includes U.S. dollars restricted for use by the International Monetary Fund (IMF), which are maintained in two accounts at the Federal Reserve Bank of New York. FCDAs represent Foreign Currency Agreements (swap agreements) between the Treasury Department and various countries that provide for drawing of dollars by those countries and/or drawing of foreign currency by the Treasury Department. The Treasury Department enters into these agreements through the Exchange Stabilization Fund.

The foreign currency holdings are normally invested in interest bearing securities issued by or held through foreign governments or monetary authorities. FCDAs with original maturities of three months or less, (except for foreign currencies under swap agreements with developing countries) were valued at $6.8 billion as of September 30, 2006 ($6.6 billion as of September 30, 2005). Other FCDAs with maturities greater than three months are also held and may at times include foreign currencies acquired under swap agreements with developing countries. As of September 30, 2006, FCDAs with maturities greater than three months were valued at $3.8 billion ($3.6 billion as of September 30, 2005).

The SDRs is an international reserve asset created by the IMF. It was created as a supplement to existing reserve assets and on several occasions SDRs have been allocated by the IMF to members participating in the IMF's SDRs department. The SDRs' value as a reserve asset derives, essentially, from the commitments of participants to hold and accept SDRs and to honor various obligations connected with its proper functioning as a reserve asset.

The Special Drawing Rights Act of 1968 authorizes the Secretary of Treasury to issue certificates, not to exceed the value of SDR holdings, to the Federal Reserve Bank in return for interest free dollar amounts equal to the face value of certificates issued. The certificates maybe issued for the purpose of financing the acquisition of SDRs from other countries or to provide resources for the financing of the Treasury Department's Exchange Stabilization Fund's activities. Certificates issued are to be redeemed by the Treasury Department at such times and in such amounts as the Secretary of the Treasury may determine. As of September 30, 2006, the value of the certificates issued to Federal Reserve Banks amounted to $2.2 billion ($2.2 billion as of September 30, 2005).

On a daily basis, the IMF calculates the value of the SDR using the market value, in terms of the U.S. dollar, from the amounts of each of four freely usable weighted currencies, as defined by the IMF. These currencies are the U.S. dollar, the European euro, the Japanese yen, and the British pound sterling. Treasury's SDR holdings (assets resulting from various SDR related activities including remuneration received on interest earned on the U.S. reserve position – see note 8) and allocations from the IMF (liabilities of the U.S. coming due only in the event of a liquidation of, or U.S. withdrawal from the SDR department of the IMF, or cancellation of SDRs) are revalued monthly based on the SDR valuation rate calculated by the IMF.

Pursuant to the IMF Articles of Agreement, SDRs allocated to or otherwise acquired by the United States are permanent resources unless:

a. canceled by the Board of Governors based on an 85% majority decision of the total voting power of the Executive Board of the IMF;
b. the SDR Department of the IMF is liquidated;
c. the IMF is liquidated; or
d. the United States chooses to withdraw from the IMF or terminate its participation in the SDR Department.

Except for the payment of interest and charges on SDRs allocations to the United States, the payment of the Treasury Department's commitment related to SDRs allocations is conditional on events listed above, in which the United States has a substantial or controlling voice. Allocations of SDRs were made on January 1, 1970, 1971, 1972, 1979, 1980 and 1981. Since 1981, the IMF has made no further allocations of SDRs. As of September 30, 2006, the amount of SDR holdings of the United States was the equivalent of $8.7 billion and the amount of SDR allocations to the United States was the equivalent of $7.2 billion. As of September 30, 2005, the amount of SDR holdings of the United States was the equivalent of $8.2 billion and the amount of SDR allocations to the United States was the equivalent of $7.1 billion.

During FY 2006, the Treasury Department received remuneration on the U.S. reserve position in the IMF, at the prevailing rates, in the amount of $210 million equivalent of SDRs ($316 million equivalent of SDRs during FY 2005), and paid the General Fund of the Federal Government $.5 million ($.5 million in FY 2005) in interest on these funds until they were transferred to the General Fund.

### *Non-Entity*

Non-entity cash, foreign currency, and other monetary assets include the Operating Cash of the U.S. government, managed by the Treasury Department. Also included is foreign currency maintained by various U.S. and military disbursing offices. It also includes seized monetary instruments, undistributed cash, and offers in compromises which are maintained as the result of the Treasury Department's tax collecting responsibilities.

The Operating Cash of the U.S. government represents balances from tax collections, other revenues, federal debt receipts, time deposits, and other various receipts net of checks outstanding, which are held in the Federal Reserve Banks, foreign and domestic financial institutions, and in U.S. Treasury tax and loan accounts at commercial banks.

The Operating Cash of the U.S. Government also includes other cash representing the balances of petty cash and funds held in other Federal agencies' books. With the passage of the Consolidated Appropriation Act of 2004, the Treasury Department received a permanent and indefinite appropriation to compensate banks for services rendered. Therefore, compensating balances and depository compensation securities accounts were closed. Operating Cash of the U.S. Government is either insured (for balances up to $100,000) by the Federal Deposit Insurance Corporation (FDIC) or collateralized by securities pledged by the depository institutions and held by the Federal Reserve Banks.

## 6. Gold & Silver Reserves, and Gold Certificates Issued to Federal Reserve Banks

The Treasury Department is responsible for safeguarding most of the U.S. government's gold and silver reserves in accordance with 31 USC 5117. The consolidated Balance Sheet also reflects the value of the gold being held in the Federal Reserve Bank of New York.

Gold reserves being held by the Treasury Department are offset by a liability for gold certificates issued by the Secretary of the Treasury to the Federal Reserve as provided in 31 USC 5117. Since 1934, Gold certificates have been issued in non-definitive or book-entry form to the Federal Reserve. The Treasury Department's liability incurred by issuing the Gold Certificates is limited to the gold being held by the Treasury Department at the legal standard value established by law. Upon issuance of gold certificates to the Federal Reserve, the proceeds from the certificates are deposited into the operating cash of the U.S. government. All of the Treasury Department's certificates issued are payable to the Federal Reserve.

Gold and silver reserves are reported at the statutory rates of $42.2222 per fine troy ounce (FTO) for gold and $1.292929292 per FTO for silver for the entire custodial reserves, which are in the custody of the U.S. Mint and the Federal Reserve Bank of New York. As of September 30, 2006 and September 30, 2005, the gold and silver reserves consisted of the following (in millions):

| | FTOs | Statutory Rate | 9/30/06 Statutory Value | Market Rate | 9/30/06 Market Value |
|---|---|---|---|---|---|
| Gold | 248,046,116 | $ 42.2222 | $ 10,473 | $ 599.25 | $ 148,642 |
| Gold Held by Federal Reserve | 13,452,784 | 42.2222 | 568 | 599.25 | 8,062 |
| **Subtotal - Gold** | **261,498,900** | | **$ 11,041** | | **156,704** |
| Silver | 16,000,000 | $ 1.292929292 | 21 | $ 11.55 | 185 |
| **Total Gold and Silver Reserves** | | | **$ 11,062** | | **$ 156,889** |

| | FTOs | Statutory Rate | 9/30/05 Statutory Value | Market Rate | 9/30/05 Market Value |
|---|---|---|---|---|---|
| Gold | 245,262,897 | $ 42.2222 | $ 10,356 | $ 473.25 | $ 116,071 |
| Gold Held by Federal Reserve | 13,450,413 | 42.2222 | 568 | 473.25 | 6,366 |
| **Subtotal - Gold** | **258,713,310** | | **10,924** | | **122,437** |
| Silver | 7,075,171 | $ 1.292929292 | 9 | $ 7.53 | 53 |
| **Total Gold and Silver Reserves** | | | **$ 10,933** | | **$ 122,490** |

## 7. Investments and Related Interest

Investments in U.S. government Securities held by the Treasury Department entities have been eliminated against the federal debt liability for financial reporting purposes (See Note 4). The Exchange Stabilization Fund holds most of the Treasury Department's other investments. Securities that the Treasury Department has both the positive intent and ability to hold to maturity are classified as investment securities held to maturity and are carried at historical cost, adjusted for amortization of premiums and accretion of discounts. Foreign investment holdings are normally invested in interest bearing securities issued or held through foreign governments or monetary authorities (see Note 5). As of September 30, 2006 and September 30, 2005, entity investments consisted of the following (in millions):

| Type of Investment | Cost/ Acquisition Value | Unamortized (Premium)/ Discount | Net Investment | Interest Receivable | 9/30/06 Investment Balance | 9/30/06 Market Value |
|---|---|---|---|---|---|---|
| Euro Bonds | $ 3,713 | $ 68 | $ 3,781 | $ 102 | $ 3,883 | $ 3,873 |
| Japanese Government Bond | 5,386 | 4 | 5,390 | 4 | 5,394 | 5,386 |
| Other Investments | 53 | (5) | 48 | 0 | 48 | 0 |
| **Total Non-Federal** | **$ 9,152** | **$ 67** | **$ 9,219** | **$ 106** | **$ 9,325** | **$ 9,259** |

| Type of Investment | | Cost/ Acquisition Value | | Unamortized (Premium)/ Discount | | Net Investment | | Interest Receivable | | 9/30/05 Investment Balance | | 9/30/05 Market Value |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Euro Bonds | $ | 3,398 | $ | 95 | $ | 3,493 | $ | 104 | $ | 3,597 | $ | 3,677 |
| Japanese Financing Bills | | 874 | | 0 | | 874 | | 0 | | 874 | | 873 |
| Japanese T Bills | | 1,986 | | 0 | | 1,986 | | 0 | | 1,986 | | 1,986 |
| Japanese Government Bond | | 2,751 | | 8 | | 2,759 | | 0 | | 2,759 | | 2,756 |
| Other | | 191 | | (3) | | 188 | | 0 | | 188 | | 188 |
| **Total Non-Federal** | **$** | **9,200** | **$** | **100** | **$** | **9,300** | **$** | **104** | **$** | **9,404** | **$** | **9,480** |

## 8. Reserve Position in the International Monetary Fund

The United States participates in the IMF through a quota subscription. Quota subscriptions are paid partly through the transfer of reserve assets, such as foreign currencies or SDRs, which are international reserve currency assets created by the IMF, and partly by making domestic currency available as needed through a non-interest-bearing letter of credit. This letter of credit, issued by the Treasury Department and maintained by the Federal Reserve Bank of New York (FRBNY), represents the bulk of the IMF's holdings of dollars. Approximately one quarter of 1 % of the U.S. quota is maintained in cash balances in an IMF account at FRBNY.

While resources for transactions between the IMF and the United States are appropriated, they do not result in net budgetary outlays. This is because U.S./IMF quota transactions constitute an exchange of monetary assets in which the United States receives an equal offsetting claim on the IMF in the form of an increase in the U.S. reserve position in the IMF, which is interest-bearing and can be drawn at any time for balance of payments needs. When the IMF draws dollars from the letter of credit to finance its operations and expenses, the drawing does not represent a net budget outlay on the part of the United States because there is a commensurate increase in the U.S. reserve position. When the IMF repays dollars to the United States, no net budget receipt results because the U.S. reserve position declines concurrently in an equal amount.

As of September 30, 2006, the U.S. quota in the IMF was 37.1 billion SDRs, valued at approximately $54.8 billion. (The quota as of September 30, 2005 was 37.1 billion SDRs, valued at approximately $53.8 billion.) The quota consisted of the following (in millions):

| | | 2006 | | 2005 |
|---|---|---|---|---|
| Letter of Credit /1 | $ | 48,090 | $ | 40,419 |
| U.S. Dollars Held in Cash by the IMF /1 | | 135 | | 181 |
| Reserve Position /2 | | 6,621 | | 13,247 |
| **U.S Quota in the IMF** | **$** | **54,846** | **$** | **53,847** |

1/ *This amount is included in entity appropriated funds under Note 2, Fund Balance with Treasury, and unexpended appropriations – Obligations/Undelivered orders.*

2/ *This amount is included in the Cumulative Results of Operations.*

The U.S. reserve position is denominated in SDRs, as is the U.S. quota. Consequently fluctuations in the value of the dollar with respect to the SDR results in valuation changes in dollar terms for the U.S. reserve position in the

IMF as well as the IMF letter of credit. The Treasury Department periodically adjusts these balances to maintain the SDR value of the U.S. quota and records the change as a deferred gain or loss in its cumulative results of operations. These adjustments, known as maintenance of value adjustments, are settled annually after the close of the IMF financial year on April 30. Such adjustments do not involve a flow of funds. At April 30, 2006, the annual settlement with the IMF resulting from the appreciation of the dollar against the SDR since April 30, 2005, called for an downward adjustment of the U.S. quota by $1.057 billion (at April 30, 2005, the depreciation of the dollar against the SDR since April 30, 2004, called for an upward adjustment of the U.S. quota by $1.523 billion) and a corresponding increase to Unexpended Appropriations on the Statement of Changes in Net Position. The dollar balances shown above for the U.S. quota include accrued valuation adjustments. At September 30, 2006, the Treasury Department recorded a net deferred valuation gain in the amount of $76.9 million ($54.1 million valuation loss as of September 30, 2005) for deferred maintenance of value adjustments needed at year end.

The United States earns "remuneration" (interest) on its reserve position in the IMF except for the portion of the reserve position originally paid in gold. Remuneration is paid quarterly and is calculated on the basis of the SDR interest rate. (The SDR interest rate is a market-based interest rate determined on the basis of a weighted average of interest rates on short-term instruments in the markets of the currencies included in the SDR valuation basket.) Payment of a portion of this remuneration is deferred as part of a mechanism for creditors and debtors to share the financial consequences of overdue obligations to the IMF, such as unpaid overdue interest, and to similarly share the burden of establishing any contingency accounts deemed necessary to reflect the possibility of non-repayment of relevant principal amounts. As overdue interest is paid, previously deferred remuneration corresponding to the creditors' share of the burden of earlier nonpayment is included in the next payment of remuneration. The deferred remuneration corresponding to the creditors' share of establishing the contingency accounts is usually paid when there are no longer any relevant overdue obligations or when the IMF Executive Board determines to pay the remuneration. There was $3 million deducted in the remuneration paid by the IMF as a result of burden-sharing during FY 2006. There were no deductions in the remuneration paid by the IMF as a result of burden-sharing during FY 2005. For FY 2006 and 2005, the Treasury Department received $210 million and $316 million as remuneration (see note 5).

In addition to quota subscriptions, the IMF maintains borrowing arrangements to supplement its resources in times of crisis when IMF liquidity is low. The United States currently participates in two such arrangements – the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB). There were no U.S. loans outstanding under these arrangements in FY 2006 and FY 2005. The dollar equivalent of SDR 6.7 million has been appropriated to finance U.S. participation in the GAB and NAB; as of September 30, 2006, and September 30, 2005, this amounted to $9.9 billion and $9.7 billion, respectively, in standing appropriations available for lending through the GAB or NAB as needed. As is the case for the U.S. quota in the IMF, budgetary treatment of U.S. participation in the GAB and NAB does not result in net budgetary outlays, since transactions under the GAB or NAB result in concurrent adjustments to the U.S. reserve position in the IMF.

## 9. Investments in International Financial Institutions

The Treasury Department participates in Multilateral Development Banks (MDBs) to support poverty reduction, private sector development, transition to market economies and sustainable economic growth and development, thereby advancing United States' economic, political, and commercial interests abroad. The MDBs consist of the World Bank Group (International Bank for Reconciliation & Development, International Finance Corporation, and Multilateral Investment Guarantee Agency), and five regional development banks (the African, Asian, European, Inter-American, and North American institutions), as enumerated in the table below. These investments are non-marketable equity investments valued at cost.

As of September 30, 2006 and September 30, 2005, investments in international financial institutions consisted of the following (in millions):

| | 2006 | 2005 |
|---|---|---|
| African Development Bank | $ 168 | $ 165 |
| Asian Development Bank | 458 | 458 |
| European Bank for Reconstruction & Development | 611 | 593 |
| Inter-American Development Bank | 1,477 | 1,475 |
| International Bank for Reconstruction & Development | 1,985 | 1,985 |
| International Finance Corporation | 569 | 569 |
| Multilateral Investment Guarantee Agency | 45 | 44 |
| North American Development Bank | 175 | 175 |
| **Total** | **$ 5,488** | **$ 5,464** |

Refer to Note 17 for a description of the contingent liability related to these institutions.

## 10. Accounts Receivable and Related Interest

### *A. Tax, Other, and Related Interest Receivables, Net*

Tax, other, and related interest receivables include receivables from tax assessments, excise taxes, fees, penalties, and interest assessed and accrued that were not paid or abated, reduced by an estimate for uncollectible amounts. Also included is interest income due on monies deposited in Federal Reserve Banks.

As of September 30, 2006 and September 30, 2005, tax, other, and related interest receivables, net, consisted of the following (in millions):

| **Non-Entity:** | 2006 | 2005 |
|---|---|---|
| IRS Federal Tax Receivable, Gross | $ 91,018 | $ 88,019 |
| Less Allowance on Taxes Receivable | (70,008) | (67,008) |
| Receivable, Deposit of Earnings, Federal Reserve | 774 | 312 |
| Other Receivable & Interest | 47 | 20 |
| Less: Allowance on Other & Related Interest Receivable | (6) | (6) |
| **Total Tax, and Other Non-Entity Receivables, Net** | **$ 21,825** | **$ 21,337** |
| **Entity: Miscellaneous Entity Receivables & Related Interest** | **137** | **93** |
| **Total Tax, Other & Related Interest Receivables, Net** | **$ 21,962** | **$ 21,430** |

IRS federal taxes receivable constitute the largest portion of the receivables. IRS federal taxes receivable consists of tax assessments, penalties, and interest which were not paid or abated, and which were agreed to by either the taxpayer and IRS, or the courts. An allowance for doubtful accounts is established for the difference between the gross receivables and the portion deemed collectible. The portion of tax receivables estimated to be collectible and the allowance for doubtful accounts are based on projections of collectability from a statistical sample of taxes receivable. The Treasury Department does not establish an allowance for the receivable on deposits of Federal Reserve earnings.

### *B. Intra-governmental Accounts and Related Interest Receivable*

Intra-governmental accounts receivable and interest mainly represents non-entity payments made by the Treasury Department under the Contract Disputes Act ($366 million of the $483 million and $501 million of the $626 million displayed for 2006 and 2005, respectively). Unlike Judgment Fund payments, other federal agencies are required to reimburse the Treasury Department for payments made to contractors or federal employees, on their behalf, under the Act. These amounts remain a receivable on the Treasury Department's books of the Financial Management Service and a payable on the other federal agencies' books until reimbursement is made. The remaining amount displayed as intra-governmental accounts receivable and interest is related to miscellaneous intra-governmental transactions.

## 11. Inventory and Related Property, Net

Inventory and related property includes inventory, operating materials and supplies, and forfeited property held by Treasury. The Treasury Department's operating materials and supplies are maintained for the production of bureau products. The Treasury Department maintains inventory accounts or balances (e.g., metals, paper, etc.) for use in manufacturing currency and coins. The cost of these items is included in inventory costs, and is recorded as cost of goods sold upon delivery to customers. Inventory for check processing activities is also maintained.

As of September 30, 2006 and September 30, 2005, inventory and related property consisted of the following (in millions):

| | | 2006 | | 2005 |
|---|---|---|---|---|
| Operating materials and supplies held for use | $ | 15 | $ | 16 |
| Operating materials and supplies held in reserve for future use | | 23 | | 22 |
| Forfeited property | | 59 | | 57 |
| Other related property | | 304 | | 388 |
| Total allowance for inventories and related property | | (12) | | (15) |
| **Total Inventories and Related Property** | **$** | **389** | **$** | **468** |

## 12. Property, Plant, and Equipment, Net

As of September 30, 2006 and 2005, plant, property, and equipment consisted of the following (in millions):

| | Depreciation Method | Service Life | Cost | Accumulated Depreciation | 2006 Net Book Value |
|---|---|---|---|---|---|
| Buildings, structures and facilities | S/L | 3 - 50 years | $ 642 | $ (249) | $ 393 |
| Furniture, fixtures and equipment | S/L | 2 - 20 years | 3,182 | (2,317) | 865 |
| Construction in progress | N/A | N/A | 14 | 0 | 14 |
| Land and land improvements | N/A | N/A | 12 | 0 | 12 |
| ADP software | S/L | 2 - 10 years | 1,027 | (431) | 596 |
| Assets under capital lease | S/L | 2 - 25 years | 22 | (7) | 15 |
| Leasehold improvements | S/L | 2 - 25 years | 487 | (292) | 195 |
| Other | S/L | 2 - 30 years | 92 | 0 | 92 |
| **Total** | | | **$ 5,478** | **$ (3,296)** | **$ 2,182** |

| | Depreciation Method | Service Life | Cost | Accumulated Depreciation | 2005 Net Book Value |
|---|---|---|---|---|---|
| Buildings, structures and facilities | S/L | 3 - 50 years | $ 583 | $ (216) | $ 367 |
| Furniture, fixtures and equipment | S/L | 2 - 20 years | 2,602 | (1,796) | 806 |
| Construction in progress | N/A | N/A | 172 | 0 | 172 |
| Land and land improvements | N/A | N/A | 11 | 0 | 11 |
| ADP software | S/L | 2 - 10 years | 901 | (285) | 616 |
| Assets under capital lease | S/L | 2 - 25 years | 86 | (48) | 38 |
| Leasehold improvements | S/L | 2 - 25 years | 461 | (245) | 216 |
| Other | S/L | 2 - 30 years | 584 | (412) | 172 |
| **Total** | | | **$ 5,400** | **$ (3,002)** | **$ 2,398** |

The Treasury Department leases land and buildings from the General Services Administration (GSA) to conduct most of its operations. GSA charges a standard level users fee which approximates commercial rental rates for similar properties. The service life ranges are large due to the Treasury Department's diversity of held plant, property, and equipment.

### *Stewardship Property*

The Treasury Department Complex (Main Treasury Building and Annex) was declared a national historical landmark in 1972. The Treasury Department Complex is treated as a multi-use heritage asset and is expected to be preserved indefinitely.

## 13. Non-Entity Assets

As of September 30, 2006 and September 30, 2005, non-entity assets consisted of the following (in millions):

| | | 2006 | | 2005 |
|---|---|---|---|---|
| **Intra-governmental Assets:** | | | | |
| Fund Balance (Note 2) | $ | 753 | $ | 776 |
| Loans and Interest Receivable (Note 3) | | 212,917 | | 200,534 |
| Accounts Receivable and Related Interest (Note 10) | | 372 | | 501 |
| Advances to the Black Lung Trust Fund (Note 4) | | 9,632 | | 9,186 |
| Due from the General Fund (Note 4) | | 8,540,195 | | 7,978,081 |
| **Total Non-Entity Intra-governmental Assets** | **$** | **8,763,869** | **$** | **8,189,078** |
| | | | | |
| Cash, Foreign Currency and Other Monetary Assets (Note 5) | $ | 44,359 | $ | 28,956 |
| Gold & Silver Reserves (Note 6) | | 11,062 | | 10,933 |
| Loans and Interest Receivable (Note 3) | | 220 | | 606 |
| Tax, Other, and Related Interest Receivables, Net (Note 10) | | 21,825 | | 21,337 |
| Miscellaneous Assets | | 11 | | 161 |
| **Total Non-Entity Assets** | **$** | **8,841,346** | **$** | **8,251,071** |

Non-entity assets are those that are held by the Treasury Department but are not available for use by the Treasury Department. Non-entity fund balance with Treasury represents unused balances of appropriations received by various Treasury Department entities to conduct custodial operations such as the payment of interest on the Federal debt and refunds of taxes and fees. Non-entity loans and interest receivable represents loans managed by the Treasury Department on behalf of the U.S. government. These loans are provided to federal agencies, and the Treasury Department is responsible for collecting these loans and transferring the proceeds to the General Fund of the U.S. government. Non-entity cash, foreign currency, and other monetary assets include the operating cash of the U.S. government, managed by the Treasury Department. It also includes foreign currency maintained by various U.S. and military disbursing offices, as well as seized monetary instruments.

## 14. Federal Debt & Interest Payable

The Treasury Department is responsible for administering the federal debt on behalf of the U.S. government. The federal debt includes borrowings from the public as well as borrowings from federal agencies. The federal debt managed by the Treasury Department does not include debt issued by other governmental agencies such as the Tennessee Valley Authority, or the Department of Housing and Urban Development. The federal debt as of September 30, 2006 and September 30, 2005 was as follows (in millions):

| Intra-governmental | FY 2006 | FY 2005 |
|---|---|---|
| Beginning Balance | $ 3,297,110 | $ 3,056,484 |
| New Borrowings/Repayments | 331,591 | 240,626 |
| **Subtotal at Par Value** | **3,628,701** | **3,297,110** |
| Premium/(Discount) | (1,262) | 14,597 |
| Interest Payable Covered by Budgetary Resources | 45,678 | 43,198 |
| **Total** | **$ 3,673,117** | **$ 3,354,905** |

| Owed to the Public | FY 2006 | FY 2005 |
|---|---|---|
| Beginning Balance | $ 4,601,239 | $ 4,307,345 |
| New Borrowings/Repayments | 241,882 | 293,894 |
| **Subtotal at Par Value** | **4,843,121** | **4,601,239** |
| Premium/Discount | (40,165) | (35,532) |
| Interest Payable Covered by Budgetary Resources | 41,118 | 34,961 |
| **Total** | **$ 4,844,074** | **$ 4,600,668** |

Debt held by the public approximates the U.S. government's competition with other sectors in the credit markets. In contrast, debt held by federal entities, primarily trust funds, represents the cumulative annual surpluses of these funds (i.e. excess of receipts over disbursements plus accrued interest) that have been used to finance general government operations.

### *Federal Debt held by Other Federal Agencies*

Certain federal agencies are allowed to invest excess funds in debt securities issued by the Treasury Department on behalf of the U.S. government. The terms and the conditions of debt securities issued are designed to meet the cash needs of the U.S. government. The vast majority is non-marketable securities issued at par value, but some are issued at market prices whose prices and interest rates reflect market terms. The average interest rate for debt held by the federal entities in FY 2006 was 5.2 % (5.2 % in FY 2005).

The federal debt also includes intra-governmental marketable debt securities that certain agencies are permitted to buy and sell on the open market. The debt, at par value (not including interest receivable), owed to federal agencies as of September 30, 2006 and September 30, 2005 was as follows (in millions):

| | FY 2006 | FY 2005 |
|---|---|---|
| Social Security Administration* | $ 1,995,307 | $ 1,809,422 |
| Office of Personnel Management* | 722,042 | 688,767 |
| Department of Defense Agencies | 259,961 | 234,916 |
| Department of Health and Human Services | 337,659 | 296,658 |
| All Other Federal Entities - Consolidated | 313,732 | 267,347 |
| **Total Federal Debt Held by Federal Entities** | **$ 3,628,701** | **$ 3,297,110** |

*The above balances do not include premium/discount and interest payable.*

*These amounts include marketable Treasury securities as well as non-marketable debt securities as follows (in millions):

| | Non-Marketable Debt Securities | Marketable Securities | 2006 Total |
|---|---|---|---|
| Civil Service Retirement and Disability Fund, Par Value | $ 675,936 | $ 0 | $ 675,936 |
| Federal Disability Insurance Trust Fund, Par Value | $ 202,178 | $ 0 | $ 202,178 |

| | Non-Marketable Debt Securities | Marketable Securities** | 2005 Total |
|---|---|---|---|
| Civil Service Retirement and Disability Fund, Par Value | $ 646,750 | $ 0 | $ 646,750 |
| Federal Disability Insurance Trust Fund, Par Value | $ 193,263 | $ 0 | $ 193,263 |

*** The marketable securities were called on February 15, 2005, and the proceeds were rolled over as investments in GAS securities.*

### *Federal Debt Held by the Public*

As of September 30, 2006 and September 30, 2005, Federal Debt held by the Public consisted of the following:

| (at par value, in millions) | Term | Average Interest Rates | 2006 |
|---|---|---|---|
| **Marketable:** | | | |
| Treasury Bills | 1 Year or Less | 5.0% | $ 908,474 |
| Treasury Notes | Over 1 Year - 10 Years | 4.2% | 2,445,307 |
| Treasury Bonds | Over 10 Years | 7.6% | 534,473 |
| Treasury Inflation Protected Security (TIPS) | 5 Years or More | 2.3% | 395,550 |
| **Total Marketable** | | | **$ 4,283,804** |
| Non-Marketable | On Demand to Over 10 Years | 5.0% | 559,317 |
| **Total Federal Debt (Public)** | | | **$ 4,843,121** |

| (at par value, in millions) | Term | Average Interest Rates | 2005 |
|---|---|---|---|
| **Marketable:** | | | |
| Treasury Bills | 1 Year or Less | 3.4% | $ 910,323 |
| Treasury Notes | Over 1 Year - 10 Years | 3.7% | 2,328,212 |
| Treasury Bonds | Over 10 Years | 7.9% | 520,507 |
| Treasury Inflation Protected Security (TIPS) | 5 Years or More | 2.4% | 307,011 |
| **Total Marketable** | | | **$ 4,066,053** |
| Non-Marketable | On Demand to Over 10 Years | 4.9% | 535,186 |
| **Total Federal Debt (Public)** | | | **$ 4,601,239** |

*The above balances do not include premium/discount and interest payable.*

The Treasury Department issues marketable bills at a discount and pays the par amount of the security upon maturity. The average interest rate on Treasury bills represents the original issue effective yield on securities outstanding as of September 30, 2006 and 2005, respectively. Treasury bills are issued with a term of one year or less.

The Treasury Department issues marketable notes and bonds as long-term securities that pay semi-annual interest based on the securities' stated interest rates. These securities are issued at either par value or at an amount that reflects a discount or a premium. The average interest rate on marketable notes and bonds represents the stated interest rate adjusted by any discount or premium on securities outstanding as of September 30, 2006 and 2005. Treasury notes are issued with a term of over one year to 10 years and Treasury bonds are issued with a term of more than 10 years. The Treasury Department also issues inflation–protected securities (TIPS) that have interest and redemption payments, which are tied to the Consumer Price Index, the leading measurement of inflation. TIPS are issued with a term of 5 years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal.

### *Other Debt and Interest Payable*

Borrowings outstanding are with the Civil Service Trust Fund, which is administered by the Office of Personnel Management. The interest rates on these borrowings range from 4.62% to 5.62%, and the maturity dates range from June 30, 2009 to June 30, 2019. Borrowings began in 2005.

## 15. Liability for Loan Guarantee

The liability for loan guarantees is associated with the Air Transportation Stabilization Program which guarantees loans to assist air carriers that suffered losses as a result of the terrorist attacks on the United States that occurred on September 11, 2001. In FY 2005 the guaranteed loan with Aloha airlines was repaid. In FY 2006 the guaranteed loans with US Airways and America West were sold to private investors and World Airlines fully repaid the remaining balance of its guaranteed loan.

Liabilities for loan guarantees represent the present value of future projected cash outflows from the Department, net of inflows, such as fees, and other collections. The modification that occurred in FY 2006 was related to the merger and subsequent exit from the program of US Airways and American Airlines. Related details for FY 2006 and 2005 are provided below.

| | 2006 | 2005 |
|---|---|---|
| **Loans Guaranteed** | | |
| Face value of loans outstanding | $ 0 | $ 879 |
| Amount guaranteed by the government | 0 | 799 |
| **Defaulted Guaranteed Loans** | | |
| Loan amount | $ 2 | $ 125 |
| Subsidy transferred from liability | 0 | 103 |
| Subsidy reestimate | (22) | (3) |
| **Subsidy Expense** | | |
| Components of Current Year Subsidy: | | |
| Re-estimates | $ (40) | $ (143) |
| Modifications | (537) | 0 |
| **Administrative Expenses** | $ 3 | $ 5 |

| **Schedule for Reconciling Loan Guarantee Liability Balances:** | **2006** | **2005** |
|---|---|---|
| Beginning balance of the liability for loan guarantee liability | $ 555 | $ 724 |
| Other subsidy costs | 0 | 0 |
| | **555** | **724** |
| Payment of defaulted loan | 0 | (124) |
| Loan guarantee modifications | (537) | 0 |
| Net defaulted loan assets | 0 | 22 |
| Fees received | 5 | 69 |
| Interest accumulation on the liability balance | 0 | 7 |
| Loan Asset Sale Expense | (5) | 0 |
| **Ending balance of the loan guarantee liability before reestimates** | **18** | **698** |
| Reestimate of subsidy** | (18) | (143) |
| **Ending balance of loan guarantee liability*** | **$ 0** | **$ 555** |

**This amount is included in "Other Liabilities with the Public" (Note 18).*
***The reduction in the subsidy expense in FY 2006 is associated with two guaranteed loans that were paid off.*

## 16. D.C. Pensions Actuarial Liability

Pursuant to Title XI of the Balanced Budget Act of 1997, as amended (the Act), on October 1, 1997, Treasury became responsible for certain District of Columbia retirement plans. The Act was intended to relieve the District of Columbia Government of the burden of unfunded pension liabilities transferred to the District by the U.S. government in 1979. Prior to December 23, 2004, the Act established the District of Columbia Federal Pension Liability Trust Fund (the Trust Fund), the District of Columbia Judicial Retirement and Survivors Annuity Fund (the Judicial Retirement Fund), and the Federal Supplemental District of Columbia Pension Fund (the Supplemental Fund).

The purpose of the Trust Fund was to make federal benefit payments and pay necessary administrative expenses for the District of Columbia Police Officers', Firefighters', and Teachers' Retirement Plans for benefits earned based upon service on or before June 30, 1997. The purpose of the Judicial Retirement Fund was to make federal benefit payments and pay necessary administrative expenses of the Judges' Retirement Plan for all benefits earned. The purpose of the Supplemental Fund was to accumulate funds to finance federal benefit payments and necessary administrative expenses for the Police Officers', Firefighters', and Teachers' Retirement Plans after funds in the Trust Fund were depleted.

On December 23, 2004, the President signed into law the District of Columbia Retirement Protection Improvement Act of 2004. This amendment to the Act terminated the Trust Fund and the Supplemental Fund and transferred the assets to the D.C. Teachers, Police Officers and Firefighters Federal Pension Fund (the D.C. Federal Pension Fund) effective as of October 1, 2004.

The Treasury Department is required to make annual amortized payments from the General Fund of the U.S. government to the D.C. Federal Pension Fund and Judicial Retirement Fund. The amount paid into the D.C. Federal Pension Fund from the General Fund of the U.S. government was $285.4 million during FY 2006 ($277 million during FY 2005). The amount paid into the Judicial Retirement Fund from the General Fund of the U.S. government was $7.4 million during FY 2006 ($7.0 million during FY 2005).

As of September 30, 2006, the unobligated budgetary resources of the two funds were approximately $3.6 billion, and the pension actuarial liability was $9.0 billion, resulting in an unfunded liability of $5.4 billion. (As of September 30, 2005, the unobligated budgetary resources of the two funds were approximately $3.6 billion, and the pension actuarial liability was $8.5 billion, resulting in an unfunded liability of $4.9 billion.) The actuarial cost method used to determine costs for the retirement plans is the Aggregate Entry Age Normal Actuarial Cost Method. The actuarial liability is based upon long term assumptions selected by the Treasury Department. In FY 2006, the assumption for the annual rate of investment return was 6.0% for the Judicial Fund and 4.8% for the D.C. Federal Pension Fund with a gradual increase to 6.0% by FY 2012 and the annual rate of inflation and cost-of-living adjustments were 3.5%. In FY 2005, the assumption for the annual rate of investment return was 6% for the Judicial Fund and 4.8% for the D.C. Federal Pension Fund with a gradual increase to 6% by FY 2011 and the annual rate of inflation and cost-of-living adjustments were 3%. In FY 2006, the assumption for the annual rate of salary increases was 6.5% for police officers and firefighters, 5.5% for teachers, and 3.5% for judges. In FY 2005, the assumption for the annual rate of salary increases was 6.5% for police officers and firefighters, 5.5% for teachers, and 3.5% for judges. The pension benefit costs incurred by the plans are included on the Consolidated Statements of Net Cost.

## 17. Commitments and Contingencies

The Department is a party in various administrative proceedings, legal actions, and claims including equal opportunity matters which may ultimately result in settlements or decisions adverse to the Federal government. These contingent liabilities arise in the normal course of operations and their ultimate disposition is unknown. The Department has accrued contingent liabilities where losses are determined to be probable and the amounts can be estimated. Other significant contingencies exist where a loss is reasonably possible or where a loss is probable and an estimate cannot be determined. The Department has disclosed contingent liabilities where the conditions for liability recognition have not been met and the likelihood of unfavorable outcome is more than remote.

In the opinion of the Department's management and legal counsel, based on information currently available, the expected outcome of these matters, individually or in the aggregate, will not have a materially adverse effect on the financial statements, except for the litigation described below.

### Legal Action Settlement

The Departments of Interior, Justice and Treasury settled an Indian Tribal Trust Fund case for $20 million on October 23, 2006. This settlement was paid from the Department of the Treasury's Judgment Fund.

### Pending Legal Actions

As of September 30, 2006, one claim was reported relative to proceedings and claims for which it is reasonably possible that a loss totaling $488 million may be incurred. As of September 30, 2005, no claims were reported for which a reasonable possibility of loss may be incurred.

Based on the information provided by legal counsel and in the opinion of management, the ultimate resolution of the following legal actions, for which the possibility of loss could not be determined, may materially affect Treasury's financial position or results. These specific cases all of which existed in FY 2005 are summarized as follows:

***Cobell v. Kempthorne (formerly Cobell v. Norton):*** Native Americans allege that the Departments of Interior and Treasury have breached trust obligations with respect to the management of the plaintiffs' individual

Indian monies. The plaintiffs have not made claims for specific dollar amounts in the Federal district court proceedings, but in public statements have asserted that the class is owed $27.487 billion.

***Tribal Trust Fund Cases:*** Numerous cases have been filed in which Native American Tribes seek a declaration that the U.S. has not provided the tribes with a full and complete accounting of their trust funds, and seek an order requiring the government to provide such an accounting. In addition, there are a number of other related cases for damages which do not name Treasury as a defendant. It is probable that additional tribes may file claims. It is not possible at this time to determine the number of suits that may be filed or the amount of damages that may be claimed.

***Ferreiro v. United States:*** Plaintiffs claim allegedly past due civil service retirement benefits relating to individuals' employment by the U.S. government in Cuba prior to 1963.

There are also other legal actions pending where the ultimate resolution of the legal actions, for which the possibility of loss could not be determined, may materially affect Treasury's financial position or results. As of September 30, 2006, 12 legal claims amounting to approximately $3.9 billion existed for which the possibility of loss could not be determined.

The Department also had employment cases (e.g., discrimination, Equal Employment Opportunity Commission, Merit System Protection Board, etc.) in which a loss may be reasonably possible, but for which a range of potential loss could not be determined.

## OTHER CONTINGENCIES

***Multilateral Development Banks (MDBs):*** The Treasury Department has subscribed to capital for certain MDBs, portions of which are callable under certain limited circumstances to meet the obligations of the respective MDBs. There has never been, nor is there anticipated, a call on the Treasury Department subscriptions. As of September 30, 2006 and September 30, 2005, U.S. callable capital in MDBs was as follows (in millions):

| | 2006 | 2005 |
|---|---|---|
| African Development Bank | $ 1,513 | $ 1,428 |
| Asian Development Bank | 5,911 | 5,911 |
| European Bank for Reconstruction and Development | 1,803 | 1,800 |
| Inter-American Development Bank | 28,687 | 28,687 |
| International Bank for Reconstruction and Development | 22,642 | 22,642 |
| Multilateral Investment Guarantee Agency | 293 | 285 |
| North American Development Bank | 1,275 | 1,275 |
| **Total** | **$ 62,124** | **$ 62,028** |

***Terrorism Risk Insurance Program:*** The Terrorism Risk Insurance Act (TRIA) was signed into law on November 26, 2002. This law was enacted to address market disruptions resulting from terrorist attacks on September 11, 2001. The act helps to ensure available and affordable commercial property and casualty insurance for terrorism risk, and simultaneously allows private markets to stabilize. If a certified act of terrorism occurs, insurers may be eligible to receive Federal government insured losses above a designated deductible amount. Insured losses above this amount will be shared between insurance companies and the Federal government. The Terrorism Risk Insurance Program is activated upon the certification of an "act of terrorism" by the Secretary of the Treasury in concurrence with the Secretary of State and the Attorney General.

The original TRIA program was scheduled to expire on December 31, 2005. However, this program was subsequently extended through December 31, 2007 when President Bush signed the Terrorism Risk Insurance Extension Act of 2005. This law includes the following changes: a reduced Federal role in terrorism risk insurance markets by increasing insurer deductibles and the exclusion of certain types of previously covered insurance. The act also reduces the Federal governments' share of insured losses. Another noteworthy change is a "Program Trigger" provision which precludes Federal payments unless insured losses from a certified terrorism event exceed $50 million in FY 2006 and $100 million in FY 2007.

## 18. Liabilities

### *Liabilities Not Covered by Budgetary and Other Resources*

As of September 30, 2006 and September 30, 2005, liabilities not covered by budgetary and other resources consisted of the following (in millions):

| | 2006 | 2005 |
|---|---|---|
| **Intra-governmental Liabilities Not Covered by Budgetary & Other Resources:** | | |
| Federal Debt Principal, Premium/Discount (Note 14) | $ 3,627,439 | $ 3,311,707 |
| Other Intra-governmental Liabilities | 103 | 97 |
| **Total Intra-governmental Liabilities Not Covered by Budgetary & Other Resources** | **$ 3,627,542** | **$ 3,311,804** |
| Federal Debt Principal, Premium/Discount (Note 14) | 4,802,956 | 4,565,707 |
| D.C. Pensions Liability (Note 16) | 5,422 | 4,851 |
| Other Liabilities | 1,055 | 1,072 |
| **Total Liabilities Not Covered by Budgetary & Other Resources** | **$ 8,436,975** | **$ 7,883,434** |

### *Other Liabilities with the Public*

Total "Other Liabilities" displayed on the Balance Sheets consists of both liabilities that are covered and not covered by budgetary resources. The amounts displayed of $3,816 and $4,665 million, respectively, at September 30, 2006, and September 30, 2005 consisted of the following (in millions):

| | FY 2006 | | |
|---|---|---|---|
| | Non-Current | Current | Total |
| **Intra-governmental** | | | |
| Unfunded Federal Workers Compensation Program Liability (FECA) | $ 66 | $ 51 | $ 117 |
| Accounts Payable | 0 | 60 | 60 |
| Other Accrued Liabilities | 3 | 121 | 124 |
| **Total Intra-governmental** | **$ 69** | **$ 232** | **$ 301** |
| **With the Public** | | | |
| Actuarial Federal Workers Compensation Program Liability (FECA) | $ 601 | $ 0 | $ 601 |
| Liability for Deposit Funds (Held by the Federal Government for Others) & Suspense Accounts | 0 | 498 | 498 |
| ATSB Loan Guarantee Liabilities (Note 15) | 0 | 0 | 0 |
| Accrued Funded Payroll and Benefits | 0 | 343 | 343 |
| Capital Lease Liabilities | 3 | 1 | 4 |
| Accounts Payable & Other Accrued Liabilities | 34 | 2,336 | 2,370 |
| **Total With the Public** | **$ 638** | **$ 3,178** | **$ 3,816** |

| | FY 2005 | | |
|---|---|---|---|
| | Non-Current | Current | Total |
| **Intra-governmental** | | | |
| Unfunded Federal Workers Compensation Program Liability (FECA) | $ 51 | $ 62 | $ 113 |
| Accounts Payable | 0 | 172 | 172 |
| Other Accrued Liabilities | 0 | 137 | 137 |
| **Total Intra-governmental** | **$ 51** | **$ 371** | **$ 422** |
| **With the Public** | | | |
| Actuarial Federal Workers Compensation Program Liability (FECA) | $ 645 | $ 0 | $ 645 |
| Liability for Deposit Funds (Held by the Federal Government for Others) & Suspense Accounts | 0 | 843 | 843 |
| ATSB Loan Guarantee Liabilities (Note 15) | 555 | 0 | 555 |
| Accrued Funded Payroll and Benefits | 0 | 326 | 326 |
| Capital Lease Liabilities | 10 | 16 | 26 |
| Accounts Payable & Other Accrued Liabilities | 34 | 2,236 | 2,270 |
| **Total with the Public** | **$ 1,244** | **$ 3,421** | **$ 4,665** |

## 19. Net Position

Unexpended Appropriations represents the amount of spending authorized as of year-end that is unliquidated or unobligated and has not lapsed, been rescinded, or withdrawn. No-year appropriations remain available for obligation until expended. Annual appropriations remain available for upward or downward adjustment of obligations until expired.

Cumulative Results of Operations represents the net results of operations since inception, and includes cumulative amounts related to investments in capitalized assets and donations and transfers of assets in and out without reimbursement. Also included as a reduction in Cumulative Results of Operations are accruals for which the related expenses require funding from future appropriations and assessments. These future funding requirements include, among others (a) accumulated annual leave earned but not taken, (b) accrued workers compensation, and (c) expenses for contingent liabilities.

The amount reported as "appropriations received" are appropriated from Treasury General Fund of the U.S. government receipts, such as income taxes, that are not earmarked by law for a specific purpose. This amount will not necessarily agree with the "appropriation received" amount reported on the Statement of Budgetary Resources (SBR) because of differences between proprietary and budgetary accounting concepts and reporting requirements. For example, certain dedicated and earmarked receipts are recorded as "appropriations received" on the SBR, but are recognized as exchange or non-exchange revenue (i.e. typically in special and non-revolving trust funds) and reported on the Statement of Changes in Net Position in accordance with SFFAS No.7.

The amount reported as "Transfers to the General Fund and Other" on the Consolidated Statements of Changes in Net Position under "Other Financing Sources" mainly represents the distribution of interest revenue to the General Fund of the U.S. Government of $13,192 million and $12,034 million, for the years ended September 30, 2006 and September 30, 2005, respectively. The interest revenue is accrued on inter-agency loans held by the Treasury Department on behalf of the U.S. Government. A corresponding balance is reported on the Consolidated Statement of Net Cost under "Federal Costs: Less Interest Revenue from Loans." The amount reported on the Consolidated Statement of Net Cost is reduced by eliminations with Treasury bureaus.

The Treasury Department also includes seigniorage in "Transfers to the General Fund and Other." Seigniorage is the face value of newly minted circulating coins less the cost of production. The United States Mint is required to distribute the seigniorage that it recognizes to the General Fund of the U.S. government. The distribution is also included in "Transfers to the General Fund and Other." In any given year, the amount recognized as seigniorage may differ for the amount distributed to the General Fund by an insignificant amount due to timing differences.

Seigniorage in the amounts of $682 million and $745 million was recognized, respectively, for the years ended September 30, 2006 and September 30, 2005. Distributions to the General Fund, including seigniorage, amounted to $750 million and $775 million, respectively for the years ended September 30, 2006, and September 30, 2005.

## 20. Consolidated Statement of Net Cost & Net Costs of Treasury Sub-organizations

The Treasury Department's Consolidated Statement of Net Cost displays information on a consolidated basis. The complexity of the Treasury Department's organizational structure and operations requires that supporting schedules for Net Cost be included in the notes to the financial statements. These supporting schedules provide consolidating information, which fully displays the costs of each sub-organization (Departmental Offices and each operating bureau).

The classification of sub-organizations has been determined in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *"Managerial Cost Accounting Concepts and Standards for the Federal Government"* which states that the predominant factor is the reporting entity's organization structure and existing responsibility components, such as bureaus, administrations, offices, and divisions within a department.

Each sub-organization is responsible for accumulating costs. The assignment of the costs to Treasury-wide programs is the result of using the following cost assignment methods: (1) direct costs; (2) cause and effect; and (3) cost allocation.

Intra-Departmental costs/revenues resulting from the provision of goods and/or services on a reimbursable basis among Departmental sub-organizations are reported as costs by providing sub-organizations. Accordingly, such costs/revenues are eliminated in the consolidation process.

To the extent practical or reasonable to do so, earned revenue is deducted from the gross costs of the programs to determine their net cost. There are no precise guidelines to determine the degree to which earned revenue can reasonably be attributed to programs. The attribution of earned revenues requires the exercise of managerial judgment.

The Treasury Department's Consolidated Statement of Net Cost also presents interest expense on the Federal Debt and other Federal costs incurred as a result of assets and liabilities managed on behalf of the U.S. government. These costs are not reflected as program costs related to the Treasury Department's strategic plan missions. Such costs are eliminated in the consolidation process to the extent that they involve transactions with Treasury Department sub-organizations.

