FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT

FY 2016

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

January 12, 2017

A Message from the Secretary

The annual Financial Report of the U.S. Government provides to the public a comprehensive overview of the Government's current financial position, as well as critical insight into our long term fiscal outlook. The Fiscal Year 2016 Financial Report, the final U.S. Financial Report of the Obama Administration, reflects an economy that has come a long way since 2008, with sustained private sector job growth and increasing vitality.

Under President Obama's leadership, there has been substantial economic and fiscal progress, showing what is possible when strategic investment is paired with smart reform. Labor market conditions continue to improve, we have added millions of jobs to the economy and GDP has grown steadily. Globally, the United States remains a driver of steady economic growth.

In Fiscal Year 2016, the Nation's economic gains contributed to increased revenues and sustainable deficit financing for the next decade. The Government's estimated long-term fiscal gap continues to be reduced by the provisions of the Affordable Care Act of 2010, Budget Control Act of 2011, and the American Taxpayer Relief Act of 2013. These and other measures support our economy, allow our government to operate more efficiently, and support long term fiscal health.

This Administration's policies have created the space to address the country's long term fiscal challenges; however, near term policies that reduce revenues or increase spending, such as through changes to our tax code or the Affordable Care Act, could increase the size of the fiscal gap and force more dramatic adjustments in later years. We must ensure that our prosperity is shared by all Americans, not just those at the top. I am proud of the work we have done as a country over the past eight years to address our economic challenges and am pleased to share this strong report.

Jacob J. Lew

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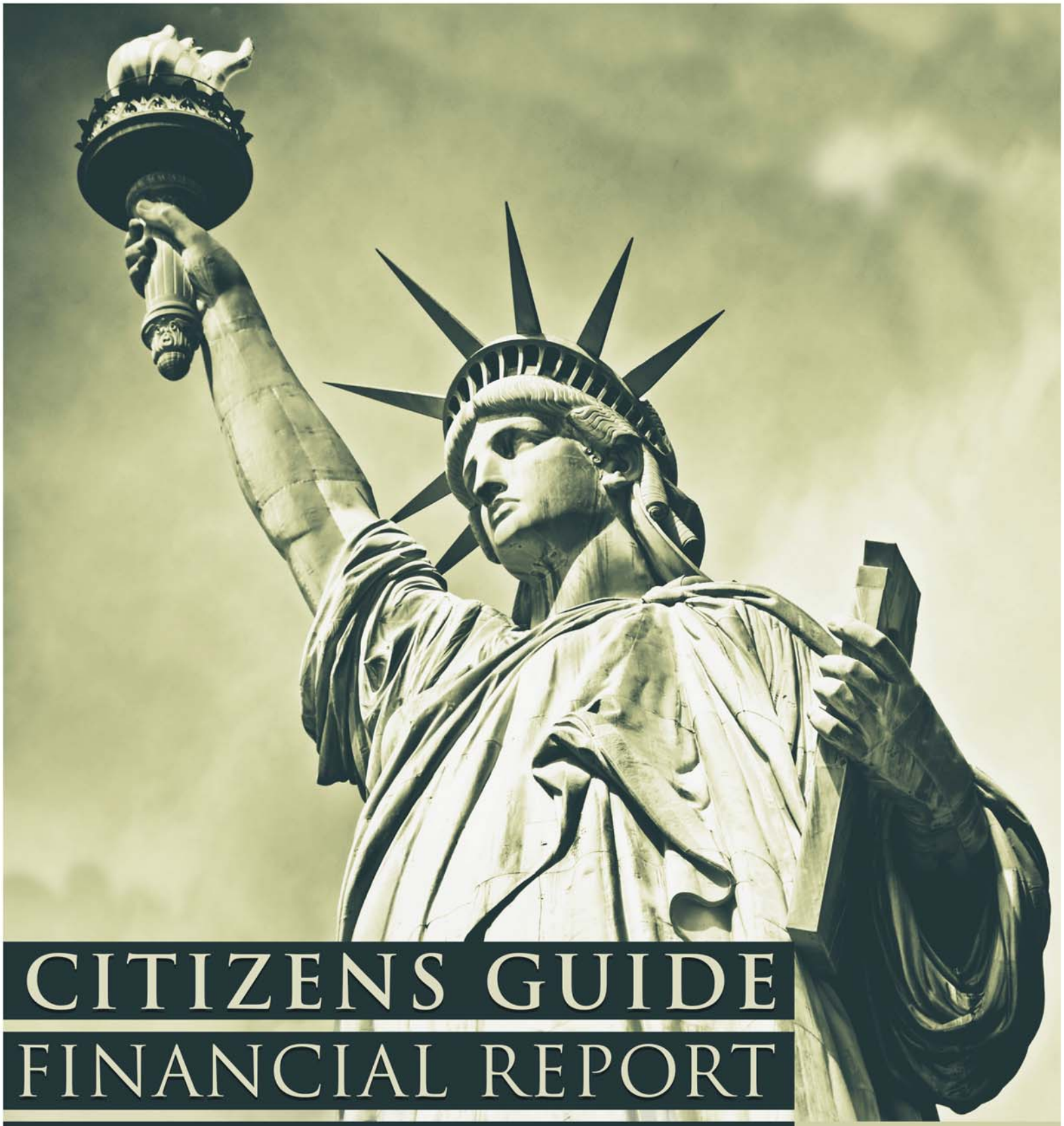


CITIZENS GUIDE FINANCIAL REPORT OF THE UNITED STATES GOVERNMENT

FY 2016

Citizen's Guide to the Fiscal Year 2016 Financial Report of the United States Government

The Citizen's Guide to the Fiscal Year 2016 *Financial Report* of the U.S. Government (*Financial Report*) summarizes the U.S. Government's current financial position and condition, and discusses key financial topics, including fiscal sustainability. This Guide and the *Financial Report* are produced by the U.S. Department of the Treasury in coordination with the Office of Management and Budget (OMB) of the Executive Office of the President. The Secretary of the Treasury, Director of OMB, and Comptroller General of the United States at the Government Accountability Office believe that the information discussed in this Guide is important to all Americans.

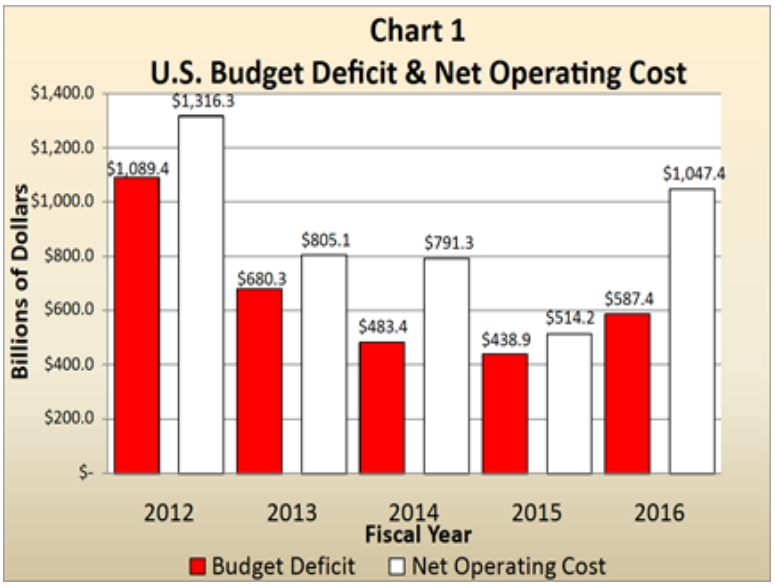
Where We Are Now

Comparing the Budget and the Financial Report

Together, the ***Budget of the United States Government* (*Budget*)** and the ***Financial Report of the U.S. Government (Financial Report)*** present complementary perspectives on the Government's financial position and condition.

- The *Budget* is the Government's primary financial planning and control tool. It accounts for past Government receipts and spending, and presents the President's proposed receipts and spending plan. The *Budget* focuses on *receipts*, or cash received by the U.S. Government (*Government*) and *outlays*, or payments made by the Government to the public. An excess of receipts over outlays is called a budget *surplus*; an excess of outlays over receipts is called a budget *deficit*.
- The *Financial Report* focuses on the Government's costs and revenues (what went out and what came in), assets and liabilities (what it owns and owes), and other important financial information. The *Financial Report* compares the Government's *revenues* (amounts earned, but not necessarily collected), with its *costs* (amounts incurred, but not necessarily paid) to derive net operating cost.

Chart 1 compares the Government's budget deficit (receipts vs. outlays) and net operating cost (revenues vs. costs) for Fiscal Years (FY) 2012 - 2016.

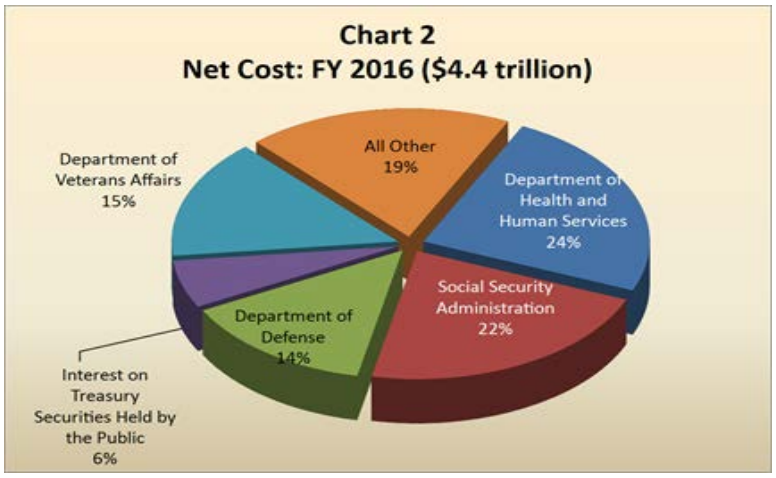


During FY 2016:

- A $166.5 billion increase in outlays was offset slightly by an $18.0 billion increase in receipts to increase the budget deficit by $148.5 billion (about 33.8 percent) to $587.4 billion.
- Net operating cost more than doubled by $533.2 billion or 103.7 percent to $1.0 trillion, due largely to a $551.1 billion increase in net cost, offset by a slight $11.3 billion increase in tax and other revenues.
- The $460.0 billion difference between the budget deficit and net operating cost is primarily due to accrued costs (incurred but not necessarily paid) associated with increases in estimated federal employee and veteran benefits liabilities and certain other liabilities that are included in net operating cost, but not the budget deficit.

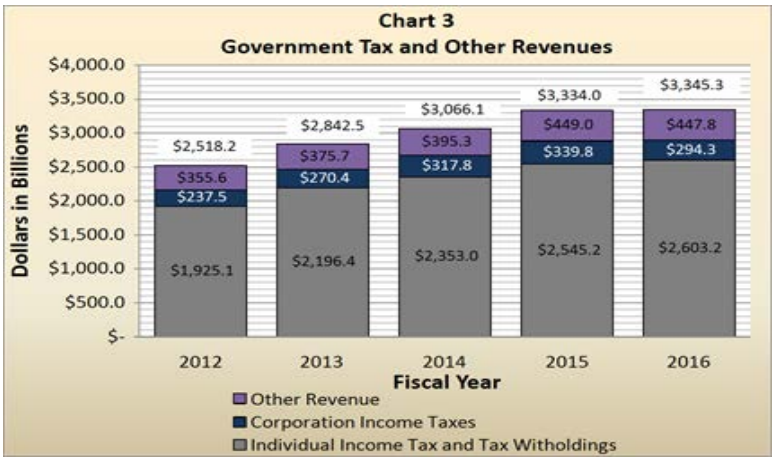
What Went Out and What Came In

The Government's "bottom line" net operating cost (Net cost of Government operations less tax and other revenues with some adjustments) more than doubled, increasing $533.2 billion (103.7 percent) during FY 2016 to $1.0 trillion. It is calculated as follows:



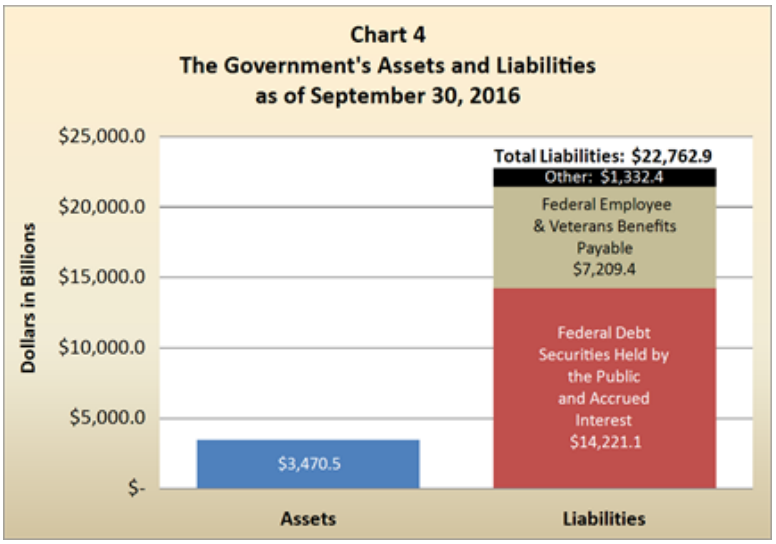
- Starting with total gross costs of $4.5 trillion, the government subtracts earned program revenues (e.g., Medicare premiums, national park entry fees, and postal service fees) and adjusts the balance for gains or losses from changes in actuarial assumptions used to estimate future liabilities for federal employee and veterans benefits to derive its net cost of $4.4 trillion, an increase of $551.1 billion (14.3 percent) from FY 2015. This net increase is the combined effect of many offsetting increases and decreases across the Government. For example:
    - Agencies administering federal employee and veterans benefits programs employ a complex series of assumptions, including but not limited to interest rates, beneficiary eligibility, life expectancy, and medical cost levels, to make actuarial projections of their long-term benefits liabilities. Across the government, the total increase in net actuarial loss (net cost increase) from assumption changes of $292.6 billion was composed largely of a $390.5 billion actuarial loss increase recorded by the Department of Veterans Affairs (VA) due largely to increases in estimates of future compensation cases. This loss was partially offset by an actuarial gains increase (net cost decrease) of $64.2 billion and $30.1 billion recorded by the Office of Personnel Management (OPM) and the Department of Defense (DOD), respectively. VA costs increased by an additional $83 billion due to actual results differing from the prior year's actuarial projections.
    - Department of Health and Human Services (HHS) and Social Security Administration (SSA) net costs increased $44.8 billion and $37.1 billion, respectively, largely due to increases in benefit expenses from the social insurance programs administered by those agencies (e.g., Medicare, Social Security). DOD net costs increased by $47.3 billion due largely to increases in costs for operations readiness and support, as well as military retirement benefits. Chart 2 shows that the largest shares of the Government's total FY 2016 net cost came from HHS, SSA, VA, and DOD.

- The Government deducts tax and other revenues from its net cost (with some adjustments) to derive its "bottom line" net operating cost of $1.0 trillion.
    - From Chart 3, total Government tax and other revenues grew by $11.3 billion (0.3 percent) to more than $3.3 trillion for FY 2016.
    - Together, individual income tax and tax withholdings, and corporation taxes accounted for about 86.6 percent of total tax and other revenues in FY 2016. Other revenues include Federal Reserve earnings, excise taxes, and customs duties.



What We Own and What We Owe

Chart 4 summarizes what the Government owns in assets and what it owes in liabilities. As of September 30, 2016:



- The Government held about $3.5 trillion in assets (mostly $1.3 trillion in net loans receivable (primarily student loans) and $979.5 billion in net property, plant, and equipment).
    - Beyond these assets, other significant Government resources not reported on the balance sheet include stewardship assets, natural resources, and the Government's power to tax and set monetary policy.
- Total liabilities ($22.8 trillion) consist mostly of: (1) $14.2 trillion in federal debt securities held by the public and accrued interest and (2) $7.2 trillion in federal employee and veteran benefits payable.
    - The "public" consists of individuals, corporations, state and local governments, Federal Reserve Banks, foreign governments, and other entities outside the federal government.
- The Government also reports about $5.5 trillion of intragovernmental debt outstanding, which arises when one part of the Government borrows from another.
    - For example, Government funds (e.g., Social Security and Medicare trust funds) typically must invest excess annual receipts in Treasury-issued federal debt securities, creating trust fund assets and Treasury liabilities. These amounts are included in the financial statements of investing agencies and Treasury, respectively, but offset each other when consolidated into the governmentwide financial statements. Thus, they are not reflected in Chart 4.

Debt held by the public plus intragovernmental debt equals gross federal debt, which, with some adjustments, is subject to a statutory debt ceiling ("debt limit"). Increasing or suspending the debt limit does not increase spending or authorize new spending; rather, it permits the Government to continue to honor pre-existing commitments. Congress suspended the debt limit during FY 2015 and FY 2016: Public Law (P.L.) 113-83 suspended the debt limit from February 15, 2014 through March 15, 2015; and P.L. 114-74 suspended it again from November 2, 2015 through March 15, 2017. The debt limit was last raised to $18.1 trillion in March 2015. When delays in raising the debt limit occur, as they did during both fiscal years 2015 and 2016, Treasury implements "extraordinary measures," on a temporary basis, to enable the Government to protect the full faith and credit of the United States by continuing to pay the Nation's bills.

As budget deficits continue to occur, the Government will have to continue to borrow from the public. Instances where the debt held by the public increases faster than the economy for extended periods can pose challenges to the sustainability of current fiscal policy.

Considering key macroeconomic indicators can help place the discussion of the Government's financial results in a broader context. During FY 2016 the economy continued to grow, job growth accelerated, and the unemployment rate declined. These and other economic and financial developments are discussed in greater detail in the *Financial Report*.

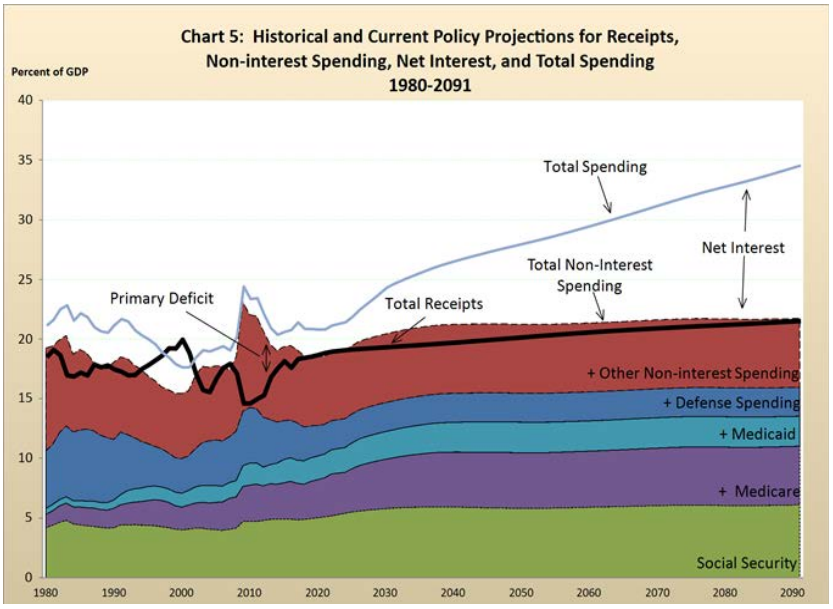
Where We Are Headed

An important purpose of this Guide and the *Financial Report* is to help citizens understand current fiscal policy and the importance and magnitude of policy reforms necessary to make it sustainable. A sustainable policy is one where the ratio of debt held by the public to Gross Domestic Product (GDP) (the debt-to-GDP ratio) is stable or declining over the long term. GDP measures the size of the Nation's economy in terms of the total value of all final goods and services that are produced in a year. Considering financial results relative to GDP is a useful indicator of the economy's capacity to sustain the Government's many programs.

To determine if current fiscal policy is sustainable, the projections discussed in this Guide assume current policy will continue indefinitely and draw out the implications for the growth of the debt-to-GDP ratio.[1] The projections are therefore neither forecasts nor predictions. As policy changes are enacted, actual financial outcomes will be different than those projected.

Receipts, Spending, and the Debt

Chart 5 shows historical and current policy projections for receipts, non-interest spending by major category, and total spending expressed as a percent of GDP.



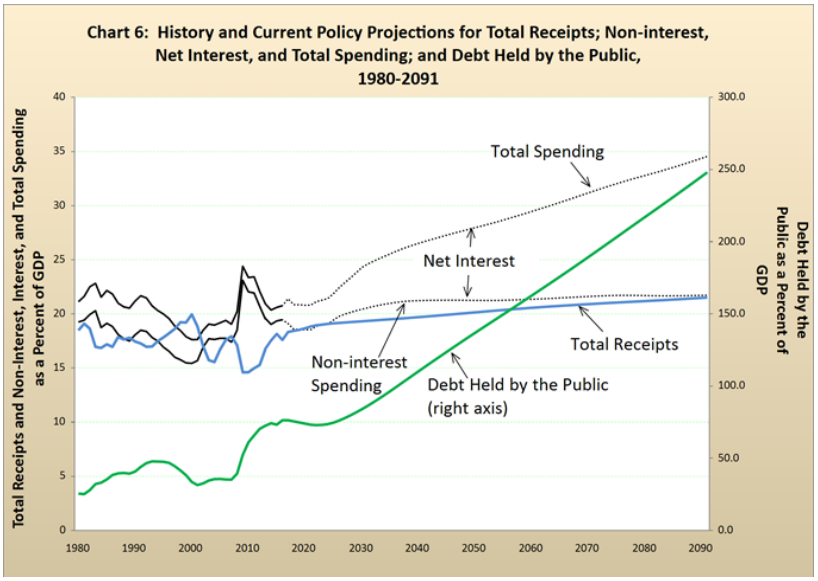
- The difference between the receipts and non-interest spending shares of GDP (the primary deficit-to-GDP ratio) grew rapidly in 2009 due to the financial crisis, the recession, and the policies pursued to combat both. The ratio remained high from 2010 to 2012, despite shrinking in each successive year, and fell significantly in 2013 and 2014.
- The primary deficit is projected to shrink further in the next few years as spending limits called for in the *Budget Control Act* (BCA) continue and the economy continues to recover, becoming a surplus starting in 2020 that peaks at 0.3 percent of GDP in 2021.
- After 2021, however, increased spending for Social Security and health programs[2] due to the continued retirement of the baby boom generation and increases in the price of health care services is expected to cause primary surpluses to steadily deteriorate and become a primary deficit starting in 2025 that reaches 1.0 percent of GDP by 2029 and peaks at 1.6 percent of GDP in 2038. After 2038, the aging of the population continues at a slower pace, causing the primary deficit to gradually decrease to 0.2 percent of GDP in 2091.

[1] Current policy in the projections is based on current law, but includes extension of certain policies that expire under current law but are routinely extended or otherwise expected to continue.

[2] The 2016 Medicare Trustees Report projects that the Hospital Insurance (HI) Trust Fund will remain solvent until 2028 (two years earlier than noted in last year's report), at which point, HI revenues are projected to cover 87 percent of program costs. This percentage is projected to decrease to 79 percent in 2040, and then increase to about 86 percent by the end of the projection period. As for Social Security, under current law, the Old-Age, Survivors, and Disability Insurance (OASDI) Trust Fund reserves, considered on a theoretical combined basis, are projected to be depleted in 2034 (unchanged from last year's Financial Report), at which time the projected share of scheduled benefits payable from trust fund income is 79 percent, decreasing to about 74 percent by 2090. The Disability Insurance (DI) Trust Fund alone is projected to become depleted by the end of 2023, at which time 89 percent of scheduled benefits would be payable, rising to a somewhat higher level through 2040, then declining to 82 percent by 2090. The projections assume full Social Security and Medicare benefits are paid after the corresponding trust funds are exhausted. See the 2016 Trustees Report for Medicare (pp 5, 29) and Social Security (pp 3, 6, 13, 24).

- In these projections, the *Affordable Care Act* (ACA)[3] provision of health insurance subsidies and expanded Medicaid coverage boosts federal spending, and other ACA provisions significantly reduce per-beneficiary Medicare cost growth.
- Overall, the ACA is projected to substantially reduce the growth rate of federal expenditures for Medicare over the next 75 years. However, as noted in the *Financial Report*, there is uncertainty about the extent to which the ACA's provisions will result in reduced health care cost growth. Even if those provisions work as intended and as assumed in these projections, Chart 5 still shows a persistent gap between projected receipts and total spending.

The primary deficit projections in Charts 5 and 6 (left axis), along with those for interest rates and GDP, determine the debt-to-GDP ratio projections shown in Chart 6 (right axis).



- The debt-to-GDP ratio was 77 percent at the end of FY 2016, and under the long-term fiscal projections of current policy is projected to be 71 percent in 2026, 122 percent in 2046, and 252 percent in 2091. The debt-to-GDP ratio rises at an accelerating rate despite primary deficits that flatten out because higher levels of debt lead to higher net interest expenditures, and higher net interest expenditures lead to higher debt. The continuous rise of the debt-to-GDP ratio after 2026 indicates that current policy is unsustainable.
- These debt-to-GDP projections are generally higher than the corresponding projections in the FY 2015 *Financial Report*, but still lower than those in the FY 2014 *Financial Report*. For example, the debt-to-GDP projection for 2089 (the final projection year for the 2014 report) is 246 percent in this year's *Financial Report*, was 220 percent in the FY 2015 *Financial Report*, and was 321 percent in the FY 2014 *Financial Report*.

The Fiscal Gap and the Cost of Delaying Policy Reform

- It is estimated that preventing the debt-to-GDP ratio from rising over the next 75 years would require some combination of spending reductions and receipt increases that amount to 1.6 percent of GDP on average over the next 75 years, 0.4 percentage points greater than the 1.2 percent estimate in 2015.
- The timing of changes to non-interest spending and receipts that close this "75-year fiscal gap" has important implications for the well-being of future generations.
  - For example, relative to a policy that begins immediately, if action is delayed by 10 years, it is estimated that the magnitude of reforms necessary to close the 75-year fiscal gap will increase by about 18 percent; if action is delayed by 20 years, the magnitude of reforms necessary will increase by about 50 percent.
  - If policy changes in the near term were to go in the reverse direction, by reducing revenues and/or increasing spending, the policy changes needed to close the fiscal gap would be made all the larger.

[3] The ACA refers to P.L. 111-148, as amended by P.L. 111-152. The ACA expands health insurance coverage, provides health insurance subsidies for low-income individuals and families, includes many measures designed to reduce health care cost growth, and significantly reduces Medicare payment rates relative to the rates that would have occurred in the absence of the ACA. (See Note 22 and the Required Supplementary Information section of the Financial Report, and the 2015 Medicare Trustees Report for more information).

- Future generations are harmed by a policy delay of this sort because the higher the primary surpluses are during their lifetimes, the greater is the difference between the taxes they pay and the programmatic spending from which they benefit.

Conclusion

- The Government took significant steps towards fiscal sustainability by enacting the ACA in 2010, the BCA in 2011, and the *American Taxpayer Relief Act* (ATRA) in 2013. The ACA holds the prospect of lowering long-term per beneficiary spending growth for Medicare and Medicaid, the BCA significantly curtails discretionary spending, and ATRA increased revenues. Together, these three laws substantially reduce the estimated long-term fiscal gap.
- But even after enactment of these laws, the Government's debt-to-GDP ratio is projected to remain relatively flat over the next ten years, and then commence a continuous rise over the remaining projection period and beyond if current policy is kept in place. This trend implies that current policy is not sustainable.
- Subject to the important caveat that changes in policy are not so abrupt that they slow continued economic growth, the sooner policies are put in place to avert these trends, the smaller the revenue increases and/or spending decreases will need to be to return the Government to a sustainable fiscal path.
- If policies are put in place in the near term that increase the fiscal gap, then even more dramatic fiscal adjustments will be necessary in the future.

The Nation By The Numbers

The *Financial Report* provides the President, Congress, and the American people a comprehensive view of how the Government is managing taxpayer dollars. It discusses the Government's financial position and condition, its revenues and costs, assets and liabilities, and other responsibilities and commitments, as well as important financial issues that affect the nation and its citizens both now and in the future. The table on the following page presents several key indicators of the Government's financial position and condition, which are summarized in this Guide and discussed in greater detail in the *Financial Report*.

The Government Accountability Office's (GAO) audit report on the U.S. Government's consolidated financial statements can be found beginning on page 237 of the full *Financial Report*. For the reasons discussed below, GAO was prevented from expressing (disclaimed) an opinion on these consolidated financial statements. GAO disclaimed an opinion on the 2016 and 2015 Statements of Long-Term Fiscal Projections; the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance (SOSI); and the 2016 and 2015 Statements of Changes in Social Insurance Amounts because of significant uncertainties (discussed in Note 22 in the *Financial Report*) primarily related to the achievement of projected reductions in Medicare cost growth and certain other limitations. In addition, GAO disclaimed an opinion on the remaining FY 2016 and 2015 financial statements in the *Financial Report* due to certain material financial reporting control weaknesses and other limitations on the scope of its work.

NATION BY THE NUMBERS

A Snapshot of The Government's Financial Position & Condition

	2016	2015*
Financial Measures (Dollars in Billions):		
Gross Costs	**$ (4,507.7)**	**$ (4,248.2)**
Less: Earned Revenue	$ 376.6	$ 375.6
Gain/(Loss) from Changes in Assumptions	$ (273.3)	$ 19.3
Net Cost	**$ (4,404.4)**	**$ (3,853.3)**
Less: Total Tax and Other Revenues	**$ 3,345.3**	**$ 3,334.0**
Unmatched Transactions and Balances[1]	$ 11.7	$ 5.1
Net Operating Cost	**$ (1,047.4)**	**$ (514.2)**
Assets:	**$ 3,470.5**	**$ 3,261.2**
Less: Liabilities, comprised of:		
Debt Held By the Public & Accrued Interest	$ (14,221.1)	$ (13,172.5)
Federal Employee & Veteran Benefits	$ (7,209.4)	$ (6,772.4)
Other	$ (1,332.4)	$ (1,559.9)
Total Liabilities	**$ (22,762.9)**	**$ (21,504.8)**
Net Position (Assets Less Liabilities)	**$ (19,292.4)**	**$ (18,243.6)**
Sustainability Measures (Dollars in Trillions):		
Social Insurance Net Expenditures[2]	$ (46.7)	$ (41.5)
Total Non-Interest Net Expenditures[3]	$ (10.6)	$ (4.1)
Sustainability Measures as Percent of Gross Domestic Product (GDP)[4]:		
Social Insurance Net Expenditures	(3.8%)	(3.7%)
Total Non-Interest Net Expenditures	(0.8%)	(0.3%)
Budget Results (Dollars in Billions)		
Unified Budget Deficit	**$ (587.4)**	**$ (438.9)**

*2015 amounts restated. See Financial Statement Notes 1V, 6, and 12.

1 Reflects adjustments made to bring certain accounts into balance for such items as restatements and errors in federal agency reporting and unreconciled intragovernmental transactions and balances among agencies.

2 Source: Statement of Social Insurance. Amounts equal present value of projected revenues and expenditures for scheduled benefits over the next 75 years of certain benefit programs that are referred to as Social Insurance (e.g., Social Security, Medicare). Amounts represent 'open group' population (all current and future beneficiaries). These amounts are not considered liabilities on the balance sheet.

3 Source: Statement of Long-Term Fiscal Projections. Represents the 75-year projection of the federal government's receipts less non-interest spending.

4 GDP values used represent the average of 75-year present value of nominal GDP for 2016 and 2015 based on the Social Security and Medicare Trustees Reports.

Find Out More

The *2016 Financial Report of the United States Government* and other information about the nation's finances are available at:

- U.S. Department of the Treasury, http://www.fiscal.treasury.gov/fsreports/rpt/finrep/fr/fr_index.htm;
- OMB's Office of Federal Financial Management, http://www.whitehouse.gov/omb/financial/index.html; and
- GAO, http://www.gao.gov/financial.html.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The Fiscal Year (FY) *2016 Financial Report of the United States Government (Financial Report)* provides the President, Congress, and the American people with a comprehensive view of the federal government's finances, i.e., its financial position and condition, its revenues and costs, assets and liabilities, and other obligations and commitments. The *Financial Report* also discusses important financial issues and significant conditions that may affect future operations, including the need to achieve fiscal sustainability over the medium and long term.

Pursuant to 31 U.S.C. § 331(e)(1), the Department of the Treasury (Treasury), in cooperation with the Office of Management and Budget (OMB), must submit an audited (by the Government Accountability Office or GAO) financial statement for the preceding fiscal year, covering all accounts and associated activities of the executive branch of the United States Government[1] – the central component of the *Financial Report* – to the President and Congress no later than six months after the September 30 fiscal year end. To encourage timely and relevant reporting, OMB accelerated both individual agency and governmentwide reporting deadlines.

The *Financial Report* is prepared from the audited financial statements of specifically designated federal agencies, including the Cabinet departments and many smaller, independent agencies (see organizational chart on the next page). As it has for the past nineteen years, GAO issued a "disclaimer" of opinion on the accrual-based, consolidated financial statements for the fiscal years ended September 30, 2016 and 2015. GAO also issued disclaimers of opinion on the 2016 and 2015 Statements of Long-Term Fiscal Projections (SLTFP); the 2016, 2015, 2014, 2013 and 2012 Statements of Social Insurance (SOSI); and the 2016 and 2015 Statements of Changes in Social Insurance Amounts (SCSIA). A disclaimer of opinion indicates that sufficient information was not available for the auditors to determine whether the reported financial statements were fairly presented in accordance with Generally Accepted Accounting Principles (GAAP). In FY 2016, 32[2] of the 39 most significant agencies earned unmodified opinions on their financial statement audits.

The FY 2016 *Financial Report* consists of:

- Management's Discussion and Analysis (MD&A), which provides management's perspectives on and analysis of information presented in the *Financial Report*, such as financial and performance trends;
- Principal financial statements and the related notes to the financial statements;
- Required Supplementary Information (RSI), Required Supplementary Stewardship Information (RSSI), and Other Information; and
- GAO's audit report.

In addition, a Citizen's Guide is included to provide the American taxpayer with a quick reference to the key issues in the *Financial Report* and an overview of the Government's financial position and condition.

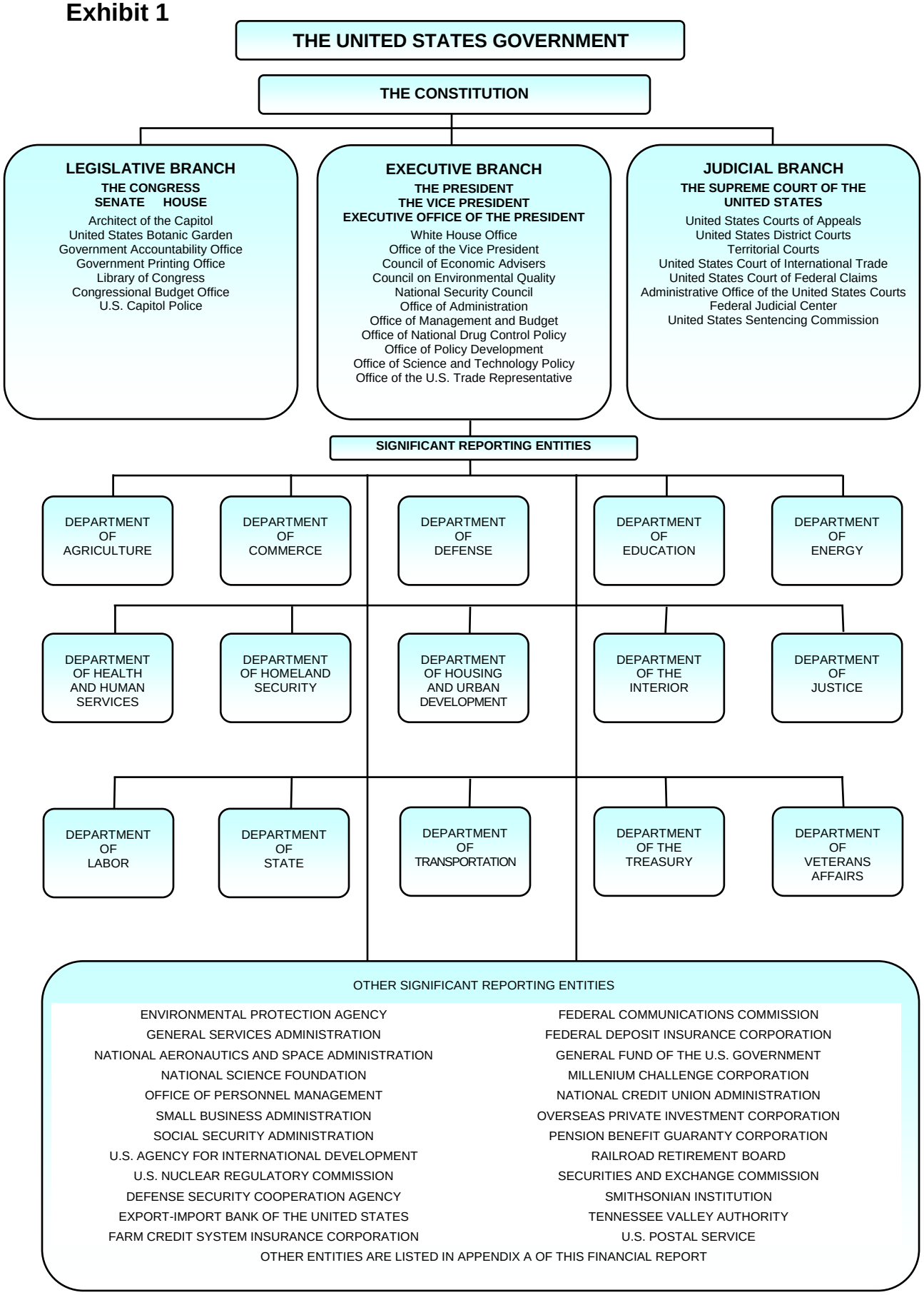
Mission & Organization

The Government's fundamental mission is derived from the Constitution: ***"…to form a more perfect union, establish justice, insure domestic tranquility, provide for the common defense, promote the general welfare and secure the blessings of liberty to ourselves and our posterity."*** Congress authorizes and agencies implement programs as missions and initiatives evolve over time in pursuit of key public services and objectives, such as providing for national defense, promoting affordable health care, fostering income security, boosting agricultural productivity, providing veterans benefits and services, facilitating commerce, supporting housing and the transportation systems, protecting the environment, contributing to the security of energy resources, and helping States provide education. Exhibit 1 provides an overview of how the U.S. Government (Government) is organized.

[1] The *Government Management Reform Act* of 1994 has required such reporting, covering the executive branch of the Government, beginning with financial statements prepared for FY 1997. Treasury and OMB have elected to include certain financial information on the legislative and judicial branches in consolidated financial statements as well.

[2] The 32 agencies include the Department of Health and Human Services, which received disclaimers of opinion on its 2015, 2014, 2013, 2012, and 2011 SOSI and on its 2016 and 2015 SCSIA and the Department of Labor, which received disclaimers of opinion on its 2016 SOSI and SCSIA.

Exhibit 1


THE UNITED STATES GOVERNMENT
THE CONSTITUTION
LEGISLATIVE BRANCH
THE CONGRESS
SENATE HOUSE
Architect of the Capitol
United States Botanic Garden
Government Accountability Office
Government Printing Office
Library of Congress
Congressional Budget Office
U.S. Capitol Police
EXECUTIVE BRANCH
THE PRESIDENT
THE VICE PRESIDENT
EXECUTIVE OFFICE OF THE PRESIDENT
White House Office
Office of the Vice President
Council of Economic Advisers
Council on Environmental Quality
National Security Council
Office of Administration
Office of Management and Budget
Office of National Drug Control Policy
Office of Policy Development
Office of Science and Technology Policy
Office of the U.S. Trade Representative
JUDICIAL BRANCH
THE SUPREME COURT OF THE UNITED STATES
United States Courts of Appeals
United States District Courts
Territorial Courts
United States Court of International Trade
United States Court of Federal Claims
Administrative Office of the United States Courts
Federal Judicial Center
United States Sentencing Commission
SIGNIFICANT REPORTING ENTITIES
DEPARTMENT OF AGRICULTURE
DEPARTMENT OF COMMERCE
DEPARTMENT OF DEFENSE
DEPARTMENT OF EDUCATION
DEPARTMENT OF ENERGY
DEPARTMENT OF HEALTH AND HUMAN SERVICES
DEPARTMENT OF HOMELAND SECURITY
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
DEPARTMENT OF THE INTERIOR
DEPARTMENT OF JUSTICE
DEPARTMENT OF LABOR
DEPARTMENT OF STATE
DEPARTMENT OF TRANSPORTATION
DEPARTMENT OF THE TREASURY
DEPARTMENT OF VETERANS AFFAIRS
OTHER SIGNIFICANT REPORTING ENTITIES
ENVIRONMENTAL PROTECTION AGENCY
GENERAL SERVICES ADMINISTRATION
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION
NATIONAL SCIENCE FOUNDATION
OFFICE OF PERSONNEL MANAGEMENT
SMALL BUSINESS ADMINISTRATION
SOCIAL SECURITY ADMINISTRATION
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
U.S. NUCLEAR REGULATORY COMMISSION
DEFENSE SECURITY COOPERATION AGENCY
EXPORT-IMPORT BANK OF THE UNITED STATES
FARM CREDIT SYSTEM INSURANCE CORPORATION
FEDERAL COMMUNICATIONS COMMISSION
FEDERAL DEPOSIT INSURANCE CORPORATION
GENERAL FUND OF THE U.S. GOVERNMENT
MILLENIUM CHALLENGE CORPORATION
NATIONAL CREDIT UNION ADMINISTRATION
OVERSEAS PRIVATE INVESTMENT CORPORATION
PENSION BENEFIT GUARANTY CORPORATION
RAILROAD RETIREMENT BOARD
SECURITIES AND EXCHANGE COMMISSION
SMITHSONIAN INSTITUTION
TENNESSEE VALLEY AUTHORITY
U.S. POSTAL SERVICE
OTHER ENTITIES ARE LISTED IN APPENDIX A OF THIS FINANCIAL REPORT

The Government's Financial Position and Condition

A complete assessment of the Government's financial condition requires analysis of historical results, projections of future revenues and expenditures, and an assessment of the Government's long-term fiscal sustainability. This *Financial Report* discusses the Government's financial position at the end of the fiscal year, explains how and why the financial position changed during the year, and gives insight into how the Government's financial condition may change in the future

Table 1
The Federal Government's Financial Position and Condition

	2016	2015*	Increase / (Decrease) $	Increase / (Decrease) %
FINANCIAL MEASURES (Dollars in Billions)				
Gross Cost	**$ (4,507.7)**	**$ (4,248.2)**	**$ 259.5**	**6.1%**
Less: Earned Revenue	$ 376.6	$ 375.6	$ 1.0	0.3%
Gain/(Loss) from Changes in Assumptions	$ (273.3)	$ 19.3	$ (292.6)	(1516.1%)
Net Cost[1]	**$ (4,404.4)**	**$ (3,853.3)**	**$ 551.1**	**14.3%**
Less: Tax and Other Revenues	$ 3,345.3	$ 3,334.0	$ 11.3	0.3%
Unmatched Transactions & Balances	$ 11.7	$ 5.1	$ 6.6	129.4%
Net Operating Cost[2]	**$ (1,047.4)**	**$ (514.2)**	**$ 533.2**	**103.7%**
Assets[3]:				
Cash & Other Monetary Assets	$ 464.6	$ 305.1	$ 159.5	52.3%
Loans Receivable, Net	$ 1,277.6	$ 1,216.0	$ 61.6	5.1%
Inventories & Related Property, Net	$ 314.3	$ 320.6	$ (6.3)	(2.0%)
Property, Plant & Equipment, Net	$ 979.5	$ 925.3	$ 54.2	5.9%
Other	$ 434.5	$ 494.2	$ (59.7)	(12.1%)
Total Assets	**$ 3,470.5**	**$ 3,261.2**	**$ 209.3**	**6.4%**
Liabilities[3] :				
Federal Debt Held by the Public & Accrued Interest	$ (14,221.1)	$ (13,172.5)	$ 1,048.6	8.0%
Federal Employee & Veterans Benefits	$ (7,209.4)	$ (6,772.4)	$ 437.0	6.5%
Other	$ (1,332.4)	$ (1,559.9)	$ (227.5)	(14.6%)
Total Liabilities	**$ (22,762.9)**	**$ (21,504.8)**	**$ 1,258.1**	**5.9%**
Net Position (Assets minus Liabilities)	**$ (19,292.4)**	**$ (18,243.6)**	**$ 1,048.8**	**5.7%**
SUSTAINABILITY MEASURES (Dollars in Trillions)				
Social Insurance Net Expenditures[4]:				
Social Security (OASDI)	$ (14.1)	$ (13.4)	$ 0.7	5.2%
Medicare (Parts A, B, & D)	$ (32.5)	$ (28.0)	$ 4.5	16.1%
Other	$ (0.1)	$ (0.1)	$ 0.0	0.0%
Total Social Insurance Net Expenditures	**$ (46.7)**	**$ (41.5)**	**$ 5.2**	**12.5%**
Total Non-Interest Net Expenditures[5]	**$ (10.6)**	**$ (4.1)**	**$ 6.5**	**158.5%**
BUDGET DEFICIT (Dollars in Billions)				
Unified Budget Deficit[6]	**$ (587.4)**	**$ (438.9)**	**$ 148.5**	**33.8%**

*2015 amounts restated. See Financial Statement Notes 1V, 6, and 12.

1 Source: Statements of Net Cost.

2 Source: Statements of Operations and Changes in Net Position.

3 Source: Balance Sheet.

4 Source: Statements of Social Insurance (SOSI). Amounts equal estimated present value of projected revenues and expenditures for scheduled benefits over the next 75 years of certain 'Social Insurance' programs (Social Security, Medicare Parts A, B, & D, Railroad Retirement - Black Lung is projected through 2040). Amounts reflect 'Open Group' totals (all current and projected program participants during the 75-year projection period).

5 Represents the 75-year projection of the federal government's receipts less non-interest spending as reported in the Statements of Long-Term Fiscal Projections.

6 Source: Final Monthly Treasury Statement (as of 9/30/2016 and 9/30/2015).

Note: Totals may not equal sum of components due to rounding.

Table 1 on the previous page and the following summarize the federal government's financial position:

- The Government's gross costs increased by $259.5 billion or 6.1 percent to $4.5 trillion. Deducting $376.6 billion in revenues earned for goods and services provided to the public (e.g., Medicare premiums, national park entry fees, and postal service fees) and adding $273.3 billion in net losses from changes in assumptions (e.g., interest rates, inflation, disability claims rates) results in the Government's net cost of $4.4 trillion in FY 2016 an increase of $551.1 billion or 14.3 percent from FY 2015.
- Tax and other revenues increased slightly by $11.3 billion or 0.3 percent to $3.3 trillion, which, when offset against the Government's net cost, with some adjustment for unmatched transactions and balances, results in a "bottom line" net operating cost of $1.0 trillion for FY 2016, more than double FY 2015's net operating cost, increasing $533.2 billion or 103.7 percent).
- Comparing total 2016 Government assets of $3.5 trillion to total liabilities of $22.8 trillion (comprised mostly of $14.2 trillion in federal debt held by the public and accrued interest payable[3], and $7.2 trillion of federal employee and veterans benefits payable) yields a negative net position of $19.3 trillion.
- The sum of debt held by the public excluding accrued interest ($14.2 trillion), and intragovernmental debt ($5.5 trillion) equals gross federal debt, which, with some adjustments, is subject to the statutory debt limit. As of September 30, 2016, the Government's total debt subject to the debt limit was $19.5 trillion. The statutory debt limit was suspended for portions of both fiscal years 2016 and 2015. The *Temporary Debt Limit Extension Act* (P.L. 113-83), enacted on February 15, 2014, suspended the statutory debt limit through March 15, 2015. The *Bipartisan Budget Act of 2015* (P.L. 114-74), enacted on November 2, 2015, suspended the statutory debt limit through March 15, 2017.

This *Financial Report* also contains information about potential impacts on the Government's future financial condition. Under federal accounting rules, social insurance spending as reported in the Statement of Long-Term Fiscal Projections (SLTFP); and social insurance expenditures, as reported in the Statement of Social Insurance (SOSI) are not considered liabilities of the Government. They can, however, provide a valuable perspective on the sustainability of the Government's fiscal path:

- Total projected spending, including other major programs (e.g., defense, Medicaid, and education) and tax revenues provide another perspective of the Government's projected fiscal condition. From the SLTFP, over the next 75 years, under current policy, the present value (PV) of the Government's total non-interest spending (including its social insurance programs) is projected to exceed the PV of total receipts by $10.6 trillion.
- The SOSI compares the actuarial present value[4] of the Government's projected expenditures for scheduled benefits for Social Security, Medicare Parts A, B and D, and other social insurance programs over 75 years[5] to a subset of the revenues[6] supporting these programs. For 2016, these projected expenditures exceeded projected revenues by about $46.7 trillion, a $5.2 billion increase from 2015 social insurance projections.
- The bottom line of the SLTFP differs from the bottom line of the SOSI, primarily due to the inclusion in the SLTFP of general revenues and spending other than on social insurance programs, which are not included in the SOSI.

The Government's current financial position and long-term financial condition can be evaluated both in dollar terms and in relation to the economy as a whole. Gross Domestic Product (GDP) measures the size of the nation's economy in terms of the total value of all final goods and services that are produced in a year. Considering financial results relative to GDP is a useful indicator of the economy's capacity to sustain the Government's many programs. For example:

- The unified budget deficit (i.e., including the consolidated receipts and outlays from federal funds and the Social Security Trust Fund) increased from $438.9 billion or 2.5 percent of GDP in FY 2015 to $587.4 billion or 3.2 percent of GDP in FY 2016. The deficit-to-GDP ratio has declined by about two-thirds since 2009 – and is equal to the average of the last 40 years.[7]
- The budget deficit is primarily financed through borrowing from the public. As of September 30, 2016, debt held by the public, excluding accrued interest, was $14.2 trillion (about 77 percent of GDP).
- The 2016 SOSI projection of $46.7 trillion net present value excess of expenditures over receipts over 75 years represents about 3.8 percent of the present value of GDP over 75 years. The excess of total projected non-interest spending over receipts of $10.6 trillion from the SLTFP represents 0.8 percent of GDP over 75 years. As discussed

[3] On the Government's balance sheet, debt held by the public and accrued interest payable consists of Treasury securities, net of unamortized discounts and premiums, and accrued interest payable. The "public" consists of individuals, corporations, state and local governments, Federal Reserve Banks, foreign governments, and other entities outside the federal government.

[4] Present values recognize that a dollar paid or collected in the future is worth less than a dollar today because a dollar today could be invested and earn interest. To calculate a present value, future amounts are thus reduced using an assumed interest rate, and those reduced amounts are summed.

[5] The Black Lung Program is projected through September 30, 2040.

[6] Social Security is funded by the payroll taxes and revenue from taxation of benefits. Medicare Part A is funded by the payroll taxes, revenue from taxation of benefits, and premiums that support those programs. Medicare Parts B and D are primarily financed by general revenues and premiums. By accounting convention, general revenues transferred to Medicare Parts B and D are eliminated in consolidation at the governmentwide level and, as such, are not included in the SOSI.

[7] Final Monthly Treasury Statement (as of September 30, 2016 and 2015), 10/14/16 press release – Joint Statement of Treasury Secretary Jacob J. Lew and OMB Director Shaun Donovan on Budget Results for Fiscal Year 2016

in this *Financial Report*, these projections can, in turn, have a significant impact on projected debt as a percent of GDP.

Fiscal Year 2016 Financial Statement Audit Results

For FY 2016, GAO issued a twentieth consecutive disclaimer of audit opinion on the accrual-based, governmentwide financial statements. In addition, GAO issued disclaimers of opinion on the 2016 and 2015 SLTFP; the 2016, 2015, 2014, 2013 and 2012 SOSI; and the 2016 and 2015 SCSIA. The SOSI, SCSIA, and SLTFP disclaimers stem from significant uncertainties (discussed in Note 22, Social Insurance), primarily related to the achievement of projected reductions in Medicare cost growth and certain other limitations.

Twenty of the 24 agencies required to issue audited financial statements under the *Chief Financial Officers* (CFO) *Act* received unmodified audit opinions as did 12 of 15 additional significant reporting agencies (see Appendix A).[8]

Table 2: FY 2016 CFO Act Financial Statement Audit Results

Chief Financial Officers (CFO) Act Agency	Audit Opinion
Department of Agriculture (USDA)[1]	Unmodified / Not Audited
Department of Commerce (DOC)	Unmodified
Department of Defense (DOD)	Pending
Department of Education (Education)	Unmodified
Department of Energy (DOE)	Unmodified
Department of Health and Human Services (HHS)[2]	Unmodified
Department of Homeland Security (DHS)	Unmodified
Department of Housing and Urban Development (HUD)	Pending
Department of the Interior (DOI)	Unmodified
Department of Justice (DOJ)	Unmodified
Department of Labor (DOL)[2]	Unmodified
Department of State (State)	Unmodified
Department of Transportation (DOT)	Unmodified
Department of the Treasury (Treasury)	Unmodified
Department of Veterans Affairs (VA)	Unmodified
Agency for International Development (USAID)	Unmodified
Environmental Protection Agency (EPA)	Unmodified
General Services Administration (GSA)	Unmodified
National Aeronautics and Space Administration (NASA)	Unmodified
National Science Foundation (NSF)	Pending
Nuclear Regulatory Commission (NRC)	Unmodified
Office of Personnel Management (OPM)	Unmodified
Small Business Administration (SBA)	Unmodified
Social Security Administration (SSA)	Unmodified

1 Received unmodified opinion on Balance Sheet only. Other financial statements were not audited.
2 Received disclaimer of opinion on Statement of Social Insurance and Statement of Changes in Social Insurance Amounts.

The Governmentwide Reporting Entity

This *Financial Report* includes the financial status and activities of the executive, legislative, and judicial branches of the federal government. The legislative and judicial branches are not required by law to submit financial statement information to Treasury; however, these branches provided cash and a significant amount of accrual basis financial information to include in the *Financial Report*. Appendix A lists the organizations and agencies (entities) included in the U.S. Government's consolidated reporting entity for the *Financial Report*, as well as some entities not included in the reporting entity.

A number of entities and organizations are excluded due to the nature of their operations, including the Federal Reserve System (considered to be an independent central bank under the general oversight of Congress), all fiduciary funds, and Government-Sponsored Enterprises (GSEs), including the Federal Home Loan Banks, the Federal National Mortgage Association (Fannie Mae), and the Federal Home Loan Mortgage Corporation (Freddie Mac). Following U.S. GAAP for federal entities, the Government has not consolidated into its financial statements the assets, liabilities, or results of operations of any financial organization or commercial entity in which Treasury holds either a direct, indirect, or beneficial majority equity investment. Under Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, these entities meet the criteria of paragraph 50 and do not appear in the Federal Budget section "Federal Programs by Agency and Account." As such, these entities are not consolidated into the financial reports of the Government. However, the values of the investments in and any related liabilities to such entities are presented on the balance sheet. Appendix A includes a list of the agencies and entities contributing to this *Financial Report*.[9]

The following pages contain a more detailed discussion of the Government's financial results for FY 2016, the budget, the economy, the debt, and a long-term perspective about fiscal sustainability, including the Government's ability to meet its social insurance benefits obligations. The information in this *Financial Report*, when combined with the Budget of the U.S. Government, collectively presents information on the Government's financial position and condition.

[8] The 20 agencies include the Department of Health and Human Services, which received disclaimers of opinions on its 2016, 2015, 2014, 2013, and 2012, SOSI and its 2016 and 2015 SCSIA and the Department of Labor, which received a disclaimer of opinion on its 2016 SOSI and SCSIA. The Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), and the Farm Credit System Insurance Corporation (FCSIC) are among the 39 significant entities. However, because these entities operate on a calendar year basis (December 31 year-end), their 2016 audits are not yet complete. Statistic reflects 2015 audit results for these organizations. In addition, neither the Defense Security Cooperation Agency (DSCA) nor the General Fund of the U.S. Government were subject to audit for FY 2016.

[9] Since programs are not administered at the governmentwide level, performance goals and measures for the federal government, as a whole, are not reported here. The outcomes and results of those programs are addressed at the individual agency level and can be found in each agency's financial report. Go to www.performance.gov for more information about Government performance.

Accounting Differences Between The Budget and the Financial Report

Each year, the Administration issues two reports that detail the Government's financial results: the *Budget of the U.S. Government (Budget)*, prepared primarily on a "cash basis", and which provides a plan for future initiatives and the resources needed to support them, as well as prior year fiscal and performance results; and this *Financial Report*, which provides the President, Congress, and the American people a broad, comprehensive overview of the cost on an "accrual basis" of the Government's operations, the sources used to finance them, its balance sheet, and the overall financial outlook.

Treasury generally prepares the financial statements in this *Financial Report* on an accrual basis of accounting as prescribed by U.S. GAAP for federal entities.[10] These principles are tailored to the Government's unique characteristics and circumstances. For example, agencies prepare a uniquely structured "Statement of Net Cost," which is intended to present net Government resources used in its operations. Also, unique to Government is the preparation of separate statements to reconcile differences and articulate the relationship between the budget and financial accounting results.

Budget of the U.S. Government	Financial Report of the U.S. Government
Prepared primarily on a "*cash basis*" • Initiative-based and prospective: focus on current and future initiatives planned and how resources will be used to fund them. • Receipts ("cash in"), taxes and other collections recorded when received. • Outlays ("cash out"), largely recorded when payment is made.	Prepared on an "*accrual and modified cash basis*" • Agency-based and retrospective – prior and present resources used to implement initiatives. • Revenue: Tax revenue (more than 90 percent of total revenue) recognized on modified cash basis (see Financial Statement Note 1.B). Remainder recognized when earned, but not necessarily received. • Costs: recognized when incurred, but not necessarily paid.

Budget Deficit vs. Net Operating Cost

The Government's primarily cash-based[11] budget deficit increased by $148.5 billion (about 33.8 percent) from approximately $438.9 billion in FY 2015 to about $587.4 billion in FY 2016 due to lower growth in receipts compared to the increase in outlays in FY 2016. The $18.0 billion (0.6 percent) increase in receipts can be attributed to the expiration of numerous individual and corporation income tax preferences in January 2015, which boosted FY 2015 collections, and the subsequent retroactive extension of these provisions in legislation enacted in December 2015, which reduced FY 2016 collections. Outlays increased $166.5 billion (4.5 percent). Contributing to the dollar increase over FY 2015 was higher spending for Social Security; Medicare and Medicaid; and interest on the public debt. A portion of these increases stemmed from the fact that October 1, 2016 fell on a weekend, which accelerated the monthly benefit payments for certain programs into September, resulting in 13 monthly payments for these programs in FY 2016. Outlays also rose because receipts from the sale of spectrum licenses and dividends from government-sponsored enterprises Fannie Mae and Freddie Mac, which are recorded as offsets to spending, were lower in FY 2016 than in FY 2015 by $22 billion and $9 billion respectively.[12] The Government's largely accrual-based net operating cost also increased by $533.2 billion, (103.7 percent), from $514.2 billion to $1.0 trillion during FY 2016. As explained below, net operating costs are affected by both changes in revenues and costs.

[10] Under U.S. GAAP, most U.S. Government revenues are recognized on a 'modified cash' basis, or when they become measurable. The Statement of Social Insurance presents the present value of the estimated future revenues and expenditures for scheduled benefits over the next 75 years for the Social Security, Medicare, Railroad Retirement programs; and through September 30, 2040 for the Black Lung program. The Statement of Long-Term Fiscal Projections presents the present value of the projected future receipts and non-interest spending for the federal government.

[11] Interest outlays on Treasury debt held by the public are recorded in the budget when interest accrues, not when the interest payment is made. For federal credit programs, outlays are recorded when loans are disbursed, in an amount representing the present value cost to the Government (excluding administrative costs), or the credit subsidy cost. Credit programs record cash payments to and from the public in non-budgetary financing accounts.

[12] 10/14/16 press release -- Joint Statement of Treasury Secretary Jacob J. Lew and OMB Director Shaun Donovan on Budget Results for Fiscal Year 2016.

Table 3: Net Operating Cost vs. Budget Deficit

Dollars in Billions		2016		2015*
Net Operating Cost	**$**	**(1,047.4)**	**$**	**(514.2)**
Change in:				
Federal Employee and Veterans Benefits Payable	$	437.0	$	99.8
Property, Plant, and Equipment, Net[1]	$	(54.2)	$	(47.0)
Environmental and disposal liabilities	$	35.0	$	42.5
Yearend Upward/(Downward) Credit Reform Subsidy Reestimates, Net[2]	$	22.2	$	(22.0)
Other, Net	$	20.0	$	2.0
Subtotal - Net Difference:	$	460.0	$	75.3
Budget Deficit	**$**	**(587.4)**	**$**	**(438.9)**

*2015 amounts restated. See Financial Statement Notes 1V, 6, and 12.