Other federal costs for the years ended September 30, 2006 and 2005 consisted of the following (in millions):

| | 2006 | 2005 |
|---|---|---|
| Credit Reform Interest on Uninvested Funds (intra-governmental) | $ 5,200 | $ 4,405 |
| Resolution Funding Corporation | 1,979 | 2,130 |
| Judgment Claims and Contract Disputes | 677 | 973 |
| Corporation for Public Broadcasting | 460 | 466 |
| Legal Services Corporation | 328 | 299 |
| Refunds of Moneys Erroneously Received | 0 | 27 |
| All Other Payments | 296 | 373 |
| **Total** | **$ 8,940** | **$ 8,673** |

### *Pricing Policies – Exchange Revenues – Reimbursable Services*

A portion of the earned revenue displayed on the Treasury Department's Statement of Net Cost is generated by the provision of goods or services to the public or to other Federal entities.

Exchange revenues resulting from work performed for other Treasury Department sub-organizations or federal entities represent reimbursements for the full costs incurred by the performing entity. Reimbursable work between federal entities is subject to the Economy Act (31 U.S.C. 1535) or other statutes authorizing reimbursement. Prices associated with revenue earned from the public are based on recovery of full cost or are set at a market price. The Treasury Department does not incur losses on the provision of goods or services on a reimbursable basis.

The tables on the following pages present the Treasury Department's earned revenues, gross costs, and net cost of operations by program and by responsibility segment (in millions).

## 20. Supporting Net Cost Schedule by Strategic Plan Goal (In Millions):

| | Economic Program | | Financial Program | | Management Program | |
|---|---|---|---|---|---|---|
| **Treasury Sub-organization** | **Promote Prosperous U.S. & World Economies** | **Promote Stable U.S. and World Economies** | **Preserve the Integrity of Financial Systems** | **Manage the U.S. Government's Finances Effectively** | **Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of the Treasury** | **2006 Totals** |
| Bureau of Engraving and Printing | $ 0 | $ 0 | $ 24 | $ 0 | $ 0 | $ 24 |
| Bureau of the Public Debt | 0 | 0 | 0 | 289 | 0 | 289 |
| Departmental Offices | 143 | 326 | 218 | 478 | 221 | 1,386 |
| Financial Crimes Enforcement Network | 0 | 0 | 99 | 0 | 0 | 99 |
| Financial Management Service | 0 | 0 | 0 | 972 | 0 | 972 |
| Internal Revenue Service | 0 | 0 | 161 | 11,324 | 0 | 11,485 |
| U.S. Mint | 0 | 0 | (43) | 0 | 0 | (43) |
| Office of the Comptroller of the Currency | (9) | 0 | (50) | 0 | 0 | (59) |
| Office of Thrift Supervision | (3) | 0 | (28) | 0 | 0 | (31) |
| Alcohol and Tobacco Tax and Trade Bureau | 0 | 47 | 0 | 48 | 0 | 95 |
| **Combined Goal Net Cost** | **$ 131** | **$ 373** | **$ 381** | **$ 13,111** | **$ 221** | **$ 14,217** |
| Eliminations & Adjustments | | 684 | | (1,079) | 207 | (188) |
| **Consolidated Program Net Cost** | | **$ 1,188** | | **$ 12,413** | **$ 428** | **$ 14,029** |

*(continued)*

## 20. Supporting Net Cost Schedule by Strategic Plan Goal (In Millions):

| | Economic Program | | Financial Program | | Management Program | |
|---|---|---|---|---|---|---|
| Treasury Sub-organization | Promote Prosperous U.S. & World Economies | Promote Stable U.S. and World Economies | Preserve the Integrity of Financial Systems | Manage the U.S. Government's Finances Effectively | Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of the Treasury | 2005 Totals |
| Bureau of Engraving and Printing | $ 0 | $ 0 | $ 34 | $ 0 | $ 0 | $ 34 |
| Bureau of the Public Debt | 0 | 0 | 0 | 312 | 0 | 312 |
| Departmental Offices | 137 | 1,783 | 192 | (1,206) | 211 | 1,117 |
| Financial Crimes Enforcement Network | 0 | 0 | 90 | 0 | 0 | 90 |
| Financial Management Service | 0 | 0 | 0 | 872 | 0 | 872 |
| Internal Revenue Service | 0 | 0 | 192 | 11,268 | 0 | 11,460 |
| U.S. Mint | 0 | 0 | (31) | 0 | 0 | (31) |
| Office of the Comptroller of the Currency | (12) | 0 | (64) | 0 | 0 | (76) |
| Office of Thrift Supervision | (2) | 0 | (12) | 0 | 0 | (14) |
| Alcohol and Tobacco Tax and Trade Bureau | 0 | 44 | 0 | 42 | 0 | 86 |
| **Combined Goal Net Cost** | **$ 123** | **$ 1,827** | **$ 401** | **$ 11,288** | **$ 211** | **$ 13,850** |
| Eliminations & Adjustments | | 334 | | (596) | 206 | (56) |
| **Consolidated Program Net Cost** | | **$ 2,284** | | **$ 11,093** | **$ 417** | **$ 13,794** |

## 20. Consolidated Statement of Net Cost & Net Costs of Treasury Sub-organizations (In Millions)

| For FYE September 30, 2006 | Bureau of Engraving & Printing | Bureau of the Public Debt | Departmental Offices | Fin. Crimes Enforcement Network | Financial Management Service | Internal Revenue Service | U.S. Mint | Office of the Comptroller of the Currency | Office of Thrift Supervsion | Alcohol and Tobacco Tax and Trade Bureau | Combined Total | Eliminations/ Adjustments | 9/30/2006 Consolidated |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Program Costs:** | | | | | | | | | | | | | |
| ***Economic Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | $ 0 | $ 0 | $ 198 | $ 0 | $ 0 | $ 0 | $ 0 | $ 12 | $ 3 | $ 13 | $ 226 | $ (21) | $ 205 |
| Less: Earned Revenue | 0 | 0 | (706) | 0 | 0 | 0 | 0 | (3) | (2) | 0 | (711) | 705 | (6) |
| Intragovernmental Net Costs | 0 | 0 | (508) | 0 | 0 | 0 | 0 | 9 | 1 | 13 | (485) | 684 | 199 |
| Gross Costs with the public | 0 | 0 | 2003 | 0 | 0 | 0 | 0 | 78 | 18 | 35 | 2,134 | 0 | 2,134 |
| Less: Earned Revenue | 0 | 0 | (1,026) | 0 | 0 | 0 | 0 | (96) | (22) | (1) | (1,145) | 0 | (1,145) |
| Net Costs with the public | 0 | 0 | 977 | 0 | 0 | 0 | 0 | (18) | (4) | 34 | 989 | 0 | 989 |
| **Net Cost: Economic Program** | **0** | **0** | **469** | **0** | **0** | **0** | **0** | **(9)** | **(3)** | **47** | **504** | **684** | **1,188** |
| ***Financial Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | 83 | 73 | 1,617 | 51 | 165 | 3,829 | 72 | 62 | 25 | 13 | 5,990 | (1,359) | 4,631 |
| Less: Earned Revenue | (6) | (17) | (2,127) | (1) | (136) | (47) | (8) | (17) | (12) | 0 | (2,371) | 280 | (2,091) |
| Intragovernmental Net Costs | 77 | 56 | (510) | 50 | 29 | 3,782 | 64 | 45 | 13 | 13 | 3,619 | (1,079) | 2,540 |
| Gross Costs with the public | 418 | 236 | 1,206 | 49 | 943 | 7,869 | 1,526 | 422 | 160 | 36 | 12,865 | 0 | 12,865 |
| Less: Earned Revenue | (471) | (3) | 0 | 0 | 0 | (166) | (1,633) | (517) | (201) | (1) | (2,992) | 0 | (2,992) |
| Net Costs with the public | (53) | 233 | 1,206 | 49 | 943 | 7,703 | (107) | (95) | (41) | 35 | 9,873 | 0 | 9,873 |
| **Net Cost: Financial Program** | **24** | **289** | **696** | **99** | **972** | **11,485** | **(43)** | **(50)** | **(28)** | **48** | **13,492** | **(1,079)** | **12,413** |
| ***Management Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | 0 | 0 | 158 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 158 | (52) | 106 |
| Less: Earned Revenue | 0 | 0 | (818) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (818) | 259 | (559) |
| Intragovernmental Net Costs | 0 | 0 | (660) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (660) | 207 | (453) |
| Gross Costs with the public | 0 | 0 | 881 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 881 | 0 | 881 |
| Less: Earned Revenue | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net Costs with the public | 0 | 0 | 881 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 881 | 0 | 881 |
| **Net Cost: Management Program** | **0** | **0** | **221** | **0** | **0** | **0** | **0** | **0** | **0** | **0** | **221** | **207** | **428** |
| **Total Program Costs, Net** | **$ 24** | **$ 289** | **$ 1,386** | **$ 99** | **$ 972** | **$ 11,485** | **$ (43)** | **$ (59)** | **$ (31)** | **$ 95** | **$ 14,217** | **$ (188)** | **$ 14,029** |

## 20. Consolidated Statement of Net Cost & Net Costs of Treasury Sub-organizations (In Millions)

| For FYE September 30, 2005 | Bureau of Engraving & Printing | Bureau of the Public Debt | Departmental Offices | Fin. Crimes Enforcement Network | Financial Management Service | Internal Revenue Service | U.S. Mint | Office of the Comptroller of the Currency | Office of Thrift Supervsion | Alcohol and Tobacco Tax and Trade Bureau | Combined Total | Eliminations/ Adjustments | 9/30/2005 Consolidated |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Program Costs:** | | | | | | | | | | | | | |
| ***Economic Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | $ 0 | $ 0 | $ 669 | $ 0 | $ 0 | $ 0 | $ 0 | $ 12 | $ 2 | $ 16 | $ 699 | $ (11) | $ 688 |
| Less: Earned Revenue | 0 | 0 | (346) | 0 | 0 | 0 | 0 | (3) | (1) | 0 | (350) | 345 | (5) |
| Intragovernmental Net Costs | 0 | 0 | 323 | 0 | 0 | 0 | 0 | 9 | 1 | 16 | 349 | 334 | 683 |
| Gross Costs with the public | 0 | 0 | 2,260 | 0 | 0 | 0 | 0 | 72 | 17 | 29 | 2,378 | 0 | 2,378 |
| Less: Earned Revenue | 0 | 0 | (663) | 0 | 0 | 0 | 0 | (93) | (20) | (1) | (777) | 0 | (777) |
| Net Costs with the public | 0 | 0 | 1,597 | 0 | 0 | 0 | 0 | (21) | (3) | 28 | 1,601 | 0 | 1,601 |
| **Net Cost: Economic Program** | **0** | **0** | **1,920** | **0** | **0** | **0** | **0** | **(12)** | **(2)** | 44 | 1,950 | 334 | 2,284 |
| ***Financial Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | 82 | 74 | 905 | 49 | 166 | 3,856 | 55 | 57 | 22 | 15 | 5,281 | (1,423) | 3,858 |
| Less: Earned Revenue | (21) | (7) | (2,688) | (1) | (133) | (118) | (7) | (14) | (9) | 0 | (2,998) | 827 | (2,171) |
| Intragovernmental Net Costs | 61 | 67 | (1,783) | 48 | 33 | 3,738 | 48 | 43 | 13 | 15 | 2,283 | (596) | 1,687 |
| Gross Costs with the public | 464 | 248 | 768 | 42 | 840 | 7,879 | 941 | 360 | 152 | 28 | 11,722 | 0 | 11,722 |
| Less: Earned Revenue | (491) | (3) | 1 | 0 | (1) | (157) | (1,020) | (467) | (177) | (1) | (2,316) | 0 | (2,316) |
| Net Costs with the public | (27) | 245 | 769 | 42 | 839 | 7,722 | (79) | (107) | (25) | 27 | 9,406 | 0 | 9,406 |
| **Net Cost: Financial Program** | **34** | **312** | **(1,014)** | **90** | **872** | **11,460** | **(31)** | **(64)** | **(12)** | 42 | 11,689 | (596) | 11,093 |
| ***Management Program:*** | | | | | | | | | | | | | |
| Intragovernmental Gross Costs | 0 | 0 | 124 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 124 | (19) | 105 |
| Less: Earned Revenue | 0 | 0 | (964) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (964) | 225 | (739) |
| Intragovernmental Net Costs | 0 | 0 | (840) | 0 | 0 | 0 | 0 | 0 | 0 | 0 | (840) | 206 | (634) |
| Gross Costs with the public | 0 | 0 | 1,051 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,051 | 0 | 1,051 |
| Less: Earned Revenue | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net Costs with the public | 0 | 0 | 1,051 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,051 | 0 | 1,051 |
| **Net Cost: Management Program** | **0** | **0** | **211** | **0** | **0** | **0** | **0** | **0** | **0** | **0** | 211 | 206 | 417 |
| **Total Program Costs, Net** | $ 34 | $ 312 | $ 1,117 | $ 90 | $ 872 | $ 11,460 | $ (31) | $ (76) | $ (14) | $ 86 | $13,850 | $ (56) | $ 13,794 |

## 21. Additional Information Related to the Statement of Budgetary Resources

Federal agencies are required to disclose additional information related to the Combined Statement of Budgetary Resources (per OMB Circular A-136, "Financial Reporting Requirements") as amended. In accordance with SFFAS No. 7, the Department must report the value of goods and services ordered and obligated which have not been received. This amount includes any orders for which advance payment has been made but for which delivery or performance has not yet occurred. The information for the fiscal years ended September 30, 2006 and September 30, 2005 was as follows (in millions):

| | 2006 | 2005 |
|---|---|---|
| Undelivered orders at the end of the period. | $ 51,382 | $ 44,722 |
| Available borrowing and contract authority at the end of the period. | $ 5,720 | $ 5,669 |
| Adjustments to beginning balance of budgetary resources. | $ 0 | $ 1 |

**Apportionment Categories of Obligations Incurred: Direct vs. Reimbursable Obligations**

| | 2006 | 2005 |
|---|---|---|
| **Obligations Incurred** | | |
| Direct - Category A | $ 8,832 | $ 6,457 |
| Direct - Category B | 13,652 | 13,704 |
| Direct - Exempt from Apportionment | 418,314 | 364,692 |
| **Total Direct** | **$ 440,798** | **$ 384,853** |
| Reimbursable - Category B | $ 3,739 | $ 2,872 |
| Reimbursable - Exempt from Apportionment | 1,014 | 937 |
| **Total Reimbursable** | **$ 4,753** | **$ 3,809** |
| **Total Direct and Reimbursable** | **$ 445,551** | **$ 388,662** |

### Reconciliation of the President's Budget

The *Budget of the United States* (also known as the President's Budget), with actual numbers for FY 2006, was not published at the time that these financial statements were issued. The President's Budget is expected to be published in January 2007. It will be available from the United States Government Printing Office. The following chart displays the differences between the Combined Statement of Budgetary Resources (SBR) in the FY 2005 Performance and Accountability Report and the actual FY 2005 balances included in the FY 2007 President's Budget (PB).

## Reconciliation of FY 2005 Combined Statement of Budgetary Resources To the 2007 President's Budget (in millions)

| | Budgetary Resources | Outlays | Offsetting Receipts | Net Outlays | Obligations Incurred |
|---|---|---|---|---|---|
| **Statement of Budgetary Resources Amounts** | $ 453,332 | $ 376,870 | $ (15,649) | $ 361,221 | $ 388,662 |
| **Included in the Treasury Chapter of the President's Budget (PB) but not in the Statement of Budgetary Resources (SBR):** | | | | | |
| IRS non-entity tax credit payments (1) | 55,392 | 55,392 | | 55,392 | 55,363 |
| Tax and Trade Bureau (TTB) non-entity collections for Puerto Rico | 421 | 421 | | 421 | 419 |
| Non-Treasury offsetting receipts included in Treasury chapter of PB | | | (27) | (27) | |
| Treasury offsetting receipts considered to be "General Fund" transaction for reporting purposes (2) | | | (2,742) | (2,742) | |
| Continued dumping subsidy – U.S. Customs | 237 | 296 | | 296 | |
| Other | 2 | 2 | (58) | (56) | 1 |
| **Subtotal** | **56,052** | **56,111** | **(2,827)** | **53,284** | **55,783** |
| **Included in the SBR but not in the Treasury chapter of the PB:** | | | | | |
| Treasury resources shown in non-Treasury chapters of the PB, included in SBR (3) | (48,117) | (5,650) | | (5,650) | (10,501) |
| Offsetting collections net of collections shown in PB | (5,331) | | | | |
| Treasury offsetting receipts shown in other chapters of PB, part of which is in SBR | | | (284) | (284) | (9) |
| Unobligated balance carried forward, recoveries of prioryear funds and expired accounts | (2,170) | | | | (29) |
| Exchange Stabilization Fund resources not shown in PB | (24,357) | (513) | | (513) | 534 |
| Treasury Financing Accounts (CDFI & ATSB) | (913) | 207 | | 207 | |
| Other | (13) | 1 | 6 | 7 | (2) |
| **Subtotal** | **(80,901)** | **(5,955)** | **(278)** | **(6,233)** | **(10,007)** |
| **Trust Fund – Comptroller of the Currency (OCC)** | | **121** | | **121** | |
| **President's Budget Amounts*** | **$ 428,483** | **$ 427,147** | **$ (18,754)** | **$ 408,393** | **$ 434,438** |

1. These are primarily Earned Income Tax Credit and Child Tax Credit payments that are reported with refunds as custodial activities in Treasury's financial statements and thus are not reported as budgetary resources.
2. These are receipt accounts that Treasury manages on behalf of other agencies and considers to be "General Fund" receipts rather than receipts of the Treasury reporting entity.
3. The largest of these is Treasury's International Assistance Programs.

**Per Presidents Budget for FY 2007 – Budgetary Resources and Outlays are from the Analytical Perspective, Offsetting Receipts and Obligations Incurred are from the Appendix.*

### *Legal Arrangements Affecting Use of Unobligated Balances*

The use of unobligated balances is restricted based on annual legislation requirements or enabling authorities. Funds are presumed to be available for only one fiscal year unless otherwise noted in the annual appropriation language. Unobligated balances in unexpired fund symbols are available in the next fiscal year for new obligations unless some restrictions had been placed on those funds by law. In those situations, the restricted funding will be temporarily unavailable until such time as the reasons for the restriction have been satisfied or legislation has been enacted to remove the restriction.

Amounts in expired fund symbols are not available for new obligations, but may be used to adjust obligations and make disbursements that were recorded before the budgetary authority expired or to meet a bona fide need that arose in the fiscal year for which the appropriation was made.

## 22. Collection and Disposition of Custodial Revenue

The Treasury Department collects the majority of federal revenue from income and excise taxes. Collection activity, by revenue type and tax year, was as follows for the fiscal years ended September 30, 2006 and September 30, 2005 (in millions):

| | Tax Year | | | | |
|---|---|---|---|---|---|
| | **2006** | **2005** | **2004** | **Pre-2004** | **2006 Collections** |
| Individual Income and FICA Taxes | $ 1,309,338 | $ 690,831 | $ 17,307 | $ 16,733 | $ 2,034,209 |
| Corporate Income Taxes | 259,140 | 103,803 | 1,669 | 15,814 | 380,426 |
| Estate and Gift Taxes | 50 | 18,806 | 1,240 | 8,592 | 28,688 |
| Excise Taxes | 53,488 | 18,999 | 91 | 196 | 72,774 |
| Railroad Retirement Taxes | 3,577 | 1,094 | 0 | 2 | 4,673 |
| Unemployment Taxes | 5,080 | 2,276 | 52 | 125 | 7,533 |
| Federal Reserve Earnings | 24,141 | 5,804 | 0 | 0 | 29,945 |
| Fines, Penalties, Interest & Other Revenue | 2,888 | 436 | 0 | 0 | 3,324 |
| **Subtotal** | **$ 1,657,702** | **$ 842,049** | **$ 20,359** | **$ 41,462** | **$ 2,561,572** |
| Less Amounts Collected for Non-Federal Entities | | | | | (374) |
| **Total** | | | | | **$ 2,561,198** |

| | Tax Year | | | | |
|---|---|---|---|---|---|
| | **2005** | **2004** | **2003** | **Pre-2003** | **2005 Collections** |
| Individual Income and FICA Taxes | $ 1,211,866 | $ 620,914 | $ 13,873 | $ 18,034 | $ 1,864,687 |
| Corporate Income Taxes | 209,398 | 83,098 | 1,178 | 13,195 | 306,869 |
| Estate and Gift Taxes | 77 | 16,616 | 1,278 | 7,634 | 25,605 |
| Excise Taxes | 52,330 | 18,954 | 104 | 582 | 71,970 |
| Railroad Retirement Taxes | 3,464 | 1,071 | 1 | 3 | 4,539 |
| Unemployment Taxes | 4,915 | 1,890 | 37 | 106 | 6,948 |
| Federal Reserve Earnings | 14,208 | 5,089 | 0 | 0 | 19,297 |
| Fines, Penalties, Interest & Other Revenue | 3,192 | 360 | 0 | 0 | 3,552 |
| **Subtotal** | **$ 1,499,450** | **$ 747,992** | **$ 16,471** | **$ 39,554** | **$ 2,303,467** |
| Less Amounts Collected for Non-Federal Entities | | | | | (454) |
| **Total** | | | | | **2,303,013** |

Amounts reported for Corporate Income Taxes collected in FY 2006 include corporate taxes of $10 billion for tax year 2007. (Similarly, amounts reported for Corporate Income Taxes collected in fiscal year 2005 include corporate taxes of $9 billion for tax year 2006.) Individual Income and FICA Taxes, includes $71 billion in payroll taxes collected from other federal agencies. Of this amount, $12 billion represents the portion paid by the employers. (The comparable amounts for FY 2005 are $68 billion in payroll taxes collected from other federal agencies and $11 billion paid by the employers.)

### *Amounts Provided to Fund the Federal Government*

For the fiscal years ended September 30, 2006 and September 30, 2005, collections of custodial revenue transferred to other entities were as follows (in millions):

| | 2006 | 2005 |
|---|---|---|
| Department of Interior | $ 250 | $ 226 |
| General Fund | 2,283,170 | 2,035,673 |
| **Total** | **$ 2,283,420** | **$ 2,035,899** |

### *Federal Tax Refunds Paid*

Refund activity, broken out by revenue type and by tax year, was as follows for the fiscal years ended September 30, 2006 and September 30, 2005 (in millions):

| | Tax Year | | | | |
|---|---|---|---|---|---|
| | 2006 | 2005 | 2004 | Pre-2004 | 2006 Refunds |
| Individual Income and FICA Taxes | $ 612 | $ 225,503 | $ 13,465 | $ 5,606 | $ 245,186 |
| Corporate Income Taxes | 1,238 | 8,805 | 3,906 | 16,514 | 30,463 |
| Estate and Gift Taxes | 429 | 240 | 332 | 279 | 1,280 |
| Excise Taxes | 0 | 479 | 46 | 178 | 703 |
| Railroad Retirement Taxes | 0 | (31) | 15 | 19 | 3 |
| Unemployment Taxes | 0 | 86 | 19 | 38 | 143 |
| **Total** | **$ 2,279** | **$ 235,082** | **$ 17,783** | **$ 22,634** | **$ 277,778** |

| | Tax Year | | | | |
|---|---|---|---|---|---|
| | 2005 | 2004 | 2003 | Pre-2003 | 2005 Refunds |
| Individual Income and FICA Taxes | $ 586 | $ 211,102 | $ 12,842 | $ 5,489 | $ 230,019 |
| Corporate Income Taxes | 970 | 7,167 | 5,500 | 21,458 | 35,095 |
| Estate and Gift Taxes | 0 | 257 | 373 | 253 | 883 |
| Excise Taxes | 329 | 337 | 46 | 283 | 995 |
| Railroad Retirement Taxes | 0 | 2 | 0 | 2 | 4 |
| Unemployment Taxes | 1 | 73 | 13 | 31 | 118 |
| **Total** | **$ 1,886** | **$ 218,938** | **$ 18,774** | **$ 27,516** | **$ 267,114** |

### *Refunds Payable*

As of September 30, 2006 and September 30, 2005, refunds payable to taxpayers consisted of the following (in millions):

| | 2006 | 2005 |
|---|---|---|
| Alcohol, Tobacco Tax and Trade Bureau | $ 6 | $ 6 |
| Internal Revenue Service | 1,695 | 1,946 |
| **Total** | **$ 1,701** | **$ 1,952** |

## 23. 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 or purposes. The Statement of Federal Financial Accounting Standards No. 27 *"Identifying and Reporting Earmarked Funds"* issued by the Federal Accounting Standards Advisory Board (FASAB) defines the following three criteria for determining an earmarked fund: 1) A statute committing the Federal Government to use specifically identified revenues and other financing sources only for designated activities, benefits or purposes; 2) Explicit authority for the earmarked fund to retain revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and 3) A requirement to account for and report on the receipt, use, and retention of the revenues and other financing sources that distinguishes the earmarked fund from the Government's general revenues.

The majority of Treasury's earmarked fund activities are attributed to the Exchange Stabilization Fund (ESF) and the pension and retirement funds managed by the Office of D.C. Pensions. In addition, several Treasury bureaus operate with "public enterprise revolving funds" and receive no appropriations from the Congress. These bureaus are the Bureau of Engraving and Printing (BEP), the U.S. Mint, the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS). Other miscellaneous earmarked funds are managed by the Bureau of Public Debt (BPD), the Departmental Offices (DO), the Financial Management Service (FMS/FMD), and the Treasury Forfeiture Fund (TFF).

The following is a list of earmarked funds and a brief description of the purpose, accounting, and uses of these funds.

**Exchange Stabilization Fund (ESF)**

| | | |
|---|---|---|
| ESF | 20X4444 | Exchange Stabilization Fund |

**D.C. Pensions**

| | | |
|---|---|---|
| DCP | 201099 | Fines, penalties & forfeitures |
| DCP | 20X1713 | Federal payment – DC Judicial Retirement |
| DCP | 20X1714 | Federal Supplemental – Pension |
| DCP | 20X5511 | D.C. Federal Pension Fund |
| DCP | 20X8212 | D.C. Judicial Retirement and Survivor's Annuity Fund |

**Public Enterprise Revolving Fund**

| | | |
|---|---|---|
| BEP | 20X4502 | Bureau of Engraving & Printing Public Enterprise Fund |
| MNT | 20X4159 | Public Enterprise Revolving Fund |
| OCC | 20X8413 | Assessment Funds |
| OTS | 20X4108 | Public Enterprise Revolving Fund |

**Other Earmarked Funds**

| | | |
|---|---|---|
| BPD | 2061738 | Payments to the Terrestrial Wildlife Habitat Restoration |
| BPD | 20X5080 | Gifts To Reduce Public Debt |
| BPD | 20X5080.001 | Gift To Reduce Public Debt |
| BPD | 20X8207 | Lower Brule Sioux Tribe Terrestrial Wildlife Habitat Restoration Trust Fund |
| BPD | 20X8209 | Cheyenne River Sioux Terrestrial Wildlife Habitat Restoration Trust Fund |
| DO | 20X5407 | Sallie Mae Assessments |
| DO | 20X5816 | Confiscated and Vested Iraqi Property and Assets |
| DO | 20X8527 | Violent Crime Reduction Trust |
| DO | 20X8790 | Gifts and Bequests Trust Fund |
| FMD | 205445 | Debt Collection |
| FMD | 20X5081 | Presidential Election Campaign |
| FMD | 20X8902 | Esther Cattell Schmitt Gift Fund |
| FMS | 200/15445 | Debt Collection Special Fund |
| FMS | 201/25445 | Debt Collection Special Fund |
| FMS | 202/35445 | Debt Collection Special Fund |
| FMS | 203/45445 | Debt Collection Special Fund |
| FMS | 204/55445 | Debt Collection Special Fund |
| FMS | 205/65445 | Debt Collection Special Fund |
| FMS | 206/75445 | Debt Collection Special Fund |
| IRR | 20X5080.001 | Gifts to the U.S. to reduce the Public Debt |
| IRR | 20X5081.001 | Presidential Election Campaign Fund |
| IRR | 20X5099 | Reimburse Law Enforcement |
| IRR | 20X5433 | Informant Reimbursement |
| TFF | 20X5697 | Treasury Forfeiture Fund |

The ESF uses funds to purchase or sell foreign currencies, to hold U.S. foreign exchange and Special Drawing Rights (SDR) assets, and to provide financing to foreign governments. ESF accounts and reports its holdings to FMS on the SF224, "Statement of Transactions," as well as to the Congress and Treasury's policy office. The Gold Reserve Act of 1934, Bretton Woods Agreement Act of 1945, P.L. 95-147 and P.L. 94-564 established and authorized the use of the Fund. SDR in the IMF, Investments in U.S. Securities (BPD), and Investments in Foreign Currency Denominated assets are the sources of revenues or other financing sources. ESF's earnings and realized gains on foreign currency denominated assets represent inflows of resources to the Government, and the revenues earned are the result of intra-governmental inflows.

D.C. Pension funds provide annuity payments for retired D.C. teachers, police officers, judges, and firefighters. The sources of revenues are through annual appropriations, employees' contributions, and interest earnings from investments. All proceeds are earmarked fund. Note 16 provides detailed information on various funds managed by the Office of D.C. Pensions.

Treasury's four non-appropriated bureaus, BEP, Mint, OCC and OTS, operate "public enterprise funds". These bureaus account for the revenue and expenses related to the production and sale of numismatic products and circulating coinage (Mint), currency printing activities (BEP), and support of oversight functions of banking (OCC) and thrift operations (OTS). 31 USC 142 established the revolving fund for the BEP to account for revenue and expenses related to the currency printing activities. Public Law 104-52 (31 USC §5136) established the Public Enterprise Fund for the U.S. Mint to account for all revenue and expenses related to the production and sale of numismatic products and circulating coinage. Revenues and other financing sources at the Mint are mainly from the sale of numismatic and bullion coins, and the sale of circulating coins to the Federal Reserve Banks system. 12 USC 481 established the Assessment Funds for the OCC, and 103 Stat. 278 established the Public Enterprise Revolving Fund for the OTS. Revenue and financing sources are from the bank examination and assessments for the oversight of the national banks, savings associations, and savings and loan holding companies. These earmarked funds do not directly contribute to the inflows of resources to the government; however, revenues in excess of costs are returned to the General Fund of the U.S. government. There are minimal transactions with other government agencies.

There are other earmarked funds at several Treasury bureaus, such as donations to the Presidential Election Campaign Fund, funds related to the debt collection program, gifts to reduce public debt, and other enforcement related activities. Public laws, statutory laws, U.S. Code, and the Debt Collection Improvement Act, established and authorized the use of these funds. Sources of revenues and other financing sources include contributions, cash and property seized in enforcement activities, public donations, the sale of forfeited properties, and debt collection.

### Intra-governmental Investments in Treasury Securities

The Federal government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. Treasury bureaus and other Federal agencies invest some of the earmarked funds that they collect from the public. The funds are invested in securities issued by the Treasury Bureau of Public Debt (BPD), which are shown an Treasury's balance sheet as "Federal Debt and Interest Payable" (under Intra-Governmental Liabilities). The cash collected by BPD is deposited in the General Fund of the U.S. Government, which uses the cash for general government purposes.

The investments provide the Treasury bureaus and other Federal agencies with authority to draw upon the General Fund of the U.S. Government to make future benefit payments or other expenditures. When Treasury bureaus or other Federal agencies require 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.

The securities are an asset to the Treasury bureaus and other Federal agencies and a liability of the BPD. The General Fund of the United States Government is liable to BPD. Because Treasury bureaus and other Federal agencies are parts of the U.S. 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. In addition, because BPD is a subcomponent of the Treasury Department reporting entity, balances related to the investments made by Treasury bureaus are eliminated from these consolidated financial statements. However, the General Fund of the U.S. government remains liable to BPD for the eliminated balances (see Note 4).

The following table presents the summary information for the Balance Sheet, Statement of Net Cost, and the Statement of Changes in Net Position for Treasury's earmarked funds.

## Summary Statements for Earmarked Funds as of and for the year ended September 30, 2006

| Balance Sheet | Exchange Stabilization Fund | D.C. Pensions | Public Enterprise Revolving Funds | Other Earmarked Funds | Combined Earmarked Funds |
|---|---|---|---|---|---|
| **ASSETS:** | | | | | |
| Fund Balance | $ 0 | $ 0 | $ 400 | $ 234 | $ 634 |
| Investments & Related Interest – Intra-governmental | 15,736 | 3,862 | 993 | 322 | 20,913 |
| Cash, Foreign Currency & Other Monetary Assets | 19,351 | 0 | 0 | 19 | 19,370 |
| Investments & Related Interest | 9,278 | 0 | 0 | 0 | 9,278 |
| Other Assets | 0 | 48 | 1,132 | 61 | 1,241 |
| **Total Assets** | **$ 44,365** | **$ 3,910** | **$ 2,525** | **$ 636** | **$ 51,436** |
| **LIABILITIES:** | | | | | |
| Intra-governmental Liabilities | $ 0 | $ 0 | $ 151 | $ 178 | $ 329 |
| Certificates Issued to Federal Reserve Banks | 2,200 | 0 | 0 | $0 | 2,200 |
| Allocation of Special Drawing Rights | 7,234 | 0 | 0 | $0 | 7,234 |
| Other Liabilities | 46 | 9,119 | 558 | 134 | 9,857 |
| **Total Liabilities** | **$ 9,480** | **$ 9,119** | **$ 709** | **$ 312** | **$ 19,620** |
| **NET POSITION:** | | | | | |
| Unexpended Appropriations | $ 200 | $ 0 | $ 0 | $ 2 | $ 202 |
| Cumulative Results of Operations | 34,685 | (5,209) | 1,816 | 322 | 31,614 |
| **Total Liabilities and Net Position** | **$ 44,365** | **$ 3,910** | **$ 2,525** | **$ 636** | **$ 51,436** |
| **Statement of Net Cost** | | | | | |
| Gross Cost | $ 377 | $ 1,069 | $ 2,879 | $ 184 | $ 4,509 |
| Less Earned Revenue | (1,710) | (163) | (2,988) | 0 | (4,861) |
| **Total Net Cost of Operations** | **$ (1,333)** | **$ 906** | **$ (109)** | **$ 184** | **$ (352)** |
| **Cumulative Results of Operations** | | | | | |
| Beginning Balance, as Adjusted | $ 33,352 | $ (4,596) | $ 1,729 | $ 332 | $ 30,817 |
| Budgetary Financing Sources | 0 | 293 | (11) | 159 | 441 |
| Other Financing Sources | 0 | 0 | (11) | 15 | 4 |
| **Total Financing Sources** | **0** | **293** | **(22)** | **174** | **445** |
| Net Cost of Operations | 1,333 | (906) | 109 | (184) | 352 |
| **Net Change** | **1,333** | **(613)** | **87** | **(10)** | **797** |
| **Total Cumulative Results of Operations** | **$ 34,685** | **$ (5,209)** | **$ 1,816** | **$ 322** | **$ 31,614** |

# Required Supplemental Information (Unaudited)

## Introduction

This section provides the Required Supplemental Information as prescribed by Office of Management and Budget (OMB) Circular A-136, *"Financial Reporting Requirements."*

## Other Claims for Refunds

The Department has estimated that $17.9 billion may be payable as other claims for tax refunds. This estimate represents amounts (principal and interest) that may be paid for claims pending judicial review by the Federal courts or internally. The total estimated payout (including principal and interest) for claims pending judicial review by the federal courts is $10.8 billion and by appeals is $7.1 billion. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5 for reporting the amounts in the Balance Sheet or for disclosure in the notes to the financial statements. However, they meet the criteria in SFFAS No. 7 for inclusion as supplemental information.

## Assessments

In accordance with SFFAS No. 7, some unpaid tax assessments do not meet the criteria for financial statement recognition as discussed in the Note 1 to the financial statements. Although compliance assessments and write-offs are not considered receivables under federal accounting standards, they represent legally enforceable claims of the federal government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

The components of the total unpaid assessments at September 30, 2006 were as follows (in billions):

| | |
|---|---|
| Gross Unpaid Assessments | $ 245 |
| Less: Compliance Assessments | (57) |
| Write Offs | (97) |
| **Gross Federal Taxes Receivable** | **$ 91** |

To eliminate double counting, the compliance assessments reported above exclude trust fund recovery penalties, totaling $9 billion, assessed against officers and directors of businesses who were involved in the non-remittance of federal taxes withheld from their employees. The related unpaid assessments of those businesses are reported as taxes receivable or write-offs, but the Department may also recover portions of those businesses' unpaid assessments from any and all individual officers and directors against whom a trust fund recovery penalty is assessed.

### *Internal Revenue Service (IRS)*

The unpaid assessments balance represents assessments resulting from taxpayers filing returns without sufficient payment; as well as from the IRS's enforcement programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. A significant portion of this balance is not considered a receivable. Also, a substantial portion of the amounts considered receivables is largely uncollectible.

Under federal accounting standards, unpaid assessments require taxpayer or court agreement to be considered federal taxes receivable. Assessments not agreed to by taxpayers or the courts are considered compliance assessments and are not considered federal taxes receivable. Due to the lack of agreement, these compliance assessments are less likely to have future collection potential than those unpaid assessments that are considered federal taxes receivable.

Assessments with little or no future collection potential are called write-offs. Write-offs principally consist of amounts owed by deceased, bankrupt or defunct taxpayers, including many failed financial institutions liquidated by the FDIC and the former Resolution Trust Corporation (RTC). As noted above, write-offs have little or no future collection potential, but statutory provisions require that these assessments be maintained until the statute for collection expires.

## Statement of Budgetary Resources Disaggregated by Sub-organization Accounts (in Millions):

| | Bureau of Engraving & Printing | Bureau of the Public Debt | Departmental Offices | Fin. Crimes Enforcement Network | Financial Management Service | Internal Revenue Service | U.S. Mint | Office of the Comptroller of the Currency | Office of Thrift Supervision | Alcohol and Tobacco Tax and Trade Bureau | 9/30/2006 Combined-Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Budgetary Resources** | | | | | | | | | | | |
| Unobligated balance brought forward | $ 118 | $ 12 | $ 63,050 | $ 9 | $ 225 | $ 490 | $ 62 | $ 507 | $ 195 | $ 2 | $ 64,670 |
| Recoveries of prior year unpaid obligations | | 17 | 131 | 3 | 96 | 128 | | | 3 | 2 | 380 |
| Budget Authority: | | | | | | | | | | | |
| Appropriations | | 409,503 | 5,686 | 74 | 11,293 | 10,780 | | | | 91 | 437,427 |
| Borrowing authority | | | 12 | | | | | | | | 12 |
| Spending authority from offsetting collections: | | | | | | | | | | | |
| Earned: | | | | | | | | | | | |
| Collected | 487 | 20 | 3,951 | 3 | 2,245 | 106 | 1,611 | 649 | 236 | 2 | 9,310 |
| Change in receivable from federal sources | (10) | | (15) | | 1 | (2) | 46 | (1) | | | 19 |
| Change in unfilled customer order: | | | | | | | | | | | |
| Advance received | (3) | | 22 | | | | | | 6 | | 25 |
| Without advance from federal sources | | | (56) | | 5 | | | | | | (51) |
| Subtotal | 474 | 409,523 | 9,600 | 77 | 13,544 | 10,884 | 1,657 | 648 | 242 | 93 | 446,742 |
| Non-expenditure transfers, net | | (2) | 136 | | | | | | | | 134 |
| Temporarily not available pursuant to Public Law | | (5) | (3,666) | | | | | | | | (3,671) |
| Permanently not available | | (3,342) | (115) | (1) | (1,394) | (227) | (84) | | | (1) | (5,164) |
| **Total Budgetary Resources** | **$ 592** | **$ 406,203** | **$ 69,136** | **$ 88** | **$ 12,471** | **$ 11,275** | **$ 1,635** | **$ 1,155** | **$ 440** | **$ 96** | **$ 503,091** |
| **Status of Budgetary Resources** | | | | | | | | | | | |
| Obligations incurred | | | | | | | | | | | |
| Direct | | $ 406,171 | $ 11,786 | $ 71 | $ 12,044 | $ 10,634 | | | | $ 92 | $ 440,798 |
| Reimbursable | $ 496 | 20 | 1,548 | 4 | 178 | 90 | $ 1,656 | $ 557 | $ 202 | 2 | 4,753 |
| Subtotal | 496 | 406,191 | 13,334 | 75 | 12,222 | 10,724 | 1,656 | 557 | 202 | 94 | 445,551 |
| Unobligated Balance | | | | | | | | | | | |
| Apportioned | 96 | 5 | 13,825 | 10 | 202 | 192 | (21) | | | | 14,309 |
| Exempt from apportionment | | 2 | 31,924 | 3 | 19 | | | 598 | 238 | | 32,784 |
| Subtotal | 96 | 7 | 45,749 | 13 | 221 | 192 | (21) | 598 | 238 | | 47,093 |
| Unobligated balance not available | | 5 | 10,053 | | 28 | 359 | | | | 2 | 10,447 |
| **Total Status of Budgetary Resources** | **$ 592** | **$ 406,203** | **$ 69,136** | **$ 88** | **$ 12,471** | **$ 11,275** | **$ 1,635** | **$ 1,155** | **$ 440** | **$ 96** | **$ 503,091** |
| **Relationship of Obligations to Outlays** | | | | | | | | | | | |
| Obligated balance, net | | | | | | | | | | | |
| Unpaid obligations brought forward | $ 106 | $ 70 | $ 43,957 | $ 23 | $ 309 | $ 1,524 | $ 233 | $ 99 | $ 39 | $ 21 | $ 46,381 |
| Uncollected customer payments from Federal sources brought forward | (43) | (1) | (532) | | (30) | (16) | (15) | (5) | | (1) | (643) |
| Total unpaid obligated balance, net | 63 | 69 | 43,425 | 23 | 279 | 1,508 | 218 | 94 | 39 | 20 | 45,738 |
| Obligations incurred, net | 496 | 406,191 | 13,334 | 75 | 12,222 | 10,724 | 1,656 | 557 | 202 | 94 | 445,551 |
| Gross Outlays | (502) | (406,182) | (6,559) | (75) | (12,178) | (10,589) | (1,580) | (538) | (198) | (93) | (438,494) |
| Recoveries of prior year unpaid obligations, actual | | (17) | (131) | (3) | (96) | (128) | | | (3) | (2) | (380) |
| Change in uncollected customer payments from federal sources | 10 | | 72 | | (6) | 2 | (46) | 1 | | | 33 |
| Obligated balance net, end of period | | | | | | | | | | | |
| Unpaid obligations | 101 | 62 | 50,599 | 19 | 257 | 1,532 | 309 | 118 | 40 | 20 | 53,057 |
| Uncollected customer payments from federal sources | (33) | (1) | (457) | | (37) | (15) | (62) | (4) | | | (609) |
| Total unpaid obligated balance, net, end of period | 68 | 61 | 50,142 | 19 | 220 | 1,517 | 247 | 114 | 40 | 20 | 52,448 |
| **Net Outlays** | | | | | | | | | | | |
| Gross outlays | 502 | 406,182 | 6,559 | 75 | 12,178 | 10,589 | 1,580 | 538 | 198 | 93 | 438,494 |
| Offsetting collections | (485) | (20) | (3,535) | (3) | (2,245) | (107) | (1,611) | (649) | (242) | (2) | (8,899) |
| Distributed offsetting receipts | | (13,625) | (1,634) | | (1,206) | (103) | | | | | (16,568) |
| **Net Outlays** | **$ 17** | **$ 392,537** | **$ 1,390** | **$ 72** | **$ 8,727** | **$ 10,379** | **$ (31)** | **$ (111)** | **$ (44)** | **$ 91** | **$ 413,027** |

## Deferred Maintenance

In FY 2006, the Department had no deferred maintenance to report on vehicles, buildings, and structures owned by the Department.

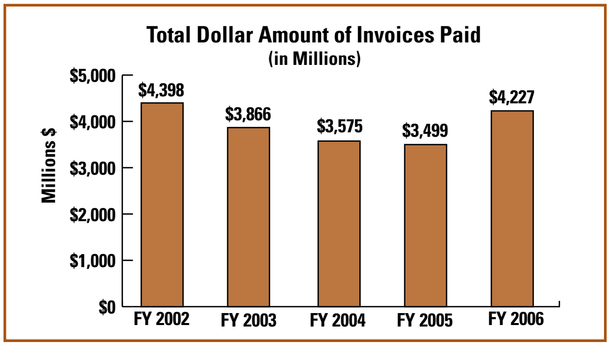
Treasury bureaus use a specific methodology in determining deferred maintenance. This procedure includes reviewing equipment, building, and other structure logistic reports. Upon completion of this review, logistic personnel use a condition assessment survey to determine the status of referenced assets. A five level rating scale (excellent, good, fair, poor, and very poor) is used for assessment purposes. Bureau logistic personnel subsequently identify maintenance not performed as scheduled and establish future performance dates.

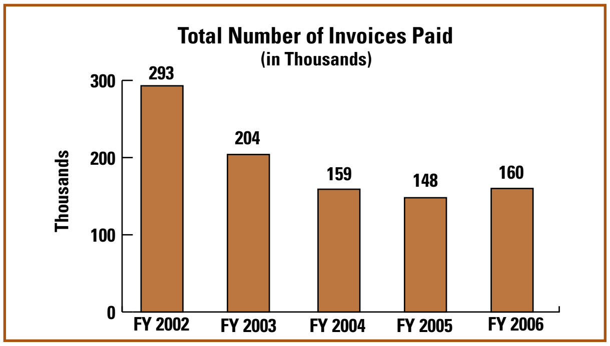
# Other Accompanying Information (Unaudited)

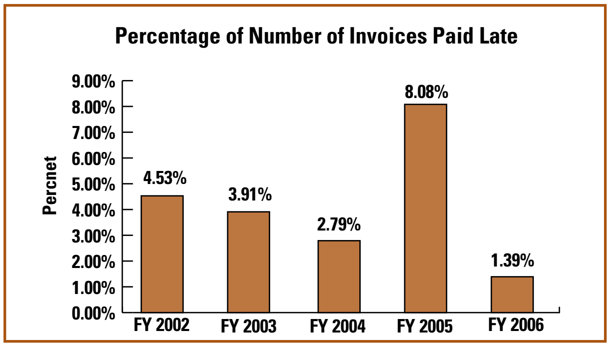
This section provides Other Accompanying Information as prescribed by OMB Circular A-136, *"Financial Reporting. Requirements"*

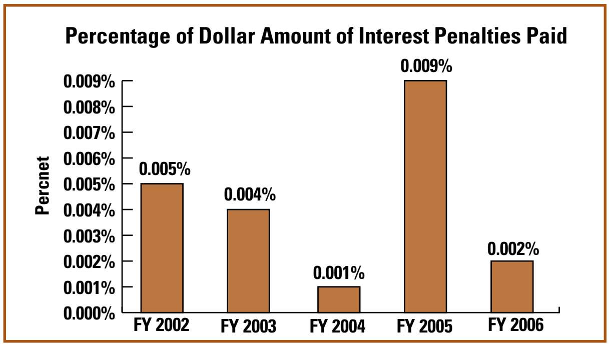
## Prompt Payment

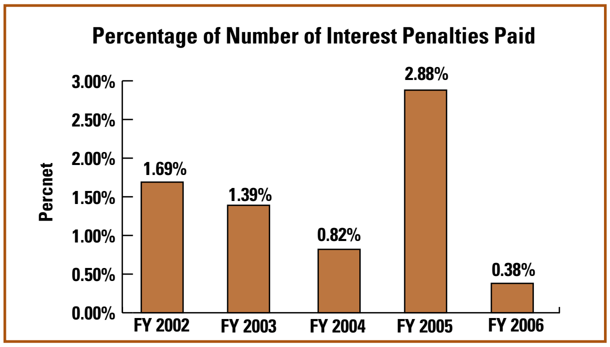
The Prompt Payment Act requires Federal agencies to make timely payments to vendors for supplies and services, to pay interest penalties when payments are made after the due date, and to take cash discounts only when they are economically justified. Treasury bureaus report Prompt Payment data on a monthly basis to the Department, and periodic quality control reviews are conducted by the bureaus to identify potential problems. The number of late payments and the amount of interest penalties decreased in FY 2006. This vast improvement was mostly due to improved management oversight and the completion of the implementation of the new financial system at the Internal Revenue Service.