1 Net effect of: capitalized fixed assets, depreciation expense, and asset disposals and revaluations

2 Net effect of: yearend upward/(downward) credit reform subsidy reestimates and effect of prior year (upward)/downward credit reform subsidy reestimates.

The budget deficit is measured as the excess of outlays, or payments made by the Government, over receipts, or cash received by the Government. Net operating cost, on an accrual basis, is the excess of costs (what the Government has incurred, but has not necessarily paid) over revenues (what the Government has collected and expects to collect, but has not necessarily received). Net operating cost typically exceeds the budget deficit due largely to the inclusion of cost accruals associated with increases in estimated liabilities for the Government's postemployment benefit programs for its military and civilian employees and veterans. Similarly, the difference between the budget deficit and net operating cost can also be affected by changes in certain asset valuations, such as investments, and in other liabilities, such as estimated insurance and guarantee program liabilities. The longer-term estimated costs of these programs are included in the Government's net operating cost, calculated on an accrual basis as described above, but are not included in the largely cash-based budget deficit. In addition, the costs of certain assets, such as property plant and equipment, are recorded in the budget as outlays when purchased but are capitalized as assets and included in net operating cost as depreciation expense (an accrual cost) as they are used over the useful life of the asset. Significant changes in the Government's net operating cost, including those related to the aforementioned longer-term estimated costs, are discussed in the next section.

The ***Reconciliation of Net Operating Cost and Unified Budget Deficit Statement***, Table 3 summarizes how the Government's net operating cost as reported in the primarily accrual-based financial statements relates to the more widely-known and primarily cash-based budget deficit. Table 3 shows how many of the elements described above contribute to the $460.0 billion net difference between the Government's budget deficit and net operating cost for FY 2016, the majority of which is attributable to: (1) a $437.0 billion net increase in liabilities for Federal employee and veteran benefits payable (FEVBP), (2) a $22.2 billion net change from reestimates of the cost of federal loan programs under credit reform; and (3) other offsetting items, including a $54 billion increase in Property, Plant, and Equipment (PP&E). These and most of the other "Change in" amounts summarized in Table 3 affect net operating cost, but not the budget deficit. In particular, the $437.0 billion FEVBP change not only represents most (95.0 percent) of the difference between the budget deficit and net operating cost, but is also, as discussed in the following section, the most significant driver of the increase in the government's net operating cost for FY 2016.

The Government's Net Position: "Where We Are"

The Government's financial position and condition have traditionally been expressed through the *Budget*, focusing on surpluses, deficits, and debt. However, this primarily cash-based discussion of the Government's net outlays (deficit) or net receipts (surplus) tells only part of the story. The Government's accrual-based net position, (the difference between its assets and liabilities), and its "bottom line" net operating cost (the difference between its revenues and costs) are also key financial indicators.

Costs and Revenues: "What Went Out & What Came In"

The Government's ***Statement of Operations and Changes in Net Position***, much like a corporation's income statement, shows the Government's "bottom line" and its impact on net position (i.e., assets net of liabilities). To derive the Government's "bottom line" net operating cost, the ***Statement of Net Cost*** first shows how much it costs to operate the federal government, recognizing expenses when incurred, regardless of when payment is made (accrual basis). It shows the derivation of the Government's *net cost* or the net of: (1) gross costs, or the costs of goods produced and services rendered by the Government, (2) the earned revenues generated by those goods and services during the fiscal year, and (3) gains or losses from changes in actuarial assumptions used to estimate certain liabilities. This amount, in turn, is offset against the Government's taxes and other revenue reported in the ***Statement of Operations and Changes in Net Position*** to calculate the "bottom line" or *net operating cost*. [13]

Table 4: Gross Cost, Revenues, Net Cost, and Net Operating Cost

Dollars in Billions	2016	2015*	Increase / (Decrease) $	Increase / (Decrease) %
Gross Cost	**$ (4,507.7)**	**$ (4,248.2)**	**$ 259.5**	**6.1%**
Less: Earned Revenue	$ 376.6	$ 375.6	$ 1.0	0.3%
Gain/(Loss) from Changes in Assumptions	$ (273.3)	$ 19.3	$ (292.6)	(1516.1%)
Net Cost	**$ (4,404.4)**	**$ (3,853.3)**	**$ 551.1**	**14.3%**
Less: Tax and Other Revenues	$ 3,345.3	$ 3,334.0	$ 11.3	0.3%
Unmatched Transactions and Balances	$ 11.7	$ 5.1	$ 6.6	129.4%
Net Operating Cost	**$ (1,047.4)**	**$ (514.2)**	**$ 533.2**	**103.7%**

*2015 amounts restated. See Financial Statement Notes 1V, 6, and 12.

Table 4 shows that the Government's "bottom line" net operating cost more than doubled, from $514.2 billion in FY 2015 to $1.0 trillion in FY 2016, including the net effects of two FY 2015 restatements which resulted in a net decrease to the Government's 2015 net cost of $5.5 billion.[14] This $533.2 billion (103.7 percent) increase in the governmentwide net cost is largely attributable to a $551.1 billion (14.3 percent) increase in agency net costs, which was offset slightly by an $11.3 billion (0.3) increase in tax and other revenues over the past fiscal year as summarized in the following.

Gross Cost and Net Cost

The ***Statement of Net Cost***, starts with the Government's total gross costs of $4.5 trillion, subtracts revenues earned for goods and services provided (e.g., Medicare premiums, national park entry fees, and postal service fees), and adjusts the balance for gains or losses from changes in actuarial assumptions used to estimate certain liabilities, including federal employee and veterans benefits to derive its net cost of $4.4 trillion, a $551.1 billion (14.3 percent) increase over FY 2015, including the FY 2015 restatement.

Typically, the annual change in the Government's net cost is impacted by a variety of offsetting increases and decreases across agencies. For example offsetting changes in net cost during FY 2016 included:

- a $473.8 billion increase at the Department of Veterans Affairs (VA). The most significant change in VA's net cost was related to increased actuarial costs associated with Veteran Benefits for Compensation, Burial, and Education, which increased by $466.6 billon, $390.5 billion of which relates to changes in actuarial assumptions for FY 2016. VA attributes $276.6 billion of this increase to higher projected average growth in compensation counts, which was updated to reflect an increase in new compensation cases over the last five years; the remainder of this increase was mainly attributable to an increase in beneficiary counts, lower discount rates, and updated mortality and trend assumptions.[15] The changes in assumptions that impacted the change in the FEVB liability discussed earlier in the

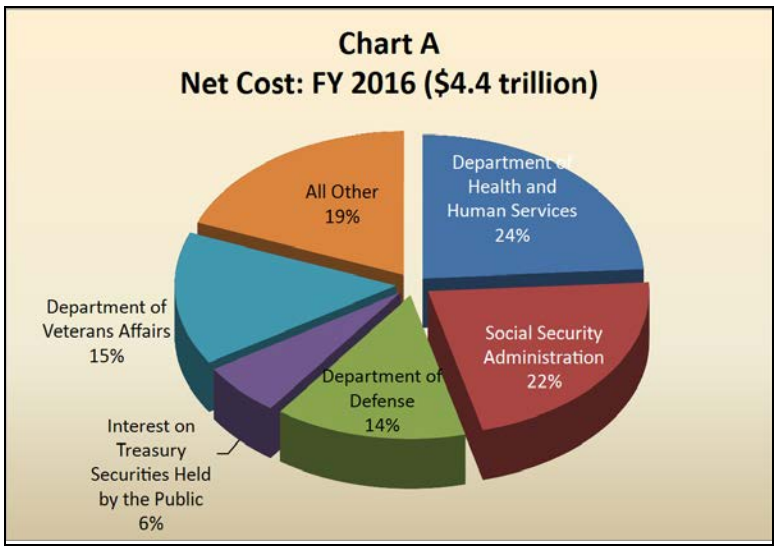
[13] As shown in Table 4, net operating cost includes an adjustment for unmatched transactions and balances, which represent unreconciled differences in intragovernmental activity and balances between Federal agencies. These amounts are described in greater detail in the Other Information section of this *Financial Report*.

[14] The Statement of Net Cost in this *Financial Report* reflects FY 2015 net cost restatements for: (1) VA from $169.1 billion to $175.3 billion and (2) the Department of Defense from $573.6 billion to $561.9 billion, (See Financial Statement Notes 1V, 6, and 12).

[15] Department of Veterans Affairs FY 2016 Agency Financial Report, p. 27-28

context of comparing the current year's budget deficit and net operating cost amounts also have a separate yet related effect on the related cost as described here. Across the government, the total net loss from changes in actuarial assumptions associated with the Government's civilian and military benefits programs amounted to $273.3 billion in FY 2016 as compared to a $19.3 billion gain in FY 2015, resulting in a $292.6 billion combined increase in net cost. Agencies administering these types of programs employ a complex series of assumptions, including but not limited to interest rates, beneficiary eligibility, life expectancy, medical cost levels, compensation levels, disability claims rates, and cost of living to make annual actuarial projections of their long-term benefits liabilities. While VA recorded a loss increase due to changes in these assumptions, the Office of Personnel Management (OPM) and the Department of Defense (DOD) both reported significantly increased gains ($64.2 billion and $30.1 billion, respectively) from changes in these assumptions for FY 2016.

- Actuarial costs also include accounting for when actual results differ from these projections. VA cost increases included $83 billion due to actual results (i.e., experience) differing from the prior year's actuarial projections;
- $44.8 billion and $37.1 billion net cost increases at the Department of Health and Human Services (HHS) and the Social Security Administration (SSA), respectively, primarily due to cost increases of the benefits programs that these agencies administer (HHS – Medicare and Medicaid programs, SSA – Old Age Survivors and Disability Insurance (OASDI) programs); and
- a $28.5 billion cost increase at the Department of Education (Education), due largely to subsidy cost reestimates (e.g., for lower than anticipated loan collection activity and greater than anticipated borrower repayment plan costs).[16];
- a $109.9 billion cost decrease at the Office of Personnel Management due largely to experience gains and to changes in actuarial assumptions referenced above (e.g., the result of lower assumed cost of living increases, salary increases, and health care cost increases).[17]



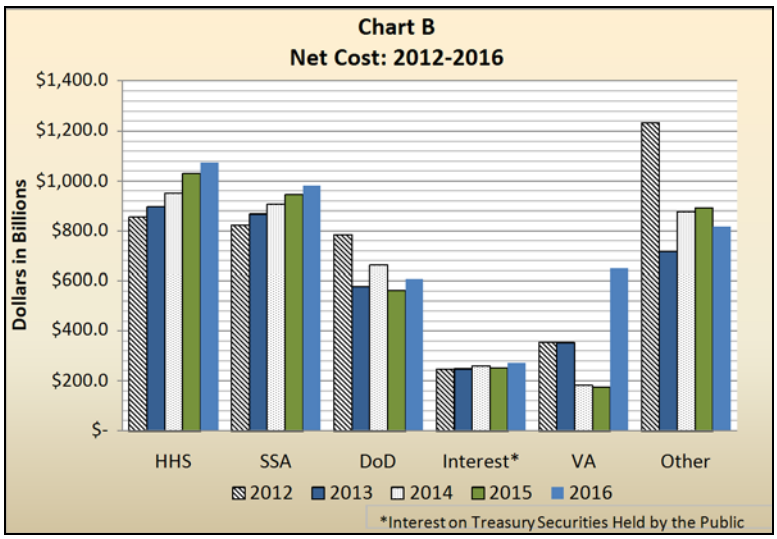
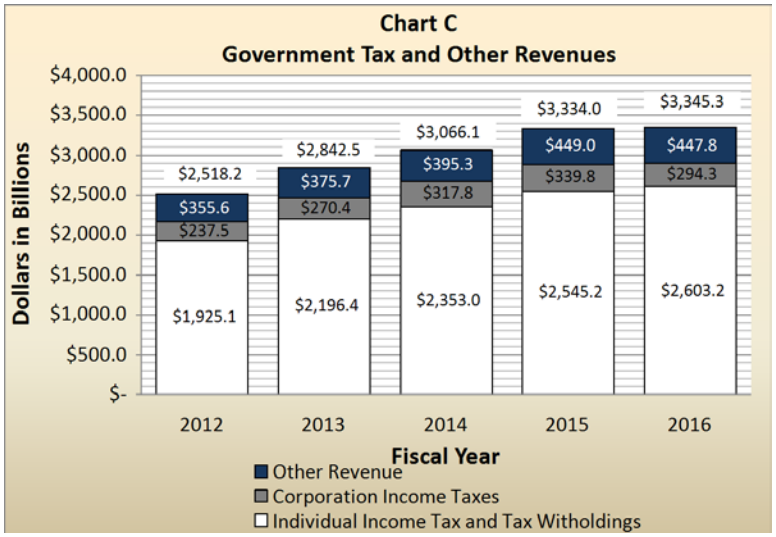


Chart A shows the composition of the Government's net cost. In FY 2016, three fourths of total net cost came from DOD, the Social Security Administration (SSA), the Department of Health and Human Services (HHS), and VA. HHS, SSA, and DOD have consistently incurred the largest agency shares of the Government's total net cost in recent years (Chart B). As indicated above, HHS and SSA net costs for FY 2016 ($1.1 trillion and $981.8 billion, respectively) are attributable to major social insurance programs administered by these agencies. The *Statements of Long-Term Fiscal Projections* (SLTFP), the *Statements of Social Insurance* (SOSI), and the related analysis and discussion included in this *Financial Report*, discuss the projected future revenues, expenditures, and sustainability of federal government programs in general and of social insurance programs in particular in greater detail. DOD net costs of $609.2 billion relate primarily to operations, readiness, and support; personnel; research; procurement; and retirement and health benefits. As explained above, increases in estimated actuarial costs of compensation programs significantly increased VA's costs during FY 2016. Chart A also shows that interest on debt held by the public contributed an additional 6.0 percent, and the other agencies included in the Government's FY 2016 Statement of Net Cost accounted for a combined 19.0 percent of the Government's total net cost for FY 2016.

[16] Department of Education FY 2016 Agency Financial Report, p. 25
[17] Office of Personnel Management FY 2016 Agency Financial Report, p. 30

Tax and Other Revenues - Getting to the "Bottom Line"

As noted earlier, tax and other revenues from the ***Statement of Operations and Changes in Net Position*** are deducted from total net cost to derive the Government's "bottom line" net operating cost. Chart C shows that total tax and other revenue did not change significantly, increasing slightly by $11.3 billion or 0.3 percent to $3.3 trillion for FY 2016. This increase is attributable mainly to an overall growth in individual income tax and withholdings, partially offset by reduced corporation income taxes, and other revenue.[18] Earned revenues from Table 4 are not considered "taxes and other revenue" and, thus, are not shown in Chart C. Individual income tax and tax withholdings and corporation income taxes accounted for about 77.8 percent and 8.8 percent of total revenue, respectively in FY 2016; other revenues from Chart C include Federal Reserve earnings, excise taxes, unemployment taxes, and customs duties.



As previously shown in Table 4, the increase in net cost more than offset the slight increase in tax and other revenues, more than doubling the government's net operating cost from $514.2 billion for FY 2015 to $1.0 trillion for FY 2016.

Assets and Liabilities: "What We Own and What We Owe"

The Government's net position at the end of the year is derived by netting the Government's assets against its liabilities, as presented in the ***Balance Sheet*** (summarized in Table 5). It is important to note that the balance sheet does not include the financial value of the Government's sovereign powers to tax, regulate commerce, and set monetary policy. It also excludes its control over nonoperational resources, including national and natural resources, for which the Government is a steward. In addition, as is the case with the ***Statement of Operations and Changes in Net Position***, the ***Balance Sheet*** includes a separate presentation of the portion of net position related to funds from dedicated collections. Moreover, the Government's exposures are broader than the liabilities presented on the balance sheet, when such items as the Government's future social insurance exposures (namely, Medicare and Social Security), as well as other fiscal projections, commitments and contingencies, are taken into account. These exposures are discussed later in this Management Discussion and Analysis (MD&A) section as well as in the financial statements and RSI sections of this *Financial Report*.

Table 5: Assets and Liabilities

Dollars in Billions	2016	2015*	Increase / (Decrease) $	Increase / (Decrease) %
Assets				
Cash & Other Monetary Assets	$ 464.6	$ 305.1	$ 159.5	52.3%
Loans Receivable, Net	$ 1,277.6	$ 1,216.0	$ 61.6	5.1%
Inventories & Related Property, Net	$ 314.3	$ 320.6	$ (6.3)	(2.0%)
Property, Plant & Equipment, Net	$ 979.5	$ 925.3	$ 54.2	5.9%
Other	$ 434.5	$ 494.2	$ (59.7)	(12.1%)
Total Assets	**$ 3,470.5**	**$ 3,261.2**	**$ 209.3**	**6.4%**
Less: Liabilities, comprised of:				
Federal Debt Held by the Public & Accrued Interest	$ (14,221.1)	$ (13,172.5)	$ 1,048.6	8.0%
Federal Employee & Veteran Benefits	$ (7,209.4)	$ (6,772.4)	$ 437.0	6.5%
Other	$ (1,332.4)	$ (1,559.9)	$ (227.5)	(14.6%)
Total Liabilities	**$ (22,762.9)**	**$ (21,504.8)**	**$ 1,258.1**	**5.9%**
Net Position (Assets Minus Liabilities)	**$ (19,292.4)**	**$ (18,243.6)**	**$ 1,048.8**	**5.7%**

*2015 amounts restated. See Financial Statement Notes 1V, 6,

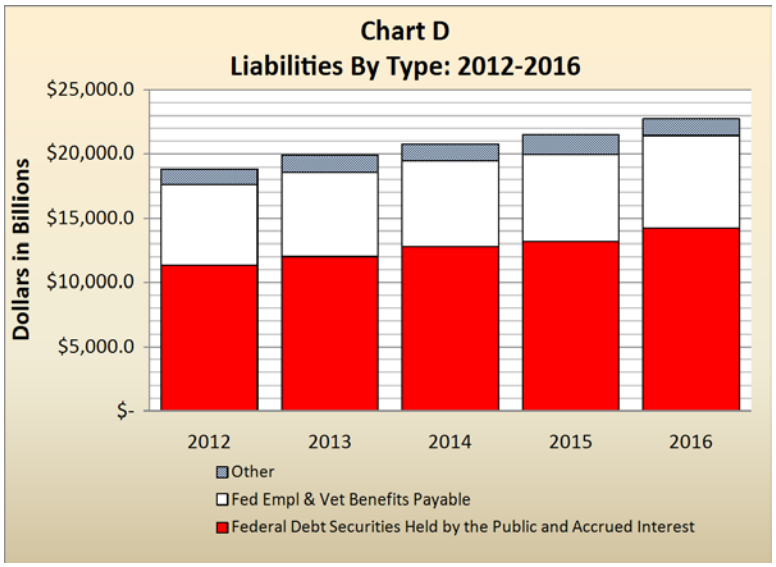
[18] Department of the Treasury FY 2016 Agency Financial Report, p. 27

Assets – "What We Own"

As of September 30, 2016, the Government held about $3.5 trillion in assets, an increase of $209.3 billion (6.4 percent).[19] The Government's assets are comprised mostly of net loans receivable ($1.3 trillion) and net property, plant, and equipment ($979.5 billion).[20] From Financial Statement Note 4, the Department of Education's (Education's) Federal Direct Student Loan Program accounted for $958.9 billion (75.1 percent) of total net loans receivable. Education's direct student loan program receivables balances have grown by more than 150 percent since FY 2011 largely due to increased direct loan disbursements, attributable to the continued effect of 2010 legislation requiring a transition for new loans from guaranteed student loans to full direct lending by Education. [21]

Liabilities – "What We Owe"

As indicated in Table 5 and Chart D, of the Government's $22.8 trillion in total liabilities, the largest liability is federal debt securities held by the public and accrued interest, the balance of which increased by just over $1.0 trillion (8.0 percent) to $14.2 trillion as of September 30, 2016.



The other major component of the Government's liabilities is federal employee and veteran benefits payable (i.e., the Government's pension and other benefit plans for its military and civilian employees), which increased $437.0 billion (6.5 percent) during FY 2016, to $7.2 trillion.[22] This total amount is comprised of $2.3 trillion in benefits payable for the current and retired civilian workforce, and $4.9 trillion for the military and veterans. OPM administers the largest civilian pension plan, covering nearly 2.7 million current employees and 2.6 million annuitants and survivors. The military pension plan covers about 2.1 million current military personnel (including active service, reserve, and National Guard) and approximately 2.7 million retirees and annuitants.

Federal Debt

The unified budget surplus or deficit is the difference between total federal spending and receipts (e.g., taxes) in a given year. The Government borrows from the public (increases federal debt levels) to finance deficits. During a budget surplus (i.e., when receipts exceed spending), the Government typically uses those excess funds to reduce the debt held by the public. ***The Statement of Changes in Cash Balance from Unified Budget and Other Activities*** reports how the annual unified budget surplus or deficit relates to the federal government's borrowing and changes in cash and other monetary assets. It also explains how a budget surplus or deficit normally affects changes in debt balances.

The Government's publicly-held debt, or federal debt held by the public, and accrued interest, which is reported on the Government's balance sheet as a liability, is comprised of Treasury securities, such as bills, notes, and bonds, net of unamortized discounts and premiums; and accrued interest payable. The "public" consists of individuals, corporations, state and local governments, Federal Reserve Banks, foreign governments, and other entities outside the federal government. Federal debt held by the public and accrued interest totaled $14.2 trillion as of September 30, 2016. As indicated above, budget surpluses have typically resulted in borrowing reductions, and budget deficits have conversely yielded borrowing increases. However, the Government's debt operations are generally much more complex. Each year, trillions of dollars of debt mature and new debt is issued to take its place. In FY 2016, new borrowings were $8.4 trillion, and repayments of maturing debt held by the public were $7.3 trillion, both increases from FY 2015).

In addition to debt held by the public, the Government has about $5.5 trillion in intragovernmental debt outstanding, which arises when one part of the Government borrows from another. It represents debt issued by the Treasury and held by Government accounts, including the Social Security ($2.8 trillion) and Medicare ($255.5 billion) trust funds.

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[19] The FY 2016 assets include the effects of an FY 2015 restatement of PP&E by DOD from $893.9 billion to $925.3 billion (see Note 6).

[20] For financial reporting purposes, other than multi-use heritage assets, stewardship assets are not recorded as part of Property, Plant, and Equipment. Stewardship assets are comprised of stewardship land and heritage assets. Stewardship land consists of public domain land (e.g., national parks, wildlife refuges). Heritage assets include national monuments and historical sites that among other characteristics are of historical, natural, cultural, educational, or artistic significance. See Note 24 – Stewardship Land and Heritage Assets.

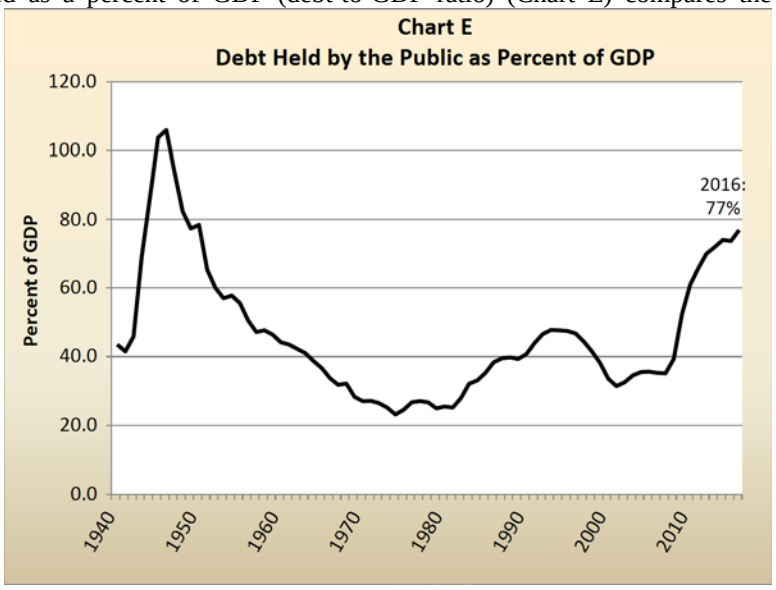
[21] With the enactment of the SAFRA Act, which was included as part of the *Health Care and Education Reconciliation Act of 2010* (HCERA) (Pub. L. 111-152), beginning in July 2010, no new loans were originated under the Federal Family Education Loan (FFEL) Program (FY 2016 Federal Student Aid Financial Report). See also: U.S. Department of Education FY 2016 Agency Financial Report p. 21.

[22] The FY 2016 Federal Employees and Veterans Benefits Payable includes the effects of an FY 2015 restatement by VA from $6,719.3 billion to $6,772.4 billion (see Note 12).

Intragovernmental debt is primarily held in Government trust funds in the form of special nonmarketable securities by various parts of the Government. Laws establishing Government trust funds generally require excess trust fund receipts (including interest earnings) over disbursements to be invested in these special securities. Because these amounts are both liabilities of the Treasury and assets of the Government trust funds, they are eliminated as part of the consolidation process for the governmentwide financial statements (see Note 11). When those securities are redeemed, e.g., to pay Social Security benefits, the Government will need to obtain the resources necessary to reimburse the trust funds. The sum of debt held by the public and intragovernmental debt equals gross federal debt, which (with some adjustments), is subject to a statutory ceiling (i.e., the debt limit). At the end of FY 2016, debt subject to the statutory limit (DSL) was $19.5 trillion.

Prior to 1917, Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress established a dollar ceiling for federal borrowing. With the *Public Debt Act of 1941* (Public Law 77-7), Congress and the President set an overall limit of $65 billion on Treasury debt obligations that could be outstanding at any one time. Since then, Congress and the President have enacted a number of measures affecting the debt limit, including several in recent years. Most recently, the *Bipartisan Budget Act of 2015* (P.L. 114-74) suspended the debt limit from November 2, 2015 through March 15, 2017. It is important to note that increasing or suspending the debt limit does not increase spending or authorize new spending; rather, it permits the United States to continue to honor pre-existing commitments to its citizens, businesses, and investors domestically and around the world.

The federal debt held by the public measured as a percent of GDP (debt-to-GDP ratio) (Chart E) compares the country's debt to the size of its economy, making this measure sensitive to changes in both. Over time, the debt-to-GDP ratio has varied widely. For most of the nation's history, the debt-to-GDP ratio has tended to increase during wartime and decline during peacetime. That pattern continued to hold following World War II until the 1970s. As shown in Chart E, wartime spending and borrowing had pushed the debt-to-GDP ratio to an all-time high of 106 percent in 1946, but it decreased rapidly in the post-war years, falling to 79 percent by 1950, 44 percent in 1960, and the postwar low point of 23 percent in 1974. Since then, the ratio has increased, growing rapidly from the mid-1970s until the early 1990s. In the 1990s, strong economic growth and fundamental fiscal decisions, including measures to reduce the federal deficit and implementation of binding "Pay As You Go" (PAYGO) rules, generated a significant decline in the debt-to-GDP ratio over the course of the 1990s, from a peak of 48 percent in 1993-1995, to 31 percent in 2001. During the last decade, much of this progress was undone as PAYGO rules were allowed to lapse, significant tax cuts were implemented, entitlements were expanded, and spending related to defense and homeland security increased. By September 2008, the debt-to-GDP ratio was 39 percent of GDP. The extraordinary demands of the last economic and fiscal crisis and the consequent actions taken by the federal government, combined with slower economic growth in the wake of the crisis, pushed the debt-to-GDP ratio up to 74.4 percent as of September 30, 2014, but the ratio declined slightly during FY 2015 to 73.8 percent despite a slight increase in borrowing to finance the deficit. During FY 2016, increases in borrowing to finance the deficit and for other changes such as net disbursements for federal credit programs increased the debt-to-GDP ratio to 77.0 percent.[23]



[23] Joint Statement of OMB Director, Shaun Donovan and Treasury Secretary, Jacob Lew.

The Economy in Fiscal Year 2016

A review of the nation's key macroeconomic indicators can help place the discussion of the Government's financial results in a broader context. As summarized in Table 6, the economy continued to expand at a moderate pace during FY 2016. Employment rose steadily and the unemployment rate declined further.

Table 6: National Economic Indicators*

	FY 2016	FY 2015
Real GDP Growth	1.7%	2.2%
Residential Investment Growth	1.5%	13.0%
Average monthly payroll job change (thousands)	209	227
Unemployment rate (percent, end of period)	5.0%	5.1%
Consumer Price Index (CPI)	1.5%	0.0%
CPI, excluding food and energy	2.2%	1.9%

* Some FY2015 data may differ from the FY2015 Financial Report due to updates and revisions.

Real (i.e., inflation-adjusted) GDP expanded 1.7 percent during FY 2016, slower than the 2.2 percent increase recorded over the four quarters of FY 2015. The moderation in the pace of expansion was due in part to a slowing of business fixed investment, particularly in the energy sector, as oil prices declined, and also due to liquidation of inventory through much of the fiscal year. Growth of consumer spending slowed somewhat during FY 2016 to 2.8 percent, and the recovery in the housing sector continued through the fiscal year at a slower pace, with residential fixed investment increasing by 1.5 percent, compared with an advance of 13.0 percent during FY 2015. Nonresidential fixed investment declined 1.1 percent during FY 2016 after a 1.4 percent advance during the previous fiscal year.

Labor market conditions improved further during FY 2016. The economy added 2.5 million nonfarm payroll jobs during the course of the fiscal year, near the 2.7 million jobs added during FY 2015. On a monthly basis, nonfarm payroll employment rose at an average rate of 209,000 jobs per month, somewhat less than the average monthly increase of 227,000 during FY 2015. The number of unemployed persons remained at 7.9 million in September 2016, matching its level a year earlier. The unemployment rate declined 0.1 percentage point, from 5.1 percent in September 2015 to 5.0 percent in September 2016.[24] At the end of FY 2016, the unemployment rate was 5.0 percentage points lower than the peak of 10.0 percent, reached in October 2009.

Inflation accelerated, but remained relatively low during FY 2016. The consumer price index (CPI) rose 1.5 percent during FY 2016, up from a flat reading in FY2015, as the effects of previous declines in energy prices dissipated. Consumer price inflation was 1.7 percent during FY 2014. Underlying core inflation (the CPI excluding food and energy) was 2.2 percent during FY 2016, compared with 1.9 percent during the previous fiscal year.

Growth of real disposable (i.e., after-tax) personal income slowed during FY 2016, as faster inflation offset a small pickup in growth of nominal disposable personal income. The level of corporate profits grew 2.8 percent during FY 2016, after a decline of 4.5 percent during the previous fiscal year.

[24] The Bureau of Labor Statistics notes that this change in the unemployment rate is not statistically significant.

The Long-Term Fiscal Outlook: "Where We Are Headed"

While the Government's immediate priority is to ensure that the economic expansion is sustained, there are longer-term fiscal challenges that must ultimately be addressed. The Government took potentially significant steps towards a sustainable fiscal policy by enacting the *Affordable Care Act* (ACA)[25] in 2010, the *Budget Control Act* (BCA) in 2011, and the *American Taxpayer Relief Act* (ATRA) in 2013. The ACA holds the prospect of lowering long-term per-beneficiary spending growth for Medicare and Medicaid, the BCA significantly curtails discretionary spending, and ATRA increases revenues. Together, these three laws substantially reduce the estimated long-term fiscal gap. However, persistent growth of health care costs, the retirement of the "baby boom" generation[26], increasing longevity, and lower birth rates leave a remaining imbalance between spending and revenue. Maintaining critical social programs, including Medicare, Medicaid, and Social Security, will require that health care cost growth be controlled and that reforms balance revenue increases with program modifications that protect the integrity of long-term commitments.

This *Financial Report* includes the ***Statements of Long-Term Fiscal Projections*** and a related Note Disclosure (Note 23). The Statement displays the present value of 75-year projections of the federal government's receipts and non-interest spending[27] for FY 2016 and FY 2015. Additional information about these projections may be found in Note 23 and the RSI section of this *Financial Report*.

Fiscal Sustainability

An important purpose of the *Financial Report* is to help citizens understand current fiscal policy and the importance and magnitude of policy reforms necessary to make it sustainable. A sustainable policy is one where the debt-to-GDP ratio is stable or declining over the long term.

To determine if current fiscal policies are sustainable, the projections of the deficit and debt discussed here assume current policy (i.e., current law, with certain adjustments, such as extension of expiring policies that are expected to continue)[28] will continue indefinitely and draw out the implications for the growth of debt held by the public as a share of GDP. The projections are therefore neither forecasts nor predictions. As policy changes are enacted, actual financial outcomes will be different than those projected.

The projections in this *Financial Report* indicate that current policy is not sustainable. As discussed below, if current policy is left unchanged, the debt-to-GDP ratio is projected to fall about 6 percentage points by 2024 before commencing a steady rise to 252 percent in 2091 and is projected to rise continuously thereafter. Preventing the debt-to-GDP ratio from rising over the next 75 years is estimated to require some combination of spending reductions and revenue increases that amount to 1.6 percent of GDP over the period. While this estimate of the "75-year fiscal gap" is highly uncertain, it is nevertheless nearly certain that current fiscal policies cannot be sustained indefinitely.

It is important to address the Government's fiscal imbalances soon. Delaying action increases the magnitude of spending reductions and/or revenue increases necessary to stabilize the debt-to-GDP ratio. For example, it is estimated that the magnitude of reforms necessary to close the 75-year fiscal gap is about 18 percent larger if reforms are delayed by just ten years, and about 50 percent larger if reform is delayed 20 years. And if policies are put in place in the near term that increase the fiscal gap, then even more dramatic fiscal adjustments will be necessary in the future.

The estimates of the cost of policy delay in this *Financial Report* assume policy does not affect GDP or other economic variables. Delaying fiscal adjustments for too long raises the risk that growing federal debt would increase interest rates, which would, in turn, reduce investment and ultimately economic growth. However, abrupt and poorly designed deficit reduction could also be counterproductive for the economy, particularly if it takes the form of reducing investments in infrastructure, education, or innovation that are essential for robust longer-term economic growth.

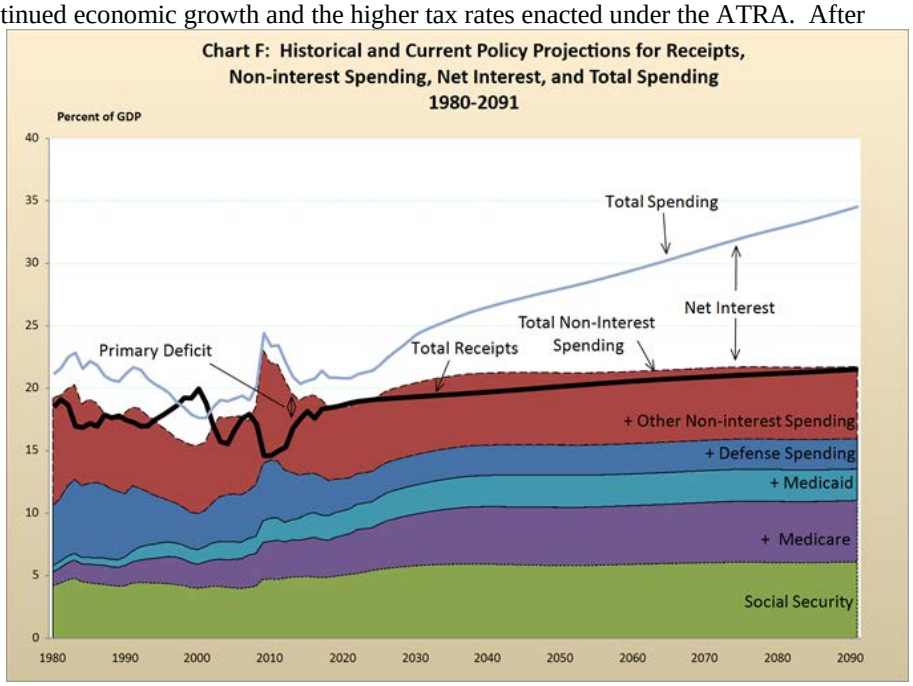
The Primary Deficit, Interest, and Debt

The primary deficit – the difference between non-interest spending and receipts – is the only determinant of the debt-to-GDP ratio that the Government controls directly. (The other determinants are interest rates and growth in GDP). Chart F shows receipts, non-interest spending, and the difference – the primary deficit – expressed as a share of GDP (primary deficit-to-GDP ratio). The primary deficit-to-GDP ratio grew rapidly in 2009 due to the financial crisis and the recession and

[25] P.L. 111-148, as amended by P.L. 111-152. The ACA expands health insurance coverage, provides health insurance subsidies for low-income individuals and families, includes many measures designed to reduce health care cost growth, and reduces the annual increases in Medicare payment rates.
[26] Refers to the segment of the population born during the post-World War II era during which time birth rates in the U.S. were higher than normal.
[27] For the purposes of the Statement of Long-Term Fiscal Projections and this analysis, spending is defined in terms of outlays. In the context of federal budgeting, spending can either refer to: (1) budget authority – the authority to commit the government to make a payment; (2) obligations – binding agreements that will result in either immediate or future payment; or (3) outlays, or actual payments made.
[28] Current policy in the projections is based on current law, but includes certain adjustments, such as extension of certain policies that expire under current law but are routinely extended or otherwise expected to continue (e.g., reauthorization of the Supplemental Nutrition Assistance Program).

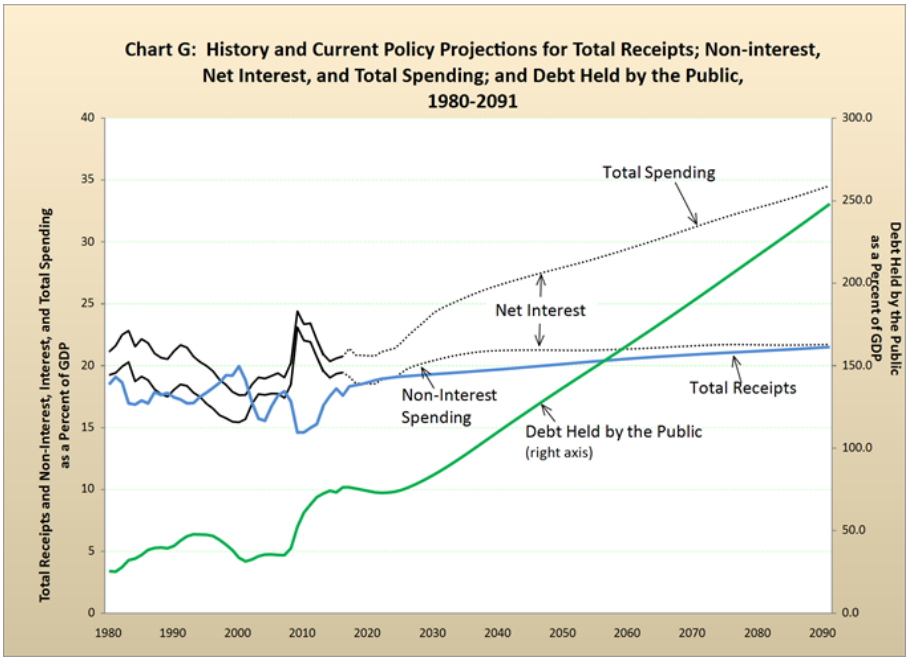
the policies pursued to combat both. The ratio remained high from 2010 to 2012 despite shrinking in each successive year, and fell significantly in 2013 and 2014. The primary deficit is projected to shrink further in the next few years as discretionary spending limits called for in the BCA continue and the economy continues to recover, becoming a primary surplus in 2020 that peaks at 0.3 percent of GDP in 2021. After 2021, however, increased spending for Social Security and health programs due to the ongoing retirement of the baby boom generation and increases in the price of health care services is expected to cause the primary surplus to steadily deteriorate and become a primary deficit starting in 2025 that reaches 1.0 percent of GDP by 2029. The primary deficit peaks at 1.6 percent of GDP in 2038, gradually decreases beyond that point as aging of the population continues at a slower pace and as receipts are projected to increase as a percentage of GDP, to 0.2 percent of GDP in 2091.

Receipts as a share of GDP fell substantially in 2009 and 2010 and remained low in 2011 and 2012 because of the recession and tax reductions enacted as part of the *American Recovery and Reinvestment Act of 2009* (ARRA) and the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010*. The share was 17.6 percent in 2016, exceeding its 30-year average due to continued economic growth and the higher tax rates enacted under the ATRA. After 2020, receipts are projected to grow slightly more rapidly than GDP as increases in real incomes cause more taxpayers and a larger share of income to fall into the higher individual income tax brackets.



Non-interest spending as a share of GDP is projected to stay at or below its current level of about 19 percent until 2026, and to then rise gradually to 21.2 percent of GDP by 2038 and 21.7 percent of GDP in 2091. The reductions in the non-interest spending share of GDP over the next few years are mostly due to the expected reductions in spending for overseas contingency operations, caps on discretionary spending, and the automatic spending cuts mandated by the BCA; the subsequent increases are principally due to faster growth in Medicare, Medicaid, and Social Security spending (see Chart F). The aging of the baby boom generation over the next 25 years is projected to increase the Social Security, Medicare, and Medicaid spending shares of GDP by about 1.1 percentage points, 1.6 percentage points, and 0.6 percentage points, respectively. After 2041, the Social Security spending share of GDP remains relatively stable, while the combined Medicare and Medicaid spending share of GDP continues to increase, albeit at a slower rate, due to projected increases in health care costs. The ACA provision of health insurance subsidies and expanded Medicaid coverage boost federal spending, and other ACA provisions significantly reduce per-beneficiary Medicare cost growth. On net, the ACA is projected to substantially reduce the growth rate of Medicare expenditures over the next 75 years. However, as discussed in Note 22, these projections are subject to much uncertainty about whether certain cost-reducing provisions of the ACA will prove unsustainable, in which case the law may be changed in ways that raise federal health care expenditures for Medicare and other programs.

The primary deficit-to-GDP projections in Charts F and G (left axis), along with projections for interest rates, determine the debt-to-GDP ratio projections shown in Chart G (right axis). That ratio was 77 percent at the end of FY 2016 and under the long-term fiscal projections of current policy is projected to be 71 percent in 2026, 122 percent in 2046, and 252 percent in 2091. The debt-to-GDP ratio rises at an accelerating rate despite primary deficits that flatten out because higher levels of debt lead to higher net interest expenditures, and higher net interest expenditures lead to higher debt.[29] The continuous rise of the debt-to-GDP ratio after 2026 indicates that current policy is unsustainable.



These debt projections are generally higher than the corresponding projections in the FY 2015 *Financial Report*, but still lower than those in the FY 2014 *Financial Report*. For example, the debt-to-GDP projection for 2089 (the final projection year for the 2014 report) is 246 percent in this year's *Financial Report*, 220 percent in the FY 2015 *Financial Report*, and 321 percent in the FY 2014 *Financial Report*.[30]

The Fiscal Gap and the Cost of Delaying Policy Reform

The 75-year fiscal gap is one measure of the degree to which current fiscal policy is unsustainable. It is the amount by which primary surpluses over the next 75 years must, on average, rise above current-policy levels in order for the debt-to-GDP ratio in 2091 to equal its level in 2016 (77 percent). This fiscal gap is estimated to equal 1.6 percent of GDP. The projections show that projected primary deficits average 0.8 percent of GDP over the next 75 years under current policies. If policies were put in place that would result in a zero fiscal gap, the average primary surplus over the next 75 years would be 0.8 percent of GDP, 1.6 percentage points higher than the projected present value net excess of non-interest spending over receipts shown in the basic financial statement. The 75-year fiscal gap is 7.9 percent as large as the 75-year present value of projected receipts and 7.6 percent as large as the 75-year present value of non-interest spending, and is 0.4 percentage points larger than the 1.2 percent estimate in 2015.

It is noteworthy that preventing the debt-to-GDP ratio from rising over the next 75 years requires that primary surpluses be substantially positive on average. This is true because projected GDP growth rates are, on average, smaller than the projected government borrowing rate over the next 75 years. The implication is that debt would grow faster than GDP if primary surpluses were zero on average. For example, if the primary surplus was precisely zero in every year, then debt would grow at the rate of interest in every year, which would be faster than GDP growth.

Table 7 illustrates the cost of delaying policy reform to close the fiscal gap by comparing policy reforms that begin on three different dates. The first policy reform begins immediately and calls for increasing primary surpluses by 1.6 percent of GDP in every year between 2017 and 2091. This is accomplished by invoking some combination of spending reductions and revenue increases that amount to 1.6 percent of GDP in every year over the 75-year projection period. The second policy reform in Table 7 begins in 2027. Because the same fiscal consolidation must be compressed into ten fewer years, this policy reform is more abrupt, calling for primary surplus increases amounting to 1.9 percent of GDP in every year between 2027

Table 7

Costs of Delaying Fiscal Reform

Period of Delay	Change in Average Primary Surplus
Reform in 2017 (No Delay)	1.6 percent of GDP between 2017 and 2091
Reform in 2027 (Ten-Year Delay)	1.9 percent of GDP between 2027 and 2091
Reform in 2037 (Twenty-Year Delay)	2.4 percent of GDP between 2037 and 2091

Note: Reforms taking place in 2016, 2026, and 2036 from the 2015 Financial Report were 1.2, 1.5, and 1.9 percent of GDP, respectively.

[29] The change in debt each year is also affected by certain transactions not included in the unified budget deficit, such as changes in Treasury's cash balances and the nonbudgetary activity of Federal credit financing accounts. These transactions are assumed to hold constant at about 0.4 percent of GDP each year, with the same effect on debt as if the primary deficit was higher by that amount.

[30] See the Required Supplementary Information section of the *FY 2015 Financial Report of the U.S. Government* for more information about changes from the long term fiscal projections for FY 2014.

and 2091. Similarly, if debt is allowed to accumulate unabated for 20 years, then closing the 75-year fiscal gap would require even more abrupt primary surplus increases amounting to 2.4 percent of GDP in every year between 2037 and 2091. The differences between the primary surplus boost starting in 2027 and 2037 (1.9 and 2.4 percent of GDP, respectively) and the primary surplus boost starting in 2017 (1.6 percent of GDP) is a measure of the additional burden policy reform delay would impose on future generations. Future generations are harmed by a policy reform delay of this sort because the higher the primary surplus is during their lifetimes the greater the difference is between the taxes they pay and the programmatic spending from which they benefit.

Conclusion

The Government took potentially significant steps towards a sustainable fiscal policy by enacting the ACA in 2010, the BCA in 2011, and ATRA in 2013. The ACA holds the prospect of lowering long-term per-beneficiary spending growth for Medicare and Medicaid, the BCA significantly curtails discretionary spending, and ATRA increases revenues. Together, these three laws substantially reduce the estimated long-term fiscal gap. But even with these laws, the debt-to-GDP ratio is projected to remain relatively flat over the next ten years and then commence a continuous rise over the remaining projection period and beyond if current policies are kept in place. This trend implies that current policies are not sustainable. Subject to the important caveat that changes in policy are not so abrupt that they slow continued economic growth, the sooner policies are put in place to avert these trends, the smaller the revenue increases and/or spending decreases will need to be to return the Government to a sustainable fiscal path over the long term.

While this *Financial Report's* projections of expenditures and receipts under current policy are highly uncertain, it is nevertheless nearly certain that current policy cannot be sustained indefinitely.

These and other issues concerning fiscal sustainability are discussed in further detail in Note 23 and the RSI section of this *Financial Report*.

Social Insurance

The preceding analysis of the Government's long-term fiscal projections considered Government receipts and spending as a whole. The Statement of Social Insurance (SOSI) provides a more focused perspective of the Government's "social insurance" programs: Social Security, Medicare, Railroad Retirement, and Black Lung. [31] For these programs, the SOSI reports: (1) the actuarial present value of all future program revenue (mainly taxes and premiums) - excluding interest - to be received from or on behalf of current and future participants; (2) the estimated future scheduled expenditures to be paid to or on behalf of current and future participants; and (3) the difference between (1) and (2). Amounts reported in the SOSI and in the RSI section in this *Financial Report* are based on each program's official actuarial calculations.

Table 8 on the following page summarizes amounts reported in the SOSI, showing that net social insurance expenditures are projected to be $46.7 trillion over 75 years as of January 1, 2016 for the "Open Group," an increase of $5.2 billion over net expenditures of $41.5 trillion projected in the 2015 *Financial Report*.[32] The current-law 2016 amounts reported for Medicare reflect the physician payment levels expected under the MACRA payment rules and the ACA-mandated reductions in other Medicare payment rates, but not the payment reductions and/or delays that would result from trust fund depletion.[33] By accounting convention, the transfers of general revenues are eliminated in the consolidation of the SOSI at the governmentwide level and as such, the general revenues that are used to finance Medicare Parts B and D are not included in these calculations even though the expenditures on these programs are included. For the FY 2016 and 2015 SOSI, the amounts eliminated totaled $28.7 trillion and $24.8 trillion, respectively. SOSI programs and amounts are included in the broader fiscal sustainability analysis in the previous section, although on a slightly different basis (as described in Note 23).

The SOSI provides perspective on the Government's long-term estimated exposures and costs for social insurance programs. These expenditures are not considered Government liabilities. Future benefit payments will be recognized as expenses and liabilities as they are incurred, based on the continuation of the social insurance programs' provisions contained in current law. The social insurance trust funds account for all related program income and expenses. Medicare and Social Security taxes, premiums, and other income are credited to the funds; fund disbursements may only be made for benefit payments and program administrative costs. Any excess revenues are invested in special non-marketable U.S. Government

[31] The *Black Lung Benefits Act* (BLBA) provides for monthly payments and medical benefits to coal miners totally disabled from pneumoconiosis (black lung disease) arising from their employment in or around the nation's coal mines. See http://www.dol.gov/owcp/regs/compliance/ca_main.htm

[32] The SOSI presented in the FY 2016 Financial Report presents projected amounts in trillions of dollars. Prior year reports expressed these amounts in hundreds of billions of dollars. 'Closed' Group and 'Open' Group differ by the population included in each calculation. From the SOSI, the 'Closed' Group includes: (1) participants who have attained eligibility and (2) participants who have not attained eligibility. The 'Open' Group adds future participants to the 'Closed' Group. See 'Social Insurance' in the Required Supplementary Information section in this *Financial Report* for more information.

[33] The *Medicare Access and CHIP Reauthorization Act* (MACRA) of 2015 permanently replaces the sustainable growth rate (SGR) formula, which was used to determine payment updates under the Medicare physician fee schedule with specified payment updates through 2025. The changes specified in MACRA also establish differential payment updates starting in 2026 based on practitioners' participation in eligible alternative payment models; payments are also subject to adjustments based on the quality of care provided, resource use, use of certified electronic health records, and clinical practice improvement.

securities at a market rate of interest. The trust funds represent the accumulated value, including interest, of all prior program surpluses, and provide automatic funding authority to pay for future benefits.

Table 8: Social Insurance Future Expenditures in Excess of Future Revenues

Dollars in Trillions	2016	2015	Increase / (Decrease) $	Increase / (Decrease) %
Open Group (Net):				
Social Security (OASDI)	$ (14.1)	$ (13.4)	$ 0.7	5.2%
Medicare (Parts A, B, & D)	$ (32.5)	$ (28.0)	$ 4.5	16.1%
Other	$ (0.1)	$ (0.1)	$ 0.0	0.0%
Total Social Insurance Expenditures, Net (Open Group)	**$ (46.7)**	**$ (41.5)**	$ 5.2	12.5%
Total Social Insurance Expenditures, Net (Closed Group)	**$ (64.9)**	**$ (58.2)**	$ 6.7	11.5%
Social Insurance Net Expenditures as a % of Gross Domestic Product (GDP)*				
Open Group				
Social Security (OASDI)	(1.1%)	(1.1%)		
Medicare (Parts A, B, & D)	(2.7%)	(2.7%)		
Total (Open Group)	**(3.8%)**	**(3.7%)**		
Total (Closed Group)	**(5.3%)**	**(5.2%)**		

Note: Amounts reported in trillions. Prior to FY 2016 reporting, amounts had been reported in billions. Some totals may not equal sum of components due to rounding.

Source: Statement of Social Insurance (SOSI). Amounts equal estimated present value of projected revenues and expenditures for scheduled benefits over the next 75 years of certain 'Social Insurance' programs (e.g., Social Security, Medicare). 'Open Group' totals reflect all current and projected program participants during the 75-year projection period. 'Closed Group' totals reflect only current participants.

* GDP values used are from the 2016 & 2015 Social Security and Medicare Trustees Reports and represent the present value of GDP over the 75-year projection period. As the GDP used for Social Security and Medicare differ slightly in the Trust Fund Reports, the two values are averaged to estimate the 'Other' and Total Net Social Insurance Expenditures as % of GDP.

Table 9 on this page identifies the principal reasons for the changes in projected social insurance amounts during 2016 and 2015.

Table 9: Changes in Social Insurance Projections

Dollars in Trillions	2016	2015
Net Present Value (NPV) - Open Group (Beginning of the Year)	**$ (41.5)**	**$ (41.9)**
Changes In:		
Valuation Period	$ (1.7)	$ (1.9)
Demographic data and assumptions	$ 1.1	$ (0.2)
Economic data and assumptions[1]	$ (0.9)	$ (0.1)
Law or policy	$ 0.3	$ 0.0
Methodology and programmatic data[1]	$ 0.0	$ 0.7
Economic and other healthcare assumptions[2]	$ (3.4)	$ 3.2
Change in projection base[2]	$ (0.6)	$ (1.2)
Net Change in Open Group measure	$ (5.2)	$ 0.4
NPV - Open Group (End of the Year)	**$ (46.7)**	**$ (41.5)**

1 Relates to SSA.

2 Relates to HHS.

Note: Amounts reported in trillions. Prior to FY 2016 reporting, amounts had been reported in billions. Some totals may not equal sum of components due to rounding.

The following briefly summarizes the significant changes for the current valuation (as of January 1, 2016) as disclosed in Note 22, Social Insurance. See Note 22 for additional information.

- Change in valuation period: This change replaces a small negative net cash flow for 2015 and replaces it with a much larger negative net cash flow for 2090. As a result, the present value of the estimated future net cash flows decreased (became more negative) by $1.7 trillion.
- Changes in economic and other healthcare assumptions: The economic assumptions used in the Medicare projections are the same as those used for the Old-Age Survivors and Disability Insurance (OASDI) and are prepared by the Chief Actuary at SSA. For the current valuation, there were three changes to the ultimate economic assumptions:
    - The ultimate rate of price inflation (CPI-W) was lowered by 0.1 percentage point to 2.6 percent.
    - The ultimate real wage differential is assumed to be 1.20 percent in the current valuation period, compared to 1.17 percent in the prior valuation period
    - The ultimate real interest rate was lowered by 0.2 percentage points to 2.7 percent.

  Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate economic assumptions were changed.
    - The projections assume a reduction in the ultimate level of actual and potential GDP of about 1.0 percent. Thus, by the end of the short-range period (2025), and for all years thereafter, projected GDP in 2009 dollars is about 1.8 percent below the level in last year's *Financial Report*.

  The health care assumptions are specific to the Medicare projections. Changes in health care assumptions in the current valuation included, but were not limited to (see Note 22):
    - Utilization rate assumptions for inpatient hospital services were increased.
    - Lower productivity increases through 2021, resulting in higher provider payment updates.
    - Greater reductions in expenditures attributable to the Independent Payment Advisory Board.
    - Higher projected drug cost trend, particularly for certain high-cost specialty drugs.

  The net impact of these changes decreased (made more negative) the present value of the estimated future cash flows by $3.4 trillion. For Part A, these changes resulted in an increase to the present value of future expenditures and income, with an overall decrease in the estimated future net cash flow. For Parts B and D, these changes increased the present value of estimated future expenditures (and also income).
- Change in demographic data and assumptions: The demographic assumptions used in the Medicare projections are the same as those used for the Old-Age Survivors and Disability Insurance (OASDI) and are prepared by the Office of the Chief Actuary at SSA. The ultimate demographic assumptions for the current valuation (beginning on January 1, 2016), with the exception of a small change in marriage rates, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed, including but not limited to:
    - Final birth rate data for 2013 and 2014 indicated lower birth rates than were expected in the prior valuation;
    - Incorporating mortality data obtained from the National Center for Health Statistics resulted in slightly higher death rates than were projected in the prior valuation;
    - Assumed ultimate marriage rates were decreased somewhat to reflect a continuation of recent trends; and
    - More recent legal and other-than-legal immigration data and historical population data were included.

  These changes had an overall net effect of increasing (making less negative) the estimated future net cash flows by $1.1 trillion.

Projected net expenditures for Medicare Parts A and B declined significantly between FY 2009 and FY 2010 reflecting provisions of the ACA. As reported in Note 22, there continues to be uncertainty about whether the projected cost savings and productivity improvements will be sustained in a manner consistent with the projected cost growth over time. Note 22 includes an alternative projection to illustrate the uncertainty of projected Medicare costs. As indicated earlier, GAO disclaimed opinions on the 2016, 2015, 2014, 2013 and 2012SOSI because of these significant uncertainties.

Costs as a percent of GDP of both Medicare and Social Security, which are analyzed annually in the Medicare and Social Security Trustees' Reports, are projected to increase substantially through the mid-2030s because: (1) the number of beneficiaries rises rapidly as the baby-boom generation retires and (2) the lower birth rates that have persisted since the baby boom cause slower growth in the labor force and GDP.[34] According to the Medicare Trustees' Report, spending on Medicare is projected to rise from its current level of 3.6 percent of GDP to 5.6 percent in 2040 and to 6.0 percent in 2090.[35] The Hospital Insurance (HI) Trust Fund is now expected to remain solvent until 2028, (two years earlier than noted in last year's report), at which point, HI revenues are projected to cover 87 percent of program costs. This percentage is projected to decrease to 79 percent in 2040, and then increase to about 86 percent by the end of the projection period.

As for Social Security, combined spending is projected to generally increase from its current level of 5.0 percent of GDP to about 6.0 percent by 2035, declining to 5.9 percent by 2050 and then generally increase to 6.1 percent by 2090. The Social Security Trustees' Report indicates that annual OASDI income, considered on a theoretical basis, including interest on

[34] 2016 Trustees Report for Medicarehttps://www.ssa.gov/oact/TRSUM/tr15summary.pdf, pp. 5, 29.
[35] Percent of GDP amounts are expressed in gross terms (including amounts financed by premiums and state transfers).

trust fund assets, will exceed annual cost and trust fund assets will increase every year until 2020, at which time it will be necessary to begin drawing down on trust fund assets to cover part of expenditures until asset reserves become depleted in 2034 (unchanged last year's Report). At that time, continuing tax income would be sufficient to pay 79 percent of scheduled benefits, decreasing to about 74 percent by 2090. The Disability Insurance (DI) Trust Fund alone is projected to become depleted in the third quarter of 2023, at which time continuing income to the DI Trust Fund would be sufficient to pay 89 percent of DI scheduled benefits, rising to a somewhat higher level through 2040, then declining to 82 percent by 2090.[36] The projections assume that full Social Security and Medicare benefits are paid after the corresponding trust fund assets are depleted.

As noted earlier, it is apparent that these programs are on a fiscally unsustainable path (as was previously discussed and as noted in the Trustees' Reports). Additional information from the Trustees Reports may be found in the RSI section of this *Financial Report*.

[36] 2016 Trustees Report for Social Securityhttps://www.ssa.gov/oact/TRSUM/tr15summary.pdf, pp. 3, 6, 13, 24.

Systems, Controls, and Legal Compliance

Systems

As federal agencies demonstrate success in obtaining opinions on their audited financial statements, the federal government continues to face challenges in implementing financial systems that meet federal requirements. The number of CFO Act agencies reporting lack of substantial compliance with one or more of the three Section 803(a) requirements of the *Federal Financial Management Improvement Act* (FFMIA) was 7 in FY 2016 and 10 in FY 2015, and the number of auditors reporting lack of substantial compliance with one or more of the three Section 803(a) FFMIA requirements was 9 in FY 2016 and 12 in FY 2015.[37] These results underscore the importance of current initiatives to standardize the financial management practices across the federal government.

Controls

Federal managers have a fundamental responsibility to develop and maintain effective internal controls. Effective internal controls help to ensure that programs are managed with integrity and resources are used efficiently and effectively through three objectives: effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. The safeguarding of assets is a subcomponent of each objective.

In response to major management challenges to agency mission and goals, agencies are increasingly recognizing the importance and utility of Enterprise Risk Management (ERM) as a tool for identifying, assessing, mitigating, managing and preparing for risk. Effectively implemented, ERM contributes to improved decision-making, adopting a proactive rather than a reactive approach towards risk. ERM has the potential to change the perception that internal controls are limited to just compliance and financial reporting. Instead, internal controls can play a key tool to address management challenges that cut across multiple agency functions. ERM is currently practiced in both the private and public sectors as well as internationally, with examples in governments of the United Kingdom, Canada, and Japan, among others. In an effort to improve taxpayers' trust in government and prepare for future challenges, OMB has promoted ERM best practices across agencies. The recent update to OMB Circular No. A-123 further explains and highlights ERM.

The Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, is the policy document that implements the requirements of 31 U.S.C. 3512 (c), (d) (commonly known as the *Federal Managers' Financial Integrity Act* or FMFIA). Circular No. A-123 focus for internal controls is primarily on providing agencies with a framework for assessing and managing risks more strategically and effectively. The Circular was recently revised to reflect changes incorporated in GAO's updated Standards for Internal Control in the federal government. The Circular contains multiple appendices that address, at a more detailed level, one or more of the objectives of effective internal control. Appendix A provides a methodology for agency management to assess, document, test, and report on internal controls over financial reporting. Appendix B requires agencies to maintain internal controls that reduce the risk of fraud, waste, and error in Government charge card programs. Appendix C implements the Requirements for Effective Estimation and Remediation of Improper Payments. Appendix D defines new requirements for determining compliance with the FFMIA and will contribute to efforts to reduce the cost, risk, and complexity of financial system modernizations.

The total number of reported material weaknesses for the CFO Act agencies as of the issuance of this *Financial Report* was 21[38] and 40 for FYs 2016 and 2015, respectively. Effective internal controls are a challenge not only at the agency level, but also at the governmentwide level. GAO reported that at the governmentwide level, material weaknesses resulted in ineffective internal control over financial reporting. While progress is being made at many agencies and across the Government in identifying and resolving internal control deficiencies, continued diligence and commitment are needed.

The Department of Health and Human Services (HHS) and the Department of the Treasury (Treasury) each have responsibilities for ensuring payment accuracy in programs created under the *Affordable Care Act*. Performing comprehensive risk assessments is critical to establishing an effective program for achieving payment accuracy in future years. In FY 2016, both Departments finalized plans for and performed comprehensive improper payment risk assessments to determine areas that might affect advance payments of the Premium Tax Credit (APTC), Premium Tax Credit (PTC), Cost Sharing Reduction and Basic Health Program payment accuracy. Updates on the status and results of the risk assessments were reported in the FY 2016 Agency Financial Reports (AFR). In addition, both Departments have established internal controls to provide for effective program operations, reliable financial reporting, and compliance with laws and regulations.

[37] The FY 2016 results do not include the Department of Defense (DOD), the Department of Housing and Urban Development (HUD), or the National Science Foundation (NSF). For FY 2015, both HUD and DOD and their auditors noted lack of substantial compliance with one or more of the three Section 803(a) requirements of the FFMIA, and neither NSF nor its auditors noted any lack of compliance with the Section 803(a) requirements.

[38] The FY 2016 results do not include DOD, which had 13 material weaknesses in FY 2015 or HUD, which had nine material weaknesses in FY 2015 or NSF, which had zero material weaknesses in FY 2015. As shown in Table 10, if the number of material weaknesses for DOD, HUD, and NSF do not change between FY 2015 and FY 2016, the total for CFO Act agencies for FY 2016 will be 43.

Legal Compliance

Federal agencies are required to comply with a wide range of laws and regulations, including appropriations, employment, health and safety, and others. Responsibility for compliance primarily rests with agency management. Compliance is addressed as part of agency financial statement audits. Agency auditors test for compliance with selected laws and regulations related to financial reporting. Certain individual agency audit reports contain instances of noncompliance. None of these instances were material to the governmentwide financial statements. However, GAO reported that its work on compliance with laws and regulations was limited by the material weaknesses and scope limitations discussed in its report.

Financial Management Progress and Priorities

Since the passage of the CFO Act of 1990, the federal financial community has made important strides in instilling strong accounting and financial reporting practices. For FY 2016, 21 of the 24 CFO Act agencies obtained an opinion from the independent auditors on their financial statements[39]. In addition, 40 auditor-identified material weaknesses were reported at the beginning of FY 2016 (see Table 10 on the following page). An increasing number of federal agencies have initiated and sustained disciplined and consistent financial reporting operations, implemented effective internal controls around financial reporting, and have successfully integrated transaction processing and accounting records. These efforts have resulted in improved results on financial statement audits. However, weaknesses in basic financial management practices and other limitations continue to prevent three of the CFO Act agencies, and the Government as a whole, from achieving an audit opinion.

Today, accountability means providing transparent information to the public about where and how federal dollars are being spent. It means protecting against fraud. It means avoiding wasteful or excessive use of taxpayer funds. It means ensuring that the federal government is not only responsible stewards of taxpayer dollars, but frugal stewards as well, looking for every opportunity to save money and create greater efficiencies.

The federal government has come a long way since the passage of the CFO Act in 1990. Today, the federal financial management community is focused on three important improvement initiatives:

- Improving the quality, utility, and transparency of financial information;
- Protecting against waste, fraud, and abuse; and
- Helping agencies maximize the impact of their limited financial resources.

[39] The 21 agencies include the Department of Health and Human Services (HHS) and Department of Labor (DOL), which received clean opinions on all statements except the Statements of Social Insurance and the Statements of Changes in Social Insurance, (both of which received a disclaimer of opinion), and the Department of Agriculture (USDA), which received a clean opinion on its balance sheet only. (DOD, HUD, and NSF expect to issue their audited Agency Financial Reports following the release of this *Financial Report*.

Table 10: Auditor-Reported Material Weaknesses: FY 2016

Agency	Beginning	New	Resolved	Consolidated	Ending
Department of Agriculture (USDA)	2	0	0	0	2
Department of Commerce (DOC)	0	0	0	0	0
Department of Defense (DOD)*	13	Pending	Pending	Pending	Pending
Department of Education (Education)	0	0	0	0	0
Department of Energy (DOE)	0	0	0	0	0
Department of Health and Human Services (HHS)	1	0	0	0	1
Department of Homeland Security (DHS)	3	0	0	0	3
Department of Housing and Urban Development (HUD)*	9	Pending	Pending	Pending	Pending
Department of the Interior (DOI)	2	0	2	0	0
Department of Justice (DOJ)	0	0	0	0	0
Department of Labor (DOL)	1	1	0	0	2
Department of State (State)	0	0	0	0	0
Department of Transportation (DOT)	1	1	0	0	2
Department of the Treasury (Treasury)	1	0	0	0	1
Department of Veterans Affairs (VA)	4	3	1	0	6
Agency for International Development (USAID)	1	0	0	0	1
Environmental Protection Agency (EPA)	1	1	0	0	2
General Services Administration (GSA)	0	0	0	0	0
National Aeronautics and Space Administration (NASA)	0	0	0	0	0
National Science Foundation (NSF)*	0	Pending	Pending	Pending	Pending
Nuclear Regulatory Commission (NRC)	0	0	0	0	0
Office of Personnel Management (OPM)	1	0	0	0	1
Small Business Administration (SBA)	0	0	0	0	0
Social Security Administration (SSA)	0	0	0	0	0
Totals	**40**	**6**	**3**	**0**	**43**

*Audit results for DOD, HUD, and NSF were not available as of the issuance of this *Financial Report.*
Ending Total assumes DOD, HUD, and NSF have 13, 9, and zero material weaknesses (Beginning Totals) as of September 30, 2016, respectively.

Improve the Quality, Utility, and Transparency of Federal Financial Information

DATA Act

The *Digital Accountability and Transparency Act of 2014* (DATA Act), signed on May 9, 2014, sets forth a clear vision for the future of Federal spending transparency. The Act amended the *Federal Funding Accountability and Transparency Act of 2006* (FFATA) by requiring that all federal spending be displayed on a website in searchable, downloadable, and machine-readable format. This data includes obligations, outlays, budgetary authority, unobligated balances, and other budgetary resources for each appropriations account. It also expands federal award reporting previously required under FFATA. In May 2015, OMB, in coordination with Treasury, issued financial data definition standards and policy guidance outlining the first set of DATA Act implementation requirements. By 2017, all agencies must report this data to a centralized website and adhere to the data standards and guidance issued by OMB and Treasury. Posting this financial information will allow spending comparisons across and within agencies that have never been possible before as well as unlock spending data for use by the public.

Since the DATA Act was signed into law, OMB and Treasury have been partnering to lead governmentwide implementation. They have established a robust governance structure with representatives from agencies and functional communities fostering collaboration on data standards, policy changes, USAspending.gov improvements, and agency implementation. The implementation approach was developed to be collaborative, iterative, incremental, and agile, with a data centric focus.

USAspending.gov

USAspending.gov was established to provide clear information on federal award spending. Continuing to improve the quality, utility and transparency of this federal spending information is a foundational government commitment to openness, as identified in the U.S. Government's National Action Plan for Open Government. To continue its efforts to improve the

quality of spending data, OMB, in coordination with Treasury, issued additional policy guidance to adjust USAspending.gov reporting requirements and procedures pursuant to the DATA Act.

To align our federal spending and financial management transparency efforts, the Administration has transferred responsibility for USAspending.gov from the General Services Administration (GSA) to Treasury. In March 2015, Treasury released a new version of USAspending.gov with improved search capabilities and visualizations of data.

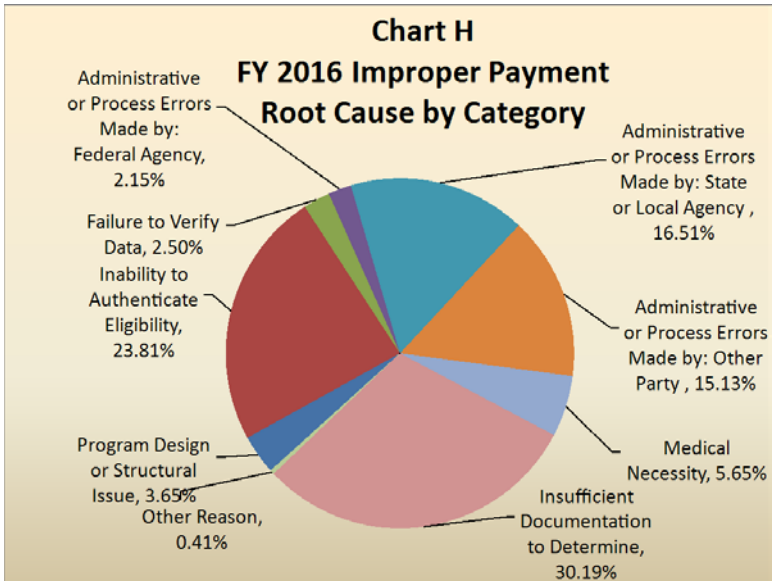
Moving forward, in concert with Treasury, OMB will continue to collaborate with federal and non-federal stakeholders to evolve the Administration's governmentwide spending transparency framework to effectively provide the public with transparent information about how taxpayer dollars are being spent.

Protect Against Waste, Fraud, and Abuse

Improper Payments

Addressing improper payments is a central component of the Administration's overall efforts to eliminate waste, fraud, and abuse. When the President took office in 2009, the improper payment error rate was 5.42 percent, an all-time high. Since then, the Administration, working together with Congress, has made progress by strengthening accountability and transparency through annual reviews by agency Inspectors General, and expanded requirements for high-priority programs. As a result of this concerted effort, in FY 2013 the Administration reported an improper payment rate of 3.53 percent. In FY 2015, the governmentwide improper payment rate was 4.39 percent, which corresponds to an improper payment dollar amount of $137 billion and in FY 2016, the governmentwide improper payment rate was 4.67 percent, which corresponds to an improper payment dollar amount of $144.4 billion.[40] This increase between FY 2015 and FY 2016 can be attributed to percentage and dollar increases in the Medicaid Program, the Direct Loan Program, the Medicare Part C Program, the Pell Grant Program, the VA Community Care Program, and the Earned Income Tax Credit (EITC) Program. The Medicare Fee for Service (FFS) program continues to account for the largest portion of the governmentwide total in FY 2016 ($41 billion or 28 percent of the governmentwide total), whereas Medicaid accounts for the second largest portion of the governmentwide total ($36 billion or 25 percent of the governmentwide total). The EITC and Medicare Part C combined account for the third largest portion of the governmentwide total ($33 billion or 23 percent of the governmentwide total). In addition, agencies recovered roughly $20 billion in overpayments through the payment recapture audits and other methods in FY 2016.

Prior to FY 2015 reporting, agencies were required to categorize their improper payment estimates based on three categories of improper payments: (1) documentation and administrative errors; (2) authentication and medical necessity errors; and (3) verification errors. However, those categories proved to be limited and not necessarily applicable to most programs. Therefore, OMB—in consultation with agencies—developed new improper payment categories. FY 2016 marked the second year of the OMB reporting requirement for root causes reporting as shown in Chart H. Approximately $44 billion of the government-wide improper payments in FY 2016 are caused by insufficient documentation. A lack of supporting documentation could be a situation where there is a lack of supporting documentation necessary to verify the accuracy of a payment identified in the improper payment testing sample such as a program not having the documentation to support a beneficiary's eligibility for a benefit. Approximately $34 billion of the government-wide improper payments in FY 2016 were caused by the inability to authenticate eligibility. The inability to authenticate eligibility is a situation in which an improper payment is made because the agency is unable to authenticate eligibility criteria such as no database or other resource exist to help the agency make a determination of eligibility or statutory constraints exist preventing a program from being able to access the information that would help prevent the improper payment. This additional detail behind the root causes of improper payments provides more granularity on improper payment estimates and will be used to inform more effective corrective actions and more focused strategies for reducing improper payments.



The Administration continues to use the Budget to build on congressional and Administration action to reduce improper payments. For example, the President's FY 2016 and 2017 Budget included a number of program integrity proposals aimed at reducing improper payments and improving Government efficiency. The FY 2016 proposals included a robust package of Medicare and Medicaid program integrity proposals, strategic reinvestment in the Internal Revenue Service (IRS), and an

[40] DOD's Commercial Payments were first included in the government-wide rate in FY 2013. When the DOD commercial payments are excluded from the government-wide figures the FY 2016 improper payment rate is 5.08 percent and the improper payment estimate is $144.3 billion.

equally robust package of Social Security program integrity proposals, in addition to many other proposals for other programs also aimed at reducing improper payments. The President's FY 2017 Budget also includes a number of new program integrity proposals.

The Government is also leveraging advanced data analytics and improved technologies to prevent improper payments before they happen. In doing so, as part of the President's Do Not Pay Initiative, the Administration established a Do Not Pay System of Records at Treasury. The Treasury Working System provides agencies a single-point of entry to access data and matching services to help detect, prevent, and recover improper payments during the award or payment lifecycle. Furthermore, Treasury has begun analyzing data across agencies to identify potential duplicative benefit payments in programs with related missions and beneficiaries. In addition to Treasury, agency payment integrity tools include the (CMS) Center for Program Integrity (which has implemented CMS' Fraud Prevention System [FPS]); the Department of Defense Business Activity Monitoring tool; and the Department of Labor's Unemployment Insurance (UI) Integrity Center of Excellence, a federal-state partnership that helps prevent, detect, and reduce improper payments in the UI program. The SSA has a process to intercept payments to beneficiaries who have died or been incarcerated, and has established an Analytics Center of Excellence which works on capturing real-time data and building more meaningful metrics, thereby allowing SSA to focus efforts on those projects or initiatives that yield the most promise. As a result of the Initiative, agencies cumulatively identified and stopped over $5.9 billion of improper payments through the Do Not Pay Initiative as of the end of FY 2015.

The Administration looks forward to continued work with Congress on Administration priorities including the sharing of death data from states to prevent improper payments to the deceased while maintaining privacy to ensure program integrity and payment accuracy.

Combating improper payments within the federal government is a top priority for the Administration and it will continue to explore new and innovative ways to address the problem. Each dollar paid in error represents a loss of public resources, and this Administration is committed to reducing waste, fraud, and abuse and continuing to improve payment accuracy with every tool at its disposal.

Improving Grants Management

The Federal government spends more than $600 billion in Federal financial assistance each year, and the effective and efficient management and use of these funds help agencies to achieve their missions while protecting these resources from fraud, waste, and abuse. The Uniform Grant Guidance, 2 CFR 200, issued in December of 2014, was the culmination of a three-year collaborative effort across Federal agencies and its non-Federal partners, to streamline eight existing OMB Circulars on financial assistance management into one consolidated set of guidance.

Since adoption of the Uniform Grant Guidance, OMB, the Council on Financial Assistance Reform (COFAR), and 28 federal awarding agencies have been diligently working to implement these requirements. In support of this effort, the COFAR hosted a webcast in June 2016 "Uniform Guidance: Promising Practices in Implementation" identifying best practices. The webcast modules, as well as tools and resources related to each session, were posted at https://cfo.gov/cofar/

In addition, OMB collected data on a suite of Administrative and Audit metrics, as outlined in the Memorandum M-14-17, *Metrics for Uniform Guidance*, to measure the effectiveness of the new policies. The metrics are also published on the COFAR website at https://cfo.gov/cofar/ and OMB will continue to evaluate the metrics to determine whether any changes need to be made to gauge additional aspects of the Uniform Guidance implementation.

OMB and the Federal awarding agencies are committed to working together to continue to ensure that the government promotes effective stewardship over its Federal financial assistance funds.

Help Agencies Maximize the Impact of their Limited Financial Resources

FedStat/Benchmarking

Over the course of this Administration, OMB has used regular data-driven management reviews to advance many of its most important shared priorities. Through implementation of the *GPRA Modernization Act of 2010* and the President's Management Agenda, these reviews have led to a number of tangible improvements in the effectiveness and efficiency of individual agencies and the Government as a whole, and OMB will continue that work through ongoing PortfolioStat, Benchmarking, and Strategic Review engagements.

The federal government's efforts to improve government efficiency aim to increase the quality and value of core administrative operations and enhance productivity to achieve cost savings or cost avoidance. Establishing cost and quality benchmarks for these operations have helped to develop tools for the federal government to measure performance in key mission-support areas, including financial reporting and audit, charge cards, DATA Act, debt collection, Do Not Pay, electronic invoicing and quick pay, ERM and internal control, grants management, improper payments, real property and shared services.

During FY 2016, OMB designed and launched the "FedStat" review to bring these efforts and other emerging priorities into focus in a cohesive discussion of opportunities with the CFO Act agencies for improved performance and risk mitigation that will more closely align with the Budget process and inform program management and administration. OMB met with agencies to discuss data-driven evidence on shared challenges across the Government, to identify potential areas for agency sub-component improvement, and to explore opportunities to pursue cross-agency solutions, including policies, processes, and leading practices of excellence for broader application.

In support of the President's Management Agenda, agency implementation of these action items will improve agency management of mission-support functions and mission delivery, identify potential Budget, legislative, or other proposals early to inform the development of the FY 2018 Budget, as appropriate, and inform the FY 2017 FedStat process with a meaningful data-driven decision making process that supports each agency's mission.

Improving Effectiveness and Efficiency in Financial Operations and Systems

The Administration continues to make significant progress in the effort to minimize the costs and risks associated with agency financial systems modernization. While in the past the use of shared services was limited to smaller agencies, cabinet-level agencies have begun to realize the benefit of shared service and other similar agreements. For example, during FY 2015, in the Government's largest shared service agreement to date, the Department of Housing and Urban Development (HUD) successfully transitioned many of its core financial management functions – as well as select administrative and human resource functions – to Treasury. More recently, the Department of Homeland Security's Transportation Security Administration and the United States Coast Guard are in the process of migrating to the Department of Interior's Interior Business Center.

In October 2015, OMB and General Services Administration (GSA) established the Unified Shared Services Management (USSM) office to drive improvement in administrative functions through shared services. In May 2016, OMB issued M-16-11, *Improving Administrative Functions Through Shared Services*, which established an enterprise-wide shared service strategy for the federal government. The strategic direction of this initiative is set by the Shared Services Governance Board (SSGB) – a cross functional, cross government board of executives charted with adopting a new lens for decision-making that at times may require prioritizing the federal enterprise over the individual agency. Led by the SSGB and USSM, stakeholders from across the Government will work together to manage and oversee mission-support shared services with an initial scope of acquisitions, financial management, human resources, travel and information technology. The SSGB also pushed to reduce the risk of costly, failed agency IT migrations and modernizations by publishing a playbook of best practices and lessons learned from across Government and aligning investment reviews to the Federal budget process through the Modernization and Migration Management (M3) Framework.

In addition, agencies continue to transition to electronic invoicing for appropriate federal procurements. The FY 2015 OMB Memorandum M-15-19, *Improving Government Efficiency and Saving Taxpayer Dollars Through Electronic Invoicing*, directed agencies to transition to electronic invoicing by the end of FY 2018. The Government is the largest single purchaser of goods and services in the United States, processing over 19 million invoices each year. The move to electronic invoicing can addresses cash flow issues for businesses, particularly small businesses, while also reducing administrative burden and costs to taxpayers.

Driving Real Property Efficiencies through Better Data and Data Analytics

The federal domestic building inventory is diverse and contains 275,000 buildings requiring approximately $18.7 billion of annual operation and maintenance expenditures, including approximately $7.1 billion of annual lease costs. Within the inventory, there are opportunities to realize cost savings by utilizing space more efficiently and reducing the portfolio. In 2013, the "Freeze the Footprint" (FTF) Policy (OMB Management Procedures Memorandum 2013-02) was issued, requiring agencies to freeze their real property footprint. From FY2013 to FY 2015 when the FTF policy expired, agencies reduced their federal domestic office and warehouse space by 24.7 million square feet. OMB estimates that the 24.7 million SF reduction will generate $300 million of annual cost avoidance for the government from FY 2016 onwards. To improve the quality of federal real property data in annual PARs or AFRs, agencies were required to validate and report "Freeze the Footprint" square footage and associated operations and maintenance costs in their 2014 through 2016 financial statements.

In FY 2016, the Government issued the National Strategy for the Efficient Use of Real Property (Strategy) and its companion implementation policy, the Reduce the Footprint (RTF) policy. The Strategy provides a strategic framework for agencies to measure the efficiency of their real property portfolios to identify and prioritize efficiency actions that reduces portfolio size. The RTF policy requires agencies to set annual portfolio reduction targets to help implement identified efficiency improvements and to implement an office space design standard to ensure office space is designed for efficiency. Over time, the Strategy and RTF policy will improve utilization of government-owned buildings to reduce reliance on leasing, lower the number of excess and underutilized properties, and improve the cost effectiveness and efficiency of the federal real property portfolio.

For the first time, the RTF policy required that agencies reduce the size of the federal real property portfolios to improve program efficiency, and agencies have developed and finalized their first ever five year RTF reduction Plans to implement the policy. The agencies' RTF Plans target an aggregate reduction of 61 million square feet (SF) over the Plans' five year (FY 2016 – FY 2020) implementation time period. The magnitude of the targeted 61 million square feet reduction indicates the Strategy and RTF policy will be effective tools to improve the efficiency of the Government's real property portfolio. Agencies will update their RTF Plans and annual reduction targets in March of each year with the goal of increasing the magnitude of targeted reductions year-over-year as agencies' ability to fully utilize the policies matures. The agencies' final FY 2017 – FY 2021 RTF Plans target 71.8 million SF of reductions during that time period.

To support increased reduction targets, the GSA and OMB have developed a new management tool within the Federal Real Property Profile (FRPP) database that enables agencies to fully analyze their portfolios. The new management tool uses

the real property performance metrics developed through the President's Management Agenda to measure the performance of agencies' portfolios and thereby enable the identification and prioritization efficiency opportunities. The management tool, combined with the improved FRPP data quality that will result from the implementation of GSA's technical guidance in FY 2017 that establishes mandatory FRPP data validation and verification requirements, will enhance agencies' ability to implement data driven decision making to develop their annual RTF reduction targets. Focusing policy on reducing the portfolio, improving the quality of FRPP data through mandatory data validation and verification procedures, and the broad use of the new FRPP management tool will support higher RTF square foot reduction targets and efficiency gains in future years.

Conclusion

The federal government has seen significant progress in financial management since the passage of the CFO Act more than 20 years ago. Yet significant challenges remain. The issues that the federal government faces today require our financial managers to move beyond the status quo and to generate a higher return on investment for our financial management activities. The steps outlined above leverage the tools and capacities in place today, and refocus energies on critical and emerging priorities – cutting wasteful spending, improving the efficiency of our operations and information technology, and laying a foundation for data quality and collaboration as the federal government enters a new era of transparency and open government.

Additional Information

This *Financial Report's* Appendix contains the names and websites of the significant Government entities included in the *Financial Report's* financial statements. Details about the information in this *Financial Report* can be found in these entities' financial statements included in their Performance and Accountability and Agency Financial Reports. This *Financial Report*, as well as those from previous years, is also available at the Treasury, OMB, and GAO websites at: http://www.fiscal.treasury.gov/fsreports/fs_reports_publications.htm; http://www.whitehouse.gov/omb/financial/index.html; and http://www.gao.gov/financial.html, respectively. Other related Government publications include, but are not limited to the:

- *Budget of the United States Government,*
- *Treasury Bulletin,*
- *Monthly Treasury Statement of Receipts and Outlays of the United States Government,*
- *Monthly Statement of the Public Debt of the United States,*
- *Economic Report of the President, and*
- *Trustees' Reports for the Social Security and Medicare Programs.*

Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the federal government, and the financial condition and changes in financial condition of its social insurance programs, and the federal government's projected long-term trends in receipts, spending, and debt, pursuant to the requirements of 31 U.S.C. § 331(e)(1). These statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

U.S. GOVERNMENT ACCOUNTABILITY OFFICE

441 G St. N.W.
Washington, DC 20548

Comptroller General
of the United States

January 12, 2017

The President
The President of the Senate
The Speaker of the House of Representatives

To operate as effectively and efficiently as possible, Congress, the administration, and federal managers must have ready access to reliable and complete financial and performance information—both for individual federal entities and for the federal government as a whole. Our report on the U.S. government's consolidated financial statements for fiscal years 2016 and 2015 underscores that much work remains to improve federal financial management and that the federal government continues to face an unsustainable long-term fiscal path.

Our audit report on the U.S. government's consolidated financial statements is enclosed. In summary, we found the following:

- Certain material weaknesses[1] in internal control over financial reporting and other limitations on the scope of our work resulted in conditions that prevented us from expressing an opinion on the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[2] About 34 percent of the federal government's reported total assets as of September 30, 2016, and approximately 18 percent of the federal government's reported net cost for fiscal year 2016 relate to significant federal entities that, as of the date of our audit report, were unable to issue audited financial statements, were unable to receive audit opinions on the complete set of financial statements, or received a disclaimer of opinion on their fiscal year 2016 financial statements.[3]

[1]A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

[2]The accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Unified Budget Deficit, (4) Statements of Changes in Cash Balance from Unified Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis.

[3]As of the date of this audit report, the audited financial statements for the Department of Defense, Department of Housing and Urban Development, National Science Foundation, and Smithsonian Institution were not issued. The Department of Agriculture obtained an unmodified opinion on its consolidated balance sheet as of September 30, 2016, but its consolidated statement of net cost, consolidated statement of changes in net position, combined statement of budgetary resources, and the related notes for the fiscal year ended September 30, 2016, were not audited. The Railroad Retirement Board received a disclaimer of opinion on its 2016 financial statements.

- Significant uncertainties (discussed in Note 22 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth, prevented us from expressing an opinion on the sustainability financial statements, which consist of the 2016 and 2015 Statements of Long-Term Fiscal Projections;[4] the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance; and the 2016 and 2015 Statements of Changes in Social Insurance Amounts.[5] About $32.5 trillion, or 70.0 percent, of the reported total present value of future expenditures in excess of future revenue presented in the 2016 Statement of Social Insurance relates to Medicare programs reported in the Department of Health and Human Services' (HHS) 2016 Statement of Social Insurance, which received a disclaimer of opinion. A material weakness in internal control also prevented us from expressing an opinion on the 2016 and 2015 Statements of Long-Term Fiscal Projections.

- Material weaknesses resulted in ineffective internal control over financial reporting for fiscal year 2016.

- Material weaknesses and other scope limitations discussed in our audit report limited our tests of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements for fiscal year 2016.

Overall, significant progress has been made in improving federal financial management since the enactment of key federal financial management reforms in the 1990s. Importantly, almost all of the 24 Chief Financial Officers Act of 1990 (CFO Act) agencies received unmodified ("clean") opinions on their respective entities' fiscal year 2016 financial statements, up from 6 CFO Act agencies that received clean audit opinions in 1996. In addition, accounting and financial reporting standards have continued to evolve to provide greater transparency and accountability over the federal government's operations, financial condition, and fiscal outlook. Further, the preparation and audit of individual federal entities' financial statements have identified numerous deficiencies, leading to corrective actions to strengthen federal entities' internal controls, processes, and systems.

However, since the federal government began preparing consolidated financial statements 20 years ago, three major impediments have continued to prevent us from rendering an opinion on the federal government's accrual-based consolidated financial statements over this period: (1) serious financial management problems at the Department of Defense (DOD) that have prevented its financial statements from being auditable, (2) the federal government's inability to adequately account for and reconcile intragovernmental activity and balances between federal entities, and (3) the federal government's ineffective process for preparing the consolidated financial statements.

Although DOD was not able to issue its audited financial statements by the end of our 2016 audit completion date, it has consistently been unable to receive an audit opinion on its financial statements in the past. The Department of the Treasury (Treasury) and the Office of

[4]The Statements of Long-Term Fiscal Projections presents for all the activities of the federal government the present value of projected receipts and noninterest spending under current policy without change, the relationship of these amounts to projected gross domestic product, and changes in the present value of projected receipts and noninterest spending from the prior year.

[5]Statements of Social Insurance are presented for the current year and each of the 4 preceding years in accordance with U.S. generally accepted accounting principles. Also, the sustainability financial statements do not interrelate with the accrual-based consolidated financial statements.

Management and Budget (OMB) have represented to us that the previously reported DOD material weaknesses continue to exist. Following years of unsuccessful financial improvement efforts, the DOD Comptroller established the Financial Improvement and Audit Readiness (FIAR) Directorate to develop, manage, and implement a strategic approach for addressing internal control weaknesses and for achieving auditability, and to integrate those efforts with other improvement activities, such as the department's business systems modernization efforts. DOD's current FIAR strategy and methodology has expanded to focus on four priorities—budgetary information, proprietary accounting data and information, asset accountability, and valuation—with an overall goal of having its department-wide financial statements audit ready by September 30, 2017.[6] Because budgetary information is widely and regularly used for management, one of DOD's highest interim priorities is to improve its budgetary information and processes underlying its Statement of Budgetary Resources (SBR).

Based on difficulties encountered in preparing for an audit of the SBR, DOD made a significant change to its FIAR Guidance that limited the scope of the first-year SBR audits for all DOD components.[7] As outlined in the November 2014 FIAR Plan Status Report and the November 2013 revised FIAR Guidance, the scope of initial SBR audits beginning in fiscal year 2015 is to focus on current-year budget activity, to be reported on a Schedule of Budgetary Activity (SBA).[8] This is intended to be an interim step toward achieving the audit of multiple-year budget activity required for an audit of the SBR. In making this strategic change, DOD officials concluded—based on the difficulties encountered in obtaining documentation for prior-year transactions on the U.S. Marine Corps SBR audit—that the most effective path to an audit of the SBR would be to start with reporting and auditing only current-year activity for fiscal year 2015 appropriations and expanding subsequent audits to include current-year appropriations and prior appropriations going back to fiscal year 2015. Consequently, certain DOD components—including the Departments of the Army, Navy, and Air Force—underwent their first SBA audits for fiscal year 2015. Those DOD components' SBAs were again audited for fiscal year 2016, but with an expanded scope that included beginning balances carried over from fiscal year 2015. Independent public accountants (IPA) issued disclaimers of opinion for all three DOD components' SBAs for both of these fiscal years and identified material weaknesses in internal control at all three DOD components. These material weaknesses included the inability to reasonably assure that the SBAs reflected all of the relevant financial transactions that occurred and that documentation was available to support such transactions. During the fiscal year 2016

[6]Section 1003 of the National Defense Authorization Act for Fiscal Year 2010, Pub. L. No. 111-84, 123 Stat. 2190, 2439-41 (Oct. 28, 2009), made the development and maintenance of the FIAR Plan a statutory requirement. Under the act, the FIAR Plan must describe specific actions to be taken and the costs associated with ensuring that DOD's financial statements are validated as ready for audit by September 30, 2017. In addition, section 1005 of the National Defense Authorization Act for Fiscal Year 2013, Pub. L. No. 112-239, 126 Stat. 1632, 1904-05 (Jan. 2, 2013), enacted a requirement for DOD's FIAR Plan to describe specific actions to be taken and the costs associated with ensuring that one of DOD's financial statements, the Statement of Budgetary Resources, would be validated as ready for audit by September 30, 2014, but DOD has acknowledged that it did not meet this target date. More recently, section 1003 of the National Defense Authorization Act for Fiscal Year 2014, Pub. L. No. 113-66, 127 Stat. 672, 842 (Dec. 26, 2013) (*reprinted in* 10 U.S.C. § 2222 note), mandated an audit of DOD's fiscal year 2018 financial statements and that the audit results be submitted to Congress by March 31, 2019.

[7]The FIAR Guidance was first issued by the DOD Comptroller in May 2010 and provides a standardized methodology for DOD components to follow for achieving financial management improvements and auditability. The DOD Comptroller periodically updates this guidance.

[8]Unlike the SBR, which reflects multiple-year budget activity, the SBA reflects the balances and associated activity related only to funding from fiscal year 2015 forward. As a result, the SBAs exclude unobligated and unexpended amounts carried over from funding prior to fiscal year 2015 as well as information on the status and use of such funding (e.g., obligations incurred and outlays) in fiscal year 2015 and thereafter.

and 2015 audits, the IPAs collectively issued hundreds of findings and recommendations. The three DOD components' management officials have generally concurred with the findings in the respective IPA reports and are at various stages of developing and implementing corrective actions to address the IPAs' recommendations.

In its November 2016 FIAR Plan Status Report, DOD reported that for fiscal year 2017, the Army and Navy will expand the scope of their audits to full SBRs, and the Air Force will again undergo an SBA audit. In addition, the U.S. Marine Corps will undergo its first audit of all its financial statements for fiscal year 2017. However, DOD still needs to address the seven critical capabilities that it has identified as necessary to achieve audit readiness.[9] Moreover, in its November 2016 FIAR Plan Status Report, DOD stated that it expects to receive disclaimers of opinion on its financial statements for a number of years.

Various efforts are also under way to address the other two major impediments to an audit of the consolidated financial statements. For example, during fiscal year 2016, Treasury continued to actively work with significant federal entities[10] to resolve differences in intragovernmental activity and balances between federal entities through its quarterly scorecard process.[11] This process highlights differences requiring the entities' attention, identifies differences that need to be resolved through a formal dispute resolution process,[12] and reinforces the entities' responsibilities to resolve intragovernmental differences. Treasury also continues to develop and refine policies and procedures over accounting for and reporting all significant activity and balances of the General Fund of the U.S. Government (General Fund),[13] and continues to improve its reconciliation process of the activity and balances between the General Fund and federal entity trading partners. Treasury is also in the process of performing an internal assessment of the audit readiness of the General Fund. Further, over the past few years, Treasury has implemented new systems to collect certain additional data from entities and to compile the consolidated financial statements and new or enhanced procedures to address certain internal control deficiencies detailed in our previously issued report.[14] To help address

[9]According to the April 2016 FIAR Guidance, these critical capabilities are related to DOD's inability to (1) provide a complete universe of transactions that is reconciled to feeder systems; (2) reconcile Fund Balance with Treasury (i.e., balance its checkbook); (3) provide supporting documentation for material adjustments to its financial records; (4) establish an auditable baseline/process for the existence, completeness, and rights of assets; (5) establish an auditable valuation baseline/process for the valuation of assets; (6) establish an auditable process for estimating and recording environmental and disposal liabilities; and (7) implement critical information technology general and application controls for material, financially relevant systems.

[10]OMB and Treasury have identified 39 federal entities that are significant to the U.S. government's fiscal year 2016 consolidated financial statements, including the 24 CFO Act agencies. See *Treasury Financial Manual*, vol. I, pt. 2, ch. 4700, for a listing of the 39 entities.

[11]For each quarter, Treasury produces a scorecard for each significant entity that reports various aspects of the entity's intragovernmental differences with its trading partners, including the composition of the differences by trading partner and category. Entities are expected to resolve, with their respective trading partners, the differences identified in their scorecards.

[12]When an entity and its respective trading partner cannot resolve an intragovernmental difference, the entity must request that Treasury resolve the dispute. Treasury will review the dispute and issue a decision on how to resolve the difference, which the entities must follow.

[13]The General Fund is a component of Treasury's central accounting function. It is a stand-alone reporting entity that comprises the activities fundamental to funding the federal government (e.g., issued budget authority, cash activity, and debt financing activities).

[14]GAO, *Management Report: Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*, GAO-16-621 (Washington, D.C.: July 13, 2016).

the magnitude of the issues in these areas, it will be important that Treasury continues to develop and implement its policies and procedures for General Fund-related activity and balances, including the use of the General Fund as a trading partner, and obtain an audit of the General Fund activity and balances. In addition to continued leadership by Treasury and OMB, strong and sustained commitment by federal entities is critical to fully address these issues.

The material weaknesses underlying these three major impediments have continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost as well as the financial and nonfinancial performance of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder the federal government from having reliable financial information to operate in an efficient and effective manner. Over the years, we have made a number of recommendations to OMB, Treasury, and DOD to address these issues.[15] These entities have taken or plan to take actions to address these recommendations.

In addition to the material weaknesses referred to above, we identified three other material weaknesses. These are the federal government's inability to (1) determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them,[16] (2) identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and (3) effectively manage its tax collection activities. Our audit report presents additional details concerning these material weaknesses and their effect on the accrual-based consolidated financial statements and on the management of federal government operations. Until the problems outlined in our audit report are adequately addressed, they will continue to have adverse implications for the federal government and American taxpayers.

Additionally, there are risks that certain factors could affect the federal government's financial condition in the future, including the following:

- The Pension Benefit Guaranty Corporation's (PBGC) financial future is uncertain because of long-term challenges related to PBGC's governance and funding structure. PBGC's liabilities exceeded its assets by over $79 billion as of the end of fiscal year 2016—an increase of over $3 billion from the end of fiscal year 2015 and of about $44 billion since 2013. PBGC reported that it is subject to potential further losses of $243 billion if plan terminations occur that are considered reasonably possible.

- In 2008, during the financial crisis, the federal government placed the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) under conservatorship and entered into preferred stock purchase agreements with these government-sponsored enterprises (GSE) to help ensure their financial stability. The agreements with the GSEs could affect the federal government's financial position. At the end of fiscal year 2016, the federal government continued to report about $109 billion of

[15]See GAO-16-621. In addition, see GAO, *DOD Financial Management – High Risk Issue*, accessed on January 12, 2017. http://www.gao.gov/key_issues/dod_financial_management/issue_summary#t=1. Further, other auditors have made recommendations to DOD to improve DOD's financial management.

[16]When excluding DOD's Defense Finance and Accounting Service Commercial Pay program, federal entity-reported estimates of improper payments totaled $144.3 billion in fiscal year 2016, an increase from the prior year estimate of $136.7 billion. This increase was mostly attributable to increased program outlays in HHS's Medicaid program.

investments in the GSEs, which is net of about $86 billion in valuation losses. The GSEs paid Treasury cash dividends of $11.5 billion and $20.4 billion during fiscal years 2016 and 2015, respectively. Although Treasury does not believe that any further draws by the GSEs are probable, the reported maximum remaining contractual commitment to the GSEs, if needed, is $258.1 billion. Importantly, the ultimate role of the GSEs in the mortgage market could affect the financial condition of the Federal Housing Administration, which in the past expanded its lending role in distressed housing and mortgage markets.

- The U.S. Postal Service (USPS) continues to be in a serious financial crisis as it has reached its borrowing limit of $15 billion and finished fiscal year 2016 with a reported net loss of $5.6 billion. USPS's business model is not viable and cannot fund its current level of services, operations, and obligations.[17] USPS's liabilities exceeded its assets by $56 billion as of the end of fiscal year 2016 and USPS reported an additional $39.5 billion in unfunded liabilities at that time for its retiree health and pension funds. USPS reported a total unfunded liability for its retiree health and pension funds of $73.4 billion, $33.9 billion of which relates to required prefunding payments for postal retirees' health benefits that have not been made and is included in the liabilities reported on its balance sheet.

Full implementation of the Digital Accountability and Transparency Act of 2014 (DATA Act) would enable federal agencies to report information that complements the annual audited financial statements and to provide much more detailed information on federal spending on federal programs, activities, and outcomes. The DATA Act holds great promise for improving the transparency and accountability of federal spending data by providing consistent, reliable, and complete data on federal spending and for helping decision makers in addressing the federal government's fiscal challenges. OMB and Treasury have taken significant steps toward implementing the DATA Act's various requirements, including establishing a data governance structure, developing government-wide data standards and technical specifications for data reporting, issuing guidance on how agencies should report certain data and provide quality assurances for submitted data, and designing a pilot for developing recommendations to reduce recipient reporting burden. Agencies have reported that they continue to face challenges implementing the DATA Act, including systems integration issues, lack of resources, evolving and complex reporting requirements, and inadequate guidance. Agencies are taking actions to mitigate these challenges; nevertheless, as we reported in December 2016, the information reported by agencies and their inspectors general indicates that some agencies are at increased risk of not fully meeting the May 2017 reporting deadline because of these challenges.[18] In order to fully and effectively implement the DATA Act, the federal government will need to continue addressing complex policy and technical issues. OMB and Treasury have made progress implementing 5 of our recommendations related to DATA Act implementation, as of December 2016. However, additional effort is needed to address 11 previous GAO recommendations that remain open.[19]

Resolving the problems outlined in our audit report is of utmost importance given the federal government's reported fiscal path. The comprehensive long-term fiscal projections presented in

[17]GAO, *U.S. Postal Service's Financial Viability – High Risk Issue*, accessed on January 12, 2017, http://www.gao.gov/key_issues/us_postal_service_financial_viability/issue_summary.

[18]GAO, *DATA Act: OMB and Treasury Have Issued Additional Guidance and Have Improved Pilot Design but Implementation Challenges Remain*, GAO-17-156 (Washington, D.C.: Dec. 8, 2016).

[19]See GAO-17-156, app. II, for a list of our previous recommendations relating to the DATA Act and their implementation status.

the Statement of Long-Term Fiscal Projections, and related information in Note 23 and in the unaudited Required Supplementary Information section of the *Fiscal Year 2016 Financial Report of the United States Government* (*2016 Financial Report*) show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path. GAO also prepares long-term federal fiscal simulations, using different sets of assumptions, which continue to show debt held by the public rising as a share of gross domestic product (GDP). Under GAO's Alternative simulation, which is discussed in our audit report, future spending in excess of receipts would be greater and debt held by the public as a share of GDP would grow more quickly than the projections in the *2016 Financial Report*. Under the Alternative simulation, debt held by the public as a share of GDP will surpass its historical high (106 percent in 1946) by 2032. Reliable and complete financial information for federal entities will be needed for making policy changes that effectively address the unsustainable long-term fiscal path. GAO plans to issue a report outlining its perspectives on the fiscal health of the federal government.

Our audit report on the U.S. government's consolidated financial statements would not be possible without the commitment and professionalism of inspectors general throughout the federal government who are responsible for annually auditing the financial statements of individual federal entities. We also appreciate the cooperation and assistance of Treasury and OMB officials as well as the federal entities' chief financial officers. We look forward to continuing to work with these individuals, the administration, and Congress to achieve the goals and objectives of federal financial management reform.

Our audit report begins on page 237. Our guide to the *Financial Report* is intended to help those who seek to obtain a better understanding of the *Financial Report* and is available on GAO's website at http://www.gao.gov.[20] In addition, the website includes a guide to understanding the differences between accrual and generally cash-based budget measures and provides a useful perspective on the different purposes that cash and accrual measures serve in providing a comprehensive picture of the federal government's fiscal condition today and over time.[21]

[20]GAO, *Understanding the Primary Components of the Annual Financial Report of the United States Government*, GAO-09-946SP (Washington, D.C.: September 2009).

[21]See http://www.gao.gov/special.pubs/longterm/deficit/, which is based on information in GAO, *Understanding Similarities and Differences between Accrual and Cash Deficits*, GAO-07-117SP (Washington, D.C.: December 2006). In January 2007 and 2008, we issued updates to this guide for fiscal years 2006 and 2007; see GAO-07-341SP (Washington, D.C.: January 2007) and GAO-08-410SP (Washington, D.C.: January 2008).

Our audit report was prepared under the direction of Robert F. Dacey, Chief Accountant, and J. Lawrence Malenich, Director, Financial Management and Assurance. If you have any questions, please contact me on (202) 512-5500 or them on (202) 512-3406.

Gene L. Dodaro
Comptroller General
of the United States

cc: The Majority Leader of the Senate
The Minority Leader of the Senate
The Majority Leader of the House of Representatives
The Minority Leader of the House of Representatives

Financial Statements of the United States Government for the Years Ended September 30, 2016, and 2015

The consolidated financial statements of the United States Government (Government) were prepared using U.S. Generally Accepted Accounting Principles (GAAP). The consolidated financial statements include the accrual-based financial statements and the sustainability financial statements, which are discussed in more detail below, and the related notes to the consolidated financial statements. Collectively, the accrual-based financial statements, the sustainability financial statements, and the notes represent basic information that is deemed essential for the consolidated financial statements to be presented in conformity with GAAP.

ACCRUAL-BASED FINANCIAL STATEMENTS

The accrual-based financial statements present historical information on what the federal government owns (assets) and owes (liabilities) at the end of the year, what came in (revenues) and what went out (net costs) during the year, and how accrual-based net operating costs of the federal government reconcile to the budget deficit and changes in its cash balances during the year. The following sections discuss each of the accrual-based financial statements.

Statements of Net Cost

These statements present the net cost of the Government operations for fiscal years 2016 and 2015, including the operations related to funds from dedicated collections (funds financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time). The Government's fiscal year begins October 1 and ends September 30. Costs and earned revenues are categorized on the Statement of Net Cost by significant entity, providing greater accountability by showing the relationship of the agencies' net cost to the governmentwide net cost. Costs and earned revenues are presented in this *Financial Report* by significant entity on an accrual basis, while the budget presents costs and revenues by outlays and receipts, generally on a cash basis. The focus of the budget of the United States is by agency. Budgets are prepared, defended, and monitored by agency. In reporting by agency, we are assisting the external users in assessing the budget integrity, operating performance, stewardship, and systems and controls of the Government.

These statements contain the following four components:

- Gross cost—is the full cost of all the departments and entities excluding (gain)/loss from changes in assumptions. These costs are assigned on a cause-and-effect basis, or reasonably allocated to the corresponding entities.
- Earned revenue—is exchange revenue resulting from the Government providing goods and services to the public at a price.
- (Gain)/loss from changes in assumptions—is the gain or loss from changes in long-term assumptions used to measure the liabilities reported for federal civilian and military employee pensions, other post-employment benefits, and other retirement benefits, including veterans' compensation.
- Net cost—is computed by subtracting earned revenue from gross cost, adjusted by the (gain)/loss from changes in assumptions.

Individual agency net cost amounts will differ from the agency's financial statements primarily because of allocations of Office of Personnel Management (OPM) benefit program costs and intragovernmental eliminations, as adjusted for buy/sell costs, buy/sell revenues, and imputed costs. Because of its specific function, most of the costs originally associated with OPM have been allocated to their user agencies for governmentwide reporting purposes. The remaining costs for OPM on the Statements of Net Cost are the administrative operating costs, the expenses from prior costs from health and pension plan amendments, and the actuarial gains and losses, if applicable. With regard to intragovernmental buy/sell costs and related revenues, the amounts recognized by each agency are added to, and subtracted from, respectively, the individual

agency non-federal net cost amounts. Because of the specific functions of the General Services Administration (GSA), as the primary provider of goods and services to federal agencies, once GSA's net cost is adjusted for its intragovernmental buy/sell costs and related revenues, the remaining costs for GSA on the Statements of Net Cost are its administrative operating costs. In addition, the intragovernmental imputed costs recognized for the receipt of goods and services, financed in whole or part by the providing agencies, are added to the individual agency non-federal net cost amounts. The interest on securities issued by the Department of the Treasury (Treasury) and held by the public is reported on Treasury's financial statements, but, because of its importance and the dollar amounts involved, it is reported separately in these statements.

Statements of Operations and Changes in Net Position

These statements report the results of Government operations, net operating costs, which include the results of operations for funds from dedicated collections. They include non-exchange revenues, which are generated from transactions that do not require a Government entity to give value directly in exchange for the inflow of resources. The Government does not "earn" the non-exchange revenue. These are generated principally by the Government's sovereign power to tax, levy duties, and assess fines and penalties. These statements also include the net cost reported in the Statement of Net Cost. They further include certain adjustments and unreconciled transactions that affect the net position.

Revenue

Inflows of resources to the government that the government demands or that it receives by donations are identified as non-exchange revenue. The inflows that it demands include individual income tax and tax withholdings, excise taxes, corporation income taxes, unemployment taxes, custom duties, and estate and gift taxes. The non-exchange revenue is recognized when collected and adjusted for the change in net measurable and legally collectable amounts receivable.

Individual income tax and tax withholdings include *Federal Insurance Contributions Act* (FICA)/*Self-Employment Contributions Act* (SECA) taxes and other taxes.

Excise taxes consist of taxes collected for various items, such as airline tickets, gasoline products, distilled spirits and imported liquor, tobacco, firearms, and other items.

Other taxes and receipts include Federal Reserve Banks (FRBs) earnings, tax related fines, penalties and interest, and railroad retirement taxes.

Miscellaneous earned revenues consist of earned revenues received from the public with virtually no associated cost. These revenues include rents and royalties on the Outer Continental Shelf Lands resulting from the leasing and development of mineral resources on public lands.

Generally, funds from dedicated collections are financed by specifically identified revenues, provided to the government by non-federal sources, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits or purposes, and must be accounted for separately from the Government's general revenue. See Note 20—Funds from Dedicated Collections for detailed information.

Intragovernmental interest represents interest earned from the investment of surplus dedicated collections, which finance the deficit spending of all other fund's non-dedicated operations. These investments are recorded as intragovernmental debt holdings and are included in Note 11—Federal Debt Securities Held by the Public and Accrued Interest, in the table titled Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts. These interest earnings and the associated investments are eliminated in the consolidation process.

Net Cost of Government Operations

The net cost of Government operations—gross cost (including gains/losses from changes in assumptions) less earned revenue—flows through from the Statements of Net Cost. The net cost associated with funds from dedicated collections activities is separately reported and starting in fiscal year 2015, the intragovernmental net cost associated with funds from dedicated collections was separately reported.

Intragovernmental Transfers

Intragovernmental transfers reflect budgetary and other financing sources for funds from dedicated collections, excluding financing sources related to non-exchange revenues, intragovernmental interest, and miscellaneous revenues. These intragovernmental transfers include appropriations, transfers, and other financing sources. These amounts are labeled as "other changes in fund balance" in Note 20—Funds from Dedicated Collections. Some transfers reflect amounts required by statute to be transferred from the General Fund of the U.S. Government (General Fund) to funds from dedicated collections. For Supplementary Medical Insurance (SMI), transfers from the General Fund financed 76 percent and 78 percent of 2016 program costs to Part B and D, respectively.

Unmatched Transactions and Balances

Unmatched transactions and balances are adjustments needed to bring the change in net position into balance due primarily to unreconciled intragovernmental differences. See Note1.S—Unmatched Transactions and Balances for detailed information.

The unmatched transactions and balances are included in net operating cost to make the sum of net operating costs and prior period adjustments for the year equal to the change in the net position balance.

Net Operating Cost

The net operating cost equals revenue less net cost of Government operations (that flows from the Statement of Net Cost) adjusted by unmatched transactions and balances (see Note 1.S—Unmatched Transactions and Balances).

Net Position, Beginning of Period

The net position, beginning of period, reflects the amount reported on the prior year's balance sheet as of the end of that fiscal year. The net position for funds from dedicated collections is shown separately.

Prior-period adjustments are revisions to the beginning net position presented on the prior year financial statements due to corrections of material errors or certain changes in accounting principles. See Note 1.T—Prior-Period Adjustments for detailed information.

Net Position, End of Period

The net position, end of period, reflects the amount as of the end of the fiscal year. The net position for funds from dedicated collections is separately shown.

Reconciliations of Net Operating Cost and Unified Budget Deficit

These statements reconcile the results of operations (net operating cost) on the Statements of Operations and Changes in Net Position (SOCNP) to the unified budget deficit. The premise of the reconciliation is that the accrual and budgetary accounting basis share transaction data.

Receipts and outlays in the budget are measured primarily on a cash basis and differ from the accrual basis of accounting used in the *Financial Report*. Refer to Note 1.B—Basis of Accounting and Revenue Recognition for details. These statements begin with the net results of operations (net operating cost) and report activities where the basis of accounting for the components of net operating cost and the unified budget deficit differ.

In fiscal year 2016, the presentation for the Reconciliation of Net Operating Cost and Unified Budget Deficit was changed, and fiscal year 2015 amounts were reclassified to conform with the new presentation.

Components of Net Operating Cost Not Part of the Budget Deficit

This information includes the operating components, such as the changes in benefits payable for veterans, military and civilian employees, environmental and disposal liabilities, and depreciation expense, not included in the budget results.

Components of the Budget Deficit Not Part of Net Operating Cost

This information includes the budget components, such as capitalized fixed assets (that are recorded as outlays in the budget when purchased and reflected in net operating cost through depreciation expense over the useful life of the asset) and increases in other assets that are not included in the operating results.

Statements of Changes in Cash Balance from Unified Budget and Other Activities

The primary purpose of these statements is to report how the annual unified budget deficit relates to the change in the Government's cash and other monetary assets, as well as debt held by the public. It explains why the unified budget deficit normally would not result in an equivalent change in the Government's cash and other monetary assets.

These statements reconcile the unified budget deficit to the change in cash and other monetary assets during the fiscal year. They also serve to explain how the budget deficits were financed. A budget deficit is the result of outlays (expenditures) exceeding receipts (revenue) during a particular fiscal year.

The budget deficit is primarily financed through borrowings from the public. Other transactions, such as the payment of interest on Treasury securities held by the public, also require cash disbursements and are not part of the deficit. Additionally, the budget deficit includes certain amounts that are recognized in the budget, but will be disbursed in a future period, or are adjustments that did not affect the cash balance. These amounts include interest accrued on Treasury securities held by the public, as well as subsidy expense related to direct and guaranteed loans.

These statements show the adjustments for non-cash outlays included in the budget, and items affecting the cash balance not included in the budget, to explain the change in cash and other monetary assets.

In fiscal year 2016, the presentation for the Statements of Changes in Cash Balance from Unified Budget and Other Activities was changed, and fiscal year 2015 amounts were reclassified to conform with the new presentation.

Balance Sheets

The balance sheets show the Government's assets, liabilities, and net position. When combined with stewardship information, this information presents a more comprehensive understanding of the Government's financial position. The net position for funds from dedicated collections is shown separately.

Assets

Assets included on the balance sheets are resources of the Government that remain available to meet future needs. The most significant assets that are reported on the balance sheets are loans receivable, net; property, plant, and equipment (PP&E), net; inventories and related property, net; and cash and other monetary assets. There are, however, other significant resources available to the Government that extend beyond the assets presented in these balance sheets. Those resources include Stewardship Land and Heritage Assets in addition to the Government's sovereign powers to tax and set monetary policy.

Liabilities and Net Position

Liabilities are obligations of the Government resulting from prior actions that will require financial resources. The most significant liabilities reported on the balance sheets are federal debt securities held by the public and accrued interest, and federal employee and veteran benefits payable. Liabilities also include environmental and disposal liabilities, benefits due and payable, as well as insurance and guarantee program liabilities.

As with reported assets, the Government's responsibilities, policy commitments, and contingencies are much broader than these reported balance sheet liabilities. They include the social insurance programs reported in the Statements of Social Insurance and disclosed in the Required Supplementary Information (RSI)—Social Insurance section, fiscal long-term projections of non-interest spending reported in the Statements of Long-Term Fiscal Projections, and a wide range of other programs under which the Government provides benefits and services to the people of this Nation, as well as certain future loss contingencies.

The Government has entered into contractual commitments requiring the future use of financial resources and has unresolved contingencies where existing conditions, situations, or circumstances create uncertainty about future losses. Commitments and contingencies that do not meet the criteria for recognition as liabilities on the balance sheets, but for which there is at least a reasonable possibility that losses have been incurred, are disclosed in Note 18—Contingencies and Note 19—Commitments.

The collection of certain taxes and other revenue is credited to the corresponding funds from dedicated collections that will use these funds to meet a particular Government purpose. If the collections from taxes and other sources exceed the payments to the beneficiaries, the excess revenue is invested in Treasury securities or deposited in the General Fund; therefore, the trust fund balances do not represent cash. An explanation of the trust funds for social insurance is included in Note 20—Funds from Dedicated Collections. That note also contains information about trust fund receipts, disbursements, and assets.

Due to its sovereign power to tax and borrow, and the country's wide economic base, the Government has unique access to financial resources through generating tax revenues and issuing federal debt securities. This provides the Government with the ability to meet present obligations and those that are anticipated from future operations, and are not reflected in net position.

The net position is the residual difference between assets and liabilities and is the cumulative results of operations since inception. For detailed components that comprise the net position, refer to the section "Statement of Operations and Changes in Net Position."

SUSTAINABILITY FINANCIAL STATEMENTS

The sustainability financial statements are comprised of the Statements of Long-Term Fiscal Projections, covering all federal government programs, and the Statements of Social Insurance and the Statement of Changes in Social Insurance Amounts, covering social insurance programs (Social Security, Medicare, Railroad Retirement, and Black Lung programs). The sustainability financial statements are designed to illustrate the relationship between projected receipts and expenditures if current policy is continued over a 75 year time horizon.[1] For this purpose, the projections assume that scheduled social insurance benefit payments would continue after related trust funds are projected to be exhausted, contrary to current law, and that debt could continue to rise indefinitely without severe economic consequences. The sustainability financial statements are intended to help citizens understand current policy and the importance and magnitude of policy reforms necessary to make it sustainable.

By accounting convention, the Statements of Social Insurance do not include projected general revenues that, under current law, would be used to finance the remainder of the expenditures in excess of revenues for Medicare Parts B and D reported in the Statements of Social Insurance. The Statements of Long-Term Fiscal Projections include all revenues (including general revenues) of the federal government.

[1] With the exception of the Black Lung program, which has a projection period through September 30, 2040.

Statements of Long-Term Fiscal Projections

The Statements of Long-Term Fiscal Projections are intended to assist readers of the Government's financial statements in assessing the financial condition of the federal government and how the Government's financial condition has changed (improved or deteriorated) during the year and may change in the future. They are also intended to assist readers in assessing whether future budgetary resources of the Government will likely be sufficient to sustain public services and to meet obligations as they come due, assuming that current policy for Federal Government public services and taxation is continued without change.

The Statements of Long-Term Fiscal Projections display the present value of 75-year projections by major category of the Federal Government's receipts and non-interest spending. These projections show the extent to which future receipts of the Government exceed or fall short of the Government's non-interest spending. The projections are presented both in terms of present value dollars and in terms of present value dollars as a percent of present value Gross Domestic Product (GDP). The projections are on the basis of policies currently in place and are neither forecasts nor predictions. These projections are consistent with the projections for Social Security and Medicare presented in the Statements of Social Insurance and are based on the same economic and demographic assumptions as underlie the Statements of Social Insurance. Note 23, Long-Term Fiscal Projections, further explains the methods used to prepare these projections and provides additional information such as the fiscal gap. Unaudited required supplementary information further assesses the sustainability of current fiscal policy and provides results based on alternative assumptions to those used in the basic statement.

As discussed further in Note 23, a sustainable policy is one where the ratio of debt held by the public to GDP (the debt-to-GDP ratio) is stable or declining over the long term. GDP measures the size of the Nation's economy in terms of the total value of all final goods and services that are produced in a year. Considering financial results relative to GDP is a useful indicator of the economy's capacity to sustain the Government's many programs.

Statements of Social Insurance and Changes in Social Insurance Amounts

The Statements of Social Insurance provide estimates of the status of the most significant social insurance programs: Social Security, Medicare, Railroad Retirement, and Black Lung. They are administered by the Social Security Administration (SSA), U.S. Department of Health and Human Services (HHS), the Railroad Retirement Board (RRB), and the Department of Labor (DOL), respectively. The estimates are actuarial present values[2] of the projections and are based on the economic and demographic assumptions representing the trustees' reasonable estimates as set forth in the relevant Social Security and Medicare trustees' reports as well as in the agency financial reports of HHS, SSA, and DOL (Black Lung) and in the relevant agency performance and accountability report for the RRB. The projections in this year's report, with one exception related to Medicare Part A, are based on current law; that is, they assume that laws on the books will be implemented and adhered to with respect to scheduled taxes, premium revenues, and payments to providers and health plans. The one exception is that the projections disregard payment reductions that would result from the projected depletion of the Medicare Hospital Insurance (Part A) Trust Fund. Under current law, payments would be reduced to levels that could be covered by incoming tax and premium revenues when the Medicare Hospital Insurance (Part A) Trust Fund is depleted.