## Tax Gap

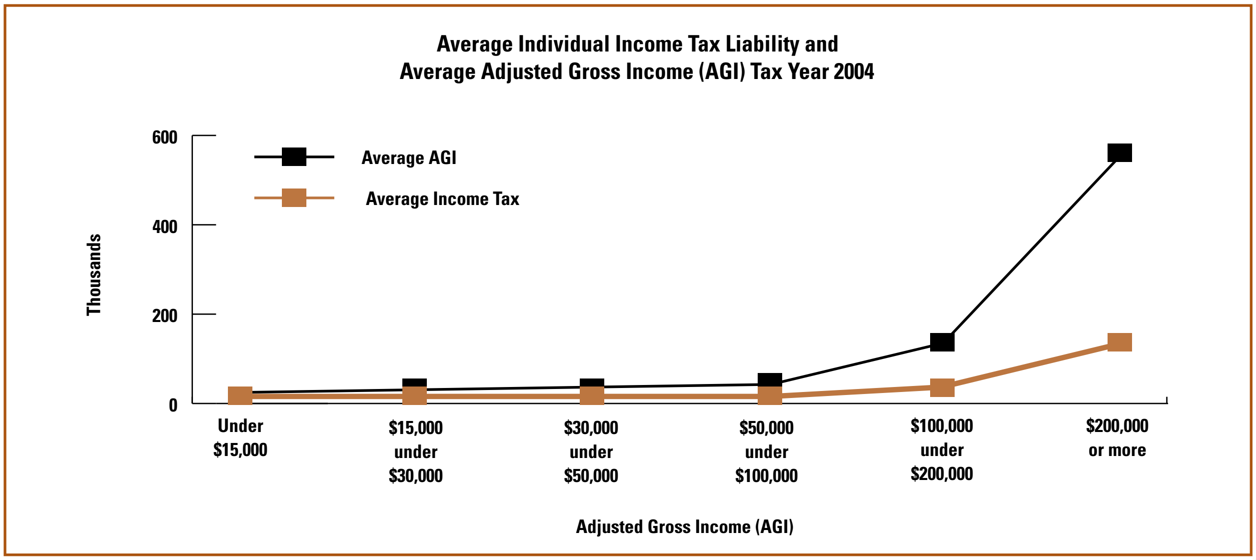
Reducing the tax gap is at the heart of IRS' enforcement programs. The tax gap is the difference between what taxpayers should pay and what they actually pay due to not filing tax returns, not paying their reported tax liability on time, or failing to report their correct tax liability. The tax gap, about $345 billion based on updated FY 2006 estimates, represents the amount of noncompliance with the tax laws. Underreporting tax liability accounts for 83% of the gap, with the remainder almost evenly divided between non-filing (8%) and underpaying (9%). The IRS remains committed to finding ways to increase compliance and reduce the tax gap, while minimizing the burden on the vast majority of taxpayers who pay their taxes accurately and on time.

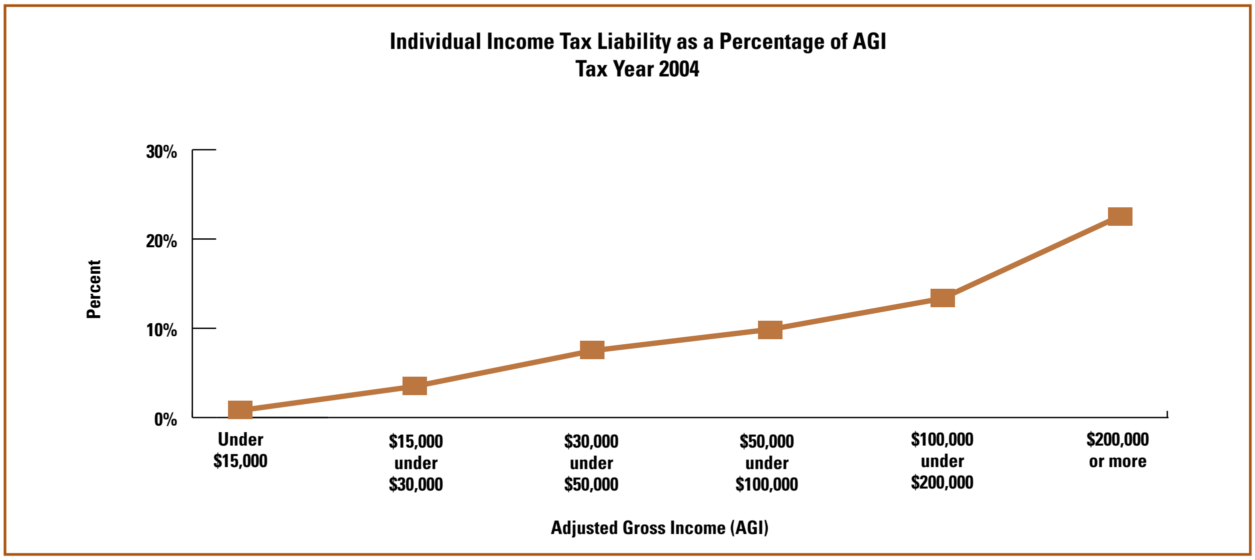
The tax gap is the aggregate amount of tax (i.e., excluding interest and penalties) that is imposed by the tax laws for any given tax year but is not paid voluntarily and timely. The tax gap arises from the three types of noncompliance: not filing required tax returns on time or at all (the non-filing gap), underreporting the correct amount of tax on timely filed returns (the underreporting gap), and not paying on time the full amount reported on timely filed returns (the underpayment gap). Of these three components, only the underpayment gap is observed; the non-filing gap and the underreporting gap must be estimated. Each instance of noncompliance by a taxpayer contributes to the tax gap, whether or not the IRS detects it, and whether or not the taxpayer is even aware of the noncompliance. Obviously, some of the tax gap arises from intentional (willful) noncompliance, and some of it arises from unintentional mistakes.

The collection gap is the cumulative amount of tax, penalties, and interest that has been assessed over many years, but has not been paid by a certain point in time, and which the Service expects to remain uncollectible. In essence, it represents the difference between the total balance of unpaid assessments and the net taxes receivable reported on the Service's balance sheet. The tax gap and the collection gap are related and overlapping concepts, but they have significant differences. The collection gap is a cumulative balance sheet concept for a particular point in time, while the tax gap is like an income statement item for a single year. Moreover, the tax gap estimates include all noncompliance, while the collection gap includes only amounts that have been assessed (a small portion of all noncompliance).

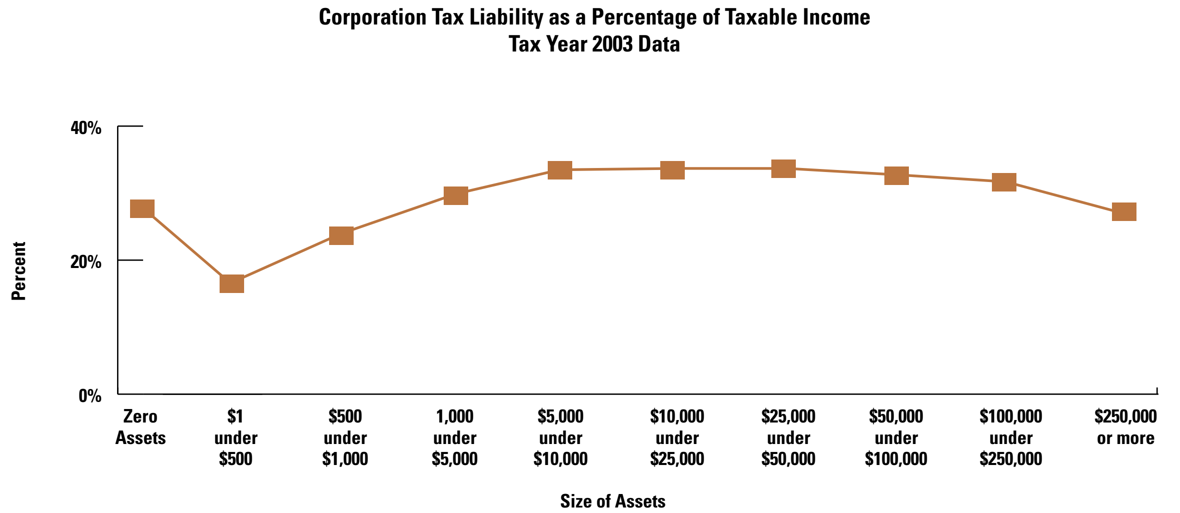
## Tax Burden

The Internal Revenue Code provides for progressive rates of tax, whereby higher incomes are generally subject to higher rates of tax. The graphs below present the latest available information on income tax and adjusted gross income (AGI) for individuals by AGI level and for corporations by size of assets. For individuals, the information illustrates, in percentage terms, the tax burden borne by varying AGI levels. For corporations, the information illustrates, in percentage terms, the tax burden borne by these entities by various sizes of their total assets. The graphs are only representative of more detailed data and analysis available from the Statistics of Income (SOI) office.




| Adjusted Gross Income (AGI) | Number of tax returns (in thousands) | AGI (in millions) | Total income tax (in millions) | Average AGI per return (in whole dollars) | Average income tax per return (in whole dollars) | Income tax as a percentage of AGI |
|---|---|---|---|---|---|---|
| Under $15,000 | 37,315 | $ 200,248 | $ 3,306 | $ 5,366 | $ 89 | 1.7% |
| $15,000 under $30,000 | 29,581 | 650,044 | 23,749 | 21,975 | 803 | 3.7% |
| $30,000 under $50,000 | 24,536 | 957,783 | 62,190 | 39,036 | 2,535 | 6.5% |
| $50,000 under $100,000 | 28,196 | 1,984,569 | 178,486 | 70,385 | 6,330 | 9.0% |
| $100,000 under $200,000 | 9,750 | 1,291,062 | 176,173 | 132,417 | 18,069 | 13.6% |
| $200,000 or more | 3,007 | 1,681,201 | 386,515 | 559,096 | 128,538 | 23.0% |
| **Total** | **132,385** | **$ 6,764,907** | **$ 830,419** | | | |




| Total Assets (in thousands) | Income subject to tax (in millions) | Total income tax after credits (in millions) | Percentage of income tax after credits to taxable income |
|---|---|---|---|
| Zero Assets | $7,476 | $1,987 | 26.6% |
| $1 under $500 | 8,159 | 1,435 | 17.6% |
| $500 under $1,000 | 3,541 | 785 | 22.2% |
| $1,000 under $5,000 | 10,482 | 2,994 | 28.6% |
| $5,000 under $10,000 | 6,240 | 2,045 | 32.8% |
| $10,000 under $25,000 | 9,033 | 2,941 | 32.6% |
| $25,000 under $50,000 | 8,208 | 2,677 | 32.6% |
| $50,000 under $100,000 | 10,321 | 3,297 | 31.9% |
| $100,000 under $250,000 | 20,870 | 6,516 | 31.2% |
| $250,000 or more | 615,006 | 152,840 | 24.9% |
| **Total** | **$699,336** | **$177,517** | **25.4%** |

# Appendices

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# Appendix A: Full Report of Treasury's FY 2006 Performance Measures by Focus and Strategic Goal

## FY 2006 PERFORMANCE SUMMARY

This section reports the results of Treasury's official performance measures by focus and strategic goal (and further by bureau/organization) for which targets were set in the FY 2006 Performance Plan (as presented in the FY 2007 Congressional Justification for Appropriations and Performance Plans). For each performance measure, there is a definition for the measure, performance levels and targets for three previous fiscal years (where available), the performance target and actual for the report year, and proposed performance targets for next fiscal year (where available). The report examines unrealized performance targets and presents actions for improvement.

The purpose of Treasury's strategic management effort is to develop effective performance measures to achieve the goals, objectives and activities that will improve *results* delivered to the American public. In its final performance plan for FY 2006 that the Department transmitted to Congress, as part of the FY 2007 budget, Treasury detailed its performance targets.

Overall, the Department established 134 performance targets in FY 2006. Of these, 9 are baseline, 8 were discontinued and 1 had no data available at the time of this report. Of the remaining 116 measures, Treasury met or exceeded 81 targets and did not meet 35 of its targets.

| FY 2006 Treasury-wide Performance Summary | | | | | |
|---|---|---|---|---|---|
| Total Measures | Targets Met | Targets Unmet | Baseline | Disc | NA |
| 134 | 81 (60%) | 35 (26%) | 9 (7%) | 8 (6%) | 1 (1%) |

### Definitions and Other Important Information:

Determination of Official Measures: A rigorous process is followed to maintain internal controls when establishing or modifying performance measures. To be included in the PAR report, a performance measure must be in the performance budget for the year in question, and must be approved by the Performance Reporting System administrator

**Actuals** For most of the measures included in this report, the FY 2006 actual data is final. Some of the actual data for FY 2006 are estimates at the time of publication, which are indicated by an asterisk (*). Actual data for these estimated measures will be presented in the FY 2008 Congressional Justification for Appropriations and the FY 2007 Performance and Accountability Report. The actual data for previous years throughout this report is the most current data available and may not reflect previous editions of the Performance and Accountability Report and the Congressional Justification.

**Targets** The targets shown for FY 2007 are proposed targets and are subject to change. The final targets will be presented in the FY 2008 Congressional Justification for Appropriations. Also included in this report are the previous year's final targets for each performance measure.

**Target Met?** For each fiscal year that there is a target and an actual number, the report tells the reader whether the target was met or not. If the target is met, "Y" will be shown. If the target was not met, "N" will be shown.

**Definition** All performance measures in this report have a detailed definition describing the measure and summarizing the calculation.

**Source** The basis for the data is included in this report.

**Future Plans/Explanation for Shortfall** If a performance target is not met, the report includes an explanation as to why Treasury did not meet its target, and what it plans to do to improve performance in the future. If a performance target is met, the report includes what future plans Treasury has to either match FY 2006 performance, or improve on that performance in future years. Explanations may also include justification for any expected degradation in performance.

**Not Available** Some measures indicated as "Not Available" did not have actual data available at the time the FY 2006 Performance and Accountability Report was published. Some data will be available after publication and will be reported in the FY 2007 Performance and Accountability Report and the FY 2008 Congressional Justification for Appropriations.

**Discontinued** Some measures will be discontinued in the FY 2008 Congressional Justification for Appropriations and the FY 2006 Performance and Accountability Report. New measures are sometimes developed in order to better measure performance; when this happens, the measure being replaced is discontinued, and an explanation is provided.

**Baseline Measures** There are 9 new FY 2006 measures included in this report. These measures undergo a process where new baseline values (data actual and targets determined for the very first time) are established during the current fiscal year. Baseline values facilitate target-setting in the future.

**Additional Information** Additional Information relating to Treasury's performance management can be found at *http://www.treas.gov/offices/management/budget/planningdocs/index.html*

## Legend

| | |
|---|---|
| * | Indicates actual data is estimated and subject to change |
| Oe | Outcome Measure |
| E | Efficiency Measure |
| Ot | Output/Workload Measure |

## Goal: Promote Prosperous U.S. and World Economies

### Objective: Stimulate Economic Growth and Job Creation

### Community Development Financial Institutions Fund

**Measure: Administrative costs per number of Bank Enterprise Award (BEA) Applications processed ($) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | | Baseline | 1280 | 1455 |
| Actual | | | 1280 | 1630 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition:** The fixed and variable cost per application for Bank Enterprise Award (BEA) applications.

**Source:** The Fund will analyze the cost of materials as well as staff time and contractor's time to determine the total cost per application.

**Future Plans/Explanation for Shortfall:** The Fund did not achieve the goal of $1,280 for FY 2006. The formula for this measure is the total costs of processing all BEA applications divided by the number of applications processed. The Fund received 23% fewer BEA applications in FY 2006 than it did in FY 2005. Most of the costs associated with processing applications are fixed (such as information technology costs) and so are not directly related to the number of applications received. Accordingly, while the Fund expects the total cost of processing all applications to change based on the change in the number of applications received, it would not expect the costs to change proportionally. In FY 2006, the total cost of processing all BEA applications decreased by 2%. Since this percentage is much smaller than the decrease in the number of applications received, the Fund will now determine the extent that variable costs contributed to this decrease. If variable costs did not decrease in proportion to the number of BEA applications received, the Fund will determine the reason and make changes to decrease these variable costs in the future.

**Measure: Increase in community development activities over prior year for all BEA program applicants ($ in millions) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | Baseline | 307 | 134 | 81 | 100 |
| Actual | 138 | 307 | 103 | 318 | |
| Target met? | Y | Y | N | Y | |

**Definition:** This measures the Bank Enterprise Award (BEA) applicants' increase in qualified community development activites over prior year.

**Source:** Each BEA Program applicant is required to submit an application containing a Report of Transactions. The BEA Program Unit administers the BEA application. All reports are submitted electronically and the data is stored in the Fund's databases.

**Future Plans/Explanation for Shortfall:** Annual performance targets for the increase in investments in community development are based on annual BEA funding levels as well as actual past performance. At the time the Fund set its FY 2006 performance target, the FY 2006 BEA funding level was not established. The Fund underestimated the BEA funding level thus leading to an underestimate of the increase in community development investment. However, the magnitude of the performance underestimate far outweighed the underestimate in the funding level. In the future, the Fund will re-examine its formula for establishing performance targets which may lead to weighing past performance more heavily than funding level.

| Measure: Administrative costs per Financial Assistance (FA) application processed (E) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | Baseline | 5130 | 0 |
| Actual | | | 5130 | 8710 | |
| Target met? | N/A | N/A | **Y** | **N** | |

**Definition**: The cost per application for Financial Assistance (FA) applications.

**Source**: The Fund will analyze the cost of materials as well as staff time and contractor's time to determine the total fixed and variable cost per application.

**Future Plans/Explanation for Shortfall:** The Fund did not achieve the goal of $5,130 for FY 2006. The formula for this measure is the total costs of processing all FA applications divided by the number of applications processed. The Fund received 49% fewer FA applications in FY 2006 than it did in FY 2005. Most of the costs associated with processing applications are fixed (such as information technology costs) and so are not directly related to the number of applications received. Accordingly, while the Fund expects the total cost of processing all applications to change based on the change in the number of applications received, it would not expect the costs to change proportionally. In FY 2006, the total cost of processing all FA applications decreased by 10%. Since this percentage is much smaller than the decrease in the number of applications received, the Fund will now determine the extent that variable costs contributed to this decrease. If variable costs did not decrease in proportion to the number of FA applications received, the Fund will determine the reason and make changes to decrease these variable costs in the future.

| Measure: Number of full-time equivalent jobs created or maintained in underserved communities by businesses financed by CDFI Program Awardees and New Markets Tax Credit (NMTC) Allocatees (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 33830 | 5852 | 26995 | 29158 | 34009 |
| Actual | 9141 | 9212 | 23656 | 22329 | |
| Target met? | **N** | **Y** | N | N | |

**Definition:** An employee that works at least a 35-hour workweek is considered a full-time equivalent (FTE). In calculating the number of FTEs, part-time employees are combined into FTEs. For example, two part-time employees that each work 17.5 hours per week are combined to count as one FTE. Jobs maintained are jobs at the business at the time the loan or investment is made. Jobs created are new jobs created after the loan or investment is made. Jobs created and maintained serve as an important indicator of the economic vitality of underserved areas. Underserved communities are those that qualify as CDFI Program Target Markets (which include a specific geography called an Investment Area or a specific community of people with demonstrated lack of access to credit, equity, or financial services called a Low-Income Targeted Population or an Other Targeted Population). Underserved communities are also those that qualify as New Markets Tax Credit (NMTC) Low Income Communities.

**Source:** Each awardee and allocatee collects and tracks job data in its own management information system(s). The information is self-reported by awardees and allocatees. Many organizations track the number of jobs projected to be created. A smaller number collect annual information on actual number of jobs created. Some do not collect the data and respond "don't know." Each CDFI Financial Assistance awardee and NMTC Allocatee is required to complete a Transaction Level Report. CDFI awardees report FTE data in the Institution Level Report or Transaction Level Report, while NMTC Allocatees report FTE data in the Transaction Level Report only. Performance covers those CDFI awardees and NMTC allocates required to submit annual performance data to the Fund for the relevant reporting period, and submitted their reports on time.

**Future Plans/Explanation for Shortfall:** The Fund did not achieve the goal of 29,158 full-time equivalent (FTE) jobs expected for FY 2006. The shortfall is driven by an overestimate of the number of jobs that the NMTC program would create or maintain per year. The Fund developed the FY 2006 NMTC FTE jobs target based on data from the allocatees' FY 2003 performance. The Fund encountered two difficulties when working with the FY 2003 data set. First, the data set is small representing only eight organizations and 28 transactions. Second, the data set represents the initial year of the NMTC activity, so the transactions may not be "typical" moving forward. The Fund is currently reviewing allocatees' FY 2005 actual performance data. Once these data are final, the Fund plans to use them and the FY 2004 actual performance data to revise future year performance targets.

| Measure: Administrative costs per number of Native American CDFI Assistance (NACA) applications processed ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 10050 | 9090 |
| Actual | | | 10050 | 8130 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The Fund will determine the total cost associated with Native American CDFI Assistance (NACA) applications based on fixed and variable costs.

**Source**: The Fund will capture this information through budget documentation.

**Future Plans/Explanation for Shortfall**: The Fund exceeded its goal of $10,050 for FY 2006. The formula for this measure is the total costs of processing all Native Initiatives (NI) Program applications divided by the number of applications processed. The Fund received 24% more NI applications in FY 2006 than it did in FY 2005. Most of the costs associated with processing applications are fixed (such as information technology costs) and so are not directly related to the number of applications received. Accordingly, when the number of applications increases, the Fund expects the cost per application to decrease almost proportionately, which in fact happened: there was a 19% decrease in the cost per application. The Fund will continue to monitor its fixed costs to ensure they remain constant, or decrease if new efficiencies can be achieved.

| Measure: Administrative costs per number of New Markets Tax Credit (NMTC) applications processed ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 5390 | 4875 |
| Actual | | | 5390 | 4360 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The cost per application for New Markets Tax Credit (NMTC) applications.

**Source**: The Fund will analyze the cost of materials as well as staff time and contractor's time to determine the total fixed and variable cost per application.

**Future Plans/Explanation for Shortfall**: The Fund exceeded its goal of $5,390 for FY 2006. The formula for this measure is the total costs of processing all NMTC Program applications divided by the number of applications processed. The Fund received 21% more NMTC applications in FY 2006 than it did in FY 2005. Most of the costs associated with processing applications are fixed (such as information technology costs) and so are not directly related to the number of applications received. Accordingly, when the number of applications increases, the Fund expects the cost per application to decrease almost proportionately, which in fact happened: there was a 19% decrease in the cost per application. The Fund will continue to monitor its fixed costs to ensure they remain constant, or decrease if new efficiencies can be achieved. .

| **Measure: Amount of investments in low-income communities that Community Development Entitites (CDEs) have made with capital raised through their New Markets Tax Credit (NMTC) tax credit allocations ($ in billions) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | Baseline | 1.4 | 1.6 | 2.1 |
| Actual | | .1 | 1.1 | 2 | |
| Target met? | N/A | **Y** | **N** | **Y** | |

**Definition**: Amount of investments in Low Income Communities that Community Development Entitites have made with capital raised through their New Markets Tax Credits (NMTC) allocations. The Fund will report NMTC Qualified Low-Income Community Investments (QLICIs) that are supported by NMTC Qualified Equity Investments (QEIs).

**Source**: The Fund will capture the data in the CDEs' annual Institution Level and Transaction Level Reports. Performance covers those NMTC allocates required to submit annual performance data to the Fund for the relevant reporting period, and submitted their reports on time.

**Future Plans/Explanation for Shortfall**: CDEs exceeded the anticipated $1.6 billion in QLICIs, by closing $2.0 billion in QLICIs. Given the newness of the NMTC Program, the Fund is just beginning to get a realistic picture of how quickly the NMTC dollars will flow. The Fund will continue to analyze the increasing rate that allocatees raise equity and make qualified investments, and use this analysis to set appropriate targets going forward.

| **Measure: Annual percentage increase in the total assets of Native CDFIs (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | Baseline | 35 | 33 | 33 |
| Actual | | 39 | 103 | 182 | |
| Target met? | N/A | **Y** | **Y** | **Y** | |

**Definition**: Measure the percent change in total assets that Native CDFIs report from one year to the next. The Fund will calculate: [Total Assets in Current Year - Total Assets in Previous Year] / [Total Assets in Previous Year]

**Source**: The Native CDFIs financial data is captured through the annual Institution Level Report. Performance covers those Native CDFI awardees required to submit annual performance data to the Fund for the relevant reporting period, and submitted their reports on time.

**Future Plans/Explanation for Shortfall**: Between FY 2005 and FY 2006, Native awardees showed growth of 182% in assets, far exceeding the projected 33% growth. The tremendous growth was driven by nearly every organization showing some growth and a single start-up CDFI that increased its assets more than ten-fold. While the Fund has limited control over the change in total assets of its awardees, the Fund can promote growth by continuing to provide financial and technical assistance to Native Awardees. The provision of such assistance will help ensure that the Fund meets its targets for this measure in the future.

| **Measure: Dollars of private and non-CDFI Fund investments that CDFIs are able to leverage because of their CDFI Fund Financial Assistance. (in millions) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 1150 | 669 | 500 | 1100 | 861 |
| Actual | 1623 | 1300 | 1800 | 1400 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: This measure represents the dollars of private and non-CDFI Fund investments that CDFIs are able to leverage because of their CDFI Fund Financial Assistance (FA) award. For CDFIs, leverage is defined as the one-to-one non-federal match (as required by the FA program), plus funds the CDFI is able to leverage with CDFI Fund FA grant and equity dollars, plus dollars that the awardees' borrowers leverage for projects. (Project leverage example - Of the total financing needed for a housing development is $5 million and the awardee lends $1 million, while other investors lend the remaining $4 million, then the $4 million is the project leverage).

**Source**: FA award disbursements are made once CDFIs provide documentation showing that they have received or been committed matching funds. Disbursements of FA are tracked by the Financial Manager and are used as the proxy for matching funds raised. The CDFI Program annual Institution Level Report captures the leverage ratio for FA grants and equity dollars, as well as project level leverage.

**Future Plans/Explanation for Shortfall**: The Fund exceeded the target of leveraging $1.1 billion in private dollars by nearly 20 percent. In FY 2006, CDFI Program awardees leveraged each dollar of the Fund's FA awards: 27:1, consisting of required matching funds, new debt they were able to secure because of Fund grant and equity awards, and additional financing from other sources for the projects financed by CDFIs. The Fund's leverage projection is based on program funding levels as well as past leverage performance. Leverage performance has grown each of the past few years and the Fund set its FY 2006 target consistent with this trend. Nonetheless, this is the second year in a row that the CDFI Fund has exceeded this target by a significant amount. The Fund will review its projection formula to determine if it should be adjusted to produce more aggressive targets.

## Departmental Offices

| **Measure: Level of MDB grant financing and satisfactory results measurements (World Bank/IDA Grants) [in millions] (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | Baseline | 1602 | 1728 | 3555 | 2025 |
| Actual | 1233 | 1681 | 1925 | 2025 | |
| Target met? | Y | Y | Y | N | |

**Definition**: Captures the portion of resources provided to borrowers from each Multilateral Development Banks (MDB) in the form of grants and whether such grant financing contains a satisfactory results measurement framework. MDB provide financial support and professional advice for economic and social development activities in developing countries.

**Source**: MDB monthly operational report, special requests to MDBs for loan and grant approvals, MDB annual reports and U.S. voting positions. This information is measured on an annual basis.

**Future Plans/Explanation for Shortfall**: After review the determination has been made that this metric does not adequately capture the progress made in this area. Subsequently, this metric will be discontinued in FY 2007. IA will be conducting a review of all performance metrics in FY 2007 and hopes to replace this metric with one that better conveys the key issues of the organization.

| Measure: Level of MDB grant financing and satisfactory results measurements (African Development Bank/AFDF Grants) (in millions) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 294 | 216 | 870 | 870 |
| Actual | 240 | 65 | 46 | 700 | |
| Target met? | Y | N | N | N | |

**Definition**: Captures the portion of resources provided to borrowers from each Multilateral Development Banks (MDB) in the form of grants and whether such grant financing contains a satisfactory results measurement framework. MDA provide financial support and professional advice for economic and social development activities in developing countries.

**Source**: MDB monthly operational report, special requests to MDBs for loan and grant approvals, MDB annual reports and U.S. voting positions. This information is measured on an annual basis.

**Future Plans/Explanation for Shortfall**: After review the determination has been made that this metric does not adequately capture the progress made in this area. Subsequently, this metric will be discontinued in FY 2007. IA will be conducting a review of all performance metrics in FY 2007 and hopes to replace this metric with one that better conveys the key issues of the organization.

| Measure: U.S. unemployment rate (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 5.6 | 5.3 | 5.2 | 5.1 |
| Actual | 5.9 | 5.4 | 5.1 | 4.8* | |
| Target met? | Y | Y | Y | Y | |

**Definition**: The percentage of the U.S. labor force reported as unemployed in the last quarter of the reference fiscal year.

**Source**: Data are collected from the U.S. Department of Labor, Bureau of Labor Statistics

**Future Plans/Explanation for Shortfall**: : The Treasury Department has an important operational and policy role in creating opportunities for U.S. citizens as well raising the standards of living through the formulation and execution of United States economic and financial policies that promote growth. The Treasury Department will continue to support U.S. economic growth by developing and implementing policies for domestic economic development, tax programs, banking and financial institutions, and other fiscal matters.

| Measure: US Real Gross Domestic Product (GDP) growth rate (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 0 | 3.5 | 3.6 | 3.4 | 3.3 |
| Actual | 3.3 | 4.5 | 3.6 | 3.4* | |
| Target met? | Y | Y | Y | Y | |

**Definition**: Real GDP is the most comprehensive measure of economic activity and is compiled throughout the year to reflect developments in each calendar quarter.

**Source**: Data are provided by the Department of Commerce, Bureau of Economic Analysis (BEA).

**Future Plans/Explanation for Shortfall**: The Treasury Department plays both a policy and an operational role in promoting prosperous U.S. and world economies. The Treasury Department will continue to support U.S. economic growth by developing and implementing policies for domestic economic development, tax programs, banking and financial institutions, and other fiscal matters. **Actual Performance was an estimate.

| Measure: Number of new Free Trade Agreement (FTA) negotiations and Bilateral Investment Treaty (BIT) negotiations underway or completed (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 5 | 9 | 7 |
| Actual | | | 7 | 12 | |
| Target met? | N/A | N/A | **Y** | **Y** | |

**Definition**: The number of international trade or investment agreements underway or completed during the period and the number of those that reflect commitments to high standards such as that includes new commitments by a foreign government to open its financial services markets to U.S. providers. It includes bilateral agreements and multilateral undertakings (e.g., WTO) from which the U.S. benefits.

**Source**: International Affairs staff and U.S. Trade Representative's office reporting.

**Future Plans/Explanation for Shortfall**: Agreements with 12 countries were under negotiation, completed, or implemented in FY 2006, compared to the planned performance of 9 countries. Treasury expects the workload to intensify this year with the imminent expiration of Trade Promotion Authority (TPA) by the middle of CY 2007. There are seven FTAs/BITs from FY 2006 or earlier years that are still being implemented or negotiated, as well as other stalled negotiations that may re-emerge. FTA/BIT negotiations normally stretch over many months and often into years, depending upon the complexity of the negotiations and the willingness of the participants to compromise. An extension of TPA beyond June 2007 could have a significant affect on the timing for completing FTA negotiations. In addition to negotiating new agreements, a relatively new and increasingly important component of the workload deals with monitoring and enforcing agreements already in place.

| Measure: Level of MDB grant financing and satisfactory results measurements (Grants as a % of AFDF FY Commitment) (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | Baseline | 21 | 19.5 | 35 | 28.5 |
| Actual | 17 | 39.2 | 21.8 | 30.5 | |
| Target met? | **Y** | **Y** | **Y** | **N** | |

**Definition**: The portion of resources provided to borrowers from each Multilateral Development Banks (MDB) in the form of grants and whether such grant financing contains a satisfactory results measurement framework. MDBs provide financial support and professional advice for economic and social development activities in developing countries.

**Source**: MDB monthly operational report, special requests to MDBs for loan and grant approvals, MDB annual reports and U.S. voting positions. This information is measured on an annual basis.

**Future Plans/Explanation for Shortfall**: Treasury successfully met its target to increase the number of grants in FY 2005 and FY 2006. Staff will continue its efforts to encourage measurable performance. The level of grants and the percentage of total AfDF commitments are decreasing because of the successful implementation of the Multilateral Debt Relief Initiative (MDRI). The debt relief provided to AfDF countries through MDRI has reduced the debt vulnerability of these countries and increased their capacity to take on a greater share of highly congressional loans from the AfDF. This metric will be reviewed in FY 2007 to determine its appropriateness in light of the impact of MDRI on debt vulnerability.

| Measure: Improve International Monetary Fund (IMF) effectiveness and quality through periodic review of IMF programs (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 90 | 90 | 90 |
| Actual | | | 78 | 100 | |
| Target met? | N/A | N/A | **N** | **Y** | |

**Definition**: This measure tracks efforts by International Affairs (IA) staff to monitor quality of IMF country programs and ensure the application of appropriately high standards. IA staff endeavors to review each country program and provide a synopsis and recommendation for action at least one week before each program is voted on by the IMB Board. The measure tracks the percentage of times the staff review is completed in a timely manner (at least one week before Board action) to allow for alterations in language if deemed necessary.

**Source**: International Affairs staff tracks and accounts for actions undertaken during the reporting period.

**Future Plans/Explanation for Shortfall**: IA staff successfully reviewed IMF country programs in 100% of cases. In 22% of cases, alternative urgent priorities resulted in circulation of the program review after the one-week target but still before the program vote. Treasury will continue to emphasize IMF effectiveness by reviewing 90% of its programs in FY 2007.

| Measure: Encourage movement towards flexible exchange rate regimes (Oe) [DISCONTINUED FY 2007] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 4 | Discontinued |
| Actual | | | 3 | 2 | |
| Target met? | N/A | N/A | **Y** | **N** | |

**Definition**: Encouraging large economies with fixed or rigid exchange rate regimes to adopt flexible exchange rate regimes is a key to addressing global imbalances and assuring sustained global growth. International Affairs staff engages in and support economic dialogue with these countries, such as China, and provide technical assistance and support so those countries will be able to transition from fixed to flexible regimes. This measure captures the work Treasury is doing to support the transition, and shows the number of actions Treasury has taken to encourage flexible exchange rate regimes.

**Source**: International Affairs staff tracks and accounts for actions undertaken during the reporting period.

**Future Plans/Explanation for Shortfall**: : After review the determination has been made that this metric does not adequately capture the progress made in this area. Subsequently, this metric will be discontinued in FY 2007. IA will be conducting a review of all performance metrics in FY 2007 and hopes to replace this metric with one that better conveys the key issues of the organization.

| Measure: Level of MDB grant financing and satisfactory results measurements (Grants as a % of IDA FY Commitment) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 22 | 19.6 | 30.4 | 30 |
| Actual | 17 | 18.8 | 21.4 | 25 | |
| Target met? | Y | N | Y | N | |

**Definition**: The portion of resources provided to borrowers from each Multilateral Development Banks (MDB) in the form of grants and whether such grant financing contains a satisfactory results measurement framework. MDB provide financial support and professional advice for economic and social development activities in developing countries.

**Source**: MDB monthly operational report, special requests to MDBs for loan and grant approvals, MDB annual reports and U.S. voting positions. This information is measured on an annual basis.

**Future Plans/Explanation for Shortfall**: : Treasury successfully met its target to increase the number of grants in FY 2005 and FY 2006. Staff will continue its efforts to encourage measurable performance. The level of grants and the percentage of total IDA commitments are decreasing because of the successful implementation of the Multilateral Debt Relief Initiative (MDRI). The debt relief provided to IDA countries through MDRI has reduced the debt vulnerability of these countries and increased their capacity to take on a greater share of highly concessional loans from the IDA. This metric will be reviewed in FY 2007 to determine its appropriateness in light of the impact of MDRI on debt vulnerability

## Objective: Provide a Flexible Legal and Regulatory Framework

## Comptroller of the Currency

| Measure: Percentage of licensing applications and notices completed within established timeframes. (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 95 | 95 | 95 | 95 | 95 |
| Actual | 97 | 96 | 96 | 94 | |
| Target met? | Y | Y | Y | N | |

**Definition**: This measure reflects the extent to which OCC meets its established timeframes for reaching decisions on licensing applications and notices. The OCC's timely and effective approval of corporate applications and notices contributes to the nation's economy by enabling national banks to engage in corporate transactions and introduce new financial products and services.

**Source**: The Chief Counsel's office uses the Corporate Activity Information System (CAIS) to identify applications completed during the fiscal year. For each filing, the actual decision date is compared to the target action date to determine whether the application was completed within established standards. The percentage is determined by comparing the number of licensing applications processed within the required timeframes to the total number of licensing applications processed during the fiscal year. The processing time is the number of calendar days from the date of OCC receipt to the date of OCC's decision. The established processing timeframe depends on the application type and if the application qualifies for expedited processing.

**Future Plans/Explanation for Shortfall**: This year, several applications that initially appeared to be routine in nature required additional processing time due to unique circumstances that became apparent in the course of application review, for example, branch applications with historical preservation issues. This caused the OCC performance in this measure to be marginally below target. To process licensing applications within establish timeframes the OCC will effectively evaluate applications as they are filed ensuring those applications with unique, complex or novel features are properly directed to appropriate OCC divisions in a timely manner. Those applications that are identified as routine will be processed at the district level with the necessary delegations to act on these applications within established timeframes.

## Office of Thrift Supervision

| Measure: Difference between the inflation rate and the OTS assessment rate increase (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 0 | 0 | 0 | 0 | 0 |
| Actual | 0 | 0 | 0 | 0 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: Without compromising responsibilities and the risk-based examination approach, OTS strives to efficiently manage its operations and budget to ensure that assessment rate increases do not exceed the inflation rate. However, if OTS believes that events require more personnel or other expenditures, OTS may increase assessments to raise the required resources. Annually, OTS analyzes its operating costs and compares them to the assessments it charges savings associations and holding companies in order to achieve a structure that keeps assessment rates as low as possible while providing OTS with the resources necessary for effective supervision.

**Source**: OTS's current assessment rates are specified in OTS's Thrift Bulletins (the TB 48 series). OTS calculates this measure annually for its January assessment cycle or whenever a new assessment bulletin is issued. The percent increase in assessment rates is calculated and compared with the inflation rate as specified in OTS's Thrift Bulletins. The difference between the inflation rate and the assessment rate increase is targeted to be greater than or equal to zero.

**Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry.

# Goal: Promote Stable U.S. and World Economies

### Objective: Increase Citizens Economic Security

## Departmental Offices

| Measure: On-time payment of federal loan guarantee fees and repayment of underlying loans by borrowers (ATSB loans) (%) (E) [DISCONTINUED FY 2007] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 100 | 100 | Discontinued |
| Actual | | | 100 | 100* | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: Federal credit instruments (loan guarantees) were made to air carriers who suffered loss and are in financial difficulty due to the September 11, 2001 terrorist attacks. Air Transportation Stabilization Board (ATSB) closely monitors a loan guarantee portfolio to determine the financial health of the borrowers and compliance with the terms of the loan agreements. This measure tracks the timely payment of fees and principal back to the U.S. Treasury. Borrowers must submit monthly and quarterly financial reports which are reviewed by the ATSB.

**Source**: Transaction data regarding guarantee fee payments come from the Financial Reporting Branch of Treasury's Departmental Offices.

**Future Plans/Explanation for Shortfall**: During FY 2006 three of the remaining four airlines paid their loans in full either on schedule or ahead of schedule. The debt for the remaining airline will be resolved in the coming months. As a result, this metric will be discontinued in FY 2007.

## Alcohol and Tobacco Tax and Trade Bureau

**Measure: Percent of electronically filed Certificate of Label Approval applications (%) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 10 | 7 | 16 | 27 | 47 |
| Actual | 3 | 10 | 25 | 38 | |
| Target met? | N | Y | Y | Y | |

**Definition**: Calculated by dividing the number of e-filed applications by the total Certificate of Label Approval applications (COLA) submissions (paper and electronic)

**Source**: Data is captured through the COLAs Online database system. There are periodic statistical reports, searches, and queries that are generated.

**Future Plans/Explanation for Shortfall**: TTB works diligently to educate industry members through access to Label Specialists and seminars to discuss electronic filing. This access and education will continue in the future in order to increase the number of electronic filings.

**Measure: Percentage of COLA approval applications processed within 9 calender days of receipt (%) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | Baseline | 60 | 30 | 55 | 45 |
| Actual | 57 | 23 | 50 | 44 | |
| Target met? | Y | N | Y | N | |

**Definition**: The percentage of Certificate of Label Applications (COLA) processed electronically and by paper within 9 days of receipt.

**Source**: Data is captured thru the COLAs Online data base system. There are periodic statistical reports, searches, and queries that are generated.

**Future Plans/Explanation for Shortfall**: This aggressive measure shows a shortfall as a result of a large rise in applications which are processed by a constant FTE level. Also, the complexity of the review process has increased significantly since the 9-day goal was put in place in the early 90s. The workload increased dramatically during the year while the FTE levels remained constant. TTB has just undergone a Protect the Public Business Process Reengineering Study. TTB anticipates that implementing the recommendations will help provide an impetus for meeting FY07 measures.

| **Measure: Percentage of permit application (original and amended) processed by the National Revenue Center within 60 days (%) (E)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 67 | 80 | 80 |
| Actual | | | 81 | 86 | |
| Target met? | N/A | N/A | **Y** | **Y** | |
| **Definition**: The portion of permit applications (original and amended) that are processed with sixty days of receipt at the NRC. | | | | | |
| **Source**: NRC generates statistical reports, searches and queries. In-place data integrity controls exist within the application to validate the data. | | | | | |
| **Future Plans/Explanation for Shortfall**: TTB continues to process applications above its target. Currently, TTB has stretched its resources considerably to achieve this goal. The organization will attempt to maintain this performance level. This increase occurred as a result of business process reengineering (BPR) nearly a year and a half ago. The BPR implementation will help maintain this measure for FY 2007. | | | | | |

## Objective: Improve the Stability of the International Financial System

## Departmental Offices

| **Measure: Percentage of grant and loan proposals containing satisfactory frameworks for results measurement (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | Baseline | 90 | 90 |
| Actual | | | 78 | 88 | |
| Target met? | N/A | N/A | **Y** | **N** | |
| **Definition**: The percentage of grant and loan project proposals that contain a satisfactory framework for measuring project results (such as outcome indicators, quantifiable and time-bound targets, etc.) This information is measured on an annual basis. | | | | | |
| **Source**: MDB monthly operational report, special requests to MDBs for loan and grant approvals, MDB annual reports and U.S. voting positions | | | | | |
| **Future Plans/Explanation for Shortfall**: Treasury saw the number of grants with results-oriented measures increase from 78% in FY05 to 88% in FY06. This performance leaves us just short of our long term goal of 90% success. Staff will continue its efforts to encourage measurable performance. | | | | | |

## Goal: Preserve the Integrity of Financial Systems

### Objective: Disrupt and Dismantle Financial Infrastructure of Terrorists, Drug Traffickers, and Other Criminals and Isolate Their Support Networks

### Departmental Offices

| **Measure: Maintain the annual increase in the number of and significance to the foreign narcotics traffickers of new designated targets (Oe) [DISCONTINUED FY 2006]** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | 136 | 136 | Discontinued | Discontinued |
| Actual | | 136 | 504 | | |
| Target met? | N/A | **Y** | **Y** | | |

**Definition**: Office of Foreign Assets Control (OFAC) systematically attacks the foreign drug cartels' networks of business investments and money laundering, especially their penetrations of the legitimate economy, by exposing, isolating, and impeding or incapacitating them, principally through denying them access to the U.S. financial and economic system. Narcotics designations (Specifically Designated Narcotics and Trafficers and KPA (Kingpin Act) Tier Is (top designations made under the Act) and Tier IIs (designations of those entities associated with the Tier I)) are a combination of major foreign drug traffickers (individuals and groups) and the persons (individuals and entities) that serve as their agents, straw men, operatives, front companies, money laundering connections, and penetrations into legitimate business. This is accomplished by investigation and research to determine who they are and to place them on the designation list.

**Source**: The evidence used to develop the designation cases is examined for sufficiency on a case-by-case basis internally and involving OFAC's legal counsel and the Justice Department.

**Future Plans/Explanation for Shortfall**: This measure will be discontinued in FY 2006.

| **Measure: Customer satisfaction with Office of Intelligence Analysis (OIA) analysis in terms of its accuracy, timeliness, and relevance (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | | | |
| Actual | | | | | |
| Target met? | N/A | N/A | N/A | N/A | |

**Definition**: Customer satisfaction with OIA analysis in terms of its accuracy, timeliness, and relevance.

**Source**: As a first step in this process, in FY 2006, we will be developing an appropriate methodology which we can use to measure customer satisfaction. This may take the form of a "customer satisfaction survey." We will be using the results from FY 2006 as a baseline by which we can measure performance in future years.) The survey will measure OIA's ability to meet needs and expectations of senior Treasury officials for intelligence support. Among the relevant factors to be measured are the following: whether intelligence provided to key decision-makers was factually correct and/or analytically precise, whether it filled gaps in knowledge on relevant/critical topics, and whether it was provided in time to influence key events or policy decision.

**Future Plans/Explanation for Shortfall**: : Baseline in FY 2006. OIA is currently refining its customer service measure to capture the usefulness of its products for its varied customers. These include both policymakers -- within the Treasury, at the White House and elsewhere – as well as its Intelligence Community counterparts. OIA is also putting together a working group, comprising its senior leadership, budget officer, as well as several analysts to lead this effort. OIA is in the process of reaching out to other IC agencies, including the FBI and State Department, which have similar metrics in place. Over the next several months, OIA will continue to work to refine this measure and the method of capturing customer service information. An additional year of data collection is expected necessary in order to have sufficient data to establish baseline values. This measure may be discontinued if a new measure is developed.

## Financial Crimes Enforcement Network

| Measure: Average time to process enforcement matters (in Years) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 1.5 | 1.2 | 1.1 | 1 | 1 |
| Actual | 1.3 | 1 | 1.3 | 1 | |
| Target met? | Y | Y | N | Y | |
| **Definition**: The average time to process an enforcement matter is determined from the date a case is referred from the Office of Compliance to the date the charging (or action) letter is issued. | | | | | |
| **Source**: The data for this measure is captured through an internal database that stores enforcement matters. The database records the date cases are received, the analyst assigned, the statute of limitations date, and the date each case was closed. | | | | | |
| **Future Plans/Explanation for Shortfall**: FinCEN met its target. The year-end result reflects effective use of resources. FinCEN will strive to maintain an average 1 year processing time by directing resources towards the timely and appropriate resolution of significant cases. | | | | | |

| Measure: Number of users accessing BSA data electronically (Oe) [DISCONTINUED FY 2006] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 900 | 1700 | 3000 | Discontinued | Discontinued |
| Actual | 1105 | 2181 | 3941 | | |
| Target met? | Y | Y | Y | | |
| **Definition**: The number of individuals with current passwords who have accessed the Bank Secrecy Act data through the Secure Outreach network in the past 90 days. | | | | | |
| **Source**: The list can be checked through the Profile function at the Detroit Computing Center | | | | | |
| **Future Plans/Explanation for Shortfall**: Discontinued in FY 06. This is not an outcome measure, and it will be replaced with a more accurate measure of performance. | | | | | |

| Measure: Percentage of customers finding FinCEN's analytic support valuable (%) (Oe) [DISCONTINUED FY 2007] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 75 | Discontinued |
| Actual | | | 73 | 69 | |
| Target met? | N/A | N/A | Y | N | |
| **Definition**: This performance measure, starting in FY 2005, combines data from surveys on strategic analytical products, investigative case reports, and investigative targets. | | | | | |
| **Source**: Bi-annual surveys | | | | | |
| **Future Plans/Explanation for Shortfall**: FinCEN did not meet its target. When the original targets were set, FinCEN had only one years worth of data to base them on. The measure has been refined through the PART process and future targets will be set accordingly based on a different measure. | | | | | |

| Measure: Percentage of customers satisfied with the BSA Direct E-Filing component (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | 90 |
| Actual | | | | 92 | |
| Target met? | N/A | N/A | N/A | Y | |

**Definition**: The measure will assess the components of BSA Direct. This will begin with the E-Filing component of BSA Direct in FY 2006. Feedback will be used to improve the system and customize it for user populations. This measure is linked to the performance goal "Accelerate the secure flow of financial information from the industries subject to the Bank Secrecy Act requirements to the law enforcement agencies that use it." The measure is meaningful because it tracks our progress toward serving the number of law enforcement and regulatory agency users accessing the BSA information through BSA Direct to support their own cases and investigations.