The magnitude and complexity of social insurance programs, coupled with the extreme sensitivity of projections relating to the many assumptions of the programs, produce a wide range of possible results. In preparing the Statements of Social Insurance, Government management considers and selects assumptions and data that it believes provide a reasonable basis for the assertions in the statements. However, because of the large number of factors that affect the Statements of Social Insurance plus the fact that such assumptions are inherently subject to substantial uncertainty (arising from the likelihood of future events, significant uncertainties, and contingencies), there will be differences between the estimates in the Statements of Social Insurance and the actual results, and those differences may be material. Note 22—Social Insurance describes the social insurance programs, reports long-range estimates that can be used to assess the financial condition of the programs, and explains some of the factors that impact the various programs. The Statements of Changes in Social Insurance Amounts reconcile the change between the current valuation period and the prior valuation period.

[2] Present values recognize that a dollar paid or collected in the future is worth less than a dollar today, because a dollar today could be invested and earn interest. To calculate a present value, future amounts are thus reduced using an assumed interest rate, and those reduced amounts are summed.

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United States Government
Statement of Net Cost
for the Year Ended September 30, 2016

(In billions of dollars)	Gross Cost	Earned Revenue	Subtotal	(Gain)/Loss from Changes in Assumptions	Net Cost
Department of Health and Human Services	1,170.0	96.1	1,073.9	0.4	1,074.3
Social Security Administration	982.1	0.3	981.8	-	981.8
Department of Veterans Affairs	276.5	4.9	271.6	377.5	649.1
Department of Defense	721.9	55.1	666.8	(57.6)	609.2
Interest on Treasury Securities Held by the Public	273.0	-	273.0	-	273.0
Department of Agriculture	142.1	8.5	133.6	-	133.6
Department of the Treasury	148.7	19.4	129.3	-	129.3
Department of Transportation	80.7	0.9	79.8	-	79.8
Department of Education	103.1	29.9	73.2	-	73.2
Department of Energy	68.6	4.3	64.3	-	64.3
Department of Homeland Security	66.5	13.1	53.4	0.2	53.6
Department of Labor	46.4	-	46.4	-	46.4
Department of Justice	38.7	1.6	37.1	-	37.1
Defense Security Cooperation Agency	36.0	-	36.0	-	36.0
Department of Housing and Urban Development	31.2	1.7	29.5	-	29.5
Department of State	32.6	4.7	27.9	(0.1)	27.8
National Aeronautics and Space Administration	20.0	0.2	19.8	-	19.8
Department of the Interior	19.2	2.5	16.7	-	16.7
U.S. Agency for International Development	12.6	-	12.6	-	12.6
Railroad Retirement Board	15.3	3.9	11.4	-	11.4
Federal Communications Commission	10.4	0.5	9.9	-	9.9
Department of Commerce	12.5	3.3	9.2	-	9.2
Environmental Protection Agency	9.0	0.4	8.6	-	8.6
National Science Foundation	7.0	-	7.0	-	7.0
U.S. Postal Service	77.2	70.4	6.8	-	6.8
Pension Benefit Guaranty Corporation	11.4	6.7	4.7	-	4.7
Smithsonian Institution	0.8	-	0.8	-	0.8
Millennium Challenge Corporation	0.6	-	0.6	-	0.6
Small Business Administration	0.5	0.3	0.2	-	0.2
U.S. Nuclear Regulatory Commission	0.9	0.8	0.1	-	0.1
General Services Administration	0.6	0.7	(0.1)	-	(0.1)
Overseas Private Investment Corporation	-	0.1	(0.1)	-	(0.1)
Securities and Exchange Commission	1.7	2.0	(0.3)	-	(0.3)
Farm Credit System Insurance Corporation	-	0.3	(0.3)	-	(0.3)
National Credit Union Administration	(0.7)	0.1	(0.8)	-	(0.8)
Tennessee Valley Authority	9.3	10.6	(1.3)	-	(1.3)
Export-Import Bank of the United States	(0.2)	1.2	(1.4)	-	(1.4)
Office of Personnel Management	60.2	21.3	38.9	(47.1)	(8.2)
Federal Deposit Insurance Corporation	0.2	9.5	(9.3)	-	(9.3)
All other entities	21.1	1.3	19.8	-	19.8
Total	4,507.7	376.6	4,131.1	273.3	4,404.4

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

United States Government
Statement of Net Cost
for the Year Ended September 30, 2015 (Restated)

(In billions of dollars)	Gross Cost	Earned Revenue	Subtotal	(Gain)/Loss from Changes in Assumptions	Net Cost
Department of Health and Human Services	1,130.9	101.3	1,029.6	(0.1)	1,029.5
Social Security Administration	945.0	0.3	944.7	-	944.7
Department of Veterans Affairs	193.1	4.8	188.3	(13.0)	175.3
Department of Defense	634.9	45.5	589.4	(27.5)	561.9
Interest on Treasury Securities Held by the Public	250.8	-	250.8	-	250.8
Department of Agriculture	147.7	9.1	138.6	-	138.6
Department of the Treasury	146.0	29.3	116.7	-	116.7
Department of Transportation	76.1	0.8	75.3	-	75.3
Department of Education	71.3	26.6	44.7	-	44.7
Department of Energy	76.5	4.6	71.9	-	71.9
Department of Homeland Security	60.2	12.1	48.1	4.1	52.2
Department of Labor	45.8	-	45.8	-	45.8
Department of Justice	32.3	1.7	30.6	-	30.6
Defense Security Cooperation Agency	38.8	-	38.8	-	38.8
Department of Housing and Urban Development	32.7	1.5	31.2	-	31.2
Department of State	30.2	4.3	25.9	0.1	26.0
National Aeronautics and Space Administration	19.8	0.2	19.6	-	19.6
Department of the Interior	19.2	2.7	16.5	-	16.5
U.S. Agency for International Development	12.7	0.1	12.6	-	12.6
Railroad Retirement Board	16.3	3.4	12.9	-	12.9
Federal Communications Commission	9.6	0.3	9.3	-	9.3
Department of Commerce	12.3	3.2	9.1	-	9.1
Environmental Protection Agency	9.3	0.7	8.6	-	8.6
National Science Foundation	7.0	-	7.0	-	7.0
U.S. Postal Service	73.8	67.9	5.9	-	5.9
Pension Benefit Guaranty Corporation	23.7	8.0	15.7	-	15.7
Smithsonian Institution	0.8	-	0.8	-	0.8
Millennium Challenge Corporation	0.8	-	0.8	-	0.8
Small Business Administration	(0.5)	0.4	(0.9)	-	(0.9)
U.S. Nuclear Regulatory Commission	1.0	0.8	0.2	-	0.2
General Services Administration	0.3	0.6	(0.3)	-	(0.3)
Overseas Private Investment Corporation	(0.1)	0.1	(0.2)	-	(0.2)
Securities and Exchange Commission	1.5	2.0	(0.5)	-	(0.5)
Farm Credit System Insurance Corporation	-	0.2	(0.2)	-	(0.2)
National Credit Union Administration	-	0.3	(0.3)	-	(0.3)
Tennessee Valley Authority	9.8	10.9	(1.1)	-	(1.1)
Export-Import Bank of the United States	(0.6)	1.3	(1.9)	-	(1.9)
Office of Personnel Management	104.9	20.3	84.6	17.1	101.7
Federal Deposit Insurance Corporation	(6.5)	8.6	(15.1)	-	(15.1)
All other entities	20.8	1.7	19.1	-	19.1
Total	4,248.2	375.6	3,872.6	(19.3)	3,853.3

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

United States Government
Statement of Operations and Changes in Net Position
for the Year Ended September 30, 2016

(In billions of dollars)	Funds other than those from Dedicated Collections (Combined)	Funds from Dedicated Collections (Note 20) (Combined)	Eliminations	Consolidated
		2016		
Revenue (Note 17):				
Individual income tax and tax withholdings	1,525.5	1,077.7	-	2,603.2
Corporation income taxes	294.3	-	-	294.3
Excise taxes	42.1	58.3	-	100.4
Unemployment taxes	-	46.9	-	46.9
Customs duties	33.3	-	-	33.3
Estate and gift taxes	21.0	-	-	21.0
Other taxes and receipts	185.1	42.9	-	228.0
Miscellaneous earned revenues	15.3	2.9	-	18.2
Intragovernmental interest	-	102.8	(102.8)	-
Total Revenue	2,116.6	1,331.5	(102.8)	3,345.3
Net Cost of Government Operations:				
Net cost	2,798.7	1,605.7	-	4,404.4
Intragovernmental net cost	(8.7)	8.7	-	-
Intragovernmental interest	102.8	-	(102.8)	-
Total net cost	2,892.8	1,614.4	(102.8)	4,404.4
Intragovernmental transfers	(409.5)	409.5	-	-
Unmatched transactions and balances (Note 1.S)	11.7	-	-	11.7
Net operating (cost)/revenue	(1,174.0)	126.6	-	(1,047.4)
Net position, beginning of period	(21,491.3)	3,247.7	-	(18,243.6)
Prior period adjustments–changes in accounting principles (Note 1.T)	(1.4)	-	-	(1.4)
Net operating (cost)/revenue	(1,174.0)	126.6	-	(1,047.4)
Net position, end of period	(22,666.7)	3,374.3	-	(19,292.4)

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

United States Government
Statement of Operations and Changes in Net Position
for the Year Ended September 30, 2015 (Restated)

(In billions of dollars)	Funds other than those from Dedicated Collections (Combined)	Funds from Dedicated Collections (Note 20) (Combined)	Eliminations	Consolidated
		2015		
Revenue (Note 17):				
Individual income tax and tax withholdings	1,521.1	1,024.1	-	2,545.2
Corporation income taxes	339.8	-	-	339.8
Excise taxes	44.2	57.5	-	101.7
Unemployment taxes	-	49.1	-	49.1
Customs duties	33.6	-	-	33.6
Estate and gift taxes	19.1	-	-	19.1
Other taxes and receipts	165.6	37.3	-	202.9
Miscellaneous earned revenues	38.8	3.8	-	42.6
Intragovernmental interest	-	108.4	(108.4)	-
Total Revenue	2,162.2	1,280.2	(108.4)	3,334.0
Net Cost of Government Operations:				
Net cost	2,294.9	1,558.4	-	3,853.3
Intragovernmental net cost	(7.2)	7.2	-	-
Intragovernmental interest	108.4	-	(108.4)	-
Total net cost	2,396.1	1,565.6	(108.4)	3,853.3
Intragovernmental transfers	(335.2)	335.2	-	-
Unmatched transactions and balances (Note 1.S)	5.1	-	-	5.1
Net operating (cost)/revenue	(564.0)	49.8	-	(514.2)
Net position, beginning of period	(20,898.3)	3,197.6	-	(17,700.7)
Prior period adjustments (Note 1.T, 1.V and 20)	(29.0)	0.3	-	(28.7)
Net operating (cost)/revenue	(564.0)	49.8	-	(514.2)
Net position, end of period	(21,491.3)	3,247.7	-	(18,243.6)

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

United States Government
Reconciliations of Net Operating Cost and Unified Budget Deficit
for the Years Ended September 30, 2016, and 2015

(In billions of dollars)	2016	Restated 2015
Net operating cost	(1,047.4)	(514.2)
Components of net operating cost not part of the budget deficit		
Excess of accrual-basis expenses over budget outlays		
* Federal employee and veteran benefits payable		
Pensions and accrued benefits	(106.9)	37.9
Veterans compensation and burial benefits	477.7	11.5
Post-retirement health and accrued benefits	56.8	(2.1)
Other benefits	9.4	52.5
Subtotal - federal employee and veteran benefits payable	437.0	99.8
Insurance and guarantee program liabilities	9.9	2.1
* Environmental and disposal liabilities	35.0	42.5
Other liabilities	9.8	45.8
* Accounts payable	(5.9)	(0.7)
* Benefits due and payable	4.3	22.3
Subtotal - excess of accrual-basis expenses over budget outlays	490.1	211.8
Amortized expenses not included in budget outlays		
Property, plant, and equipment depreciation expense	52.2	54.5
Other expenses that are not reported as budget outlays		
Property, plant, and equipment disposals and revaluations	(24.9)	(47.0)
Agencies year-end credit reform subsidy re-estimates	10.4	(2.3)
Excess of accrual-basis revenue over budget receipts		
* Accounts receivable, net	(7.4)	(12.5)
* Taxes receivable, net	(8.1)	(1.3)
Other revenue and gains that are not budget receipts		
* Investments in government-sponsored enterprises	(2.3)	(10.5)
Deposit fund balances	(0.7)	(19.1)
Subtotal - components of net operating cost not part of budget deficit	509.3	173.6
Components of the budget deficit that are not part of net operating cost		
Budget receipts not included in net operating cost		
Credit reform and other loan activities	9.5	4.8
Budget outlays not included in net operating cost		
Acquisition of capital assets	(81.5)	(54.5)
Debt and equity securities	0.5	11.0
* Other assets	21.3	(2.9)
* Inventories and related property	6.3	(2.2)
Effect of prior year agencies credit reform subsidy re-estimates	2.3	(24.5)
Subtotal - components of the budget deficit that are not part of net operating cost	(41.6)	(68.3)
Other		
All other reconciling items	(7.7)	(30.0)
Unified budget deficit	(587.4)	(438.9)

* The amounts represent the year over year net change in the Balance Sheet line items.

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

United States Government
Statements of Changes in Cash Balance from Unified Budget and Other Activities for the Years Ended September 30, 2016, and 2015

(In billions of dollars)	2016	Reclass 2015
Cash flow from unified budget activities		
Total unified budgetary receipts	3,266.7	3,248.7
Total unified budgetary outlays	(3,854.1)	(3,687.6)
Unified budget deficit	(587.4)	(438.9)
Adjustments for non-cash outlays included in the unified budget		
Interest accrued on Treasury securities held by the public	264.1	245.4
Agencies year-end credit reform subsidy re-estimates	(12.7)	26.8
Subsidy expense accrued under direct loan & guarantee programs	11.8	(22.0)
Subtotal - adjustments for non-cash transactions in unified budget	263.2	250.2
Cash flow from activities not included in unified budget		
Cash flow from non-budget activities		
Interest paid on Treasury securities held by the public	(262.7)	(243.5)
Other direct loan transactions	(80.3)	(119.9)
Repayment of principal on direct loans	(11.6)	17.4
Other guaranteed loan transactions	(10.2)	9.8
Miscellaneous liabilities	1.6	(0.3)
Deposit fund liability balances	(0.7)	20.5
Seignorage	0.6	0.6
Subtotal - cash flow from non-budget activities	(363.3)	(315.4)
Cash flow from monetary transactions		
Loans to the IMF	0.9	3.0
Other monetary assets	1.9	0.6
Special drawing rights	(0.3)	(2.9)
Subtotal - cash flow from monetary transactions	2.5	0.7
Cash flow from financing		
Borrowing from the public	8,390.4	7,037.5
Repayment of debt held by the public	(7,343.3)	(6,700.6)
Effect of uninvested principal from the Thrift Savings Plan (TSP) G Fund	(203.2)	203.2
Agency securities	0.1	0.1
Subtotal - cash flow from financing	844.0	540.2
Other	0.5	3.4
Change in cash balance	159.5	40.2
Beginning cash balance	305.1	264.9
Ending cash balance	464.6	305.1

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

United States Government
Balance Sheets
as of September 30, 2016, and 2015

(In billions of dollars)	2016	Restated 2015
Assets:		
Cash and other monetary assets (Note 2)	464.6	305.1
Accounts and taxes receivable, net (Note 3)	133.3	117.8
Loans receivable, net (Note 4)	1,277.6	1,216.0
Inventories and related property, net (Note 5)	314.3	320.6
Property, plant and equipment, net (Note 6)	979.5	925.3
Debt and equity securities (Note 7)	48.2	104.4
Investments in government-sponsored enterprises (Note 8)	108.6	106.3
Other assets (Note 9)	144.4	165.7
Total assets	3,470.5	3,261.2
Stewardship land and heritage assets (Note 24)		
Liabilities:		
Accounts payable (Note 10)	62.4	68.3
Federal debt securities held by the public and accrued interest (Note 11)	14,221.1	13,172.5
Federal employee and veteran benefits payable (Note 12)	7,209.4	6,772.4
Environmental and disposal liabilities (Note 13)	446.6	411.6
Benefits due and payable (Note 14)	218.2	213.9
Insurance and guarantee program liabilities (Note 15)	122.3	170.3
Loan guarantee liabilities (Note 4)	18.2	36.3
Other liabilities (Note 16)	464.7	659.5
Total liabilities	22,762.9	21,504.8
Contingencies (Note 18) and Commitments (Note 19)		
Net Position:		
Funds from Dedicated Collections (Note 20)	3,374.3	3,247.7
Funds other than those from Dedicated Collections	(22,666.7)	(21,491.3)
Total net position	(19,292.4)	(18,243.6)
Total liabilities and net position	3,470.5	3,261.2

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

United States Government
Statements of Long-Term Fiscal Projections (Note 23)
Present Value of 75 Year Projections as of September 30, 2016 and 2015[1]

	Dollars in Trillions			Percent of GDP[2]		
	2016	2015	Change	2016	2015	Change
Receipts:						
Social Security Payroll Taxes	56.3	52.4	3.9	4.3	4.4	(0.1)
Medicare Payroll Taxes	18.8	17.4	1.4	1.4	1.5	-
Individual Income Taxes	139.0	127.8	11.2	10.7	10.7	-
Other Receipts	47.5	43.5	3.9	3.6	3.6	-
Total Receipts	261.6	241.2	20.4	20.1	20.2	(0.1)
Non-interest Spending:						
Social Security	75.6	70.0	5.6	5.8	5.9	-
Medicare Part A[3]	26.5	24.0	2.5	2.0	2.0	-
Medicare Parts B & D[4]	31.3	28.7	2.6	2.4	2.4	-
Medicaid	31.7	27.3	4.4	2.4	2.3	0.1
Other Mandatory	41.6	36.8	4.8	3.2	3.1	0.1
Defense Discretionary	32.0	28.6	3.4	2.5	2.4	0.1
Non-defense Discretionary	33.6	30.0	3.7	2.6	2.5	0.1
Total Non-interest Spending	272.2	245.3	26.9	20.9	20.5	0.4
Non-interest Spending less Receipts	10.6	4.1	6.5	0.8	0.3	0.5

[1]75-year present value projections for 2016 are as of 9/30/2016 for the period FY 2017-2091; projections for 2015 are as of 09/30/2015 for the period FY 2016-2090.
[2]The 75-year present value of nominal Gross Domestic Product (GDP), which drives the calculations above is $1,302.8 trillion starting in FY 2017, and was $1,196.3 trillion starting in FY 2016.
[3]Represents portions of Medicare supported by payroll taxes.
[4]Represents portions of Medicare supported by general revenues. Consistent with the President's Budget, outlays for Parts B & D are presented net of premiums.

Totals may not equal the sum of components due to rounding.

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

United States Government
Statements of Social Insurance (Note 22)
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

(In trillions of dollars)	2016	2015	2014	2013	2012
Federal Old-age, Survivors and Disability Insurance (Social Security):[16]					
Revenue (Contributions and Dedicated Taxes) from:					
Participants who have attained eligibility age (age 62 and over)	1.3	1.2	1.0	0.9	0.8
Participants who have not attained eligibility age	29.3	27.8	25.4	24.6	22.7
Future participants	29.7	26.6	24.6	23.4	21.6
All current and future participants	60.3	55.5	51.0	48.9	45.2
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 62 and over)	(13.6)	(12.8)	(11.9)	(11.0)	(9.8)
Participants who have not attained eligibility age	(48.4)	(45.3)	(42.4)	(40.6)	(37.8)
Future participants	(12.4)	(10.9)	(10.0)	(9.6)	(8.9)
All current and future participants	(74.4)	(69.0)	(64.3)	(61.2)	(56.5)
Present value of future expenditures in excess of future revenue	(14.1)[1]	(13.4)[2]	(13.3)[3]	(12.3)[4]	(11.3)[5]
Federal Hospital Insurance (Medicare Part A):[16]					
Revenue (Contributions and Dedicated Taxes) from:					
Participants who have attained eligibility age (age 65 and over)	0.5	0.4	0.3	0.3	0.3
Participants who have not attained eligibility age	10.3	9.1	8.4	8.1	7.9
Future participants	10.0	8.4	7.8	7.7	7.4
All current and future participants	20.7	17.9	16.5	16.2	15.6
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(4.3)	(3.8)	(3.5)	(3.4)	(3.4)
Participants who have not attained eligibility age	(16.8)	(14.5)	(14.1)	(14.6)	(14.9)
Future participants	(3.4)	(2.8)	(2.8)	(2.9)	(2.9)
All current and future participants	(24.5)	(21.1)	(20.4)	(21.0)	(21.2)
Present value of future expenditures in excess of future revenue	(3.8)[1]	(3.2)[2]	(3.8)[3]	(4.8)[4]	(5.6)[5]
Federal Supplementary Medical Insurance (Medicare Part B):[16]					
Revenue (Premiums) from:					
Participants who have attained eligibility age (age 65 and over)	1.0	0.9	0.8	0.7	0.6
Participants who have not attained eligibility age	5.3	4.6	4.5	4.1	3.8
Future participants	1.2	1.0	1.1	0.9	0.9
All current and future participants	7.5	6.5	6.5	5.7	5.3
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(4.0)	(3.6)	(3.2)	(2.9)	(2.6)
Participants who have not attained eligibility age	(19.2)	(16.8)	(17.0)	(15.1)	(14.3)
Future participants	(4.3)	(3.5)	(4.1)	(3.4)	(3.2)
All current and future participants	(27.5)	(24.0)	(24.3)	(21.4)	(20.2)
Present value of future expenditures in excess of future revenue [6]	(20.0)[1]	(17.5)[2]	(17.9)[3]	(15.7)[4]	(14.8)[5]

Totals may not equal the sum of components due to rounding.

Prior to fiscal year 2016, the amounts in these statements were presented in billions of dollars.

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

United States Government
Statements of Social Insurance (Note 22), continued
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

(In trillions of dollars)	2016	2015	2014	2013	2012
Federal Supplementary Medical Insurance (Medicare Part D):[16]					
Revenue (Premiums and State Transfers) from:					
Participants who have attained eligibility age (age 65 and over)	0.3	0.3	0.2	0.2	0.2
Participants who have not attained eligibility age	2.2	1.8	1.6	1.5	1.5
Future participants	1.0	0.8	0.7	0.7	0.7
All current and future participants	3.5	2.9	2.5	2.3	2.3
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(1.0)	(0.9)	(0.8)	(0.7)	(0.7)
Participants who have not attained eligibility age	(7.7)	(6.4)	(5.9)	(5.9)	(5.9)
Future participants	(3.6)	(2.8)	(2.6)	(2.6)	(2.6)
All current and future participants	(12.2)	(10.2)	(9.3)	(9.2)	(9.1)
Present value of future expenditures in excess of future revenue [6]	(8.7)[1]	(7.3)[2]	(6.8)[3]	(6.9)[4]	(6.8)[5]
Other:[7]					
Present value of future expenditures in excess of future revenues [8, 9]	(0.1)[10, 15]	(0.1)[11, 2]	(0.1)[12, 3]	(0.1)[13, 4]	(0.1)[14, 5]
Total present value of future expenditures in excess of future revenue	(46.7)	(41.5)	(41.9)	(39.7)	(38.6)

Totals may not equal the sum of components due to rounding.

Prior to fiscal year 2016, the amounts in these statements were presented in billions of dollars.

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

United States Government
Statements of Social Insurance (Note 22), continued
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

(In trillions of dollars)	2016	2015	2014	2013	2012
Social Insurance Summary[16]					
Participants who have attained eligibility age:					
Revenue (e.g., contributions and dedicated taxes)	3.1	2.8	2.3	2.1	2.0
Expenditures for scheduled future benefits	(22.9)	(21.3)	(19.4)	(18.2)	(16.7)
Present value of future expenditures in excess of future revenue	(19.8)	(18.5)	(17.1)	(16.1)	(14.7)
Participants who have not attained eligibility age:					
Revenue (e.g., contributions and dedicated taxes)	47.1	43.4	40.0	38.4	36.0
Expenditures for scheduled future benefits	(92.2)	(83.1)	(79.6)	(76.3)	(72.9)
Present value of future expenditures in excess of future revenue	(45.1)	(39.7)	(39.6)	(37.9)	(36.9)
Closed-group - Total present value of future expenditures in excess of future revenue	(64.9)	(58.2)	(56.7)	(54.0)	(51.6)
Future participants:					
Revenue (e.g., contributions and dedicated taxes)	41.9	36.8	34.3	32.9	30.6
Expenditures for scheduled future benefits	(23.7)	(20.1)	(19.6)	(18.6)	(17.6)
Present value of future revenue in excess of future expenditure	18.2	16.8	14.8	14.3	13.1
Open-group - Total present value of future expenditures in excess of future revenue	(46.7)	(41.5)	(41.9)	(39.7)	(38.6)

[1] The projection period for Social Security and Medicare is 1/1/2016-12/31/2090 and the valuation date is 1/1/2016.
[2] The projection period for Social Security, Medicare, and Railroad Retirement is 1/1/2015-12/31/2089 and the valuation date is 1/1/2015.
[3] The projection period for Social Security, Medicare, and Railroad Retirement is 1/1/2014-12/31/2088 and the valuation date is 1/1/2014.
[4] The projection period for Social Security, Medicare, and Railroad Retirement is 1/1/2013-12/31/2087 and the valuation date is 1/1/2013.
[5] The projection period for Social Security, Medicare, and Railroad Retirement is 1/1/2012-12/31/2086 and the valuation date is 1/1/2012.
[6] These amounts represent the present value of the future transfers from the General Fund to the Supplementary Medical Insurance Trust Fund. These future intragovernmental transfers are included as income in both HHS' and the Centers for Medicare & Medicaid Services' Financial Reports but are not income from the governmentwide perspective of this report.
[7] Includes Railroad Retirement and Black Lung.
[8] These amounts do not include the present value of the financial interchange between the railroad retirement and social security systems, which is included as income in the Railroad Retirement Financial Report, but is not included from the governmentwide perspective of this report. (See discussion of Railroad Retirement Program in the unaudited required supplementary information section of this report).
[9] Does not include interest expense accruing on the outstanding debt.
[10] The projection period for Black Lung is 9/30/2016-9/30/2040 and the valuation date is 9/30/2016.
[11] The projection period for Black Lung is 9/30/2015-9/30/2040 and the valuation date is 9/30/2015.
[12] The projection period for Black Lung is 9/30/2014-9/30/2040 and the valuation date is 9/30/2014.
[13] The projection period for Black Lung is 9/30/2013-9/30/2040 and the valuation date is 9/30/2013.
[14] The projection period for Black Lung is 9/30/2012-9/30/2040 and the valuation date is 9/30/2012.
[15] The projection period for Railroad Retirement is 10/1/2015-9/30/2090 and the valuation date is 10/1/2015.
[16] Current participants for the Social Security and Medicare programs are assumed to be the "closed-group" of individuals who are at least 15 years of age at the start of the projection period, and are participating as either taxpayers, beneficiaries, or both.

Totals may not equal the sum of components due to rounding.

Prior to fiscal year 2016, the amounts in these statements were presented in billions of dollars.

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

United States Government
Statement of Changes in Social Insurance Amounts for the Year Ended September 30, 2016 (Note 22)

(In trillions of dollars)	Social Security[1]	Medicare HI[1]	Medicare SMI[1]	Other[2]	Total
Net present value (NPV) of future revenue less future expenditures for current and future participants (the "open group") over the next 75 years, beginning of the year	(13.4)	(3.2)	(24.8)	(0.1)	(41.5)
Reasons for changes in the NPV during the year:					
Changes in valuation period	(0.5)	(0.1)	(1.1)	-	(1.7)
Changes in demographic data, assumptions, and methods	0.6	0.2	0.3	-	1.1
Changes in economic data, assumptions, and methods	(0.9)	-	-	-	(0.9)
Changes in law or policy	0.1	-	0.2	-	0.3
Changes in methodology and programmatic data	-	-	-	-	-
Changes in economic and other health care assumptions	-	(0.4)	(3.0)	-	(3.4)
Change in projection base	-	(0.3)	(0.3)	-	(0.6)
Net change in open group measure	(0.7)	(0.6)	(3.9)	-	(5.2)
Open group measure, end of year	(14.1)	(3.8)	(28.7)	(0.1)	(46.7)

[1] Amounts represent changes between valuation dates 1/1/2015 and 1/1/2016.

[2] Includes Railroad Retirement changes between valuation dates 1/1/2015 and 10/1/2015 and Black Lung changes between 9/30/2015 and 9/30/2016.

Totals may not equal the sum of components due to rounding.

Prior to fiscal year 2016, the amounts in this statement were presented in billions of dollars.

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

United States Government
Statement of Changes in Social Insurance Amounts for the Year Ended September 30, 2015 (Note 22)

(In trillions of dollars)	Social Security[1]	Medicare HI[1]	Medicare SMI[1]	Other[2]	Total
Net present value (NPV) of future revenue less future expenditures for current and future participants (the "open group") over the next 75 years, beginning of the year	(13.3)	(3.8)	(24.7)	(0.1)	(41.9)
Reasons for changes in the NPV during the year:					
Changes in valuation period	(0.6)	(0.2)	(1.1)	-	(1.9)
Changes in demographic data, assumptions, and methods	(0.1)	-	(0.1)	-	(0.2)
Changes in economic data, assumptions, and methods	(0.1)	-	-	-	(0.1)
Changes in law or policy	-	0.2	(0.3)	-	-
Changes in methodology and programmatic data	0.7	-	-	-	0.7
Changes in economic and other health care assumptions	-	0.8	2.5	-	3.2
Change in projection base	-	(0.1)	(1.1)	-	(1.2)
Net change in open group measure	(0.1)	0.6	(0.1)	-	0.4
Open group measure, end of year	(13.4)	(3.2)	(24.8)	(0.1)	(41.5)

[1] Amounts represent changes between valuation dates 1/1/2014 and 1/1/2015.

[2] Includes Railroad Retirement changes between valuation dates 1/1/2014 and 1/1/2015 and Black Lung changes between 9/30/2014 and 9/30/2015.

Totals may not equal the sum of components due to rounding.

Prior to fiscal year 2016, the amounts in this statement were presented in billions of dollars.

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

United States Government Notes to the Financial Statements for the Years Ended September 30, 2016, and 2015

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

This *Financial Report* includes the financial status and activities of the executive branch, the legislative branch, and the judicial branch of the government. The financial reporting period ends September 30 and is the same as used for the annual budget. The legislative and judicial branches are not required by law to submit financial statement information to Treasury; however, these branches provided cash and a significant amount of accrual basis financial information to include in the *Financial Report*. Appendix A of this report lists the organizations and agencies (entities) included in the U.S. Government's consolidated reporting entity for the *Financial Report*, as well as some entities not included in the reporting entity. Federal Accounting Standards Advisory Board's (FASAB) Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, *Entity and Display*, provides criteria for determining which entities are included in the reporting entity. Such criteria are summarized in Appendix A. Also, as discussed further in Appendix A, certain entities are excluded from the *Financial Report* because they do not meet the criteria, such as Federal Home Loan Banks, or were specifically excluded from the consolidated reporting entity in accordance with SFFAC No. 2, such as the Board of Governors of the Federal Reserve System and bailout entities. Examples of bailout entities include the Federal Home Loan Mortgage Corporation (Freddie Mac) and Federal National Mortgage Association (Fannie Mae).

During fiscal year 2008, the government began a number of emergency economic measures relating to the economy that involved various financing programs. Key initiatives beginning in fiscal year 2008 involved programs concerning Fannie Mae and Freddie Mac (Government-Sponsored Enterprises [GSEs]), provision of a credit facility for GSEs and Federal Home Loan Banks, purchase of Mortgage-Backed Securities (MBSs) [see Note 1.H—Investments in Government-Sponsored Enterprises and Note 8—Investments in Government-Sponsored Enterprises].

Following GAAP for federal entities, the government has not consolidated into its financial statements the assets, liabilities, or results of operations of any financial organization or commercial entity in which Treasury holds either a direct, indirect, or beneficial equity investment. Even though some of the equity investments are significant, under SFFAC No. 2, these entities meet the criteria of paragraph 50 and do not appear in the federal budget section "Federal Programs by Agency and Account." As such, these entities are not consolidated into the financial reports of the government. However, the values of the investment in such entities are presented on the balance sheet.

Material intragovernmental transactions are eliminated in consolidation, except as described in the Other Information—Unmatched Transactions and Balances (see Note 1.S—Unmatched Transactions and Balances).

B. Basis of Accounting and Revenue Recognition

Consolidated Financial Statements

The consolidated financial statements of the Government were prepared using GAAP, primarily based on FASAB's Statement of Federal Financial Accounting Standards (SFFAS). The consolidated financial statements include accrual-based financial statements and sustainability financial statements, which are discussed in more detail below, and the related notes to the consolidated financial statements. Collectively, the accrual-based financial statements, the sustainability financial statements, and the notes represent basic information that is deemed essential for the financial statements and notes to be presented in conformity with GAAP.

Accrual-Based Financial Statements

The accrual-based financial statements were prepared under the following principles:

- Expenses are generally recognized when incurred.
- Non-exchange revenue, including taxes, duties, fines, and penalties, are recognized when collected and adjusted for the change in net measurable and legally collectible amounts receivable. Related refunds and other offsets, including those that are measurable and legally payable, are netted against non-exchange revenue.
- Exchange (earned) revenue is recognized when the government provides goods and services to the public for a price. Exchange revenue includes user charges such as admission to federal parks and premiums for certain federal insurance.

The basis of accounting used for budgetary purposes, which is primarily on a cash basis (unified budget deficit) and follows budgetary concepts and policies, differs from the basis of accounting used for the financial statements which follow U.S. GAAP. See the Reconciliations of Net Operating Cost and Unified Budget Deficit in the Financial Statements section.

Sustainability Financial Statements

The sustainability financial statements were prepared based on the projected present value of the estimated future revenue and estimated future expenditures, primarily on a cash basis, for a 75 year period[1]. They include the Statements of Long-Term Fiscal Projections, covering all federal government programs, and the Statements of Social Insurance and the Statements of Changes in Social Insurance Amounts, covering social insurance programs (Social Security, Medicare, Railroad Retirement, and Black Lung programs). These estimates are based on economic as well as demographic assumptions presented in Notes 22 and 23. The sustainability financial statements are not forecasts or predictions. The sustainability financial statements are designed to illustrate the relationship between receipts and expenditures, if current policy is continued. For this purpose, the projections assume that scheduled social insurance benefit payments would continue after related trust funds are projected to be exhausted, contrary to current law, and that debt could continue to rise indefinitely without severe economic consequences.

By accounting convention, the Statements of Social Insurance does not include projected general revenues that, under current law, would be used to finance the remainder of the expenditures in excess of revenues for Medicare Parts B and D that is reported in the Statements of Social Insurance. The Statements of Long-Term Fiscal Projections include all revenues (including general revenues) of the federal government.

New Standards Issued and Not Yet Implemented

FASAB issued the following new standards that are applicable to the *Financial Report*, but are not yet implemented at the governmentwide level for fiscal year 2016:

- In December 2014, FASAB issued SFFAS No. 47, *Reporting Entity*. SFFAS No. 47 establishes principles to identify organizations for which elected officials are accountable. The standard also guides preparers of general purpose federal financial reports in determining what organizations to report upon, whether such organizations are considered “consolidation entities” or “disclosure entities,” and what information should be presented about those organizations. Generally, an organization is considered a consolidation entity if, based on assessment of the following characteristics as a whole, the organization: is financed through taxes and other non-exchange revenues, is governed by the Congress and/or President, imposes or may impose risks and rewards to the federal government, and provides goods and services on a non-market basis. A disclosure entity has a greater degree of autonomy with the federal government than a consolidation entity. To avoid obscuring information about these more autonomous organizations while still providing accountability, such organizations are to be disclosed rather than consolidated at the governmentwide level. The standard also requires information to be provided about related party relationships of such significance that it would be misleading to exclude information. SFFAS No. 47 is effective for periods beginning after September 30, 2017 and early implementation is not permitted.
- In April 2016, FASAB issued SFFAS No. 49, *Public-Private Partnerships Disclosure Requirements.* SFFAS No. 49 establishes principles to ensure disclosure about Public-Private Partnerships (P3s) are presented in the reporting entity’s general purpose federal financial reports (GPFFRs). P3s are defined as “risk sharing” arrangements or transactions lasting more than five years between public and private sector entities. Disclosure requirements comprise quantitative information to assist users in understanding the nature of P3s. P3s disclosures help achieve the operating performance and budgetary integrity objectives outlined in SFFAC No. 1. P3s are a form of investments. They should be adequately disclosed in order to assist report users in determining: (a) the important assets of the

[1] With the exception of the Black Lung program, which has a projection period through September 30, 2040.

U.S. government and how effectively they are being managed and (b) the identification of risks and liabilities. SFFAS No. 49 is effective for periods beginning after September 30, 2018 and early implementation is permitted.

New Standards Issued and Partially Implemented

FASAB issued the following new standards that are applicable to the *Financial Report*, and have been partially implemented at the governmentwide level for fiscal year 2016:

- In January 2016, FASAB issued SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials.* SFFAS No. 48 permits a reporting entity to apply an alternative valuation method in establishing opening balances. This method is permitted when presenting financial statements or one or more line items addressed in the standard. This standard can be applied for the first time or after a period during which existing systems could not provide the information necessary for producing GAAP-based financial statements without use of the alternative valuation method. This is intended to provide an alternative method to adoption of GAAP when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS No. 3, *Accounting for Inventory and Related Property*. SFFAS No. 48 is effective for periods beginning after September 30, 2016 and early implementation is permitted. During fiscal year 2016, select Department of Defense (DOD) components adopted this standard.
- In August 2016, FASAB issued SFFAS No. 50, *Establishing Opening Balances for General Property, Plant and Equipment.* SFFAS No. 50 applies when a reporting entity is presenting financial statements, or one or more line items addressed by this statement, following GAAP promulgated by the FASAB either (1) for the first time or (2) after a period during which existing systems could not provide the information necessary for producing such GAAP-based financial statements without use of the alternative methods. These alternative methods addressed in this statement may be applied in establishing opening balances for the reporting period in which the reporting entity, taken as a whole, makes an unreserved assertion that its financial statements, or one or more line items addressed by this statement, are presented fairly in accordance with GAAP. This application is available to each reporting entity only once per line item addressed in this statement. Reporting entities meeting the conditions and electing to apply this statement should follow the guidance in SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles* paragraph 13a-13c. SFFAS No. 50 is effective for periods beginning after September 30, 2016 and early implementation is permitted. During fiscal year 2016, select Department of Defense (DOD) components adopted this standard.

SFFAS No. 48 and SFFAS No. 50 are very similar in regards to implementation and utilizing alternative methods. The reason for two separate publications is due to differing alternative methods and deemed cost criteria. SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies (OM&S), and Stockpile Materials* uses deemed cost based on one, or a combination of standard price (selling price) or fair value, latest acquisition cost, replacement cost, estimated historical cost (initial amount), and actual historical cost (initial amount). There is also an exception to valuation for agricultural, mineral, and other products. This inventory, OM&S, and stockpile materials use the criteria of units of which are interchangeable, immediately marketable, and in which appropriate costs may be difficult to obtain. SFFAS No. 50, *Establishing Opening Balances for General Property, Plant and Equipment* uses deemed cost defined as one or a combination of replacement cost, estimated historical cost, or fair value. Land and Land Rights under SFFAS No. 50 also offers the alternative method of excluding land and land rights from the opening balance of general Property Plant and Equipment (PP&E). Internal Use Software alternative method utilizes both the deemed cost defined in SFFAS No. 50 as well as prospective capitalization. Due to the differences in valuation, it was prudent for FASAB to publish separate standards. As a result of implementation at selected DOD components, DOD decreased the Beginning net position by $1.5 billion, decreased the ending balance of PP&E by $2.2 billion, and increased the ending balance of Inventories and related property by $733.7 million.

C. Accounts and Taxes Receivable

Accounts receivable represent claims to cash or other assets from entities outside the government that arise from the sale of goods or services, duties, fines, certain license fees, recoveries, or other provisions of the law. Accounts receivable are reported net of an allowance for uncollectible amounts. An allowance is established when it is more likely than not the receivables will not be totally collected. The allowance method varies among the agencies in the government and is usually based on past collection experience and is re-estimated periodically as needed. Methods include statistical sampling of receivables, specific identification and intensive analysis of each case, aging methodologies, and percentage of total receivables based on historical collection.

Taxes receivable consist primarily of uncollected tax assessments, penalties, and interest when taxpayers have agreed or a court has determined the assessments are owed. Taxes receivable do not include unpaid assessments when taxpayers or a court have not agreed that the amounts are owed (compliance assessments) or the government does not expect further collections due to factors such as the taxpayer's death, bankruptcy, or insolvency (write-offs). Taxes receivable are reported net of an allowance for the estimated portion deemed to be uncollectible. The allowance for uncollectible amounts is based on projections of collectibles from a statistical sample of unpaid tax assessments.

D. Loans Receivable and Loan Guarantee Liabilities

Direct loans obligated and loan guarantees committed after fiscal year 1991 are reported based on the present value of the net cash flows estimated over the life of the loan or guarantee. The difference between the outstanding principal of the direct loans and the present value of their net cash inflows is recognized as a subsidy cost allowance. The present value of estimated net cash flows of the loan guarantees is recognized as a liability for loan guarantees.

The subsidy expense for direct or guaranteed loans disbursed during a fiscal year is the present value of estimated net cash flows for those loans or guarantees. A subsidy expense also is recognized for modifications made during the year to loans and guarantees outstanding and for re-estimates made as of the end of the fiscal year to the subsidy allowances or loan guarantee liability for loans and guarantees outstanding.

Direct loans obligated and loan guarantees committed before fiscal year 1992 are valued under two different methodologies within the government: the allowance-for-loss method and the present-value method. Under the allowance-for-loss method, the outstanding principal of direct loans is reduced by an allowance for uncollectible amounts; the liability for loan guarantees is the amount the agency estimates would more likely than not require future cash outflow to pay default claims. Under the present-value method, the outstanding principal of direct loans is reduced by an allowance equal to the difference between the outstanding principal and the present value of the expected net cash flows. The liability for loan guarantees is the present value of expected net cash outflows due to the loan guarantees.

E. Inventories and Related Property

Inventory is tangible personal property that is (1) held for sale, principally to federal agencies, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee. SFFAS No. 3, *Accounting for Inventory and Related Property*, requires inventories held for sale and held in reserve for future sale within the government to be valued using either historical cost or latest acquisition cost (LAC). Historical cost methods include first-in-first-out, weighted average, and moving average. When LAC methods are used, the inventory is revalued periodically and an allowance account should be established for unrealized holding gains and losses.

DOD values approximately 98 percent of resale inventory using the moving average cost method. Additionally, DOD reports the remaining 2 percent of resale inventories at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses to approximate the historical cost of resale inventory items remaining in its legacy system. The latest acquisition cost method is used because legacy inventory systems were designed for material management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3. DOD is continuing to transition inventories currently accounted for under the LAC methods, to be accounted for under the moving average cost methods. When using historical cost valuation, estimated repair costs reduce the value of inventory held for repair. Excess, obsolete, and unserviceable inventories are valued at estimated net realizable value. When LAC is used to value inventory held for sale, it is adjusted for holding gains and losses in order to approximate historical cost.

Related property includes commodities, seized monetary instruments, forfeited and foreclosed property, raw materials and work in process. Operating materials and supplies are valued at historical cost, LAC, and standard price using the purchase and consumption method of accounting. Operating materials and supplies that are valued at latest acquisition cost and standard pricing are not adjusted for holding gains and losses.

F. Property, Plant, and Equipment

Property, Plant and Equipment (PP&E) consists of tangible assets including buildings, equipment, construction in progress, internal use software, assets acquired through capital leases (including leasehold improvements), and other assets used to provide goods and services.

PP&E used in government operations are carried at acquisition cost, with the exception of some DOD equipment. In some instances, DOD equipment is valued at estimated historical costs, which are calculated using internal DOD records. To establish a baseline, DOD accumulated information relating to program funding and associated equipment, equipment useful life, program acquisitions, as well as disposals. The equipment baseline is updated using expenditure information and information related to acquisitions and disposals.

All PP&E is capitalized if the acquisition costs (or estimated acquisition cost for DOD) are in excess of capitalization thresholds that vary considerably between the federal entities. Depreciation and amortization expense applies to PP&E reported on the balance sheets except for land, unlimited duration land rights, and construction in progress. Depreciation and amortization are recognized using the straight-line method over the estimated useful lives of the assets. All PP&E are assigned useful lives depending on their category. The cost of acquisition, betterment, or reconstruction of all multi-use heritage assets is capitalized as general PP&E and is depreciated. Construction in progress is used for the accumulation of the cost of construction or major renovation of fixed assets during the construction period. The assets are transferred out of construction in progress when the project is substantially completed. Internal use software includes purchased commercial off-the-shelf software, contractor-developed software, and software internally developed.

For financial reporting purposes, other than multi-use heritage assets, stewardship assets are not recorded as part of PP&E. Stewardship Assets consist of public domain land (Stewardship Land) and Heritage Assets. Examples of stewardship land include national parks, wildlife refuges, national forests, and other lands of national and historical significance. Heritage assets include national monuments, and historical sites that among other characteristics are of historical, natural, cultural, educational, or artistic significance. Stewardship land and most heritage assets are considered priceless and irreplaceable, and as such they are measured in physical units with no financial value assigned to them. Some heritage assets have been designated as multi-use heritage assets, for example the White House, the predominant use of which is in government operations. For more details on stewardship assets, see Note 24—Stewardship Land and Heritage Assets.

G. Debt and Equity Securities

Debt and equity securities are classified as held-to-maturity, available-for-sale, and trading. Held-to-maturity debt and equity securities are reported at amortized cost, net of unamortized premiums and discounts. Available-for-sale debt and equity securities are reported at fair value. Trading debt and equity securities are reported at fair value.

H. Investments in Government-Sponsored Enterprises

The senior preferred stock and associated common stock warrants in GSEs are presented at their fair value. The annual valuation to estimate the asset's fair value incorporates various forecasts, projections, and cash flow analyses. These valuations are performed on the senior preferred stock and warrants and any changes in valuation, including impairment, are recorded and disclosed in accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources*. Since the valuation is an annual process, the changes in valuation of the senior preferred stock and warrants are deemed usual and recurring. Accordingly, changes in valuation are recorded as an exchange transaction which is either an expense or revenue. Since the costs of the senior preferred stock and warrants are reflected in exchange transactions, any change in valuation is also recorded as an exchange transaction.

The *Housing and Economic Recovery Act of 2008 (HERA)* established the Federal Housing Finance Agency (FHFA), which was created to enhance authority over the GSEs, and provide the Secretary of the Treasury with certain authorities to support the financial stability of the GSEs. In September 2008, Treasury entered into a Senior Preferred Stock Purchase Agreement (SPSPA) with each GSE. The GSEs were placed under conservatorship and require that Treasury increase their investment in the GSEs' senior preferred stock if, at the end of any quarter, the FHFA, acting as the conservator, determines that the liabilities of either GSE exceed its respective assets. The potential liabilities to the GSEs, if any, are assessed annually and recorded at the gross estimated amount. For more detailed information on investments in GSEs, refer to Note 8—Investments in Government-Sponsored Enterprises.

I. Federal Debt

Accrued interest on Treasury securities held by the public is recorded as an expense when incurred, instead of when paid. Certain Treasury securities are issued at a discount or premium. These discounts and premiums are amortized over the term of the security using an interest method for all long-term securities and the straight line method for short-term securities. Treasury also issues Treasury Inflation-Protected Securities (TIPS). The principal for TIPS is adjusted daily over the life of the security based on the Consumer Price Index for all Urban Consumers (CPI-U).

J. Federal Employee and Veteran Benefits Payable

Generally, federal employee and veteran benefits payable are recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans, veterans' compensation, burial and education benefits, post-retirement health benefits, and post-retirement life insurance benefits, are recorded at estimated present value of future benefits, less any estimated present value of future normal cost contributions. Normal cost is the portion of the actuarial present value of projected benefits allocated as an expense for employee services rendered in the current year. Actuarial gains and losses (as well as prior service cost, if any) are recognized immediately in the year they occur without amortization.

The Department of Veterans Affairs (VA) also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled for nonservice-related causes. The actuarial present value of the future liability for these VA pension benefits is a non-exchange transaction and is not required to be recorded on the Balance Sheet. These benefits are expenses when benefits are paid rather than when employee services are rendered.

The liabilities for *Federal Employees' Compensation Act* (workers compensation) benefits are recorded at estimated present value of future benefits for injuries and deaths that have already been incurred.

Gains and losses from changes in long-term assumptions used to estimate federal employee pensions, Other Retirement Benefits (ORB), and Other Postemployment Benefits (OPEB) liabilities are reflected separately on the Statement of Net Cost and the components of the expense related to federal employee pension, ORB, and OPEB liabilities are disclosed in Note 12—Federal Employee and Veteran Benefits Payable as prescribed by SFFAS No. 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*. In addition, SFFAS No. 33 also provides a standard for selecting the discount rate assumption for present value estimates of federal employee pension, ORB, and OPEB liabilities.

K. Environmental and Disposal Liabilities

Environmental and disposal liabilities are recorded at the estimated current cost of removing, containing, treating, and/or disposing of radioactive waste, hazardous waste, chemical and nuclear weapons, as well as other environmental contaminations (including asbestos), assuming the use of current technology. Hazardous waste is a solid, liquid, or gaseous waste that, because of its quantity or concentration, presents a potential hazard to human health or the environment. Remediation consists of removal, decontamination, decommissioning, site restoration, site monitoring, closure as well as post-closure cost, treatment, and/or safe containment. Where technology does not exist to clean up radioactive or hazardous waste, only the estimable portion of the liability (typically monitoring and safe containment) is recorded.

L. Insurance and Guarantee Program Liabilities

Insurance and guarantee programs (such as Federal Crop Insurance Program and Benefit Pension Plans Program) provide protection to individuals or entities against specified risks except for those specifically covered by federal employee and veteran benefits, social insurance, and loan guarantee programs. Insurance and guarantee program funds are commonly held in revolving funds in the government and losses sustained by participants are paid from these funds. Many of these programs receive appropriations to pay excess claims and/or have authority to borrow from the Treasury. The values of insurance and guarantee program liabilities are particularly sensitive to changes in underlying estimates and assumptions. Insurance and guarantee programs with recognized liabilities in future periods (i.e., liabilities that extend beyond one year) are reported at their actuarial present value.

M. Deferred Maintenance and Repairs

Deferred maintenance and repairs are maintenance and repairs that were not performed when they should have been or scheduled maintenance and repairs that were delayed or postponed. Maintenance is the act of keeping fixed assets in acceptable condition, including preventative maintenance, normal repairs, and other activities needed to preserve the assets, so they continue to provide acceptable service and achieve their expected life. Maintenance and repairs exclude activities aimed at expanding the capacity of assets or otherwise upgrading them to serve needs different from those originally intended. Deferred maintenance and repairs expenses are not accrued in the Statements of Net Cost or recognized as liabilities on the Balance Sheet. However, deferred maintenance and repairs information is disclosed in the unaudited RSI section of this report. Please see unaudited RSI, Deferred Maintenance & Repairs for additional information including measurement methods.

N. Contingencies

Liabilities for contingencies are recognized on the Balance Sheet when both:

- A past transaction or event has occurred, and
- A future outflow or other sacrifice of resources is probable and measurable.

The estimated contingent liability may be a specific amount or a range of amounts. If some amount within the range is a better estimate than any other amount within the range, then that amount is recognized. If no amount within the range is a better estimate than any other amount, then the minimum amount in the range is recognized and the range is disclosed.

Contingent liabilities that do not meet the above criteria for recognition, but for which there is at least a reasonable possibility that a loss may be incurred, are disclosed in Note 18—Contingencies.

O. Commitments

In the normal course of business, the government has a number of unfulfilled commitments that may require the use of its financial resources. Note 19—Commitments describes the components of the government's actual commitments that are disclosed due to their nature and/or their amount. They include long-term leases, undelivered orders, and other commitments.

P. Social Insurance

A liability for social insurance programs (Social Security, Medicare, Railroad Retirement, Black Lung, and Unemployment) is recognized for any unpaid amounts currently due as of the reporting date. No liability is recognized for future benefit payments not yet due. For further information, see the unaudited RSI—Social Insurance section, and Note 22—Social Insurance.

Q. Funds from Dedicated Collections

Generally, funds from dedicated collections are financed by specifically identified revenues, provided to the government by non-federal sources, often supplemented by other financing sources that remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the government's general revenues. The three required criteria for a fund from dedicated collections are:

- A statute committing the government to use specifically identified revenues and/or other financing sources that are originally provided to the government by a non-federal source only for designated activities, benefits, or purposes;
- Explicit authority for the fund to retain revenues and/or other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and
- A requirement to account for and report on the receipt, use, and retention of the revenues and/or other financing sources that distinguishes the fund from the government's general revenues.

For more details on funds from dedicated collections, see Note 20—Funds from Dedicated Collections.

R. Related Party Transactions

Federal Reserve System

The Federal Reserve System (FR System) was created by Congress under the *Federal Reserve Act of 1913*. The FR System consists of the Federal Reserve Board of Governors (Board), the Federal Open Market Committee (FOMC), and the Federal Reserve Banks (FRBs). Collectively, the FR System serves as the nation's central bank and is responsible for formulating and conducting monetary policy, issuing and distributing currency (Federal Reserve Notes), supervising and regulating financial institutions, providing nationwide payments systems (including large-dollar transfers of funds, Automated Clearing House (ACH) operations, and check collection), providing certain financial services to federal agencies and fiscal principals, and serving as the U.S. government's bank. Monetary policy includes actions undertaken by the FR System that influence the availability and cost of money and credit as a means of helping to promote national economic goals. The FR System also conducts operations in foreign markets in order to counter disorderly conditions in exchange markets or to meet other needs specified by the FOMC to carry out its central bank responsibilities. The FR System is not included in the federal budget. It is considered an independent central bank, and its decisions are not ratified by the executive branch of the federal government.

The government interacts with the FRBs in a variety of ways, including the following:

- The FRBs serve as the government's fiscal agent and depositary, executing banking and other financial transactions on the government's behalf. The government reimburses the FRBs for these services, the cost of which is included on the Statements of Net Cost;
- The FRBs hold Treasury and other federal securities in the FRBs' System Open Market Account (SOMA) for the purpose of conducting monetary policy (Note 11—Federal Debt Securities Held by the Public and Accrued Interest);
- The FRBs hold gold certificates issued by the government in which the certificates are collateralized by gold (Note 2—Cash and Other Monetary Assets);
- The FRBs hold Special Drawing Rights (SDR) certificates issued by the government which are collateralized by SDRs (see Note 2—Cash and Other Monetary Assets); and,
- The FRBs are required by Board policy to transfer their excess earnings to the government, which are included in Other Taxes and Receipts on the Statements of Operations and Changes in Net Position.

The government also consults with the FR System on matters affecting the economy and certain financial stability activities (Note 4—Loans Receivable and Loan Guarantee Liabilities, Net). The above financial activities involving the government are accounted for and disclosed in the government consolidated financial statements. In accordance with SFFAC No. 2, *Entity and Display*, the FR System's assets, liabilities, and operations are not consolidated into the government's financial statements, and are, therefore, not a part of the reporting entity.

Federal Reserve System Structure

The Board is an independent organization governed by seven members who are appointed by the President and confirmed by the Senate. The full term of a Board member is 14 years, and the appointments are staggered so that one term expires on January 31 of each even-numbered year. The Board has a number of supervisory and regulatory responsibilities for institutions including, among others, state-chartered banks that are members of the FR System, bank holding companies, and savings and loan holding companies. In addition, the Board has general supervisory responsibilities for the 12 FRBs, and issues currency (Federal Reserve Notes) to the FRBs for distribution.

The FOMC is comprised of the seven Board members and five of the 12 FRB presidents, and is charged with formulating and conducting monetary policy primarily through open market operations (the purchase and sale of certain securities in the open market), the principal tool of national monetary policy. These operations affect the amount of reserve balances available to depository institutions, thereby influencing overall monetary and credit conditions. The 12 FRBs are chartered under the *Federal Reserve Act*, which requires each member bank to own the capital stock of its FRB. Supervision and control of each FRB is exercised by a board of directors, of which three are appointed by the Board of Governors of the FR System, and six are elected by their member banks.

The FRBs participate in formulating and conducting monetary policy, distribute currency and coin, and serve as fiscal agents for the government, other federal agencies, and fiscal principals. Additionally, the FRBs provide short-term loans to depository institutions and loans to participants in programs or facilities with broad-based eligibility in unusual and exigent circumstances when approved by the Board and the Treasury Secretary.

Federal Reserve System Assets and Liabilities

The FRBs hold Treasury and other securities in the SOMA for the purpose of conducting monetary policy. Treasury securities held by the FRBs totaled $1,750.2 billion and $1,845.3 billion at September 30, 2016 and 2015, respectively (Note 11—Federal Debt Securities Held by the Public and Accrued Interest). These assets are generally subject to the same market (principally interest-rate) and credit risks as other financial instruments. In the open market, the FR System purchases and sells Treasury securities as a mechanism for controlling the money supply.

The FRBs have deposit liabilities with Treasury and depository institutions. The FRBs issue Federal Reserve Notes, the circulating currency of the United States, which are collateralized by the Treasury securities and other assets held by the FRBs. Financial and other information concerning the FR System, including financial statements for the Board and the FRBs, may be obtained at http://www.federalreserve.gov.

FRB Residual Earnings Transferred to the Government

FRBs generate income from interest earned on securities, reimbursable services provided to federal agencies, and the provision of priced services to depository institutions, as specified by the *Monetary Control Act of 1980*. Although the FRBs generate earnings from carrying out open market operations (via the earnings on securities held in the SOMA account), their execution of these operations is for the purpose of accomplishing monetary policy rather than generating earnings. Each FRB is required by Board policy to transfer to the government its residual (or excess) earnings, after providing for the cost of operations, payment of dividends, and surplus funds not to exceed an FRB's allocated portion of an aggregate of $10 billion for all FRBs. This is in accordance with the provisions of a new statute, *Fixing America's Surface Transportation Act of 2015* (P.L. 114-94), which became effective December 4, 2015. Prior to this statute, each FRB was required to maintain surplus funds equal to the amount of capital paid-in. The new statute limits the aggregate amount of surplus funds to $10 billion that can be maintained by all FRBs. These residual earnings may vary due to, among other things, changes in the SOMA balance levels that may occur in conducting monetary policy. Under P.L. 114-94, if an FRB's earnings for the year are not sufficient to provide for the cost of operations, payment of dividends, or allocated portion of $10 billion aggregate surplus funds limitation, an FRB will suspend its payments to the government until such earnings become sufficient. The FRB residual earnings of $115.7 billion and $96.5 billion for fiscal years ended September 30, 2016 and 2015, respectively, are reported as other taxes and receipts on the Statements of Operations and Changes in Net Position. Accounts and taxes receivables, net, includes a receivable for FRB's residual earnings which represents the earnings due to the General Fund as of September 30, but not collected by the General Fund until after the end of the month. As of September 30, 2016 and 2015, interest receivable on FRB's residual earnings are $0.4 billion and $0.3 billion, respectively (Note 3—Accounts and Taxes Receivables, Net).

Other Related Parties

The federal government, through the Federal Housing Finance Agency (FHFA) is the conservator for Fannie Mae and Freddie Mac. See Note 8—Investments in Government-Sponsored Enterprises.

The Secretary of Transportation has possession of two long term notes with the National Railroad Passenger Service Corporation (more commonly referred to as Amtrak). The first note is for $4 billion and matures in 2975 and the second note is for $1.1 billion and matures in 2082 with renewable 99 year terms. Interest is not accruing on these notes as long as the current financial structure of Amtrak remains unchanged. If the financial structure of Amtrak changes, both principal and accrued interest are due and payable. The Department of Transportation (DOT) does not record the notes in its financial statements since the notes, with maturity dates of 2975 and 2082, are considered fully uncollectible due to the lengthy terms and Amtrak's history of operating losses.