**Source**: Active status user survey (encompasses law enforcement and regulatory)

**Future Plans/Explanation for Shortfall**: FinCEN met its target by establishing a baseline for customer satisfaction with the e-filing component of BSA Direct. An impressive baseline was established of 92%. We have set our future targets at maintaining a 90% level of satisfaction. Once FinCEN has more data points, FinCEN will assess whether more ambitious targets are achievable.

| Measure: Number of federal and state regulatory agencies with which FinCEN has concluded memoranda of understanding/information sharing agreements (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 45 | 50 |
| Actual | | | 41 | 48 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: This measure tracks the number of Memorandum of Understanding agreements the Office of Compliance concludes with other regulators of targeted jurisdictions. This measure is meaningful because it tracks our progress in sharing information on Bank Secrecy Act compliance with the regulatory agencies that either have delegated authority to examine for Bank Secrecy Act compliance or are expending resources to review for Bank Secrecy Act compliance under other authorities (for example, many states have Bank Secrecy Act-style laws/regulations or have laws that require compliance with all applicable laws and regulations). Some states must pass legislation to permit information sharing with the Financial Crimes Enforcement Network. Ultimately, information derived from these agreements will allow us to meet the intermediate outcome measure of improving our ability to monitor industry compliance.

**Source**: Office of Compliance-maintained list of Memorandum of Understanding agreements with targeted regulators.

**Future Plans/Explanation for Shortfall**:FinCEN surpassed its target. FinCEN was able to exceed the FY06 target of 45 by aggressively pursuing agreements with state agencies. FinCEN will continue to pursue agreements with the remaining state agencies.

## Treasury Forfeiture Fund

| Measure: Percent of forfeited cash proceeds resulting from high-impact cases (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 75 | 75 | 75 | 75 | 75 |
| Actual | 80.55 | 83.95 | 81 | 72.93 | |
| Target met? | Y | Y | Y | N | |
| **Definition**: A "high impact case" is a case, based on designation or executive order, resulting in a cash forfeiture equal to or greater than $100,000. This measure is calculated by dividing the amount of cash forfeited in amounts equal to or greater than $100,000 (as measured by individual deposits that are equal to or greater than $100,000) divided by the total amount of cash forfeitures to the Fund (as of the end of the year, or other reporting period.) | | | | | |
| **Source**: The Treasury Forfeiture Fund is able to capture this data on a monthly basis and the source of the data is the Detailed Collection Report (DCR). | | | | | |
| **Future Plans/Explanation for Shortfall**: Although the total number of cash forfeitures cases in FY 2006 was up by over 10 percent compared to FY 2005, the number of high-impact cases did not rise at the same rate, resulting in the Fund missing the target by just 2 percent. While this is a small shortfall, we will work to ensure that the financial plan in FY 2007 and future years emphasizes those spending areas that will rectify this imbalance. | | | | | |

### Objective: Execute the Nation's Financial Sanctions Policies

## Departmental Offices

| Measure: Increase the number of international measures and bodies established internationally to protect the financial system from money laundering and terrorist financing (Ot) [DISCONTINUED FY 2006] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | Discontinued | Discontinued |
| Actual | | | 5 | | |
| Target met? | N/A | N/A | Y | | |
| **Definition**: Financial Action Task Force on Money Laundering (FATF) and the FATF style regional bodies (FSRBs) are the international bodies that hold members to FATF standards. At the end of FY04, such bodies existed in South America, the Caribbean, Africa, Europe and Asia Pacific. At the beginning of FY05, no such bodies existed for Central Asia, and in the Middle East/North Africa--two key regions in the fight against terrorism. This is a major achievement that will bring a range of critical jurisdictions under the financial standards of the international community. | | | | | |
| **Source**: FATF data | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| **Measure: Maintain turnaround time for license submissions with significantly increased workload. a. Requiring internal OFAC review with significantly increased workload (Days) (E) [DISCONTINUED FY 2006]** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 20 | Discontinued | Discontinued |
| Actual | | | 27.5 | | |
| Target met? | N/A | N/A | **N** | | |
| **Definition**: The number of business days to process a license application from the time it is received in the Licensing Division to the time the final determination is issued. | | | | | |
| **Source**: Database maintained by Office of Foreign Assets Control (OFAC). | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| **Measure: Maintain turnaround time for license submissions with significantly increased workload. b. Requiring Chief Counsel's and interagency review with significantly increased workload (Days) (E) [DISCONTINUED FY 2006]** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 75 | Discontinued | Discontinued |
| Actual | | | 63 | | |
| Target met? | N/A | N/A | **N** | | |
| **Definition**: The number of business days to process a license application from the time it is received in the Licensing Division to the time the final determination is issued | | | | | |
| **Source**: Database maintained by Office of Foreign Assets Control (OFAC). | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| **Measure: Turn-around time for license and interpretive submissions (Days) (E) [DISCONTINUED FY 2006]** | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 75 | Discontinued | Discontinued |
| Actual | | | 63 | | |
| Target met? | N/A | N/A | **N** | | |
| **Definition**: Timeliness in responding to inquiries from the public regarding sensitive and complex economic sanctions and minimizes disruptions to U.S. and international trade, financial and investment transactions. Timliness in licensing determinations means that Treasury is able to tailor sanctions programs to meet U.S. foreign policy goals, licensing humanitarian and other activities consistent with those goals. | | | | | |
| **Source**: Database maintained by OFAC. | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| Measure: Number of open civil penalty cases that are resolved within the Statute of Limitations period (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 85 | 85 |
| Actual | | | 85 | 85 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: Timely imposition of civil penalties plays a major role in deterring and appropriately punishing violations of sanctions by U.S. persons. OFAC receives a very high volume of law enforcement referrals regarding potential violations. It is devising strategies to reduce the backlog of civil penalty and enforcement actions and increase efficiency in drafting warning and cautionary letters, assessing penalties, negotiating penalty resolutions and processing monetary penalties.

**Source**: OFAC database.

**Future Plans/Explanation for Shortfall**: In FY 2006, 85 civil penalty cases were resolved within the statue of limitations. The target for FY 2007 has been established at 85 cases and will be achieved through continued focus and effort by Treasury staff.

| Measure: Increase the number of outreach engagements with the charitable and international financial communities (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 105 | 70 |
| Actual | | | 95 | 45 | |
| Target met? | N/A | N/A | Y | N | |

**Definition**: The effectiveness of the USG's efforts to combat terrorist financing and other forms of illicit finance depends upon the understanding and cooperation of the domestic and international private sector, particularly the financial services industries and other vulnerable sectors such as charities. The Office of Terrorist Finance and Financial Crimes (TFFC) outreach engagements allows the USG to assess first-hand domestic and international Anti-money Laundering and Combating the Financing of Terrorism (AML/CFT) practices by governments and private institutions alike and engage with these entities to ensure that they safeguard themselves and the financial system against illicit activity. When followed-up consistently, this outreach has proven to be one of our most efficacious tools for changing behavior, raising awareness, and improving capacity among foreign governments as well as domestic and foreign institutions with gaps in their AML/CFT programs.

**Source**: Data collected by the Department of Treasury's Office of Terrorism and Financial Intelligence (TFI); Terrorist Financing and Financial Crimes (TFFC).

**Future Plans/Explanation for Shortfall**: Engagement with the international and charitable sectors has always played a key role in TFFC's work. Bilateral and multilateral engagements with the public and private sectors have enabled TFFC to promote and promulgate greater transparency and accountability in financial systems worldwide. TFFC's metric targets for both FY06 and for FY07 are and will be adjusted to reflect only non-sensitive reporting. Looking ahead to FY07, TFFC aims to broaden and deepen these engagements yet further by improving USG understanding of private sector challenges, private sector understanding of illicit financing threats, and implementation of effective AML/CFT safeguards across the private and charitable sectors.

| Measure: Number of countries that are assessed for compliance with the Financial Action Task Force (FATF) 40+9 recommendations (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 45 | 12 |
| Actual | | | 49 | 5 | |
| Target met? | N/A | N/A | Y | N | |
| **Definition**: TFFC is the lead Treasury component and representative to the Financial Action Task Force (FATF). As such, TFFC is responsible for leading international efforts to identify and close money laundering and terrorist financing vulnerabilities in the international financial system, and to ensure that countries throughout the world comply with international anti-money laundering/counter-terrorist financing standards. In concert with the international community, Treasury is deploying a three-prong strategy that 1) objectively assesses all countries against the FATF 40+9, 2) provides capacity-building assistance for key countries in need and 3) isolates and punishes those countries and institutions that facilitate terrorist financing. TFI is working with international bodies like FATF, IMF (International Monetary Fund) and World Bank to ensure compliance. The IMF and World Bank have adopted the FATF 40+9 and they use those standards to assess countries for compliance. | | | | | |
| **Source**: Data collected by the Department of Treasury's Office of Terrorism and Financial Intelligence (TFI); Terrorist Financing and Financial Crimes (TFFC). | | | | | |
| **Future Plans/Explanation for Shortfall**: Assessing compliance for the FATF 40+9 recommendations is crucial to identifying money laundering and terrorist financing vulnerabilities, and is one of the most effective levers to encourage reforms. Through participation by international bodies such as FATF, IMF, and World Bank, assessments for compliance with FATF's standards should become more widespread. Treasury will continue efforts to increase assessments and international cooperation, which will allow TFFC to pursue vital international initiatives relating to trade-based money laundering, cross border funds reporting, and the abuse of charities for terrorist financing, for example. Though gradual, growth in the number of countries assessed reflects increased acceptance of key international standards and should focus attention on key money laundering and terrorist financing issues and remaining implementation challenges. These issues and challenges should be targeted for technical assistance, which should promote greater Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) capabilities and greater vigilance in safeguarding the international financial system against illicit activity. The FY 06 results reflect only the non-sensitive information and thus appear that the target was not met. TFFC's metric targets for both FY06 and for FY07 are and will be adjusted to reflect only non-sensitive reporting. | | | | | |

## Objective: Increase the Reliability of the U.S. Financial System

## Bureau of Engraving & Printing

| Measure: Manufacturing costs for currency (dollar costs per thousand notes produced) ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 31 | 35 | 31 | 28.5 | 32.5 |
| Actual | 29.14 | 28.06 | 28.83 | 27.49 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: An indicator of currency manufacturing efficiency and effectiveness of program management. This standard is developed annually based on the past year's performance, contracted price factors, and anticipated productivity improvements. Actual performance comparison against the standard depends on BEP's ability to meet annual spoilage, efficiency, and capacity utilization goals established for this product line. | | | | | |
| **Source**: Cost data is collected through BEP's accrual-based cost accounting system. | | | | | |
| **Future Plans/Explanation for Shortfall**: During FY 2007, BEP will continue to pursue process improvements that will enable the Bureau to continue to meet or favorably exceed this measure. | | | | | |

| Measure: Currency shipment discrepancies per million notes ($) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | .01 | .01 | .01 | .01 | .01 |
| Actual | 0 | .01 | 0 | .01 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: A qualitative indicator reflecting BEP's ability to provide effective product security and accountability. This measure refers to product overages or underages of as little as a single currency note in shipments of finished notes to the Federal Reserve Banks. | | | | | |
| **Source**: The customer captures this data and report to BEP on a monthly basis. | | | | | |
| **Future Plans/Explanation for Shortfall**: During FY 2007, BEP will continue to pursue process improvements that will enable the Bureau to continue to meet or favorably exceed this measure. | | | | | |

| Measure: Security costs per 1000 notes delivered ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 5.95 | 6.25 | 6 |
| Actual | | 5.95 | 5.75 | 6 | |
| Target met? | N/A | Y | Y | Y | |
| **Definition**: An indicator reflecting the cost of providing effective and efficient product security and accountability. This standard is developed annually based on the past year's cost performance and anticipated cost increases. The formula used to calculate this measure is the total cost for security divided by the number of notes produced divided by 1000. | | | | | |
| **Source**: Cost data is collected through BEP's accrual-based cost accounting system. This standard is developed annually based on the past year's cost performance and anticipated cost increases. | | | | | |
| **Future Plans/Explanation for Shortfall**: During FY 2007, BEP will continue to pursue process improvements that will enable the Bureau to continue to meet or favorably exceed this measure. | | | | | |

| Measure: Percent of currency notes delivered to the Federal Reserve that meet customer quality requirements (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 99.9 | 99.9 | 99.9 | 99.9 | 99.9 |
| Actual | 99.9 | 100 | 99.9 | 99.9 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: A qualitative indicator reflecting the Bureau's ability to provide a quality product. All notes delivered to the Federal Reserve go through rigorous quality inspections. These inspections ensure that all counterfeit deterrent features, both overt and covert are functioning as designed | | | | | |
| **Source**: Quality inspections are performed at each Federal Reserve Bank. Any discrepancies found are reported to BEP on a per shipment basis. | | | | | |
| **Future Plans/Explanation for Shortfall**: During FY 2007, BEP will continue to pursue process improvements that will enable the Bureau to continue to meet or favorably exceed this measure. | | | | | |

## Departmental Offices

| Measure: Timely audit report received on government-wide financial statements (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Met | Met | Met | Met | Met |
| Actual | Met | Met | Met | Met | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: This is the independent audit report rendered on government-wide financial statements by GAO. Treasury expects to receive a disclaimer of opinion at least until FY 2011. | | | | | |
| **Source**: GAO is the statutorily prescribed auditor. | | | | | |
| **Future Plans/Explanation for Shortfall**: Audit report will be available on December 15, 2006. Treasury expects to receive a disclaimer of opinion. Improvement of the audit result is dependent upon the Defense Department's (DoD) audit. It is estimated that DoD will not obtain a clean audit opinion until FY 2011, at the earliest. Treasury will work to ensure that the government-wide audit, with the exception of DoD, is favorable. | | | | | |

## United States Mint

| Measure: Cycle Time (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 150 | 53 | 53 | 67 | 75 |
| Actual | 73 | 85 | 69 | 72 | |
| Target met? | Y | N | N | N | |
| **Definition**: Cycle time is the length of time from when material enters a production facility until it is delivered to the customer. | | | | | |
| **Source**: Data for each element is pulled from the United States Mint's Enterprise Resource Planning system. | | | | | |
| **Future Plans/Explanation for Shortfall**: As of September 2006, the United States Mint's cycle-time was 72 days, an increase of 3 days from 69 days as of September 2005. The targeted cycle-time was 67 days. This performance goal was set at an approximate target level, and the deviation from that level is slight. There was no significant effect on the overall program or activity performance. The United States Mint plans to continue improving the cycle-time of the circulating coinage through further implementation of lean manufacturing techniques. In FY 2006, the United States Mint completed training for many manufacturing managers on lean manufacturing processes. This training will serve to eliminate unnecessary or redundant practices and should lead to improvements in plant productivity. The Presidential $1 Coin program will begin in FY 2007. This program will present challenges to reducing the cycle-time from current levels, as four new presidential designs (one per quarter) will be introduced into circulation. To address this challenge, Mint and Federal Reserve officials are working together to ensure that sufficient quantities of the new Presidential dollar coins will be ready to be distributed into circulation on each launch date. The Federal Reserve has assigned one of its staff members with expertise in coin distribution and inventory control from its Washington headquarters to help coordinate the circulation plans. | | | | | |

| Measure: Order Fulfillment (%)(Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 0 | 95 | 96 |
| Actual | | 0 | 94 | 95 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: This measure will track order fulfillment in both the circulating and numismatic products. Each component will be scaled by its percentage of the total revenue to create an index. The formula for this measure is [(circulating shipments/circulating orders) (circulating revenue/total revenue) + (numismatic orders shipped within 7 days/numismatic orders requiring shipping) (numismatic revenue/total revenue)] The numismatic revenue and total revenue components exclude bullion revenue.

**Source**: United States Mint analysts maintain circulating orders and shipment data in a database. Numismatic orders data are pulled via a query from the United States Mint's order management system. Revenue data are from the accounting system.

**Future Plans/Explanation for Shortfall**: Order fulfillment tracks the overall order fulfillment for circulating coins shipped to the Federal Reserve Banks and the numismatic coins sold to the public. Order fulfillment in FY 2006 was 95 percent, a slight increase from the result of 94 percent in FY 2005. Essentially, this result means that 95 percent of the United States Mint's revenue and other financing sources during FY 2006 were earned from products that were shipped to the customer in a timely fashion. In FY 2006, the Mint increased its target for the third consecutive year.

| Measure: Cost per 1000 Coin Equivalents ($)(E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 9.78 | 7.03 | 6.62 | 6.96 |
| Actual | 9.96 | 7.93 | 7.42 | 7.55 | |
| Target met? | Y | Y | N | N | |

**Definition**: Cost per 1000 coin equivalents is the cost of production (conversion cost) divided by the number of products made. Conversion costs are controllable costs within manufacturing. Those costs include manufacturing payroll, non-payroll, and depreciation costs. To determine the coin equivalents, an equivalency factor is assigned to each circulating denomination and numismatic product based on the resources it takes to make the product (indexed against the resources it takes to make one product – the quarter). The production quantity for each product is multiplied by the equivalency factor, resulting in a coin equivalent quantity. Thus, all denominations and products are equivalized to a quarter.

**Source**: Conversion costs are pulled from financial reports from the accounting system. Production data is pulled from the enterprise resource planning system via queries and converted to coin equivalents.

**Future Plans/Explanation for Shortfall**: The conversion cost per 1,000 coin equivalents during FY2006 is $7.55, an increase of two percent from the FY 2005 result of $7.42. The performance measure did not meet the FY 2006 target of $6.62. This target (stretch goal) was an 11 percent decrease from the FY 2005 actual results and was set based on forecasted volume and cost estimates. Coin equivalent production increased to 21.1 billion in FY 2006 compared with 19.9 billion in FY 2005, an increase of six percent. The associated conversion cost increased to $159 million from $147 million in FY 2005, an increase of eight percent. The increase in conversion cost between FY 2006 and FY 2005 is the result of rising energy costs, replenishment of shipping and packaging supplies, overtime to support new numismatic products, and a 21 percent increase in depreciation expense. In FY 2006, the United States Mint completed training for many manufacturing managers on lean manufacturing processes and for sales and marketing staff on project management techniques. This training will serve to eliminate unnecessary or redundant practices and should lead to improvements in plant productivity and reductions in controllable operating costs.

| Measure: Protection Cost Per Square Foot ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 31.86 | 32 | 31 |
| Actual | | 32.51 | 32.43 | 32.49 | |
| Target met? | N/A | Y | N | N | |

**Definition**: Protection cost per square foot is the Protection operating costs divided by the area of usable space in square feet that the United States Mint Police protects. Usable space is defined as 90% of total square footage. The year-to-date result is then annualized on a straight-line basis.

**Source**: The Protection costs are automatically pulled from the United States Mint's accounting system on a monthly basis. The square footage is relatively stable and is monitored by the Protection office and United States Mint management.

**Future Plans/Explanation for Shortfall**: Protection cost per square foot for FY 2006 was $32.49, a slight increase from $32.43 in FY 2005. This performance did not meet the target of $32.00. The United States Mint is identifying the use of automation to replace the functions currently performed by police officers. While these strategies may help reduce certain personnel and overtime costs, the ability to apply downward pressure on costs is taken with a long-term view and must be tempered by the level of readiness necessary to fulfill the Protection mission.

| Measure: Total Losses ($) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 250000 | 15000 | 15000 |
| Actual | | 3109 | 1135 | 0 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: The United States Mint performs its protection function by minimizing the vulnerability to theft or unauthorized access to critical assets. The measure is comprised of the sum of three elements 1. Financial Losses: Losses that have been reported, investigated and verified as unrecoverable; from a. Strategic reserves (Theft of Treasury Reserves) b. Coining products (Theft from the production facilities) c. Sales of products to the public (Theft by fraud) d. Other losses (Other theft) 2. Productivity losses: The cost of intentional damage or destruction of United States Mint production capability and the cost to utilize alternative productivity as needed as a result of the intentional damage or destruction. 3. Intrusion losses: The cost to repair and/or recover from intentional intrusions into United States Mint facilities and systems, either physically or electronically.

**Source**: The United States Mint Police maintains a secure database of monthly reports on incidents included in the categories above. Any theft or fraud amount determined as unrecoverable is assessed on a case-by-case basis. In the event that cost information is needed, data on the value of United States Mint assets and costs are in the ERP system.

**Future Plans/Explanation for Shortfall**: The target value for FY 2005 was established based on losses from the previous two years, which were high; subsequent losses have been significantly lower and targets have been set to reflect this. Total losses as of the end of FY 2006 were $0 (zero) compared with $1,135 in FY 2005. This performance exceeds the target of $15,000. Results are from cases that have been investigated and closed during the fiscal year. While the FY 2006 result represents the ideal performance, there are open cases that are still under investigation that may be reported as losses at a future date. The protection of United States Mint assets remains a high priority. Efforts to prevent losses include automating exit scanning procedures to scan employees for valuable assets and error coins, and installing electronic systems to verify identity and scan for weapons and explosives upon entry to each facility.

## Comptroller of the Currency

**Measure: Rehabilitated problem national banks as a percentage of the problem national banks one year ago (CAMELS 3, 4 or 5) (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 40 | 40 | 40 | 40 | 40 |
| Actual | 32 | 40 | 44 | 46 | |
| Target met? | N | Y | Y | Y | |

**Definition**: This measure reflects the successful rehabilitation of problem national banks during the past twelve months. Problem banks can ultimately reach a point where rehabilitation is no longer feasible. The OCC's early identification of and intervention with problem banks can lead to successful remediation of problem banks.

**Source**: The Supervisory Information office in OCC's headquarters office uses Examiner View (EV) and the Supervisory Information System (SIS) to identify and compare the composite CAMELS ratings for problem banks from twelve months prior to the current period composite CAMELS ratings for the same banks. The percentage is determined by comparing the number of national banks that have upgraded composite CAMELS ratings of 1 or 2 from composite CAMELS ratings of 3, 4 or 5 to the total number of national banks that had composite CAMELS ratings of 3, 4 or 5 twelve months ago.

**Future Plans/Explanation for Shortfall**: To sustain this level of achievement, the OCC will execute its Bank Supervision Operating Plan that focuses on credit quality, allowance of loan and lease losses (ALLL) adequacy, off-balance-sheet activities, liquidity and interest rate risk management, consumer protection, and Bank Secrecy Act/Anti-money Laundering compliance. The OCC also will continue recruiting for entry-level examiners, aligning supervision resources to the areas of greatest risk, training the examiner staff, and enhancing examination guidance.

**Measure: Percentage of national banks with composite CAMELS rating 1 or 2 (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 90 | 90 | 90 | 90 | 90 |
| Actual | 94 | 94 | 94 | 95 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: This measure reflects the overall condition of the national banking system at fiscal year-end. Bank regulatory agencies use the Uniform Financial Institutions Rating System, CAMELS, to provide a general framework for assimilating and evaluating all significant financial, operational and compliance factors inherent in a bank. Evaluations are made on: Capital adequacy, Asset quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. The rating scale is 1 through 5 where 1 is the highest rating granted.

**Source**: The Supervisory Information office identifies the current composite ratings from Examiner View (EV) and Supervisory Information System (SIS) at fiscal year-end. The number of national banks at fiscal year-end is obtained from the Federal Reserve Board's National Information Center database. The percentage is determined by comparing the number of national banks with current composite CAMELS ratings of 1 or 2 to the total number of national banks at fiscal year-end.

**Future Plans/Explanation for Shortfall**: To sustain this level of achievement, the OCC will execute its Bank Supervision Operating Plan that focuses on credit quality, allowance of loan and lease losses (ALLL) adequacy, off-balance-sheet activities, liquidity and interest rate risk management, consumer protection, and Bank Secrecy Act/Anti-money Laundering compliance. The OCC also will continue recruiting for entry-level examiners, aligning supervision resources to the areas of greatest risk, training the examiner staff, and enhancing examination guidance.

| Measure: Total OCC costs relative to every $100,000 in bank assets regulated ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | 9.55 |
| Actual | | | | 8.84 | |
| Target met? | N/A | N/A | N/A | Y | |

**Definition**: This measure reflects the efficiency of OCC operations while meeting the increasing supervisory demands of a growing and more complex national banking system.

**Source**: OCC costs are those reported as total program costs on the annual audited Statement of Net Cost. Banks assets are those reported quarterly by national banks on their Reports of Condition and Income.

**Future Plans/Explanation for Shortfall**: Baseline in FY 06. Ensure a vigorous budget formulation process so that programs are continually reviewed for effectiveness and productivity. Continue to analyze business processes to improve quality and efficiency, eliminate waste, reduce the burden of compliance with statutory and regulatory requirements and deliver more value to national banks.

| Measure: Percentage of national banks that are well capitalized (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 95 | 95 | 95 | 95 | 95 |
| Actual | 99 | 99 | 99 | 99 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: This measure reflects whether the national banking system is well capitalized at fiscal year-end. The Federal Deposit Insurance Act established a system of prompt corrective action (PCA) that classifies insured depository institutions into five categories (well capitalized; adequately capitalized; undercapitalized, significantly undercapitalized; and critically undercapitalized) based on their relative capital levels. The purpose of PCA is to resolve the problems of insured depository institutions at the least possible long-term cost to the deposit insurance fund.

**Source**: National banks file quarterly Reports of Condition and Income with the Federal Finance Institution Examination Council through the Federal Deposit Insurance Corporation's data processing center. The Supervisory Information office reviews the Reports of Condition and Income (i.e., call reports) for each quarter to identify national banks that meet all of the criteria for a well capitalized institution. The number of national banks at fiscal year-end is obtained from the Federal Reserve Board's National Information Center database. The percentage is determined by comparing the number of national banks that meet all of the established criteria for being well capitalized to the total number of national banks at fiscal year-end.

**Future Plans/Explanation for Shortfall**: To sustain this level of achievement, the OCC will execute its Bank Supervision Operating Plan that focuses on credit quality, allowance of loan and lease losses (ALLL) adequacy, off-balance-sheet activities, liquidity and interest rate risk management, consumer protection, and Bank Secrecy Act/Anti-money Laundering compliance. The OCC also will continue recruiting for entry-level examiners, aligning supervision resources to the areas of greatest risk, training the examiner staff, and enhancing examination guidance.

| Measure: Percentage of national banks with consumer compliance rating of 1 or 2 (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 94 | 94 | 94 | 94 | 94 |
| Actual | 96 | 96 | 94 | 94 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: This measure reflects the national banking system's compliance with consumer laws and regulations. Bank regulatory agencies use the Uniform Financial Institutions Rating System, Interagency Consumer Compliance Rating, to provide a general framework for assimilating and evaluating significant consumer compliance factors inherent in a bank. Each bank is assigned a consumer compliance rating based on an evaluation of its present compliance with consumer protection and civil rights statutes and regulations, and the adequacy of its operating systems designed to ensure continuing compliance. Ratings are on a scale of 1 through 5 in increasing order of supervisory concern. | | | | | |
| **Source**: The Supervisory Information office identifies the number of banks with current consumer compliance ratings of 1 or 2 and the total number of national banks from Examiner View (EV) and Supervisory Information System (SIS) subject to consumer compliance examinations at fiscal year-end. The percentage is determined by comparing the number of national banks with current consumer compliance ratings of 1 or 2 to the total number of national banks subject to consumer compliance examinations at fiscal year-end. | | | | | |
| **Future Plans/Explanation for Shortfall**: To sustain this level of achievement, the OCC will execute its Bank Supervision Operating Plan that focuses on credit quality, allowance of loan and lease losses (ALLL) adequacy, off-balance-sheet activities, liquidity and interest rate risk management, consumer protection, and Bank Secrecy Act/Anti-money Laundering compliance. The OCC also will continue recruiting for entry-level examiners, aligning supervision resources to the areas of greatest risk, training the examiner staff, and enhancing examination guidance. | | | | | |

## Office of Thrift Supervision

| Measure: Percent of thrifts that are well capitalized (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 95 | 95 | 95 | 95 |
| Actual | 99.6 | 99.4 | 99.5 | 99.9 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: Capital absorbs losses, promotes public confidence and provides protection to depositors and the FDIC insurance funds. It provides a financial cushion that can allow a savings association to continue operating during periods of loss or other adverse conditions. The Federal Deposit Insurance Act established a system of prompt corrective action (PCA) that classifies insured depository institutions into five categories (well-capitalized; adequately capitalized; undercapitalized, significantly undercapitalized; and critically undercapitalized) based on their relative capital levels. The purpose of PCA is to resolve the problems of insured depository institutions at the least possible long-term cost to the deposit insurance fund. | | | | | |
| **Source**: PCA ratings are stored in the Examination Data System and can also be found in the Thrift Overview Report and off-site financial monitoring reports. OTS calculates this measure by dividing the number of savings associations that are well capitalized by the total number of OTS-regulated institutions. | | | | | |
| **Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry. | | | | | |

| Measure: Percent of thrifts with compliance examination ratings of 1 or 2 (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 90 | 90 | 90 | 90 |
| Actual | 94 | 94 | 94 | 93 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: A uniform, interagency compliance rating system was first approved by the Federal Financial Institutions Examination Council (FFIEC) in 1980. The FFIEC rating system was designed to reflect, in a comprehensive and uniform fashion, the nature and extent of an association's compliance with consumer protection statutes, regulations and requirements. The Compliance Rating System is based upon a scale of 1 through 5 in increasing order of supervisory concern. OTS began to combine safety and soundness and compliance examinations in 2002 to attain exam efficiencies and to improve risk assessment. Using comprehensive exam procedures, compliance with consumer protection laws is reviewed at more frequent intervals, which has improved the quality of the examination process.

**Source**: Compliance examination ratings are stored in the Examination Data System. OTS calculates this measure by dividing the number of OTS-regulated savings associations that received a compliance examination rating of 1 or 2 on their most recent examination by the total number of OTS-regulated savings associations that have been assigned a compliance examination rating.

**Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry.

| Measure: Percent of thrifts with composite CAMELS ratings of 1 or 2 (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 90 | 90 | 90 | 90 |
| Actual | 93 | 93 | 94 | 93 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: On December 9, 1996, the FFIEC adopted the CAMELS rating system as the internal rating system to be used by the Federal and State regulators for assessing the safety and soundness of financial institutions on a uniform basis. The CAMELS rating system puts increased emphasis on the quality of risk management practices. "CAMELS" stands for Capital adequacy, Asset quality, Management, Earnings, Liquidity and Sensitivity to market risk. OTS assigns a composite CAMEL rating to savings associations at each examination and may adjust the rating between examinations if the association's overall condition has changed. New savings associations are typically not assigned a composite CAMELS rating until the first examination. OTS adjusts the level of supervisory resources devoted to an association based on the composite rating. The CAMELS rating is based upon a scale of 1 through 5 in increasing order of supervisory concern.

**Source**: Composite CAMELS ratings are stored in and retrieved from the online Examination Data System. OTS calculates this measure by dividing the number of savings associations having a composite CAMEL rating of 1 or 2 by the total number of OTS-regulated savings associations that have been assigned a composite CAMELS rating.

**Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry.

| Measure: Percent of safety and soundness exams started as scheduled (%) (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 90 | 90 | 90 | 90 |
| Actual | 92 | 94 | 93 | 94 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: OTS examines savings associations every 12-18 months for safety and soundness, compliance and consumer protection laws. OTS performs safety and soundness examinations of its regulated savings associations consistent with the requirements in the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) as amended by the Riegle Community Development and Regulatory Improvement Act of 1994. When safety and soundness or compliance issues are identified during its risk-focused examinations, OTS acts promptly to ensure association management and directors institute corrective actions to address supervisory concerns. OTS staff often meets with the savings association's board of directors after delivery of the Report of Examination to discuss findings and recommendations.

**Source**: When a savings association is examined, OTS staff enters into the Examination Data System the examination type, examination beginning and completion dates, report of examination mail date, and CAMELS or equivalent ratings. The percentage success rate for this measure is calculated by dividing the number of examinations that were started by the number of examinations that were scheduled to be started during the review period.

**Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry.

| Measure: Total OTS costs relative to every $100,000 in savings association assets regulated ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | 14.33 |
| Actual | | | 0 | 13.46 | |
| Target met? | N/A | N/A | N/A | Y | |

**Definition**: Beginning in FY 2006, OTS included a performance measure that reflects the efficiency of its operations while meeting the increasing supervisory demands of a growing and more complex thrift industry. This measure supports OTS' ongoing efforts to efficiently use agency resources. The efficiency measure is impacted by the relative size of the savings associations regulated. As of June 30, 2006, 63% of all savings associations have total assets of less than $250 million and are generally community-based organizations that provide retail financial services in their local markets. In addition, the measure does not include over $7 trillion in assets of holding company enterprises regulated by OTS.

**Source**: The OTS expenses published in OTS' annual audited financial statement are used in this calculation. If the performance measure calculation is provided before the audited financial statement is available, the estimated expenses are derived from OTS' Budget Variance System. The OTS regulated assets are published in the OTS quarterly press release of thrift industry financial highlights and are derived from the institutions' quarterly Thrift Financial Reports. The measure is calculated by dividing total fiscal year expenses by total thrift assets.

**Future Plans/Explanation for Shortfall**: OTS plans to maintain its current high level of achievement for this measure. The FY 2007 Budget/Performance Plan describes the goals, strategies, and priorities that will guide OTS' operations. OTS will continue tailoring supervisory examinations to the risk profile of the institutions, while effectively allocating resources to oversee and assess the safety and soundness and consumer compliance record of the thrift industry.

## Goal: Manage the Government's Finances Effectively

### Objective: Collect Federal Tax Revenue When Due Through a Fair and Uniform Application of the Law

### Financial Management Service

| Measure: Percentage of delinquent debt referred to FMS for collection compared to amount eligible for referral (%) (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 85 | 90 | 92 | 93 | 94 |
| Actual | 92 | 99 | 97 | 95 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: The measure tracks the percentage of the dollar volume of debt referred to the total dollar volume that is eligible for referral. | | | | | |
| **Source**: The process of collecting and reporting the debt collection data is performed on a monthly basis. The methodology and the origin of the data are consistent from month to month. The referral data is contained in the program systems (TOP and DMSC). The referral data is loaded from the files received from Federal Program Agencies (FPAs). | | | | | |
| **Future Plans/Explanation for Shortfall**: FMS will continue to educate and encourage agencies to refer all eligible delinquent debt in a timely manner. | | | | | |

| Measure: Amount of delinquent debt collected through all available tools (Billions $) (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 2.9 | 2.9 | 3 | 3.1 | 3.2 |
| Actual | 3.1 | 3 | 3.25 | 3.34 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: This measure provides information on the total amount collected, in billions, through debt collection tools operated by Debt Management Services. | | | | | |
| **Source**: The process of collecting and reporting the debt collection data is performed on a monthly basis. The methodology and the origin of the data are consistent from month to month. The collection data is generated by the program systems (TOP and DMSC) and is reported on a monthly basis. The tools include: tax refund offset, administrative offset, private collection agencies, demand letters, and credit bureau reporting. FMS also collects debt through the State debt program and tax levy. | | | | | |
| **Future Plans/Explanation for Shortfall**: FMS had record collections in FY 2006 as a result of program efficiencies, streamlining systems and increased volumes in the Federal Payment Levy program. For the future, FMS will continue these efforts as well as work to incorporate additional payment types into the payment offset and levy programs and seek legislative proposals to increase the amount of delinquent debt collected. | | | | | |

| Measure: Amount of delinquent debt collected per $1 spent ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 41.09 | 36.4 | 36.5 |
| Actual | | | 36.23 | 39.97* | |
| Target met? | N/A | N/A | **N** | **Y** | |
| **Definition**: This measure shows the efficiency of the Debt Collection program. The costs include all debt collection activities and all funding sources. | | | | | |
| **Source**: Collection of data and reporting on the cost of the debt collection program are performed on an annual basis. | | | | | |
| **Future Plans/Explanation for Shortfall**: FMS will continue to look for efficiencies to lower program costs by streamlining debt management systems while increasing delinquent debt collected. *Unit measure is estimated until costs are finalized. | | | | | |

## Internal Revenue Service - Business System Modernization (BSM)

| Measure: BSM Project Cost Variance by Release/Subrelease | | | | | | | |
|---|---|---|---|---|---|---|---|
| FY 2006 BSM Project Cost Variance by Release/Subrelease | | | | | | | |
| Project | Release | Milestone | PlannedCost (000) | CurrentCost (000) | Variance ($)(000) | Variance (%) | Within Acceptable Tolerance |
| F&PC | R1.2 | 3 | 16,550 | 9,014 | (7,536) | -46% | NO |
| F&PC | R1.2 | 4a | 10,536 | 10,536 | - | 0% | YES |
| MeF (Fed/ State Project) | R3.2 | 4 | 23,773 | 31,323 | 7,550 | 32% | NO |
| MeF | R4 | 3 | 8,000 | 3,800 | (4,200) | -53% | NO |
| CADE | R1.3.2 | FS06 | 20,767 | 20,833 | 66 | 0% | YES |
| CADE | R2.1 | 4 | 27,049 | 31,239 | 4,190 | 15% | NO |
| **Definition:** Percent variance by release/sub-release of a BSM funded project's initial, approved cost estimate versus current, approved cost estimate. Cost variances < or = to +/- 10% are categorized as being within acceptable thresholds. Cost variances greater than +/- 10% are considered outside acceptable thresholds. | | | | | | | |
| **Source:** The data is collected from the approved and enacted Expenditure Plan and subsequent modifications resulting from changes to project cost plans as approved via the BSM Governance Procedures and documented by the Resource Management Office. | | | | | | | |
| **Future Plans/Explanation for Shortfall:** In FY 2006, the baseline year, the IRS used an improved methodology for determining project cost variance by release/subrelease. Cost variance is reported separately for each major release/subrelease. Overall, the BSM program delivered nearly half of project segment cost within target, and is meeting target expectations for nearly all project segments currently in-progress. In some cases, BSM cost targets exceeding a -10 percent threshold are attributed to reducing project scope. (Note: For a detailed variance explanation by project segment, refer to the FY 2006/FY 2007 BSM Expenditure Plan.) The IRS will continue reporting on this measure in accordance with the agreed upon performance methodology. At each review juncture, management ensures that proposed project changes as reported in the BSM expenditure plan are valid and that mitigation plans are in place when applicable. | | | | | | | |

| Measure: BSM Project Schedule Variance by Release/Sub release | | | | | | | |
|---|---|---|---|---|---|---|---|
| FY 2006 BSM Project Schedule Variance by Release/Subrelease | | | | | | | |
| **Project** | **Release** | **Milestone** | **Planned Finish Date** | **Current Finish Date** | **Variance (days)** | **Variance (%)** | **Within Acceptable Tolerance** |
| F&PC | R1.2 | 3 | 02/28/06 | 02/28/06 | 0 | 0% | YES |
| F&PC | R1.2 | 4a | 06/30/06 | 07/10/06 | 5 | 6% | YES |
| MeF (Fed/ State Project) | R3.2 | 4 | 03/31/06 | 03/22/06 | -7 | -2% | YES |
| MeF | R4 | 3 | 06/30/05 | 12/09/05 | 111 | 59% | NO |
| CADE | R1.3.2 | FS06 | 12/31/05 | 12/31/05 | 0 | 0% | YES |
| CADE | R2.1 | 4 | 08/10/06 | 08/25/06 | 11 | 7% | YES |

**Definition:** Percent variance by release/sub-release of a BSM funded project's initial, approved schedule estimate versus current, approved schedule estimate. Schedule variances < or = to +/- 10% are categorized as being within acceptable thresholds. Schedule variances greater than +/- 10% are considered outside acceptable thresholds.

**Source:** The data is collected at the time of Expenditure Plan creation and subsequent modifications resulting from changes to project schedule plans as approved via the BSM Governance Procedures and documented by the Resource Management Office

**Future Plans/Explanation for Shortfall:** In FY 2006, the baseline year, the IRS used an improved methodology for determining project schedule variance by release/subrelease. Schedule variance is reported separately for each major release/subrelease. The BSM program delivered most (5 out of 6) project segments within schedule variance. (Note: For a detailed variance explanation by project segment, refer to the FY 2006/FY 2007 BSM Expenditure Plan.) The IRS will continue reporting on this measure in accordance with the agreed upon performance methodology. At each review juncture, management ensures that proposed project changes as reported in the BSM expenditure plan are valid and mitigation plans are in place when applicable.

## Internal Revenue Service

| Measure: Customer Accuracy - Tax Law Phones (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 87 | 85 | 82 | 90 | 90.5 |
| Actual | 82 | 80 | 89 | 90.9 | |
| Target met? | **N** | **N** | **Y** | **Y** | |

**Definition**: The percentage of correct tax law answers provided by a telephone assistor. The measure indicates how often customers receive the correct answer to their tax law inquiry based upon all available information and Internal Revenue Manual required actions.

**Source**: Quality reviewers on the Centralized Quality staff complete a data collection instrument as calls are reviewed. Data is input to the Quality Review Database for product review and reporting.

**Future Plans/Explanation for Shortfall**: Incremental improvement in the performance is expected in FY 2007 and beyond from the completion of the Contact Recording project, a program to record customer contacts for quality review to help employees improve their skills, ease manager burden, and raise quality for customers.

| Measure: Customer Accuracy - Accounts (Phones) (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 88 | 89 | 89.8 | 92 | 92.6 |
| Actual | 88 | 89 | 91.5 | 93.2 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: The percentage of correct answers provided by a telephone assistor. The measure indicates how often customers receive the correct answer to their account inquiry and/or had their case resolved correctly based upon all available information and Internal Revenue Manual required actions.

**Source**: Quality reviewers on the Centralized Quality staff complete a data collection instrument as calls are reviewed. Data is input to the Quality Review Database for product review and reporting.

**Future Plans/Explanation for Shortfall**: Incremental improvement in performance is expected in FY 2007 and beyond from continued improvement efforts such as the development of new online tools for assistors to research taxpayer questions.

| Measure: Automated Collection System (ACS) Accuracy (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 88 | 88 | 89 |
| Actual | | 87.8 | 88.5 | 91 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: Percent of taxpayers who receive the correct answer to their ACS question.

**Source**: The Centralized Quality Review System (CQRS) monitors the calls as they are reviewed. Data is input to the Quality Review Database for product review and reporting.

**Future Plans/Explanation for Shortfall**: The IRS will leverage the process improvements made to its Electronic Automated Collection Service Guide, a tool designed to further increase response accuracy. Also, the IRS will trend accuracy statistics to better focus managerial reviews.

| Measure: Collection Efficiency | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | 1650 | 1717 |
| Actual | | | 1514 | 1677 | |
| Target met? | N/A | N/A | N/A | Y | |

**Definition**: Total work (delinquent accounts, investigations, offer-in-compromise, automated substitution for return) divided by the total Full Time Equivalent (FTE) realized in field collection and in campus collection. The new methodology for FY 2006 includes balance due and delinquent return cases still in notice status whereas, the FY 2005 methodology only considered accounts or investigations in delinquent status (Taxpayer Delinquent Account (TDA) and Taxpayer Delinquent Investigation (TDI) statuses). The new methodology was applied to recalculate the prior actual and the FY 2006 plan number.

**Source**: The data comes from the Collection Activity Report (CAR) and the Integrated Financial System (IFS).

**Future Plans/Explanation for Shortfall**: The IRS plans to continue its practice of allocating resources and planning for program delivery through the Collection Governance Council to ensure enterprise-wide coordination of case selection and program delivery decisions.

| Measure: Taxpayer Self Assistance Rate | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 42.5 | 45.7 | 47.5 |
| Actual | 51.0 | 46.4 | 42.5 | 46.8 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The percent of contacts that are resolved by automated self-assistance applications.

**Source**: Enterprise Telephone Data (ETD) Snapshot Report, Accounts Management Information Report (AMIR), Internet Refund/Fact of Filing Project Site, MIS Reporting Tool, Electronic Tax Administration (ETA) Website, Microsoft Excel Spreadsheet tracking (Kiosk Visits)

**Future Plans/Explanation for Shortfall**: The IRS expects performance to continue to increase as more taxpayers choose to use automated applications to resolve issues and questions instead of more traditional methods such as contact with the IRS by telephone and correspondence.

| Measure: Timeliness of Critical Filing Season Tax Products to the Public (%) (E) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | 75 | 80 | 92 | 93 |
| Actual | | 76 | 91.4 | 83 | |
| Target met? | N/A | Y | Y | N | |

**Definition**: The percentage of Critical Filing Season tax products made available to the public in a timely fashion. Critical Filing Season tax products are forms, schedules, instructions, publications, tax packages, and certain notices normally filed between January 1 through April 15 that are mailed to taxpayers. This measure contains two components: (1) percentage of paper tax products shipped no later than December 20 (December 27 for tax packages), and (2) the percentage of scheduled electronic tax products available on the Internet no later than the first five business days of January 2006.

**Source**: Publishing Services Data (PSD) System

**Future Plans/Explanation for Shortfall**: The IRS did not meet the FY 2006 target. In FY 2006, the IRS shipped 166 of 200 (83 percent) Critical Filing Season tax products timely. Shipment of the remaining products was delayed intentionally to incorporate changes mandated in legislation enacted late in 2005, P.L. 109-73, Katrina Emergency Tax Relief Act of 2005 (KETRA) and P.L. 109-135, Gulf Opportunity Zone Act of 2005 (GOZONE). The IRS expects to resume timely delivery of all tax products in FY 2007.

| **Measure: Examination Coverage - Individual (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | .9 | .9 | 1 |
| Actual | | | .9 | 1 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The sum of all individual returns closed by SB/SE, W&I, and LMSB (Field Examination and Correspondence Examination) divided by the total individual return filings for the prior calendar year. In FY 2005, Automated Underreported (AUR) cases were included as part of this measure. In FY 2006, AUR is covered as a separate measure. The new methodology was applied to prior year actual and FY 2006 plan number.

**Source**: The data comes from the Audit Information Management System (AIMS) closed case data base, the automated underreporter Management Information System for Top Level Executives (MISTLE) reports and Research projections for individual return filings.

**Future Plans/Explanation for Shortfall**: The IRS will continue to balance its audit coverage to emphasize reduction of the tax gap. Specific areas targeted for improvement include the workload identification processes, the audit selection criteria, and restructured examination training classes.

| **Measure: Office Exam Embedded Quality (Oe) (Replaces Examination Quality Office)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | | Baseline | TBD |
| Actual | | | | TBD | |
| Target met? | N/A | N/A | N/A | TBD | |

**Definition**: The score awarded to a reviewed Office Examination case by a Quality Reviewer using the Examination Quality Measurement System (EQMS) quality standards.

**Source**: Examination Quality Measurement System

**Future Plans/Explanation for Shortfall**: FY 2006 was the baseline year for this measure. Baseline data will be available on December 1, 2006. The IRS will complete the full implementation of EQ with the addition of the front line manager phase. This phase directly links Critical Job Elements to the quality measurement system, improving the relationship between individual performance and organizational objectives. Full implementation of EQ is expected to help identify potential problem areas in need of process improvements or focused training and, ultimately, lead to reductions in examination cycle time.

| **Measure: AUR Efficiency (E)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | | 1759 | 1834 |
| Actual | | 1514 | 1701 | 1832 | |
| Target met? | N/A | N/A | N/A | Y | |

**Definition**: The total number of W&I and SB/SE contact closures (a closure resulting from a case where the IRS made contact with the taxpayer) divided by the total FTE.

**Source**: AUR Management Information System for Top Level Executives (MISTLE)

**Future Plans/Explanation for Shortfall**: The IRS plans to leverage the process improvements implemented in FY 2006 to improve workload selection and productivity, reducing the number of cases closed without taxpayer contact.

| Measure: Percent of Individual Returns Filed Electronically (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 41 | 45 | 51 | 55 | 58.8* |
| Actual | 40 | 47 | 51 | 54.1 | |
| Target met? | **N** | **Y** | **Y** | **N** | |

**Definition**: Number of electronically filed individual tax returns divided by the total individual returns filed.

**Source**: Electronic Tax Administration reports

**Future Plans/Explanation for Shortfall**: The IRS did not meet the target. Although the January through June performance was at 55 percent, historically, a higher percentage of paper returns are received during July through September causing the fiscal year percentage of electronically filed returns to drop. The plan number is derived from semi-annual filing projections prepared by the IRS Research organization, incorporating changes in filing patterns, economic and demographic trends, legislative requirements, and IRS administrative processes. E-file participation rates are projected to increase to 58.2 percent in 2007 based on current experience, historical growth, increased advertising, marketing, and expanded e-file programs and do not reflect gains from any mandates. (* The FY 2007 target was changed based on revised projections.)

| Measure: Timeliness of Critical Other Tax Products to the Public (%) (E) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | Baseline | 80 | 85 | 86 |
| Actual | | 76 | 80 | 61.2 | |
| Target met? | N/A | **Y** | **Y** | **N** | |

**Definition**: The percentage of Critical Other Tax Products, paper and electronic, made available to the public timely. Critical Other Tax Products are business tax products, Tax Exempt and Government Entities and miscellaneous tax products. This measure contains two components: (1) percentage of paper tax products that meet the scheduled start to ship date within five business days of the actual start to ship date and (2) percentage of scheduled electronic tax products that is available on the Internet within five business days of the ok-to-print date. The intent is to have the tax products available to the public 30 days before the form is required to be filed.