In addition, DOT has possession of all the preferred stock shares (109.4 million) of Amtrak. Congress, through DOT, has continued to fund Amtrak since approximately 1972; originally through grants, then, beginning in 1981, through the purchase of preferred stock, and then through grants again after 1997. The *Amtrak Reform and Accountability Act of 1997* changed the structure of the preferred stock by rescinding the voting rights with respect to the election of the Board of Directors and by eliminating the preferred stock's liquidation preference over the common stock. The Act also eliminated further issuance to DOT of preferred stock. DOT does not record the Amtrak preferred stock in its financial statements because, under the Corporation's current financial structure, the preferred shares do not have a liquidation preference over the common shares, the preferred shares do not have any voting rights, and dividends are neither declared nor in arrears.

In general, Amtrak is not a department, agency, or instrumentality of the government or DOT. The nine members of Amtrak's Board of Directors are appointed by the President and are subject to confirmation by the United States Senate. Once appointed, board members, as a whole, act independently without the consent of the government or any of its officers to set Amtrak policy, determine its budget, and decide operational issues. The Secretary of Transportation is statutorily appointed to the nine member board. Traditionally, the Secretary of Transportation has designated the FRA Administrator to represent the Secretary at Board meetings.

The Export-Import Bank of the United States (Ex-Im Bank) has contractual agreements with the Private Export Funding Corporation (PEFCO). PEFCO, which is owned by a consortium of private-sector banks, industrial companies, and financial services institutions, makes and purchases from private sector lenders, medium-term and long-term fixed-rate and variable-rate loans guaranteed by Ex-Im Bank to foreign borrowers to purchase U.S. made equipment "export loans".

Ex-Im Bank's credit and guarantee agreement with PEFCO provides that Ex-Im Bank will guarantee the due and punctual payment of interest on PEFCO's secured debt obligations which Ex-Im Bank has approved, and grants to Ex-Im Bank a broad measure of supervision over PEFCO's major financial manage decisions, including entitlement to have representatives and attend and participate in all meetings of PEFCO's board of directors, advisory board, and exporters' council, and to review PEFCO's financials and other records. This agreement extends through December 31, 2020.

The contractual agreements provide that Ex-Im Bank will (1) guarantee the due and punctual payment of principal, as well as interest on export loans made by PEFCO and (2) guarantee the due and punctual payment of interest on PEFCO's long-term secured debt obligations when requested by PEFCO. Related to the amounts for Ex-Im Bank as shown in Note 4—Loans Receivable and Loan Guarantee Liabilities, Net, these guarantees to PEFCO, aggregating $5.7 billion and $12.6 billion at September 30, 2016, and 2015, respectively, are included within the principal amounts guaranteed by the United States. The allowance related to these transactions is included within the guaranteed loan liability. Ex-Im Bank received fees for the agreements totaling $0.05 billion and $0.03 billion for fiscal years 2016 and 2015, respectively, which are included as earned revenue on the Statements of Net Cost.

S. Unmatched Transactions and Balances

The reconciliation of the change in net position requires that the difference between ending and beginning net position equals the difference between revenue and cost, plus or minus prior-period adjustments.

The unmatched transactions and balances are needed to bring the change in net position into balance. The primary factors affecting this out of balance situation are:

- Unmatched intragovernmental transactions and balances between federal agencies; and
- Errors and restatements in federal agencies' reporting.

Refer to the Other Information (unaudited)—Unmatched Transactions and Balances for detailed information.

T. Prior-Period Adjustments

During fiscal year 2016, Pension Benefit Guaranty Corporation (PBGC) and DOD reported prior period adjustments. In fiscal year 2016, clarifying guidance was provided to agencies on fiduciary fund classification. Based on the information provided, PBGC Single-Employer Program reports a change in accounting principle of a $0.1 billion increase to no longer report the trust fund portion of the present value of future benefits on the Balance Sheet and the respective notes. In fiscal year 2016, the trust fund portion of the present value benefits are reported in the Fiduciary Activities footnote. This reporting explains PBGC's role as guarantor, per Title IV of ERISA, to provide guaranteed benefits to the extent allowed within statutory limits.

DOD reported a $1.5 billion decrease to beginning net position due to early implementation of standards SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials* and SFFAS No. 50 *Establishing Opening Balances for General Property, Plant and Equipment*. DOD adopted SFFAS No. 48 for stockpile materials for selected components, which is reported in Inventories and Related Property. In addition, DOD used several cost methodologies to provide PP&E opening balances instead of acquisition value. These standards permit alternative methods in opening balances and selected components adopted them in fiscal year 2016. The $1.5 billion decrease is reported on the Balance Sheet and the respective notes.

During fiscal year 2015, several entities reported the prior-period adjustments line item. Environmental Protection Agency (EPA) changed its accounting treatment to record special accounts funds settlement proceeds as unearned revenue after determining that collections previously recorded as past costs were being used for future site cleanup. The effect is a $1.3 billion decrease in EPA's beginning net position.

For fiscal year 2015, Department of Justice (DOJ) applied a change in accounting principle to certain components based on the implementation of their Financial Management Policy Memorandum (FMPM) 13-12, Capitalization of General Property, Plant, and Equipment and Internal Use Software. The primary impact of the policy change was an increase in the thresholds for capitalizing and reporting real property, including leasehold improvements, personal property, and internal use

software. The change in DOJ's accounting principle caused a $0.1 billion reduction in the overall PP&E balance for fiscal year 2015.

As discussed in Note 20 – Funds from Dedicated Collections, the Commodity Future Trading Commission erroneously did not report as a fund from dedicated collections for fiscal year 2014. This error was corrected in fiscal year 2015 and resulted in a prior-period adjustment amount of $0.3 billion.

U. Reclassifications

The Railroad Retirement and Black Lung programs are combined on the Statements of Social Insurance (SOSI) in 2016. In previous years, these programs were broken out and displayed separately. In addition, for fiscal year 2016, the amounts in the SOSI and in the Statement of Changes in Social Insurance Amounts (SCSIA) for current and prior years are presented in trillions of dollars instead of in billions of dollars, as they have been presented in the past.

In fiscal year 2016 Federal Deposit Insurance Corporation (FDIC) determined the information previously reported in Insurance and Guarantee Program Liabilities should be included in Other Liabilities. The effect was a reclassification of $7.2 billion on the fiscal year 2015 Balance Sheet and the respective notes.

In fiscal year 2016, the presentation for the Reconciliation of Net Operating Cost and Unified Budget Deficit and the Statements of Changes in Cash Balance from Unified Budget and Other Activities for fiscal year 2015 was reclassified to conform with new statements.

V. Restatements

In fiscal year 2016, VA reassessed the application of *SFFAS 5, Accounting for Liabilities of the Federal Government*, as it relates to Post- 9/11 GI Bill (Chapter 33) liabilities. With the change in the application of SFFAS 5, VA began to record a liability for any portion of the costs that remain unpaid at the end of the period. This change resulted in a correction of errors for years preceding the prior year and was reported as a decrease of $46.9 billion to the fiscal year 2015 beginning net position, and as a correction of error to the fiscal year 2015 financial statements which is reported as a restatement of amounts on the Balance Sheet, Statement of Net Cost, Statement of Operations and Changes in Net Position, Reconciliations of Net Operating Cost and Unified Budget Deficit, and Note 12—Federal Employee and Veteran Benefits Payable.

During ongoing audit readiness efforts within DOD, the PP&E balance on the September 30, 2015 financial statements did not accurately or completely represent expenditures associated with the construction in progress (CIP) of PP&E assets. General Equipment CIP was not recorded for multi-year acquisition programs for ships and aircrafts during their construction. CIP should have been recorded for these assets until they were delivered and reported as equipment. The finding resulted in a correction of errors for years preceding the prior year and was reported as an increase of $19.7 billion to the fiscal year 2015 beginning net position, and a correction of error to the fiscal year 2015 financial statements which is reported as a restatement of amounts on the Balance Sheet, Statement of Net Cost, Statement of Operations and Changes in Net Position, Reconciliations of Net Operating Cost and Unified Budget Deficit and Note 6—Property, Plant and Equipment.

W. Fiduciary Activities

Fiduciary activities are the collection or receipt, as well as the management, protection, accounting, investment and disposition by the government of cash or other assets in which non-federal individuals or entities have an ownership interest that the government must uphold. Fiduciary cash and other fiduciary assets are not assets of the government and are not recognized on the Balance Sheet. See Note 21—Fiduciary Activities, for further information.

X. Use of Estimates

The government 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. There are a large number of factors that affect these assumptions and estimates, which are inherently subject to substantial uncertainty arising from the likelihood

of future changes in general economic, regulatory, and market conditions. As such, actual results will differ from these estimates and such differences may be material.

Significant transactions subject to estimates include loans and credit program receivables, federal employee and veteran benefits payable, credit reform subsidy costs, investments in GSEs, and other non-federal securities and related impairment, tax receivables, loan guarantees, depreciation, imputed costs, other actuarial liabilities, cost and earned revenue allocations, as well as contingencies and any related recognized liabilities.

The government recognizes the sensitivity of credit reform modeling to slight changes in some model assumptions and uses regular review of model factors, statistical modeling, and annual re-estimates to reflect the most accurate cost of the credit programs to the U.S. Government. *Federal Credit Reform Act of 1990* (FCRA) loan receivables and loan guarantees are disclosed in Note 4—Loans Receivable and Loan Guarantee Liabilities, Net.

The forecasted future cash flows used to determine credit reform amounts are sensitive to slight changes in model assumptions, such as general economic conditions, specific stock price volatility of the entities in which the government has an equity interest, estimates of expected default, and prepayment rates. Therefore, forecasts of future financial results have inherent uncertainty.

The annual valuation performed as of September 30 on the preferred stock and warrants comprising the Investments in GSEs line item on the Balance Sheets incorporates various forecasts, projections, and cash flow analyses to develop an estimate of the asset's fair value. The value of the senior preferred stock is estimated by first estimating the fair value of the total equity of each GSE (which, in addition to the senior preferred stock, is comprised of other equity instruments including common stock, common stock warrants, and junior preferred stock). The fair value of the total equity is based on a discounted cash flow valuation methodology, whereby the primary input is the present value of the projected quarterly dividend payments. The fair value of the GSE's other equity instruments are then deducted from its total equity, with the remainder representing the fair value of the senior preferred stock. The primary input into the warrants valuation is the market value of the shares of common stock of the GSEs which, along with the junior preferred stock, are traded on the over-the-counter (OTC) Bulletin Board. Treasury evaluates the need for adjusting the OTC market-based valuation of the warrants for the effects, if any, of significant events occurring after the close of the market but before the end of the measurement date. Treasury records any changes in valuation, including impairment, and discloses changes in accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources.* Since the valuation is an annual process, Treasury deems changes in valuation of the preferred stock and warrants as usual and recurring.

Treasury performs annual calculations, as of September 30, to assess the need for recording an estimated liability in accordance with SFFAS No. 5, *Accounting for Liabilities of The Federal Government*, related to the government's funding commitment to the GSEs under the SPSPAs. Liability recognition is predicated on the probable future occurrence of an excess of liabilities and minimum capital reserve amounts, as defined, over the assets of either GSE at the end of any reporting quarter. The occurrence of future GSE deficits, which ultimately determines the liability to the GSEs, is most sensitive to future changes in the housing price index and, to a lesser extent, future changes in guarantee fees received by the GSEs on single family mortgages. For more detailed information on investments in GSEs and the amended SPSPAs, see Note 8—Investments in Government-Sponsored Enterprises.

The government offers its employees' pension and other post-employment retirement benefits, as well as life and health insurance. The Office of Personnel Management administers the largest civilian plan and the Department of Defense and Department of Veterans Affairs administer the military plans. Generally the benefits payable are recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans, veterans' compensation and burial benefits, post-retirement health benefits, life insurance benefits, education benefits, and *Federal Employees' Compensation Act* benefits are recorded at estimated present value of future benefits, less any estimated present value of future normal cost contributions. See Note 12—Federal Employee and Veteran Benefits Payable for additional information.

Y. Credit Risk

Credit risk is the potential, no matter how remote, for financial loss from a failure of a borrower or counterparty to perform in accordance with underlying contractual obligations. The government takes on credit risk when it makes direct loans or guarantees to non-federal entities, provides credits to foreign entities, or becomes exposed to institutions which engage in financial transactions with foreign countries.

The government also takes on credit risk related to committed, but undisbursed direct loans, funding commitments to GSEs, guarantee of money market funds, and other activities. These activities generally focus on the underlying problems in the credit markets. These programs were developed to provide credit where borrowers are not able to get access to credit with reasonable terms and conditions. Because these programs attempt to correct for a market imperfection, it can expose the

Government to potential costs and losses. The extent of the risk assumed is described in more detail in the notes to the financial statements, and where applicable, is factored into credit reform models and reflected in fair value measurements.

Note 2. Cash and Other Monetary Assets

Cash and Other Monetary Assets as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Unrestricted cash:		
Cash held by Treasury for governmentwide operations	347.0	193.3
Other	11.6	6.6
Restricted	22.4	26.1
Total cash	381.0	226.0
International monetary assets	59.6	58.5
Gold and silver	11.1	11.1
Foreign currency	12.9	9.5
Total cash and other monetary assets	464.6	305.1

Unrestricted cash includes cash held by Treasury for governmentwide operations (Operating Cash) and all other unrestricted cash held by the federal agencies. Operating Cash represents balances from tax collections, other revenue, federal debt receipts, and other various receipts net of cash outflows for budget outlays and other payments. Treasury checks outstanding are netted against Operating Cash until they are cleared by the Federal Reserve System. Other unrestricted cash not included in Treasury's Operating Cash balance includes balances representing cash, cash equivalents, and other funds held by agencies, such as undeposited collections, deposits in transit, demand deposits, amounts held in trust, and imprest funds. Operating Cash held by the Treasury increased by $153.7 billion (an increase of approximately 80 percent) in fiscal year 2016 due to Treasury's investment and borrowing decisions to manage the balance and timing of the Government's cash position.

Restrictions on cash are due to the imposition on cash deposits by law, regulation, or agreement. Restricted cash is primarily composed of cash held by the DSCA. The Foreign Military Sales Program - DSCA included $20.7 billion and $23.9 billion as of September 30, 2016, and 2015, respectively.

International monetary assets include the U.S. reserve position in the International Monetary Fund (IMF) and U.S. holdings of Special Drawing Rights (SDRs). The U.S. reserve position in the IMF is an interest-bearing claim on the IMF that includes the reserve asset portion of the financial subscription that the United States has paid in as part of its participation in the IMF as well as any amounts drawn by the IMF from a letter of credit made available by the United States as part of its financial subscription to the IMF. The IMF promotes international monetary cooperation and a stable payments system to facilitate growth in the world economy. Its primary activities are surveillance of members' economies, financial assistance, as appropriate, and technical assistance.

Only a portion of the U.S. financial subscription to the IMF is made in the form of reserve assets; the remainder is provided in the form of a letter of credit from the United States to the IMF. The balance available under the letter of credit totaled $105.8 billion and $49.6 billion as of September 30, 2016, and 2015 respectively. The increase in fiscal year 2016 is due to Congress passing the *Consolidated Appropriations Act of 2016* (P.L. 114-113) which authorized and funded a SDR 40.9 billion (approximately $57 billion) increase in the U.S. quota in the IMF. The U.S. reserve position in the IMF had a U.S. dollar equivalent of $9.6 billion and $9.4 billion as of September 30, 2016, and 2015, respectively.

The SDR is an international reserve asset created by the IMF to supplement the existing reserve assets of its members. These interest-bearing assets can be obtained by IMF allocations, transactions with IMF member countries, or in the form of interest earnings on SDR holdings and reserve positions in the IMF. U.S. SDR holdings are an interest-bearing asset of Treasury's Exchange Stabilization Fund (ESF). The total amount of SDR holdings of the United States was the equivalent of $50.1 billion and $50.3 billion as of September 30, 2016, and 2015, respectively.

The IMF allocates SDRs to its members in proportion to each member's quota in the IMF. The *SDR Act*, enacted in 1968, authorized the Secretary of the Treasury to issue SDR Certificates (SDRCs) to the Federal Reserve in exchange for dollars. The amount of SDRCs outstanding cannot exceed the dollar value of SDR holdings. The Secretary of the Treasury

determines when Treasury will issue or redeem SDRCs. SDRCs outstanding totaled $5.2 billion as of September 30, 2016, and 2015, and are included in Note 16—Other Liabilities.

As of September 30, 2016, and 2015, other liabilities included $49.3 billion and $49.6 billion, respectively, of interest-bearing liability to the IMF for SDR allocations. The SDR allocation item represents the cumulative total of SDRs distributed by the IMF to the United States in allocations. The United States has received no SDR allocations since 2009.

Gold is valued at the statutory price of $42.2222 per fine troy ounce. The number of fine troy ounces of gold was 261,498,927 as of September 30, 2016, and 2015. The market value of gold on the London Fixing was $1,323 and $1,114 per fine troy ounce as of September 30, 2016, and 2015, respectively. In addition, silver is valued at the statutory price of $1.2929 per fine troy ounce. The number of fine troy ounces of silver was 16,000,000 as of September 30, 2016, and 2015. The market value of silver on the London Fixing was $19.35 and $14.65 per fine troy ounce as of September 30, 2016, and 2015, respectively. Gold totaling $11.0 billion as of September 30, 2016, and 2015, was pledged as collateral for gold certificates issued and authorized to the FRBs by the Secretary of the Treasury. Gold certificates were valued at $11.0 billion as of September 30, 2016, and 2015, which are included in Note 16—Other Liabilities. Treasury may redeem the gold certificates at any time. Foreign currency is translated into U.S. dollars at the exchange rate at fiscal year-end. The foreign currency is maintained by the ESF and various U.S. federal agencies as well as foreign banks.

Note 3. Accounts and Taxes Receivable, Net

Accounts and Taxes Receivable as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Accounts receivable:		
Gross accounts receivable	110.5	100.9
Allowance for uncollectible amounts	(29.6)	(27.4)
Accounts receivable, net	80.9	73.5
Taxes receivable:		
Gross taxes receivable	184.7	177.4
Allowance for uncollectible amounts	(132.3)	(133.1)
Taxes receivable, net	52.4	44.3
Total accounts and taxes receivable, net	133.3	117.8

Gross accounts receivable include related interest receivable of $3.2 billion and $3.7 billion as of September 30, 2016, and 2015, respectively.

Treasury comprises approximately 38.0 percent of the Government's reported accounts and taxes receivable, net, as of September 30, 2016. Refer to the financial statements of the Department of the Treasury, the Department of Health and Human Services, the Social Security Administration, the Department of Defense, the Department of Homeland Security, the Pension Benefit Guaranty Corporation, the Department of Energy, the Federal Deposit Insurance Corporation, the Department of Veterans Affairs, the Department of Agriculture, the Department of the Interior, the Office of Personnel Management, the National Credit Union Administration, the Tennessee Valley Authority, and the Department of Labor for details on gross accounts and taxes receivable and the related allowance for uncollectible amounts. These agencies comprise 95.7 percent of the Government's accounts and taxes receivable, net, of $133.3 billion as of September 30, 2016.

Note 4. Loans Receivable and Loan Guarantee Liabilities, Net

Direct Loans and Defaulted Guaranteed Loans as of September 30, 2016, and 2015

(In billions of dollars)	Face Value of Loans Outstanding		Long-term Cost of (Income from) Direct Loans and Defaulted Guaranteed Loans Outstanding		Loans Receivable, Net		Subsidy Expense (Income) for the Fiscal Year	
	2016	2015	2016	2015	2016	2015	2016	2015
Federal Direct Student Loans - Education	953.6	845.1	(5.3)	(35.5)	958.9	880.6	16.1	(0.9)
Federal Family Education Loans - Education	128.0	132.2	13.1	(2.5)	114.9	134.7	3.5	0.4
Electric Loans - USDA	47.3	47.9	2.1	2.0	45.2	45.9	-	(0.4)
Rural Housing Services - USDA	25.1	32.2	2.0	3.5	23.1	28.7	-	0.1
Export-Import Bank Loans	25.3	24.1	1.6	2.6	23.7	21.5	(0.3)	(0.3)
Housing and Urban Development Loans	22.4	23.1	5.7	6.9	16.7	16.2	(0.7)	(3.1)
Water and Environmental Loans - USDA	12.6	12.6	0.1	0.2	12.5	12.4	-	(0.1)
International Monetary Fund Program - Treasury	9.4	11.7	0.8	1.0	8.6	10.7	-	0.3
All other programs	88.9	81.7	14.9	16.4	74.0	65.3	(0.7)	1.5
Total direct loans and defaulted guaranteed loans	1,312.6	1,210.6	35.0	(5.4)	1,277.6	1,216.0	17.9	(2.5)

Loan Guarantees as of September 30, 2016, and 2015

(In billions of dollars)	Principal Amount of Loans Under Guarantee		Principal Amount Guaranteed by the United States		Loan Guarantee Liabilities		Subsidy Expense (Income) for the Fiscal Year	
	2016	2015	2016	2015	2016	2015	2016	2015
Federal Housing Administration Loans - HUD	1,335.7	1,292.1	1,213.4	1,178.1	(0.8)	16.1	(9.7)	(13.6)
Veterans Housing Benefit Programs - VA	517.2	453.9	132.8	117.4	10.0	9.9	(1.1)	0.5
Rural Housing Services - USDA	114.8	113.2	103.3	101.9	0.7	4.8	(4.3)	1.0
Small Business Loans - SBA	113.1	105.7	93.8	88.3	2.4	1.7	(0.4)	(1.3)
Export-Import Bank Guarantees	60.5	72.2	60.5	72.2	1.4	1.4	(0.1)	(0.2)
Israel Loan Guarantee Program - AID	9.1	10.5	9.1	10.5	1.2	1.0	-	-
Federal Family Education Loans - Education	196.9	219.7	192.7	215.1	1.4	-	6.7	(4.3)
All other guaranteed loan programs	49.6	45.5	44.4	40.4	1.9	1.4	0.7	0.3
Total loan guarantees	2,396.9	2,312.8	1,850.0	1,823.9	18.2	36.3	(8.2)	(17.6)

The Government has two types of loan programs: direct loans and loan guarantees. One major type of loan is direct loans such as the Department of Education's (Education) Federal Direct Student Loans. The second type is loan guarantee programs, such as the Department of Housing and Urban Development's (HUD's) Federal Housing Administration Loans program.

Direct loans and loan guarantee programs are used to promote the Nation's welfare by making financing available to segments of the population not served adequately by non-federal institutions, or otherwise providing for certain activities or investments. For those unable to afford credit at the market rate, federal credit programs provide subsidies in the form of direct loans offered at an interest rate lower than the market rate. For those to whom non-federal financial institutions are reluctant to grant credit because of the high risk involved, federal credit programs guarantee the payment of these non-federal loans and absorb the cost of defaults.

The amount of the long-term cost of post-1991 direct loans and loan guarantees outstanding equals the subsidy cost allowance for direct loans and the liability for loan guarantees as of September 30. The amount of the long-term cost of pre-1992 direct loans and loan guarantees equals the allowance for uncollectible amounts (or present value allowance) for direct loans and the liability for loan guarantees. The long-term cost is based on all direct loans and guaranteed loans disbursed in this fiscal year and previous years that are outstanding as of September 30. It includes the subsidy cost of these loans and guarantees estimated as of the time of loan disbursement and subsequent adjustments such as modifications, re-estimates, amortizations, and write-offs.

Net loans receivable includes related interest and foreclosed property. Foreclosed property is property that is transferred from borrowers to a federal credit program, through foreclosure or other means, in partial or full settlement of post-1991 direct loans or as a compensation for losses that the Government sustained under post-1991 loan guarantees. Please refer to the financial statements of the United States Department of Agriculture (USDA), VA, and HUD for significant detailed information regarding foreclosed property. The total subsidy expense/(income) is the cost of direct loans and loan guarantees recognized during the fiscal year. It consists of the subsidy expense/(income) incurred for direct and guaranteed loans disbursed during the fiscal year, for modifications made during the fiscal year of loans and guarantees outstanding, and for upward or downward re-estimates as of the end of the fiscal year of the cost of loans and guarantees outstanding. This expense/(income) is included in the Statements of Net Cost.

Loan Programs

The majority of the loan programs are provided by Education, HUD, USDA, Treasury, Small Business Administration (SBA), VA, Export-Import Bank and United States Agency for International Development (USAID). For significant detailed information regarding the direct and guaranteed loan programs listed in the tables above, please refer to the financial statements of the agencies.

Education has two major loan programs, authorized by Title IV of the *Higher Education Act of 1965* (HEA). The first program is the William D. Ford Federal Direct Loan Program, (referred to as the Direct Loan Program) that was established in fiscal year 1994. The Direct Loan Program offers four types of educational loans: Stafford, Unsubsidized Stafford, PLUS for parents and/or graduate or professional students, and consolidation loans. With this program, the Government makes loans directly to students and parents through participating institutions of higher education. Direct loans are originated and serviced through contracts with private vendors. Education disbursed approximately $140.5 billion in Direct Loans to eligible borrowers in fiscal year 2016 and approximately $142.2 billion in fiscal year 2015. The second program is the Federal Family Education Loan (FFEL) Program. This program was established in fiscal year 1965, and is a guaranteed loan program. Like the Direct Loan Program, it offers four types of loans: Stafford, Unsubsidized Stafford, PLUS for parents and/or graduate or professional students, and consolidation loans. The *Student Aid and Fiscal Responsibility Act* (SAFRA), which was enacted as part of the *Health Care Education and Reconciliation Act of 2010* (Public Law 111-152), eliminated the authority to guarantee new FFEL after June 30, 2010. During fiscal year 2016, Education net loans receivable increased by $58.8 billion, largely the result of increased Direct Loan Program disbursements for new loan originations and FFEL consolidations, net of borrower principal and interest collections.

HUD's Federal Housing Administration (FHA) provides mortgage insurance to encourage lenders to make credit available to expand home ownership. FHA serves many borrowers that the conventional market does not serve adequately. This includes first-time homebuyers, minorities, low-income, and other underserved households to realize the benefits of home ownership. Borrowers obtain an FHA insured mortgage and pay an upfront premium as well as an annual premium to FHA. The proceeds from those premiums are used to fund FHA program costs, including claims on defaulted mortgages and holding costs, property management fees, property sales, and other associated costs.

The *Consolidated Appropriations Act of 2016* (P.L. 114-113) resulted in no net change in the U.S. overall financial commitment to the IMF. P.L. 114-113 rescinded the provisions of the *Supplemental Appropriations Act of 2009* (P.L. 111-32), which previously authorized program increases in both the U.S. quota and U.S. participation in the NAB to be treated as direct loans to the IMF.

USDA offers direct and guaranteed loans through credit programs in the Farm and Foreign Agricultural Services (FFAS) mission area through the Farm Service Agency (FSA), and the Commodity Credit Corporation (CCC), and in the Rural Development (RD) mission area. The FFAS delivers commodity, credit, conservation, disaster, and emergency assistance programs that help strengthen and stabilize the agricultural economy. The FSA offers direct and guaranteed loans to farmers who are temporarily unable to obtain private, commercial credit. Through this supervised credit offered by FSA, the goal is to graduate its borrowers to commercial credit. The CCC offers both credit guarantee and direct credit programs for buyers of U.S. exports, suppliers, and sovereign countries in need of food assistance. The RD provides affordable housing and essential community facilities to rural communities through its rural housing loan and grant programs. The Rural Utilities Program helps to improve the quality of life in rural America through a variety of loan programs for electric energy, telecommunications, and water and environmental projects.

The Export-Import Bank aids in financing and promoting U.S. exports. Loans and guarantees extended under the medium-term loan program typically have repayment terms of one to seven years, while loans and guarantees extended under the long-term loan program usually have repayment terms in excess of seven years. Generally, both the medium-term and long-term loan and guarantee programs cover up to 85 percent of the U.S. contract value of shipped goods.

The SBA provides guarantees that help small businesses obtain bank loans and licensed companies to make investments in qualifying small businesses. The SBA also makes loans to microloan intermediaries and provides a direct loan program that assists homeowners, renters and businesses to recover from disasters.

VA operates the following direct loan and loan guaranty programs: Vocational Rehabilitation and Employment, Home Loans, and Insurance. The VA Home Loans program is the largest of the VA loan programs. The Home Loans program provides loan guarantees and direct loans to veterans, service members, qualifying dependents, and limited non-veterans to purchase homes and retain homeownership with favorable market terms. During fiscal year 2016, the VA principal amount of loans under guarantee increased by $63.3 billion. This increase was primarily due to new loans under guarantee with a principal totaling $151.9 billion, partially offset by guaranteed loan terminations with a principal amount of $88.6 billion.

In fiscal year 1993, USAID's Israel Loan Guarantee Program received the first authorization by Congress guaranteeing the repayment of loans made from commercial sources that covered the costs for immigrants resettling to Israel from the former Soviet Union, Ethiopia, and other countries. As of fiscal year 2016, $5.0 billion in loan guarantees remains

outstanding on this first initiative. In fiscal year 2003, USAID's Israel Loan Guarantee Program received a second authorization by Congress to support Israel's comprehensive economic plan to overcome economic difficulties and create conditions for higher and sustainable growth of which $4.1 billion in loan guarantees remains outstanding, as of September 30, 2016. The Israel Loan Guarantee Program has a total of $9.1 billion in loan guarantees outstanding from both initiatives.

Note 5. Inventories and Related Property, Net

Inventories and Related Property, Net as of September 30, 2016, and 2015

(In billions of dollars)	Defense	All Others	Total	Defense	All Others	Total
	2016			2015		
Inventory purchased for resale	61.9	0.5	62.4	61.3	0.4	61.7
Inventory and operating material and supplies held for repair	88.1	1.2	89.3	79.6	1.5	81.1
Inventory—excess, obsolete, and unserviceable	1.1	-	1.1	1.4	-	1.4
Operating materials and supplies held for use	105.0	3.5	108.5	121.9	3.5	125.4
Operating materials and supplies held in reserve for future use	-	0.2	0.2	-	0.2	0.2
Operating materials and supplies-excess, obsolete, and unserviceable	2.1	-	2.1	2.0	-	2.0
Stockpile materials held in reserve for future use	1.1	47.3	48.4	0.4	52.8	53.2
Stockpile materials held for sale	-	5.6	5.6	-	-	-
Other related property	2.4	1.2	3.6	1.5	1.1	2.6
Allowance for loss	(6.4)	(0.5)	(6.9)	(6.4)	(0.6)	(7.0)
Total inventories and related property, net	255.3	59.0	314.3	261.7	58.9	320.6

Inventory purchased for resale is the cost or value of tangible personal property purchased by an agency for resale. As of September 30, 2016, DOD values approximately 98 percent of its resale inventory using the moving average cost (MAC) method. DOD reports the remaining 2 percent of resale inventories at an approximation of historical cost using LAC adjusted for holding gains and losses. The LAC method is used because DOD's legacy inventory systems do not maintain historical cost data. DOD improved its capability to distinguish between held for use and held for repair for operating materials and supplies which resulted in an increase for inventory and operating material and supplies held for repair, and a decrease for operating materials and supplies held for use for fiscal year 2016. Please refer to the individual financial statements of DOD for significant detailed information regarding its inventories.

Inventory and operating materials and supplies held for repair are damaged inventory that require repair to make them suitable for sale (inventory) or is more economical to repair than to dispose of (operating materials and supplies). Excess, obsolete, and unserviceable inventory is reported at net realizable value. Inventory—excess, obsolete, and unserviceable consists of:

- Excess inventory that exceeds the demand expected in the normal course of operations and which does not meet management's criteria to be held in reserve for future sale.
- Obsolete inventory that is no longer needed due to changes in technology, laws, customs, or operations.
- Unserviceable inventory that is damaged beyond economic repair.

Operating materials and supplies held for use are tangible personal property to be consumed in normal operations.

Operating materials and supplies held in reserve for future use are materials retained because they are not readily available in the market or because they will not be used in the normal course of operations, but there is more than a remote chance they will eventually be needed. DOD, which accounts for most of the reported operating materials and supplies held for use, uses LAC and MAC, and expenses a significant amount when purchased instead of when consumed.

Operating materials and supplies—excess, obsolete, and unserviceable consists of:

- Excess operating materials and supplies are materials that exceed the demand expected in the normal course of operations, and do not meet management's criteria to be held in reserve for future use.
- Obsolete operating materials and supplies are materials no longer needed due to changes in technology, laws, customs, or operations.
- Unserviceable operating materials and supplies are materials damaged beyond economic repair.

DOD, which accounts for most of the reported excess, obsolete, and unserviceable operating materials and supplies, revalues it to a net realizable value of zero through the allowance account. Please refer to the individual financial statements of DOD for significant detailed information regarding operating materials and supplies. Stockpile materials include strategic and critical materials held in reserve for use in national defense, conservation, or national emergencies due to statutory requirements; for example, nuclear materials and oil, as well as stockpile materials that are authorized to be sold. FASAB issued SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials* which permits a reporting entity to apply an alternative evaluation method in establishing opening balances. During fiscal year 2016, select DOD components adopted this standard for stockpile materials, see Note 1. T—Prior-Period Adjustments. The majority of the stockpile materials held for sale and stockpile materials held in reserve for future use were reported by the Department of Energy (DOE). Please refer to the financial statements of DOE for more information on stockpile materials.

Other related property consists of the following:

- Commodities include items of commerce or trade that have an exchange value used to stabilize or support market prices. Please refer to the financial statements of the USDA for detailed information regarding commodities.
- Seized monetary instruments are comprised only of monetary instruments that are awaiting judgment to determine ownership. The related liability is included in other liabilities. Other property seized by the Government, such as real property and tangible personal property, is not considered a Government asset. It is accounted for in agency property-management records until the property is forfeited, returned, or otherwise liquidated. Please refer to the financial statements of the Department of Justice (DOJ), Treasury, and the Department of Homeland Security (DHS) for detailed information regarding seized property.
- Forfeited property is comprised of monetary instruments, intangible property, real property, and tangible personal property acquired through forfeiture proceedings; property acquired by the Government to satisfy a tax liability; and/or unclaimed/abandoned merchandise. Please refer to the financial statements of DOJ, Treasury, and DHS for detailed information regarding forfeited property.
- Foreclosed property is comprised of assets received in satisfaction of a loan receivable or as a result of payment of a claim under a guaranteed or insured loan (excluding commodities acquired under price support programs). All properties included in foreclosed property are assumed to be held for sale. Please refer to the financial statements of USDA and HUD for detailed information regarding foreclosed property.

Note 6. Property, Plant, and Equipment, Net

Property, Plant, and Equipment as of September 30, 2016

(In billions of dollars)	Cost		Accumulated Depreciation/ Amortization		Net	
	Defense	All Others	Defense	All Others	Defense	All Others
Buildings, structures, and facilities	384.1	275.3	230.1	150.8	154.0	124.5
Furniture, fixtures, and equipment	1,054.5	172.7	639.7	113.3	414.8	59.4
Construction in progress	118.1	46.5	N/A	N/A	118.1	46.5
Land	10.7	13.0	N/A	N/A	10.7	13.0
Internal use software	9.5	33.1	6.0	20.7	3.5	12.4
Assets under capital lease	0.4	4.1	0.2	1.7	0.2	2.4
Leasehold improvements	0.6	10.4	0.3	6.3	0.3	4.1
Other property, plant, and equipment	10.3	10.8	-	5.5	10.3	5.3
Subtotal	1,588.2	565.9	876.3	298.3	711.9	267.6
Total property, plant, and equipment, net		2,154.1		1,174.6		979.5

Property, Plant, and Equipment as of September 30, 2015

(In billions of dollars)	Cost		Accumulated Depreciation/ Amortization		Net	
	(Restated) Defense	All Others	Defense	All Others	(Restated) Defense	All Others
Buildings, structures, and facilities	283.2	268.1	137.0	144.0	146.2	124.1
Furniture, fixtures, and equipment	1,010.6	169.6	584.0	110.0	426.6	59.6
Construction in progress	73.2	43.3	N/A	N/A	73.2	43.3
Land	10.9	12.8	N/A	N/A	10.9	12.8
Internal use software	12.0	32.6	8.4	19.5	3.6	13.1
Assets under capital lease	0.4	3.4	0.2	1.7	0.2	1.7
Leasehold improvements	0.5	9.9	0.2	5.7	0.3	4.2
Other property, plant, and equipment	0.4	10.3	-	5.2	0.4	5.1
Subtotal	1,391.2	550.0	729.8	286.1	661.4	263.9
Total property, plant, and equipment, net		1,941.2		1,015.9		925.3

See Note 24—Stewardship Land and Heritage Assets for additional information on multi-use heritage assets.

DOD comprises approximately 72.7 percent of the Government's reported property, plant, and equipment, net, as of September 30, 2016. Fiscal year 2015 was restated due to DOD correcting a $31.4 billion understatement of their property, plant and equipment balance, see Note 1.V—Restatements. Also, during fiscal year 2016, DOD reclassified other assets, relating to outstanding contract financing payments, to property, plant and equipment-construction in progress in accordance with internal guidance.

FASAB issued SFFAS No. 50, *Establishing Opening Balances for General Property, Plant and Equipment*, which permits alternative methods in establish opening balances for general property, plant and equipment. During fiscal year 2016, select DOD components implemented this standard, see Note 1.T—Prior-Period Adjustments.

Refer to the financial statements of DOD, DOE, the Tennessee Valley Authority (TVA), GSA, VA, the Department of the Interior (DOI), DHS, the Department of State (DOS), the United States Postal Service (USPS), and the Department of Transportation (DOT) for detailed information on the useful lives and related capitalization thresholds for property, plant, and equipment. These agencies comprise 95 percent of the Government's reported property, plant, and equipment net of $979.5 billion as of September 30, 2016.

Note 7. Debt and Equity Securities

Debt and Equity Securities as of September 30, 2016

	By Category									
	Held-To-Maturity			Available-for-Sale			Trading Securities			
(In billions of dollars)	Cost Basis	Unamortized Premium/ Discount	Net Investment	Cost Basis	Unrealized Gain (Loss)	Fair Value	Cost Basis	Unrealized Gain (Loss)	Fair Value	Total
Debt Securities:										
Non-U.S. Government	0.1	-	0.1	9.5	0.4	9.9	0.1	-	0.1	10.1
Corporate and other bonds	-	-	-	-	-	-	0.2	-	0.2	0.2
Mortgage/asset backed	0.3	-	0.3	-	-	-	-	-	-	0.3
All other debt securities	-	-	-	-	-	-	0.2	-	0.2	0.2
Equity Securities:										
Unit trust	-	-	-	-	-	-	1.0	0.3	1.3	1.3
Common stocks	-	-	-	-	-	-	0.2	-	0.2	0.2
All other equity securities	0.1	-	0.1	-	-	-	0.2	-	0.2	0.3
Other	10.9	-	10.9	-	-	-	0.4	-	0.4	11.3
Total debt and equity securities categorized as held-to-maturity, available-for-sale or trading	11.4	-	11.4	9.5	0.4	9.9	2.3	0.3	2.6	23.9
Total RRB debt and equity securities										24.3
Total debt and equity securities										48.2

Debt and Equity Securities as of September 30, 2015

	By Category									
	Held-To-Maturity			Available-for-Sale			Trading Securities			
(In billions of dollars)	Cost Basis	Unamortized Premium/ Discount	Net Investment	Cost Basis	Unrealized Gain (Loss)	Fair Value	Cost Basis	Unrealized Gain (Loss)	Fair Value	Total
Debt securities:										
Non-U.S. Government	0.1	-	0.1	12.4	(0.7)	11.7	10.9	(0.8)	10.1	21.9
Corporate and other bonds	-	-	-	-	-	-	11.3	-	11.3	11.3
Mortgage/asset backed	0.2	-	0.2	-	-	-	3.6	-	3.6	3.8
Commercial	-	-	-	-	-	-	0.2	-	0.2	0.2
All other debt securities	-	-	-	-	-	-	3.5	-	3.5	3.5
Equity securities:										
Unit trust	-	-	-	-	-	-	17.4	3.8	21.2	21.2
Common stocks	-	-	-	-	-	-	1.3	0.3	1.6	1.6
All other equity securities	0.1	-	0.1	-	-	-	2.5	(0.4)	2.1	2.2
Other	3.7	-	3.7	-	-	-	11.1	0.4	11.5	15.2
Total debt and equity securities categorized as held-to-maturity, available-for-sale or trading	4.1	-	4.1	12.4	(0.7)	11.7	61.8	3.3	65.1	80.9
Total RRB debt and equity securities										23.5
Total debt and equity securities										104.4

Debt and Equity Securities as of September 30, 2016, and 2015

(In billions of dollars)	By Agency 2016	2015
Railroad Retirement Board	24.3	23.5
Department of the Treasury	9.9	11.7
Tennessee Valley Authority	9.8	9.2
Pension Benefit Guaranty Corporation	-	55.7
All other	4.2	4.3
Total securities and investments	48.2	104.4

These debt and equity securities do not include nonmarketable Treasury securities, which have been eliminated in consolidation. Held-to-maturity debt and equity securities are reported at amortized cost, net of unamortized discounts and premiums. Available-for-sale debt and equity securities are reported at fair value. Trading debt and equity securities are reported at fair value. TVA invests primarily in fixed maturity and equity securities, classified as trading. TVA reported gains related to trading securities still held as of September 30, 2016 and 2015 of $0.3 billion and $0.2 billion, respectively. Treasury invests primarily in fixed maturity and equity securities, classified as available-for-sale securities. Treasury's Exchange Stabilization Fund invests primarily in foreign fixed maturity debt, with a fair value of $9.8 billion and $11.7 billion as of September 30, 2016, and 2015, respectively. The National Railroad Retirement Investment Trust (NRRIT), on behalf of the RRB, manages and invests railroad retirement assets that are to be used to pay retirement benefits to the Nation's railroad workers under the Railroad Retirement Program. As an investment company, NRRIT is subject to different accounting standards that do not require the classifications presented above. Please refer to NRRIT's financial statements for more detailed information concerning this specific investment. The TVA balance includes $7.3 billion and $6.9 billion as of September 30, 2016, and 2015, respectively, for the Tennessee Valley Authority Retirement System (TVARS). TVARS includes unrealized gains of $0.5 billion and $0.1 billion as of September 30, 2016 and 2015, respectively. The Department of the Defense reflects majority of all other total securities and investments. NRRIT, Treasury and TVA base market values on the last sale of a listed security, on the mean of the "bid-and-ask" for nonlisted securities, or on a valuation model in the case of fixed income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. Please refer to the individual financial statements of DOD, NRRIT, Treasury, and TVA for more detailed information related to debt and equity securities. These agencies comprise 98.0 percent of the total reported debt and equity securities of $48.2 billion as of September 30, 2016. In fiscal year 2016, PBGC reported the amounts for its Trust Fund, that represents the present value of future benefits, in Note 21—Fiduciary Activities. Per Title IV of ERISA, PBGC is directed in its role as guarantor to provide guaranteed benefits to the extent allowed within statutory limits. As a result of reflecting the Trust Fund as fiduciary activity for fiscal year 2016, amounts in the table above display a decrease of $55.7 billion since the Trust Fund balances were reported with debt and equity securities in fiscal year 2015. PBGC's reporting changed as a result of clarifying Treasury guidance for fiscal year 2016 regarding fiduciary activities.

Note 8. Investments in Government-Sponsored Enterprises

Congress established Fannie Mae and Freddie Mac as GSEs to support mortgage lending. A key function of the GSEs is to purchase mortgages, package those mortgages into securities, which are subsequently sold to investors, and guarantee the timely payment of principal and interest on these securities.

Leading up to the financial crisis, increasingly difficult conditions in the housing market challenged the soundness and profitability of the GSEs, thereby threatening to undermine the entire housing market. In response Congress passed HERA (P.L.110-289) in July 2008. This act created FHFA, with enhanced regulatory authority over the GSEs, and provided the Secretary of the Treasury with certain authorities intended to ensure the financial stability of the GSEs, if necessary. In September 2008, FHFA placed the GSEs under conservatorship and Treasury invested in the GSEs by entering into a SPSPA with each GSE. These actions were taken to preserve the GSEs' assets, ensure a sound and solvent financial condition, and mitigate systemic risks that contributed to market instability.

The purpose of such actions is to maintain the solvency of the GSEs so they can continue to fulfill their vital roles in the home mortgage market while the Administration and Congress determine what structural changes should be made to the housing finance system. Draws under the SPSPAs result in an increased investment in the GSEs as further discussed below. Per SFFAC No. 2, *Entity and Display*, these entities meet the criteria of "bailed out" entities. Accordingly, the government has not consolidated them into the financial statements, but included disclosure of the relationship(s) with the bailed out entities and any actual or potential material costs or liabilities in the consolidated financial statements.

Senior Preferred Stock Purchase Agreements

Under the SPSPAs, Treasury initially received from each GSE: 1) 1,000,000 shares of non-voting variable liquidation preference senior preferred stock with a liquidation preference value of $1,000 per share and 2) a non-transferable warrant for the purchase, at a nominal cost, of 79.9 percent of common stock on a fully-diluted basis. The warrants expire on September 7, 2028. Under the amended SPSPAs, the quarterly dividend payment changed from a 10.0 percent per annum fixed rate dividend on the total liquidation preference to an amount equivalent to the GSE's positive net worth above a capital reserve amount. The capital reserve amount, which was initially set at $3.0 billion for calendar year 2013, declines by $600 million at the beginning of each calendar year thereafter until it reaches zero by calendar year 2018. On January 1, 2016, and 2015, the capital reserve amount had declined to $1.2 billion and $1.8 billion for calendar years 2016 and 2015, respectively. The GSEs will not pay a quarterly dividend if their positive net worth is below the required capital reserve threshold. Cash dividends of $11.5 billion and $20.4 billion were received during fiscal years ended September 30, 2016, and 2015, respectively.

The SPSPAs, which have no expiration date, provide that Treasury will disburse funds to the GSEs if at the end of any quarter, the FHFA determines that the liabilities of either GSE exceed its assets. Draws from Treasury under the SPSPAs are designed to ensure that the GSEs maintain positive net worth, with a fixed maximum amount available to each GSE under this agreement established as of December 31, 2012 (refer to the "Contingent Liability to GSEs" section below). Draws against the funding commitment of the SPSPAs do not result in the issuance of additional shares of senior preferred stock; instead, it increases the liquidation preference of the initial 1,000,000 shares by the amount of the draw. The combined cumulative liquidation preference totaled $189 billion as of September 30, 2016 and 2015. There were no payments to the GSEs for the fiscal years ended September 30, 2016 and 2015.

Senior Preferred Stock and Warrants for Common Stock

In determining the fair value of the senior preferred stock and warrants for common stock, Treasury relied on the GSEs' public filings and press releases concerning their financial statements, as well as non-public, long-term financial forecasts, monthly summaries, quarterly credit supplements, independent research regarding preferred stock trading, independent research regarding the GSEs' common stock trading on the OTC Bulletin Board, discussions with each of the GSEs and FHFA, and other information pertinent to the valuations. Because the instruments are not publicly traded, there is no comparable trading information available. The fair valuations rely on significant unobservable inputs that reflect assumptions about the expectations that market participants would use in pricing.

The fair value of the senior preferred stock considers the amount of forecasted dividend payments. The fair valuations assume that a hypothetical buyer would acquire the discounted dividend stream as of the transaction date. The fair value of the senior preferred stock increased as of September 30, 2016 when compared to September 30, 2015, primarily reflecting a lower discount rate which was driven by a lower long-term Treasury rate (or risk-free rate), as well as a reduction in the market value of the GSEs' other equity securities that comprise their total equity.

Factors impacting the fair value of the warrants include the nominal exercise price and the large number of potential exercise shares, the market trading of the common stock that underlies the warrants as of September 30, the principal market,

and the market participants. Other factors impacting the fair value include, among other things, the holding period risk related directly to the assumption of the amount of time that it will take to sell the exercised shares without depressing the market. The fair value of the warrants decreased at the end of fiscal year 2016, when compared to 2015, primarily due to decreases in the market price of the underlying common stock of each GSE.

Contingent Liability to GSEs

As part of the annual process undertaken by Treasury, a series of long-term financial forecasts are prepared to assess, as of September 30, the likelihood and magnitude of future draws to be required by the GSEs under the SPSPAs within the forecast time horizon. Treasury used 25-year financial forecasts prepared through years 2041 and 2040 in assessing if a contingent liability was required as of September 30, 2016 and 2015, respectively. If future payments under the SPSPAs are deemed to be probable within the forecast horizon, Treasury will estimate and accrue a contingent liability to the GSEs to reflect the forecasted equity deficits of the GSEs. This accrued contingent liability will be undiscounted and will not take into account any of the offsetting dividends that could be received, as the dividends, if any, would be owed directly to the General Fund. Such recorded accruals will be adjusted in subsequent years as new information develops or circumstances change.

Based on the annual assessment, Treasury estimated there was no probable future funding draws as of September 30, 2016 and 2015, and thereby accrued no contingent liability. However, as of September 30, 2016, it is reasonably possible that volatility in interest rates and fair value losses could potentially cause the GSEs to generate quarterly losses and, therefore, result in future funding draws against our funding commitment. Due to challenges quantifying future volatility in interest rates and fair value losses, Treasury could not estimate the total amount of this reasonably possible future funding liability as of September 30, 2016. At September 30, 2016 and 2015, the maximum remaining contractual commitment to the GSEs for the remaining life of the SPSPAs was $258.1 billion. Refer to Note 19—Commitments for a full description of other commitments and risks.

In assessing the need for an estimated contingent liability, Treasury relied on the GSEs' public filings and press releases concerning their financial statements, monthly summaries, and quarterly credit supplements, as well as non-public, long-term financial forecasts, the FHFA House Price Index, discussions with each of the GSEs and FHFA, and other information pertinent to the liability estimates. The forecasts prepared in assessing the need for an estimated contingent liability as of September 30, 2016 include three potential wind-down scenarios, with varying assumptions regarding the timing as to when the GSEs would cease issuing new guaranteed mortgage-backed securities. The forecasts also assume a continued gradual wind-down of the retained portfolios (and corresponding net interest income) through 2018, as directed under the amended SPSPAs for each GSE to reduce the maximum balance of its retained mortgage portfolio by 15.0 percent per annum beginning December 31, 2013. The maximum balance of the GSEs' retained mortgage portfolio was initially set at $650 billion as of December 31, 2012, and the amended SPSPAs requires that GSEs reduce this maximum balance to $250 billion by December 31, 2018.

Estimation Factors

Treasury's forecasts concerning the GSEs may differ from actual experience. Estimated senior preferred values and future draw amounts will depend on numerous factors that are difficult to predict including, but not limited to, changes in government policy with respect to the GSEs, the business cycle, inflation, home prices, unemployment rates, interest rates, changes in housing preferences, home financing alternatives, availability of debt financing, market rates of guarantee fees, outcomes of loan refinancings and modifications, new housing programs, and other applicable factors.

Regulatory Environment

To date, Congress has not approved a plan to address the future of the GSEs, thus the GSEs continue to operate under the direction of their conservator, the FHFA, whose stated strategic goals for the GSEs are to: (1) maintain foreclosure prevention activities and credit availability to foster liquid, efficient, competitive, and resilient national housing finance markets; (2) reduce taxpayer risk through increasing the role of private capital in the mortgage market, and (3) build a new single-family securitization infrastructure.

The *Temporary Payroll Tax Cut Continuation Act of 2011* (TPTCCA) was funded by an increase of 10-basis points in the GSEs' guarantee fees (referred to as "the incremental fees") which began in April 2012, and is effective through October 1, 2021. The incremental fees are to be remitted to Treasury and not retained by the GSEs and, thus, do not affect the profitability of the GSEs. For fiscal years 2016 and 2015, the GSEs remitted to Treasury the incremental fees totaling $2.8 billion and $2.4 billion, respectively.

As of September 30, 2016, and 2015, GSEs investments consisted of the following:

Investments in GSEs as of September 30, 2016

(In billions of dollars)	Gross Investments	Cumulative Valuation Gain/(Loss)	Fair Value
Fannie Mae senior preferred stock	117.0	(58.9)	58.1
Freddie Mac senior preferred stock	72.1	(32.5)	39.6
Fannie Mae warrants common stock	3.1	4.0	7.1
Freddie Mac warrants common stock	2.3	1.5	3.8
Total investments in GSEs	194.5	(85.9)	108.6

Investments in GSEs as of September 30, 2015

(In billions of dollars)	Gross Investments	Cumulative Valuation Gain/(Loss)	Fair Value
Fannie Mae senior preferred stock	117.0	(61.7)	55.3
Freddie Mac senior preferred stock	72.1	(35.5)	36.6
Fannie Mae warrants common stock	3.1	6.2	9.3
Freddie Mac warrants common stock	2.3	2.8	5.1
Total investments in GSEs	194.5	(88.2)	106.3

Note 9. Other Assets

Other Assets as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Advances and prepayments	92.9	108.1
Regulatory assets	21.8	22.4
FDIC receivable from resolution activity	9.0	13.9
Other	20.7	21.3
Total other assets	144.4	165.7

Advances and prepayments are assets that represent funds disbursed in contemplation of the future performance of services, receipt of goods, the incurrence of expenditures, or the receipt of other assets. These include advances to contractors and grantees, travel advances, and prepayments for items such as rents, taxes, insurance, royalties, commissions, and supplies.

During fiscal year 2016, DOD reclassified other assets, relating to outstanding contract financing payments, to property, plant, and equipment - construction in progress in accordance with internal guidance. With regard to regulatory assets, the DOE's Power Marketing Administrations (PMAs) and the TVA record certain amounts as assets in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 980, *Regulated Operations.* The provisions of FASB ASC Topic 980 require that regulated enterprises reflect rate actions of the regulator in their financial statements, when appropriate. These rate actions can provide reasonable assurance of the existence of an asset, reduce or eliminate the value of an asset, or impose a liability on a regulated enterprise. In order to defer incurred costs under FASB ASC Topic 980, a regulated entity must have the statutory authority to establish rates that recover all costs, and those rates must be charged to and collected from customers. If the PMAs' or TVA's rates should become market-based, FASB ASC Topic 980 would no longer be applicable, and all of the deferred costs under that standard would be expensed. Other items included in "other" are purchased power generating capacity, deferred nuclear generating units, nonmarketable equity investments in international financial institutions, derivative assets, and the balance of assets held by the experience rated carriers participating in the Health Benefits and Life Insurance Program (pending disposition on behalf of OPM).

The Federal Deposit Insurance Corporation (FDIC) has the responsibility for resolving failed institutions in an orderly and efficient manner. The resolution process involves valuing a failing institution, marketing it, soliciting and accepting bids for the sale of the institution, determining which bid is least costly to the insurance fund, and working with the acquiring institution through the closing process. FDIC records receivables for resolutions that include payments by the Deposit Insurance Fund to cover obligations to insured depositors, advances to receiverships and conservatorships for working capital, and administrative expenses paid on behalf of receiverships and conservatorships.

Note 10. Accounts Payable

Accounts Payable as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Department of Defense	18.3	18.9
Department of Veterans Affairs	4.8	10.9
Department of Justice	6.2	6.3
Department of the Treasury	4.4	3.9
Department of Education	4.0	3.7
Department of Energy	3.6	3.7
Department of State	2.5	2.5
Department of Homeland Security	2.0	2.1
General Services Administration	2.4	2.0
Department of Agriculture	1.9	1.8
U.S. Postal Service	1.8	1.8
U.S. Agency for International Development	1.7	1.8
Tennessee Valley Authority	1.5	1.5
National Aeronautics and Space Administration	1.3	1.4
Department of the Interior	0.7	1.0
All other	5.3	5.0
Total accounts payable	62.4	68.3

Accounts payable includes amounts due for goods and property ordered and received, services rendered by other than federal employees, accounts payable for cancelled appropriations, and non-debt related interest payable.

Note 11. Federal Debt Securities Held by the Public and Accrued Interest

Federal Debt Securities Held by the Public and Accrued Interest

(In billions of dollars)	Balance September 30, 2015	Net Change During Fiscal Year 2016	Balance September 30, 2016	Average Interest Rate 2016	Average Interest Rate 2015
Treasury securities (public):					
Marketable securities:					
Treasury bills	1,355.2	289.6	1,644.8	0.4%	0.1%
Treasury notes	8,366.0	258.3	8,624.3	1.8%	1.8%
Treasury bonds	1,688.2	137.1	1,825.3	4.4%	4.7%
Treasury inflation-protected securities (TIPS)	1,135.4	74.4	1,209.8	0.8%	0.8%
Treasury floating rate notes (FRN)	287.1	47.0	334.1	0.4%	0.1%
Total marketable Treasury securities	12,831.9	806.4	13,638.3		
Nonmarketable securities	292.0	243.1	535.1	2.0%	2.5%
Net unamortized premiums/(discounts)	(31.4)	(2.4)	(33.8)		
Total Treasury securities, net (public)	13,092.5	1,047.1	14,139.6		
Agency securities:					
Tennessee Valley Authority	23.7	0.1	23.8		
All other agencies	0.2	-	0.2		
Total agency securities, net of unamortized premiums and discounts	23.9	0.1	24.0		
Accrued interest payable	56.1	1.4	57.5		
Total federal debt securities held by the public and accrued interest	13,172.5	1,048.6	14,221.1		

Types of marketable securities:
Bills–Short-term obligations issued with a term of 1 year or less.
Notes–Medium-term obligations issued with a term of 2-10 years.
Bonds–Long-term obligations of more than 10 years.
TIPS–Term of more than 5 years.
FRN–Term of 2 years.

Federal debt securities held by the public outside the Government are held by individuals, corporations, state or local governments, FRBs, foreign governments, and other entities outside the federal government. The above table details Government borrowing primarily to finance operations and shows marketable and nonmarketable securities at face value less net unamortized premiums and discounts including accrued interest.

Securities that represent federal debt held by the public are issued primarily by the Treasury and include:

- Interest-bearing marketable securities (bills, notes, bonds, inflation-protected, and floating rate notes).
- Interest-bearing nonmarketable securities (government account series held by deposit and fiduciary funds, foreign series, state and local government series, domestic series, and savings bonds).
- Non-interest-bearing marketable and nonmarketable securities (matured and other).

Section 3111 of Title 31, United States Code (U.S.C.) authorizes the Secretary of the Treasury to use money received from the sale of an obligation and other money in the General Fund to buy, redeem, or refund, at or before maturity, outstanding bonds, notes, certificates of indebtedness, Treasury bills, or savings certificates of the Government.

Gross federal debt (with some adjustments) is subject to a statutory ceiling (i.e., the debt limit). Prior to 1917, Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress and the President first enacted a statutory dollar ceiling for federal borrowing. With the *Public Debt Act of 1941* (Public Law 77-7), Congress and the President set an overall limit of $65 billion on Treasury debt obligations that could be outstanding at any one time; since then, Congress and the President have enacted a number of debt limit increases.

When delays in raising or suspending the debt limit occur, as they did during both fiscal years 2015 and 2016, Treasury implements “extraordinary actions,” on a temporary basis. Many of the extraordinary actions taken by Treasury during the period of March 16, 2015 through October 30, 2015, resulted in federal debt securities not being issued to certain federal government accounts. As a result of Treasury securities not being issued to the Government Securities Investment Fund (G Fund) of the Thrift Savings Plan (TSP) of the Federal Retirement Thrift Investment Board (FRTIB) as of September 30, 2015, Treasury reported miscellaneous liabilities in the amount of $204.6 billion that represent uninvested principal of and related interest for the G Fund that would have been reported as Federal Debt Securities Held by the Public and Accrued Interest had there not been a delay in raising the statutory debt limit as of September 30, 2015, and had the Treasury securities been issued. On Monday, November 2, 2015, The *Bipartisan Budget Act of 2015* (Public Law 114-74) was enacted suspending the statutory debt limit through March 15, 2017. Treasury subsequently restored the uninvested principal and related interest to the G Fund, resulting in an increase in federal debt securities held by the public from 2015 to 2016. See Note 16—Other Liabilities and Note 21—Fiduciary Activities for more information.

As of September 30, 2016, and 2015, debt subject to the statutory debt limit was $19,538.5 billion and $18,113.0 billion, respectively. The debt subject to the limit includes Treasury securities held by the public and Government guaranteed debt of federal agencies (shown in the table above) and intragovernmental debt holdings (shown in the following table). As noted above, a delay in raising the statutory debt limit existed as of September 30, 2015. Extraordinary measures taken by Treasury during the period of March 16, 2015 through September 30, 2015 resulted in federal debt securities not being issued to certain federal government accounts. See Note 16—Other Liabilities and Note 21—Fiduciary Activities.

Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts as of September 30, 2016, and 2015

(In billions of dollars)	Balance 2015	Net Change During Fiscal Year 2016	Balance 2016
Social Security Administration, Federal Old-Age and Survivors Insurance Trust Fund	2,766.6	30.1	2,796.7
Office of Personnel Management, Civil Service Retirement and Disability Fund	731.3	155.9	887.2
Department of Defense, Military Retirement Fund	531.0	60.0	591.0
Department of Defense, Medicare-Eligible Retiree Health Care Fund	205.8	7.7	213.5
Department of Health and Human Services, Federal Hospital Insurance Trust Fund	195.5	(3.3)	192.2
Federal Deposit Insurance Corporation, Deposit Insurance Fund	60.1	11.4	71.5
Department of Transportation, Highway Trust Fund	7.7	56.9	64.6
Department of Health and Human Services, Federal Supplementary Medical Insurance Trust Fund	66.1	(2.8)	63.3
Department of Labor, Unemployment Trust Fund	44.4	9.4	53.8
Department of Energy, Nuclear Waste Disposal Fund	51.8	0.6	52.4
Office of Personnel Management, Postal Service Retiree Health Benefits Fund	45.2	6.3	51.5
Social Security Administration, Federal Disability Insurance Trust Fund	41.6	4.3	45.9
Office of Personnel Management, Employees Life Insurance Fund	44.0	1.2	45.2
Department of Housing and Urban Development, FHA, Mutual Mortgage Insurance Capital Reserve Account	14.7	21.7	36.4
Office of Personnel Management, Employees Health Benefits Fund	23.0	0.7	23.7
Pension Benefit Guaranty Corporation	18.5	5.2	23.7
Department of the Treasury, Exchange Stabilization Fund	20.8	1.9	22.7
Department of State, Foreign Service Retirement and Disability Fund	18.1	0.2	18.3
Department of Housing and Urban Development, Guarantees of Mortgage-Backed Securities Capital Reserve Account	12.8	3.0	15.8
Department of Transportation, Airport and Airway Trust Fund	12.7	0.7	13.4
National Credit Union Share Insurance Fund	11.6	0.7	12.3
All other programs and funds	103.5	1.3	104.8
Subtotal	5,026.8	373.1	5,399.9
Total net unamortized premiums/(discounts) for intragovernmental	75.3	(2.6)	72.7
Total intragovernmental debt holdings, net	5,102.1	370.5	5,472.6

Intragovernmental debt holdings represent the portion of the gross federal debt held as investments by government entities such as trust funds, revolving funds, and special funds. As noted above, the delay in raising the debt limit still existed as of September 30, 2015. On November 2, 2015 Congress enacted the *Bipartisan Budget Act of 2015* (Public Law No. 114-74) which temporarily suspended the debt limit through March 15, 2017. Treasury subsequently restored uninvested principal and related interest, resulting in an increase to the Civil Service Retirement and Disability Fund from 2015 to 2016.

Government entities that held investments in Treasury securities include trust funds that have funds from dedicated collections. For more information on funds from dedicated collections, see Note 20─Funds from Dedicated Collections. These intragovernmental debt holdings are eliminated in the consolidation of these financial statements.

Note 12. Federal Employee and Veteran Benefits Payable

Federal Employee and Veteran Benefits Payable as of September 30, 2016, and 2015

	Civilian		Military		Total	
(In billions of dollars)	2016	2015	2016	Restated 2015	2016	Restated 2015
Pension and accrued benefits	1,910.7	1,945.0	1,490.6	1,563.2	3,401.3	3,508.2
Veterans compensation and burial benefits	N/A	N/A	2,496.3	2,018.6	2,496.3	2,018.6
Post-retirement health and accrued benefits	352.3	364.0	799.7	731.2	1,152.0	1,095.2
Veterans education benefits	N/A	N/A	59.6	53.1	59.6	53.1
Life insurance and accrued benefits	50.9	49.6	7.7	8.4	58.6	58.0
FECA benefits	30.1	28.1	8.3	8.3	38.4	36.4
Liability for other benefits	1.0	0.9	2.2	2.0	3.2	2.9
Total federal employee and veteran benefits payable	2,345.0	2,387.6	4,864.4	4,384.8	7,209.4	6,772.4

Change in Pension and Accrued Benefits

	Civilian		Military		Total	
(In billions of dollars)	2016	2015	2016	2015	2016	2015
Actuarial accrued pension liability, beginning of fiscal year	1,945.0	1,905.2	1,563.2	1,565.1	3,508.2	3,470.3
Pension expense:						
Prior (and past) service costs from plan amendments or new plans	(1.0)	-	(18.7)	-	(19.7)	-
Normal costs	39.2	37.9	26.9	31.3	66.1	69.2
Interest on liability	73.9	75.9	63.4	66.6	137.3	142.5
Actuarial (gains)/losses (from experience)	(27.1)	(0.8)	(25.5)	(33.8)	(52.6)	(34.6)
Actuarial (gains)/losses (from assumption changes)	(33.0)	12.0	(61.2)	(9.4)	(94.2)	2.6
Other	0.1	0.3	-	-	0.1	0.3
Total pension expense	52.1	125.3	(15.1)	54.7	37.0	180.0
Less benefits paid	(86.4)	(85.5)	(57.5)	(56.6)	(143.9)	(142.1)
Actuarial accrued pension liability, end of fiscal year	1,910.7	1,945.0	1,490.6	1,563.2	3,401.3	3,508.2

Change in Post-Retirement Health and Accrued Benefits

(In billions of dollars)	Civilian 2016	Civilian 2015	Military 2016	Military 2015	Total 2016	Total 2015
Actuarial accrued post-retirement health benefits liability, beginning of fiscal year	364.0	336.8	731.2	760.5	1,095.2	1,097.3
Post-Retirement health benefits expense:						
Prior (and past) service costs from plan amendments or new plans	(0.2)	-	(5.8)	(21.2)	(6.0)	(21.2)
Normal costs	14.1	11.5	19.4	19.6	33.5	31.1
Interest on liability	14.8	14.3	30.3	33.0	45.1	47.3
Actuarial (gains)/losses (from experience)	(11.1)	7.6	40.9	(22.5)	29.8	(14.9)
Actuarial (gains)/losses (from assumption changes)	(14.0)	8.8	3.6	(18.1)	(10.4)	(9.3)
Total post-retirement health benefits expense	3.6	42.2	88.4	(9.2)	92.0	33.0
Less claims paid	(15.3)	(15.0)	(19.9)	(20.1)	(35.2)	(35.1)
Actuarial accrued post-retirement health benefits liability, end of fiscal year	352.3	364.0	799.7	731.2	1,152.0	1,095.2

The Government offers its employees retirement and other benefits, as well as health and life insurance. The liabilities for these benefits, which include both actuarial amounts and amounts due and payable to beneficiaries and health care carriers, apply to current and former civilian and military employees. Large fluctuations in actuarial amounts can result from changes in estimates to future outflows for benefits based on complex assumptions and cost models.

OPM administers the largest civilian plan. DOD and VA administer the largest military plans. Other significant pension plans with more than $10 billion in accrued benefits payable include those of the Coast Guard (DHS), Foreign Service (Department of State), TVA, and HHS's Public Health Service Commissioned Corps Retirement System. Please refer to the financial statements of the agencies listed for further details regarding their pension plans and other benefits.

Change in Civilian Life Insurance and Accrued Benefits

(In billions of dollars)	2016	2015
Actuarial accrued life insurance benefits liability, beginning of fiscal year	49.6	48.3
Life insurance benefits expense:		
New entrant expense	0.4	0.3
Interest on liability	1.9	2.0
Actuarial (gains)/losses (from experience)	(0.8)	(0.9)
Actuarial (gains)/losses (from assumption changes)	0.4	0.4
Total life insurance benefits expense	1.9	1.8
Less costs paid	(0.6)	(0.5)
Actuarial accrued life insurance benefits liability, end of fiscal year	50.9	49.6

Significant Long-Term Economic Assumptions Used in Determining Pension Liability and the Related Expense

	Civilian				Military	
	2016		2015		2016	2015
	FERS	CSRS	FERS	CSRS		
Rate of interest	4.00%	3.50%	4.10%	3.70%	3.90%	4.10%
Rate of inflation	1.90%	1.90%	2.30%	2.30%	1.70%	2.10%
Projected salary increases	1.50%	1.50%	1.70%	1.70%	2.10%	2.30%
Cost of living adjustment	1.60%	1.90%	1.80%	2.30%	N/A	N/A

Significant Long-Term Economic Assumptions Used in Determining Post-Retirement Health Benefits and the Related Expense

	Civilian		Military	
	2016	2015	2016	2015
Rate of interest	4.00%	4.10%	4.00%	4.10%
Single equivalent medical trend rate	5.00%	5.30%	4.56%	4.56%
Ultimate medical trend rate	3.50%	3.90%	4.45%	4.85%

Significant Long-Term Economic Assumptions Used in Determining Life Insurance Benefits and the Related Expense

	Civilian	
	2016	2015
Rate of interest	3.80%	4.00%
Rate of increase in salary	1.50%	1.70%

In accordance with SFFAS No. 33, *Pension, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, agencies are required to separately present gains and losses from changes in long-term assumptions used to estimate liabilities associated with pensions, Other Retirement Benefits (ORB), and Other Postemployment Benefits (OPEB) on the Statement of Net Cost. SFFAS No. 33 also provides a standard for selecting the discount rate assumption for present value estimates of federal employee pension, ORB, and OPEB liabilities. The SFFAS No. 33 standard for selecting discount rate assumption requires it be based on a historical average of interest rates on marketable Treasury securities consistent with the cash flows being discounted. Additionally, SFFAS No. 33 provides a standard for selecting the valuation date for estimates of federal employee pension, ORB, and OPEB liabilities that establishes a consistent method for such measurements.

To provide a sustainable, justifiable data resource for the affected agencies, Treasury developed a new model and methodology for developing these interest rates in fiscal year 2014. The new method that was developed is based on methodology used to produce the High Quality Market (HQM) Yield Curve pursuant to the *Pension Protection Act of 2006*.[2] As of July 2014, Treasury began releasing interest rate yield curve data using this new U.S. Department of the Treasury's Yield Curve for Treasury Nominal Coupon Issues (TNC yield curve), which is derived from Treasury notes

[2] Treasury's HQM resource is available at: http://www.treasury.gov/resource-center/economic-policy/corp-bond-yield/Pages/Corp-Yield-Bond-Curve-Papers.aspx.

and bonds. The TNC yield curve provides information on Treasury nominal coupon issues and the methodology extrapolates yields beyond 30 years through 100 years maturity. The TNC yield curve is used to produce a Treasury spot yield curve (a zero coupon curve), which provides the basis for discounting future cash flows.

Civilian Employees

Pensions

OPM administers the largest civilian pension plan, which covers substantially all full-time, permanent civilian federal employees. This plan includes two components of defined benefits, the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). The basic benefit components of the CSRS and the FERS are financed and operated through the Civil Service Retirement and Disability Fund (CSRDF), a trust fund. CSRDF monies are generated primarily from employees' contributions, agency contributions, payments from the General Fund, and interest on investments in Treasury securities.

The Federal Retirement Thrift Investment Board administers the TSP. The TSP investment options include two fixed income funds (the G and F Funds), three stock funds (the C, S, and I Funds) and five lifecycle funds (L 2050, L 2040, L 2030, L 2020, and L Income). The L Funds diversify participant accounts among the G, F, C, S, and I Funds, using professionally determined investment mixes (allocations) that are tailored to different time horizons. Treasury securities held in the G Fund are included in federal debt securities held by the public and accrued interest on the Balance Sheet. The G Fund held $220.9 billion and $0.0 billion in nonmarketable Treasury securities as of September 30, 2016, and 2015, respectively. The increase in nonmarketable Treasury securities held in the G Fund relates to the delay in raising the debt limit that was ongoing as of September 30, 2015. The Secretary of the Treasury has authority to take extraordinary actions to stay within the statutory debt limit imposed by Congress. One such action involves the suspension of the issuance of securities to the G Fund if the issuance cannot be made without causing the debt limit to be exceeded. Please see Note 16—Other Liabilities for additional information.

The liability for civilian pension and accrued benefits payable decreased $34.3 billion. The $34.3 billion decrease is largely attributable to assumption changes and experience. The experience gain is primarily driven by the actual annuitant cost-of-living adjustment (COLA) increase for 2016 (0.0% for both CSRS and FERS) being lower than previously assumed (2.3% for CSRS and 1.8% for FERS). The assumption gain results primarily from decreases to the assumed future long-term rate of annuitant COLA and assumed rate of general salary increase.

Post-Retirement Health Benefits

The post-retirement civilian health benefit liability is an estimate of the Government's future cost of providing post-retirement health benefits to current employees and retirees. Although active and retired employees pay insurance premiums under the Federal Employees Health Benefits Program (FEHB), these premiums cover only a portion of the costs. The OPM actuary applies economic assumptions to historical cost information to estimate the liability. The *Postal Accountability and Enhancement Act of 2006* (Postal Act of 2006) (Public Law No 109-435, Title VIII), made significant changes in the funding of future retiree health benefits for employees of the USPS, including the requirement for the USPS to make scheduled payments to the Postal Service Retiree Health Benefits (PSRHB) Fund. Various legislation requires the USPS to make scheduled payments to the PSRHB Fund ranging from $5.4 billion to $5.8 billion per year from fiscal year 2007 through fiscal year 2016. Thereafter, the law requires USPS to make annual payments in the amount of the normal cost plus or minus an amount to amortize the unfunded liability or surplus. USPS currently owes the PSRHB Fund: $11.1 billion for fiscal year 2012, $5.6 billion for fiscal year 2013, $5.7 billion for both fiscal years 2014 and 2015, and $5.8 billion for fiscal year 2016. As of September 30, 2016, USPS has not indicated its intention regarding payment of the total $33.9 billion due. At this time, Congress has not taken further action on these payments due to the PSRHB Fund from USPS. The cost for each year's payment, including any defaulted payment, along with all other benefit program costs, are included in USPS' net cost for that year in the consolidated Statements of Net Cost.

The post-retirement civilian health benefit liability decreased $11.7 billion. The $11.7 billion decrease is primarily attributable to assumption changes and experience. The experience gain is due to a lower medical cost increase compared to the prior year's assumed trend. The assumption gain results mainly from decreases to the assumed future long-term medical trend rates.

Life Insurance Benefits

One of the largest other employee benefits is the Federal Employee Group Life Insurance (FEGLI) Program. Employee and annuitant contributions and interest on investments fund a portion of this liability. The actuarial life insurance liability is the expected present value of future benefits to pay to, or on behalf of, existing FEGLI participants, less the expected present value of future contributions to be collected from those participants. The OPM actuary uses salary increase and interest rate yield curve assumptions that are generally consistent with the pension liability.

Workers' Compensation Benefits

The DOL determines both civilian and military agencies' liabilities for future workers' compensation benefits for civilian federal employees, as mandated by the *Federal Employees' Compensation Act* (FECA), for death, disability, medical, and miscellaneous costs for approved compensation cases, and a component for incurred, but not reported, claims. The FECA liability is determined annually using historical benefit payment patterns related to injury years to predict the future payments.

The actuarial methodology provides for the effects of inflation and adjusts historical payments to constant dollars by applying wage inflation factors (cost-of-living adjustments or COLA) and medical inflation factors (consumer price index-medical or CPIM) to the calculation of projected benefits.

DOL selects the COLA factors, CPIM factors, and discount rate by averaging the COLA rates, CPIM rates, and interest rates for the current and prior four years. Using averaging renders estimates that reflect historical trends over five years instead of conditions that exist in one year.

The COLAs and CPIMs used in the projections for fiscal year 2016 are listed below in the table. For the COLAs and CPIMs used in the projections for fiscal year 2015, refer to the *Fiscal Year 2015 Financial Report of the U.S. Government*.

Fiscal Year	COLA	CPIM
2017	1.31%	2.99%
2018	1.13%	3.09%
2019	1.23%	3.40%
2020	1.45%	3.68%
2021+	1.85%	3.87%

DOL selected the interest rate assumptions whereby projected annual payments were discounted to present value based on interest rate assumptions on the TNC Yield Curve to reflect the average duration of income payments and medical payments. The average durations for income payments and medical payments were 14.7 years and 9.8 years in fiscal year 2016 and 14.9 years and 9.8 years in fiscal year 2015, respectively. Based on averaging the TNC Yield Curves for the current and prior four years, the interest rate assumptions for income payments and medical payments were 2.78% and 2.26% in fiscal year 2016 and 3.13% and 2.50% in fiscal year 2015, respectively.

Military Employees (Including Veterans)

Pensions

The military retirement system consists of a funded, noncontributory, defined benefit plan. It applies to military personnel (Departments of Army, Navy, Air Force, and the Marine Corps). This system includes non-disability retired pay, disability retired pay; survivor annuity programs, and Combat-Related Special Compensation. The Service Secretaries may approve immediate non-disability retired pay at any age with credit of at least 20 years of active duty service. Reserve retirees must be at least 60 years old and have at least 20 qualifying years of service before retired pay commences; however, in some cases, the age can be less than 60 if the reservist performs certain types of active service. P.L. 110-181 provides for a 90-day reduction in the reserve retirement age from age 60 for every 3 months of certain active duty service served within a fiscal year for service after January 28, 2008 (not below age 50). There is no vesting of benefits before non-disabled retirement. There are distinct non-disability benefit formulas related to four populations within the Military Retirement System: Final Pay, High-3, Career Status Bonus/Redux, and the Blended Retirement System (BRS) enacted in the *National Defense*

Authorization Act for Fiscal Year 2016, effective January 1, 2018. The date an individual enters the military determines which retirement system they would fall under and if they have the option to pick their retirement system. For more information on these benefits, see DOD's Office of Military Compensation website http://militarypay.defense.gov.

The DOD Military Retirement Fund was established by Public Law (P.L.) 98-94 (currently Chapter 74 of Title 10, U.S.C.) and accumulates funds to finance, on an accrual basis, the liabilities of DOD military retirement and survivor benefit programs. This Fund receives income from three sources: monthly normal cost payments from the Services and Treasury to pay for the current years' service cost; annual payments from the Treasury to amortize the unfunded liability and pay for the increase in the normal cost attributable to Concurrent Receipt per Public Law 108-136; and investment income.

The $72.6 billion decrease in the Military Retirement Pension liability is attributable to experience gains, assumption changes, and a plan amendment gain reflecting the new Blended Retirement System statutory provisions, which together offset the liability growth generated by benefit accruals (normal cost) and interest on the outstanding liability. Liabilities in the future will depend on expected changes due to interest and benefit accruals, future benefit changes, assumption changes, and actuarial experience.

Post-Retirement Health Benefits

Military retirees and their dependents are entitled to health care in military medical facilities if a facility can provide the needed care. The Military Retiree Health Benefits are post-retirement benefits DOD provides to non-Medicare-eligible military retirees, Medicare-eligible retired beneficiaries and other eligible beneficiaries through private sector health care providers and DOD's medical treatment facilities. Prior to becoming Medicare eligible, military retirees and other eligible beneficiaries are entitled to participate in TRICARE (now managed by the Defense Health Agency)[3], which reimburses (net of beneficiary copay and deductible requirements) for the cost of health care from civilian providers. TRICARE options are available in indemnity, preferred provider organization, and health maintenance organization (HMO) designs.

Since fiscal year 2002, TRICARE, as second payer to Medicare, covers military retirees and other eligible beneficiaries after they become Medicare eligible. This TRICARE coverage for Medicare eligible beneficiaries requires that the beneficiary enroll in Medicare Part B (unless the beneficiary that is Medicare eligible is the spouse of an Active Duty Service Member) and is referred to as TRICARE for Life (TFL). Health care under TFL can be obtained from military medical facilities on an "as available" basis or from civilian providers. Military retiree health care actuarial liabilities are calculated annually using assumptions and actual experience. Trend assumptions include inpatient and outpatient care and prescriptions for both direct care and purchased services. Military retiree health care liability figures include projected costs incurred in military medical facilities, as well as projected claims paid to civilian providers and certain administrative costs. Costs paid to civilian providers are net of Medicare's portion of the cost.

10 U.S.C., Chapter 56 created the DOD Medicare-Eligible Retiree Health Care Fund (MERHCF), which became operative on October 1, 2002. The purpose of this fund is to account for the health benefits of Medicare-eligible military retirees, their dependents, and survivors who are Medicare eligible. The Fund receives revenues from three sources: interest earnings on MERHCF assets, Uniformed Services normal cost contributions, and Treasury contributions. The DOD Medicare-Eligible Retiree Health Care Board of Actuaries (the Board) approves the methods and assumptions used to calculate the per capita normal cost rates and the U.S. Treasury contribution, and the Secretary of Defense directs the Secretary of Treasury to make the payments. The MERHCF pays costs incurred in military medical facilities, claims for care provided by civilian providers under TFL administration, costs associated with processing the TFL claims, and capitated payments for coverage provided by U.S. Family Health Plans. The actuaries calculate the actuarial liabilities annually using assumptions and actual experience (e.g., mortality and retirement rates, direct care costs, purchased care).

Military post-retirement health and accrued benefits payable increased $68.5 billion. The $68.5 billion increase is due primarily to actuarial experience losses being different from what was assumed (demographic and claims data).

In addition to the health care benefits for civilian and military retirees and their dependents, the VA also provides medical care to veterans on an "as available" basis, subject to the limits of the annual appropriations. In accordance with 38 CFR 17.36 (c), VA's Secretary makes an annual enrollment decision that defines the veterans, by priority, who will be treated for that fiscal year subject to change based on funds appropriated, estimated collections, usage, the severity index of enrolled veterans, and changes in cost. While VA expects to continue to provide medical care to veterans in future years, an estimate of such future benefits cannot be reasonably made. Accordingly, VA recognizes the medical care expenses in the period the medical care services are provided. For the fiscal years 2012 through 2016, the average medical care cost per year was $47.0 billion.

[3] On October 1, 2013, the Department of Defense established the Defense Health Agency (DHA) to manage the activities of the Military Health System. These activities include those previously managed by TRICARE Management Activity (TMA), which was disestablished on the same date.

Veterans Compensation and Burial Benefits

The Government compensates disabled veterans and their survivors. Veterans' compensation is payable as a disability benefit or a survivor's benefit. Entitlement to compensation depends on the veteran's disabilities having been incurred in, or aggravated during, active military service; death while on duty; or death resulting from service-connected disabilities, if not on active duty.

Eligible veterans who die or are disabled from military service-related causes, as well as their dependents, receive compensation benefits. Also, veterans are provided with burial flags, headstones/markers, and grave liners for burial in a VA national cemetery or are provided a burial flag, headstone/marker and a plot allowance for burial in a private cemetery. These benefits are provided under 38 U.S.C., Part 2, Chapter 23 in recognition of a veteran's military service and are recorded as a liability in the period the requirements are met.

The liability for veterans' compensation and burial benefits payable is based on an actuarial estimate of future compensation and burial payments and increased by $477.7 billion in fiscal year 2016. The $477.7 billion increase is primarily attributable to assumption changes and experience. The major actuarial assumption changes and experience impacts include growth in compensation counts, new mortality rates, changes in the discount rate, and an increase in beneficiary counts.

Several significant actuarial assumptions were used in the valuation of compensation and burial benefits to calculate the present value of the liability. A liability was recognized for the projected benefit payments to: 1) those beneficiaries, including veterans and survivors, currently receiving benefit payments; 2) current veterans who will in the future become beneficiaries of the compensation program; and 3) a proportional share of those in active military service as of the valuation date who will become veterans in the future. Future benefit payments to survivors of those veterans in classes 1, 2, and 3 above are also incorporated into the projection. The projected liability does not include any administrative costs.

The veterans' compensation and burial benefits liability is developed on an actuarial basis. It is impacted by interest on the liability balance, experience gains or losses, changes in actuarial assumptions, prior service costs, and amounts paid for costs included in the liability balance.

Change in Veterans Compensation and Burial Benefits

	Compensation		Burial		Total	
(In billions of dollars)	2016	2015	2016	2015	2016	2015
Actuarial accrued liability, beginning of fiscal year	2,014.0	2,002.6	4.6	4.5	2,018.6	2,007.1
Current year expense:						
Interest on the liability balance	82.2	85.9	0.2	0.2	82.4	86.1
Actuarial (gains)/losses (from experience)	91.9	9.5	0.2	0.1	92.1	9.6
Actuarial (gains)/losses (from assumption changes)	377.4	(13.0)	0.1	-	377.5	(13.0)
Total current year expense	551.5	82.4	0.5	0.3	552.0	82.7
Less benefits paid	(74.1)	(71.0)	(0.2)	(0.2)	(74.3)	(71.2)
Actuarial accrued liability, end of fiscal year	2,491.4	2,014.0	4.9	4.6	2,496.3	2,018.6

Significant Economic Assumptions Used in Determining Veterans Compensation and Burial Benefits as of September 30, 2016, and 2015

	2016	2015
Rate of interest	3.93%	4.08%
Rate of inflation	2.30%	2.44%

Veterans Education Benefits

In fiscal year 2016, VA reassessed the application of *Statement of Federal Financial Accounting Standards (SFFAS) 5, Accounting for Liabilities of the Federal Government*, as it relates to Post-9/11 GI Bill (Chapter 33) liabilities. The Post-9/11 GI Bill is an education benefit program for individuals who served on active duty after September 10, 2001. Based on this assessment, VA determined that accrued Post-9/11 GI Bill (Chapter 33) education benefits should be recognized at the time an accountable event occurs, and that any portion of costs that remain unpaid at the end of the period should be recorded as a liability. Therefore, for fiscal year 2016 these amounts are reported for the first time in the following table titled Change in Veterans Education Benefits with a $46.9 billion correction of error to the fiscal year 2015 beginning net position. Prior to fiscal year 2016, the liability recorded for Chapter 33 benefits was limited to funds that had not been disbursed at month-end and did not include future liability amounts that were probable.

Veterans with at least 90 days of aggregate service after September 10, 2001, or individuals discharged with a service-connected disability after 30 days are eligible to receive Post-9/11 GI Bill (Chapter 33) benefits, which include tuition and fees and a monthly housing allowance. Eligibility for veterans and/or their beneficiaries to use Chapter 33 benefits continues for 15 years after their last period of 90 consecutive days or more of active duty. Veterans are eligible for up to 36 months of enrollment in an educational institution, which includes a monthly housing allowance, yearly textbook and supplies stipend, and one-time payment for relocation. Veterans' eligibility for these amounts is based upon the length of their active duty service.

VA recognizes an education benefit liability once VA has approved an original enrollment certification. VA estimates the unfunded education benefit liability using the following assumptions:

- As of September 30, 2016, 1,668,467 beneficiaries are currently eligible, and have an enrollment certification.
- Due to limited experience data, dropout rates were not incorporated into the model. The data from 2009 to 2016 was not sufficient to estimate the dropout rates. As an example, those who have dropped out can reclaim their eligibility for benefits up to the end of the 15-year window of eligibility.
- For beneficiaries with remaining eligibility who are not using the benefits as of September 30, 2016, the model assumes the beneficiary will start using the benefits beginning in fiscal year 2017.
- The model assumes that beneficiaries use the benefits for 6 months each year until all the benefits are exhausted.
- The annual payment trend rates used in the model were 4.38%, 4.25%, and 3.16% for fiscal year 2017, fiscal year 2018, and fiscal year 2019 and later, respectively.

Change in Veterans Education Benefits

(In billions of dollars)	2016	Restated 2015
Actuarial accrued liability, beginning of fiscal year	53.1	46.9
Current year expense:		
Enrollment certifications issued	18.0	17.4
Interest on liability	0.2	0.1
Total current year expense	18.2	17.5
Less benefits paid	(11.7)	(11.3)
Actuarial accrued liability, end of fiscal year	59.6	53.1

Life Insurance Benefits

The largest veterans' life insurance programs consist of the following:

- National Service Life Insurance (NSLI) covers policyholders who served during World War II.
- Veterans' Special Life Insurance (VSLI) was established in 1951 to meet the insurance needs of veterans who served during the Korean Conflict and through the period ending January 1, 1957.
- Service-Disabled Veterans Insurance (S-DVI) program was established in 1951 to meet the insurance needs of veterans who received a service-connected disability rating.

The components of veteran life insurance liability for future policy benefits are presented below:

Veterans Life Insurance Liability as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Insurance death benefits:		
NSLI	3.4	3.8
VSLI	1.3	1.3
S-DVI	0.6	0.6
Other	0.3	0.5
Total death benefits	5.6	6.2
Death benefit annuities	0.1	0.1
Disability income & waiver	0.8	0.8
Insurance dividends payable	1.2	1.3
Total veterans life insurance liability	7.7	8.4

Insurance dividends payable consists of dividends left on a deposit with VA, related interest payable, and dividends payable to policyholders.

The VA supervises Service members Group Life Insurance (SGLI) and Veterans Group Life Insurance programs that provide life insurance coverage to members of the uniformed armed services, reservists, and post-Vietnam Veterans as well as their families. All SGLI insureds are automatically covered under the Traumatic Injury Protection (TSGLI) program, which provides for insurance payments to Veterans who suffer a serious traumatic injury in service. VA has entered into a group policy with the Prudential Insurance Company of America to administer these programs.

Pension Benefits

The VA also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled for nonservice-related causes. VA pension benefits are recognized as a non-exchange transaction due to the nature of the VA pension plan. Therefore, the actuarial present value of these future benefits is not required to be recorded on the Balance Sheet. The projected amounts of future payments for pension benefits (presented for informational purposes only) as of September 30, 2016, and 2015, was $87.2 billion and $94.1 billion, respectively.

Note 13. Environmental and Disposal Liabilities

Environmental and Disposal Liabilities as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Department of Energy:		
Environmental and disposal liabilities	371.8	339.8
Department of Defense:		
Environmental restoration	26.8	27.2
Disposal of weapon systems program	21.9	22.2
Environmental corrective other	9.3	6.7
Base realignment and closure	4.6	3.9
Total Department of Defense	62.6	60.0
All other agencies	12.2	11.8
Total environmental and disposal liabilities	446.6	411.6

During World War II and the Cold War, DOE (or predecessor agencies) developed a massive industrial complex to research, produce, and test nuclear weapons. This included nuclear reactors, chemical-processing buildings, metal machining plants, laboratories, and maintenance facilities that manufactured tens of thousands of nuclear warheads and conducted more than 1,000 nuclear tests.

At all sites where these activities took place, some environmental contamination occurred. This contamination was caused by the production, storage, and use of radioactive materials and hazardous chemicals, which resulted in contamination of soil, surface water, and groundwater. The environmental legacy of nuclear weapons production also includes thousands of contaminated buildings and large volumes of waste and special nuclear materials requiring treatment, stabilization, and disposal.

Estimated cleanup costs at sites for which there are no current feasible remediation approaches, such as the Nevada nuclear test site, are excluded from the estimates, although applicable stewardship and monitoring costs for these sites are included. DOE has not been required through regulation to establish remediation activities for these sites.

Estimating DOE's environmental cleanup liability requires making assumptions about future activities and is inherently uncertain. The future course of DOE's environmental cleanup and disposal will depend on a number of fundamental technical and policy choices, many of which have not been made. The sites and facilities could be restored to a condition suitable for any desirable use, or could be restored to a point where they pose no near-term health risks. Achieving the former conditions would have a higher cost but may (or may not) warrant the costs, or be legally required. The environmental and disposal liability estimates include contingency estimates intended to account for the uncertainties associated with the technical cleanup scope of the program.

DOE's environmental and disposal liabilities estimates are dependent on annual funding levels and achievement of work as scheduled. Congressional appropriations at lower than anticipated levels or unplanned delays in project completion would cause increases in life-cycle costs.

DOE's environmental and disposal liabilities also include the estimated cleanup and post-closure responsibilities, including surveillance and monitoring activities, soil and groundwater remediation, and disposition of excess material for sites. The Department is responsible for the post-closure activities at many of the closure sites as well as other sites. The costs for these post-closure activities are estimated for a period of 75 years after the balance sheet date, i.e., through 2091 in fiscal year 2016 and through 2090 in fiscal year 2015. While some post-cleanup monitoring and other long-term stewardship activities post-2091 are included in the liability, there are others the Department expects to continue beyond 2091 for which the costs cannot reasonably be estimated.

A portion of DOE's environmental and disposal liabilities at various field sites includes anticipated costs for facilities managed by DOE's ongoing program operations which will ultimately require stabilization, deactivation, and decommissioning. The estimate is largely based upon a cost-estimating model. Site specific estimates are used in lieu of the cost-estimating model, when available. Cost estimates for ongoing program facilities are updated each year. For facilities

newly contaminated since fiscal year 1997, cleanup costs allocated to future periods and not included in environmental and disposal liabilities amounted to $0.7 billion for both fiscal years 2016 and 2015.

Please refer to the financial statements of the DOE for significant detailed information regarding DOE's environmental and disposal liabilities, including cleanup costs.

DOD must restore active installations, installations affected by base realignment and closure, and other areas formerly used as Defense sites. DOD also bears responsibility for disposal of chemical weapons and environmental costs associated with the disposal of weapons systems (primarily nuclear powered aircraft carriers and submarines).

DOD follows the *Comprehensive Environmental Response, Compensation, and Liability Act* (CERCLA), *Superfund Amendments and Reauthorization Act*, *Resource Conservation and Recovery Act* (RCRA) and other applicable federal or state laws to clean up contamination. The CERCLA and RCRA require the DOD to clean up contamination in coordination with regulatory agencies, current owners of property damaged by the Department, and third parties that have a partial responsibility for the environmental restoration. Failure to comply with agreements and legal mandates puts the DOD at risk of incurring fines and penalties.

DOD uses engineering estimates and independently validated models to estimate environmental costs. The engineering estimates are used after obtaining extensive data during the remedial investigation/feasibility phase of the environmental project.

For general PP&E placed into service after September 30, 1997, DOD expenses associated environmental costs systematically over the life of the asset using two methods: physical capacity for operating landfills and life expectancy in years for all other assets. DOD expenses the full cost to clean up contamination for stewardship property, plant, and equipment at the time the asset is placed into service. DOD has expensed the costs for cleanup associated with general property, plant, and equipment placed into service before October 1, 1997, except for costs intended to be recovered through user charges; for those costs, DOD has expensed cleanup costs associated with that portion of the asset life that has passed since it was placed into service. DOD systematically recognizes the remaining cost over the remaining life of the asset. The unrecognized portion of the cleanup cost associated with general property, plant, and equipment is $2.7 billion and $3.1 billion for fiscal years 2016 and 2015, respectively. Not all components of DOD are able to compile the necessary information for this disclosure, thus the amount reported may not accurately reflect DOD's total unrecognized costs associated with general property, plant, and equipment. DOD is implementing procedures to address these deficiencies.

DOD is unable to estimate and report a liability for environmental restoration and corrective action for buried chemical munitions and agents, because the extent of the buried chemical munitions and agents is unknown at this time. DOD is also unable to provide a complete estimate for the Formerly Utilized Sites Remedial Action Program. DOD has ongoing studies and will update its estimate as additional liabilities are identified. DOD has the potential to incur costs for restoration initiatives in conjunction with returning overseas Defense facilities to host nations. However, DOD is unable to provide a reasonable estimate at this time because the extent of required restoration is unknown.

Please refer to the financial statements of DOD for further detailed information regarding DOD's environmental and disposal liabilities, including cleanup costs.

In addition, in accordance with Technical Bulletin 2006-1, agencies recorded an environmental and disposal liability for asbestos-related cleanup costs totaling $5.4 billion and $4.3 billion as of September 30, 2016, and 2015, respectively.

Note 14. Benefits Due and Payable

Benefits Due and Payable as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Federal Old-Age and Survivors Insurance	69.1	66.1
Federal Supplementary Medical Insurance (Medicare Parts B and D)	36.2	37.9
Grants to States for Medicaid	35.4	36.8
Federal Disability Insurance	28.1	27.1
Federal Hospital Insurance (Medicare Part A)	27.8	28.3
Supplemental Security Income	5.4	5.3
Unemployment Insurance	1.4	1.1
All other benefits programs	14.8	11.3
Total benefits due and payable	218.2	213.9

Benefits due and payable are amounts owed to program recipients or medical service providers as of September 30 that have not been paid. HHS and the SSA administer the majority of the medical service programs and the DOL administers the Unemployment Insurance program. For a description of the programs, see Note 22—Social Insurance and the Unaudited Required Supplementary Information—Social Insurance section.

Note 15. Insurance and Guarantee Program Liabilities

Insurance and Guarantee Program Liabilities as of September 30, 2016, and 2015

(In billions of dollars)	2016	Reclass 2015
Insurance and Guarantee Program Liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	110.0	161.1
Department of Agriculture - Federal Crop Insurance	8.9	8.3
All other insurance and guarantee programs	3.4	0.9
Total insurance and guarantee program liabilities	122.3	170.3

As of September 30, 2016, and 2015, $110.0 billion and $161.1 billion, respectively, pertain to the PBGC single-employer and multiemployer pension plans. PBGC insures pension benefits for participants in covered defined benefit pension plans. As a wholly-owned corporation of the government, PBGC's financial activity and balances are included in the consolidated financial statements of the government. The decrease from 2016 to 2015 is due to a change resulting from clarifying Treasury guidance for fiscal year 2016 regarding fiduciary activities. As a result of reflecting PBGC's Trust Fund as fiduciary activity for fiscal year 2016, amounts in the table above display a decrease for the PBGC – Benefit Pension Plans. The PBGC single-employer program now reports a portion of the present value of future benefits in Note 21—Fiduciary Activities.

As of September 30, 2016, and 2015, $8.9 billion and $8.3 billion, respectively, pertain to the USDA's Federal Crop Insurance Program. The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters.

In fiscal year 2016, FDIC liabilities were reclassified to Note 16—Other Liabilities for fiscal year 2016 and 2015.

Note 16. Other Liabilities

Other Liabilities as of September 30, 2016, and 2015 (In billions of dollars)	2016	Reclass 2015
Unearned revenue and assets held for others:		
Unearned fees for nuclear waste disposal (DOE) and other unearned revenue	54.4	67.2
Assets held on behalf of others	114.4	106.6
Subtotal	168.8	173.8
Employee-related liabilities:		
Accrued federal employees' wages and benefits	36.2	38.1
Selected DOE contractors' and D.C. employees' pension benefits	53.1	50.0
Subtotal	89.3	88.1
International monetary liabilities and gold certificates:		
Exchange Stabilization Fund	54.5	54.8
Gold certificates (see Note 2)	11.0	11.0
Subtotal	65.5	65.8
Subsidies and grants:		
Farm and other subsidies	13.5	5.5
Grant payments due to state and local governments and others	21.9	17.8
Subtotal	35.4	23.3
Miscellaneous liabilities:		
Legal and other contingencies	49.6	47.1
Non-federal power projects and capital lease liabilities, and disposal liabilities	11.0	11.1
Liability for restoration of federal debt principal and interest	-	204.6
Other miscellaneous	45.1	45.7
Subtotal	105.7	308.5
Total	464.7	659.5

Other liabilities represent liabilities that are not separately identified on the Balance Sheet and are presented on a comparative basis by major category.

Unearned Revenue and Assets Held for Others

The government recognizes a liability when it receives money in advance of providing goods and services or assumes custody of money belonging to others. The government's unearned revenue from fees DOE has collected from utility companies for the future cost of managing the disposal of nuclear waste and interest income received is about $38.8 billion and $37.4 billion as of September 30, 2016, and 2015, respectively. Other unearned revenue includes USPS income for such things as prepaid postage, outstanding money orders, and prepaid P.O. Box rentals. Assets held on behalf of others include funds collected in advance, and undelivered Defense articles. DSCA holds $80.9 billion and $78.1 billion as of September 30, 2016, and 2015, respectively for articles and services for future delivery to foreign governments.

In fiscal year 2016, Federal Deposit Insurance Corporation (FDIC) determined the information previously report in Note 15– Insurance and Guarantee Program Liabilities should be included in Note 16– Other Liabilities. The effect was a reclassification of $7.2 billion to the Assets held on behalf of others line for the fiscal year 2015.

Employee-Related Liabilities

This category includes amounts owed to employees at year-end and actuarial liabilities for certain non-federal employees. Actuarial liabilities for federal employees and veteran benefits are included in Note 12–Federal Employee and Veteran Benefits Payable and are reported on another line on the Balance Sheet. The largest liability in the employee-related liabilities category is the amount owed at the end of the fiscal year to federal employees for wages and benefits (including accrued annual leave). In addition, DOE is liable to certain contractors for contractor employee pension and postretirement benefits, which is about $28.9 billion and $26.3 billion as of September 30, 2016 and 2015, respectively. Also, the government owed about $8.8 billion as of September 30, 2016, and 2015, for estimated future pension benefits of the District of Columbia's judges, police, firefighters, and teachers.

International Monetary Liabilities and Gold Certificates

Consistent with U.S. obligations in the IMF on orderly exchange arrangements and a stable system of exchange rates, the Secretary of the Treasury, with the approval of the President, may use the Exchange Stabilization Fund to deal in gold, foreign exchange, and other instruments of credit and securities.

Gold certificates are issued in nondefinitive or book-entry form to the Federal Reserve Bank of New York (FRBNY). The government's liability incurred by issuing the gold certificates, as reported on the Balance Sheet, is limited to the gold being held by the Department of the Treasury at the standard value established by law. Upon issuance of gold certificates to the FRBNY, the proceeds from the certificates are deposited into the operating cash of the U.S. Government. All of the Department of the Treasury's certificates issued are payable to the FRBNY.

Subsidies and Grants

The government supports the public good through a wide variety of subsidy and grant programs in such areas as agriculture, medical and scientific research, education, and transportation. USDA programs such as Conservation Reserve; grants, subsidies, and contributions; and Agricultural Risk Coverage and Price Loss Coverage account for the majority of the subsidies due, about $12.7 billion and $8.9 billion as of September 30, 2016 and 2015, respectively.

The government awards hundreds of billions of dollars in grants annually. These include project grants that are competitively awarded for agency-specific projects, such as HHS grants to fund projects to "enhance the independence, productivity, integration, and inclusion into the community of people with developmental disabilities." Other grants are formula grants, such as matching grants. Formula grants go to state governments for such things as education and transportation programs. These grants are paid in accordance with distribution formulas that have been provided by law or administrative regulations. Of the total liability reported for grants as of September 30, 2016, and 2015, DOT, Education, and HHS collectively owed their grantees about $16.6 billion and $12.6 billion, respectively. Refer to the financial statements and footnotes of the respective agencies for additional information.

Miscellaneous Liabilities

Some of the more significant liabilities included in this category are for (1) legal and other contingencies (see Note 18—Contingencies), (2) Bonneville Power Administration liability to pay annual budgets of several power projects for its electrical generating capacity, (3) payables due to the purchases of securities, and (4) other liabilities reported by Treasury as a result of the occurrence of a delay in raising the statutory debt limit as of September 30, 2015. When delays in raising the statutory debt limit occur, Treasury often must deviate from its normal debt management operations and take a number of extraordinary actions to meet the Government's obligations as they come due without exceeding the debt limit. Many extraordinary actions taken by Treasury during the period of March 16, 2015, through October 30, 2015, resulted in federal debt securities not being issued to certain federal government accounts. As a result of Treasury securities not being issued to

the G Fund of the Thrift Savings Plan (TSP), Treasury reported miscellaneous liabilities in the amount of $204.6 billion that represent uninvested principal of and related interest for the TSP's G Fund that would have been reported in Note 11—Federal Debt Securities Held by the Public and Accrued Interest had there not been a delay in raising the statutory debt limit as of September 30, 2015, and had the Treasury securities been issued. On Monday, November 2, 2015, the *Bipartisan Budget Act of 2015* (Public Law 114-74) was enacted suspending the statutory debt limit through March 15, 2017. Treasury subsequently restored the uninvested principal and related interest to the G Fund, resulting in an increase of Federal Debt Securities Held by the Public and Accrued Interest from 2015 to 2016. For further information, see Note 11—Federal Debt Securities Held by the Public and Accrued Interest and Note 21—Fiduciary Activities.

In addition, many federal agencies reported relatively small amounts of miscellaneous liabilities that are not otherwise classified.

Note 17. Collections and Refunds of Federal Revenue

Collections of Federal Tax Revenue for the Year Ended September 30, 2016

(In billions of dollars)	Federal Tax Revenue Collections	Tax Year to Which Collections Relate			
		2016	2015	2014	Prior Years
Individual income tax and tax withholdings	2,874.9	1,833.5	982.9	32.8	25.7
Corporation income taxes	345.6	228.2	107.2	2.5	7.7
Excise taxes	101.8	78.6	23.0	0.1	0.1
Unemployment taxes	47.1	31.9	15.1	-	0.1
Customs duties	35.0	35.0	-	-	-
Estate and gift taxes	22.3	-	8.0	0.9	13.4
Railroad retirement taxes	5.9	4.5	1.4	-	-
Fines, penalties, interest, and other revenue	6.6	6.5	0.1	-	-
Subtotal	3,439.2	2,218.2	1,137.7	36.3	47.0
Less: amounts collected for non-federal entities	(0.4)				
Total	3,438.8				

Treasury is the Government's principal revenue-collecting agency. Collections of individual income and tax withholdings include FICA/SECA and individual income taxes. These taxes are characterized as non-exchange revenue.

Excise taxes, also characterized as non-exchange revenue, consist of taxes collected for various items, such as airline tickets, gasoline products, distilled spirits and imported liquor, tobacco, firearms, and others.

Federal Tax Refunds Disbursed for the Year Ended September 30, 2016

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate			
		2016	2015	2014	Prior Years
Individual income tax and tax withholdings	372.3	37.0	300.7	26.5	8.1
Corporation income taxes	51.4	6.5	19.2	7.4	18.3
Excise taxes	1.5	0.2	0.6	0.4	0.3
Unemployment taxes	0.2	-	0.2	-	-
Customs duties	1.6	0.9	0.3	0.1	0.3
Estate and gift taxes	1.3	0.4	0.5	0.1	0.3
Total	428.3	45.0	321.5	34.5	27.3

Reconciliation of Revenue to Tax Collections for the Year Ended September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Consolidated revenue per the Statement of Operations and Changes in Net Position	3,345.3	3,334.0
Tax refunds	428.3	406.5
Earned income tax and child tax credit imputed revenue	(80.8)	(80.7)
Other tax credits and accrual adjustments	(41.0)	(36.9)
Federal Insurance Contributions Act - Tax	21.2	20.1
Federal Reserve earnings	(115.7)	(96.5)
Nontax-related fines and penalties reported by agencies	(100.3)	(93.0)
Nontax-related earned revenue	(18.2)	(42.6)
Collections of federal tax revenue	3,438.8	3,410.9

Consolidated revenue in the SOCNP is presented on a modified cash basis, net of tax refunds, and includes other non-tax related revenue. Earned Income Tax Credit, Child Tax Credit, and other tax credits amounts (unaudited) are included in gross cost in the Statements of Net Cost. The *Federal Insurance Contributions Act* – Tax is included in the Individual income and tax withholdings line in the Collections of Federal tax revenue; however, it is not reported on the SOCNP as these collections are intragovernmental revenue and eliminated in consolidation. The table above reconciles total revenue to federal tax collections.

Collections of Federal Revenue for the Year Ended September 30, 2015

(In billions of dollars)	Federal Tax Revenue Collections	Tax Year to Which Collections Relate			
		2015	2014	2013	Prior Years
Individual income tax and tax withholdings	2,799.1	1,790.8	954.6	28.3	25.4
Corporation income taxes	389.9	260.2	114.9	3.9	10.9
Excise taxes	102.8	79.9	22.8	0.1	-
Unemployment taxes	49.3	33.4	15.7	-	0.2
Customs duties	36.4	36.4	-	-	-
Estate and gift taxes	20.0	-	6.8	0.6	12.6
Railroad retirement taxes	6.4	5.0	1.4	-	-
Fines, penalties, interest and other revenue	7.4	7.3	0.1	-	-
Subtotal	3,411.3	2,213.0	1,116.3	32.9	49.1
Less: amounts collected for non-federal entities	(0.4)				
Total	3,410.9				

Federal Tax Refunds Disbursed for the Year Ended September 30, 2015

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate			
		2015	2014	2013	Prior Years
Individual income tax and tax withholdings	351.4	30.7	290.0	23.6	7.1
Corporation income taxes	50.1	6.2	20.8	5.5	17.6
Excise taxes	1.1	0.4	0.6	0.1	-
Unemployment taxes	0.2	-	0.1	-	0.1
Customs duties	2.8	1.5	0.8	0.2	0.3
Estate and gift taxes	0.9	-	0.2	0.3	0.4
Total	406.5	38.8	312.5	29.7	25.5

Note 18. Contingencies

Financial Treatment of Loss Contingencies

Loss contingencies are existing conditions, situations, or set of circumstances involving uncertainty as to possible loss to an entity. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. The reporting of loss contingencies depends on the likelihood that a future event or events will confirm the loss or impairment of an asset or the incurrence of a liability. Terms used to assess the range for the likelihood of loss are probable, reasonably possible, and remote. Loss contingencies that are assessed as probable and measurable are accrued in the financial statements. Loss contingencies that are assessed to be at least reasonably possible are disclosed in this note and loss contingencies that are assessed as remote are not reported in the financial statements, nor disclosed in the notes. The following table provides criteria for how federal agencies are to account for loss contingencies, based on the likelihood of the loss and measurability.[4]

Likelihood of future outflow or other sacrifice of resources	Loss amount can be reasonably measured	Loss range can be reasonably measured	Loss amount or range cannot be reasonably measured
Probable Future confirming event(s) are more likely to occur than not.[5]	Accrue the liability. Report on Balance Sheet and Statement of Net Cost.	Accrue liability of the best estimate or (if there is no best estimate) minimum amount in loss range, and disclose nature of contingency and range of estimated liability.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Reasonably possible Possibility of future confirming event(s) occurring is more than remote and less than likely.	Disclose nature of contingency and estimated loss amount.	Disclose nature of contingency and estimated loss range.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Remote Possibility of future event(s) occurring is slight.	No disclosure.	No disclosure.	No disclosure.

[4] In addition, a third condition must be met to be a loss contingency: a past event or an exchange transaction must occur.

[5] For loss contingencies related to litigation, probable is defined as the future confirming event or events are more likely than not to occur, with the exception of pending or threatened litigation and unasserted claims. For the pending or threatened litigation and unasserted claims, the future confirming event or events are likely to occur.

The Government is subject to loss contingencies that include insurance and litigation cases. These loss contingencies arise in the normal course of operations and their ultimate disposition is unknown. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the financial statements, except for the insurance and litigation described in the following section, which could have a material adverse effect on the financial statements.

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The Government has insurance contingencies that are reasonably possible in the amount of $243.8 billion as of September 30, 2016, and $239.1 billion as of September 30, 2015. The major programs are identified below:

- PBGC reported $242.8 billion and $237.7 billion as of September 30, 2016, and 2015, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined benefit pension plans that are classified as a reasonably possible exposure to loss. This increase is primarily due to the growth in the number of companies meeting the reasonably possible criteria for the single-employer program, while the multiemployer program experienced a decrease in liability due to changes in the data and underlying assumptions.
- FDIC reported $0.7 billion and $1.2 billion as of September 30, 2016, and 2015, respectively, for identified additional risk in the financial services industry that could result in additional loss to the DIF should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

Deposit Insurance

Deposit insurance covers all types of deposit accounts such as checking, Negotiable Order of Withdrawal and savings accounts, money market deposit accounts, and certificates of deposit received at an insured bank, savings association, or credit union. The insurance covers the balance of each depositor's account and shares, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured financial institution's closing. As a result, the Government has the following exposure from federally-insured financial institutions:

- FDIC has estimated insured deposits of $6,822.9 billion as of September 30, 2016, and $6,420.0 billion as of September 30, 2015, for the DIF.
- National Credit Union Administration (NCUA) has estimated insured shares of $1,015.9 billion as of September 30, 2016, and $939.9 billion as of September 30, 2015, for the National Credit Union Share Insurance Fund.

Legal Contingencies

Legal contingencies as of September 30, 2016, and 2015, are summarized in the table below:

(In billions of dollars)	2016 Accrued Liabilities [1]	2016 Estimated Range of Loss for Certain Cases [2] Lower End	2016 Estimated Range of Loss for Certain Cases [2] Upper End	2015 Accrued Liabilities [1]	2015 Estimated Range of Loss for Certain Cases [2] Lower End	2015 Estimated Range of Loss for Certain Cases [2] Upper End
Legal contingencies:						
Probable	7.2	7.2	7.9	6.0	6.0	7.4
Reasonably possible	-	9.2	16.3	-	8.7	13.7

[1] Accrued liabilities are recorded and presented in the related line items of the Balance Sheet.

[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is party to various administrative claims and legal actions brought against it, some of which may ultimately result in settlements or decisions against the Government.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for "probable" cases against the government are $7.2 billion and $6.0 billion as of September 30, 2016, and 2015, respectively, and are included in "Other Liabilities" on the Balance Sheet. For example, the U.S. Supreme Court decision in *Salazar v. Ramah Navajo Chapter*, dated June 18, 2012, is likely to result in additional claims against the Indian Health Service (IHS), which is a component within HHS. As a result of this decision, many tribes have filed claims. Some claims have been settled and others have been asserted but not yet settled.

There are also administrative claims and legal actions pending where adverse decisions are considered by management and legal counsel as "reasonably possible" with an estimate of potential loss or a range of potential loss. The estimated potential losses for such claims and actions range from $9.2 billion to $16.3 billion as of September 30, 2016, and from $8.7 billion to $13.7 billion as of September 30, 2015. For example, the Department of the Treasury's *American Recovery and Reinvestment Tax Act of 2009* (ARRA) Related Cases are a number of cases that were filed in the U.S. Court of Federal Claims alleging that the U.S. government violated statutory and regulatory mandates to make proper payments to plaintiffs under ARRA, Section 1603, for having placed certain energy properties into service. The Department has determined there is a reasonably possible likelihood of unfavorable outcomes in some of the cases.

Numerous litigation cases are pending where the outcome is uncertain or it is reasonably possible that a loss has been incurred and where estimates cannot be made. There are other litigation cases where the plaintiffs have not made claims for specific dollar amounts, but the settlement may be significant. The ultimate resolution of these legal actions for which the potential loss could not be determined may materially affect the U.S. government's financial position or operating results. An example of a specific case is summarized below:

- In the case, *Starr International Co., Inc. v. United States*, the plaintiff, an American International Group, Inc. (AIG) shareholder that brought suit on behalf of two classes of shareholders, alleges that the U.S. government violated the Fifth Amendment to the United States Constitution by illegally exacting or taking property without just compensation. One class, the Credit Agreement Class, claimed that the Fifth Amendment was violated when a majority share of AIG's equity and voting rights was conveyed in connection with an $85 billion loan to AIG during the 2008 financial crisis. Starr also asserted a Fifth Amendment violation on behalf of the second class, the Reverse Stock Split Shareholder Class, alleging that a June 2009 reverse split of AIG's common stock constituted a taking of the common stockholders' asserted right to a shareholder vote on whether to approve a reverse split of AIG's common stock. The U.S. Court of Federal Claims held that the Credit Agreement Shareholder Class prevails on liability, but recovers no damages, and that the Reverse Stock Split Shareholder class does not prevail on liability or damages. Both the Plaintiff and the United States have appealed. The Government is unable to determine the likelihood of an unfavorable outcome or make an estimate of potential loss at this time.

Environmental and Disposal Contingencies

Environmental and disposal contingencies as of September 30, 2016, and 2015, are summarized in the table below:

	2016			2015		
		Estimated Range of Loss for Certain Cases [2]			Estimated Range of Loss for Certain Cases [2]	
(In billions of dollars)	Accrued Liabilities [1]	Lower End	Upper End	Accrued Liabilities [1]	Lower End	Upper End
Environmental and disposal contingencies:						
Probable	25.9	25.8	25.9	25.9	25.9	26.0
Reasonably possible	-	0.7	1.8	-	0.7	1.0

[1] Accrued liabilities are recorded and presented in the related line items of the Balance Sheet.

[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is subject to loss contingencies for a variety of environmental cleanup costs for the storage and disposal of hazardous material as well as the operations and closures of facilities at which environmental contamination may be present.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for these cases are $25.9 billion and $25.9 billion as of September 30, 2016, and 2015, respectively, and are included in "Other Liabilities" on the Balance Sheet.

In accordance with the *Nuclear Waste Policy Act of 1982* (NWPA), DOE entered into contracts with more than 45 utilities in return for payment of fees established by the NWPA into the Nuclear Waste Fund. DOE agreed to begin disposal of spent nuclear fuel (SNF) by January 31, 1998. Because DOE has no facility available to receive SNF under the NWPA, it has been unable to begin disposal of the utilities' SNF as required by the contracts. Therefore, DOE is subject to SNF litigation for damages suffered by all utilities as a result of the delay in beginning disposal of SNF and also damages for alleged exposure to radioactive and/or toxic substances. Significant claims for partial breach of contract and a large number of class action and/or multiple plaintiff tort suits have been filed with estimated liability amounts of $24.7 billion and $23.7 billion as of September 30, 2016, and 2015, respectively.

Other Contingencies

DOT, HHS, and Treasury reported the following other contingencies:

- The Federal Highway Administration (FHWA) preauthorizes states to establish construction budgets without having received appropriations from Congress for such projects. FHWA has authority to approve projects using advance construction under 23 U.S.C. 115(a). FHWA does not guarantee the ultimate funding to the states for these "advance construction" projects and does not obligate any funds for these projects. When funding becomes available to FHWA, the states can then apply for reimbursement of costs that they have incurred on such projects, at which time FHWA can accept or reject such requests. FHWA has pre-authorized $50.6 billion and $50.4 billion to the states to establish budgets for its construction projects for fiscal years ending September 30, 2016, and 2015, respectively. Congress has not provided appropriations for these projects and no liability is accrued in the DOT consolidated financial statements.
- Contingent liabilities have been accrued as a result of Medicaid audit and program disallowances that are currently being appealed by the states and for reimbursement of state plan amendments. The Medicaid amounts are $10.2 billion and $7.5 billion for fiscal years ending September 30, 2016, and 2015, respectively. In all cases, the funds have been returned to HHS. If the appeals are decided in favor of the states, HHS will be required to pay these amounts. In addition, certain amounts for payment have been deferred under the Medicaid program when there is

reasonable doubt as to the legitimacy of expenditures claimed by a state. There are also outstanding reviews of the state expenditures in which a final determination has not been made.

- Through an annual process, Treasury assesses the need for an estimated contingent liability that reflects the forecasted equity deficits of the GSEs. While no accrued contingent liability was determined to be needed for fiscal years 2016 and 2015, it is reasonably possible that volatility in interest rates and fair value losses could potentially cause the GSEs to generate quarterly losses and, therefore, result in future funding draws against the funding commitment. Due to challenges quantifying future volatility in interest rates and fair value losses, Treasury could not estimate the total amount of this reasonably possible future funding liability as of September 30, 2016. See Note 8– Investments in Government-Sponsored Enterprises for further information.

Treaties

The U.S. Government is a party to major treaties and other international agreements. These treaties and other international agreements address various issues including, but not limited to, trade, commerce, security, and arms that may involve financial obligations or give rise to possible exposure to losses. A comprehensive analysis to determine any such financial obligations or possible exposure to loss and their related effect on the consolidated financial statements of the U.S. Government has not yet been performed.

Note 19. Commitments

Long-Term Operating Leases as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
General Services Administration	23.1	23.9
U.S. Postal Service	7.4	7.1
Department of State	1.6	1.5
Department of Health and Human Services	1.0	1.1
Department of Defense	0.9	1.1
Department of Agriculture	0.6	0.5
Department of the Treasury	0.6	0.6
Agency for International Development	0.4	0.4
Department of Transportation	0.4	0.5
Securities and Exchange Commission	0.3	0.4
Other operating leases	1.9	2.3
Total long-term operating leases	38.2	39.4

The government has entered into contractual commitments that require future use of financial resources. It has significant amounts of long-term lease obligations and undelivered orders. Undelivered orders represent the value of goods and services ordered that have not yet been received.

The government has other commitments that may require future use of financial resources. For example, the government has callable subscriptions in certain Multilateral Development Banks (MDBs), which are international financial institutions that finance economic and social development projects in middle-income developing countries. Callable capital in the MDBs serve as a supplemental pool of resources that may be redeemed and converted into ordinary paid in shares, if the MDB cannot otherwise meet certain obligations through its other available resources. MDBs are able to use callable capital as backing to obtain favorable financing terms when borrowing from international capital markets. To date, there has never been a call on this capital at any MDBs and none are anticipated.

Undelivered Orders and Other Commitments as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Undelivered Orders:		
Department of Defense	239.6	236.2
Defense Security Cooperation Agency	130.0	136.4
Department of Education	123.4	124.9
Department of Transportation	105.9	108.7
Department of Health and Human Services	96.1	98.9
Department of Agriculture	52.4	40.3
Department of Homeland Security	35.7	33.2
Department of Housing and Urban Development	35.1	38.1
Department of Energy	22.2	22.5
Department of State	21.6	21.0
Department of the Treasury	18.0	169.6
U.S. Agency for International Development	17.6	18.2
Department of Veterans Affairs	12.2	11.9
National Science Foundation	12.0	11.5
Federal Communications Commission	9.4	11.9
Department of the Interior	8.9	8.3
Department of Labor	8.4	9.2
All other agencies	22.7	24.0
Total undelivered orders	971.2	1,124.8
Other Commitments:		
GSE Senior Preferred Stock Purchase Agreement	258.1	258.1
U.S. Participation in the International Monetary Fund	155.1	-
Callable Capital Subscriptions for Multilateral Development Banks	120.0	112.3
Agriculture Direct Loans and Guarantees	4.9	5.0
Fuel Purchase Obligations	4.5	4.9
Power Purchase Obligations	2.8	4.3
Other Purchase Obligations	2.0	2.8
Long-term Satellite and Systems	0.9	2.3
All other commitments	1.6	15.1
Total other commitments	549.9	404.8

Other Commitments and Risks

Undelivered Orders

The Department of the Treasury reported undelivered orders of $18.0 billion and $169.6 billion as of September 30, 2016 and 2015, respectively. This decrease was primarily due to a change in budgetary accounting and reporting policy for transactions related to the United States' participation in International Monetary Fund (IMF). Effective October 1, 2015, in accordance with OMB guidance, Treasury changed its budgetary accounting and reporting policy for transactions related to the United States' participation in the IMF. Under this change in policy for transactions, other than related interest earnings and cost estimates for U.S. quota and New Arrangements to Borrow adjustments, are no longer reported as budgetary resources and used in Treasury's Combined Statement of Budgetary Resources. As a result of this change in budgetary accounting, Treasury adjusted the beginning balances of "Unobligated" and "Unpaid Obligations" on its Combined Statement of Budgetary Resources for fiscal year 2016 to remove those balances associated with IMF programs. This contributed to the significant decline in undelivered orders and the $155.1 billion increase in other commitments in fiscal year 2016.

Commitments to GSEs

At September 30, 2016 and 2015, the maximum remaining potential commitment to the GSEs for the remaining life of the SPSPAs was $258.1 billion, which was established on December 31, 2012. Refer to Note 8-Investments in Government-Sponsored Enterprises for a full description of the SPSPA agreements, related commitments, and contingent liability, if any, as well as additional information.

Terrorism Risk Insurance Program

Congress originally enacted the *Terrorism Risk Insurance Act* (TRIA) in November 2002 to address market disruptions resulting from terrorist attacks on September 11, 2001. Most recently, the *Terrorism Risk Insurance Program Reauthorization Act of 2015* extended the Terrorism Risk Insurance Program (TRIP) until December 31, 2020. The TRIP helps to ensure available and affordable commercial property and casualty insurance for terrorism risk, and simultaneously allows private markets to stabilize. The authority to pay claims under the TRIP Program is activated when the Secretary of the Treasury (in consultation with the Secretary of the U.S. Department of Homeland Security and the U.S. Attorney General) certifies an "act of terrorism." In the event of certification of an "act of terrorism" insurers may be eligible to receive reimbursement from the U.S. government for associated insured losses assuming an aggregate insured loss threshold ("program trigger") has been reached once a particular insurer has satisfied its designated deductible amount. For calendar years 2016 and 2015, the program trigger amount was $120 million and $100 million, respectively. This amount will increase by $20 million annually through calendar year 2020. Insured losses above insurer deductibles will be shared between insurance companies and the U.S. government. The TRIP includes both mandatory and discretionary authority for the Department of the Treasury to recoup federal payments made under the TRIP through policyholder surcharges under certain circumstances, and contains provisions designed to manage litigation arising from or relating to a certified act of terrorism. There were no claims under the TRIP as of September 30, 2016 or 2015.

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Note 20. Funds from Dedicated Collections

Funds from Dedicated Collections as of September 30, 2016[1]

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Federal Hospital Insurance Trust Fund (Medicare Part A)	Federal Disability Insurance Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Funds from Dedicated Collections	Total Funds from Dedicated Collections (Combined)
Assets:						
Cash and other monetary assets	-	-	-	-	63.2	63.2
Fund balance with Treasury	(0.1)	2.1	(0.1)	51.8	122.1	175.8
Investments in U.S. Treasury securities, net of unamortized premiums/discounts	2,796.7	192.2	45.9	63.3	277.3	3,375.4
Other federal assets	21.2	35.9	0.3	40.3	15.9	113.6
Non-federal assets	2.5	8.0	4.3	21.2	115.8	151.8
Total assets	2,820.3	238.2	50.4	176.6	594.3	3,879.8
Liabilities and net position:						
Due and payable to beneficiaries	69.2	27.7	28.5	36.2	10.8	172.4
Other federal liabilities	4.7	35.1	1.1	45.0	63.4	149.3
Other non-federal liabilities	-	1.3	-	0.9	181.6	183.8
Total liabilities	73.9	64.1	29.6	82.1	255.8	505.5
Total net position	2,746.4	174.1	20.8	94.5	338.5	3,374.3
Total liabilities and net position	2,820.3	238.2	50.4	176.6	594.3	3,879.8
Change in net position:						
Beginning net position	2,720.4	170.5	18.0	76.3	262.5	3,247.7
Prior-period adjustment	-	-	-	-	-	-
Beginning net position, adjusted	2,720.4	170.5	18.0	76.3	262.5	3,247.7
Investment revenue	88.1	7.9	1.4	2.0	3.4	102.8
Individual income taxes	679.6	250.5	147.6	-	-	1,077.7
Unemployment and excise taxes	-	-	-	-	105.2	105.2
Other taxes and receipts	-	0.8	-	2.9	39.2	42.9
Miscellaneous earned revenue	-	-	-	-	2.9	2.9
Other changes in fund balance (e.g., appropriations, transfers)	23.7	22.2	(1.9)	301.7	63.8	409.5
Total financing sources	791.4	281.4	147.1	306.6	214.5	1,741.0
Program gross costs and non-program expenses	765.4	281.4	144.3	365.7	187.5	1,744.3
Less: program revenue	-	(3.6)	-	(77.3)	(49.0)	(129.9)
Net cost	765.4	277.8	144.3	288.4	138.5	1,614.4
Ending net position	2,746.4	174.1	20.8	94.5	338.5	3,374.3

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Funds from Dedicated Collections as of September 30, 2015[1]

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Federal Hospital Insurance Trust Fund (Medicare Part A)	Federal Disability Insurance Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Funds from Dedicated Collections	Total Funds from Dedicated Collections (Combined)
Assets:						
Cash and other monetary assets	-	-	-	-	59.2	59.2
Fund balance with Treasury	(0.1)	1.4	-	43.4	123.6	168.3
Investments in U.S. Treasury securities, net of unamortized premiums/discounts	2,766.6	195.5	41.6	66.1	207.0	3,276.8
Other federal assets	22.3	35.5	0.5	51.8	19.2	129.3
Non-federal assets	2.3	1.3	4.4	5.9	106.9	120.8
Total assets	2,791.1	233.7	46.5	167.2	515.9	3,754.4
Liabilities and net position:						
Due and payable to beneficiaries	66.2	28.3	27.5	37.9	6.7	166.6
Other federal liabilities	4.5	34.3	1.0	52.4	67.6	159.8
Other non-federal liabilities	-	0.6	-	0.6	179.1	180.3
Total liabilities	70.7	63.2	28.5	90.9	253.4	506.7
Total net position	2,720.4	170.5	18.0	76.3	262.5	3,247.7
Total liabilities and net position	2,791.1	233.7	46.5	167.2	515.9	3,754.4
Change in net position:						
Beginning net position	2,670.6	179.8	47.7	57.2	242.3	3,197.6
Prior period adjustment	-	-	-	-	0.3	0.3
Beginning net position, adjusted	2,670.6	179.8	47.7	57.2	242.6	3,197.9
Investment revenue	92.2	8.4	2.4	2.4	3.0	108.4
Individual income taxes	672.2	237.7	114.2	-	-	1,024.1
Unemployment and excise taxes	-	-	-	-	106.6	106.6
Other taxes and receipts	-	0.6	-	3.0	33.7	37.3
Miscellaneous earned revenue	-	-	-	-	3.8	3.8
Other changes in fund balance (e.g., appropriations, transfers)	22.7	18.7	(2.0)	286.2	9.6	335.2
Total financing sources	787.1	265.4	114.6	291.6	156.7	1,615.4
Program gross cost and non-program expenses	737.3	278.4	144.3	344.5	198.7	1,703.2
Less: program revenue	-	(3.7)	-	(72.0)	(61.9)	(137.6)
Net cost	737.3	274.7	144.3	272.5	136.8	1,565.6
Ending net position	2,720.4	170.5	18.0	76.3	262.5	3,247.7

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Generally, funds from dedicated collections are financed by specifically identified revenues, often supplemented by other financing sources, provided to the government by non-federal sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes and must be accounted for separately from the government's general revenues. Funds from dedicated

collections generally include trust funds, public enterprise revolving funds (not including credit reform financing funds), and special funds. Funds from dedicated collections specifically exclude any fund established to account for pensions, other retirement benefits, other postemployment or other benefits provided for federal employees (civilian and military). In the federal budget, the term "trust fund" means only that the law requires a particular fund be accounted for separately, used only for a specified purpose, and designated as a trust fund. A change in law may change the future receipts and the terms under which the fund's resources are spent. In the private sector, trust fund refers to funds of one party held and managed by a second party (the trustee) in a fiduciary capacity. The activity of funds from dedicated collections differs from fiduciary activities primarily in that assets within funds from dedicated collections are government-owned. For further information related to fiduciary activities, see Note 21—Fiduciary Activities.

Public enterprise revolving funds include expenditure accounts authorized by law to be credited with offsetting collections, mostly from the public, that are generated by and dedicated to finance a continuing cycle of business-type operations. Some of the financing for these funds may be from appropriations.

Special funds are federal funds dedicated by law for a specific purpose. Special funds include the special fund receipt account and the special fund expenditure account.

The tables above depict major funds from dedicated collections chosen based on their significant financial activity and importance to taxpayers. All other government funds from dedicated collections not shown separately are aggregated as "all other."

Total assets represent the unexpended balance from all sources of receipts and amounts due to the funds from dedicated collections, regardless of source, including related governmental transactions. These are transactions between two different entities within the government (for example, monies received by one entity of the government from another entity of the government).

The intragovernmental assets are comprised of fund balances with Treasury, investments in Treasury securities—including unamortized amounts, and other assets that include the related accrued interest receivable on federal investments. These amounts were eliminated in preparing the principal financial statements. The non-federal assets represent only the activity with individuals and organizations outside of the government.

Most of the assets within funds from dedicated collections are invested in intragovernmental debt holdings. The government does not set aside assets to pay future benefits or other expenditures associated with funds from dedicated collections. The cash receipts collected from the public for funds from dedicated collections are deposited in the General Fund, which uses the cash for general government purposes. Treasury securities are issued to federal agencies as evidence of its receipts. Treasury securities are an asset to the federal agencies and a liability to the U.S. Treasury and, therefore, they do not represent an asset or a liability in the *Financial Report*. These securities require redemption if a fund's disbursements exceeds its receipts. Redeeming these securities will increase the government's financing needs and require more borrowing from the public (or less repayment of debt), or will result in higher taxes than otherwise would have been needed, or less spending on other programs than otherwise would have occurred, or some combination thereof. See Note 11—Federal Debt Securities Held by the Public and Accrued Interest for further information related to the investments in federal debt securities.

Depicted below is a description of the major funds from dedicated collections shown in the above tables, which also identifies the government agencies that administer each particular fund. For detailed information regarding these funds from dedicated collections, please refer to the financial statements of the corresponding administering agencies. For information on the benefits due and payable liability associated with certain funds from dedicated collections, see Note 14—Benefits Due and Payable.

Federal Old-Age and Survivors Insurance Trust Fund

The Federal Old-Age and Survivors Insurance Trust Fund, administered by the SSA, provides retirement and survivors benefits to qualified workers and their families.

Payroll and self-employment taxes primarily fund the Federal Old-Age and Survivors Insurance Trust Fund. Interest earnings on Treasury securities, federal agencies' payments for the Social Security benefits earned by military and federal civilian employees, and Treasury payments for a portion of income taxes collected on Social Security benefits provide the fund with additional income. The law establishing the Federal Old-Age and Survivors Insurance Trust Fund and authorizing the depositing of amounts to the credit of the fund is set forth in 42 U.S.C. § 401.

Federal Hospital Insurance Trust Fund (Medicare Part A)

The Federal Hospital Insurance Trust Fund, administered by HHS, finances the Hospital Insurance Program (Medicare Part A). This program funds the cost of inpatient hospital and related care for individuals age 65 or older who meet certain insured status requirements, and eligible disabled people.

The Federal Hospital Insurance Trust Fund is financed primarily by payroll taxes, including those paid by federal agencies. It also receives income from interest earnings on Treasury securities, a portion of income taxes collected on Social Security benefits, premiums paid by, or on behalf of, aged uninsured beneficiaries, and receipts from fraud and abuse control activities. Section 1817 of the *Social Security Act* established the Medicare Hospital Trust Fund.

Federal Disability Insurance Trust Fund

The Federal Disability Insurance Trust Fund provides assistance and protection against the loss of earnings due to a wage earner's disability in form of monetary payments. The SSA administers this fund.

Like the Federal Old-Age and Survivors Insurance Trust Fund, payroll taxes primarily fund the Federal Disability Insurance Trust Fund. The fund also receives income from interest earnings on Treasury securities, federal agencies' payments for the Social Security benefits earned by military and federal civilian employees, and Treasury payments for a portion of income taxes collected on Social Security benefits. The law establishing the Federal Disability Insurance Trust Fund and authorizing the depositing of amounts to the credit of the fund is set forth in 42 U.S.C. § 401.

Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)

The Federal Supplementary Medical Insurance Trust Fund, administered by HHS, finances the Supplementary Medical Insurance Program (Medicare Part B) and the Medicare Prescription Drug Benefit Program (Medicare Part D). These programs provide supplementary medical insurance for enrolled eligible participants to cover physician and outpatient services not covered by Medicare Part A and to obtain qualified prescription drug coverage, respectively. Medicare Part B financing is not based on payroll taxes; it is primarily based on monthly premiums, income from the General Fund, and interest earnings on Treasury securities. Medicare Supplementary Medical Insurance Trust Fund was established by Section 1841 of the *Social Security Act*.

Medicare Part D was created by the *Medicare Prescription Drug, Improvement, and Modernization Act of 2003* (Public Law No. 108-173). Medicare Part D financing is similar to Part B; it is primarily based on monthly premiums and income from the General Fund, not on payroll taxes. The fund also receives transfers from States. The law creating the Medicare prescription drug account within the Federal Supplementary Medical Insurance Trust Fund and authorizing the depositing of amounts to the credit of the fund is set forth in 42 U.S.C. § 1395w-116.

All Other Funds from Dedicated Collections

The government is responsible for the management of numerous funds from dedicated collections that serve a wide variety of purposes. The funds from dedicated collections presented on an individual basis in the above tables represent the majority of the government's net position attributable to funds from dedicated collections. All other activity attributable to funds from dedicated collections is aggregated in accordance with SFFAS No. 27, *Identifying and Reporting Funds from Dedicated Collections*, as amended by SFFAS No. 43, *Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds*. For the years ending September 30, 2016, and 2015, there were approximately 814 and 624 funds from dedicated collections, respectively. The methodology for reporting the number of funds changed in fiscal year 2016. Agencies now report the number of Treasury Account Symbols marked as Dedicated Collections, which is at a lower level of detail than the fiscal year 2015 reporting. The funds from dedicated collections within the "all other" aggregate, along with the agencies that administer them, include the following:

- Highway Trust Fund and Airport and Airway Trust Fund—administered by DOT.
- Land and Water Conservation Fund, Reclamation Fund, and Water and Related Resources Fund—administered by DOI.
- Exchange Stabilization Fund—administered by Treasury.
- Unemployment Trust Fund (UTF) and Black Lung Disability Trust Fund (BLDTF)—administered by DOL.
- National Flood Insurance Program—administered by DHS.
- Railroad Retirement Trust Fund—administered by RRB.
- Government National Mortgage Association—administered by HUD.
- Decommissioning and Decontamination Fund—administered by DOE.
- Crime Victims Fund—administered by DOJ.
- Harbor Maintenance Trust Fund—administered by DOD.

In accordance with SFFAS No. 43, any funds established to account for pension, other retirement, or other post-employment benefits to civilian or military personnel are excluded from the reporting requirements related to funds from dedicated collections.

Other changes in fund balance line increased from $9.6 billion in fiscal year 2015 to $63.8 billion in fiscal year 2016. On December 4, 2015, the President signed into law the *Fixing America's Surface Transportation Act*, or "*FAST Act*" (P.L.114-94), providing funding for surface transportation through September 30, 2020. An additional $70 billion was transferred to the Highway Trust Fund from the General Fund.

The Commodity Future Trading Commission erroneously did not report as a fund from dedicated collections for fiscal year 2014. This error was corrected in fiscal year 2015 and resulted in a prior-period adjustment of $0.3 billion.

Unemployment and Excise Taxes

Unemployment Taxes

The Unemployment Trust Fund (UTF), within the "all other" aggregate, represents all the unemployment tax revenues attributable to funds from dedicated collections shown on the consolidated Statement of Operations and Changes in Net Position.

UTF provides temporary assistance to workers who lose their jobs. The program is administered through a unique system of federal and state partnerships, established in federal law, but executed through conforming state laws by state officials. DOL administers the federal operations of the program.

Employer taxes provide the primary funding source for the UTF and constitute the largest portion of unemployment tax revenues attributable to funds from dedicated collections as shown on the consolidated Statement of Operations and Changes in Net Position. However, interest earnings on Treasury securities also provide income to the fund. For the years ending September 30, 2016, and 2015, UTF unemployment tax revenues were $46.9 billion and $49.1 billion, respectively. Appropriations have supplemented the fund's income during periods of high and extended unemployment. UTF was established under the authority of Section 904 of the *Social Security Act of 1935*.

Excise Taxes

There are 10 funds from dedicated collections within the "all other" aggregate that represent all of the dedicated excise tax revenue attributable to funds from dedicated collections shown on the consolidated Statement of Operations and Changes in Net Position. The Highway Trust Fund and the Airport and Airway Trust Fund, combined, represent more than 95 percent of all dedicated excise tax revenues. Both of these funds are administered by the DOT. For more information, please refer to DOT's financial statements.

The Highway Trust Fund was established to promote domestic interstate transportation and to move people and goods. The fund provides federal grants to states for highway construction, certain transit programs, and related transportation purposes. The Highway Trust Fund was created by the *Highway Revenue Act of 1956*. Funding sources include designated excise taxes on gasoline and other fuels, the initial sale of heavy trucks, and highway use by commercial motor vehicles. For the years ending September 30, 2016, and 2015, Highway Trust Fund excise tax revenues were $41.3 billion and $40.8 billion, respectively. As funds are needed for payments, the Highway Trust Fund corpus investments are liquidated and funds are transferred to the Federal Highway Administration, the Federal Transit Administration, or other DOT entities, for payment of obligations.

The Airport and Airway Trust Fund provides for airport improvement and airport facilities maintenance. It also funds airport equipment, research, and a portion of the Federal Aviation Administration's administrative operational support. The

Airport and Airway Trust Fund was authorized by the *Airport and Airway Revenue Act of 1970*. Funding sources include aviation-related excise tax collections from:

- Passenger tickets,
- Passenger fight segments,
- International arrival/departures,
- Cargo waybills, and
- Aviation fuels.

For the years ending September 30, 2016, and 2015, Airport and Airway Trust Fund excise tax revenues were $14.4 billion and $14.3 billion, respectively.

Miscellaneous Earned Revenues

Miscellaneous earned revenues due to activity attributable to funds from dedicated collections primarily relate to royalties retained by various funds within DOI.

Note 21. Fiduciary Activities

Fiduciary activities are the collection or receipt, and the management, protection, accounting, investment and disposition by the Government of cash or other assets in which non-federal individuals or entities have an ownership interest that the Government must uphold. Fiduciary cash and other assets are not assets of the Government and are not recognized on the consolidated Balance Sheet. Examples of the Government's fiduciary activities include the Thrift Savings Plan (TSP), which is administered by the Federal Retirement Thrift Investment Board (FRTIB), and the Indian Tribal and individual Indian Trust Funds, which are administered by the DOI. This note also addresses guarantor activities.

Schedule of Fiduciary Net Assets as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Thrift Savings Fund	472.1	427.3
Department of the Interior	5.1	5.1
All other	5.3	2.8
Total fiduciary net assets	482.5	435.2

In accordance with the requirements of SFFAS No. 31, *Accounting for Fiduciary Activities*, fiduciary investments in Treasury securities and fund balance with Treasury held by fiduciary funds are to be recognized on the Balance Sheet as debt held by the public and a liability for fiduciary fund balance with Treasury, respectively.

As of September 30, 2016, total fiduciary investments in Treasury securities and in non-Treasury securities are $226.2 billion and $268.9 billion, respectively. As of September 30, 2015, total fiduciary investments in Treasury securities and in non-Treasury securities were $4.9 billion and $243.1 billion, respectively. This increase relates to the delay in raising the statutory debt limit that was ongoing as of September 30, 2015. See the Thrift Savings Fund section below. Refer to Note 11—Federal Debt Securities Held by the Public and Accrued Interest for more information on the Treasury securities.

As of September 30, 2016, and 2015, the total fiduciary fund balance with Treasury is $1.1 billion and $1.2 billion, respectively. A liability for this fiduciary fund balance with Treasury is reflected as other miscellaneous liabilities in Note 16—Other Liabilities.

As of September 30, 2016, and 2015, collectively, the fiduciary investments in Treasury securities and fiduciary fund balance with Treasury held by all Government entities represent $6.4 billion and $210.6 billion, respectively, of unrestricted cash included within cash held by Treasury for Governmentwide Operations shown in Note 2—Cash and Other Monetary Assets. This decrease relates to the delay in raising the statutory debt limit that was ongoing as of September 30, 2015. See the Thrift Savings Fund section below.

Thrift Savings Fund

The Thrift Savings Fund (TSF) maintains and holds in trust the assets of the TSP. The TSP is administered by an independent Government agency, the Federal Retirement Thrift Investment Board, which is charged with operating the TSP prudently and solely in the interest of the participants and their beneficiaries.

The TSP is a retirement savings and investment plan for federal employees and members of the uniformed services. It was authorized by the United States Congress in the *Federal Employees' Retirement System Act of 1986*. The Plan provides federal employees and members of the uniformed services with a savings and tax benefit similar to what many private sector employers offer their employees under 401(k) plans. The Plan was primarily designed to be a key part of the retirement package (along with a basic annuity benefit and Social Security) for employees who are covered by FERS.

Federal employees, who are participants of FERS, the CSRS, or equivalent retirement systems, as provided by statute, and members of the uniformed services, are eligible to join the Plan immediately upon being hired. Generally, FERS employees are those employees hired on or after January 1, 1984, while CSRS employees are employees hired before January 1, 1984, who have not elected to convert to FERS. Each group has different rules that govern contribution rates. As of December 31, 2015, and 2014, there were approximately 4.8 million and 4.8 million participants in the TSP, respectively,

with approximately 3.3 and 2.9 million contributing their own money, respectively. For further information about FRTIB and the TSP, please refer to the FRTIB website at http://www.frtib.gov.

As of September 30, 2016, and 2015, the TSF held $472.1 billion and $427.3 billion, respectively, in net assets, which included $220.9 billion and $0.0 billion, respectively, of U.S. Government Securities (amounts are unaudited). When delays in raising or suspending the debt limit occur, as they did during both fiscal years 2015 and 2016, Treasury implements "extraordinary actions" on a temporary basis. Many of the extraordinary actions taken by Treasury during the period of March 16, 2015 through October 30, 2015, resulted in federal debt securities not being issued to certain federal government accounts. As a result of Treasury securities not being issued to the G Fund as of September 30, 2015, Treasury reported miscellaneous liabilities in the amount of $204.6 billion that represent uninvested principal of and related interest for the G Fund that would have been reported as Federal Debt Securities Held by the Public and Accrued Interest had there not been a delay in raising the statutory debt limit as of September 30, 2015, and had the Treasury securities been issued. On Monday, November 2, 2015, the *Bipartisan Budget Act of 2015* (Public Law 114-74) was enacted suspending the statutory debt limit through March 15, 2017. Treasury subsequently restored the uninvested principal and related interest to the G Fund, resulting in an increase of U.S. Government Securities from 2015 to 2016. The most recent audited financial statements for the TSF are as of December 31, 2015, and 2014. As of December 31, 2015, and 2014, the TSF held $443.2 billion and $428.1 billion, respectively, in net assets, which included $206.9 billion and $191.3 billion, respectively, of U.S. Government Securities. These unaudited amounts above are included to enhance comparability of the TSF net assets with the remainder of the Government's fiduciary net assets as of September 30, 2016, and 2015.

DOI–Indian Trust Funds

As stated above, DOI has responsibility for the assets held in trust on behalf of American Indian Tribes and individuals, and these account for all of DOI's fiduciary net assets. DOI maintains accounts for Tribal and Other Trust Funds (including the Alaska Native Escrow Fund and Individual Indian Money Trust Funds) in accordance with the *American Indian Trust Fund Management Reform Act of 1994*. The fiduciary balances that have accumulated in these funds have resulted from land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, judgment awards, settlements of claims, and investment income. These funds are maintained for the benefit of individual Native Americans as well as for designated Indian tribes. DOI maintains separate financial statements for these trust funds which were prepared using the cash or modified cash basis of accounting, a comprehensive basis of accounting other than GAAP. The independent auditors' reports were qualified as it was not practical to extend audit procedures sufficiently to satisfy themselves as to the fairness of the trust fund balances. For further information related to these assets, please refer to the DOI website at http://www.doi.gov.

All Other Entities with Fiduciary Activities

The Government is responsible for the management of other fiduciary net assets on behalf of various non-federal entities. The component entities presented individually in the table on the previous page represent the vast majority of the Government's fiduciary net assets. All other component entities with fiduciary net assets are aggregated in accordance with SFFAS No. 31. As of September 30, 2016, and 2015, including TSF and DOI, there are a total of 20 and 17 federal entities, respectively, with fiduciary activities at a grand total of 68 and 65 fiduciary funds, respectively. SBA and LOC are the significant agencies relating to the fiduciary activities of the remaining component entities within the "all other" aggregate balance. As of September 30, 2016, "all other" fiduciary net assets were $5.3 billion, compared to $2.8 billion as of September 30, 2015.

Guarantor Activities

PBGC is a federal corporation established under ERISA of 1974, as amended. It guarantees payment of basic pension benefits earned by nearly 40 million of America's workers and retirees participating in nearly 24,000 private-sector defined benefit pension plans. The Corporation receives no funds from general tax revenues and its liabilities are not backed by the "full faith and credit" of the federal government. In other words, ERISA requires that PBGC programs be self-financing and provides that the U.S. Government is not liable for any obligation or liability incurred by PBGC. Operations are financed by

insurance premiums set by Congress and paid by sponsors of defined benefit plans, assets from pension plans trusteed by PBGC, investment income, and recoveries from the companies formerly responsible for the plans.

When an underfunded single-employer plan terminates, PBGC in its role as guarantor steps in to provide guaranteed benefits. This typically happens when the employer sponsoring an underfunded plan goes bankrupt or out of business, and can no longer afford to keep the plan going. In this type of termination, PBGC as trustee takes over the plan's assets which are commingled and placed in PBGC's trust fund. At the time of trusteeship, PBGC assumes responsibility for administration and payment of plan benefits.

Per Title IV of ERISA, PBGC is directed in its role as guarantor (and not as a fiduciary) to provide guaranteed benefits to the extent allowed within statutory limits. Under PBGC's proportional funding policy, the trust fund portion of benefit payments is determined by the ratio of trust fund assets to the value of PBGC's liability for future benefits. The remaining portion is assigned to the revolving fund. The trust fund's net liabilities as of September 30, 2016 and 2015 were $49.0 billion and $51.2 billion, respectively.

The trust fund includes assets (e.g., pension plan investments) PBGC assumes (or expects to assume) once a terminated plan has been trusteed, and related investment income. These assets (i.e. private monies for the benefit of terminated plans) generally are held by custodian banks and are prudently invested to help fund the payment of future participant benefits. The revolving funds include insurance premiums collected, related investment income and administrative expenses.

Note 22. Social Insurance

The Statement of Social Insurance (SOSI) presents the projected actuarial present value of the estimated future revenue and estimated future expenditures of the Social Security, Medicare, Railroad Retirement, and Black Lung social insurance programs which are administered by the SSA, HHS, RRB, and DOL, respectively. These estimates are based on the intermediate economic and demographic assumptions presented later in this note as set forth in the relevant Social Security and Medicare trustees' reports and in the agency financial reports of HHS, SSA, and DOL, as well as in the relevant agency performance and accountability report for RRB. Due to a change in the presentation of the consolidated SOSI from billions of dollars to trillions of dollars for fiscal year 2016, and in the accompanying note to social insurance, some amounts in the narrative will not be traceable to the corresponding agency financial statements. The projections in this year's report, with one exception related to Medicare Part A, are based on current law; that is, they assume that laws on the books will be implemented and adhered to with respect to scheduled taxes, premium revenues, and payments to providers and health plans. The one exception is that the projections disregard payment reductions that would result from the projected depletion of the Medicare Hospital Insurance (Part A) Trust Fund. Under current law, payments would be reduced to levels that could be covered by incoming tax and premium revenues when the Medicare Hospital Insurance (Part A) Trust Fund is depleted. The estimates in the consolidated SOSI of the open group measures are for persons who are participants or eventually will participate in the programs as contributors (workers) or beneficiaries (retired workers, survivors, and disabled) during the 75-year projection period. Beginning with this year's projections, the Part A present values in the SOSI include the income and expenditures for the roughly 1 percent of beneficiaries who are 65 or over but are uninsured because they do not meet the normal insured status or related requirements to qualify for entitlement to Part A benefits. The reason that these beneficiaries were previously excluded is that their costs were separately funded either through general revenue appropriations or through premium payments, and accordingly the exclusion of such amounts did not materially affect the financial balance of Part A. The Black Lung projection period ends September 30, 2040, the date when the BLDTF's last debt instrument matures. The projection period illustrates the future long-term condition and sustainability of the fund because it presents the value for the open group measure plus fund assets (funds with U.S. Treasury and receivables from benefits overpayments) available to service the BLDTF debt and interest until the last debt instrument matures.

Contributions and dedicated taxes consist of: payroll taxes from employers, employees, and self-employed persons; revenue from federal income taxation of Old-Age Survivors and Disability Insurance (OASDI) and railroad retirement benefits; excise tax on the domestic sale of coal (Black Lung); premiums from, and state transfers on behalf of, participants in Medicare; and reimbursements from the General Fund to the OASDI Trust Funds to make up for reductions in payroll tax revenue due to temporary payroll tax rate reductions. Income for all programs is presented from a consolidated perspective. Future interest payments and other future intragovernmental transfers have been excluded upon consolidation. Expenditures include scheduled benefit payments and administrative expenses. Scheduled benefits are projected based on the benefit formulas under current law, with an exception in regard to payment reductions that would result from the projected depletion of the Social Security and Medicare Hospital Insurance (Part A) Trust Funds. Current Social Security and Medicare law also provides for full benefit payments only to the extent that there are sufficient balances in the trust funds. Expenditures reflect full benefit payments even after the point at which assets are projected to be depleted.

Actuarial present values of estimated future income (excluding interest) and estimated future expenditures for the Social Security, Medicare, and Railroad Retirement social insurance programs are presented for three different groups of participants: (1) current participants who have not yet attained eligibility age; (2) current participants who have attained eligibility age; and (3) new entrants, who are expected to become participants in the future. Current participants in the Social Security and Medicare programs are the "closed group" of taxpayers and/or beneficiaries who are at least age 15 years at the start of the projection period. Since the projection period for the Social Security, Medicare, and Railroad Retirement social insurance programs consists of 75 years, the period covers virtually all of the current participants' working and retirement years, a period that could be greater than 75 years in a relatively small number of instances. Future participants for Social Security and Medicare include births during the projection period and individuals below age 15 as of January 1 of the valuation year. Railroad Retirement's future participants are the projected new entrants as of October 1 of the valuation year. For fiscal year 2015 and years prior, future participants for Railroad Retirement were the projected new entrants as of January 1 of the valuation year[6].

The present values of estimated future expenditures in excess of estimated future revenue are calculated by subtracting the actuarial present values of future scheduled contributions as well as dedicated tax income by and on behalf of current and

[6] Beginning with the fiscal year 2016 reporting period, the valuation date for the Railroad Retirement program has been changed from calendar year to fiscal year.

future participants from the actuarial present value of the future scheduled benefit payments to them or on their behalf. To determine a program's funding shortfall over any given period of time, the starting trust fund balance is subtracted from the present value of expenditures in excess of revenues over the period.

The trust fund balances as of the valuation date for the respective programs, including interest earned, are shown in the table below[7]. Substantially all of the Social Security (OASDI), Medicare Hospital Insurance (HI), and Supplementary Medical Insurance (SMI) Trust Fund balances consist of investments in special nonmarketable U.S. Treasury securities that are backed by the full faith and credit of the U.S. Government.

Social Insurance Programs Trust Fund Balances [1]

(In trillions of dollars)	2016	2015	2014	2013	2012
Social Security	2.8	2.8	2.8	2.7	2.7
Medicare	0.3	0.3	0.3	0.3	0.3

[1] As of the valuation date of the respective programs.

Social Security

The Federal Old-Age and Survivors Insurance (OASI) program, created in 1935, and the Federal Disability Insurance (DI) program, created in 1956, collectively referred to as OASDI or "Social Security," provides cash benefits for eligible U.S. citizens and residents. Eligibility and benefit amounts are determined under the laws applicable for the period. Current law provides that the amount of the monthly benefit payments for workers, or their eligible dependents or survivors, is based on the workers' lifetime earnings histories.

The primary financing of the OASDI Trust Funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Refer to the Unaudited Required Supplementary Information—Social Insurance section for additional information on Social Security program financing.

That portion of each trust fund not required to pay benefits and administrative costs is invested, on a daily basis, in interest-bearing obligations of the U.S. Government. The *Social Security Act* authorizes the issuance by the Treasury of special nonmarketable, intragovernmental debt obligations for purchase exclusively by the trust funds. Although the special issues cannot be bought or sold in the open market, they are redeemable at any time at face value and thus bear no risk of fluctuation in principal value due to changes in market yield rates. Interest on the bonds is credited to the trust funds and becomes an asset to the funds and a liability to the General Fund. These Treasury securities and related interest are eliminated in consolidation at the governmentwide level.

Medicare

The Medicare Program, created in 1965, has two separate trust funds: the HI (Medicare Part A) and SMI (Medicare Parts B and D) Trust Funds. HI pays for inpatient acute hospital services, hospice, and major alternatives to hospitals (skilled nursing services, for example), and SMI pays for hospital outpatient services, physician services, and assorted other services and products through the Part B account and pays for prescription drugs through the Part D account. Though the events that trigger benefit payments are similar, HI and SMI have different dedicated financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Other income to the HI Trust Fund includes a small amount of premium income from voluntary enrollees, receipts from fraud and abuse control activities, a portion of the federal income taxes that beneficiaries pay on Social Security benefits and interest credited on Treasury securities held in the HI Trust Fund. These Treasury securities and related interest are eliminated in the consolidation at the governmentwide level.

For SMI, transfers from the General Fund represent the largest source of income for both Parts B and D. Generally, beneficiaries finance the remainder of Parts B and D costs via monthly premiums to these programs. With the introduction of Part D drug coverage, Medicaid is no longer the primary payer for beneficiaries dually eligible for Medicare and Medicaid. For those beneficiaries, states must pay a portion of their estimated foregone drug costs into the Part D account (referred to as state transfers). Fees related to brand-name prescription drugs, required by the *Affordable Care Act* (ACA), are included as income for Part B of SMI. As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund and these Treasury securities as well as related interest are eliminated in consolidation at the governmentwide level. By

[7] Trust fund balances for the Railroad Retirement and Black Lung programs are not included, as these balances are less than $50 billion.

accounting convention, the transfers of general revenues are eliminated in the consolidation of the SOSI at the governmentwide level and as such, the general revenues that are used to finance Medicare Parts B and D are not included in these calculations even though the expenditures on these programs are included. For the fiscal year 2016 and 2015 SOSI, the amounts eliminated totaled $28.7 trillion and $24.8 trillion, respectively. Refer to Unaudited Required Supplementary Information—Social Insurance section for additional information on Medicare program financing.

The *Medicare Prescription Drug, Improvement, and Modernization Act* (MMA), enacted on December 8, 2003, created the Part D account in the SMI Trust Fund to account for the prescription drug benefit that began in 2006. The MMA established within SMI two Part D accounts related to prescription drug benefits: the Medicare Prescription Drug Account and the Transitional Assistance Account. The Medicare Prescription Drug Account was used in conjunction with the broad, voluntary prescription drug benefits that commenced in 2006. The Transitional Assistance Account was used to provide transitional assistance benefits, beginning in 2004 and extending through 2005, for certain low-income beneficiaries prior to the start of the new prescription drug benefit.

Affordable Care Act (ACA) and Medicare Access and CHIP Reauthorization Act (MACRA)

In fiscal year 2010, President Barack Obama signed health insurance reform legislation giving Americans more control over their health care. The *Patient Protection and Affordable Care Act* and the *Health Care and Education Reconciliation Act* collectively referred to as the *Affordable Care Act* ensures that all Americans have access to quality, affordable health care, while helping to reduce health care costs.

The *Affordable Care Act* contains the most significant changes to health care coverage since passage of the *Social Security Act*. The *Affordable Care Act* provided funding for the establishment by CMS of a Center for Medicare and Medicaid Innovation to test innovative payment and service delivery models to reduce program expenditures while preserving or enhancing the quality of care furnished to individuals. It also allowed for the establishment of a Center for Consumer Information and Insurance Oversight (CCIIO). The programs under CCIIO include Health Insurance Marketplaces (the "Marketplace") and the Consumer Operated and Oriented Plan Program (CO-OP). A brief description of these programs and their impact on the financial statement is presented below.

Grants have been provided to the states to establish Health Insurance Marketplaces. The initial grants were made by the HHS to the states "not later than one year after the date of enactment." Thus, HHS made the initial grants by March 23, 2011. Subsequent grants were issued by CMS through December 31, 2014, after which time no further grants could be made. All Marketplaces were launched on October 1, 2013.

To help make health insurance more affordable to consumers, HHS makes advance payments of the premium tax credits (APTC) and cost-sharing reductions (CSR) to health insurance issuers on behalf of consumers who are eligible for financial assistance. States may also opt to cover some Marketplace-eligible individuals through the Basic Health Program (BHP), and a state that operates a BHP receives federal funding equal to 95 percent of the amount of the premium tax credits and CSRs that would have otherwise been provided to (or on behalf of) eligible individuals if those individuals enrolled in Qualified Health Plans through the Marketplace. APTC, CSR, and BHP payments (which are included in the IRS financial statements) are a critical component of the Marketplace, and $42.0 billion has been allocated for these payments. In addition to these payments on behalf of consumers, HHS collects Marketplace user fees from issuers participating in the Federally-Facilitated Marketplace (FFM).

The CO-OP Program fosters qualified non-profit health insurance issuers created to offer qualified health plans to the individual and small group markets. Under this program, HHS provides assistance to organizations applying to become qualified non-profit health insurance issuers through loans to assist in meeting start-up costs and to assist the applicant meet state solvency requirements. In accordance with regulations as well as legislative requirements, start-up loans shall be repaid within five years and the solvency loans within 15 years after disbursement, considering state reserve requirements and solvency regulations.

The Transitional Reinsurance Program was established in each state to help stabilize premiums for coverage in the individual market from 2014 through 2016. All health insurance issuers and third party administrators, on behalf of self-insured group health plans, must make contributions to support reinsurance payments that cover high-cost individuals in non-grandfathered plans in the individual market, inside and outside the Marketplace. The Transitional Reinsurance Program is a critical element in helping to ensure a stabilized individual market in the initial years of the implementation of the *Affordable Care Act's* insurance market reforms.

The Risk Adjustment Program is a permanent program. It applies to non-grandfathered individuals and small group plans inside and outside the Marketplaces. It provides payments to health insurance issuers that disproportionately attract higher-risk populations (such as individuals with chronic conditions) and transfers funds from plans with relatively lower risk enrollees to plans with relatively higher risk enrollees to protect against adverse selection. States may operate risk adjustment

programs and CMS will operate a risk adjustment program for each state that does not operate its own. In 2015 and 2016, Massachusetts is the only state that operated its own risk adjustment program.

The temporary Risk Corridors Program will operate during the years 2014 through 2016. This program applies to qualified health plans in the individual and small group markets, inside and outside the Marketplaces and protects against inaccurate rate-setting by sharing risk (gains and losses) on allowable costs between CMS and qualified health plans to help ensure stable health insurance premiums.

The financial projections for the Medicare program reflect substantial, but very uncertain, cost savings deriving from provisions of the ACA and MACRA that lower increases in Medicare payment rates to most categories of health care providers. However, it is important to note that the improved results for HI and SMI Part B since 2010 depend in part on the long-range feasibility of the various cost-saving measures in the ACA–most importantly, the reductions in the annual payment rate updates for most categories of Medicare providers by the growth in economy-wide private nonfarm business multifactor productivity and the specified physician updates put in place by MACRA. Under the ACA, the rate of increase of Medicare payment rates is equal to the prior law rate of increase (equal to the rate of increase in the prices of inputs used to produce Medicare services) less the rate of increase of total economy multifactor productivity. Without fundamental changes in the current delivery system, these productivity-related adjustments to Medicare payment rates would probably not be viable indefinitely. However, this outcome is achievable if health care providers are able to realize productivity improvements at a faster rate than experienced historically. On the other hand, if the health sector cannot transition to more efficient models of care delivery and achieve productivity increases commensurate with economy-wide productivity, and if the provider reimbursement rates paid by commercial insurers continue to follow the same negotiated process used to date, then the availability and quality of health care received by Medicare beneficiaries would, under current law, fall over time relative to that received by those with private health insurance.

A transformation of health care in the United States, affecting both the means of delivery and the method of paying for care, is also a possibility. The ACA takes important steps in this direction by initiating programs of research into innovative payment and service delivery models, such as accountable care organizations, patient-centered medical homes, improvement in care coordination for individuals with multiple chronic health conditions, improvement in coordination of post-acute care, payment bundling, pay for performance, and assistance for individuals in making informed health choices. Such changes have the potential to reduce health care costs as well as cost growth rates and could, as a result, help lower Medicare cost growth rates to levels compatible with the lower price updates payable under current law.

The ability of new delivery and payment methods to significantly lower cost growth rates is uncertain at this time, since specific changes have not yet been designed, tested, or evaluated. Preliminary indications are that some of these delivery reforms have had modest levels of success in lowering costs, but at this time it is too early to tell if these reductions in spending will continue, or if they will grow to the magnitude needed to align with the statutory Medicare price updates. The ability of health care providers to sustain the price reductions for those providers impacted by the productivity adjustments and the specified updates to physician payments will be challenging, as the best available evidence indicates that most providers cannot improve their productivity to this degree for a prolonged period given the labor-intensive nature of these services and that physician costs will grow at a faster rate than the specified updates. As a result, actual Medicare expenditures are highly uncertain for reasons apart from the inherent difficulty in projecting health care cost growth over time.

The SOSI projections are based on current law, with one exception in regard to payment reductions that would result from the projected depletion of the Medicare Hospital Insurance (Part A) Trust Fund; under current law, payments would be reduced to levels that could be covered by incoming tax and premium revenues when the Medicare Hospital Insurance (Part A) Trust Funds are depleted.

The extent to which actual future Part A and Part B costs exceed the projected amounts due to changes to the productivity adjustments and specified physician updates depends on what specific changes might be legislated and whether Congress would pass further provisions to help offset such costs. However, absent an unprecedented change in health care delivery systems and payment mechanisms, the prices paid by Medicare for health services will fall increasingly short of the cost of providing such services. If this issue is not addressed by subsequent legislation, it is likely that access to, and quality of, physicians' services would deteriorate over time for beneficiaries. The specified rate updates could be an issue in years when levels of inflation are high and would be problematic when the cumulative gap between the price updates and physician costs becomes large. The gap will continue to widen throughout the projection, and it is anticipated that physician payment rates under current law will be lower than they would have been under the sustainable growth rate (SGR) formula by 2048 and will be about 30 percent lower by 2090. Absent a change in the delivery system or level of update by subsequent legislation, access to Medicare-participating physicians is expected to become a significant issue in the long term under current law. Overriding the productivity adjustments and specified physician updates, as lawmakers repeatedly did in the case of physician payment rates under the SGR formula, would lead to substantially higher costs for Medicare in the long range than those projected in this report.

To help illustrate and quantify the potential magnitude of the cost understatement, the Trustees asked the Office of the Actuary at CMS to prepare an illustrative Medicare Trust Fund projection under a hypothetical alternative that assumes that, starting in 2020, the economy-wide productivity adjustments gradually phase down to 0.4 percent, and starting in 2025, physician payments transition from a payment update of 0.0 percent to an increase of 2.2 percent. In addition, the illustrative alternative assumes that the 5 percent bonuses paid to physicians in alternative payment models (APMs) would continue and that the Independent Payment Advisory Board (IPAB) requirements would not be implemented.[8] This alternative was developed for illustrative purposes only; the calculations have not been audited; no endorsement of the policies underlying the illustrative alternative by the Trustees, CMS, or the Office of the Actuary should be inferred; and the examples do not attempt to portray likely or recommended future outcomes. Thus, the illustrations are useful only as general indicators of the substantial impacts that could result from future legislation affecting the productivity adjustments and physician updates under Medicare and of the broad range of uncertainty associated with such impacts. The table below contains a comparison of the Medicare 75-year present values of estimated future income and estimated future expenditures under current law with those under the illustrative alternative scenario.

[8] The illustrative alternative projections included changes to the productivity adjustments starting with the 2010 annual report, following enactment of the *Affordable Care Act*. The assumption regarding physician payments is being used because the SGR was replaced in 2015.

Medicare Present Values (in trillions) (Unaudited)

	2016 Consolidated SOSI Current Law	Illustrative Alternative Scenario [1, 2]
Income:		
Part A	$20.7	$20.9
Part B [3]	$7.5	$9.4
Part D [4]	$3.5	$3.6
Total income	$31.7	$33.9
Expenditures:		
Part A	$24.5	$30.6
Part B	$27.5	$34.5
Part D	$12.2	$12.4
Total expenditures	$64.2	$77.5
Income less expenditures:		
Part A	$3.8	$9.7
Part B	$20.0	$25.0
Part D	$8.7	$8.8
Excess of expenditures over income	$32.5	$43.5

[1] These amounts are not presented in the 2016 Trustees' Report.

[2] At the request of the Trustees, the Office of the Actuary at CMS has prepared an illustrative set of Medicare Trust Fund projections that differ from current law. No endorsement of the illustrative alternative to current law by the Trustees, CMS, or the Office of the Actuary should be inferred.

[3] Excludes $20.0 trillion and $25.0 trillion of General Revenue Contributions from the 2016 Consolidated SOSI Current Law projection and the Illustrative Alternative Scenario's projection, respectively; i.e., to reflect Part B income on a consolidated governmentwide basis.

[4] Excludes $8.7 trillion and $8.8 trillion of General Revenue Contributions from the 2016 Consolidated SOSI Current Law projection and the Illustrative Alternative Scenario's projection, respectively; i.e., to reflect Part D income on a consolidated governmentwide basis.

Note: Totals may not equal the sum of components due to rounding.

The difference between the current-law and illustrative alternative projections is substantial for Parts A and B. All Part A fee-for-service providers and roughly half of Part B fee-for-service providers are affected by the productivity adjustments, so the current-law projections reflect an estimated 1.1 percent reduction in annual cost growth each year for these providers. If the productivity adjustments were gradually phased out, the physician updates transitioned to the Medicare Economic Index update of 2.2 percent, the 5 percent bonuses paid to physicians in APMs did not expire, and the IPAB requirements were not implemented, as illustrated under the alternative scenario, the estimated present values of Part A and Part B expenditures would each be higher than the current-law projections by roughly 25 percent. As indicated above, the present value of Part A income is basically unaffected under the alternative scenario.

The Part D values are similar under each projection because the services are not affected by the productivity adjustments or the physician updates. The very minor effect is the result of the removal of the IPAB impact and a slight change in the discount rates that are used to calculate the present values.

The extent to which actual future Part A and Part B costs exceed the projected amounts due to changes to the productivity adjustments and physician updates depends on what specific changes might be legislated and whether Congress would pass further provisions to help offset such costs. As noted, these examples reflect only hypothetical changes to provider payment rates.

Social Security and Medicare–Demographic and Economic Assumptions

The Boards of Trustees[9] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. Assumptions are made about many economic and demographic factors, including Gross Domestic Product (GDP)[10], disability incidence and terminations, earnings, the Consumer Price Index (CPI), the unemployment rate, the fertility rate, immigration, mortality, and for the Medicare projections health care cost growth. The assumptions used for the most recent set of projections shown in Table 1A (Social Security) and Table 1B (Medicare) are generally referred to as the "intermediate assumptions," and reflect the trustees' reasonable estimate of expected future experience. For further information on Social Security and Medicare demographic and economic assumptions, refer to SSA's and HHS' Agency Financial Reports.

[9] There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor, the Commissioner of the Social Security Administration, and two public trustees who are generally appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees are members of two different political parties.

[10] In July 2013, the Bureau of Economic Analysis (BEA) revised upward the historical values for GDP beginning with estimates for 1929.

Table 1A
Social Security – Demographic and Economic Assumptions

	Demographic Assumptions				
				Period Life Expectancy at Birth[4]	
Year	Total Fertility Rate[1]	Age-Sex Adjusted Death Rate (per 100,000)[2]	Net Annual Immigration (persons per year)[3]	Male	Female
2016	1.90	773.0	1,579,000	77.0	81.6
2020	2.00	742.8	1,508,000	77.5	82.0
2030	2.00	679.1	1,332,000	78.8	83.0
2040	2.00	624.5	1,284,000	79.8	83.9
2050	2.00	576.8	1,259,000	80.9	84.7
2060	2.00	534.8	1,244,000	81.8	85.5
2070	2.00	497.6	1,235,000	82.7	86.2
2080	2.00	464.6	1,230,000	83.5	86.9
2090	2.00	435.1	1,228,000	84.2	87.5

	Economic Assumptions					
Year	Real Wage Differ-ential (percent)[5]	Average Annual Wage In Covered Employment (percent change)[6]	CPI (percent change)[7]	Real GDP (percent change)[8]	Total Employ-ment (percent change)[9]	Average Annual Interest Rate (percent)[10]
2016	2.08	2.94	0.86	2.8	1.1	2.4
2020	1.68	4.28	2.60	2.8	1.1	4.7
2030	1.30	3.90	2.60	2.1	0.5	5.3
2040	1.22	3.82	2.60	2.2	0.6	5.3
2050	1.25	3.85	2.60	2.2	0.5	5.3
2060	1.21	3.81	2.60	2.1	0.4	5.3
2070	1.15	3.75	2.60	2.1	0.5	5.3
2080	1.14	3.74	2.60	2.1	0.5	5.3
2090	1.15	3.75	2.60	2.0	0.4	5.3

[1]The total fertility rate for any year is the average number of children that would be born to a woman in her lifetime if she were to experience, at each age of her life, the birth rate observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period.
[2]The age-sex-adjusted death rate is based on the enumerated total population as of April 1, 2010, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[3]Net annual immigration is the number of persons who enter during the year (both legally and otherwise) minus the number of persons who leave during the year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[4]The period life expectancy at a given age for a given year is the average remaining number of years expected prior to death for a person at that exact age, born on January 1, using the mortality rates for that year over the course of his or her remaining life. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[5]The real-wage differential is the annual percentage change in the average annual wage in covered employment less the annual percentage change in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). Values are rounded after all computations.
[6]The average annual wage in covered employment is the total amount of wages and salaries for all employment covered by the OASDI program in a year, divided by the number of employees with any such earnings during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[7]The CPI is the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W).
[8]The real GDP is the value of total output of goods and services in 2009 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[9]Total employment is total U.S. military and civilian employment. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[10]The average annual interest rate is the average of the nominal interest rates, which compound semiannually, for special public-debt obligations issuable to the OASI and DI Trust Funds in each of the 12 months of the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

Table 1B
Medicare – Demographic and Economic Assumptions

	Demographic Assumptions		
Year	Total Fertility Rate[1]	Age-Sex Adjusted Death Rate (per 100,000)[2]	Net Annual Immigration (persons per year)[3]
2016	1.90	773.0	1,579,000
2020	2.00	742.8	1,508,000
2030	2.00	679.1	1,332,000
2040	2.00	624.5	1,284,000
2050	2.00	576.8	1,259,000
2060	2.00	534.8	1,244,000
2070	2.00	497.6	1,235,000
2080	2.00	464.6	1,230,000
2090	2.00	435.1	1,228,000

	Economic Assumptions							
					Per Beneficiary Cost[8] (percent change)			
						SMI		
Year	Real Wage Differ-ential (percent)[4]	Average Annual Wage In Covered Employment (percent change)[5]	CPI (percent change)[6]	Real GDP (percent change)[7]	HI	Part B	Part D	Real Interest Rate (percent)[9]
2016	2.08	2.94	0.86	2.8	0.9	2.1	0.9	1.2
2020	1.68	4.28	2.60	2.8	3.9	5.6	6.7	1.9
2030	1.30	3.90	2.60	2.1	3.9	4.5	4.7	2.7
2040	1.22	3.82	2.60	2.2	4.7	4.0	4.7	2.7
2050	1.25	3.85	2.60	2.2	3.8	3.7	4.6	2.7
2060	1.21	3.81	2.60	2.1	3.6	3.6	4.5	2.7
2070	1.15	3.75	2.60	2.1	3.8	3.6	4.4	2.7
2080	1.14	3.74	2.60	2.1	3.8	3.6	4.4	2.7
2090	1.15	3.75	2.60	2.0	3.4	3.4	4.3	2.7

[1]The total fertility rate for any year is the average number of children that would be born to a woman in her lifetime if she were to experience, at each age of her life, the birth rate observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period.

[2]The age-sex-adjusted death rate is based on the enumerated total population as of April 1, 2010, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

[3]Net annual immigration is the number of persons who enter during the year (both legally and otherwise) less the number of persons who leave during the year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

[4]The real-wage differential is the annual percentage change in the average annual wage in covered employment less the annual percentage change in CPI. Values are rounded after computations.

[5]The average annual wage in covered employment is the total amount of wages and salaries for all employment covered by the OASDI program in a year, divided by the number of employees with any such earnings during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

[6]The CPI is the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W).

[7]The real GDP is the value of total output of goods and services produced in the U.S. in 2009 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.

[8]These increases reflect the overall impact of more detailed assumptions that are made for each of the different types of service provided by the Medicare program (for example, hospital care, physician services, and pharmaceutical costs). These assumptions include changes in the payment rates, utilization, and intensity of each type of service.

[9]The real interest rate is the average rate of interest earned on new trust fund securities, above and beyond the rate of inflation.

Railroad Retirement

The Railroad Retirement and Survivor Benefit program pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses and divorced spouses of retired workers and to widow(er)s, surviving divorced spouses, partitioned surviving spouses, partitioned surviving divorced spouses, remarried widow(er)s, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

The RRB and the SSA share jurisdiction over the payment of retirement and survivor benefits. The RRB has jurisdiction over the payment of retirement benefits if the employee has at least 10 years of railroad service, or five years if performed after 1995. For survivor benefits, RRB requires that the employee's last regular employment before retirement or death be in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee's railroad retirement credits to SSA, where they are treated as social security credits.

Payroll taxes paid by railroad employers and their employees are a primary source of income for the Railroad Retirement and Survivor Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay Tier I taxes at the same rate as Social Security taxes and Tier II taxes to finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: financial transactions with the Social Security and Medicare Trust Funds, earnings on investments, federal income taxes on railroad retirement benefits, and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits). The financial interchange between RRB's Social Security Equivalent Benefit (SSEB) Account, the Federal Old-Age and Survivors Insurance Trust Fund, the Disability Insurance Trust Fund, and the Federal Hospital Insurance Trust Fund is intended to put the latter three trust funds in the same position they would have been had railroad employment been covered under the *Social Security Act*. From a governmentwide perspective, these future financial interchanges and transactions are intragovernmental transfers and are eliminated in consolidation.

Railroad Retirement–Employment, Demographic, and Economic Assumptions

The most recent set of projections is prepared using employment, demographic, and economic assumptions reflecting the Board Members' reasonable estimate of expected future experience.

Three employment assumptions were used in preparing the projections and reflect optimistic, moderate, and pessimistic future passenger rail as well as freight employment. The average railroad employment is assumed to be 226,000 in 2016 under the moderate employment assumption. This employment assumption, based on a model developed by the Association of American Railroads, assumes that (1) passenger service employment will remain at the level of 46,000 and (2) the employment base, excluding passenger service employment, will decline at a constant 2.0 percent annual rate for 25 years, at a falling rate over the next 25 years, and remain level thereafter. All the projections are based on an open-group (i.e., future entrants) population.

The moderate (middle) economic assumptions include a long-term cost of living increase of 2.7 percent, an interest rate of 7.0 percent, and a wage increase of 3.7 percent. The cost of living assumption reflects the expected level of price inflation. The interest (or investment) rate assumption reflects the expected rate of return on NRRIT investments. The wage increase reflects the expected increase in railroad employee earnings.

Sources of the demographic assumptions (including mortality rates and total termination rates, remarriage rates for widow(er)s, retirement rates, and withdrawal rates) are listed in Table 2. For further details on the employment, demographic, economic and all other assumptions, refer to the *26th Actuarial Valuation of the Assets and Liabilities under the Railroad Retirement Acts* (Valuation Report) as of December 31, 2013, with Technical Supplement, and the Annual Report on the Railroad Retirement System required by Section 502 of the *Railroad Retirement Solvency Act of 1983*.

Table 2
Railroad Retirement Demographic Actuarial Assumptions (Sources)

Mortality Rates [1]	Mortality after age retirement	2010 Base Year RRB Annuitants Mortality Table with 2013 RRB Mortality Improvement Scale
	Mortality after disability retirement	2010 Base Year RRB Disabled Mortality Table for Annuitants with Disability Freeze with 2013 RRB Mortality Improvement Scale
		2010 Base Year RRB Disabled Mortality Table for Annuitants without Disability Freeze with 2013 RRB Mortality Improvement Scale
	Mortality during active service	2009 RRB Active Service Mortality Table
	Mortality of widowed annuitants	2013 RRB Mortality Table for Widows
Total Termination Rates [2]	Termination for spouses	2010 Base Year RRB Spouse Total Termination Table with 2013 RRB Mortality Improvement Scale
	Termination for disabled children	2004 RRB Total Termination Table for Disabled Children
Widow(er) Remarriage Rates [3]	1997 RRB Remarriage Table	
Retirement Rates [4]	Age retirement	See the Valuation Report.
	Disability retirement	See the Valuation Report.
Withdrawal Rates [5]	See the Valuation Report.	

[1] These mortality tables are used to project the termination of eligible employee benefit payments within the population.

[2] Total termination rates are used to project the termination of dependent benefits to spouses and disabled children.

[3] These rates are used to project the termination of spousal survivor benefits.

[4] The retirement rates are used to determine the expected annuity to be paid based on age and years of service for both age and disability retirees.

[5] The withdrawal rates are used to project all withdrawals from the railroad industry and resultant effect on the population and accumulated benefits to be paid.

Black Lung–Disability Benefit Program

The Black Lung Disability Benefit Program provides for compensation, medical, and survivor benefits for eligible coal miners who are totally disabled due to pneumoconiosis (black lung disease) attributed to their coal mine employment. The same program also provides for survivor benefits for eligible survivors of coal miners who died due to pneumoconiosis. DOL operates the Black Lung Disability Benefit Program.

Black lung disability benefit payments are funded by excise taxes from coal mine operators based on the domestic sale of coal, as are the fund's administrative costs. These taxes are collected by the Internal Revenue Service (IRS) and transferred to the BLDTF, which was established under the authority of the *Black Lung Benefits Revenue Act*, and administered by the Treasury.

P.L. 110-343, *Division B-Energy Improvement and Extension Act of 2008*, enacted on October 3, 2008, among other things, restructured the BLDTF debt by refinancing the outstanding high interest rate repayable advances with low interest rate discounted debt instruments similar in form to zero-coupon bonds, plus a one-time appropriation. This Act also allowed that any subsequent debt issued by the BLDTF may be used to make benefit payments, other authorized expenditures, or to repay debt and interest from the initial refinancing.