**Source**: Publishing Services Data System (PSD)

**Future Plans/Explanation for Shortfall**: The IRS did not meet the target. Production schedules required modification to accommodate the delay in completion of the critical filing season tax products, necessitating changes to the scheduled modification and ship dates for these other tax products (non-critical). Monthly timeliness results during early FY 2006 reflected this shift to the work plans. The IRS could not recover the lost production days and as a result, could not meet the target. The IRS expects to resume timely delivery of all tax products in FY 2007.

| Measure: Customer Service Representative (CSR) Level of Service (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 72 | 83 | 82 | 82 | 82 |
| Actual | 80 | 87 | 82.6 | 82 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: The relative success rate of taxpayers that call for toll-free services seeking assistance from a Customer Service Representative.

**Source**: Enterprise Telephone Database (ETD)

**Future Plans/Explanation for Shortfall**: The IRS will continue to maintain CSR Level of Service at 82 percent in FY 2007. The IRS expects an increase in telephone demand in FY 2007 from the Telecommunications Excise Tax Refund (TETR) initiative, and plans to increase staffing to meet the expected demand.

| Measure: Customer Contacts Resolved per Staff Year (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 7261 | 7477 | 7555 |
| Actual | 8316 | 8015 | 7585 | 7414 | |
| Target met? | N/A | N/A | Y | N | |

**Definition**: The number of Customer Contacts resolved in relation to time expended based on staff usage. Customer Contacts Resolved are derived from all telephone and paper inquiries received by Accounts Management, in which all required actions have been taken, and the taxpayer has been notified as appropriate. The measure includes all self-service, Internet-based applications, such as the "Where's My Refund?" service available on *www.irs.gov.*

**Source**: Contacts resolved volumes are derived from internal telephone management systems and modernization project websites. Staff year data is extracted from the weekly Work Planning & Control report and consolidated and included in the weekly resource usage report.

**Future Plans/Explanation for Shortfall**: Despite answering 2.7 million more contacts than planned, the IRS did not meet this target. Efficiencies expected from the reduction of Toll-free telephone service operating hours (from 15 to 12 hours per day) did not occur because the service operating hours were not reduced due to reduction in service concerns expressed by Congress. Staffing for the 15 hours required an additional 482 FTE over plan. Overall, the IRS came within 99 percent of the goal, answering almost 2 million additional automated calls, 564,000 assistor calls, and completing over 750,000 additional Web Services. Completing a web service is defined as providing a service requested by a taxpayer or tax practitioner through self-assist internet-based applications such as Internet Refund Fact of Filing ("Where's My Refund"), Transcript Delivery System, Preparer Tax Identification Number, Internet-EIN, Prior Year Earned Income Option, and Disclosure Authorizations. The IRS is expecting efficiency to increase as more taxpayers choose to use automated means to contact the IRS instead of traditional, labor intensive methods.

| Measure: Percent of Eligible Taxpayers who File for EITC (Participation Rate) (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 80 | 80 | TBD |
| Actual | | 80 | 80 | TBD | |
| Target met? | N/A | Y | Y | TBD | |

**The participation rate is an estimate, based on a methodology which includes underlying assumptions about the potential EITC eligible population.*

**Definition**: The number of taxpayers who actually claim the Earned Income Tax Credit (EITC) compared to the number of taxpayers who appear to be eligible for the EITC.

**Source**: Individual Returns Transaction File data; Census Bureau Survey; and EITC Compliance Studies.

**Future Plans/Explanation for Shortfall**: Data to estimate the participation rate will be available after the close of Calendar Year 2006. The methodology for estimating the EITC participation rate is being validated using Census data in an effort to improve the accuracy of estimates.

| Measure: Percent of Business Returns Processed Electronically (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 17 | 18.6 | 20.6 |
| Actual | | 17.4 | 17.8 | 16.6 | |
| Target met? | N/A | Y | Y | N | |

**Definition**: The number of electronically filed business returns divided by the total business returns filed.

**Source**: Data is extracted from the Business Master file and fed into the Business Measures Datamart database.

**Future Plans/Explanation for Shortfall**: The IRS did not meet the target primarily due to the elimination of Telefile, resulting in an increase of 3 million paper employment returns while there were 325,000 fewer electronic employment returns. The plan number is derived from semi-annual filing projections prepared by the IRS Research organization semi-annually, incorporating changes in filing patterns, economic and demographic trends, legislative requirements, and IRS administrative processes. The projections provide a basis for IRS workload estimates. The IRS expects the percentage of business filers to increase in the future from increased marketing and expanded business e-file programs, including the acceptance of new forms and schedules attached to employer, estates and trusts, and partnership filings, acceptance of amended returns, and acceptance of the new annualized employment tax return. The IRS will continue to pursue additional mandates for businesses to file electronically similar to the one recently imposed for corporations.

| Measure: Collection Coverage - Units (Oe) (Revised) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 57 | 52 | 52 |
| Actual | | | 33 | 54 | |
| Target met? | N/A | N/A | **N** | **Y** | |

**Definition**: The volume of collection work disposed (closed) compared to the volume of collection work available. The new methodology for FY 2006 includes balance due and delinquent return cases still in notice status whereas, the FY 2005 methodology only considered those accounts or investigations in delinquent status (Taxpayer Delinquent Account (TDA) and Taxpayer Delinquent Investigation (TDI) statuses). The new methodology was applied to recalculate the prior actual and the FY 2006 plan number.

**Source**: The data comes from the Collection Activity Report (CAR.)

**Future Plans/Explanation for Shortfall**: The IRS plans to continue to facilitate the process for allocating resources and planning for program delivery through the Collection Governance Council. This will ensure enterprise-wide coordination of case selection and delivery decisions.

| Measure: Examination Coverage - Business Corporations > $10 million (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 7 | 7.5 | 8.4 |
| Actual | | 7.5 | 7.8* | 7.4 | |
| Target met? | N/A | N/A | **Y** | **N** | |

**Revised FY 2005 actual reflects updated case closure information from the Automated Inventory Management System (AIMS)*

**Definition**: The number of Large and Mid-Size Business customer returns with assets greater than $10 million examined and closed during the current fiscal year, divided by filing of the same type returns from the preceding calendar year.

**Source**: The number of returns examined and closed during the Fiscal Year is from the Audit Information Management System (AIMS) closed case database, accessed via A-CIS (an MS Access application). Filings are from Document 6186, which is issued by the Office of Research, Analysis and Statistics.

**Future Plans/Explanation for Shortfall**: The IRS did not meet the FY 2006 target. The target was missed by 1 percent due to the IRS being prevented from taking enforcement action on a significant number of partnership return examinations involving a tax shelter promoter. Also, partnership audits were not as productive as expected so the IRS stopped opening these audits until improvement of the examination selection methodology. The IRS will continue to focus on the issues that pose the greatest compliance risk, and to identify enterprises that appear to be non-compliant. The IRS' emphasis on streamlining and improving the examination process, coupled with better risk analysis, will continue to provide for early resolution of post-filing examination issues and enhance large business examination coverage.

| Measure: Field Exam Embedded Quality (Replaces Examination Quality Field) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | TBD |
| Actual | | | | TBD | |
| Target met? | N/A | N/A | N/A | TBD | |

**Definition**: The score awarded to a reviewed Field Examination case by a Quality Reviewer using the Examination Quality Measurement System (EQMS) quality standards.

**Source**: Monthly reports supplied from the EQMS database.

**Future Plans/Explanation for Shortfall**: FY 2006 was the baseline year for this measure. Baseline data will be available on December 1, 2006. The IRS will complete the full implementation of EQ with the addition of the front line manager phase. This phase directly links Critical Job Elements to the quality measurement system, improving the relationship between individual performance and organizational objectives. Full implementation of EQ is expected to help identify potential problem areas in need of process improvements or focused training and ultimately, lead to reductions in examination cycle time.

| Measure: TEGE Determination Case Closures (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 189000 | 141000 | 131700 | 112400 | 112400 |
| Actual | 171812 | 143877 | 126481 | 107761 | |
| Target met? | N | **Y** | **N** | **N** | |

**Definition**: Cases established and closed on the Employee Plans-Exempt Organizations Determination System (EDS) includes all types of tax exempt and employee plan application cases.

**Source**: Tax Exempt and Government Entities (TE/GE) Determination System (EDS) Table 2A

**Future Plans/Explanation for Shortfall**: The FY 2006 target was not met. The implementation of the new staggered amendment filing process for employee plans changed the FY 2006 inventory mix. Over 40 percent of the 25,000 receipts were prototype plans that required more extensive review. These cases will not close until FY 2007, resulting in the closure of 3,600 fewer cases than originally planned. Additionally, recent increases in user fees for employee plan determinations resulted in a slight decrease in determination applications and ultimately 1500 fewer projected closures. To stabilize the flow of determination receipts and mitigate the significant swings in workload experienced prior to FY 2006, the IRS will continue its roll-out of the staggered amendment process. The IRS also plans to test and pilot (with external partners) a new interactive software application for preparing determination applications designed to improve the quality of determination requests and establish the foundation for future electronic filing of these applications. (* The FY 2007 target was revised based on the implementation of the new staggered amendment filing system.)

| Measure: Examination Quality - Coordinated Industry (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 85 | 70 | 90 | 92 | 93 |
| Actual | 89 | 87 | 89 | 96 | |
| Target met? | **Y** | **Y** | **N** | **Y** | |
| **Definition**: The average of the percentage of critical elements passed on Coordinated Industry cases reviewed. | | | | | |
| **Source**: The Large & Mid-Size Business (LMSB) Quality Measurement System (LQMS) database. | | | | | |
| **Future Plans/Explanation for Shortfall**: The IRS plans to identify areas that warrant further attention and improvement through its quality reviews. All examination training courses will expand modules on the identified improvement targets and incorporate pertinent information about the auditing standards used to measure case quality. The IRS will also continue its work with the Case Quality Improvement Council (CQIC) and its Industry contacts to drive quality improvement efforts. | | | | | |

| Measure: Examination Quality - Industry (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 75 | 80 | 78 | 80 | 84 |
| Actual | 74 | 74 | 77 | 85 | |
| Target met? | **N** | **N** | **N** | **Y** | |
| **Definition**: The average of the percentage of critical quality attributes passed on Industry cases (corporations, S-corps (pass through corporations) and partnerships with assets over $10 million) reviewed. | | | | | |
| **Source**: The Large & Mid-Size Business (LMSB) Quality Measurement System (LQMS) database. | | | | | |
| **Future Plans/Explanation for Shortfall**: The IRS plans to identify areas that warrant further attention and improvement through its quality reviews. All examination training courses will expand modules on the identified improvement targets and incorporate pertinent information about the auditing standards used to measure case quality. The IRS will also continue its work with the Case Quality Improvement Council (CQIC) and its Industry contacts to drive quality improvement efforts. | | | | | |

| Measure: Field Collection Embedded Quality (EQ) (%) (Oe) (Replaces Field Collection Quality of Cases Handled in Person) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | TBD |
| Actual | | | | 84.2 | |
| Target met? | N/A | N/A | N/A | **Y** | |
| **Definition**: The number of EQ quality attributes that are scored as "met" by an independent centralized review staff divided by the total attributes measured (met + not met) in a sample of closed cases. All measured attributes have the same weight when calculating the score. | | | | | |
| **Source**: Monthly reports supplied from the EQMS database. | | | | | |
| **Future Plans/Explanation for Shortfall**: This measure was baseline in FY 2006. The IRS will complete the full implementation of EQ with the addition of the front line manager phase. This phase directly links Critical Job Elements to the quality measurement system, improving the relationship between individual performance and organizational objectives. Full implementation of EQ is expected to help identify potential problem areas in need of process improvements or focused training and ultimately, lead to reductions in collection cycle time. | | | | | |

| Measure: AUR Coverage (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 2.5 | 2.3 | 2.3 |
| Actual | | 1.9 | 2.2 | 2.4 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: Total number of W&I and SB/SE contact closures (a closure resulting from a case where IRS made contact) divided by the total return filings from the prior year.

**Source**: AUR Management Information System for Top Level Executives (MISTLE)

**Future Plans/Explanation for Shortfall**: The IRS plans to leverage the process improvements implemented in FY 2006 to improve workload selection and productivity, reducing the number of cases closed without taxpayer contact.

| Measure: Examination Efficiency – Individual (E) (Revised) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 121 | 121 | 128 |
| Actual | | | 121 | 128 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The sum of all individual returns closed by SB/SE, W&I, and LMSB (Field Examination and Correspondence Examination) divided by the Total Full Time Equivalents (FTE) expended in examining those individual returns. In FY 2005, Automated Underreporter (AUR) cases were included as part of this measure. In FY 2006, AUR Efficiency is covered as a separate measure. The new methodology was applied to prior year actual and FY 2006 plan number.

**Source**: The data comes from the Audit Information Management System (AIMS) closed case data base, the automated underreporter Management Information System for Top Level Executives (MISTLE) reports and Exams time reporting system and the Integrated Financial System.

**Future Plans/Explanation for Shortfall**: The IRS will continue to provide balanced exam coverage for those individual return categories with the highest risk of non-compliance, focusing on both understatement of income and overstatement of offsets to income. Newly designed training supports this emphasis, with its focus on auditing techniques.

| Measure: Refund Timeliness - Individual (paper) (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | 98.3 | 98.4 | 99.2 | 99.2 |
| Actual | 98.8 | 98.4 | 98.3 | 99.3 | |
| Target met? | N/A | N/A | N | Y | |

**Definition**: The percentage of refunds resulting from processing Individual Master File paper returns issued within 40 days or less.

**Source**: Submission Processing Measures Analysis and Reporting Tool (SMART). Data is extracted from a Generalize Mainframe Framework computer run that processes data input by the processing centers.

**Future Plans/Explanation for Shortfall**: The IRS expects its performance for refund timeliness to remain stable within the current processing system and resource constraints.

## Alcohol and Tobacco Tax and Trade Bureau

**Measure: Percentage of total tax receipts collected electronically (%) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 98 | 98 | 98 | 98 | 98 |
| Actual | 98 | 97.3 | 98 | 98 | |
| Target met? | Y | N | Y | Y | |

**Definition**: The portion of total tax collected from taxpayers via electronic funds transfer (EFT).

**Source**: Data on tax payments made electronically are recorded in Cashlink (Deposit reporting and cash concentration system). The Revenue Accounting Unit retrieves the wire transfer information from Cashlink. The detail records are input into the Electronic Wire Transfer table using the Federal Excise Tax System.

**Future Plans/Explanation for Shortfall**: This target is nearing the maximum amount that can conceivably be achieved considering the significance of the number. TTB will continue to implement the recommendations of its business process reengineering study for Collect the Revenue from 18 months ago which will help maintain this measure.

**Measure: Resources as a percentage of revenue (%) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | | .4 | .34 | .34 |
| Actual | | | .37 | .31 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: Represents the amount of resources expended to collect taxes, divided by the amount of taxes collected.

**Source**: Taxes collected is captured by the Federal Excise Tax database; expense data is maintained in Oracle Financials.

**Future Plans/Explanation for Shortfall**: This figure is among the best in the world. The goal will be to find ways to maintain it based on increasing labor costs, an already small percentage of administrative costs for the amount of activities that TTB is able to perform.

**Measure: Percentage of Voluntary Compliance in filing tax payments timely and accurately (in terms of number of compliant industry members) (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | | 70 | 74 | 74 |
| Actual | | | 70 | 75.95 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: The portion of total taxpayers that file payments on or before the scheduled due date, without notification of any delinquency.

**Source**: TTB maintains late-filed tax payments in FETS.

**Future Plans/Explanation for Shortfall**: : TTB has increased the number of audits of small taxpayers and audits in general. With CPAs accounting for a highly trained workforce, TTB plans to continue to perform audits using a recently developed risk-based model for Fiscal Year 2007. Along with educating industry members, this approach should serve to increase voluntary compliance.

| Measure: Cumulative percentage of excise tax revenue audited over 3 years (%) (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | 65 | 90 | 12 |
| Actual | | | 82 | 93 | |
| Target met? | N/A | N/A | Y | Y | |
| **Definition**: The portion of total excise tax revenue that is audited in the fiscal years covered in the 5-year period. | | | | | |
| **Source**: TTB tracks completion of all scheduled audits. | | | | | |
| **Future Plans/Explanation for Shortfall**: TTB continued its three year effort to audit the largest taxpayers who are responsible for 98 percent of the annual federal excise tax collections. This effort is the driving force in measuring the tax gap and ensuring that the bureau is collecting the amount of revenue that is rightfully due the federal government. FY 2006 is the last year in TTB's initial 3-year audit cycle and the second audit cycle begins in FY 2007. TTB will have completed audits on 90-100 of the largest federal excise taxpayers. Audit findings have included underpayment of tax, recordkeeping violations, and internal control irregularities. While the audit effort focuses on the major taxpayers, the remaining taxpayers are selected for audit based on risk and random sampling. TTB will no longer track this measure electronically. TTB's risk- based model will drive some of its audit activity in the future. | | | | | |

| Measure: Unit cost to process an excise tax return based on new legislation ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | | Baseline | 76 |
| Actual | | | | 76 | |
| Target met? | N/A | N/A | N/A | Y | |
| **Definition**: The cost of resources that it takes to process one excise tax return. | | | | | |
| **Source**: Capturing excise tax returns: Tax returns are submitted via mail and the Pay.gov system. Mail submissions are assigned a unique control number and date of receipt is logged into the Integrated Revenue Information System (IRIS). Pay.gov assigns a unique number and date of submission automatically. This information is then transmitted and consolidated in IRIS. TTB generates a report from IRIS indicating the number of tax returns processed. Capturing resource cost data: NRC captures resource expenses in the Status of Funds Report in Discoverer (Oracle Financial Reporting System). | | | | | |
| **Future Plans/Explanation for Shortfall**: This is a baseline cost and reflects TTB's work with industry to reduce the burden for small taxpayers. TTB has restructured its National Revenue Center by mission. This will help better prepare for a more efficient operation in the future. | | | | | |

| Measure: Percentage of Voluntary Compliance in filing tax payments timely and accurately (in terms of revenue) (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Baseline | 82 | 84 | 86 | 86 |
| Actual | 80 | 81.2 | 86.3 | 87.2 | |
| Target met? | Y | N | Y | Y | |
| **Definition**: The portion of total taxpayers that file payments on or before the scheduled due date, without notification of any delinquency. | | | | | |
| **Source**: Late filed tax payments are maintained in the Federal Excise Tax system (FET). | | | | | |
| **Future Plans/Explanation for Shortfall**: TTB has audited 93% of the revenue produced by industry members over the past three years. In addition to providing education through seminars, etc. for industry members, TTB has also hired mostly CPAs for audit activities. For FY 2007, TTB will continue to educate and hire high quality auditors if and when current members of the workforce retire. | | | | | |

## Objective: Manage Federal Debt Effectively and Efficiently

## Bureau of Public Debt

| Measure: Cost per federal funds investment transaction ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 90.15 | 64.5 |
| Actual | | | 88.74 | 55.06* | |
| Target met? | N/A | N/A | Y | Y | |
| **Actuals are estimated results* | | | | | |
| **Definition**: This performance measure divides the Federal funds investment costs, determined by an established cost allocation methodology, by the number of issues, redemptions, and interest payments for more than 200 trust funds, as well as the Treasury managed funds. | | | | | |
| **Source**: The automated investment accounting system captures and reports transaction counts. Costs are captured in our administrative accounting system. | | | | | |
| **Future Plans/Explanation for Shortfall**: The cost per federal funds investment transaction is forecasted not to exceed the FY 2006 target of $90.15. Expected continuing volume increases in FY 2007 related to additional Government entity investment transactions allow us to establish a target for FY 2007 of $64.50. Expenditure projections reflect increases for inflation. | | | | | |

| Measure: Percent of auction results released in 2 minutes +/- 30 seconds (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | 95 | 95 | 95 | 95 |
| Actual | | 99.53 | 95 | 100 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: This measures the elapsed time from the auction close to the public release of the auction results. The annual percentage of auctions meeting the release time target of 2 minutes plus or minus 30 seconds is calculated for the fiscal year.

**Source**: BPD's automated auction processing systems

**Future Plans/Explanation for Shortfall**: To improve performance and continue to meet its target, Public Debt will continue training all auction staff members by conducting mock auctions to enhance its ability to handle various contingencies.

| Measure: Percentage of retail customer service transactions completed within 13 business days (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | 90 | 90 | 90 | 90 |
| Actual | | 92.5 | 88.7 | 98 | |
| Target met? | N/A | Y | N | Y | |

**Definition**: The length of time to complete a customer service transaction is measured from the date each transaction is received to the date it is completed.

**Source**: For customer service transactions received by mail and for some requests received by phone or Internet, BPD uses an automated tracking system that measures the length of time it takes to complete the transactions. Simple phone and Internet requests are manually tracked.

**Future Plans/Explanation for Shortfall**: For FY 2007, the goal is to complete 90 percent of retail customer service transactions within 12 business days and strive toward a long-term goal to complete 90 percent of retail customer service transactions within 10 business days by FY 2010. Efficiencies gained from improved work processes and an increase in electronic transactions will allow the Bureau to meet these goals.

| Measure: Cost per TreasuryDirect assisted transaction ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 7.75 | 4.73 |
| Actual | | | 8.51 | 4.75* | |
| Target met? | N/A | N/A | Y | Y | |

** Actuals are estimated results.*

**Definition**: This performance measure divides TreasuryDirect customer service transaction costs, determined by an established cost allocation methodology, by the number of customer requests completed with assistance by a customer service representative.

**Source**: For customer service transactions received by mail and for some requests received by phone or Internet, BPD obtains volumes from an automated tracking system. Simple phone and Internet requests are manually counted. Costs are captured in BPD's administrative accounting system.

**Future Plans/Explanation for Shortfall**: The cost per TreasuryDirect assisted transaction is forecasted not to exceed the FY 2006 target of $7.75 and target levels for FY 2007 are projected at $4.73. Public Debt will reallocate resources to handle a continuing increase in customer transactions that result from the growing number of TreasuryDirect accounts.

| Measure: Percentage of Government Agency customer initiated transactions conducted online (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | Baseline | 65 | 75 |
| Actual | | | 72.7 | 97.03 | |
| Target met? | N/A | N/A | **Y** | **Y** | |

**Definition**: Public Debt administers three programs in which Government agencies conduct transactions. 1. Government Account Series Securities (Federal Investments) 2. Treasury Loans Receivable (Borrowings) 3. State and Local Government Series (securities). Prior to an initiative to make our systems available on the Internet, customers faxed all requests to Public Debt, and BPD manually entered the transactions into the various systems. BPD's long-term goal is to have 80% of customer-initiated transactions completed online by the end of FY 2008.

**Source**: Total transaction counts are captured from the investment accounting systems in automated reports that differentiate online transactions from other transactions entered into the systems.

**Future Plans/Explanation for Shortfall**: Public Debt, in an effort to expand on-line investment services to its federal, state and local customers, has exceeded fiscal year 2006 projections. This achievement has taken place primarily due to the implementation of the new SLGS regulations effective in August 2005. These regulations require state and local government securities customers to submit investment transactions online via the SLGSafe internet application. The Bureau expects investment online percentages to remain at the current level in the upcoming years.

| Measure: Cost per TreasuryDirect online transaction ($) (E) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | Baseline | 2.99 | 2.21 |
| Actual | | | 3.43 | 2.43* | |
| Target met? | N/A | N/A | **Y** | **Y** | |

**Actuals are estimated results.*

**Definition**: This performance measure divides TreasuryDirect online transaction costs, determined by an established cost allocation methodology, by the number of TreasuryDirect online transactions.

**Source**: Workload figures are captured from information stored in TreasuryDirect. Costs are captured in BPD's administrative accounting system.

**Future Plans/Explanation for Shortfall**: The cost per TreasuryDirect online transaction is forecasted not to exceed the FY 2006 target of $2.99. As more customers purchase book-entry securities through TreasuryDirect, Public Debt forecasts the cost of an online transaction at $2.21 for FY 2007.

| Measure: Cost per debt financing operation ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 133683 | 219114 |
| Actual | | | 126828 | 127066.54 | |
| Target met? | N/A | N/A | Y | Y | |
| **Actuals are estimated results.* | | | | | |
| **Definition**: This performance measure divides debt financing operations costs, determined by an established cost allocation methodology, by the number of auctions and buybacks. | | | | | |
| **Source**: The number of debt financing operations is captured in the Auction Information Calendar (AIC) and the Auction Analysis System. Costs are captured in BPD's administrative accounting system. | | | | | |
| **Future Plans/Explanation for Shortfall**: The cost per debt financing operations is forecasted not to exceed the FY 2006 target of $133,683. The projection for FY 2007 of $219,114 includes increases for inflation, and the estimated cost of replacing the legacy auction system, which will provide Treasury debt managers the ability to bring new types of securities to market. | | | | | |

## Departmental Offices

| Measure: Release Federal Government-wide financial statements on time (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | Met | Met | Met | Met | Met |
| Actual | Met | Met | Met | Met | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: This report is the audited consolidated financial report of the Federal Government required by the Government Management Reform Act. | | | | | |
| **Source**: Data are collected from the audited financial results of all federal agencies and is audited by GAO. | | | | | |
| **Future Plans/Explanation for Shortfall**: Treasury plans to continue to establish policies and procedures to release the Federal government-wide financial statements on time. | | | | | |

## Objective: Make Collections and Payments on Time and Accurately, Optimizing Use of Electronic Mechanisms

## Departmental Offices

**Measure: Variance between estimated and actual receipts (annual forecast) (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | 5 | 5 | 5 | 5 |
| Actual | | 3.8 | 5 | 3.9 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: Percentage error measures the accuracy of the Mark receipts forecasts produced monthly by the Office of Fiscal Projections (OFP). It measures the relative amount of error or bias in OCDM's receipts forecasts.

**Source**: OFP within the Office of the Fiscal Assistant Secretary compiles receipts data by major categories (i.e., withheld income taxes, individual taxes, FICA, corporate, customs deposits, estate and excise) as well as by types of collection mechanisms (electronic and paper coupons). OFP is also responsible for forecasting the daily tax receipts in order to manage the Federal Government's cash flow. Data on monthly and daily federal tax receipts of actual and forecasts are compiled by the office and are used to report on the United States' monthly, weekly, and daily cash position in addition to determining the optimal financing for cash management.

**Future Plans/Explanation for Shortfall**: In FY 2007, the tolerance will continue to be 5%. To meet the performance measure in FY 2006, Domestic Finance increased the frequency of its meetings with the Office of Macroeconomic Analysis (Office of the Assistant Secretary for Economic Policy) to monthly and expanded them to include staff from the Revenue Estimating Staff (Office of the Assistant Secretary for Tax Policy) . These meetings focused on identifying revisions to key macro-economic variables and indicators and the impact that these revisions, both retrospective and prospective, had on current receipt projections The success of this process is evident by the annual performance, which exceeded the tolerance for FY 2006 and resulted in a reduction in the forecast variance from FY 2005. The process will be continued in FY 2007 and revised, as necessary, to ensure positive results.

## Financial Management Service

**Measure: Percentage collected electronically of total dollar amount of Federal government receipts (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 80 | 81 | 82 | 83 | 84 |
| Actual | 80 | 81 | 79 | 79 | |
| Target met? | Y | Y | N | N | |

**Definition**: Electronic collections data are retrieved from the CA$H-LINK system, which encompasses eight collection systems.

**Source**: This measure considers the percentage of government collections that are collected by electronic mechanisms (Electronic Federal Tax Payment System, Plastic Card, FEDWIRE Deposit System, Automated Clearinghouse (ACH))compared to total government collections. The system receives deposit and accounting information from local depositories and provides detailed accounting information to STAR, FMS' central accounting and reporting system.

**Future Plans/Explanation for Shortfall**: : A large component of this performance measure is IRS lockbox collections, which represents paper checks mailed from individuals and small businesses. FMS did not meet this measure due to the number of paper 1040 tax remitters during the third quarter of the fiscal year. Excluding those months when IRS lockbox processing is at its peak, electronic collections totaled 85 percent. FMS continues to try to move paper deposits to electronics.

**Measure: Unit cost to process a Federal revenue collection transaction ($) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | Baseline | 1.4 | 1.37 | 1.33 |
| Actual | | 1.4 | 1.2 | 1.1* | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: The unit cost to process a revenue collection transaction.

**Source**: The cost data is captured through an activity based costing process. The unit cost is the calculated ratio of total direct and indirect costs over total government-wide collection transactions.

**Future Plans/Explanation for Shortfall**: FMS will continue to expand electronic collection tools to other agencies in an effort to improve efficiency and keep costs low. In late FY 2006 FMS concluded the re-bid of the Plastic Card Network and will see significant cost savings in future years. FMS will continue reviewing other collection tools to determine new efficiencies and potential cost savings. **Unit measure is estimated until costs are finalized.*

**Measure: Percentage of Treasury Payments and associated information made electronically (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | 74 | 75 | 76 | 78 | 79 |
| Actual | 74 | 75 | 76 | 77 | |
| Target met? | Y | Y | Y | N | |

**Definition**: The portion of the total volume of payments that is made electronically by FMS. Electronic payments include transfers through the automated clearinghouse and wire transfer payments through the FEDWIRE system.

**Source**: The volume of payments is tracked through FMS' Production Reporting System. The amount and number of payments are also maintained under accounting control.

**Future Plans/Explanation for Shortfall**: In FY 2006, FMS set an aggressive goal to increase the amount of payments made electronically by 2 percent instead of our initial 1 percent. We set this goal because FMS implemented the Go-Direct Campaign. While the Go-Direct campaign was successful (converting over 600,000 individuals from checks to direct deposit in the first full year), the aggressive target, coupled with continued large number of social security check and emergency check payments for FEMA, has prevented FMS from achieving its goal of making 78 percent of all federal payments electronically. Although the performance measure was missed, FMS issued over 7.5 million fewer checks than last year. FMS continues to expand and market the use of electronic media to deliver federal payments, improve service to payment recipients, and reduce government program costs. FMS is working to implement a pilot program, which is directed at the un-banked, to disburse benefit payments through debit cards.

| Measure: Percentage of paper check and Electronic Funds Transfer (EFT) payments made accurately and on time (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 99.9999 | 100 | 100 | 100 | 100 |
| Actual | 99.9999 | 100 | 100 | 100 | |
| Target met? | **Y** | **Y** | **Y** | **Y** | |

**Definition**: Accurately refers to the percentage of check and EFT payments that FMS makes which are not duplicative or double payments. On time means that FMS releases checks to the U.S. Postal Service and EFT payments to the Federal Reserve Bank such that normal delivery by them results in timely receipt by payees.

**Source**: Accuracy data is captured through FMS' Regional Financial Centers which submit statistics on duplicate payments and data for the performance measure. The payments are balanced with payment certifications submitted to FMS by Federal Program Agencies. On time data on check and EFT volumes are captured monthly in a report from FMS' Production Reporting System.

**Future Plans/Explanation for Shortfall**: FMS has met our FY 2006 performance goal. In FY 2007 FMS plans to continue to issue 100% of our payments accurately and on-time. The Secure Payment System (SPS) used by program agencies to certify checks, clearinghouses, or wire payments to recipients in a secure environment is a critical component in achieving the performance goal.

| Measure: Unit cost for Federal Government payments ($) (E) | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | Baseline | .35 | .35 | .35 |
| Actual | | .35 | .355 | .37* | |
| Target met? | N/A | **Y** | **N** | **N** | |

**Definition**: Unit cost combines both paper and electronic payment mechanisms and includes the aftermath processes (reconciliation and claims) for both types of payment mechanisms.

**Source**: The cost data is captured through an activity based costing process. The unit cost is the calculated ratio of cost per payment.

**Future Plans/Explanation for Shortfall**: As a result of increased infrastructure costs, as well as postage increases, FMS did not meet its FY 2006 unit cost measure. FMS will continue to improve efficiencies in payment delivery by concentrating on expanding electronic payments, which cost substantially less than check payments. To assist in this endeavor, FMS will continue its "Go Direct" campaign which converted over 600,000 individuals from check to direct deposit in the first full year of the campaign, as well as look to other means (such as debit cards) to increase electronic payments. **Unit measure is estimated until costs are finalized.*

## Objective: Optimize Cash Management and Effectively Administer the Government's Financial Systems

## Bureau of Public Debt

| Measure: Cost per summary debt accounting transaction ($) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 11.59 | 10.34 |
| Actual | | | 12.62 | 9.08* | |
| Target met? | N/A | N/A | Y | Y | |

**Actuals are estimated results*

**Definition**: This performance measure divides summary debt accounting transaction costs, determined by an established cost allocation methodology, by the number of summary debt accounting transactions.

**Source**: Public debt accounting systems capture and report transaction counts. Costs are captured in BPD's administrative accounting system.

**Future Plans/Explanation for Shortfall**: The cost per summary debt accounting transaction is forecasted not to exceed the FY 2006 target of $11.59 and target levels for FY 2007 are projected at $10.34. FY 2007 target levels assume static transaction volumes that support accounting for the public debt, a key component of Public Debt's mission. Public Debt will continue to maintain and support strong accounting controls to ensure the integrity of operations and the accuracy of the public debt accounting information provided to the public.

## Financial Management Service

| Measure: Unit Cost to Manage $1 Million Dollars of Cash Flow | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 8.72 | 6.4 |
| Actual | | | 0 | 8.5* | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: This Unit Cost Measure assesses Government Wide Accounting's (GWA's) Cost to Manage Government Operations. The Government Operations consists of total GWA costs which consist of all Directorates, Systems, Administrative Overhead, and major initiatives performed within GWA. On a monthly basis the Cost-per-Million of Cash Flow managed by GWA is calculated.

**Source**: The Total GWA Cost data is retrieved from the year ending Cost Accounting Report. The Operating Cash, which is rounded in millions, is determined from the final DTS of each month for the fiscal year. The ratio of total costs to GWA per month over Deposits and Withdrawals (Excluding Transfers) gives us the cost to manage $1 Million dollars of cash flow. This ratio is calculated for GWA alone to determine controllable costs, and using Information Resources / TWAI and Management Overhead to determine the uncontrollable costs attributed to GWA.

**Future Plans/Explanation for Shortfall:** BASELINE. **Unit measure is estimated until costs are finalized.*

| Measure: Percentage of Government-wide accounting reports issued timely (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 100 | 100 | 100 | 100 | 100 |
| Actual | 100 | 100 | 100 | 100 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: All Government-wide financial data that FMS publishes relating to U.S. Treasury cash-based accounting reports (i.e., the Daily Treasury Statement, the Monthly Treasury Statement, and the Annual Combined Report) will be on time 100% of the time.

**Source**: A monthly reporting system is used to track the release dates to the public of all of the various governmentwide statements.

**Future Plans/Explanation for Shortfall**: FMS has met its FY 2006 performance goal. FMS is building and implementing a system to improve the exchange of financial information among FMS, Federal Program Agencies (FPA), Office of Management and Budget (OMB) and the banking community. Once completed, this Government-wide Accounting (GWA) Modernization Project will comprehensively replace current government-wide accounting functions and processes that are both internal and external to FMS. It will improve the reliability, usefulness, and timeliness of the government's financial information.

| Measure: Percentage of Government-wide accounting reports issued accurately (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 98 | 100 | 100 | 100 | 100 |
| Actual | 98 | 100 | 100 | 100 | |
| Target met? | Y | Y | Y | Y | |

**Definition**: All Government-wide financial data that FMS publishes relating to U.S. Treasury cash-based accounting reports (i.e., the Daily Treasury Statement, the Monthly Treasury Statement, and the Annual Combined Report) will be 100% accurate.

**Source**: A monthly tracking system reports on the various published statements and monitors errata as it pertains to this data.

**Future Plans/Explanation for Shortfall**: FMS has met its FY 2006 performance goal. FMS will continue to revamp government-wide accounting processes to provide more useful and reliable financial information on a regular basis. FMS is building and implementing a system to improve the exchange of financial information among FMS, Federal Program Agencies (FPA), Office of Management and Budget (OMB) and the banking community. Once completed, this Government-wide Accounting (GWA) Modernization Project will comprehensively replace current government-wide accounting functions and processes that are both internal and external to FMS. It will improve the reliability, usefulness, and timeliness of the government's financial information, provide FPAs and other users with better access to that information, and will eliminate duplicate reporting and reconciliation burdens by agencies.

## Goal: Ensure Professionalism, Excellence, Integrity, and Accountability in the Management and Conduct of the Department of the Treasury

### Objective: Protect the Integrity of the Department of the Treasury

### Office of Inspector General

| Measure: Number of completed audits and evaluations (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 146 | 48 | 53 | 56 | 56 |
| Actual | 116 | 49 | 54 | 57 | |
| Target met? | N | Y | Y | Y | |
| **Definition**: Audits, attestation engagements, and evaluations: (1) promote economy, efficiency, and effectiveness of Treasury programs and operations; (2) prevent and detect fraud, waste, and abuse in those programs and operations; (3) keep the Secretary and the Congress fully informed; and (4) help the Federal government to be accountable to the public. | | | | | |
| **Source**: OIG audits, attestation engagements, and evaluations result in sequentially numbered written products. | | | | | |
| **Future Plans/Explanation for Shortfall**: OIG exceeded the target number of audits for FY 2006, and expects to meet the FY 2007 target at the expected resource levels. | | | | | |

| Measure: Percent of statutory audits completed by the required date (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 100 | 100 | 100 | 100 | 100 |
| Actual | 92 | 100 | 100 | 100 | |
| Target met? | N | Y | Y | Y | |
| **Definition**: Legislation mandating certain audit work generally prescribes, or authorizes OMB to prescribe, the required completion date for recurring audits and evaluations, such as those for annual audited financial statements. For other types of mandated audit work, such as a Material Loss Review (MLR) of a failed financial institution, the legislation generally prescribes a timeframe to issue a report (6 months for an MLR, as an example) from the date of an event that triggers the audit. | | | | | |
| **Source**: The date OIG issues an audit, attestation engagement, or evaluation report is printed on the cover. The required dates vary each year and are specified in different legislation, most often in the Annual Treasury Appropriation language. | | | | | |
| **Future Plans/Explanation for Shortfall**: OIG completed 100% of mandatory audits on time, and expects to do so in FY 2007 | | | | | |

| Measure: Number of investigations referred for criminal prosecution, civil litigation or corrective administrative action. (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 24 | 15 | 72 | 85 | 105 |
| Actual | 26 | 23 | 85 | 144 | |
| Target met? | Y | Y | Y | Y | |
| **Definition**: In order to protect the integrity and efficiency of Treasury programs it is important that findings of criminal or civil misconduct be referred to the Justice Department, state and/or local governments for prosecution and litigation in a timely manner. Criminal and civil convictions have a greater impact and carry a greater deterrent effect when they are prosecuted expeditiously. Some investigations will identify violations of the Ethical Standards of conduct, Federal Acquisition Regulations, or other administrative standards, which do not rise to the level of criminal or civil prosecution. In these cases it is important that OIG findings are reported to the bureau or office in a timely manner to allow them to take administrative action against the individuals engaging in misconduct. | | | | | |
| **Source**: This data will be retrieved from the Investigations Data Management System (IDMS) system. | | | | | |
| **Future Plans/Explanation for Shortfall**: OIG significantly exceeded the target for this measure. A nearly two-fold increase in investigative personnel that was appropriated in FY 05 is requiring the target to be adjusted in the future. In FY 07, we will continue to work with the Department to refine and fairly set this measure. | | | | | |

## Treasury Inspector General for Tax Administration

| Measure: Average calendar days to issue final audit report (Ot) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 250 | 300 | 300 | 325 | 325 |
| Actual | 317 | 338 | 358 | 334 | |
| Target met? | N | N | N | N | |
| **Definition**: The total number of calendar days elapsed from the start of an audit to the date the final report is issued. This figure is divided by the total number of final reports issued to determine the average. | | | | | |
| **Source**: TIGTA's management information system. | | | | | |
| **Future Plans/Explanation for Shortfall**: Historically, TIGTA OA has not been able to meet this goal due to the increased complexity of its audits and the need to provide IRS sufficient time to respond to its reports. TIGTA OA initiated efforts to re-examine its processes by empanelling two task forces and a pilot test for implementing the concept of an Inspection and Evaluation (I&E) Group. TIGTA OA will implement the recommendations of its Human Capital Task Force staff and I&E staff to provide positive long term impacts on its oversight of tax administration, as well as its program delivery. TIGTA OA will continue to stress the importance of meeting Calendar Day standards with our staff. | | | | | |

| **Measure: Number of total taxpayer accounts potentially impacted as a result of audit activities (in Millions) (Ot)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 14 | 13.4 | 13 | 14.5 | 7.25 |
| Actual | 47 | 49.7 | 2.8 | 1.8 | |
| Target met? | **Y** | **Y** | **N** | **N** | |

**Definition**: This indicator measures the number of taxpaying entities that benefit from audit recommendations. The benefits include: insuring taxpayers receive refunds when warranted and are granted due process when the IRS conducts its return filing and compliance programs; decreasing the number, time or cost of contacts with the IRS by compliant taxpayers; increasing protection of taxpayer account and financial information; and improving security over tax administration systems.

**Source**: Data is entered into a centralized database and verified against draft and final report documents.

**Future Plans/Explanation for Shortfall**: The ability to establish specific outcomes in advance of the overall audit program and individual audit scope being determined is challenging at best. This measure is somewhat dependent on changes in legislation that would lead to misunderstandings by taxpayers or IRS processing shortcomings that need to be identified and resolved. There have not been many significant tax law changes that impacted areas of our FY 2006 audit program. In addition, this measure has its nexus in goals that were developed when TIGTA came into existence in 1999. While taxpayer rights are still a priority for TIGTA OA, additional priorities such as identification of monetary benefits, erroneous payments, increased revenue/revenue protected and security over IRS facilities and information have increased in priority. As such, our resources have been directed to audits in many high-risk tax administration areas. TIGTA OA has experienced a decline in resources dropping from 388 FTEs in FY 2000 to a staffing level of 293 at the end of FY 2006. TIGTA OA has made efforts to modify its goals over time to be commensurate with the decline in staffing levels. As such, some of our audits have not produced the taxpayer account-related outcomes at the rate we have in the past. TIGTA OA will revisit its goal for FY 2007 to establish a target that is more in line with available resources and the focus of its audit program.

| **Measure: Percentage of positive results from investigative activities (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | Baseline | 67 | 70 | 73 |
| Actual | | 64 | 82 | 79 | |
| Target met? | N/A | **Y** | **Y** | **Y** | |

**Definition**: Investigative reports resulting in Criminal, Civil or Administrative adjudication or the identification of matters of security or investigative interest.

**Source**: The total number of investigative cases closed along with the total number of completed Criminal, Civil and Administrative Actions is extracted from the Performance and Results Information System (PARIS).

**Future Plans/Explanation for Shortfall**: TIGTA OI will continue to measure performance consistent with FY 2006 criteria. TIGTA OI increased its measure by 5 percent over FY 2006. TIGTA OI will monitor and evaluate FY 2007 performance and may make adjustments if deemed appropriate. The FY 2008 targets will be determined based on evaluation of the FY 2007 performance results.

## Objective: Manage Treasury Resources Effectively to Accomplish the Mission and Provide Quality Customer Service

## Treasury Franchise Fund

| Measure: Customer satisfaction approval rating-Financial Management Administrative Support Services (%) (Ot) [DISCONTINUED FY 2006] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 80 | 80 | 80 | Discontinued | Discontinued |
| Actual | 94 | 85 | 96 | | |
| Target met? | Y | Y | Y | N/A | |
| **Definition**: Indicates an objective level of customer satisfaction | | | | | |
| **Source**: The result of the survey is derived from the following: (a) ongoing management service reviews with customers through on-site visits; (b) ongoing management contract review with contractors; and (c) customer surveys using scale method with quantitative statistical analysis and results. | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| Measure: Customer satisfaction approval rating–Financial System, Consulting & Training (%) (Ot) [DISCONTINUED FY 2006] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 80 | 80 | 80 | Discontinued | Discontinued |
| Actual | 87 | 87 | 88 | | |
| Target met? | Y | Y | Y | N/A | |
| **Definition**: Indicates an objective level of customer satisfaction | | | | | |
| **Source**: The result of the survey is derived from the following: (a) ongoing management service reviews with customers through on-site visits; (b) ongoing management contract review with contractors; and (c) customer surveys using scale method with quantitative statistical analysis and results. | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| Measure: Customer satisfaction approval ratings–Consolidated/Integrated Administrative Management (Ot) (%) [DISCONTINUED FY 2006] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 80 | 80 | 80 | Discontinued | Discontinued |
| Actual | 81 | 87 | 81 | | |
| Target met? | Y | Y | Y | N/A | |
| **Definition**: Indicates an objective level of customer satisfaction | | | | | |
| **Source**: The result of the survey is derived from the following: (a) ongoing management service reviews with customers through on-site visits; (b) ongoing management contract review with contractors; and (c) customer surveys using scale method with quantitative statistical analysis and results. | | | | | |
| **Future Plans/Explanation for Shortfall**: Measure discontinued in FY 2006. | | | | | |

| Measure: Customer Satisfaction Index – Financial Management Administrative Support Services (%) (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | | Baseline | 71 | 80 |
| Actual | | | 71 | 75 | |
| Target met? | N/A | N/A | Y | Y | |
| **Definition**: : Established in 1994, the American Customer Satisfaction Index (ACSI) is a uniform and independent measure of household consumption experience. A powerful economic indicator, the ACSI tracks trends in customer satisfaction and provides valuable benchmarking insights of the consumer economy for companies, industry trade associations, and government agencies. The ACSI is produced by the Stephen M. Ross Business School at the University of Michigan. | | | | | |
| **Source**: University of Michigan's American Customer Satisfaction Index (ACSI) | | | | | |
| **Future Plans/Explanation for Shortfall**: This was Arc's first year using the ACSI. ARC will learn from the results and further improve customer satisfaction. Based on this FY 2007 target was established at 80. | | | | | |

| Measure: Operating expenses as a percentage of revenue – Consolidated/Integrated Administrative Management (%)(E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 4 | 12 | 12 |
| Actual | | 4 | 4 | 4 | |
| Target met? | N/A | Y | Y | Y | |
| **Definition**: The Franchise Fund will either maintain or decrease their operating (administrative) expenses as a percentage of revenue year to year. | | | | | |
| **Source**: The data is captured in Oracle Financials system and reported through Oracle's Discoverer Reporting system. Measure is calculated as Operating Expenses divided by Total Revenue. | | | | | |
| **Future Plans/Explanation for Shortfall**: FedSource plans to continue to consolidate their operations. | | | | | |

| Measure: Operating expenses as a percentage of revenue – Financial Management Administrative Support (%) (E) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | Baseline | 11 | 12 | 12 |
| Actual | | 9 | 9 | 17 | |
| Target met? | N/A | Y | Y | N | |
| **Definition**: The Franchise Fund will either maintain or decrease their operating (administrative) expenses as a percentage of revenue year to year. | | | | | |
| **Source**: The data is captured in Oracle Financials system and reported through Oracle's Discoverer Reporting system. Measure is calculated as Operating Expenses divided by Total Revenue. | | | | | |
| **Future Plans/Explanation for Shortfall**: ARC did not meet the performance target due to the excessive expenses that they incurred from their provider for IT and administrative support. The expenses associated with these two services account for approximately 70% of their total Administrative Operating Expense. In FY 2006, ARC incurred $1.6 million in expenses for furniture. ARC plans to get percentage under 12% through negotiations. | | | | | |

**Measure: Customer Satisfaction Index - Financial System, Consulting & Training**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | | Baseline | 71 | 80 |
| Actual | | | 71 | 81 | |
| Target met? | N/A | N/A | Y | Y | |

**Definition**: Established in 1994, the American Customer Satisfaction Index (ACSI) is a uniform and independent measure of household consumption experience. A powerful economic indicator, the ACSI tracks trends in customer satisfaction and provides valuable benchmarking insights of the consumer economy for companies, industry trade associations, and government agencies. The ACSI is produced by the Stephen M. Ross Business School at the University of Michigan.

**Source**: American Customer Satisfaction Index (ACSI)

**Future Plans/Explanation for Shortfall**: Federal Consulting Group has put an action plan together using the results of this year's ACSI to further improve customer satisfaction.

**Measure: Customer Satisfaction Index–Consolidated/Integrated Administrative Management (%) (Oe)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | | Baseline | 71 | 80 |
| Actual | | | 71 | 51 | |
| Target met? | N/A | N/A | Y | N | |

**Definition**: Established in 1994, the American Customer Satisfaction Index (ACSI) is a uniform and independent measure of household consumption experience. A powerful economic indicator, the ACSI tracks trends in customer satisfaction and provides valuable benchmarking insights of the consumer economy for companies, industry trade associations, and government agencies. The ACSI is produced by the Stephen M. Ross Business School at the University of Michigan.

**Source**: University of Michigan's American Customer Satisfaction Index (ACSI)

**Future Plans/Explanation for Shortfall**: FedSource has been working through significant restructuring issues. With the elimination of three FedSource field offices, work had to be transitioned to other offices, which disrupted customer service and affected their score. Other work had to be re-competed due to contract ceiling issues that also hurt their score. FedSource has a moratorium new business while they focus on these issues.

**Measure: Operating expenses as a percentage of revenue–Financial Systems, Consulting and Training (%) (E)**

| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|---|---|
| Target | | Baseline | 12 | 12 | 12 |
| Actual | | 14 | 11 | 10 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: The Franchise Fund will either maintain or decrease their operating (administrative) expenses as a percentage of revenue year to year.

**Source**: The data is captured in Oracle Financials system and reported through Oracle's Discoverer Reporting system. Measure is calculated as Operating Expenses divided by Total Revenue.

**Future Plans/Explanation for Shortfall**: Treasury Agency Services was able to drastically reduce their rent expense which helped them meet this performance measure. Federal Consulting Group is currently looking to reduce their rent expense.

## Departmental Offices

| **Measure: Percent of complainants informally contacting EEO (for the purposes of seeking counseling or filing a complaint) who participate in the ADR process (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | 25 | 25 | 30 |
| Actual | | | 25 | 25 | |
| Target met? | N/A | N/A | **Y** | **Y** | |
| **Definition**: Equal Employment Opportunity (EEO) contact means an instance where an EEO Counselor or an ADR Intake Officer performs the counseling duties described in Chapter 2 of MD 110 (Government-wide managing directive on EEO). This is the same information which is reported in Part One, Section one of 462 reports (Government-wide EEO report). Participation means both parties agree to enter an ADR process. | | | | | |
| **Source**: Treasury's automated Complaint Tracking System. | | | | | |
| **Future Plans/Explanation for Shortfall**: An emphasis was placed on ensuring that Alternative Dispute Resolution (ADR) was offered to each complainant at both the pre-investigative stage and the post-investigative stage. Although these offers did not frequently result in the complainant's acceptance of ADR, there were more opportunities to resolve the case without investigation. The total number of ADR offers increased from 169 in FY05 to 407 in FY06, an increase of 238 or 42%. | | | | | |

| **Measure: Complete investigations of EEO complaints within 180 days (%) (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | 40 | 50 | 50 | 50 |
| Actual | | 31 | 36 | 27* | |
| Target met? | N/A | **N** | **N** | **N** | |
| **Definition**: The average time it takes to complete investigations of Equal Employment Opportunity (EEO) complaints. | | | | | |
| **Source**: The Annual Federal EEO Statistical Report of Discrimination Complaints and the Department's Complaint Tracking System are the primary sources of data. | | | | | |
| **Future Plans/Explanation for Shortfall**: While Treasury did not meet the standard for processing complaints within the 180 day timeframe, the Department was successful in eliminating the 200+ backlog of cases by working aged cases first. To do this, the Center took a proactive approach and developed a system where: managers are assigned to review cases at the acceptance stage, identifying issues and then making a determination to accept or dismiss the claim; technical advisors write dismissal letters; and with the use of collateral duty and task force assignments; this system allows for more timely processing and efficient determination of a case. | | | | | |

| **Measure: Management cost per Treasury employee ($) (E)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | | | Baseline | 40.27 | 38.21 |
| Actual | | | 39.33 | 40.59 | |
| Target met? | N/A | N/A | **Y** | **N** | |

**Definition**: Total amount obligated for Treasury's strategic objective, M5B, divided by total amount of Treasury FTEs (excluding IRS employees).

**Source**: Total amount obligated for M5B is taken from year end execution reports. The total amount of Treasury FTEs is taken by each bureau (except IRS) from the Department of Agriculture's National Finance Center database.

**Future Plans/Explanation for Shortfall**: While Treasury overall funding and FTE's decreased in FY 2006, funding for strategic objective M5B increased as well as non-IRS FTE's, causing the measure to be slightly over target. Targets for FY 2007 have been established based on the congressional justification, but this measure may be discontinued and replaced with a measure that indicates the degree of alignment of budget resources to outcomes from the new Treasury strategic plan.

| **Measure: Number of open material weaknesses (Oe)** | | | | | |
|---|---|---|---|---|---|
| | **FY 2003** | **FY 2004** | **FY 2005** | **FY 2006** | **FY 2007** |
| Target | 8 | 6 | 4 | 2 | 1 |
| Actual | 9 | 8 | 7 | 1 | |
| Target met? | **N** | **N** | **N** | **Y** | |

**Definition**: Treasury seeks to reduce and eventually eliminate the material weaknesses that currently exist within Treasury, while simultaneously taking actions which will serve to avoid new material weaknesses. Material weaknesses are significant problems with an organization's internal controls, systems' reliability, controls on waste, fraud or abuse, mission performance, and compliance with laws and regulations.

**Source**: Identified by the General Accounting Office, Treasury's Inspectors General, and/or Treasury bureaus.

**Future Plans/Explanation for Shortfall**: Treasury began FY 2006 with 7 material weaknesses and downgraded 1 to a reportable condition during the year, leaving a reportable balance of 6 beginning FY 2007. Although significant success has been achieved, those material weaknesses that remain have long-term solutions of which are many are dependent upon the implementation of major systems. Success has been achieved through ongoing management attention in the form of quarterly progress reports to executive management on the status of material weaknesses, the inclusion of material weaknesses as an agenda topic for bureau heads meetings, and similar vehicles which help focus attention on major challenges. Although certain long-standing challenges will remain problematic for the foreseeable future, responsible progress toward closure on these challenges continues to be achieved and no new material weaknesses have been identified.

| Measure: Bureau performance plans for supervisors, managers, and SES members contain elements that link to the bureau mission (%) (Oe) [DISCONTINUED FY 2007] | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | | 75 | 100 | 100 | 100 |
| Actual | | 77 | 100 | 100 | |
| Target met? | N/A | Y | Y | Y | |

**Definition**: The overall percentage of bureaus whose performance plans for supervisors, managers, and SES members contain elements that specifically link to the bureau mission.

**Source**: Data will include bureau feedback in response to questions posed by the Office of Human Resources Strategy and Solutions, bureau results from using the Office of Personnel Management's Performance Appraisal and Assessment Tool to assess their performance management systems, and submission of sample bureau performance plans.

**Future Plans/Explanation for Shortfall**: The target was met and will continue to be met in FY 2007 and FY 2008. The goal has been clearly communicated to supervisors, managers, and SES members and continued compliance is expected. As a result of continued success, Treasury will be discontinuing the tracking of this metric in FY 2007. It will be replaced by a metric aimed at evaluating retention of new hires.

| Measure: Injury and illness rate Treasurywide-including DO (Oe) | | | | | |
|---|---|---|---|---|---|
| | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 |
| Target | 3.21 | 3.12 | 3 | 2.8 | 2.6 |
| Actual | 3.9 | 3.94 | 2.8 | 1 | |
| Target met? | N | N | Y | Y | |

**Definition**: The number of reported work-related injuries and illnesses Treasury-wide.

**Source**: Safety and Health Information Management System

**Future Plans/Explanation for Shortfall**: In FY 2004, Treasury was recognized by the Department of Labor for reducing the Departments total injury and lost time injury rates by more than 10 % each, well below the recommended 3 % for all Federal Agencies. Over the past two years, the injury rate has remained low due to an increased focus on employee safety and health. In FY 2006, Treasury started to pursue an aggressive occupational safety and health program and this program will be continued in FY 2007 and beyond.

* Current year end data is projected actual.

## Key

| | |
|---|---|
| Oe | Outcome Measure |
| E | Efficiency Measure |
| Ot | Output/Workload Measure |

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# Appendix B: Completeness and Reliability of Performance Data

## Treasury's Commitment to Quality Performance Measurement

Bureaus to rate the data for each performance measure as having:

- *Reasonable Accuracy:* : Judged to be sufficiently accurate for program management and performance reporting purposes (specified in OMB Circular A-11, Section 230-4(f)).
- *Questionable or Unknown Accuracy:* Judged to be materially inadequate (specified in OMB Circular A-11, Section 230-4(f) as "materially inadequate").
- Where statistical confidence intervals are available, these are provided instead of the rating statements. More verification efforts were added in FY 2001 - FY 2003, when bureaus were required to address any data reliability issues regarding their performance measures in the Assurance Statements required by the Federal Managers' Financial Integrity Act (FMFIA) and the Federal Financial Management Improvement Act (FFMIA).

## Completeness of Data

**Not Available** The following performance measures did not have any data available for this Report, but will have final numbers presented in the FY 2007 Congressional Justification for Appropriations:

| Bureau | Performance Measure |
|---|---|
| DO | Customer satisfaction with OIA in terms of its accuracy, timeliness, and relevance. |

**Discontinued** The following performance measures were discontinued in FY2006 and will not have data available for this Report:

| Bureau | Performance Measure |
|---|---|
| FinCEN | Number of users accessing BSA data electronically |
| DO | Maintain the annual increase in the number of and significance to the foreign narcotics traffickers of newly designated targets |
| DO | Increase the number of international measures and bodies established internationally to protect the financial system from money-laundering and terrorist financing |
| DO | Maintain turnaround time for license submissions with significantly increased workload requiring internal OFAC review |
| DO | Maintain turnaround time for license submissions with significantly increased workload requiring internal Chief Counsel and interagency review |
| Franchise Fund | Customer satisfaction approval rating – Financial Management Administrative Support Services |
| Franchise Fund | Customer satisfaction approval rating – Financial System, Consulting and Training |
| Franchise Fund | Customer satisfaction approval rating – Consolidated/Integrated Administrative Management |

**Baseline** The following measures established baseline values and targets in FY 2006.

| Bureau | Performance Measure |
|---|---|
| FinCEN | Percentage of customers satisfied with the BSA Direct E-filing component |
| OCC | Total OCC costs relative to every $100,000 in bank assets regulated |
| OTS | Total OTS costs relative to every $100,000 in savings association assets regulated |
| TTB | Unit cost to process in excise tax return based on new legislation |
| IRS | BSM Project Cost Variance by Release/subrelease - % project meeting +/- 1-% cost variance |

*(table continued next page)*

*(Baseline table continued from previous page)*

| Bureau | Performance Measure |
|---|---|
| IRS | BSM Project Schedule Variance by Release/sub-release - % project meeting +/- 1-% schedule variance |
| IRS | Field Collection Embedded Quality |
| IRS | Field Exam Embedded Quality |
| IRS | Office Exam Embedded Quality |

**Data Reliability** Performance data presented in this report meets the standards for reliability set forth in OMB Circular A-11, Section 230-5(f). There is neither a refusal nor a marked reluctance by agency managers or Government decision makers to use the data in carrying out their responsibilities.

# Appendix C: Improper Payments Information Act



The Improper Payments Information Act of 2002 (IPIA) requires agencies to annually review their programs and activities to identify those that are susceptible to significant erroneous payments. "Significant" means that an estimated error rate and a dollar amount exceed the threshold of 2.5% and $10 million of total program funding. IPIA also requires the agency to implement a corrective action plan that includes improper payment reduction and recovery targets.

Some Federal programs are so complex that developing an annual error rate is not feasible. The government-wide Chief Financial Officers Council developed an alternative for such programs to assist them in meeting the IPIA requirements. Agencies may establish an annual estimate for a high-risk component of a complex program (e.g., a specific program population) with Office of Management and Budget (OMB) approval. Agencies must also perform trend analyses to update the program's baseline error rate in the interim years between detailed program studies. When development of a statistically valid error rate is possible, the reduction targets are revised and become the basis for future trend analyses.

## I. Description of the Department's risk assessment(s) performed subsequent to compiling its full program inventory and risk-susceptible programs.

Each year, a comprehensive inventory of the funding sources for all programs and activities is developed and distributed to the Department's bureaus and offices. If program or activity funding is at least $10 million, Risk Assessments are required at the payment type level (e.g., payroll, contracts, vendors, travel, etc.). For those payment types resulting in high risk assessments that comprise at least 2.5% and $10 million of a total funding source, (1) statistical sampling must be performed to determine the actual improper payment rate, and (2) a Corrective Action Plan must be developed and submitted to the Department and OMB for approval.

Responses to the Risk Assessments produce a score that falls into pre-determined categories of risk. The following table describes the actions required to be taken at each risk level:

| Risk Level | Required Action(s) |
|---|---|
| High Risk > 2.5% Error Rate & > $10 Million | Corrective Action Plan |
| Medium Risk | Review Payment Controls for Improvement |
| Low Risk | No Further Action Required |

The Risk Assessments performed across Department in FY 2006 resulted in all programs and activities as low and medium risk susceptibility for improper payments. The Earned Income Tax Credit (EITC) high-risk status is well-documented, having been previously identified in the former Section 57 of OMB Circular A-11, and has been deemed a complex program for the purposes of the Improper Payments Information Act.

**II. Describe the statistical sampling process conducted to estimate the improper payment rate for each program identified.**

### Earned Income Tax Credit

The Earned Income Tax Credit (EITC) is a refundable federal tax credit that offsets income taxes owed by low income workers and, if the credit exceeds the amount of taxes owed, provides a lump-sum payment to those who qualify.

Discussions between the Department, the IRS and OMB did not result in identification of a viable error rate measurement, however, IRS plans to conduct an annual EITC compliance study, as a component of the multi-year National Research Program (NRP). Meanwhile, progress is being made on the action items included in the Corrective Action Plan.

The rest of this section explains how the IRS currently develops its erroneous payment projections. The most recent projection is based on a Tax Year 2001 reporting compliance study that estimated the level of improper over claims for FY 2006 to range between $9.8 - $11.6 billion and 23% (lower bound) to 28% (upper bound) of approximately $42.1 billion in total program payments.

### National Research Program (NRP) Analysis

The complexity of EITC's program, the nature of tax processing, and the expense of compliance studies preclude statistical sampling on an annual basis in order to develop error rates for comparison to reduction targets.

Under the TY 2001 NRP reporting compliance study, individual income tax returns filed during calendar year 2002 for TY 2001 were randomly selected for examination.[1] This selection method allows the measures for the entire NRP individual income tax return population to be estimated from the results of the NRP program sample returns. Because one of the objectives of the NRP is to provide data for compliance measurement, NRP procedures and data collection differed from those followed in standard examination programs. NRP classification and examination procedures were more comprehensive in scope and depth than those for standard examination programs. These expanded procedures were designed to provide a very accurate determination of what taxpayers should have reported on their returns.

Estimates of various compliance measures for individual income taxpayers can be calculated by comparing the NRP sample case results—the estimate of what taxpayers should have reported on their returns—to what these taxpayers voluntarily reported on their returns and then projecting the sample results to the population. The projection to the population is done using weights assigned to each return. These weights reflect the number of returns in the population that the sample return represents.

The TY 2001 NRP individual income tax return study covered filers of individual income tax returns. About 6,400 of the approximately 44,400 returns in the regular NRP sample were EITC claimants. About 1,600 other returns (the "calibration sample") were included in the TY 2001 NRP Individual Income Tax Study. These

1 The NRP used a stratified, random sample design. Returns are grouped into predefined categories or "strata" and selected randomly within each stratum.

returns went through a somewhat different examination process and they were not used for these calculations. The NRP study results for this EITC claimant subset of NRP returns were the primary source of data for the improper payments estimates. Other data and information sources used for the estimates included IRS Enforcement Revenue Information System (ERIS) data (which tracks assessments and collections from IRS enforcement-related activities), Treasury Department estimates of the effect of the EITC provisions in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) on EITC erroneous claims, and Treasury Department FY 2006 EITC budget estimates.

The general approach for developing the FY 2006 set of EITC improper payments estimates involved the following steps: (1) estimating an improper payment rate for TY 2001 using the NRP data, (2) adjusting the TY 2001 rate to reflect the estimated impact of the EITC-related EGTRRA provisions, (3) estimating EITC claims for FY 2002- FY 2007 by projecting TY 2001 claims forward using the growth rates implicit in Treasury Department budget outlay estimates, and (4) multiplying the adjusted improper payment rate by the estimated claims to calculate estimated improper payments for each fiscal year.

**III. Describe the Corrective Action Plans for reducing the estimated rate of improper payments for the EITC program.**

The IRS uses a two-pronged approach to reduce erroneous EITC payments:

1. Continually seek opportunities to increase program efficiency within existing resources – in other words, make the base program better; and
2. Test potential business process enhancements to reduce error and then request implementation funding if the tests prove successful.

### Base Program

In 2006, the IRS will spend approximately $167 million to prevent more than $2 billion from being paid in error. Three areas of activity compose the bulk of this spending:

- **Examinations** – the IRS identifies tax returns for examination and holds the EITC portion of the refund until an audit can be conducted. This is the *only* IRS audit program where exams are conducted *before* a refund is released. The audit closures and enforcement revenue protected in the charts below do not include test initiatives.
- **Math Error** – this refers to an automated process in which IRS identifies math or other statistical irregularities and automatically prepares an adjusted return for a taxpayer. Congressional approval is required for math error use.
- **Document Matching** – involves comparing income information provided by the taxpayer with matching information (e.g. W-2s, 1099s) from employers to identify discrepancies.

The chart below shows significant results from FY 2002 through FY 2005. In FY2005 alone, the IRS issued 659,333 math error notices, conducted 521,872 audits and closed 324,419 document matching reviews.

| Compliance Activities (thousands) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **FY02** | **FY03** | **FY04** | **FY05** | **FY06**** | **FY07*** | **FY08*** | **FY02-FY08* Total** |
| Audit Closures | 373,508 | 422,033 | 449,435 | 521,872 | 516,181 | 489,940 | 502,768 | 3,275,737 |
| Math Error Notices** | 993,387 | 922,465 | 817,440 | 659,333 | 617,430 | 586,559 | 557,231 | 5,153,845 |
| Document Matching | | | 300,000 | 324,419 | 364,020 | 300,000 | 300,000 | 1,588,439 |

**Original estimates based on FY 04.*
***TY data. FY 2006 is estimate*

These activities had a significant effect. We project that continued enforcement efforts will protect a total of $13.22 billion in revenue through FY 2008.

| Enforcement Revenue Protected ($ billions) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **FY02** | **FY03** | **FY04** | **FY05** | **FY06**** | **FY07*** | **FY08** | **FY02-FY08 Total** |
| Examination | 0.95 | 1.00 | 1.10 | 1.34 | 1.48 | 1.48 | 1.55 | 8.90 |
| Math Error Notices** | 0.42 | 0.34 | 0.42 | 0.29 | 0.27 | 0.25 | 0.24 | 2.23 |
| Document Matching | | | 0.31 | 0.53 | 0.60 | 0.32 | 0.33 | 2.09 |
| TOTAL | 1.37 | 1.34 | 1.83 | 2.16 | 2.35 | 2.05 | 2.12 | 13.22 |

**Original estimates based on FY 04.*
***TY data. FY 2006 is estimate*

## Business Process Enhancements

In 2003 and 2004, the IRS received a total of $75 million to fund a number of EITC business process improvement initiatives. These initiatives, referred to as the “Investment Portfolio”, included the use of private sector solutions to better identify egregious cases, apply appropriate collection methods, assign and manage case inventory more efficiently, catch problems with amended returns, improve communications with taxpayers, better focus on under-reported income and explore use of new notices to improve taxpayer response. The entire initiative process was managed using a project management governance structure known as the Enterprise Life Cycle – which, among other requirements – includes a business case analysis to justify investment choices. It was conceived of, designed and implemented in three separate releases over a three year period. Here are the estimated benefits of the EITC investment portfolio. These estimates represent the low end of the range of estimates of revenue protected from the EITC investment portfolio:

| Enforcement Revenue Protected ($ billions) | | | | | |
|---|---|---|---|---|---|
| | FY05 | FY06 | FY07 | FY08 | FY02-FY08 Total |
| Investment Portfolio | 0.01 | 0.08 | 0.08 | 0.08 | 0.25 |

### Testing New Business Processes

In addition to building new solutions for existing business processes, the IRS is developing options for certain EITC taxpayers to certify they meet a key eligibility requirement before receiving the credit. This analysis is scheduled to be completed by FY 2007. This process could potentially affect a significant portion of EITC taxpayers and is the subject of careful evaluation. If the IRS concludes the process should be implemented, it will request additional funding to expand the scope of its existing EITC activities.

Finally, the IRS has a number of other activities it is using to combat program error. This past year saw the second year of a study to address egregious EITC return preparers. In addition, the IRS is partnering with two states to share information to prevent erroneous payments. The IRS is also developing possible new candidates for math error authority and has developed new strategies to prevent duplicate claims of qualifying children. The IRS has developed an annual enterprise research strategy in partnership with internal and external organizations to better focus EITC compliance and outreach activities. The research strategy includes a multi-dimensional database that tracks behavioral patterns of EITC claimants and qualifying children over a period of years.

### IV. EITC Improper Payment Reduction Outlook

The reduction outlook for EITC improper payments is as follows:

| Improper Payment Reduction Outlook ($ in millions) | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Program | PY Outlays | PY % | PY $ | CY Outlays | CY IP% | CY IP$ | CY+1 Est Outlays | CY+1 1P% | CY+1 1P$ | CY+2 Est Outlays | CY+2 IP% | CY+2 IP$ | CY+3 Est Outlays | CY+3 IP% | CY+3 IP$ |
| EITC Upper Bound Estimate | $41.3 | 28% | $11.4 | $42.1 | 28% | $11.6 | $42.7 | 28% | $11.8 | $42.7 | 28% | $11.8 | $42.7 | 28% | $11.8 |
| EITC Lower Bound Estimate | $41.3 | 23% | $9.6 | $42.1 | 23% | $9.8 | $42.7 | 23% | $10.0 | $42.7 | 23% | $10.0 | $42.7 | 23% | $10.0 |

*Outlays: Following prior methodology, the amount shown is the total EITC claimed.*
*IP % and IP $: These estimates follow the prior approach which provided a range for improper payments.*

Note: The *Improper Payment Percentage* and *Estimated Outlay* columns reflect a constant error rate pending the development of an annual error rate measurement.

## Recovery Act

### V. The Department's Recovery Auditing Program

Section 831 of the Defense Authorization Act for Fiscal Year 2002 added a new subchapter to the U.S. Code (31 U.S.C 3561-3567) that requires agencies that enter into contracts with a total value in excess of $500,000,000 in a fiscal year carry out a cost-effective program for identifying errors made in paying contractors and for recovering amounts erroneously paid to the contractors. A required element of such a program is the use of recovery audits and recovery activities. In accordance with Office of Management and Budget (OMB) Circular A-123, Management's Responsibility for internal Controls, Appendix C, reporting on recovery auditing is required annually.

In FY 2006, the Department issued contracts totaling $4.6 billion. The annual Improper Payments Information Act Risk Assessment process includes a review of pre-payment controls that minimize the likelihood and occurrence of improper payments. For Recovery Act compliance, Treasury requires each bureau and office to review their post-payment controls and report on recovery auditing activities, contracts issued, improper payments made, and recoveries achieved. Bureaus and offices may use recovery auditing firms to perform many of the steps in their recovery program and identify candidates for recovery action.

The Department considers both pre-payment and post-payment reviews to identify payment errors a good management practice that should be included among basic payment controls. All of the Department's bureaus use some form of recovery auditing techniques to identify improper payments during post-payment reviews. At times, bureaus may use the services of recovery auditors to help them identify payment anomalies and target areas for improvement. The Department has extensive contract payment controls that are applied at the time each payment is processed making recovery activity minimal. Our ongoing reviews of contract payment controls do not exclude any type of contract actions. Further, the low level of improper payments in 2006 did not require any Treasury bureau to develop a management improvement program under Recovery Act guidance. However, if during the course of the recovery auditing activity errors are identified, reviews are conducted for further action. If the errors are significant, Corrective Action Plans are developed.

| Agency | Amount Subject to Review for CY Reporting | Actual Amount Reviewed and Reported | Amounts Identified for Recovery | Amounts Recovered CY | Amounts Recovered PY |
|---|---|---|---|---|---|
| Treasury | $4,622,300,599 | $4,216,057,584 | $2,305,424 | $1,442,708 | $515 |

### VI. Management Accountability

The Secretary of the Treasury has delegated responsibility for improper payments to the Assistant Secretary for Management/Chief Financial Officer (ASM/CFO). Improper payments falls under the Department's management control program. A component of the management control program is risk assessments, which are an extension of each bureau's annual improper payment review process. Through Treasury Directive 40-04, executives and other managers are required to have management control responsibilities as part of their annual performance plans. With oversight mechanisms such as the Treasury CFO Council and IRS' Financial and Management Control Executive Steering Committee, managerial responsibility and accountability in all management control areas are visible and well documented.

Improper payments are a separate initiative under the President's Management Agenda and have been monitored for improvement as a material weakness under the Federal Managers' Financial Integrity Act. Managers who are responsible and accountable for reducing the level of EITC over claims have been identified, while other senior and mid-level officials have responsibility for monitoring progress in this area as bureau and program internal control officers.

**VII. Resources Requested in the FY 2006 Budget Submission to Congress**

Several new initiatives were requested in the IRS FY 2006 President's Budget submission which relate to the enforcement of tax laws. However, the only initiative approved in the President's Budget, *Increase Individual Taxpayer Compliance*, addressed reducing the tax gap and Non-EITC audit coverage.

**VIII. Limiting Statutory and Regulatory Barriers**

A number of factors serve as barriers to reducing overclaims in the EITC program. These include:

- The complexity of the tax law
- The structure of the earned income credit
- Confusion among eligible claimants
- High program turnover
- Unscrupulous preparers
- Fraud

No one of these factors can be considered the primary driver of program error. Furthermore, the interaction among the factors makes addressing the credit's erroneous claims rate, while balancing the need to ensure the credit makes its way to taxpayers who are eligible, extremely difficult.

**IX. Other Factors**

Since June 2003, EITC has focused on reducing erroneous over claims by implementing a five-point initiative that serves to:

- Reduce the backlog of pending EITC examinations to ensure that eligible taxpayers whose returns are being examined receive their refunds quickly.
- Minimize the burden and enhance the quality of communications with taxpayers by improving the existing audit process.
- Encourage eligible taxpayers to claim the EITC by increasing outreach efforts and making the requirements for claiming the credit easier to understand.
- Ensure fairness by refocusing compliance efforts on taxpayers who claimed the credit but were ineligible because their income was too high.
- Pilot a certification effort to substantiate qualifying child residency eligibility for claimants whose returns are associated with a high risk for error.

As part of this initiative, in FY 2005, the IRS completed the following tests designed to evaluate new ways of reducing erroneous EITC payments while maintaining participation by eligible taxpayers:

- Qualifying Child Test: Required EITC claimants to certify that they met qualifying child residency requirement before paying out the refund;
- Filing Status Test: Reviewed filing status claims to ensure they were correct. IRS selected claimants whose filing status had changed to one that increased the value of the credit (generally, from married filing joint to head of household);
- Misreporting Income (Automated Underreporter) Test: Enhanced error detection through the automated underreporter program. This test focused not on the number of cases IRS reviewed, but on improved selection methodologies.

In FY 2006, IRS initiated the final year of the Qualifying Child test focusing on improved selection methodology. Preliminary data from this test indicates both a compliance and deterrence impact.

Carefully analyzing the final results of these tests will be imperative to assessing their effectiveness in reducing erroneous EITC over claims while maintaining high participation rates by eligible taxpayers.

# Appendix D: Management Challenges and Responses

Each year, the Inspectors General issue Semiannual Reports to Congress that include specific management challenges facing the Department. These challenges are sent to the Secretary at the end of each fiscal year and cite the challenges for the upcoming fiscal year.

The letters sent to the Secretary and the Secretary's responses are reflected on the following pages for each respective Inspector General.

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

October 16, 2006

MEMORANDUM FOR SECRETARY PAULSON

FROM: Harold Damelin
Inspector General

SUBJECT: Management and Performance Challenges Facing the Department of the Treasury (OIG-CA-07-002)

The Reports Consolidation Act of 2000 requires that we provide you with our perspective on the most serious management and performance challenges facing the Department of the Treasury, for inclusion in the Department's annual performance and accountability report.

Last year we identified five challenges that we believe seriously impeded the Department's ability to conduct its program responsibilities and ensure the integrity of its operations. These challenges are: (1) Corporate Management, (2) Management of Capital Investments, (3) Information Security, (4) Linking Resources to Results, and (5) Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement. While some progress on each of these five challenges has been made, they continue to represent significant risks to the Department. Listed below is a detailed discussion of each challenge.

**Challenge 1 – Corporate Management**

This is an overarching management challenge. Treasury needs to provide effective corporate leadership in order to resolve serious bureau and program office deficiencies that adversely impact the performance of Treasury as a whole. In particular, Treasury needs to assert strong leadership and supervision over the Internal Revenue Service (IRS) to resolve the longstanding material weaknesses and system deficiencies that hamper the timely and reliable information necessary to effectively manage IRS operations. In addition, while progress has been made, the Department has not fully implemented a corporate-level control structure to ensure that capital investments are properly managed, information about government operations and citizens is adequately secured, and financial resources used by Treasury can be linked to its operational results. These matters are discussed in more detail in the following challenges.

The increasing emphasis on agency-wide accountability envisioned in the management reform legislation of the past decade and the President's Management Agenda, has underscored the need for effective corporate management at Treasury. With nine bureaus and many program offices, Treasury is a highly decentralized organization. As such, Treasury management should ensure consistency, cohesiveness, and economy among all bureaus and program offices in achieving Treasury's goals and objectives. Inherent in this is the need for clear lines of accountability between corporate, bureau, and program office management; enterprise solutions for core business activities; consistent application of accounting principles; and effective oversight of capital investments and information security.

This past year, the Department's senior leadership has asserted more direct and substantive involvement in developing and implementing Treasury-wide polices and initiatives across a number of fronts. For example, Treasury established, for the first time, a substantially complete systems inventory. This is a critical step to ensuring security over its information technology assets. Also, the Deputy Secretary recently issued a memorandum requiring that internal control programs (programs to ensure accountability and promote effective management and stewardship) be included in all fiscal year 2007 senior leadership performance plans. In the future, this type of direct involvement by senior leadership needs to be maintained so that progress continues.

**Challenge 2 – Management of Capital Investments**

Treasury needs to better manage large acquisitions of mission-critical systems and other capital investments. In the past, we discussed serious problems related to the Treasury Communications Enterprise (TCE) procurement, Treasury's HR Connect system, and the Treasury and Annex Repair and Restoration (TBARR) project.

This year, we note continuing issues with TCE and new problems have been brought to light with BSA Direct, and the web-based Electronic Fraud Detection System (Web EFDS). Specifically, we found that the TCE procurement, estimated to cost $1 billion over its useful life, was poorly planned, executed, and documented. For example, Treasury's consideration of General Services Administration contract vehicles, both at the outset and following a successful TCE bid protest, was incomplete, and the TCE business case documentation was deficient. Treasury amended and reopened the TCE solicitation in October 2005, but has yet to award the TCE contract. In July 2006, after nearly 2 years in development and $15 million spent, the Financial Crimes Enforcement Network (FinCEN) terminated its contract for the storage and retrieval component of BSA Direct after significant concerns were raised about schedule delays and project management. IRS had similar problems with Web EFDS, a system costing more than $20 million intended to prevent fraudulent refunds. In April 2006, after a significant delay, IRS stopped all development activities for Web EFDS. IRS also was unable to use EFDS to prevent fraudulent refunds during processing year 2006. The Treasury Inspector General for Tax Administration reported that without Web EFDS, more than $300 million in fraudulent refunds may have been allowed.

The Deputy Secretary recently emphasized the need to better manage information technology capital investments to the heads of Treasury bureaus, noting that this is a responsibility of all senior management and not just that of the Chief Information Officer. Involvement and accountability at the top is a critical factor to ensure the successful implementation of systems.

**Challenge 3 – Information Security**

Despite some notable accomplishments, the Department needs to improve its information security program and practices to achieve compliance with the Federal Information Security Management Act of 2002 (FISMA) and Office of Management and Budget (OMB) requirements. In the past, we reported that Treasury's systems inventory was not accurate, complete, or consistently reported. During the past year, the Department overcame this weakness in its security program by providing direction to the bureaus in developing a Department-wide inventory of information systems. Although the Department still needs to implement additional actions to further improve the system inventory, we believe the inventory is substantially complete and generally conforms to applicable requirements.

Nevertheless, our 2006 FISMA evaluation disclosed deficiencies that, in the aggregate, constitute substantial noncompliance with FISMA. Specifically, we noted that improvements are needed in the areas of: certification and accreditation, security awareness, training employees with significant security responsibilities, tracking corrective actions, identifying and documenting system interfaces, security self-assessments, configuration management, and incident response. As a result of the improved inventory, Treasury identified that it has national security systems that are not part of its intelligence program. For the first time, we evaluated the information security program and practices as it relates to these non-intelligence national security systems. We noted that significant improvements are also needed in this area.

During 2006, OMB issued Memorandum 06-16, Protection of Sensitive Agency Information (M-06-16), requiring agencies to perform specific actions to protect certain personally identifiable information. Our evaluation of Treasury's compliance with M-06-16 disclosed that Treasury still faces significant challenges to meet these requirements. Specifically, we noted that the Department needs to ensure that security controls pertaining to personally identifiable information are addressed Treasury-wide in the following areas: assessing risk, reviewing and revising policies, transporting, offsite storage, and remote access. In a July 2006 memorandum to Treasury bureaus, the Department provided implementation guidance and required bureaus to identify their specific actions taken and planned, including dates, to address weaknesses in security controls pertaining to personally identifiable information.

**Challenge 4 – Linking Resources to Results**

Because the Department has not fully developed and incorporated managerial cost accounting (MCA) into its business activities, the Department cannot adequately link financial resources to operating results. This inhibits comprehensive program performance reporting and meaningful cost benefit analyses of the Department's programs and operations. MCA involves the accumulation and analysis of financial and non-financial data, resulting in the allocation of costs to organizational pursuits such as performance goals, programs, activities, and outputs, and should be a fundamental part of a financial/performance management system.

The Government Accountability Office (GAO) reported in December 2005 that Treasury delegated to its bureaus responsibility to implement MCA systems and processes to meet federal standards. Although Treasury retained oversight responsibility to ensure consistent implementation of MCA department-wide, Treasury officials had no specific procedures in place to ensure that consistent, periodic department-level oversight was conducted, and they promoted MCA and monitored MCA implementation on an informal and sporadic basis. This contributed to widely disparate implementation and use of MCA among Treasury's program offices and bureaus. GAO also found that controls to ensure the reliability of MCA data needed improvement in two of the three Treasury bureaus it reviewed.

Since GAO's review, the Department has developed a high-level MCA implementation plan. This plan focuses on (1) clarifying and reaffirming the Department's MCA policy for all bureaus; (2) identifying MCA needs across the Department; (3) ensuring MCA needs are linked to the Department's strategic plan, budget, and performance measures; (4) identifying gaps between Department and bureau needs and existing MCA capabilities; and (5) developing plans to eliminate these gaps. However, none of the specific action items in the plan have been completed and target dates for certain actions have been missed.

**Challenge 5 – Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement**

Treasury faces unique challenges in carrying out its responsibilities under the Bank Secrecy Act (BSA) and USA Patriot Act to prevent and detect money laundering and terrorist financing. To effectively prevent and detect financial crimes and terrorist financing it is necessary to have: (1) strong control environments at financial institutions that ensure that business is conducted with reputable parties, and large currency transactions and suspicious activities are properly and timely reported to Treasury, (2) strong federal and state regulatory agencies that examine and enforce BSA and USA Patriot Act requirements at financial institutions, and (3) strong analytical capacity to identify and refer to law enforcement leads provided through reports filed by financial institutions.

While FinCEN is the Treasury bureau responsible for administering BSA, it relies on other Treasury and non-Treasury agencies to enforce compliance with the Act's requirements. The Office of Foreign Assets Control (OFAC), the Treasury office responsible for administering U.S. foreign sanction programs, also relies on other Treasury and non-Treasury agencies to ensure compliance with OFAC requirements. Past audits and Congressional hearings, however, have surfaced serious regulatory gaps in the detection of and/or timely enforcement action against financial institutions for BSA and related violations. For example, a recent audit found that the Office of the Comptroller of the Currency (OCC) took a questionable (non-public) enforcement action when it found serious recurring BSA program deficiencies at the nation's fifth largest bank. Another recent audit found that FinCEN was slow in developing possible new leads for law enforcement through analysis of BSA data, devoting most of its analytical work to processing routine data requests. Another recent audit found that OCC and Office of Thrift Supervision (OTS) examinations of financial institutions for OFAC compliance were not documented well enough to determine whether the examined institutions were in compliance.

In an attempt to improve compliance and address some of these gaps, Treasury created the Office of Terrorism and Financial Intelligence (TFI) through which FinCEN and OFAC now report. In addition, FinCEN, beginning in 2004, (1) created a compliance office to improve BSA oversight and coordination with financial institution regulators; and (2) entered into memoranda of understanding (MOUs) with the federal banking regulators, IRS, and most states to enhance communication and coordination. Furthermore, OCC and OTS took immediate steps to improve their respective documentation of OFAC examinations. Additionally, OFAC also executed MOUs with the federal banking regulators that provides for increased information sharing. While similar to the MOUs between FinCEN and the regulators, legislative impairments may ultimately limit the information shared with OFAC. For this reason and others, the effectiveness of these actions to address regulatory gaps and ultimately improve compliance is yet to be determined.

Given the criticality of this management challenge to the Department's mission, we will continue to devote a significant portion of our audit resources on TFI, FinCEN, OFAC, OCC, and OTS programs and operations. For example, we are planning comprehensive reviews of the effectiveness of (1) FinCEN's Office of Compliance, and (2) the MOUs that have been established.

We would be pleased to discuss our views on these management and performance challenges in more detail.

cc: Robert M. Kimmitt
Deputy Secretary

Sandra L. Pack
Assistant Secretary for Management and Chief Financial Officer

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

November 13, 2006

**MEMORANDUM FOR HAROLD DAMELIN**
**INSPECTOR GENERAL**

**FROM:** Henry M. Paulson, Jr.

**SUBJECT:** Response to Management and Performance Challenges Facing the Department of the Treasury

I am responding to your October 16, 2006 memorandum describing the Treasury Department's management and performance challenges.

This memorandum provides information on the actions that we completed in FY 2006 and those actions we plan to take during FY 2007 to address these five challenges.

**Challenge 1 - Corporate Management**

The Treasury Department is committed to strong corporate leadership through sound oversight and policy direction for all its components, and we have taken actions to strengthen Department-wide collaboration and unity. For example, the Department established Treasury-wide councils of Chief Financial Officers, Human Capital Directors, Chief Information Officers, and Senior Procurement Officials. These councils are chaired by senior Department officials, who meet monthly to address issues of mutual concern and to clarify Department guidance on key policies. In addition, in FY 2006, the Treasury Department reinstituted the monthly bureau heads meetings to provide a forum for policy discussions and guidance at the Department level.

In FY 2006, the Department established an Executive Planning Board (EPB) to provide a corporate review and assessment of on-going bureau core business activities and multi-year funding requests. Through this board, Department-wide issues and challenges, and solutions for leveraging resources are identified. In addition, the Treasury Department embarked on a revision of its strategic plan. When finalized, this new plan will use an integrated management system, based on the principles of continuous improvement, to achieve strategic goals, objectives and outcomes for a highly decentralized organization.

In FY 2007 we will implement corporate strategies to review major information technology (IT) investments on a quarterly basis and to leverage Treasury's buying power by promoting corporate strategic sourcing.

**Challenge 2 - Management of Capital Investments**

In FY 2006, the Treasury Department continued to strengthen its information technology (IT) management and governance. The EPB, the Treasury CIO Council, and the Treasury Technical Investment Review Board (TIRB) provided executive oversight for the Department's planning and management of information and IT resources. The Department enhanced IT capital planning policy and improved Department oversight during FY 2006. Working in consultation with the Inspector General's (IG) office, we addressed IG findings related to the Treasury Communications Enterprise (TCE) audit. The Department worked with IG staff to strengthen TCE planning and business case documentation, completing all required corrective actions to close the audit in August 2006. The Department now applies this standardized business case model to other large investments. The reporting of IT investment management improved through the mapping of major IT systems to IT portfolio investments. Additional improvements occurred by implementing a more rigorous baseline change process and requiring bureau validation of project manager qualifications for major IT investments.

In addition, the Treasury Department now requires that IT investments be placed on an internal Treasury watchlist if they do not meet defined performance and compliance criteria. Investments on the watchlist are subject to greater oversight, including review by the Assistant Secretary for Management/Chief Financial Officer and bureau heads.

In FY 2007, the Treasury Department will continue its certification program of bureau Chief Information Officers and program managers to ensure that earned value management data they provide on IT investments are accurate and timely. Furthermore, the Department established a program to review bureau IT governance structures, capital planning processes, and select investments. This program was piloted at one bureau during this reporting period and reviews will be conducted for all bureaus throughout FY 2007.

**Challenge 3 - Information Security**

In FY 2006, the Treasury Department made progress in bringing its systems into compliance with federal IT security policies, standards, and guidelines. A significant milestone was achieved when the IG agreed with the Department's FY 2006 Federal Information Security Management Act (FISMA) evaluation of its systems inventory. In addition, the IG generally agreed with the Department's first national security (non-intelligence) system inventory.

The Treasury Department continued to improve FISMA compliance by addressing certification and accreditation, contingency planning, and training for individuals with specialized security responsibilities. Furthermore, the Department enhanced its Treasury-wide systems inventory and improved the integrity of the process by addressing all cyber security weaknesses identified through the IG and Government Accountability Office audits and incident reports, resulting in improved performance in the 2006 FISMA evaluation.

For FY 2007, the Treasury Department will further refine its non-national security systems inventory for completeness and consistency, issue new Treasury policy to incorporate new Office of Management and Budget and National Institute of Standards and Technology requirements, and monitor implementation of existing cyber security policy and guidance. For non-intelligence national security systems, the Department will initiate updates to associated security policy and develop an oversight program for the non-intelligence national security systems program. The Treasury Department plans on strengthening its evaluation methodology for review of contingency plans, security testing, certification and accreditation.

**Challenge 4 - Linking Resources to Results**

As noted in your memorandum, the Treasury Department has developed a formal plan to address Department-wide implementation of cost accounting practices. This plan, developed at the end of June 2006, contained six steps to include "best practices" across the federal government, the integration of cost accounting with other ongoing financial reporting initiatives, the identification of gaps between cost accounting needs and practices, and the development of methods to bridge those gaps. We had planned to complete all actions by September 30, 2006 however, due to competing priorities we could only partially address these steps in FY 2006. We have re-scheduled these steps to begin after our FY 2006 year-end reporting requirements are met.

In addition, the Treasury Department took actions to link financial resources to operating results by exploring Extensible Business Reporting Language and several business intelligence products. We will continue our consideration of these tools during FY 2007. The Treasury Department also participated in the Association of Government Accountants' process based accounting advisory group, which is focused on linking costs to outcomes in financial reporting. The goal is to link budget and cost to outcomes, enabling the Treasury Department to measure the value it produces for the American people.

In an effort to align resources to strategic priorities, as discussed earlier, the Department embarked on a revision of its strategic plan in FY 2006. The new strategic plan will establish shared objectives by identifying activities that cross organizational boundaries in the achievement of the Department's strategic goals, effectively aligning operational and policy activities to desired corporate outcomes. In FY 2007, the Department will examine how to allocate effectively full costs of program activities to Treasury-level outcomes.

**Challenge 5 -Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement**

The Treasury Department faces unique challenges in carrying out its responsibilities, under the Bank Secrecy Act (BSA) and USA PATRIOT Act (USPA), to prevent and detect money laundering and terrorist financing. The Department has several ongoing efforts to address the IG management challenges.

To address the need for stronger controls and improve the quality of reported information, federal banking agencies released updated supervisory guidance for financial institutions to conduct compliance examinations in FY 2006. FinCEN continued to process and communicate enforcement actions in accordance with Departmental timelines and identify opportunities to reduce the time required to process these actions.

The Treasury Department acknowledges the need for strong federal and state regulatory agencies that enforce BSA and USPA requirements at financial institutions. In FY 2006, FinCEN surpassed its performance goal in establishing information sharing agreements or memoranda of understanding (MOUs) with federal and state regulatory agencies. These agreements help provide FinCEN access to the data necessary to monitor industry compliance. The Office of the Comptroller of the Currency (OCC), in its role as a regulator, created a national pool of BSA examiners and completed examinations for all large banks and for 100 percent of high-risk banks. In addition, the OCC brought enforcement actions against several banks for inadequate compliance programs, which ranged from issuing a cease-and desist order to imposition of civil money penalties. These actions also ordered financial institutions to develop and implement internal controls, conduct audits, designate BSA compliance officers, and conduct employee training programs.

In FY 2007, FinCEN will continue to improve regulatory compliance efforts, facilitate timely analysis of BSA records, enhance its analytical products, and improve threat assessment capabilities. Finally, FinCEN will improve the expertise and capabilities of personnel in anti-money laundering and anti-terrorist financing areas through training and expanded partnerships with customers.

We look forward to continue working with you to address these challenges.

cc: The Deputy Secretary
Assistant Secretary for Management and Chief Financial Officer

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

October 2, 2006

MEMORANDUM FOR SECRETARY PAULSON

FROM: J. Russell George
Inspector General

SUBJECT: Management and Performance Challenges Facing the Internal Revenue Service for Fiscal Year 2007

The Reports Consolidation Act of 20001 requires that the Treasury Inspector General for Tax Administration (TIGTA) summarize, for inclusion in the *Department of the Treasury Accountability Report for Fiscal Year 2006*, its perspective of the most serious management and performance challenges currently confronting the Internal Revenue Service (IRS).

TIGTA's assessment of the major IRS management challenge areas for Fiscal Year (FY) 2007 has not changed substantially from the prior year. While the IRS has continued to address each challenge area, TIGTA was unable to remove any challenge area at this time. This year, TIGTA has divided the category of Tax Compliance Initiatives into two subcategories – Business and Individual and Tax-Exempt Entities. TIGTA believes that these subcategories better define the need to administer tax regulations and collect tax dollars for businesses and individuals and to oversee compliance issues for tax-exempt entities. Both play a crucial role in the IRS' compliance efforts.

The 10 current challenges, in order of priority, are:

### *Modernization of the Internal Revenue Service*

The Business Systems Modernization (BSM) program is a complex effort to modernize the IRS' technology and related business processes. According to the IRS, this effort will involve integrating thousands of hardware and software components. All of this must be done while replacing outdated technology and maintaining the current tax system. The BSM program is in its eighth year and has received approximately

$2.1 billion for contractor services. This past year, the IRS began taking actions to restructure and redesign significant areas within the BSM program. For example, the IRS took over the role of systems integrator from the PRIME contractor2 and changed its approach from completely replacing current business systems to using current business systems to accomplish modernization.

While the IRS and its contractors have completed modernization projects that provide significant benefits to taxpayers, since FY 2002, TIGTA's annual assessments of the BSM program have cited four specific challenges the IRS needs to overcome to deliver a successful modernization effort: 1)

1 31 U.S.C. § 3516(d) (2000).
2 The PRIME contractor is the Computer Sciences Corporation, which heads an alliance of leading technology companies brought together to assist with the IRS' efforts to modernize its computer systems and related information technology.

implement planned improvements in key management processes and commit necessary resources to enable success;

2) manage the increasing complexity and risks of the BSM program; 3) maintain the continuity and strategic direction with experienced leadership; and 4) ensure that contractor performance and accountability are effectively managed. TIGTA continues to believe the eventual success of the modernization effort will depend on how well the IRS addresses these four specific challenges.

### *Tax Compliance Initiatives*

Tax compliance initiatives include the need to administer tax regulations and collect the correct amount of tax for businesses and individuals, as well as to oversee tax-exempt and government entities for compliance.

#### Business and Individual

Increasing compliance with the tax code is at the heart of IRS enforcement programs. The IRS is targeting its casework and enforcement activities to deliver better results and to better target those corporations and high-income individual taxpayers who fail to report or pay what they owe. Despite actions the IRS has taken to improve its enforcement efforts, TIGTA continues its designation of tax compliance initiatives as a major management challenge for the IRS. The IRS defines the gross tax gap as the difference between the estimated amount taxpayers owe and the amount they voluntarily and timely pay for a tax year, and estimated the gross tax gap for Tax Year 2001 at $345 billion. TIGTA's evaluation of the reliability of the IRS-developed tax gap figures concluded that the IRS still does not have sufficient information to completely and accurately assess the overall tax gap and voluntary compliance. The IRS has significant challenges in both obtaining complete and timely data, and developing the methods for interpreting the data.

#### Tax-Exempt Entities

The IRS continues to face challenges in administering programs focused on tax-exempt organizations to ensure that they comply with applicable laws and regulations to qualify for tax-exempt status. While the IRS has noted that the nonprofit community has not been immune from the recent trends toward bad corporate practices that have been highlighted in the for-profit area, it has only recently begun to re-emphasize this area since suffering a decline in staffing during the late 1990s. TIGTA has made recommendations for improving the IRS' oversight of filing compliance by political organizations and ensuring abusive tax avoidance transactions in the tax-exempt sector are being identified and addressed. Further, TIGTA recommended additional improvements to assure that timely, accurate, and complete information returns are received for employee benefit plans. TIGTA also noted that the IRS must develop better research tools, improve training to trace funds through complex transactions, and develop the ability to analyze data to determine the high-risk noncompliant areas. The IRS agreed with the TIGTA recommendations and initiated corrective actions to address these concerns.

### *Security of the Internal Revenue Service*

Millions of taxpayers entrust the IRS with sensitive financial and personal data stored and processed by IRS computer systems. Recent reports of identity thefts from both the private and public sectors have heightened awareness of the need to protect this data. The risks that sensitive data or computer systems could be compromised and computer operations could be disrupted continue to increase. These risks are due to internal factors, such as the increased connectivity of the computer systems and the increased use of portable laptop computers, and external factors, such as the volatile threat environment resulting from increased terrorist and hacker activity. The IRS has designated computer security as a material weakness under the Federal Managers' Financial Integrity Act of 1982.[3] Section 301 of the Federal Information Security Management Act (FISMA)[4] requires each Federal agency to report annually to the Office of Management and Budget and Congress on the effectiveness of its security programs and to perform an annual independent evaluation of its information security program and practices. During FY 2006, the IRS developed a corporate approach to FISMA by elevating its FISMA processes and procedures into an enterprise-wide program. Recognizing that it will take time to achieve long-term improvements, the process changes made by the IRS have not yet had a positive effect on some measurements provided in the President's Management Agenda, including certification and accreditation and tracking the resolution of security vulnerabilities. TIGTA's FISMA evaluations and other audits lead to the conclusion that sufficient attention is not yet being given to the security of sensitive systems.

### *Providing Quality Taxpayer Service Operations*

Since the late 1990s, the IRS has increased its delivery of quality customer service to taxpayers. In fact, in its current strategic plan, the IRS' first goal is to improve taxpayer service. There are recent signs, however, that this trend may be reversing as the IRS proposes to allocate more resources to its collection, examination, and criminal investigation functions and fewer resources to taxpayer service functions. Moreover, the IRS' FY 2006 budget request proposed a 1 percent reduction in funding for taxpayer service activities at the same time it proposed an 8 percent increase in funding for enforcement activities.[5] The Senate Committee on Appropriations recently noted that the IRS lacks a concrete plan to provide adequate alternative services to replace the services proposed for reduction or elimination.[6] In response, the IRS developed a five-year Taxpayer Assistance Blueprint that will help it focus on providing the appropriate types and amounts of service. TIGTA continues to identify the need for improvements in taxpayer services provided through toll-free, face-to-face, and electronic methods.

### *Complexity of the Tax Law*

Simplicity, transparency, and ease of administration are interrelated and desirable features of a tax system. Over the years, the Federal tax system, especially the Federal income tax, has become more complex, less transparent, and subject to frequent revision. Tax system complexity and frequent revisions to the Internal Revenue Code make it more difficult and costly for taxpayers who want to comply to do so and for the IRS to explain and enforce the tax laws. Tax law complexity results in higher costs for both tax administration and tax compliance. Simplification and reform have the potential to reduce the tax gap by billions of dollars. Although the IRS has consistently sought to ease the tax compliance process for all taxpayers, tax law complexity remains a problem. The complexities of the tax laws affect the ability of the IRS to administer the nation's tax system. The IRS' efforts to provide assis-

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3 31 U.S.C. §§ 1105, 1113, 3512 (2000).

4 Pub. L. No. 107-347, tit. III, Stat. 2899, 2946 (2002) (codified as amended at 44 U.S.C. §§ 3541-49).

5 *The* Budget in Brief: Internal Revenue Service (Feb. 2005).

6 U.S. Congress. Senate. Senate Report 109-109. *Transportation, Treasury, the Judiciary, Housing And Urban Development, And Related Agencies Appropriations Bill, 2006* 109th Cong.

tance to taxpayers are hampered because of these complexities. Without meaningful simplification, it is likely that the complexities of the current tax code will continue to contribute to the tax gap.

### *Using Performance and Financial Information for Program and Budget Decisions*

While the IRS has made some progress in using performance and financial information for program and budget decisions, this area is still a major challenge. The IRS lacks a comprehensive, integrated system that provides accurate, relevant, and timely financial and operating data describing the performance measures, productivity, and associated costs of IRS programs. During FY 2005, the IRS collected about $2.3 trillion in Federal tax revenue, which constituted approximately 95 percent of all Federal revenue. However, the IRS' Federal tax revenue financial management systems have serious internal control and systems deficiencies, which require the IRS to rely extensively on resource-intensive compensating processes to prepare its financial statements. Due to these serious conditions, the IRS did not, in the Government Accountability Office's opinion, maintain effective internal controls over financial reporting (including safeguarding of assets) or compliance with laws and regulations. Thus, the IRS could not provide reasonable assurance that losses, misstatements, and noncompliance with laws material to the financial statements would be prevented or detected on a timely basis.[7] In addition, the IRS cannot produce timely, accurate, and useful information needed for day-to-day decisions, which inhibits the IRS' ability to address financial management and operational issues to fulfill its responsibilities. TIGTA has continued to report that various IRS management information systems are insufficient to enable IRS management to measure costs, determine if performance goals have been achieved, or monitor progress in achieving program goals.

### *Erroneous and Improper Payments*

An improper payment is any payment that should not have been made or that was made in an incorrect amount under a statutory, contractual, administrative or other legally applicable requirement. For the IRS, improper and erroneous payments generally involve improperly paid refunds, tax return filing fraud, or overpayments to vendors or contractors. Some tax credits, such as the Earned Income Tax Credit (EITC) and the Education Credit, provide opportunities for abuse in income tax claims. The IRS estimated that between 27 percent and 32 percent of the $31 billion in EITC claimed on TY 1999 returns should not have been paid.[8] The IRS' Criminal Investigation function is responsible for detecting and combating tax refund fraud through its Questionable Refund Program (QRP), which was established to address the serious problem of refund fraud, now estimated to exceed $500 million annually. In past years, it has been repeatedly reported that additional controls and procedures were necessary not only to identify additional instances of potential fraud, but also to properly and timely release refunds that are determined not to be fraudulent.[9] Recently, the National Taxpayer Advocate criticized the IRS for unnecessarily stopping refunds properly owed to taxpayers.[10] In response to

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7 Government Accountability Office (GAO), Pub. No. GAO-06-137, Financial Audit: IRS's Fiscal Years 2005 and 2004 Financial Statement (Nov. 2005).

8 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2005-40-093, The Earned Income Tax Credit Income Verification Test Was Properly Conducted (May 2005).

9 Audit reports previously issued by TIGTA: Ref. No. 2004-40-018, The Internal Revenue Service Can Improve the Effectiveness of Questionable Refund Detection Team Activities (Dec. 1999); Ref. No. 2001-40-025, Revised Questionable Refund Program Procedures Were Not Consistently Implemented (Jan. 2001); Ref. No. 2003-10-094, Improvements Are Needed in the Monitoring of Criminal Investigation Controls Placed on Taxpayers' Accounts When Refund Fraud Is Suspected (Mar. 2003); and Ref. No. 2005-10-164, The Internal Revenue Service Needs to Do More to Stop the Millions of Dollars in Fraudulent Refunds Paid to Prisoners (Sept. 2005).

10 National Taxpayer Advocate 2005 Annual Report to Congress (Dec. 2005).

the National Taxpayer Advocate's concern, on February 6, 2006, the IRS announced that it is taking steps to improve the QRP and reduce the number of taxpayers subject to frozen refunds. TIGTA is extremely concerned about this and believes that a necessary balance must be struck between allowing sufficient time to detect fraudulent claims and issuing timely refunds.

### *Taxpayer Protection and Rights*

The IRS continues to dedicate significant resources and attention toward implementing the taxpayer rights provisions of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) [11]. Audit reports are mandated for the following taxpayer rights provisions:

- *Notice of Levy*
- *Restrictions on the Use of Enforcement Statistics to Evaluate Employees*
- *Fair Debt Collection Practices Act Violations*
- *Notice of Lien*
- *Seizures*
- *Illegal Protestor Designations*
- *Assessment Statute of Limitations*
- *Restrictions on Directly Contacting Taxpayers Instead of Authorized Representatives*
- *Separated or Divorced Joint Filer Requests*

In general, the IRS has improved its compliance with these statutory taxpayer rights provisions. For example, based on TIGTA audit work, TIGTA believes the IRS' efforts to ensure that managers are not using enforcement statistics, production goals or quotas to evaluate employees are generally effective and are helping to protect the rights of taxpayers. Nonetheless, there is still room for improvement with respect to certain provisions. TIGTA continues to identify instances in which there is no documentation that taxpayers were advised of their rights regarding extensions to the tax assessment period. TIGTA also continues to identify instances in which IRS employees refer to taxpayers as Illegal Tax Protesters or similar designations.

Some IRS management information systems do not track specific cases. Thus, neither TIGTA nor the IRS could evaluate the IRS' compliance with certain RRA 98 provisions.

### *Processing Returns and Implementing Tax Law Changes During the Tax Filing Season*

Each filing season tests the ability of the IRS to implement tax law changes made by Congress. It is during the filing season that most individuals file their income tax returns and call the IRS if they have questions about specific tax laws or filing procedures. Correctly implementing tax law changes is a continuing challenge because the IRS must identify the tax law changes; revise the various tax forms, instructions, and publications; and reprogram the computer systems used for processing returns. Changes to the tax laws can have a major effect on how the IRS conducts its activities, how many resources are required, and how much progress can be made on strategic goals. Congress frequently changes the tax laws, so some level of change is a normal part of the IRS environment. However, certain types of changes can significantly impact the IRS in terms of the quality and effectiveness of service and in how taxpayers perceive the IRS. For example, the 2006 Filing Season was an unusually difficult one for the IRS because there were many late tax law changes in response to the hurricanes

11 Pub. L. No. 105-206, 112 Stat. 685 (Codified as amended in scatter sections of 2 U.S.C., 5 U.S.C. App., 16 U.S.C., 19 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

that struck the United States. Disaster relief provisions were enacted into law for taxpayers affected by Hurricanes Katrina, Rita, and Wilma. The Gulf Opportunity Zone (GO Zone) Act of 2005, [12] was signed into law on December 21, 2005. The late timing of this legislation gave the IRS very little time to revise the necessary tax forms and computer programs before the start of the 2006 Filing Season.

### *Human Capital*

Human capital is a major challenge facing many agencies, and the President's Management Agenda identifies Strategic Management of Human Capital as the first of five Government-wide initiatives for improving Government performance. Like many other Federal agencies, over the past several years the IRS has experienced workforce challenges. Those challenges include recruiting, training and retaining employees, as well as an increasing number of employees who are eligible to retire. The Small Business/Self-Employed and the Large and Mid-Size Business Divisions reported in their FY 2006 strategic assessments that the human capital crisis continues to intensify as employees in key occupational series increasingly become eligible to retire, are lost through attrition, or migrate to other business divisions. While the IRS has made some progress, the strategic management of human capital remains one of the IRS' major management challenge areas. TIGTA has made a significant number of recommendations for improvement in the areas of recruiting, workforce planning, delivery of training, and employee turnover. The IRS agreed with TIGTA recommendations and is taking corrective actions. TIGTA will continue to provide coverage of this major management challenge.

### *Conclusion*

These are the 10 major IRS management challenge issues for FY 2006. TIGTA's *FY 2007 Annual Audit Plan* categorizes its planned audits by these challenges. If you have questions or wish to discuss TIGTA's views on these management and performance challenges in greater detail, please contact me at (202) 622-6500.

cc: The Deputy Secretary
Assistant Secretary for Management and Chief Financial Officer
Commissioner of Internal Revenue

12 Pub. L. No. 109-135, 199 Stat. 2577.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

November 13, 2006

**MEMORANDUM FOR J. RUSSELL GEORGE**
**TREASURY INSPECTOR GENERAL**
**FOR TAX ADMINISTRATION**

**FROM:** Henry M. Paulson, Jr.

**SUBJECT:** Response to Management and Performance Challenges Facing the Internal Revenue Service

I am responding to your October 2, 2006, memorandum describing the Internal Revenue Service's (IRS) management and performance challenges.

This memorandum provides information on the actions that the IRS completed in FY 2006 and the actions that are planned for FY 2007 to address these ten challenges.

**Challenge 1 - Modernization of the Internal Revenue Service**

Through the Business Systems Modernization program, the IRS continued to develop tax administration systems that fulfill revenue collection requirements while making sustained progress toward realizing the modernization vision.

In FY 2006, the modernization program implemented best practices combined with expertise in business solutions. In addition, the program established a foundation of disciplined project delivery and accomplishment by meeting the target of plus or minus ten percent variance for both cost and schedule components for major release and sub-release milestones. This was a significant achievement that validates program management effectiveness while transitioning from a contractor-led program to an IRS-led program.

In FY 2007, the IRS will continue its focus on technological advances, continuity of programs, and strategic direction to optimize both taxpayer service and enforcement programs. The modernization will continue to implement its revised strategy, emphasizing the incremental release of complex projects to deliver business value sooner and at a lower risk.

**Challenge 2 - Tax Compliance Initiatives**

During FY 2006, the IRS's efforts focused on high-risk cases, enforcement of criminal statutes, investigations, and continued outreach activities using improved analytics and workload identification and selection systems.

By targeting high-risk cases, the IRS improved performance on individual, high income, and small business audits, resulting in a fifteen percent increase in collection case closures and a nine percent increase in revenue received from collection activities. Enforcement of criminal statutes was an integral component of the efforts to enhance voluntary compliance with the tax laws. In FY 2006, abusive tax schemes and shelters remained a high investigative priority, given the high profile and egregious nature of these activities.

In FY 2006, the IRS implemented the first phase of the private debt collection initiative, which allows private collection agencies to collect certain delinquent tax debts. Outreach activities were focused on return preparers and tax practitioner groups to prevent and deter fraud, while data exchanges with state taxing organizations continued to leverage limited government resources.

In addition, the IRS continued its enforcement efforts for entities with special tax status, including tax-exempt organizations, employee retirement plans, and government entities. The entities that comprise this customer base are subject to unique rules and have diverse needs, ranging from small community organizations and municipalities to major universities, pension funds, state and tribal governments, and tax-exempt bond issuers. Administering and enforcing the complex body of law governing these entities to ensure proper adherence to applicable statutes is a significant and ongoing challenge.

In FY 2007, the IRS plans to develop and implement corporate strategies to ensure optimum, balanced audit coverage, improved resource allocation, and the use of alternative resolution strategies to support efforts to reduce the tax gap. In addition, the IRS will continue to identify and investigate high-impact corporate fraud, improve criteria for identifying unscrupulous return preparers, and develop, test and evaluate new ways of reducing erroneous Earned Income Tax Credit (EITC) payments while maintaining participation by eligible taxpayers.

**Challenge 3 - Security of the Internal Revenue Service**

In FY 2006, the IRS began deployment of a three-pronged strategy focusing on encryption solutions, employee education and awareness, and critical analysis of IRS policies and procedures.

The IRS established a steering committee to coordinate efforts and leverage subject matter experts from the areas of information technology security, physical security, privacy, and identify theft. In addition, the IRS established requirements and increased protection of sensitive information housed in networks, laptops, and other mobile computing devices.

In a collaborative effort, the IRS partnered with TIGTA to develop and implement the IRS Phishing Web Site which provided guidance to employees as well as internal and external stakeholders. To comply with process guidance, the IRS updated its security certification and accreditation of business applications. In addition, an enterprise-wide strategy for systems disaster recovery, including strategic testing of disaster recovery plans, was implemented.

Moreover, during FY 2006, the IRS developed a comprehensive action plan to address all identified systems security shortcomings.

In FY 2007, the IRS will continue to improve compliance by implementing this action plan, solidifying gains from business owner participation in all areas, establishing disaster recovery processes for critical business processes, and continuing to implement a nationwide Disaster Recovery Plan, including conducting annual exercises in major computing environments.

**Challenge 4 - Providing Quality Taxpayer Service Operations**

In FY 2006, the IRS made significant improvements in taxpayer service, both internally and externally. These improvements include improved operations, increased use of web-based tools, and improved clarity of information and publications and quality of outreach activities. The IRS installed Contact Recording in 47 Taxpayer Assistance Centers which provides immediate performance feedback of employees to improve the quality and completeness of responses provided to taxpayers.

In FY 2006, the IRS continued expansion of the Internet Refund Fact of Filing (IRFOF) "Where's My Refund?" application to reduce toll-free telephone demand and offer taxpayers alternative methods of service. In addition, the IRS implemented a multi-year Quality Improvement Process Plan, using web-based tools, to improve information quality for the Volunteers in Taxpayer Assistance program.

In FY 2006, the IRS continued to improve the quality and clarity of tax forms, instructions and publications through feedback from taxpayers and practitioners. The "Life Cycle Products" line of publications was refined to educate taxpayers about the tax impact of significant life events. The IRS implemented a national rural strategy that provided outreach, free tax return preparation, and financial literacy education to rural America. In addition, the IRS revised its Spanish-language tax publications and products. In FY 2006, the EITC marketing and awareness campaigns were assessed to increase participation and improve compliance among eligible participants.

In FY 2007, the IRS will continue its progress in developing the Issue Management Resolution System, which will gather and track data on emerging issues, detect trends, and provide resolutions and communications with greater effectiveness. The IRS will continue to expand refund status and information programs to add more error explanations, accommodate split refunds inquiries, and provide new inquiry capability for those taxpayers filing for telephone excise tax refunds.

**Challenge 5 - Complexity of the Tax Law**

In FY 2006, the IRS continued to propose new legislation and develop more efficient means of administering the tax law. The IRS developed a prospectus for a Unified Family Credit that combines the provisions of the EITC, Child Tax Credit, and Dependency Exemption, to reduce taxpayer compliance burdens associated with claiming these provisions. In addition, the IRS continued to revise the regulations on the use and disclosure of tax return information by tax return preparers, and updated the *EITC Assistant* to include nontaxable combat pay in earned income.

The Administration's FY 2007 budget includes six proposals to simplify the tax treatment of savings and families by consolidating existing programs and clarifying eligibility requirements. Simplifying the tax law reduces unintentional errors caused by lack of understanding and opportunities for intentional evasion, making compliance easier for taxpayers and tax law administration easier for the IRS. In FY 2007, the IRS will continue progress with two significant efforts: 1) to implement an option for taxpayers to split refunds into as many as three separate accounts; and, 2) to develop a compliance strategy to identify and prevent erroneous Telecommunications Excise Tax Refunds (TETR).

## Challenge 6 - Using Performance and Financial Information for Program and Budget Decisions

The IRS's accomplishments in FY 2006 reflect increased analysis of financial activity, restructuring of budget programs, and progress in implementing cost accounting to support decision making.

In FY 2006, the IRS implemented a monthly assessment of financial activity across all financial plans and appropriations, incorporating a line-by-line review of spending activity. Budget programs and appropriations are realigned for FY 2007, to reflect accurately the direct funding of programs for Taxpayer Service and Enforcement (TSE). This realignment will identify funding for reinvestments for higher priority programs, and enhance the ability to fully cost TSE activities.

In addition, the IRS continued to make incremental functional improvements to its financial systems and reporting by transferring the Statement of Net Cost to the Business Warehouse. This change will improve performance, and the cost allocation methodology, providing decision makers greater detail, and developing multiple "Status of Funds" reports to support business unit decision making. In addition, the IRS developed improved business processes, new interfaces and posting models to support the Private Collection Agency mandate.

In 2007, the IRS will continue to implement the managerial cost accounting action plan, conducting cost pilots which facilitate development of a cost policy, assessing and refining current cost allocations, and using cost accounting data for resource allocation decisions. In addition, the IRS will improve its detailed tax revenue accounting by enhancing financial systems and reporting through the development of the Custodial Detail Data Base (CDDB). The CDDB will create subsidiary ledgers by adding Revenues and Refund transactions, thereby addressing a long-standing material weakness.

## Challenge 7 - Erroneous and Improper Payments

The IRS has a robust, balanced, and comprehensive plan to reduce improper payments which include base compliance activities and redesign efforts. In FY 2006, the IRS opened over 520,000 examinations of EITC returns based on enhanced scoring and selection methodology, completing more than 515,000 and uncovering 315,000 misreported income cases. Part of this plan involved matching taxpayer income information to third party information (e.g. W-2s, 1099s). As a result, the IRS issued over 650,000 math error notices. In FY 2006, in partnership with internal and external organizations, the IRS developed and implemented an enterprise research strategy, which focuses on compliance and outreach activities, and continued the third year of the EITC Qualifying Child test, to better understand the effect of certification on participation, claim accuracy, and burden. Collectively, these enforcement efforts prevented nearly $2 billion in erroneous payments.

In FY 2007, the IRS will continue its improvement efforts, including: 1) a new process to score and select amended returns for examination; 2) a risk-based scoring strategy to identify and select cases for examination, ensuring the IRS works the most egregious and productive examination cases; 3) a systemic assignment of examination cases to campuses using new data, such as capacity and risk-based scores; and, 4) the integration of a decision support tool which automates issue identification, increases consistency in case documentation and eliminates duplicative data entry when the case is closed.

The Electronic Fraud Detection System (EFDS) is one of several tools used by IRS to combat erroneous and improper payments. All refund returns are scrutinized by the EFDS, which identifies a substantial number of false returns. The EFDS efficiently automates the review process which includes screening for income verification, scheme development, and scheme inventory management, even as new schemes are identified.

The manner and means by which individuals deploy fraudulent refund schemes are constantly evolving and are becoming more complex and sophisticated. The Questionable Refund Program (QRP) and the Return Preparer Program (RPP) will continue to serve an important tax administration purpose by enabling the IRS to identify and stop the payment of fraudulent refund claims, as well as identify and investigate unscrupulous return preparers.

## Challenge 8 - Taxpayer Protection and Rights

In FY 2006, the IRS completed several actions to address taxpayer protection and rights. These actions include: the development and implementation of the Taxpayer Rights Impact Statement which will incorporate awareness and consideration of taxpayer rights into all IRS programs; the refining of procedures to certify compliance with requirements of Title VI of the Civil Rights Act of 1964 and provide equal access and non-discriminatory services to all eligible taxpayers; and, the redesign of the education and awareness program which enables taxpayers to feel confident with their preparers competence and that the IRS will take appropriate enforcement actions on preparers who perform negligently or recklessly. In addition, the IRS continued their emphasis on the Return Preparer Program, by increasing Program Action Cases against preparers who filed incorrect or fraudulent returns.

In FY 2007, the IRS will continue efforts to enhance security programs to safeguard taxpayer data. In addition, the IRS will continue to study the Questionable Refund Program workflow processes to identify where improvements can be made, particularly in the area of refund freezes.

**Challenge 9 - Processing Returns and Implementing Tax Law Changes During the Tax Filing Season**

In FY 2006, despite natural disasters that affected a large number of taxpayers and required an unprecedented response, the IRS delivered a successful 2006 tax filing season. The IRS set a new record, in FY 2006, with over 72.8 million individuals filing returns electronically, a seven percent increase over FY 2005, with home computer filings showing the greatest increase, up eighteen percent. In addition, the IRS piloted an automated adjustment document to make changes or corrections to a taxpayer account, increasing quality and reducing the adjustment time. The IRS achieved enforcement processing economies by completing deployment of the e-services Transcript Delivery System, which significantly reduced the number of transcript requests from state agencies.

Based on recent court decisions, the IRS developed processes and procedures for administering telephone excise tax refunds to more than 150 million taxpayers. In FY 2007, the IRS will complete the continuing administration of the telephone excise tax refund program by providing additional services to taxpayers claiming the refund. In addition, the IRS will target a new compliance effort to minimize excise tax refund over-claims. The IRS will redesign Form 1040 and create a new Schedule O, for processing year 2008, which will simplify the reporting of certain adjustments to income, credits, taxes, and payments, and provide taxpayers with the option to split refunds into different bank accounts. The IRS will continue to expand its electronic filing program.

**Challenge 10 - Human Capital**

In FY 2006, the IRS began implementing a plan to ensure that it builds a highly productive and engaged workforce, by aligning the IRS's and the Treasury Department's strategic goals and establishing performance monitoring against objectives, processes, and projects.

In addition, the IRS identified and examined trends to address workforce planning challenges such as those present in its recent restructuring initiatives. In FY 2006, the IRS created a hiring plan to ensure replacement of critical enforcement positions lost to attrition, reach aggressive new hire targets, and implement several restructuring consolidation projects.

In FY 2006, the IRS began a multi-year recruitment and marketing plan which targets a diverse applicant pool. This plan identifies applicants with the appropriate knowledge, skills, and abilities for the IRS to meet its current and future business needs. In addition, the IRS increased the use of workforce planning tools to develop a more robust link between business plans and workforce replenishment.

In FY 2006, the IRS deployed the Learning Content Management System which permits efficient development of training materials and ensures consistency in training bureau-wide to improve the skills of current employees and prepare them for the workplace of tomorrow.

In FY 2007, the IRS will continue the redesign of management training using tailored case studies, training simulations, and break-out sessions to provide hands–on experience to develop and retain qualified managers. The IRS will continue working with OMB to develop a process for identifying high-performing organizations and the potential impact on recruiting, retention, and turnover issues.

We look forward to continue working with you to address these challenges.

cc: The Deputy Secretary
Assistant Secretary for Management and Chief Financial Officer
Commissioner of Internal Revenue

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# Appendix E: Material Weaknesses, Audit Follow-up, and Financial Systems

### The Department's Material Weaknesses

Management may declare audit findings or internal situations as a material weakness whenever a condition exists that may jeopardize the Department's mission or continued operations. Material weaknesses are required in these instances by the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and the Federal Financial Management Improvement Act of 1996 (FFMIA).

| Summary of FMFIA and FFMIA Material Weaknesses | Section 2 | Section 4 | Total |
|---|---|---|---|
| Balance at the beginning of FY 2006 | 6 | 1 | 7 |
| Closures or downgrades during FY 2006 | 1 | 0 | 1 |
| New Material Weaknesses declared during FY 2006 | 0 | 0 | 0 |
| Balance at the end of FY 2006 | 5 | 1 | 6 |

## Federal Managers Financial Integrity Act of 1982 (FMFIA)

The FMFIA requires agencies to establish and maintain a system of internal control. The Secretary must annually evaluate and report on the controls (Section 2) and financial systems (Section 4) that protect the integrity of Federal programs. The requirements of FMFIA serve as an umbrella under which other reviews, evaluations and audits should be coordinated and considered to support management's assertion about the effectiveness of internal control over operations, financial reporting, and compliance with laws and regulations.

The Department has five material weaknesses under Section 2 and one under Section 4 of the FMFIA, summarized as follows:

<table>
<tr><th colspan="2">Material Weakness Description<br>INTERNAL REVENUE SERVICE - IMPROVE MODERNIZATION MANAGEMENT CONTROLS AND PROCESSES.</th></tr>
<tr><td colspan="2">The IRS needs to improve its Business Systems Modernization program. Key elements include:<br>• IRS needs to assess the recommendations from the Special Studies and Reviews of the Business Systems Modernization program and projects.<br>• Implement and institutionalize procedures for validating contractor-developed costs and schedules.<br>• Establish effective contract management practices.<br>• Complete a human capital strategy.<br>• Improve configuration management practices</td></tr>
<tr><th>Actions Completed</th><th>What Remains to be Done</th></tr>
<tr><td>✓ Study and review recommendations assessed and implemented where warranted<br>✓ Formal process for contractor-developed cost and schedule evaluation implemented<br>✓ Contract management policy and procedures developed and implemented<br>✓ Human Capital Plan completed<br>✓ Configuration management policies and practices improved and implemented</td><td>➤ Allow assessment time to observe long-term effect of actions completed<br>➤ Targeted Downgrade/Closure: FY 2007</td></tr>
</table>

| Material Weakness Description | |
|---|---|
| **INTERNAL REVENUE SERVICE – REDUCE EARNED INCOME TAX CREDIT (EITC) OVERCLAIMS.** | |
| The IRS has high erroneous payment error rates within the EITC program. Key elements:<br>✓ Review and implement the EITC Task Force Recommendation to reduce overclaims<br>✓ Need to develop enhanced initiatives to reduce overclaims in existing EITC programs<br>✓ Need to develop focused initiatives to educate the EITC population<br>✓ Need to identify new ways to administer EITC by partnering with State, federal, and Private organizations and through the productive use of proactive research initiatives | |
| **Actions Completed** | **What Remains to be Done** |
| ✓ Task Force recommendations assessed and implemented where warranted<br>✓ Special studies conducted to identify solutions for 3 key overclaim areas<br>✓ Education and outreach initiatives completed<br>✓ Productive partnerships established for data sharing and research initiatives | ➤ Partner with OMB to develop more accurate error rate estimates<br>➤ Development of Corrective Action Plan required per the Improper Payments Information Act of 2002<br>➤ Monitor plan for improper payment reduction<br>➤ Targeted Downgrade/Closure: FY 2008 |

| Material Weakness Description | |
|---|---|
| **INTERNAL REVENUE SERVICE – COMPUTER SECURITY.** | |
| The IRS has various computer security controls that need improvement. Key elements:<br>• Adequately restrict electronic access to and within computer network operational components<br>• Adequately ensure that access to key computer applications and systems was limited to authorized persons for authorized purposes<br>• Adequately configure system software to ensure the security and integrity of system programs, files, and data<br>• Appropriately delineate security roles and responsibilities within functional business, operating, and program units, as required by FISMA<br>• Appropriately segregate system administration and security administration responsibilities<br>• Sufficiently plan or test the activities require to restore certain critical business systems when unexpected events occur<br>• Effectively monitor key networks and systems to identify unauthorized activities and inappropriate system configurations<br>• Provide sufficient technical security-related training to key personnel·<br>• Certify and accredit 90% of all systems | |
| **Actions Completed** | **What Remains to be Done** |
| ✓ Delineated responsibilities for carrying out security management activities within organizational units across IRS as well as the expectation of performance of security-related tasks associated with individual roles.<br>✓ Ensured that one individual cannot independently control all key aspects of a process or computer-related operation for systems administration. | ➤ Restrict electronic access to and at the operating system level of network operational components.<br>➤ Control access to systems software and applications.<br>➤ Implement configuration management and change control to safeguard the security and integrity of system programs, files, and data.<br>➤ Plan and test the activities for contingency and disaster recovery planning for critical information technology systems.<br>➤ Monitor user activity on network operating devices, operating systems, and applications.<br>➤ Provide training development, delivery, and evaluation for security responsibilities to key personnel<br>➤ Certify 90% of total systems<br>➤ Targeted Downgrade/Closure: FY 2009 |

| **Material Weakness Description**<br>**FINANCIAL MANAGEMENT SERVICE – CONSOLIDATED GOVERNMENT-WIDE FINANCIAL STATEMENTS.** | |
|---|---|
| The government did not have adequate systems, controls, and procedures to properly prepare the consolidated government-wide financial statements. Key elements include:<br>• The government lacks a process to obtain information to effectively reconcile the reported excess of revenue over net costs with the budget surplus<br>• Weaknesses in financial reporting procedures in internal control over the process for preparing the Consolidated Financial Statements | |
| **Actions Completed** | **What Remains to be Done** |
| ✓ Developed a model to provide analysis of unreconciled transactions that affect the change in net position<br>✓ Accounted for intra-governmental differences through formal consolidating and elimination accounting entries using all reciprocal fund categories including the General Fund<br>✓ Established a process to ensure that Federal agencies submit complete closing packages to GAO | ➤ Create the reciprocal category for the Treasury General Fund.<br>➤ Implement changes identified by the Fiscal Assistant Secretary as a result of their review of the Reporting Entity definitions per the Financial Accounting Standards Advisory Board (FASAB) criteria.<br>➤ Establish traceability from agency footnotes to the Consolidated Financial Statements (CFS) for completeness<br>➤ Include all disclosures as appropriate.<br>➤ Include all loss contingencies as appropriate<br>➤ Targeted Downgrade/Closure Date: FY 2007* |
| | ** Additional corrective actions may be added at the completion of each annual closing cycle* |

| **Material Weakness Description**<br>**TREASURY DEPARTMENTAL OFFICES – LACK OF SUBSTANTIAL COMPLIANCE WITH THE FEDERAL INFORMATION SECURITY MANAGEMENT ACT (FISMA).** | |
|---|---|
| Key elements include:<br>• Need to establish a Departmental Offices Headquarters Information Technology Security Program<br>• The Treasury Chief information Officer needs to implement the Treasury Communications System disaster recovery plan and ensure bureau connectivity to the backup facility is established for uninterrupted services<br>• Provide effective oversight to ensure Treasury's compliance with the FISMA and track bureaus inventories and Plans of Actions and Milestones to ensure all systems are certified and accredited. | |
| **Actions Completed** | **What Remains to be Done** |
| ✓ Departmental Offices Headquarters Information Technology Security Program developed and implemented<br>✓ The Treasury Communications System Disaster Recovery Plan (including connectivity and backup capability) developed, tested, and implemented.<br>✓ Policy and procedures issued and infrastructure in place to allow for tracking of systems and plans of action. | ➤ Monitoring of plans of action and of system certification and accreditation progress.<br>➤ Targeted Downgrade/Closure: FY 2008 |

| Material Weakness Description | |
|---|---|
| **INTERNAL REVENUE SERVICE – ACCOUNTING FOR REVENUE.** | |
| The IRS needs to have detail data to support custodial financial reporting for revenue. Key elements include:<br>• Inability to provide detailed support for large types of revenue for employment and excise tax<br>• Lack of effective custodial supporting systems/subsidiary detail<br>• Subsidiary ledger does not track and report one Trust Fund Recovery Posting (TFRP) balance<br>• Untimely posting of TFRP assessments and untimely review of TFRP accounts<br>• Lack of a single, integrated general ledger to account for tax collection activities and the costs of conducting those activities<br>• Inability to generate and report reliable cost-based performance data for collection activities to make informed resource allocation decisions<br>• IRS's general ledger for its custodial activities does not use the standard federal accounting classification structure | |
| **Actions Completed** | **What Remains to be Done** |
| ✓ Detailed disclosures for employment and excise taxes drafted to accompany FY 2006 financial statements<br>✓ Release 1 of the Custodial Detail Data Base (CDDB) implemented<br>✓ Plan for CDDB Release 2 completed.<br>✓ Tracking and reporting of one TFRP balance completed.<br>✓ Timely processing of TFRP transcripts certified. | ➤ Completion of CDDB Releases to provide a single, integrated subsidiary ledger using standard federal accounting classification structure.<br>➤ Targeted Downgrade/Closure Date: FY 2009 |

## Federal Financial Management Improvement Act of 1996 (FFMIA)

The FFMIA requires agencies to have financial management systems that substantially comply with the Federal financial management systems requirements, standards promulgated by the Federal Accounting Standards Advisory Board (FASAB), and the U.S. Standard General Ledger (USSGL) at the transaction level. Financial management systems shall have general and application controls in place in order to support management decisions by providing timely and reliable data. The Secretary shall make a determination annually about whether the agency's financial management systems substantially comply with the FFMIA. If the systems are found not to be compliant, management shall develop a remediation plan to bring those systems into substantial compliance. Management shall determine whether non-compliances with FFMIA should also be reported as non-conformances with Section 4 of FMFIA.

### Audit Follow-Up Activities

During FY 2006, the Department made steady progress in both the general administration of management control issues throughout the Department and the timeliness of the resolution of all findings and recommendations identified by the Office of the Inspector General (OIG), the Treasury Inspector General for Tax Administration (TIGTA), the Government Accountability Office, and external auditors. During the year, the Department continued to provide enhancements to the tracking system called the "Joint Audit Management Enterprise System" (JAMES). JAMES is a Department-wide, interactive, Web-based system accessible to the OIG, TIGTA, Bureau Management, Departmental Management, and others. The system contains tracking information on audit reports from issuance through completion of all corrective actions required to address findings and recommendations contained in an audit report.

In addition, Departmental oversight of bureau management control program activities, as well as communication and coordination with the bureaus in general, was strengthened through a combination of:

- Inclusion of Internal Control responsibilities in the performance plans of Senior Executives and their direct reports.
- Ongoing discussion of internal control issues at senior management councils and meetings
- The issuance of Internal Control Program Quarterly Reports which focus on significant control issues throughout the organization and which are distributed to the Secretary, Under Secretaries, Assistant Secretaries, bureau heads, bureau CFOs and CIO's, and other key personnel.

## Potential Monetary Benefits

The Inspector General Act Amendments of 1988, Public Law 101-504, require that the Inspectors General and the Secretaries of Executive Agencies and Departments submit semiannual reports to the Congress on actions taken on audit reports issued that identify potential monetary benefits. The Department consolidates and annualizes all relevant information for inclusion in this report. The information contained in this section represents a consolidation of information provided separately by the OIG, TIGTA, and Department management.

In the course of their audits, the Inspectors General periodically identify questionable costs, make recommendations that funds be put to better use, and identify measures that demonstrate the value of audit recommendations to tax administration and business operations. Questioned cost means:

- a costs that is questioned because of an alleged violation of a provision of a law, regulation, contract, or other requirement governing the expenditure of funds;
- a finding, at the time of the audit, that such costs is not supported by adequate documentation (an unsupported cost); or
- a finding that expenditure of funds for the intended purpose is unnecessary or unreasonable.

The phrase "disallowed costs" means a questioned cost that management, in a management decision, has sustained or agreed should not be charged to the Government.

The Department regularly reviews progress made by the bureaus in realizing potential monetary benefits identified in audit reports, and coordinates with the auditors as necessary to ensure the consistency and integrity of information on monetary benefit recommendations being tracked.

The statistical data in the following summary table and proceeding charts represents audit report activity for the period from October 1, 2005 through September 30, 2006. The data reflects information on reports that identified potential monetary benefits that were issued by the Office of Inspector General (OIG) and the Treasury Inspector General for Tax Administration (TIGTA).

| **Audit Report Activity With Potential Monetary BenefitsFor Which Management Has Identified Corrective Actions (OIG and TIGTA)** October 1, 2005 through September 30, 2006 (Dollars in Millions) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Disallowed Costs** | | **Better Used Funds** | | **Revenue Enhancements** | | **Totals** | |
| | **Reports** | **Dollars** | **Reports** | **Dollars** | **Reports** | **Dollars** | **Report Total**** | **Total Dollars** |
| Beginning Balance* | 12 | $8.7 | 10 | $59.4 | 16 | $16,445.7 | **35** | **$16,513.8** |
| New Reports | 7 | 38.5 | 5 | 112.4 | 6 | 1,113.5 | **18** | **1,264.4** |
| Total | 19 | 47.2 | 15 | 171.8 | 22 | 17,559.2 | **53** | **17,778.2** |
| Reports Closed | 11 | 8.0 | 10 | 56.5 | 6 | 3,362.0 | **25** | **3,426.5** |
| *a. Realized or Actual* | 8 | 13.3 | 5 | 9.2 | 2 | 468.0 | **13** | **490.5** |
| *b. Unrealized - Written off* | 9 [1] | 3.0[1] | 8[2] | 47.3[2] | 6[3] | 2,893.9[3] | **23** | **2,944.2** |
| **Ending Balance** | **8** | **39.2** | **5** | **115.3** | **16** | **14,197.2** | 28 | **14,351.7** |

** The beginning balance row was revised to reflect certain retroactive corrections of the beginning balances.*
***Report total column may not add across due to inclusion of reports in multiple categories.*

[1] *This category includes one report, with $2.4 million written off, for which IRS management did not concur with TIGTA's projected benefit.*

[2] *This category includes three reports, with $3.3 million written off, for which TIGTA does not agree with the IRS that the benefits have not been realized; one report, with $1.8 million written off, for which IRS management did not agree with TIGTA's recommended corrective action; and also includes three reports, with $42.1 million written off, for which IRS management did not concur with TIGTA's projected benefits.*

[3] *This category includes one report, with $1.4 billion written off, for which TIGTA does not agree with the IRS that the benefits have not been realized, and four reports, with $1.49 billion written off, for which IRS management did not concur with TIGTA's projected benefits.*

The following table provides a snap shot of OIG and TIGTA audit reports with significant recommendations reported in previous semiannual reports for which corrective actions had not been completed at September 30, 2005 and September 30, 2006, respectively. There were no "Undecided Audit Recommendations" during the same periods.

| **Significant Unimplemented Recommendations** | | | | |
|---|---|---|---|---|
| | **9/30/2005** | | **9/30/2006** | |
| | *OIG* *No. of Reports* | *TIGTA* *No. of Reports* | *OIG* *No. of Reports* | *TIGTA* *No. of Reports* |
| *Unimplemented* | *12* | *45* | *9* | *37* |

The following table presents a summary of TIGTA and OIG audit reports that were open for more than a year with potential monetary benefits at the end of PAR Report Year.

| Number of Reports Open for More than One Year | | | | |
|---|---|---|---|---|
| | **PAR Report Year** | **FY 2004** | **FY 2005** | **FY 2006** |
| **TIGTA** | **No. of Reports** | 14 | 17 | 15 |
| | **$ Projected Benefits** | $7,262.1 million | $7,581.8 million | $ 13,097.6 million |
| **OIG** | **No. of Reports** | 2 | 0 | 0 |
| | **$ Projected Benefits** | $0.5 million | $0 million | $0 million |

The following table presents a summary of TIGTA and OIG audit reports on which management decisions were made on or before September 30, 2005, but the final actions have not been taken as of September 30, 2006.

**Details of the Audit Reports on Which Management Decisions Were Made On or Before September 30, 2005, But Final Actions Have Not Been Taken as of September 30, 2006 (Dollars In Thousands)**

| Bureau | Report Number | Report Issue Date | Brief Description | Disallowed Costs | Funds Put to Better Use | Revenue Enhancement | Total | Due Date/Reason for Delay |
|---|---|---|---|---|---|---|---|---|
| IRS | 2000-30-165 | 9/20/2000 | The IRS can better use collectibility information during the examination process | | | 8,100.0 | 8,100.0 | Delayed 12/15/06 pending clarifying update to the IRM publication |
| **FY 2000** | **1** | | | | | **8,100.00** | **8,100.0** | |
| IRS | 2001-30-165 | 9/27/2001 | Implement a process to identify taxpayers that are likely personal service corporations but did not file as such | | | 78,158.6 | 78,158.6 | Delayed to 11/15/06 so 2005 data can be extracted and analyzed to provide an accurate response |
| **FY 2001** | **1** | | | | | **78,158.6** | **78,158.6** | |
| IRS | 2003-30-071 | 3/14/2003 | Improvements could be made to the Schedule K-1 matching program by increasing the use of electronic or scannable data | | 3,000.0 | | 3,000.0 | Delayed to 1/15/07. IRS has decided to consider mandating e-filing at the time each form is to be converted in the Modernized e-file environment |
| IRS | 2003-30-162 | 8/6/2003 | The regulations for granting extensions of time to file are delaying the receipt of billions of tax dollars and creating substantial burden for compliant taxpayers | | | 6,900,000.0 | 6,900,000.0 | Delayed to 12/15/06. IRS seeking TIGTA concurrence |
| **FY 2003** | **2** | | | | **3,000.0** | **6,900,000.0** | **6,903,000.0** | |

| **Details of the Audit Reports on Which Management Decisions Were Made On or Before September 30, 2005, But Final Actions Have Not Been Taken as of September 30, 2006** (Dollars In Thousands) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Bureau** | **Report Number** | **Report Issue Date** | **Brief Description** | **Disallowed Costs** | **Funds Put to Better Use** | **Revenue Enhancement** | **Total** | **Due Date/Reason for Delay** |
| IRS | 2004-10-128 | 7/28/2004 | LOU: Contractor's documentation was not adequate to support the tax forum income and expenses | 684.0 | | | 684.0 | Due 10/15/07 |
| IRS | 2004-20-014 | 11/19/2003 | The IRS should use the planned Travel and Reimbursement Accounting System long-term travel authorization processing enhancements to assure that IRS periodically reassesses employee travel plans | 25.0 | | | 25.0 | Due 3/31/2007 |
| IRS | 2004-20-014 | 11/19/2003 | The IRS should use the planned Travel and Reimbursement Accounting System long-term travel authorization processing enhancements to assure that IRS periodically reassesses employee travel plans | | | 180.5 | 180.5 | Due 3/31/2007 |
| IRS | 2004-20-142 | 8/26/2004 | The IRS should ensure the Storage Strategy Study addresses the data storage capacity deficiency and recommends a cost-effective Virtual tape system solution to reduce maintenance and tape shipping costs | | 200.0 | | 200.0 | Due 12/31/2010 |
| IRS | 2004-30-170 | 9/21/2004 | Improvements are needed for processing income tax returns of controlled corporate groups | | | 29,670.0 | 29,670.0 | Due 12/15/2006 |
| IRS | 2004-10-185 | 9/27/2004 | The IRS should develop and distribute a Collection Due Process (CDP) Tracking System to identify CDP cases | | | 2,000.0 | 2,000.0 | Due 2/15/2007 |

| Details of the Audit Reports on Which Management Decisions Were Made On or Before September 30, 2005, But Final Actions Have Not Been Taken as of September 30, 2006 (Dollars In Thousands) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Bureau** | **Report Number** | **Report Issue Date** | **Brief Description** | **Disallowed Costs** | **Funds Put to Better Use** | **Revenue Enhancement** | **Total** | **Due Date/Reason for Delay** |
| **FY 2004** | **5** | | | **709.0** | **200.0** | **31,850.5** | **32,759.5** | |
| IRS | 2005-30-013 | 12/2/2005 | Consider requiring the use of a standardized tool, such as Decision Point, or analysis tools in the offer evaluation process | | | 135.0 | 135.0 | Due 12/15/2006 |
| IRS | 2005-20-098 | 7/21/2005 | To improve Storage Area Network (SAN) management, the CIO should ensure the implementation of the SAN Development Laboratory and the Enterprise Data Warehouse Strategy | | 9.858.1 | | 9,858.1 | Rejected 7/27/2005 |
| IRS | 2005-30-048 | 3/31/2005 | To improve the filing compliance of pass-through businesses and to ensure fairness in the tax system for all similarly-situated pass-through businesses, IRS requires the assessment of late filing penalties regardless of the number of partners in a partnership | | | 5,100,000.0 | 5,100,000.0 | Due 2/15/2007 |
| IRS | 2005-30-048 | 3/31/2005 | Same as above | | | 316,200.00 | 316,200.00 | Due 2/15/2007 |
| IRS | 2005-30-048 | 3/31/2005 | Same as above | | | 302,700.0 | 302,700.0 | Due 2/15/2007 |
| IRS | 2005-30-048 | 3/31/2005 | Same as above | | | 299,000.0 | 299,000.0 | Due 2/15/2007 |
| IRS | 2005-30-073 | 4/28/2005 | To assist the IRS in its efforts to improve voluntary filing compliance, the IRS should conduct a study to determine the feasibility of expanding backup withholding treatment to all non-wage income sources that form the basis for the non-filing condition | | | 45,000.0 | 45,000.0 | Rejected 5/10/2005 |

| Details of the Audit Reports on Which Management Decisions Were Made On or Before September 30, 2005, But Final Actions Have Not Been Taken as of September 30, 2006 (Dollars In Thousands) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Bureau** | **Report Number** | **Report Issue Date** | **Brief Description** | **Disallowed Costs** | **Funds Put to Better Use** | **Revenue Enhancement** | **Total** | **Due Date/Reason for Delay** |
| IRS | 2005-30-101 | 7/26/2005 | To ensure compliance will all applicable laws, the IRS should implement a proactive strategy to enforce Foreign Bank and Financial Account Report (FBAR) filing requirements using foreign source income data and the Currency Banking and Retrieval System data | | | 2,600.0 | 2,600.0 | Due 7/15/2007 |
| IRS | 2005-1c-175 | 9/29/2005 | Contractor provides more training to its personnel emphasizing unreasonable costs per the FAR and applicable supplements | 81.8 | | | 81.8 | Due 9/15/2008 |
| **FY 2005** | **6** | | | **81.8** | **9,858.1** | **6,065,635.0** | **6,075,574.9** | |
| **TOTAL** | **15** | | | **790.8** | **13,058.1** | **13,083,744.1** | **13,097,593.0** | |

## Plan For Financial Management Systems Framework

### Overview

The Department of the Treasury's financial management systems structure consists of financial and mixed systems maintained by the Treasury bureaus and the Department-wide Financial Analysis and Reporting System (FARS). The bureau systems process and record the detailed financial events and submit summary-level information to FARS on a scheduled basis. FARS maintains the key financial data necessary for consolidated financial reporting. In addition, the FARS modules also maintain data on performance management, and the status of audit-based corrective actions. Under this systems structure, the bureaus are able to maintain financial management systems that meet their specific business requirements. On a scheduled basis, the required financial and performance data is submitted to FARS to meet Departmental analysis and reporting requirements. The Department uses FARS to produce its periodic financial and performance reports as well as the annual Performance and Accountability Report. This structured financial systems environment enables the Department to receive an unqualified audit opinion and supports its required financial management reporting and analysis requirements.

The FARS structure consists of the following components: bureau financial management systems that process and record detailed financial transactions; the Treasury Information Executive Repository (TIER) data warehouse; CFO Vision to produce monthly financial statements and analyze financial results; the Joint Audit Management

Enterprise System (JAMES) to capture information on audit findings; and the Performance Reporting System (PRS) to track the status of key performance measures. Bureaus submit summary-level financial data to TIER on a monthly basis, within three business days of the month-end. This data is then used by CFO Vision to generate financial statements and reports on both a Department-wide and bureau-level basis. This structure enables the Department to produce its quarterly and audited annual financial statements. During fiscal year 2006, CFO Vision was upgraded to a web-based environment. Direct access to the new version will be made available to Treasury bureaus via the Department's Intranet web-portal during fiscal year 2007.

Treasury continues with its plans to enhance the financial management systems structure. As of September 2006, Treasury's inventory of financial management systems lists 69 financial and mixed systems compared to 68 in September 2005. As part of the Department's enhancement effort, eleven Treasury bureaus and reporting entities are cross-serviced by the Bureau of Public Debt's Administrative Resource Center (ARC). Cross-servicing enables these bureaus to have access to core financial systems without having to maintain the necessary technical and systems architectures. In addition, as part of the Department's implementation of the e-Travel initiative, bureaus have eliminated their legacy travel systems.

### E-Government Activities

As part of the President's Management Agenda, Treasury participates in the government-wide initiatives to implement E-Gov solutions. Treasury awarded an E-Gov Travel contract to one of the three GSA approved travel vendors. The Bureau of Public Debt's Administrative Resource Center (ARC) has taken the lead in the management and implementation of the E-Gov Travel initiative. As of September 2006, eleven bureaus have implemented the new Treasury E-Gov Travel solution. Of the remaining bureaus, one completed its pilot review. During testing the team identified an issue of connectivity from remote locations. They will be working to address this issue prior to a full implementation. The two remaining bureaus are working with the Department to address issues and finalize plans for E-Gov Travel implementation.

Building upon the efforts of the Federal Enterprise Architecture Program to expand E-Government, OMB launched the Financial Management Lines of Business (FMLOB) initiative. The vision of the FMLOB is to establish a government-wide financial management solution that improves business performance while ensuring integrity in accountability, financial controls, and mission effectiveness. The Office of Management and Budget selected ARC as a financial management Shared Service Provider to service other Federal agencies. Currently ARC services seventeen non-Treasury agencies and eleven Treasury bureaus with core financial system and financial processing support.

Treasury is also participating in the government-wide Integrated Acquisition Environment (IAE). The goal of the IAE is to create a simpler, common integrated business process for buyers and sellers that promote competition and integrity. As a result of the IAE initiative, Treasury has benefited from more accurate procurement data, improved transaction processing by reducing paper-based transactions, improved communication and processing with Treasury's contractors. Treasury is a voting member on the Acquisition Committee for E-Gov (ACE) which serves as the governing body of the IAE and also actively participates on various system-related Change Control Boards.

### Continued Improvement

Treasury's target financial management systems structure will build upon the current FARS foundation. As processing and reporting requirements change and FARS is expanded to collect additional financial data, it may be necessary to implement additional applications to support these new requirements. FARS will provide management with the appropriate tools needed to analyze Department and bureau performance.

During fiscal year 2005, the IRS implemented the Integrated Financial System (IFS) as their new core financial system. IFS replaced multiple financial systems with a single, integrated and certified commercial off-the-shelf system (COTS). IFS provides core financial accounting, budget management, cost management, and reporting capabilities. IRS received a clean audit opinion in the first year of IFS operations as well as for this fiscal year. During the audits of FY 2005 and FY 2006, GAO had not identified any systemic reportable conditions or material weaknesses. Since implementation of IFS, the IRS made some incremental functional improvements to improve performance, provide more timely and reliable data to decision-makers, improve financial reporting, provide automated interfaces, and reduce manual processing.

The current version of IFS software will no longer be supported by the vendor, effective December 2009. The IRS developed an initial alternatives analysis that examines several options for a "go forward" strategy for the financial system. Further analysis is being developed to provide a framework for the decision on financial management system modernization options. This will include evaluating cost, benefit, and risks associated with both Federal and private Shared Service Provider (SSP) options. IRS's goal is to upgrade the financial system, including Asset Management and Procurement enhancements, in FY 2010.

As a result of budget considerations, the IRS canceled the planned implementation of the Custodial Accounting Project (CAP). The IRS developed an alternative solution to CAP, the Custodial Detail Data Base (CDDB). Release 1 of CDDB was implemented in fiscal year 2006 to serve as the sub-ledger for tax revenue accounting, providing transaction level details. Work continues on the Customer Account Data Engine (CADE) which is replacing the decades-old Master File legacy system. Over 7.3 million returns were processed and 7 million refunds were issued, totaling in excess of $3.4 billion. CADE is expected to process an estimated 33 million returns in 2007.

As previously indicated the Administrative Resource Center cross-services eleven Treasury bureaus and reporting entities. The Department anticipates a further reduction in the number of core financial systems as additional bureaus move to the ARC. Over the next two years, two additional Treasury bureaus will migrate to ARC for core financial systems support. In addition to the cross-servicing for core financial systems, Treasury bureaus are also being cross-serviced for other financial management services, such as electronic travel and human resource processing.

### Federal Financial Management Improvement Act Compliance

At the beginning of FY 2005, IRS implemented a new core financial system, the Integrated Financial System (IFS). Implementation of IFS is expected to position IRS administrative financial activities so that they are substantially compliant with the Federal Financial Management Improvement Act (FFMIA). GAO's FY 2005 and 2006 audits did not disclose any new area of systemic non-compliance with the Federal Financial Management Improvement Act (FFMIA). The IRS will continue to report on remediation activities related to future releases of IFS, although at present, all future releases are on hold.

The IRS began development of the Custodial Detailed Data Base (CDDB), a financial data warehouse that leverages existing legacy assets to address the critical GAO financial material weaknesses. Release 1 of CDDB uses the files from the subsidiary ledger of unpaid assessments for the FY 2006 financial statement audit. CDDB incrementally builds to FFMIA compliance, and each CDDB future release addresses one or more of the material weaknesses in financial reporting. The IRS incorporated additional milestones for developing Releases 2 and 3 into its material weakness and FFMIA remediation action plans, and will continue to report on remediation activities related to future releases of CDDB. With full implementation of all CDDB releases, the IRS expects to be compliant with FFMIA.

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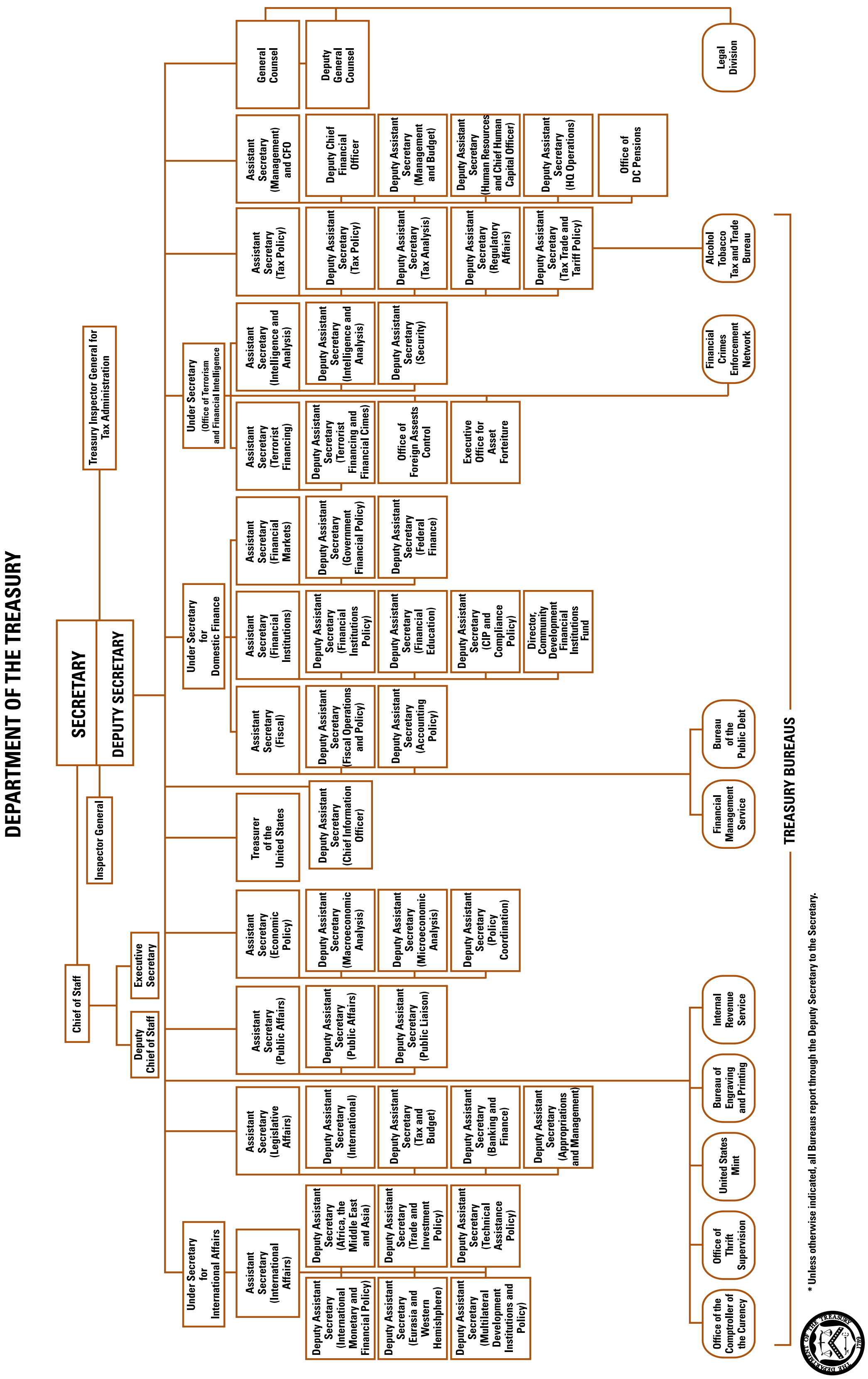
# Appendix F: Organizational Structure




Appendix F

Organizational Structure

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# Appendix G: Program Assessment Rating Tool (PART) Evaluations

| **Departmental Office** | **FY PARTed: FY 2002** |
|---|---|
| **Program: Economic and Trade Sanctions/Office of Foreign Asset Control** | |
| Rating: **Results Not Demonstrated** | |
| **OMB Found:**<br>• The program lacks long-term performance goals with specific targets.<br>• The program has not yet instituted annual performance goals to determine the effectiveness of its sanctions.<br>• The program is lacking unit cost measures. | |
| **In Response, DO is:**<br>• Developing long-term performance goals with specific timeframes and measures.<br>• Adopting annual performance goals and aligning them with the long-term performance goals. | |

| **Internal Revenue Service** | **FY PARTed: FY 2002** |
|---|---|
| **Program: Earned Income Tax Credit** | |
| Rating: **Ineffective** | |
| **OMB Found:**<br>• The program has failed to reduce EITC erroneous payments to acceptable levels. While IRS prevents roughly $1 billion in erroneous EITC payments per year, 27 to 32 percent of all EITC payments were still made in error for 1999. The magnitude of this error rate is the reason for the rating of "ineffective."<br>• IRS has a strong planning process closely linked to its budget process, but it has not yet used outcome information for this program to set performance targets that allow it to demonstrate results.<br>• IRS has made numerous management improvements in recent years. However, its financial management systems do not provide the information needed to make effective day to day management decisions. | |
| **In Response, IRS is:**<br>• Conducting 500,000 examinations of EITC returns per year based on enhanced case selection systems.<br>• Preventing $270 million in incorrect refunds in 2006 by detecting and correcting errors during return processing.<br>• Identifying paid tax return preparers with high EITC error rates and using education and enforcement procedures to improve their performance. | |

| **Community Development Financial Institution** | **FY PARTed: FY 2002** |
|---|---|
| **Program: Bank Enterprise Award** | |
| Rating: **Results Not Demonstrated** | |
| **OMB Found:**<br>• This program is unable to measure results because it can not determine how awardees would behave in the absence of the program. | |
| **In Response, CDFI is:·**<br>• Revising the BEA Program regulations and NOFA to more effectively achieve its strategic objectives. The revisions better target awards to CDFIs with a greater need for the incentive provided by the BEA Program award and to "personal wealth" and "community asset" building activities. | |

| Departmental Office<br>Program: International Development Association | FY PARTed: FY 2002 |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• The International Development Association is in the process of improving its performance measurement and performance-based budget allocations. In the latest donor negotiation, the World Bank and its donors agreed to significantly expand and improve the result measurement framework to increase the Association's effectiveness in achieving key development results in areas such as education.<br>• The latest donor negotiation agreed to implement reforms to significantly improve the ability of the poorest countries to handle their debts. In particular, the International Development Association will increase the share of funding for grants for the most debt-vulnerable countries to roughly 30 percent, making progress towards the President's goal of 50 percent.<br>• The International Development Association is improving transparency and access to its information. The United States helped secure significant improvements by insisting on a review of the World Bank's internal financial controls and the disclosure of individual country's performance scores under the International Development Association's new performance measurement system. | |
| • **In Response, DO is:**<br>Working with Congress to secure funding for the US contribution of $950 million per year from 2006 to 2008 to institute the reforms recently agreed to for the International Development Association.<br>• Monitoring the institution's effectiveness, including the implementation of measures to better track its progress in meeting development objectives across-the-board.<br>• Working with the World Bank and other donors to improve developing countries' ability to handle their debt, including increasing the amount of grants provided to the most debt-vulnerable countries. | |

| Departmental Office<br>Program: Office of Technical Assistance | FY PARTed: FY 2002 |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• Independent evaluations have not assessed the program's effectiveness. State and Treasury Inspectors General and the Government Accountability Office have reviewed aspects of the program, but none has evaluated effectiveness in advising foreign governments.<br>• Budget requests are not explicitly tied to accomplishment of goals such as increases in annual per capita income, and resource needs are not presented in a complete and transparent manner in the program's budget.<br>• The program does not routinely measure and achieve efficiencies in program execution. The program lacks efficiency measures to compare relative costs. | |
| **In Response, DO is:**<br>• Implementing the Project Management Tracking System<br>• Developing long-term and annual measures and targets. | |

| **Office of Thrift Supervision**<br>**Program: Thrift Supervision** | **FY PARTed: FY 2002** |
|---|---|
| Rating: **Effective** | |
| **OMB Found:**<br>• The program contributes to the safety and soundness of the banking industry.<br>• The program recently developed new goals that are outcome-oriented and program measurements which are clear and the program is efficiently and effectively managed.<br>• The program is not unique because other Federal agencies perform similar types of regulatory functions in the banking industry. | |
| **In Response, OTS is:**<br>• Working with Federal banking regulatory agencies to align outcome goals and related measures to allow for greater comparison of program performance in the industry.<br>• Conducting comprehensive examination for both Safety and Soundness and Compliance instead of two separate examinations and providing one consolidated report of examination to institutions.<br>• Examining long-term systemic risks in the industry. | |

| **Internal Revenue Service**<br>**Program: Tax Collection** | **FY PARTed: FY 2002** |
|---|---|
| Rating: **Results Not Demonstrated** | |
| **OMB Found:**<br>• IRS collection of unpaid taxes yields substantial revenue ($18 billion in 2001). However, IRS does not work enough collection cases with its current resources, work processes and technology to ensure fair tax enforcement. Each year billions of dollars of unpaid taxes goes uncollected.<br>• IRS has been working to make management improvements in the last several years, including implementing good output measures. However, its financial management systems do not provide the information needed to make effective day to day management decisions.<br>• IRS has a strong planning process closely linked to its budget process. IRS is currently developing improved collection outcome measures and goals. | |
| **In Response, IRS is:**<br>• Implementing new tools in 2007 to segment collection workload according to risk to ensure IRS takes the right action to secure delinquent taxes.<br>• Implementing legislation - including strong taxpayer rights protections - allowing IRS to hire private collection agents to help secure delinquent tax debt (full implementation by January 2008).<br>• Reviewing the effectiveness of the revised collection performance measures of workload coverage and efficiency. Information from these measures will be used in the development of the 2008 budget. | |

| **U.S. Mint**<br>**Program: Coin Production** | **FY PARTed: FY 2002** |
|---|---|
| Rating: **Effective** | |
| **OMB Found:**<br>• The Mint has established performance measures focused on customer satisfaction and improving cost efficiencies. For instance, the Mint reports the results of a Federal Reserve Board Customer Satisfaction survey.<br>• The Mint needs to improve customer satisfaction survey scores.<br>• The Mint has shown some efficiency improvements in achieving reduced manufacturing costs. The Mint has achieved a 19 percent reduction in manufacturing costs since 1997. | |
| **In Response, Mint is:**<br>• Reducing the maintenance down time of coin manufacturing machinery.<br>• Competing customer service and order mailing staff to determine if contractors could handle these functions more efficiently.<br>• Establishing a performance target to reduce the time required to process raw materials into produce coins. | |

| **Alcohol & Tobacco Tax and Trade Bureau**<br>**Program: Consumer Product Safety Commission** | **FY PARTed: FY 2002** |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• The program has a clear and unique Federal role. It is the only Federal agency that has the authority to identify and regulate a wide range of consumer products. As such, it provides a fair and consistent oversight for consumers and business (both domestic and foreign).<br>• Prior to 2004, program performance targets were not ambitious, set below already achieved levels. It has since revised its targets for performance measures which include: the death rate from fire-related causes and the death rate from carbon monoxide poisoning. These measures are discrete, quantifiable, measurable, and directly support the agency's mission.<br>• The program currently conducts cost-benefit analysis for most of its substantive regulations. The Poison Prevention Packaging Act (PPPA) regulations and those regulations directed by Congress that waive statutory requirements for cost-benefit analysis are accepted. | |
| **In Response, TTB is:**<br>• Reviewing new performance targets to ensure they are sufficiently ambitious.<br>• Reviewing the conduct of cost-benefit analyses on PPPA regulations to ensure that these regulations are conducted in a more comprehensive, consistent and thorough manner.<br>• Developing a plan to systematically review its current regulations to ensure consistency among regulations in accomplishing program goals. | |

| **Departmental Office** | **FY PARTed: FY 2003** |
|---|---|
| **Program: African Development Fund** | |
| Rating: **Results Not Demonstrated** | |

**OMB Found:**

- The African Development Fund is starting to improve its performance measurement and use of performance-based funding allocations. In the latest donor negotiation, the Fund and donors agreed to implement better results measurement for key development goals, such as education, and reconfirmed the allocation of funding towards better-performing countries, but more remains to be done.
- In the negotiations, the Fund and donors agreed to reforms to improve the ability of the poorest countries to handle their debts. In particular, they agreed that grants to assist the poorest countries will be expanded based on countries' debt vulnerability. Grants are expected to rise to more than one-third of the Fund's assistance.
- Accountability and transparency require additional improvements. The Bank Group has established a new anti-corruption and fraud unit and improved internal financial controls. The Bank Group is also expanding public access to its documents but more remains to be done.

**In Response, DO is:**

- Working with Congress to secure $136 million annually for the period 2006 to 2008 to fund the US commitment to the latest African Development Fund replenishment.
- Monitoring the Fund's effectiveness in achieving its development objectives, including its progress in measuring and meeting development objectives across-the-board.
- Working with Fund and other donors to improve the ability of developing countries to handle their debt, including providing grants to the most debt-vulnerable countries using the Fund.

| **Bureau of Engraving and Printing** | **FY PARTed: FY 2003** |
|---|---|
| **Program: New Currency Manufacturing** | |
| Rating: **Effective** | |

**OMB Found:**

- The program's New Currency program has a clear purpose, is well planned, and is managed effectively.
- The program met the initial production and timeline goals of its New Currency program with the rollout of the new twenty dollar bill in 2003.
- The program has adequate long-term targets and timeframes, including planned rollouts of counterfeit deterrent features for use in future generation notes through the next 7 to 10 years.

**In Response, BEP is:**

- Working closely with the Advanced Counterfeit Deterrent Steering Committee to identify and evaluate future counterfeit deterrent designs.
- Continuing to work with the Advanced Counterfeit Deterrent Steering Committee to assess the impact of New Currency on counterfeiting performance measures across government.
- Monitoring its design and overhead costs related to the manufacture of New Currency to ensure the most efficient production and distribution of future denominations.

| **Financial Management Services** | **FY PARTed: FY 2003** |
|---|---|
| **Program: Debt Collection** | |
| Rating: **Effective** | |
| **OMB Found:**<br>• The program has a clear purpose, is well designed, well managed, and generally meets or exceeds its annual performance targets. In 2005, the program collected $3.25 billion in delinquent debts owed to Federal agencies and States, up from $2.84 billion in 2002.<br>• The program has the potential to collect additional delinquent debt. Its effective performance indicates that it is capable of taking on additional debt collection activities. Legislation to increase and enhance debt collection opportunities should be sought. | |
| **In Response, FMS is:**<br>• Proposing legislation to increase and enhance debt collection opportunities. | |

| **Bureau of Public Debt** | **FY PARTed: FY 2003** |
|---|---|
| **Program: Administering the Public Debt** | |
| Rating: **Effective** | |
| **OMB Found:**<br>• The Bureau of Public Debt has a clear purpose and is well designed and managed.<br>• The program meets it annual performance goals and continues to improve targets for subsequent fiscal years.<br>• The program lacks long-term performance measures and targets. | |
| **In Response, BPD is:**<br>• Continuing to improve annual performance measures.<br>• Identifying new long-term goals to improve efficiency and effectiveness. | |

| **Financial Management Services** | **FY PARTed: FY 2004** |
|---|---|
| **Program: Collections** | |
| Rating: **Effective** | |
| **OMB Found:**<br>• The program has a clear purpose, is well designed and well managed. The program effectively collects, deposits, and accounts for approximately $2.7 trillion in revenue on behalf of Federal agencies each year through a network of more than 10,000 financial institutions.<br>• The program must develop stronger policies and techniques to ensure its program partners (customer Federal agencies and agent commercial banks) work toward achieving the long-term goals of the program. In 2005, 79 percent of Federal receipts were collected electronically. The goal of the program is to reach 90 percent by 2010. | |
| **In Response, FMS is:**<br>• Eliminating paper checks by converting them into electronic data or truncating them so only the image of the check is processed.<br>• Partnering with Customs and Border Protection to convert the $20 billion in customs fees CBP receives annually into electronic collections via *Pay.gov.*<br>• Piloting and implementing TGAnet, an automated system designed to eliminate the paper deposit tickets that accompany over-the-counter deposits by Federal agencies at financial institutions. | |

| **U.S. Mint** | **FY PARTed: FY 2004** |
|---|---|
| **Program: Numismatic** | |
| Rating: **Effective** | |

**OMB Found:**

- The program has made enormous strides over the past several years to streamline the production of numismatic products. Between 1999 and 2003, the Mint reduced costs by 38 percent and reduced workforce by 50 percent. During that same time period, production levels increased by 46 percent.
- The Mint has an excellent internal management structure that is able to receive and analyze real-time financial, production, and other operating data on a daily basis. This enables the Mint to respond quickly to changing production and customer.
- The Mint is making significant progress toward meeting its inventory turnover target of 4.2 in 2005, which reflects the number of times per year the Mint works through its inventory. This measure improved 27 percent from 1.96 in 2003 to 2.48 in 2004. By improving performance, the Mint reduces costs associated with inventory and the production planning process runs more efficiently.

**In Response, Mint is:**

- Continuing substantial progress toward reaching the Mint's target goal for inventory turnover.
- Continuing to streamline the production of numismatic products in order to reduce costs and improve efficiency.

| **Internal Revenue Service** | **FY PARTed: FY 2004** |
|---|---|
| **Program: Taxpayer Advocate Service** | |
| Rating: **Moderately Effective** | |

**OMB Found:**

- The quality of the Advocate's case work on behalf of taxpayers has improved from 71 percent with quality standards in 2001 to 90.5 percent in 2004.
- Taxpayer hardship cases caused by flaws in IRS' business processes have declined from 217,081 in 2001 to 129,382 in 2004 as the Advocate has worked with IRS program managers to improve processes.
- During the assessment, the program set goals and developed an efficiency measure. These include achieving a 100 percent closure-to-receipts ratio through 2010, 95 percent case quality score by 2009, and 4.53 (out of 5) customer satisfaction score by 2009. Efficiency is measured by counting the reduction in the quantity of taxpayer problems resulting from flaws in IRS' business processes.

**In Response, IRS is:**

- Developing a unit cost measure for its casework by 2006 (delayed to 2007).
- Exploring other means to measure its effectiveness in solving systemic problems leading to taxpayer hardship. IRS will report its findings in 2006 for possible inclusion in its FY 2008 Budget.
- Improving case quality to 91.5 percent by 2006, 93 percent by 2009, and 95 percent by 2014.

| Departmental Office<br>Program: Global Environment Facility | FY PARTed: FY 2004 |
|---|---|
| Rating: **Results Not Demonstrated** | |

**OMB Found:**

- The Global Environment Facility has been very slow to implement the reforms agreed to in 2002 as part of the last donor negotiation, the GEF-3 replenishment. Several of those reforms are incomplete, such as some performance related reforms. Several of these issues remain part of the current negotiations begun in 2005 to replenish the Facility's funding.
- The Facility has not yet fully instituted key performance improvements. For example, the Facility has not fully instituted improvements in the measurement of environmental results and implementation of a system to prioritize the allocation of its funding based on country performance and environmental benefit.
- The Facility lacks strong anti-corruption mechanisms. These include, for example, setting high standards, independent audit functions, financial disclosure and codes of ethics, obtaining clean annual external financial audits, and implementing procurement based on best practices.

**In Response, DO is:**

- Working with the Facility donors to fully implement a performance-based funding allocation system based on relative country performance and environmental benefit.
- Working with the Facility and donors to establish ambitious long-term performance goals and measures and undertaking more rigorous evaluations of project performance.
- Working with the Facility and donors to strengthen anti-corruption mechanism, including establishing high fiduciary standards and achieving clean annual audits from independent external auditors.

| Departmental Office<br>Program: Tropical Forest Conservation Act | FY PARTed: FY 2004 |
|---|---|
| Rating: **Results Not Demonstrated** | |

**OMB Found:**

- The program has been unable to measure its impact on increasing tropical forest conservation. It does not have performance measures that would enable a meaningful evaluation of program effectiveness.
- The Administration has developed a tool to help manage and measure the success of existing and pending agreements. This evaluation sheet will measure the success of country boards and oversight committees in developing a strategic plan that specifies key objectives, conservation and funding priorities, target dates in meeting those objectives, and key efficiency measures.
- The Administration is now collecting evaluation sheet data, and actual performance data will be reported in 2006. A re-evaluation may be performed as early as 2007.

**In Response, DO is:**

- Using information presented in evaluation sheets for existing programs to develop recommendations for improved program management and to justify future funding requests.
- Working with the boards, oversight committees, and program partners to include the evaluation sheet tool or other appropriate evaluations in all new agreements.

| Internal Revenue Service<br>Program: Taxpayer Service | FY PARTed: FY 2004 |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• IRS has significantly improved taxpayer service and maintained high levels of customer satisfaction in recent years. In 2001 IRS was able to answer only 62 percent of taxpayer calls. In 2005, IRS had improved this to 83 percent with a 94 percent customer satisfaction rate.<br>• IRS continues to have trouble with the accuracy of answers. In 2004, IRS estimates only 80 percent of tax law calls were answered accurately (improved to 89 percent in 2005). Accuracy is a significant challenge given the complexity of the tax code.<br>• IRS has developed a strong set of balanced measures (quality, customer satisfaction and results) to understand its taxpayer service performance. During the assessment IRS added an efficiency measure (customer contacts per staff year) for this program. | |
| **In Response, IRS is:**<br>• Converting to cost based efficiency measures for the 2007 budget (e.g., cost per call answered) and adding efficiency measures for service processes for management. (Delayed until 2008)<br>• Improving the accuracy of tax law telephone information provided to taxpayers to 90 percent accuracy by 2010.<br>• Researching the impact of taxpayer service programs on voluntary compliance and reporting findings by 2007. | |

| Community Development Financial Institution<br>Program: Financial and Technical Assistance | FY PARTed: FY 2004 |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• This program duplicates several Federal, state and private community and economic efforts.<br>• The program has long-term and annual performance measures but has not the opportunity to demonstrate success in accomplishing its long-term goals. | |
| **In Response, CDFI is:**<br>• Not taking any action because fewer than ten states administer CDFI programs and none of these state programs fully meet the capital needs of the CDFIs in its state. Furthermore, there are too few private sector equity investments available to meet CDFIs needs for capital. | |

| Community Development Financial Institution<br>Program: New Markets Tax Credit | FY PARTed: FY 2004 |
|---|---|
| Rating: **Adequate** | |
| **OMB Found:**<br>• The program has established meaningful long-term and annual performance measures.<br>• The program needs to measure progress towards achievement of its goals. | |
| **In Response, CDFI is:**<br>• Establishing and refining baselines and targets for its long-term and annual measures.<br>• Conducting an independent evaluation of the program in 2006. | |

| **Departmental Office** | **FY PARTed: FY 2005** |
|---|---|
| **Program: Asian Development Fund** | |
| Rating: **Results Not Demonstrated** | |

**OMB Found:**

- The Fund recently agreed to improve its performance measurement and performance-based allocations. In the latest donor negotiations, the AsDF-9 replenishment, the Fund and donors adopted several important reforms to improve performance and to implement results measurement, including launching the Managing for Results action plan. These reforms remain to be implemented and expanded in the future.
- AsDF-9 agreed to reforms to improve the ability of the poorest countries to handle their debts. In particular, it established a new program to give 30 percent of funding in the form of grants to these countries. These reforms remain to be implemented.
- Transparency and accountability in the Bank Group are improving. AsDF-9 requires more transparency through improved information disclosure and communication policies. The Bank Group's anti-corruption and auditing procedures require improvements.

**In Response, DO is:**

- Working with Congress to secure $115 million annually for the period 2006 to 2009 to fund the US commitment to the latest Asian Development Fund replenishment (AsDF-9).
- Monitoring the Fund's improvements and implementation of measures to show its effectiveness in achieving development goals, including its progress in meeting development objectives across-the board.
- Working with Fund and other donors to improve the ability of developing countries to handle their debt, including increasing the amount of grants for the most debt-vulnerable Asian countries.

| **Financial Crimes Enforcement Network (FinCEN)** | **FY PARTed: FY 2005** |
|---|---|
| **Program: Bank Secrecy Act (BSA) Data, Collection, Retrieval and Sharing** | |
| Rating: **Moderately Effective** | |

**OMB Found:**

- The program has long-term performance measures that focus on the program's purpose and strategic goals, but more work is needed to measure the quality of data collected. The program is looking at how to measure data quality.
- Federal managers are held accountable for cost, schedule and performance results. However, some activities are managed by another entity and are outside the scope of the performance measures.
- The program can show improved efficiencies and cost effectiveness for collecting and sharing data. The program has been able to show substantial increases in the number of users directly accessing data, the share of filings submitted electronically, and improved cost effectiveness for costs per form e-filed.

**In Response, DO is:**

- Surveying users to determine if they are receiving needed information in a timely manner, if the information is helpful, and if there are any problems with the information and format. FinCEN should have results from the first survey conducted on E-filing users by the end of 2006.
- Creating targets to measure the number of top 650 filers who file reports electronically. FinCEN has created the targets and implemented the performance measure.
- Creating a performance measure to measure the quality of information provided on Suspicious Activity Reports, possibly by measuring the number of completed fields that are critical to law enforcement. FinCEN is working on how best to measure this.

| **Internal Revenue Service**<br>**Program: Criminal Investigations** | **FY PARTed: FY 2005** |
|---|---|
| Rating: **Moderately Effective** | |
| **OMB Found:**<br>• The tax gap, the difference for a given year between taxes legally owed and taxes actually paid, for 2001 (latest available figure) is estimated to be between $312 and $353 billion. Criminal Investigation is one of the major IRS programs intended to minimize this revenue loss.<br>• Research suggests that higher levels of criminal sentences lead to higher tax compliance. IRS has succeeded in raising convictions in recent years. They rose from 1,926 in 2002 to 2,215 in 2005. However, they remain low by historical standards (in 1996 convictions totaled 2,915).<br>• IRS has set long term goals and efficiency measures. However, it has difficulty measuring compliance in a timely manner due to the complexity and expense involved and in holding employees accountable for performance due to legal restrictions. | |
| **In Response, IRS is:**<br>• Exploring methods for measuring the impact of criminal investigations on tax compliance. IRS will report on its progress by the end of 2006.<br>• Implementing a new information management system in 2006 to enhance investigative case tracking and improve efficiency.<br>• Developing methods to improve case prioritization in 2006 to ensure that cases yield the greatest impact on compliance. | |

| **Internal Revenue Service**<br>**Program: Examinations** | **FY PARTed: FY 2005** |
|---|---|
| Rating: **Moderately Effective** | |
| **OMB Found:**<br>• The tax gap, the difference for a given year between taxes legally owed and taxes actually paid, for 2001 (latest available figure) is estimated to be between $312 and $353 billion. Examination is one of the major IRS programs intended to minimize this revenue loss.<br>• After dropping substantially in the late 1990s, IRS' audit rates have begun to rise and will continue to increase, largely through productivity growth. IRS' audit rate has grown from a low of 1.49 percent (i.e., less than two returns in one hundred audited) in 2001 to 3.09 percent in 2005.<br>• IRS has set long term goals and efficiency measures. However, it has difficulty measuring compliance in a timely manner due to the complexity and expense involved and in holding employees accountable for performance due to legal restrictions. It also needs cost based efficiency measures. | |
| **In Response, IRS is:**<br>• Researching tax compliance of S-corporations (a popular business form where profits are taxed only once passed through to the owners) based on a statistically valid sample of the filing population.<br>• Improving tools for selecting the most productive audit cases by 2007 using the detailed compliance information gathered in the recent individual tax gap study.<br>• Introducing cost based efficiency measures by 2008 (e.g., enforcement revenue/program budget). | |

| **Internal Revenue Service**<br>**Program: Submission Processing** | **FY PARTed: FY 2005** |
|---|---|
| Rating: **Moderately Effective** | |
| **OMB Found:**<br>• More Americans are electronically filing their taxes. Electronic filing is growing more than 10 percent per year. However, this growth is not sufficient for IRS to meet the legislative goal of 80 percent electronic filing by 2007. Congress has not yet acted on the Administration's proposals to accelerate the increase in electronic filing.<br>• Every return converted from paper to electronic filing saves the IRS $2.15 in processing costs. More importantly, electronically filed returns have a less than one percent error rate compared to five percent for paper filed returns, saving taxpayers time and money. Finally, according to the annual American Customer Satisfaction Results report electronic filers have high satisfaction rates.<br>• Based on IRS' recently completed tax gap study, approximately 13 percent of refund dollars (excluding earned income tax credit refunds) are paid in error. With current third party reporting and technology, IRS is unable to identify and prevent these errors during processing. | |
| **In Response, IRS is:**<br>• Seeking legislative changes to promote electronic filing, including greater authority to require electronically-filed returns.<br>• Setting goals by 2007 for reduced taxpayer filing burden resulting from the time and expense of preparing and filing their returns.<br>• Using a single cost based efficiency measure by 2008 (cost per return processed). | |

| **U.S. Mint**<br>**Program: Protection Program** | **FY PARTed: FY 2005** |
|---|---|
| Rating: **Effective** | |
| **OMB Found:**<br>• The Mint has developed adequate long-term performance measures with ambitious targets and timeframes. The Mint's target for total losses is $250,000 in 2005 and $0 in 2010.<br>• Mint's Protection program has a clear purpose, is well planned, and managed effectively. However, it is somewhat duplicative of other Federal efforts aimed at protecting money, such as the Bureau of Engraving and Printing, and the Federal Reserve Police forces.<br>• The Mint regularly achieves its annual performance goals and works with other law enforcement partners to assess threat levels and assist in achieving future goals. The Mint is a participant in the multi-agency Counter-Terrorism Program. | |
| **In Response, Mint is:**<br>• Continue to assess and implement ways in which the cost of protection per square foot can be minimized.<br>• Continue to improve employee confidence in the United States Mint protection program. | |

| **Alcohol & Tobacco Tax and Trade Bureau** | **FY PARTed: FY 2005** |
|---|---|
| **Program: Collect the Revenue** | |
| Rating: **Effective** | |
| **OMB Found:**<br>• The Collect the Revenue program has a clear purpose and is well designed to achieve its goals. TTB administers and ensures compliance with portions of the Internal Revenue Code dealing with collection of excise taxes on alcohol, tobacco, firearms and ammunitions and regulation of those manufacturers.<br>• The program has developed adequate long-term performance measures with ambitious targets and timeframes. TTB measures the percent of voluntary compliance in filing tax payments and will increase this target from 82% in 2004 to 92% in 2010.<br>• The program has not developed adequate baselines for its annual performance measures. Three out of the four annual measures do not have baselines. | |
| **In Response, TTB is:**<br>• Developing baselines for annual performance measures.<br>• Improving estimates of how funds are distributed across TTB's two lines of business to ensure that funds are obligated in accordance with planned schedules.<br>• Developing a baseline to compare the incremental costs and net benefits of regulation. | |

| **Financial Management Services** | **FY PARTed: FY 2005** |
|---|---|
| **Program: FMS Payments** | |
| Rating: **Effective** | |
| **OMB Found:**<br>• The assessment found that the program has a clear purpose, is well managed, and generally meets its annual performance targets. In 2005, the Program issued 100 percent of payments accurately and on time, and 76 percent of these payments were made electronically (approximately 725 million of the 952 million total payments).<br>• The program must continue its effort towards an all-electronic Treasury. Each payment transaction that occurs electronically saves the taxpayer about 75 cents and is more secure for the recipient. | |
| **In Response, FMS is:**<br>• Working with Federal agencies to reduce the number of paper check payments and increasing the number of more efficient and secure electronic payments.<br>• Implementing Go Direct, a nationwide campaign to encourage current Federal check recipients to switch to direct deposit. | |

The following programs were evaluated in 2006 and are awaiting OMB recommendations that will be part of the FY 2008 budget.

| Bureau | Program | Rating |
|---|---|---|
| BEP | Protection | Rating Pending |
| FinCEN | Bank Secrecy Act Administration | Rating Pending |
| FinCEN | Bank Secrecy Act Analysis | Rating Pending |
| FMS | Government Wide Accounting and Reporting | Rating Pending |
| IRS | Health Care Tax Credit Administration | Rating Pending |
| IRS | IRS Retirement Savings Regulatory Program | Rating Pending |

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# Appendix H: Glossary of Acronyms

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|---|---|
| ACD | Advanced Counterfeit Deterrence |
| AGI | Adjusted Gross Income |
| ARC | Administrative Resource Center |
| ASM/CFO | Assistant Secretary for Management/Chief Financial Officer |
| ATAT | Abusive Tax Avoidance Transaction |
| AUR | Automated Under-Reporter |
| BEP | Bureau of Engraving and Printing |
| BIT | Bilateral Investment Treaties |
| BMENA | Broader Middle East and North Africa |
| BPD | Bureau of the Public Debt |
| BSA | Bank Secrecy Act |
| BSM | Business System Modernization |
| C&A | Certified and Accredited |
| CADE | Customer Account Data Engine |
| CAFTA | Central American Free Trade Agreement |
| CDDB | Custodial Detailed Data Base |
| CDE | Community Development Entity |
| CDFI | Community Development Financial Institution |
| CFO | Chief Financial Officer |
| CHCO | Office of the Chief Human Capital Officer |
| COLA | Certificates of Label Approval |
| CSI | Customer Satisfaction Index |
| CSRS | Civil Service Retirement System |
| D.C. Federal Pension Fund | D.C. Teachers, Police Officers and Firefighters Federal Pension Fund |
| DCP | Office of D.C. Pensions |
| DO | Departmental Office |
| EBRD | European Bank for Reconstruction and Development |
| e-File | Electronic Filing |
| EFT | Electronic Funds Transfer |
| EFTPS | Electronic Federal Tax Payment System |
| EGRPRA | Economic Growth and Regulatory Paperwork Reduction Act |
| EGTRRA | Economic Growth and Tax Relief Reconciliation Act |
| EIN | Employer Identification Number |
| EITC | Earned Income Tax Credit |
| EP | Economic Policy |

| | |
|---|---|
| EQ | Embedded Quality |
| ERIS | Enforcement Revenue Information System |
| ESF | Exchange Stabilization Fund |
| EU | European Union |
| F&PC | Filing and Payment Compliance |
| FACT | Federal Accurate Credit Transaction |
| FACTS I | Federal Agencies' Centralized Trial Balance System |
| FAIR | Federal Activities Inventory Reform Act |
| FARS | Financial Analysis and Reporting System |
| FASAB | Federal Accounting Standards Advisory Board |
| FBI | Federal Bureau of Investigation |
| FDIC | Federal Deposit Insurance Corporation |
| FECA | Federal Employees' Compensation Act |
| FEGLI | Federal Employees Group Life Insurance |
| FEHBP | Federal Employees Health Benefits Program |
| FERS | Federal Employees' Retirement System |
| FET | Federal Excise Tax |
| FFB | Federal Financing Bank |
| FFMIA | Federal Financial Management Improvement Act |
| FinCEN | Financial Crimes Enforcement Network |
| FISMA | Federal Information Security Management Act |
| FMFIA | Federal Managers' Financial Integrity Act |
| FMIS | Financial Management Information System |
| FMS | Financial Management Service |
| FPA | Federal Program Agencies |
| FTA | Free Trade Agreement |
| FTE | Full Time Equivalents |
| FY | Fiscal Year |
| GAB | General Arrangements to Borrow |
| GAIS | Government Agency Investment Services |
| GAO | Government Accountability Office |
| GDP | Gross Domestic Product |
| GEMAP | Governance and Economic Management Assistance |
| GFRS | Government-wide Financial Report System |
| GPRA | Government Performance and Results Act |
| GSA | General Services Administration |

| | |
|---|---|
| GTF | Government Trust Funds |
| GWA | Government-wide Accounting |
| HCSIP | Human Capital Strategic Implementation Plan |
| HIPC | Heavily Indebted Poor Countries |
| HSPD-12 | Homeland Security Presidential Directive-12 |
| IA | International Affairs |
| IAE | Integrated Acquisition Environment |
| IAP | International Assistance Programs |
| IEEPA | International Emergency Economic Powers Act |
| IFS | Integrated Financial System |
| IG | Inspector General |
| IISOWG | Information Security Officers' Working Group |
| IMF | International Monetary Fund |
| IPIA | Improper Payments Information Act |
| IRIS | Integrated Revenue Information System |
| IRS | Internal Revenue Service |
| IRS-CI | Internal Revenue Service Criminal Investigation |
| IT | Information Technology |
| JAMES | Joint Audit Management Enterprise System |
| JIATF | Joint Interagency Task Force |
| Judicial Retirement Fund | District of Columbia Judicial Retirement and Survivors Annuity Fund |
| LMSB | Large and Mid-Sized Business Division |
| MDB | Multilateral Development Banks |
| MeF | Modernized Electronic File |
| MEO | Most Efficient Organization |
| MINT | United States Mint |
| NAB | New Arrangements to Borrow |
| NMTC | New Markets Tax Credit |
| NRP | National Research Project |
| OCC | Office of the Comptroller of the Currency |
| OCIO | Office of the Chief Information Officer |
| OECD | Organization for Economic Cooperation and Development |
| OFAC | Office of Foreign Asset Control |
| OIA | Office of Intelligence Analysis and Security Programs |
| OIG | Office of the Inspector General |
| OMB | Office of Management and |

| | |
|---|---|
| OPEB | Other Post Employment Benefits |
| OPM | Office of Personnel Management |
| ORB | Other Retirement Benefits |
| OTS | Office of Thrift Supervision |
| PAR | Performance and Accountability Report |
| PART | Program Assessment Rating Tool |
| PCA | Planned Corrective Actions |
| PCIE | President's Council for Integrity and Efficiency |
| PIJ | Palestinian Islamic Jihad |
| PMA | President's Management Agenda |
| RIS | Requested for Information Services |
| RTC | Resolution Trust Corporation |
| SBR | Statement of Budgetary Resources |
| SDNT | Specially Designated Narcotics Traffickers |
| SDR | Special Drawing Rights |
| SES | Senior Executive Service |
| SFFAS | Statement of Federal Financial Accounting Standards |
| SME | Small and Medium Enterprise |
| Supplemental Fund | Federal Supplemental District of Columbia Pension Fund |
| TAC | Tax Assistance Center |
| TBARR | Treasury and Annex Repair and Restoration |
| TCE | Treasury Communications Enterprise |
| TEOAF | Treasury Executive Office for Asset Forfeiture |
| TFFC | Terrorist Financing and Financial Crimes |
| TFI | Terrorism and Financial Intelligence |
| TIGTA | Treasury Inspector General for Tax Administration |
| TIPS | Treasury Inflation-Protected Securities |
| Trust Fund | District of Columbia Federal Pension Liability Trust Fund |
| TTB | Alcohol & Tobacco Tax and Trade Bureau |
| TY | Tax Year |
| UAE | United Arab Emirates |
| USPS | United States Postal Service |
| VITA | Volunteer Income Tax Assistance |
| VPCR | Voluntary Payment Compliance Rates |

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|---|---|
| Treasury On-line | **www.treas.gov** |
| Alcohol and Tobacco Tax And Trade Bureau | **www.ttb.gov** |
| Community Development Financial Institutions Fund | **www.treas.gov/cdfi** |
| Comptroller of the Currency | **www.occ.treas.gov** |
| Bureau of Engraving & Printing | **www.bep.treas.gov** |
| Financial Crimes Enforcement Network | **www.treas.gov/fincen** |
| Financial Management Service | **www.fms.treas.gov** |
| Internal Revenue Service | **www.irs.gov** |
| U.S. Mint | **www.usmint.gov** |
| Bureau of the Public Debt | **www.publicdebt.treas.gov** |
| Office of Thrift Supervision | **www.ots.treas.gov** |