Black Lung–Demographic and Economic Assumptions

The demographic assumptions used for the most recent set of projections are the number of beneficiaries and their life expectancy. The beneficiary population data is updated from information supplied by the program. The beneficiary population is a nearly closed universe in which attrition by death exceeds new entrants by a ratio of more than ten to one. SSA Life Tables are used to project the life expectancies of the beneficiary population.

The economic assumptions used for the most recent set of projections are coal excise tax revenue estimates, the tax rate structure, federal civilian pay raises, medical cost inflation, and the interest rates used to discount future cash flows.

The black lung coal excise tax rate structure is $1.10 per ton of underground-mined coal and $0.55 per ton of surface-mined coal sold, with a cap of 4.4 percent of sales price until the earlier of December 31, 2018 (used in all presentations), or the first December 31, in which there exists no (1) balance of repayable debt described in section 9501 of the Internal Revenue Code and (2) unpaid interest on the debt. At that time, the tax rates revert to $0.50 per ton of underground-mined coal and $0.25 per ton of surface-mined coal sold, and a limit of 2.0 percent of sales price.

DOL estimates future excise tax income using two approaches: one approach is used for the first ten years in the projection period and another approach is used for the remaining years in the projection period. For the first ten years in the projection period, the Treasury's Office of Tax Analysis (OTA) provides estimates of future excise tax income of the black lung excise tax. Its estimates are based on projections of future coal production prepared by the Energy Information Administration (EIA) of DOE and coal sale prices prepared by OMB. In fiscal years 2016 and 2015, EIA projections of future coal production reflect, among other things, regulation pursuant to the Clean Power Plan (CPP).

For the remaining years in the projection period, DOL applies a growth rate to the projection for the tenth year and grows the estimates of future excise tax income year-by-year. In fiscal year 2016, DOL further refined the approach for selecting the growth rate to enhance consistency of future tax receipts over the projection period. In fiscal year 2016, the growth rate is based on the average EIA growth rates for future coal production that reflect, among other things, regulation pursuant to the CPP, adjustments to exclude coal exports and lignite (coal exports and lignite are not subject to black lung excise tax), and inflation. In fiscal year 2015, the growth rate was based on the average EIA growth rates for future coal production that reflected, among other things, regulation pursuant to the CPP. In fiscal years 2012 through 2014, for the remaining years, estimates of future excise tax income used a growth rate based on both historical tax receipts and the Treasury's estimated tax receipts.

In February 2016 the U.S. Supreme Court stayed implementation of regulation pursuant to the CPP due to litigation pending in the U.S. Court of Appeals; as of September 30, 2016 the stay remained in effect.

OMB supplies assumptions for future monthly benefit rate increases based on increases in the federal pay scale and future medical cost inflation based on increases in the CPIM, which are used to calculate future benefit costs. During the current projection period, the future benefit rate increases 1.0 percent in 2017, 1.38 percent in 2018, 1.88 percent in 2019, 2.38 percent in 2020, 2.88 percent in 2021, and 3.0 percent in each year thereafter, and medical cost increases 5.0 percent in each year. Estimates for administrative costs for the first 10 years of the projection period are supplied by DOL's Budget Office, based on current year enacted amounts, while later years are based on the number of projected beneficiaries.

Statement of Changes in Social Insurance Amounts

The Statement of Changes in Social Insurance Amounts reconciles the change (between the current valuation and the prior valuation) in the present value of estimated future revenue less estimated future expenditures for current and future participants (the open group measure) over the next 75 years (except Black Lung which has a projection period through September 30, 2040). The reconciliation identifies several components of the changes that are significant and provides reasons for the changes. The following disclosures relate to the Statement of Changes in Social Insurance Amounts including the reasons for the components of the changes in the open group measure during the reporting period from the end of the previous reporting period for the Government's social insurance programs.

Social Security

The Statement of Changes in Social Insurance Amounts shows two reconciliations for Social Security: (1) changes from the period beginning on January 1, 2015, to the period beginning on January 1, 2016, and (2) changes from the period beginning on January 1, 2014, to the period beginning on January 1, 2015. All estimates relating to the Social Security Program in the Statement of Changes in Social Insurance Amounts represent values that are incremental to the prior change. As an example, the present values shown for economic data, assumptions, and methods represent the additional effect of these new data, assumptions, and methods after considering the effects from demography and the change in the valuation period. In general, an increase in the present value of net cash flows represents a positive change (improving financing), while a decrease in the present value of net cash flows represents a negative change (worsening financing).

Assumptions Used for the Components of the Changes for the Social Security Program

The present values included in the Statement of Changes in Social Insurance Amounts are for the current and prior years and are based on various economic as well as demographic assumptions used for the intermediate assumptions in the Social Security Trustees Reports for these years. Table 1A summarizes these assumptions for the current year.

Period Beginning on January 1, 2015, and Ending January 1, 2016

Present values as of January 1, 2015 are calculated using interest rates from the intermediate assumptions of the 2015 Social Security Trustees Report. All other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated as a present value as of January 1, 2016. Estimates of the present value of changes in social insurance amounts due to changing the valuation period and changing demographic data, assumptions, and methods are presented using the interest rates under the intermediate assumptions of the 2015 Social Security Trustees Report. Because interest rates are an economic estimate and all estimates in the table are incremental to the prior change, all other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated using the interest rates under the intermediate assumptions of the 2016 Social Security Trustees Report.

Period Beginning on January 1, 2014, and Ending January 1, 2015

Present values as of January 1, 2014, are calculated using interest rates from the intermediate assumptions of the 2014 Social Security Trustees Report. All other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated as a present value as of January 1, 2015. Estimates of the present value of changes in social insurance amounts due to changing the valuation period and changing demographic data, assumptions, and methods are presented using the interest rates under the intermediate assumptions of the 2014 Social Security Trustees Report. Because interest rates are an economic estimate and all estimates in the table are incremental to the prior change, all other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated using the interest rates under the intermediate assumptions of the 2015 Social Security Trustees Report.

Changes in Valuation Period

Period Beginning on January 1, 2015, and Ending January 1, 2016

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2015-2089) to the current valuation period (2016-2090) is measured by using the assumptions for the prior valuation and extending them to cover the current valuation. Changing the valuation period removes a small negative net cash flow for 2015, replaces it with a much larger negative net cash flow for 2090, and measures the present values as of January 1, 2016, one year later. Thus, the present value of estimated future net cash flows (excluding the combined OASI and DI Trust Fund asset reserves at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2015-2089 to 2016-2090. In addition, the effect on the level of asset reserves in the combined OASI and DI Trust Funds of changing the valuation

period is measured by assuming all values projected in the prior valuation for the year 2015 are realized. The change in valuation period increased the starting level of asset reserves in the combined OASI and DI Trust Funds.

Period Beginning on January 1, 2014, and Ending January 1, 2015

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2014-2088) to the current valuation period (2015-2089) is measured by using the assumptions for the prior valuation and extending them to cover the current valuation. Changing the valuation period removes a small negative net cash flow for 2014, replaces it with a much larger negative net cash flow for 2089, and measures the present values as of January 1, 2015, one year later. Thus, the present value of estimated future net cash flows (excluding the combined OASI and DI Trust Fund asset reserves at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2014-2088 to 2015-2089. In addition, the effect on the level of asset reserves in the combined OASI and DI Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2014 are realized. The change in valuation period increased the level of asset reserves in the combined OASI and DI Trust Funds.

Changes in Demographic Data, Assumptions, and Methods

Period Beginning on January 1, 2015, and Ending January 1, 2016

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2016), with the exception of a small change in marriage rates, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2013 and 2014 indicated lower birth rates than were expected in the prior valuation. The data also show an increase in birth rates starting in 2014, one year later than assumed in the prior valuation.
- Incorporating mortality data obtained from the National Center for Health Statistics at ages under 65 for 2012 and 2013 and from Medicare experience at ages 65 and older for 2013 resulted in slightly higher death rates than were projected in the prior valuation.
- Assumed ultimate marriage rates were decreased somewhat to reflect a continuation of recent trends.
- More recent legal and other-than-legal immigration data and historical population data were included.

The effect of including the new birth rate data and immigration data was a decrease in the present value of estimated future net cash flows, while the inclusion of the mortality data and the marriage rate changes increased the present value of estimated future net cash flows.

There were two changes in demographic methodology:

- The transition from recent mortality rates to the ultimate rates starts sooner, immediately after the year of final data. The approach used for the prior valuation extended the trend of the last 10 years through the valuation year for the report and only thereafter started the transition to assumed ultimate rates of decline.
- Historical non-immigrant population counts were revised to match recent totals provided by the Department of Homeland Security. In addition, emigration rates for the never-authorized and visa-overstayer populations were recalibrated to reflect a longer historical period and to be less influenced by the high emigration rates experienced during the recent recession. Finally, the method for projecting emigration of the never-authorized population was altered to reflect lower rates of emigration for those who have resided here longer.

The effect of including these methodological improvements was an increase in the present value of estimated future net cash flows.

Period Beginning on January 1, 2014, and Ending January 1, 2015

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2015), with the exception of changes made due to the executive actions on immigration, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2012 and preliminary data for 2013 indicated lower birth rates than were expected in the prior valuation. In this year’s report the total fertility rate reaches the ultimate in 2027, which is eleven years earlier than in last year’s report.
- Incorporating mortality data obtained from Medicare experience at ages 65 and older for 2012 resulted in slightly higher death rates for 2012 and a slightly slower rate of decline in mortality over the next 25 years than were projected in last year’s report. Incorporating mortality data obtained from the National Centers for Health Statistics at ages under 65 for 2011 resulted in slightly lower death rates for 2011 and a slightly faster rate of decline in mortality over the next 25 years than were projected in last year’s report.

- Historical legal immigration was revised to include single age data (rather than 5-year age groups); including more recent marriage, legal immigration, and other-than-legal immigration data; historical data since 2001 was revised to be more consistent with the most recent estimates from the Census Bureau.

The effect of including the new birth rate data and immigration data was a decrease in the present value of estimated future net cash flows, while the inclusion of the remaining data increased the present value of estimated future net cash flows.

Changes in Economic Data, Assumptions, and Methods

Period Beginning on January 1, 2015, and Ending January 1, 2016

For the current valuation (beginning on January 1, 2016), there were three changes to the ultimate economic assumptions.

- The ultimate rate of price inflation (CPI-W) was lowered by 0.1 percentage point, to 2.6 percent from 2.7 percent for the previous valuation.
- The ultimate average real wage differential is assumed to be 1.20 percent in the current valuation period, compared to 1.17 percent in the previous valuation period.
- The ultimate real interest rate was lowered by 0.2 percentage point, to 2.7 percent from 2.9 percent for the previous valuation period.

While very low inflation in recent years is reflective of U.S. and international supply and demand factors that have been affected by the global recession, the average rate of change in the CPI-W over the last two complete business cycles (from 1989 to 2007) is 2.63 percent. The lower ultimate CPI decreases the present value of estimated future net cash flows.

The higher real-wage differential assumption is based on new projections by the Centers for Medicare & Medicaid Services of slower growth in employer sponsored group health insurance premiums. Because these premiums are not subject to the payroll tax, slower growth in these premiums means that a greater share of employee compensation will be in the form of wages that are subject to the payroll tax. The higher real-wage differential increased the present value of estimated future net cash flows.

Real interest rates have been low since 2000, and particularly low since the start of the recent recession. An ongoing and much-debated question among experts is how much of this change is cyclic or a temporary response to extraordinary events, versus a fundamental permanent change. The Trustees believe that lowering the long-term ultimate real interest rate somewhat is appropriate at this time. The lower real interest rate decreased the present value of estimated future net cash flows.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed.

- A reduction in the ultimate level of actual and potential gross domestic product (GDP) of about 1.0 percent is assumed. Thus, by the end of the short-range period (2025) and for all years thereafter, projected GDP in 2009 dollars is about 1.8 percent below the level in last year's report.

The change to GDP decreased the present value of estimated future net cash flows. Other, smaller changes in starting values and near term growth assumptions combined to increase the present value of estimated future net cash flows.

Period Beginning on January 1, 2014, and Ending January 1, 2015

For the current valuation (beginning on January 1, 2015), there was one change to the ultimate economic assumptions.

- The ultimate real-wage differential is assumed to be 1.17 percent in the current valuation period, compared to 1.13 percent in the previous valuation period.

The higher real-wage differential assumption is more consistent with recent experience and expectations of slower growth in employer-sponsored group health insurance premiums from the Centers for Medicare & Medicaid Services. Because these premiums are not subject to the payroll tax, slower growth in these premiums means that a greater share of employee compensation will be in the form of wages that are subject to the payroll tax. This change to the real-wage assumption increased the present value of estimated future net cash flows.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed.

- The ratio of average taxable earnings to the average wage averages about 0.6 percentage point higher during the long-range period, compared to the previous valuation period.

- The projected suspense file contains fewer wage items, which is consistent with having fewer workers (many of whom are undocumented immigrants) with wages on the suspense file and more of these workers with earnings in the underground economy, compared to the previous valuation.

The change to the ratio of average taxable earnings to the average wage index increased the present value of estimated future net cash flows while the change to the suspense file decreased the present value of estimated future net cash flows. Other, smaller changes in starting values and near term growth assumptions combined to increase the present value of estimated future net cash flows.

Changes in Law or Policy

Period Beginning on January 1, 2015, and Ending January 1, 2016

In the current valuation period (beginning on January 1, 2016), one law was enacted that is expected to have a significant effect on the long-range cost of the OASDI program. On November 2, 2015, the President signed into law Public Law 114-74, the *Bipartisan Budget Act of 2015*. Several sections of the law had significant effects on long-range actuarial status, including:

- Section 831. Closure of unintended loopholes. This provision eliminates (1) the ability to receive only a retired-worker benefit or an aged-spouse benefit when eligible for both, for those attaining age 62 in 2016 and later, and (2) the ability of a family member other than a divorced spouse to receive a benefit based on the earnings of a worker with a voluntarily suspended benefit, for voluntary suspensions requested after April 29, 2016.
- Section 832. Requirement for medical review. This section requires that the medical portion of the case review and any applicable residual functional capacity assessment for an initial disability determination be completed by an appropriate physician, psychiatrist, or psychologist.
- Section 833. Reallocation of payroll tax rates. For earnings in calendar years 2016 through 2018, this section temporarily reallocates from 1.80 percent to 2.37 percent the portion of the total 12.40 percent OASDI payroll tax that is directed to the DI Trust Fund. This reallocation of the payroll tax rates had no cost effect on the combined OASDI program.

The effect of including this law was an increase in the present value of estimated future net cash flows.

Period Beginning on January 1, 2014, and Ending January 1, 2015

In the current valuation period (beginning on January 1, 2015), no laws were enacted that are expected to have significant effects on the long-range cost of the OASDI program. However, on November 20, 2014, the President announced a series of executive actions on immigration, which are expected to have a significant effect on the long-range income and cost of the OASDI program. Due to a federal court order, implementation of the actions affecting undocumented children and parents is on hold at the time of this report. However, the estimates in this report assume this court order will be temporary and that the executive actions will proceed by the end of 2015.

The effect of including these executive actions was an increase in the present value of estimated future net cash flows.

Changes in Methodology and Programmatic Data

Period Beginning on January 1, 2015, and Ending January 1, 2016

Several methodological improvements and updates of program-specific data are included in the current valuation (beginning on January 1, 2016). The most significant are identified below.

- The sample used in the prior valuation for projecting average benefit levels of retired worker and disabled-worker beneficiaries newly entitled for benefits was for worker beneficiaries newly entitled in 2008. The current valuation uses the results from worker beneficiaries newly entitled in 2013. In addition, the method used to determine initial entitlements was improved, primarily to take into account the recent increase of “file and suspend” cases, which were not fully included under the previous methodology.
- Recent data and estimates provided by the Office of Tax Analysis at the Treasury indicated higher levels of revenue from taxation of OASDI benefits than projected in the prior valuation.

Both of these methodological improvements increased the present value of estimated future net cash flows.

Period Beginning on January 1, 2014, and Ending January 1, 2015

Several methodological improvements and updates of program-specific data are included in the current valuation (beginning on January 1, 2015). The most significant are identified below.

- The earnings histories of worker beneficiaries were changed to be more consistent with: (1) the projected employment and earnings by single year of age and gender used in estimating payroll tax revenue and (2) the projected distribution by single year of age and gender of newly entitled worker beneficiaries for each projection year.
- The projected relative earnings levels for those over age 65 were changed to those age 65 and younger. The projected insured rate for some immigrants was lowered. The affected group of immigrants includes those working in covered employment with a temporary visa that allows them to work and those working in covered employment without current legal work authorization.
- The ultimate projected ratio of income from taxation of benefits to total benefits was increased for this valuation period. There were also updates to programmatic data, changes in projections of beneficiaries and benefit levels over the first 10 years of the projection period, other small methodological improvements, and interactions.

All of these methodological improvements increased the present value of estimated future net cash flows.

Potential Impact on the Social Insurance Statements of the June 23, 2016 Supreme Court Judgment on the 2014 DACA and DAPA Executive Actions

In November 2014, Presidential executive actions expanded the Deferred Action for Childhood Arrivals program (DACA) and established the Deferred Action for Parents of Americans program (DAPA). On June 23, 2016, the Supreme Court was divided (tied 4-4) on the ruling of the legality of the expanded DACA and DAPA programs, so the lower court's ruling, temporarily blocking these programs from being implemented, was upheld. As a result, the expanded DACA and DAPA programs will be either delayed or never implemented. The SSA Office of the Chief Actuary has concluded that the Supreme Court's judgment has an effect on the actuarial methods and assumptions used in developing the estimates presented in the Statements of Social Insurance and the Statement of Changes in Social Insurance Amounts. Whether the expanded DACA and DAPA programs are delayed or never implemented, it is expected that the judgment will have an impact of less than $25 billion on the present value of future noninterest income less future cost for current and future participants (open group measure) presented in the Statements of Social Insurance and Statement of Changes in Social Insurance Amounts. These effects are not considered to be material.

Medicare

The Statement of Changes in Social Insurance Amounts shows two reconciliations for Medicare: (1) changes from the period beginning on January 1, 2015, to the period beginning on January 1, 2016, and (2) changes from the period beginning on January 1, 2014, to the period beginning on January 1, 2015. All estimates relating to the Medicare program in the Statement of Changes in Social Insurance Amounts represent values that are incremental to the prior change. As an example, the present values shown for demographic data, assumptions, and methods represent the additional effect that these assumptions have, once the effects from the change in the valuation period and projection base have been considered. In general, an increase in the present value of net cash flows represents a positive change (improving financing), while a decrease in the present value of net cash flows represents a negative change (worsening financing).

Assumptions Used for the Components of the Changes for the Medicare Program

The present values included in the Statement of Changes in Social Insurance Amounts are for the current and prior years and are based on various economic and demographic assumptions used for the intermediate assumptions in the Medicare Trustees Reports for these years. Table 1B summarizes these assumptions for the current year**.**

Period Beginning on January 1, 2015, and Ending January 1, 2016

Present values as of January 1, 2015 are calculated using interest rates from the intermediate assumptions of the 2015 Medicare Trustees Report. All other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated as a present value as of January 1, 2016. Estimates of the present value of changes in social insurance amounts due to changing the valuation period, projection base, demographic assumptions, and law are presented using the interest rates under the intermediate assumptions of the 2015 Medicare Trustees Report. Since interest rates are an economic estimate and all estimates in the table are incremental to the prior change, the estimates of the present values of changes in economic and health care assumptions are calculated using the interest rates under the intermediate assumptions of the 2016 Medicare Trustees Report.

Period Beginning on January 1, 2014, and Ending January 1, 2015

Present values as of January 1, 2014 are calculated using interest rates from the intermediate assumptions of the 2014 Medicare Trustees Report. All other present values in this part of the Statement of Changes in Social Insurance Amounts are calculated as a present value as of January 1, 2015. Estimates of the present value of changes in social insurance amounts due to changing the valuation period, projection base, demographic assumptions, and law are presented using the interest rates under the intermediate assumptions of the 2014 Medicare Trustees Report. Since interest rates are an economic estimate and all estimates in the table are incremental to the prior change, the estimates of the present values of changes in economic and health care assumptions are calculated using the interest rates under the intermediate assumptions of the 2015 Medicare Trustees Report.

Changes in Valuation Period

Period Beginning on January 1, 2015, and Ending January 1, 2016

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2015-2089) to the current valuation period (2016-2090) is measured by using the assumptions for the prior valuation period and extending them, in the absence of any other changes, to cover the current valuation period. Changing the valuation period removes a small negative net cash flow for 2015, replaces it with a much larger negative net cash flow for 2090, and measures the present values as of January 1, 2016, one year later. Thus, the present value of estimated future net cash flow (including or excluding the combined Medicare Trust Fund assets at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2015-2089 to 2016-2090. In addition, the effect on the level of assets in the combined Medicare Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2015 are realized. The change in valuation period slightly increased the starting level of assets in the combined Medicare Trust Funds.

Period Beginning on January 1, 2014, and Ending January 1, 2015

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2014-2088) to the current valuation period (2015-2089) is measured by using the assumptions for the prior valuation period and applying them, in the absence of any other changes, to the current valuation period. Changing the valuation period removes a small negative net cash flow for 2014 and replaces it with a much larger negative net cash flow for 2089. The present value of estimated future net cash flow (including or excluding the combined Medicare Trust Fund assets at the start of the period) was therefore decreased (made more negative) when the 75-year valuation period changed from 2014-2088 to 2015-2089. In addition, the effect on the level of assets in the combined Medicare Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2014 are realized. The change in valuation period decreased the level of assets in the combined Medicare Trust Funds.

Changes in Demographic Data, Assumptions, and Methods

Period Beginning on January 1, 2015, and Ending January 1, 2016

The demographic assumptions used in the Medicare projections are the same as those used for the Old-Age Survivors and Disability Insurance (OASDI) and are prepared by the Office of the Chief Actuary at SSA.

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2016), with the exception of a small change in marriage rates, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2013 and 2014 indicated lower birth rates than were expected in the prior valuation. The data also show an increase in birth rates starting in 2014, one year later than assumed in the prior valuation.
- Incorporating mortality data obtained from the National Center for Health Statistics at ages under 65 for 2012 and 2013 and from Medicare experience at ages 65 and older for 2013 resulted in slightly higher death rates than were projected in the prior valuation.
- Assumed ultimate marriage rates were decreased somewhat to reflect a continuation of recent trends.
- More recent legal and other-than-legal immigration data and historical population data were included.

There were two changes in demographic methodology:

- The transition from recent mortality rates to the ultimate rates starts sooner, immediately after the year of final data. The approach used for the prior valuation extended the trend of the last 10 years through the valuation year for the report and only thereafter started the transition to assumed ultimate rates of decline.

- Historical non-immigrant population counts were revised to match recent totals provided by the Department of Homeland Security. In addition, emigration rates for the never-authorized and visa-overstayer populations were recalibrated to reflect a longer historical period and to be less influenced by the high emigration rates experienced during the recent recession. Finally, the method for projecting emigration of the never-authorized population was altered to reflect lower rates of emigration for those who have resided here longer.

These changes slightly lowered overall Medicare enrollment for the current valuation period and resulted in an increase in the estimated future net cash flow. The present value of estimated expenditures is lower for all parts of Medicare; and the present value of estimated income is also lower for Parts B and D but very slightly higher for Part A.

Period Beginning on January 1, 2014, and Ending January 1, 2015

The demographic assumptions used in the Medicare projections are the same as those used for the Old-Age Survivors and Disability Insurance (OASDI) and are prepared by the Office of the Chief Actuary at the SSA.

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2015), with the exception of changes made due to the execution on immigration, are the same as those for the prior valuation. However, the starting demographic values, and the way these values transition to the ultimate assumptions, were changed.

- Final birth rate data for 2012 and preliminary data for 2013 indicated lower birth rates than were expected in the prior valuation. In this year's report, the total fertility rate reaches the ultimate in 2027, which is eleven years earlier than in last year's projections.
- Incorporating mortality data obtained from Medicare experience at ages 65 and older for 2012 resulted in slightly higher death rates for 2012 and a slightly slower rate of decline in mortality over the next 25 years than were projected last year. Incorporating mortality data obtained from the National Centers for Health Statistics at ages under 65 for 2011 resulted in slightly lower death rates for 2011 and a slightly faster rate of decline in mortality over the next 25 years than were projected last year.
- Historical legal immigration was revised to include single age data (rather than 5-year age groups); including more recent marriage, legal immigration, and other-than-legal immigration data; historical data since 2001 was revised to be more consistent with the most recent estimates from the Census Bureau.

These changes slightly lowered overall Medicare enrollment for the current valuation period resulting in a decrease in the estimated future net cash flow, and had a very minor impact on the present value of estimated income and estimated expenditures for Part A, Part B, and Part D.

Changes in Economic and Other Health Care Assumptions

Period Beginning on January 1, 2015, and Ending January 1, 2016

The economic assumptions used in the Medicare projections are the same as those used for the Old-Age Survivors and Disability Insurance (OASDI) and are prepared by the Office of the Chief Actuary at SSA.

For the current valuation (beginning on January 1, 2016), there were three changes to the ultimate economic assumptions.

- The ultimate rate of price inflation (CPI-W) was lowered by 0.1 percentage point, to 2.6 percent from 2.7 percent for the previous valuation.
- The ultimate average real wage differential is assumed to be 1.20 percent in the current valuation period, compared to 1.17 percent in the previous valuation period.
- The ultimate real interest rate was lowered by 0.2 percentage point, to 2.7 percent from 2.9 percent for the previous valuation period.

While very low inflation in recent years is reflective of U.S. and international supply and demand factors that have been affected by the global recession, the average rate of change in the CPI-W over the last two complete business cycles (from 1989 to 2007) is 2.63 percent.

The higher real wage differential assumption is based on new projections by the Centers for Medicare & Medicaid Services of slower growth in employer-sponsored group health insurance premiums. Because these premiums are not subject to the payroll tax, slower growth in these premiums means that a greater share of employee compensation will be in the form of wages that are subject to the payroll tax.

Real interest rates have been low since 2000, and particularly low since the start of the recent recession. An ongoing and much-debated question among experts is how much of this change is cyclic or a temporary response to extraordinary events, versus a fundamental permanent change. The Trustees believe that lowering the long-term ultimate real interest rate

somewhat is appropriate at this time. The long-range present values are very sensitive to the ultimate interest rate assumption because they are used as the discount factor. The reduction in the ultimate interest rate assumption from 2.9 percent to 2.7 percent increases each of the present values by roughly 15 to 16 percent.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed.

- A reduction in the ultimate level of actual and potential gross domestic product (GDP) of about 1.0 percent is assumed. Thus, by the end of the short-range period (2025) and for all years thereafter, projected GDP in 2009 dollars is about 1.8 percent below the level in last year's report.

The health care assumptions are specific to the Medicare projections. The following health care assumptions were changed in the current valuation.

- Utilization rate assumptions for inpatient hospital services were increased.
- The number of beneficiaries enrolled in Medicare Advantage plans and their relative costs are slightly different from last year’s assumptions.
- Lower productivity increases through 2021, resulting in higher provider payment updates.
- Greater reductions in expenditures attributable to the Independent Payment Advisory Board.
- Inclusion of the income and expenditures for aged non-insured beneficiaries in the Medicare Part A long-range analysis.
- Higher projected drug cost trend, particularly for certain high-cost specialty drugs.

The net impact of these changes resulted in a decrease in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in an increase to the present value of estimated future expenditures and income, with an overall decrease in the estimated future net cash flow. For Part B and Part D, these changes increased the present value of estimated future expenditures (and also income).

Period Beginning on January 1, 2014, and Ending January 1, 2015

The economic assumptions used in the Medicare projections are the same as those used for the OASDI and are prepared by the Office of the Chief Actuary at the SSA.

For the current valuation (beginning on January 1, 2015), there was one change to the ultimate economic assumptions:

- The ultimate real-wage differential is assumed to be 1.17 percent in the current valuation period, compared to 1.13 percent in the previous valuation period.

The higher real-wage differential assumption is more consistent with recent experience and expectations of slower growth in employer sponsored group health insurance premiums from the Office of the Actuary at the CMS. Because these premiums are not subject to the payroll tax, slower growth in these premiums means that a greater share of employee compensation will be in the form of wages that are subject to the payroll tax.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values, and the way these values transition to the ultimate assumptions, were changed.

- The ratio of average taxable earnings to the average wage averages about 0.6 percentage point higher during the long-range period, compared to the previous valuation period.
- The projected suspense file contains fewer wage items, which is consistent with having fewer workers (many of whom are undocumented immigrants) with wages on the suspense file and more of these workers with earnings in the underground economy, compared to the previous valuation.

The health care assumptions are specific to the Medicare projections. The following health care assumptions were changed in the current valuation.

- Lower long-range growth rate assumptions.
- Utilization rate assumptions for inpatient hospital services were decreased.
- Lower assumed hospice spending.
- Higher assumed enrollment in Medicare Advantage plans where benefits are more costly.
- Introduction of high-cost specialty drugs used to treat hepatitis C.

The net impact of these changes resulted in an increase in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in an increase to the present value of estimated future expenditures and income, with an overall

increase in the estimated future net cash flow. For Part B and Part D, these changes decreased the present value of estimated future expenditures (and also income), with an overall increase in the estimated future net cash flow.

Changes in Law or Policy

Period Beginning on January 1, 2015, and Ending January 1, 2016

Most of the provisions enacted as part of Medicare legislation since the prior valuation date had little or no impact on the program. The following provisions did have a financial impact on the present value of the 75-year estimated future income, expenditures, and net cash flow.

- The *Trade Preference Extension Act of 2015* requires Medicare coverage for renal dialysis services provided by outpatient renal dialysis facilities to individuals with acute kidney injury, effective January 1, 2017.
- The *Bipartisan Budget Act of 2015* (BBA) included provisions that affect the HI and SMI programs.
    - The BBA required that the 2016 actuarial rate for enrollees aged 65 and older be determined as if the hold-harmless provision does not apply, thereby lowering the standard Part B premium rate from what it otherwise would have been. The premium revenue that was lost by using the resulting lower premium (excluding the forgone income-related premium revenue) was to be replaced by a transfer of general revenue from the Treasury, which will be repaid over time to the General Fund. Starting in 2016, in order to repay the balance due (which is to include the transfer amount and the forgone income-related premium revenue), the monthly Part B premium otherwise determined is to be increased by $3.00. These repayment amounts are to be added to the Part B premium otherwise determined each year and paid back to the General Fund. This $3.00 increase will not be matched by government contributions. These repayment amounts are to continue until the total amount collected is equal to the beginning balance due. (In the final year of the repayment, the additional amounts may be modified to avoid an overpayment.) The repayment amounts (excluding those for high-income enrollees) are subject to the hold-harmless provision. The BBA also stipulated that if the Social Security cost-of-living adjustment (COLA) was 0 percent in 2017, then an additional transfer (and $3 repayment amount) would have again applied. However, the 2017 COLA of 0.3 percent was released on October 18, 2016.
    - Outpatient hospital services provided on or after January 1, 2017 by most new off-campus hospital provider-based outpatient departments (that is, those established on or after the BBA date of enactment of November 2, 2015 and located more than 250 yards from the campus) are excluded from the outpatient hospital prospective payment system, and are instead to be reimbursed under the applicable Part B payment system.
    - The sequestration process that is in place should Congress fail to address the budget deficit by certain deadlines is extended by one year, through fiscal year 2025. In addition, Medicare benefit payments for services provided under periods of sequestration incur a payment reduction limited to 2 percent, so that the former differential payment reduction limits imposed for fiscal years 2023 and 2024 are replaced with 2-percent limits. Finally, the 2-percent limit is raised to 4.0 percent for the first 6 months of sequestration required for fiscal year 2025 and reduced to 0.0 percent for the second 6 months of the year.
- The *Consolidated Appropriations Act of 2016* included provisions that affect the HI and SMI programs.
    - The payment calculation associated with inpatient hospital operating costs for Puerto Rico hospital discharges on or after January 1, 2016 is to be based on 0 percent of the applicable Puerto Rico percentage and 100 percent of the applicable federal percentage. (In addition, CMS announced that both the fiscal year 2016 Inpatient Prospective Payment System Pricer and the Long-Term Care Hospital Pricer, which are used to determine all inpatient hospital payment rates and certain long-term care hospital payment rates, respectively, for providers nationwide, are to incorporate the Puerto Rico inpatient hospital payment modification. These conforming changes are applicable to inpatient hospital discharges and long-term care hospital discharges on or after January 1, 2016.)
    - Puerto Rico hospitals are eligible to receive incentive payments under the Medicare Electronic Health Records Incentive Program, effective January 1, 2016.
    - Effective January 1, 2017, separate Medicare payment is authorized to home health agencies when they use cost-effective disposable alternatives to negative pressure wound therapy equipment.
    - To incentivize the transition from traditional x-ray imaging to digital radiography, Part B payment for the technical component of film x-rays, under the hospital outpatient prospective payment system and under the physician fee schedule, is reduced by 20 percent beginning in 2017. In addition, payment for the technical component of x-rays taken using computed radiography technology is reduced by 7 percent during 2018 through 2022 and by 10 percent beginning in 2023. Also, the discount in payment for the

professional component of multiple imaging services furnished on or after January 1, 2017 is reduced from 25 percent to 5 percent, and the 5 percent reduction is taken in a non-budget neutral manner.

- A one-year moratorium for calendar year 2017 is placed on the annual fee to be paid by health insurance providers. This fee, which was established by the *Affordable Care Act*, is imposed on certain large health insurance providers, including those furnishing coverage under Medicare Advantage (Part C) and Medicare Part D. (Since Medicare Advantage is paid for by the HI Trust Fund and the Part B account of the SMI Trust Fund, this provision affects all parts of Medicare.)

Overall these provisions resulted in a slight increase in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in a slight decrease to the present value of estimated future expenditures, with an overall increase in the estimated future net cash flow. For Part B, these changes decreased the present value of estimated future expenditures (and also income). For Part D, the above-mentioned changes also resulted in a lower present value of estimated future expenditures (and also income) but only very slightly.

Period Beginning on January 1, 2014, and Ending January 1, 2015

Although Medicare legislation was enacted since the prior valuation date, some of the provisions have a negligible impact on the present value of the 75-year estimated future income, expenditures, and net cash flow. The *Veteran's Access, Choice, and Accountability Act of 2014* established a temporary program that allows eligible veterans to receive hospital care and medical services from eligible providers outside of the Department of Veterans Affairs (VA) system, rather than waiting for a VA appointment or traveling to a VA facility. The *Improving Medicare Post-Acute Care Transformation Act of 2014* standardized the collection of data for post-acute providers and aligned the inflation of the hospice aggregate cap with that of hospice reimbursement. The *Tax Increase Prevention Act of 2014* accelerated the start date for the payment adjustment of misvalued codes under the physician fee schedule from 2017 to 2016, and delayed inclusion of oral-only end-stage renal disease (ESRD)-related drugs into the ESRD bundled payment system from 2024 to 2025. MACRA included many provisions affecting Medicare spending, including the repeal of the SGR formula for determining payments under the physician fee schedule, the continuation of extensions for several provisions from prior legislation, a reduction in payment updates for most post-acute providers in 2018, the replacement of a 3.2 percent reduction to inpatient hospitals in 2018 with a 0.5 percent reduction in 2018 through 2023, and a revision to the income thresholds for determining the income-related monthly adjustment amounts under Part B and Part D.

Overall these provisions resulted in a slight decrease in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in a decrease to the present value of estimated future expenditures, with an overall increase in the estimated future net cash flow. For Part B, these changes increased the present value of estimated future expenditures (and also income). For Part D, the above-mentioned changes decreased the present value of estimated future expenditures (and also income) only very slightly.

Change in Projection Base

Period Beginning on January 1, 2015, and Ending January 1, 2016

Actual income and expenditures in 2015 were different than what was anticipated when the 2015 Medicare Trustees Report projections were prepared. Part A income and expenditures were higher than anticipated, based on actual experience. Part B total income and expenditures were lower than estimated based on actual experience. For Part D, actual income and expenditures were both higher than prior estimates. The net impact of the Part A, B, and D projection base changes is a decrease in the estimated future net cash flow. Actual experience of the Medicare Trust Funds between January 1, 2015 and January 1, 2016 is incorporated in the current valuation and is slightly less than projected in the prior valuation.

Period Beginning on January 1, 2014, and Ending January 1, 2015

Actual income and expenditures in 2014 were different than what was anticipated when the 2014 Medicare Trustees Report projections were prepared. Part A income was slightly lower and expenditures were slightly higher than anticipated, based on actual experience. Part B total income and expenditures were also higher than estimated based on actual experience. For Part D, actual income and expenditures were both higher than prior estimates. The net impact of the Part A, B, and D projection base changes is a decrease in the estimated future net cash flow. Actual experience of the Medicare Trust Funds between January 1, 2014 and January 1, 2015 is incorporated in the current valuation and is slightly more than projected in the prior valuation.

Potential Impact on the Social Insurance Statements of the June 23, 2016 Supreme Court Judgment on the 2014 DACA and DAPA Executive Actions

In November 2014, Presidential executive actions expanded the Deferred Action for Childhood Arrivals program (DACA) and established the Deferred Action for Parents of Americans program (DAPA). On June 23, 2016, the Supreme Court was divided (tied 4-4) on the ruling of the legality of the expanded DACA and DAPA programs, so the lower court's ruling, temporarily blocking these programs from being implemented, was upheld. As a result, the expanded DACA and DAPA programs will be either delayed or never implemented. The SSA Office of the Chief Actuary has concluded that the Supreme Court's judgment has an effect on the actuarial methods and assumptions used in developing the estimates presented in the Statements of Social Insurance and the Statement of Changes in Social Insurance Amounts. Whether the expanded DACA and DAPA programs are delayed or never implemented, it is expected the judgment will not have a material impact on the present value of future noninterest income less future costs for current and future participants (open group measure) presented in the Statements of Social Insurance and Statement of Changes in Social Insurance Amounts.

Other

The present values included in the Statement of Changes in Social Insurance Amounts for the Railroad Retirement program are for the current and prior valuation and are based on various employment, demographic, and economic assumptions that reflect the RRB's reasonable estimate of expected future financial and actuarial status of the trust funds.

Note that beginning with fiscal year 2016, the present values included in the Statement of Changes in Social Insurance Amounts for the Railroad Retirement program are on a fiscal year basis, as of October 1, 2015. In the past, all present values were on a calendar year basis, as of January 1. The primary reasons for the changes in the 2016 Statement of Changes in Social Insurance Amounts for Railroad Retirement are for the 9-month period between January 1, 2015 and October 1, 2015. Consequently, the Railroad Retirement changes on the 2016 Statement of Changes in Social Insurance Amounts will not be comparable to the Railroad Retirement changes on the 2015 Statement of Changes in Social Insurance Amounts, which presents the primary reasons for the changes for the 12-month period between January 1, 2014 and January 1, 2015. For a more detailed description of the primary reasons for the changes in the 2016 Statement of Changes in Social Insurance Amounts, please refer to RRB's financial statements.

The significant assumptions used in the projections of the Black Lung social insurance program presented in the Statement of Social Insurance are the coal excise tax revenue estimates, the tax rate structure, the number of beneficiaries, life expectancy, federal civilian pay raises, medical cost inflation, and the interest rates used to discount future cash flows. These assumptions also affect the amounts reported on the Statement of Changes in Social Insurance Amounts, which shows two reconciliations for Black Lung: (1) changes in the open group measure for the year ended September 30, 2016, and (2) changes in the open group measure for the year ended September 30, 2015. For a more detailed description of the primary reasons for the changes in the 2016 Statement of Changes in Social Insurance Amounts, please refer to DOL's financial statements.

Note 23. Long-Term Fiscal Projections

The Statement of Long-Term Fiscal Projections is prepared pursuant to SFFAS No. 36, *Comprehensive Long-Term Projections for the U.S. Government*, as amended. The basic financial statement, Note 23, and related unaudited required supplementary information (RSI) provide information to aid users in assessing whether current policies for Federal spending and taxation can be sustained and the extent to which the cost of public services received by current taxpayers will be shifted to future taxpayers under sustainable policies. This assessment requires prospective information about receipts and spending, the resulting debt, and how these amounts relate to the economy. A sustainable policy is defined as one where the ratio of Federal debt held by the public to GDP (the debt-to-GDP ratio) is ultimately stable or declining. The *Financial Report* does not address the sustainability of State and local government fiscal policy.

The projections and analysis presented here are extrapolations based on an array of assumptions described in detail below. A fundamental assumption is that current Federal policy will not change. This assumption is made so as to inform the question of whether current fiscal policy is sustainable and, if it is not sustainable, the magnitude of needed reforms to make fiscal policy sustainable. The projections are therefore neither forecasts nor predictions. If policy changes are implemented, perhaps in response to projections like those presented here, then actual financial outcomes will be different than those projected. The methods and assumptions underlying the projections are subject to continuing refinement.

The projections focus on future cash flows, and do not reflect either the accrual basis or the modified-cash basis of accounting. These cash-based projections reflect receipts or spending at the time cash is received or when a payment is made by the Government. In contrast, accrual-based projections would reflect amounts in the time period in which income is earned or when an expense or obligation is incurred. The cash basis accounting underlying the long-term fiscal projections is consistent with methods used to prepare the Statements of Social Insurance (SOSI) and the generally cash-based Federal budget.

The basic financial statement, Long-Term Fiscal Projections for the U.S. Government, displays the present value of 75-year projections for various categories of the Federal Government's receipts and non-interest spending.[11] The projections for fiscal years 2016 and 2015 are expressed in present value dollars and as a percentage of the present value of Gross Domestic Product (GDP)[12] as of September 30, 2016 and September 30, 2015, respectively. The present value of a future amount, for example $1 billion in October 2091, is the amount of money that if invested on September 30, 2016 in an account earning the government borrowing rate would have a value of $1 billion in October 2091.[13]

The present value of a receipt or expenditure category over 75 years is the sum of the annual present value amounts. When expressing a receipt or expenditure category over 75 years as a percent of GDP, the present value dollar amount is divided by the present value of GDP over 75 years. Measuring receipts and expenditures as a percentage of GDP is a useful indicator of the economy's capacity to sustain Federal Government programs.

Fiscal Projections

Receipt categories in the long-term fiscal projections include individual income taxes, Social Security and Medicare payroll taxes, and residual remaining category of "other receipts." On the spending side, categories include: (1) discretionary spending that is funded through annual appropriations, such as spending for national security, and (2) mandatory (entitlement) spending that is generally financed with permanent or multi-year appropriations, such as spending for Social Security and Medicare. This year's projections for Social Security and Medicare are based on the same economic and demographic assumptions that underlie the 2016 Social Security and Medicare trustees' reports and the 2016 Statement of Social Insurance, while comparative information presented from last year's report is based on the 2015 Social Security and Medicare trustees' reports and the 2015 Statement of Social Insurance. Projections for the other categories of receipts and spending are consistent with the economic and demographic assumptions in the trustees' reports. The projections assume the continuance of current policy which, as is explained below, can be different than current law in cases where lawmakers have in the past periodically changed the law in a consistent way.

The projections shown in the basic statement are made over a 75-year time frame, consistent with the time frame featured in the Social Security and Medicare trustees' reports. However, these projections are for fiscal years starting on

[11] For the purposes of this analysis, spending is defined in terms of outlays. In the context of Federal budgeting, spending can either refer to budget authority – the authority to commit the government to make a payment; to obligations – binding agreements that will result in payments, either immediately or in the future; or to outlays – actual payments made.

[12] GDP is a standard measure of the overall size of the economy and represents the total market value of all final goods and services produced domestically during a given period of time. The components of GDP are: private sector consumption and investment, government consumption and investment, and net exports (exports less imports). Equivalently, GDP is a measure of the gross income generated from domestic production over the same time period.

[13] Present values recognize that a dollar paid or collected in the future is worth less than a dollar today because a dollar today could be invested and earn interest. To calculate a present value, future amounts are thus reduced using an assumed interest rate, and those reduced amounts are summed.

October 1, whereas the trustees' reports feature calendar-year projections. This difference allows the projections to start from the actual budget results from fiscal years 2016 and 2015.

Changes in Long-Term Fiscal Projections

Present Value (PV) of 75-Year Projections	Trillions of $	Percent of 75-Year PV of GDP
Non-Interest Spending Less Receipts as of September 30, 2015	4.1	0.3
Components of Change:		
Change due to Economic and Demographic Assumptions	1.8	0.1
Change due to Program-Specific Actuarial Assumptions	(0.1)	-
Change due to Updated Budget Data	2.9	0.2
Change in Reporting Period	(0.1)	-
Change in Model Technical Assumptions	2.0	0.2
Total	6.5	0.5
Non-Interest Spending Less Receipts as of September 30, 2016	10.6	0.8

NOTE: Totals may not equal the sum of components due to rounding.

This year's estimate of the 75-year present value imbalance of non-interest spending over receipts expressed as a share of the 75-year present value of GDP is 0.8, compared to 0.3 as was projected in last year's *Financial Report*.[14] The above table reports the effects of various factors on the updated projections. The largest factor, increasing the imbalance by 0.2 percent of GDP ($2.9 trillion), is attributable to actual budget results for fiscal year 2016 and other budget data used in formulating the projection. Nearly half of this effect is due to slightly lower projections of effective tax rates for individual income taxes resulting from the extension of a number of tax expenditures in December 2015 in the *Protecting Americans from Tax Hikes* (PATH) *Act* (P.L. 114-113). The next largest change in the table – increasing the imbalance by 0.2 percent of GDP ($2.0 trillion) – is attributable to changes in technical assumptions underlying the model, including revised assumptions about mandatory sequestration and refinements to the Medicaid projections, as described later in this note. Changes in economic and demographic assumptions increased the imbalance by 0.1 percent of GDP ($1.8 trillion). Economic changes include lowering the assumed average interest rate over the period from 5.4 to 5.1 percent, which had the effect of increasing the 75-year present value of both non-interest spending and receipts, but had relatively little effect on the imbalance between the two.

The last row in the basic financial statement shows that this year's estimate of the overall 75-year present value net excess of non-interest spending over receipts is 0.8 percent of the 75-year present value of GDP ($10.6 trillion, as compared to GDP of $1,302.8 trillion). This imbalance can be broken down by funding source. There is a surplus of receipts over spending of 0.7 percent of GDP ($8.7 trillion) among programs funded by the government's general revenues, but an imbalance of 1.5 percent of GDP ($19.4 trillion[15]) for the combination of Social Security (OASDI) and Medicare Part A,

[14] More information on the projections in last year's Financial Report can be found in Note 24 to the Financial Statements.

[15] The 75-year present value imbalance for Social Security and Medicare Part A of $19.4 trillion is comprised of several line items from the long-term fiscal projections – Social Security outlays net of Social Security Payroll Taxes ($19.3 trillion) and Medicare Part A outlays net of Medicare Payroll Taxes ($7.7 trillion) – as well as subcomponents of these programs not presented separately in the table. These subcomponents include Social Security and Medicare Part A administrative costs that are classified as non-defense discretionary spending ($0.7 trillion) and Social Security and Medicare Part A revenue other than payroll taxes: taxation of benefits (-$3.9 trillion), Federal employer share (-$1.2 trillion), and other income (-$3.2 trillion).

which under current law are funded with payroll taxes and not in any material respect with general revenues.[16, 17] By comparison, the fiscal year 2015 projections showed that programs funded by the Government's general revenues had an excess of receipts over spending of 1.1 percent of GDP ($13.2 trillion) while the payroll tax-funded programs had an imbalance of spending over receipts of 1.4 percent of GDP ($17.3 trillion).

Sustainability and the Fiscal Gap

As discussed further in RSI, the projections in this report indicate that current policy is not sustainable. If current policy is left unchanged, the projections show the debt-to-GDP ratio will fall about 6 percentage points between 2016 and 2024 before commencing a steady rise, exceeding its 2016 level by 2030, exceeding 100 percent by 2039, and reaching 252 percent in 2091. Moreover, if the trends that underlie the 75-year projections were to continue, the debt-to-GDP ratio would continue to rise beyond the 75-year window.

The fiscal gap measures how much the primary surplus (receipts less non-interest spending) must increase in order for fiscal policy to achieve a target debt-to-GDP ratio in a particular future year. In these projections, the fiscal gap is estimated over a 75-year period, from 2017 to 2091, and the target debt-to-GDP ratio is equal to the ratio at the beginning of the projection period, in this case the debt-to-GDP ratio at the end of fiscal year 2016.

The 75-year fiscal gap under current policy is estimated at 1.6 percent of GDP, which is 7.9 percent of the 75-year present value of projected receipts and 7.6 percent of the 75-year present value of non-interest spending. This estimate of the fiscal gap is 0.4 percentage point larger than was estimated in 2015 (1.2 percent of GDP).

The projections show that projected primary deficits average 0.8 percent of GDP over the next 75 years under current policies. If policies were put in place that would result in a zero fiscal gap, the average primary surplus over the next 75 years would be 0.8 percent of GDP, 1.6 percentage points higher than the projected present value net excess of non-interest spending over receipts shown in the basic financial statement. Closing the fiscal gap requires that primary surpluses be substantially positive because the projections assume that interest rates will exceed the growth rate of GDP, so merely achieving primary balance would result in debt growing faster than GDP.

Assumptions Used and Relationship to Other Financial Statements

A fundamental assumption underlying the projections is that current Federal policy (defined below) does not change. The projections are therefore neither forecasts nor predictions, and do not consider large infrequent events such as natural disasters, military engagements, or economic crises. If policy changes are enacted, perhaps in response to projections like those presented here, then actual fiscal outcomes will be different than those projected.

Even if policy does not change, actual expenditures and receipts could differ materially from those projected here. Long-range projections are inherently uncertain and are necessarily based on simplifying assumptions. For example, one key simplifying assumption is that interest rates paid on debt held by the public remain unchanged, regardless of the amount of debt outstanding. To the contrary, it is likely that future interest rates would increase if the debt-to-GDP ratio rises as in these projections. To help illustrate this uncertainty, projections that assume higher and lower interest rate scenarios are presented in the "Alternative Scenarios" discussion in the RSI section of this *Financial Report*.

As is true for prior fiscal year projections, the assumptions for GDP, interest rates, and other economic factors underlying this year's projections are the same assumptions that underlie the most recent Social Security and Medicare trustees' report projections, adjusted for historical revisions that occur annually. The use of discount factors consistent with

[16] As an example of General Fund transfers to these programs, the OASDI trust fund received General Fund transfers, primarily in 2011 and 2012, to account for lost payroll taxes resulting from enactment of the temporary 2 percent reduction of the employee payroll taxes. Social Security and Medicare Part A expenditures can exceed payroll tax revenues in any given year to the extent that there are sufficient balances in the respective trust funds, balances that derive from past excesses of payroll tax revenues over expenditures and interest earned on those balances and represent the amount the General Fund owes the respective trust fund programs. When spending does exceed payroll tax revenues, as has occurred each year since 2008 for Medicare Part A and 2010 for Social Security, the excess spending is financed first with interest due from the General Fund and secondly with a drawdown of the General Fund's loan balance; in either case, the spending is ultimately supported by general revenues or borrowing. Under current law, benefits for Social Security and Medicare Part A can be paid only to the extent that there are sufficient balances in the respective trust funds. In order for the projections here to reflect the full size of these program's commitments to pay future benefits, the projections assume that all scheduled benefits will be financed with borrowing to the extent necessary after the trust funds are exhausted.

[17] The fiscal imbalances reported in the long-term fiscal projections are limited to future outlays and receipts. They do not include the initial level of publicly-held debt, which was $14.2 trillion in 2016 and $13.1 trillion in 2015, and therefore they do not by themselves answer the question of how large fiscal reforms must be to make fiscal policy sustainable, or how those reforms divide between reforms to Social Security and Medicare Part A and to other programs. Other things equal, past cash flows (primarily surpluses) for Social Security and Medicare Part A reduced Federal debt at the end of 2016 by $3.0 trillion (the trust fund balances at that time); the contribution of other programs to Federal debt at the end of 2016 was therefore $17.2 trillion. Because the $19.4 trillion imbalance between outlays and receipts over the next 75 years for Social Security and Medicare Part A does not take account of the Social Security and Medicare Part A trust fund balances, it overstates the magnitude of reforms necessary to make Social Security and Medicare Part A solvent over 75 years by $3.0 trillion. The $3.0 trillion combined Social Security and Medicare Part A trust fund balance represents a claim on future general revenues.

the Social Security trustees' rate allows for consistent present value calculations over 75 years between the Statements of Long-Term Fiscal Projections and the Statements of Social Insurance.

The following bullets summarize the key assumptions used for the categories of receipts and spending presented in the basic financial statement and the disclosures:

- **Social Security:** Projected Social Security (OASDI) spending excludes administrative expenses, which are classified as discretionary spending, and is based on the projected expenditures in the 2016 Social Security trustees' report for benefits and for the Railroad Retirement interchange. The projections of Social Security payroll taxes and Social Security spending are based on future spending and for payroll taxes as are projected in the 2016 Social Security trustees' report, adjusted for presentational differences and converted to a fiscal year basis. More information about the assumptions for Social Security cost growth can be found in Note 22 and the RSI discussion of Social Insurance.
- **Medicare:** Projected Medicare spending is also shown net of administrative expenses and is based on projected incurred expenditures from the 2016 Medicare trustees' report. The projections here make some adjustments to the trustees' report projections. Medicare Part B and D premiums, as well as State contributions to Part D, are subtracted from gross spending in measuring Part B and Part D outlays, just as they are subtracted from gross cost to yield net cost in the financial statements.[18] Here, as in the Federal budget, premiums are treated as "negative spending" rather than receipts since they represent payment for a service rather than payments obtained through the Government's sovereign power to tax. This is similar to the financial statement treatment of premiums as "earned" revenue as distinct from all other sources of revenue, such as taxes. The projections are based on Medicare spending in the Medicare trustees' report, adjusted for presentational differences and converted to a fiscal year basis. Medicare Part A payroll taxes are projected similarly. More information about the assumptions for Medicare cost growth can be found in Note 22 and the Required Supplementary Information for Social Insurance. As discussed in Note 22, there is uncertainty about whether the reductions in health care cost growth projected in the Medicare trustees' report will be fully achieved. Note 22 illustrates this uncertainty by considering Medicare cost growth assumptions under varying policy assumptions.
- **Medicaid:** The Medicaid spending projections start with the projections from the *2015 Actuarial Report on the Financial Outlook for Medicaid* prepared by the Office of the Actuary, Centers for Medicare & Medicaid Services (CMS)[19]. These projections are based on recent trends in Medicaid spending, the demographic, economic, and health cost growth assumptions in the 2015 Medicare Trustees' Report, and projections of the effect of the *Affordable Care Act* (ACA) on Medicaid enrollment. The projections, which end in 2024, are adjusted to accord with the actual Medicaid expenditures in fiscal year 2016. After 2024, the projections assume no further expansion in State Medicaid coverage under the ACA, with the number of Medicaid beneficiaries expected to grow at the same rate as total population, and Medicaid costs per beneficiary assumed to grow at the same rate as Medicare benefits per beneficiary, as is generally consistent with the experience since 1987. Between 1987 and 2015, the average annual growth rate of outlays per beneficiary for Medicaid and Medicare were within 0.2 percentage point of each other. Projections of Medicaid spending are subject to added uncertainty related to: (1) assumed reductions in health care cost growth discussed above in the context of Medicare, and (2) the projected size of the Medicaid enrolled population, which depends on a variety of factors, including the future extent of the ACA Medicaid expansion.
- **Other Mandatory Spending:** Other mandatory spending, which includes Federal employee retirement, veterans' disability benefits, and means-tested entitlements other than Medicaid, is projected in two steps. First, spending prior to the automatic spending cuts called for by the enforcement provisions of the *Budget Control Act* (BCA) is projected and, second, the effect of the BCA enforcement is projected through 2025. With regard to pre-BCA spending: (a) Current mandatory spending components that are judged permanent under current policy are assumed to increase by the rate of growth in nominal GDP starting in 2017, implying that such spending will remain constant as a percentage of GDP[20]; and (b) Projected spending for insurance exchange subsidies starting in 2017 grows with growth in the non-elderly population and with the National Health Expenditure (NHE) projected per enrollee cost growth for other private health insurance for the NHE projection period (through 2025 for the fiscal year 2016 projections), and with growth in per enrollee health care costs as projected for the Medicare program after that period. As discussed in Note 22, there is uncertainty about whether the reductions in health care cost growth projected in the Medicare trustees' report will be fully achieved. Exchange subsidy spending as a percentage of GDP remains below the failsafe provision in the ACA that limits this spending to 0.504 percent of GDP.

[18] Medicare Part B and D premiums and State contributions to Part D are subtracted from the Part B and D spending displayed in the basic financial statement. The total 75-year present value of these subtractions is $12.1 trillion, or 0.9 percent of GDP.

[19] Christopher J. Truffer, Christian J. Wolfe, and Kathryn E. Rennie, *2015 Actuarial Report on the Financial Condition for Medicaid*, Office of the Actuary, Centers for Medicare and Medicaid Services, United States Department of Health and Human Services, December 2015.

[20] This assumed growth rate for other mandatory programs exceeds the growth rate in the most recent OMB and CBO 10-year budget baselines.

- **Defense and Non-defense Discretionary Spending:** Through 2021, discretionary spending other than for Overseas Contingency Operations (OCO) is dictated by the spending caps and automatic spending cuts called for by the BCA. After 2021, this spending is assumed to grow at the same rate as nominal GDP, and thus plateaus at a long-term level of 5.0 percent of GDP. The BCA is projected to reduce the present value of spending by $0.3 trillion through 2021, and by an additional $4.3 trillion between 2022 and 2091 because of the lower base spending in 2021. Projected OCO spending steadily declines and is fully phased out after 2026, and amounts to $0.1 trillion in present value. To illustrate uncertainty, present value calculations under alternative discretionary growth scenarios are presented in the "Alternative Scenarios" RSI section.
- **Receipts (Other than Social Security and Medicare):** It is assumed that individual income taxes will equal the same share of wages and salaries as in the Administration's latest Budget current law baseline projection. That baseline accords with current policy as defined above, and incorporates the effects of the economic recovery and bracket creep. After reaching about 22 percent of wages and salaries in 2024, individual income taxes increase gradually to 28 percent of wages and salaries in 2091 as real taxable incomes rise over time and an increasing share of total income is taxed in the higher tax brackets. The ratio of all other receipts combined to GDP is projected to remain at 3.6 percent of GDP, based on a long-run historical average. To illustrate uncertainty, present value calculations under higher and lower receipts growth scenarios are presented in the "Alternative Scenarios" section.
- **Debt and Interest Spending:** Interest spending is determined by projected interest rates and the level of outstanding debt held by the public. The long-run interest rate assumptions accord with those in the 2016 Social Security trustees' report.[21] The average interest rate over the projection period is 5.1 percent. These rates are also used to convert future cash flows to present values as of the start of fiscal year 2017. Debt at the end of each year is projected by adding that year's deficit and other financing requirements to the debt at the end of the previous year.

The methods described above include several refinements from those used to produce the fiscal year 2015 projections. First, automatic spending cuts due to BCA enforcement are no longer assumed to be extended past their statutory expiration date. Even though these enforcement mechanisms have been extended several times in recent years, these extensions have been enacted as savings measures to offset increases to the discretionary spending caps. Second, the Medicaid projections are refined by recognizing the differences in per capita costs of different beneficiary categories, such as the aged and disabled populations.

Departures of Current Policy from Current Law

The long-term fiscal projections are made on the basis of current Federal policy, which in some cases is different from current law. The notable differences between current policy that underlies the projections and current law are: (1) projected spending and receipts imply violation of the current statutory limit on Federal debt, (2) continued discretionary appropriations are assumed throughout the projection period, (3) scheduled Social Security and Medicare benefit payments are assumed to occur beyond the projected point of trust fund exhaustion, and (4) many mandatory programs with expiration dates prior to the end of the 75-year projection period are assumed to be reauthorized. As is true in the Medicare trustees' report and in the Statement of Social Insurance, the projections incorporate programmatic changes already scheduled in law, such as the ACA productivity adjustment for non-physician Medicare services.

[21] As indicated in the more detailed discussion of Social Insurance in Note 22 to the financial statements.

Note 24. Stewardship Land and Heritage Assets

Stewardship land is federally-owned land set aside for the use and enjoyment of present and future generations, and land on which military bases are located. Except for military bases, this land is not used or held for use in general government operations. Stewardship land is land that the government does not expect to use to meet its obligations, unlike the assets listed in the Balance Sheets. Stewardship land is measured in non-financial units such as acres of land and lakes, and the number of National Parks and National Marine Sanctuaries. Examples of stewardship land include national parks, national forests, wilderness areas, and land used to enhance ecosystems for the encouragement of animal and plant species, and nature conservation. This category excludes lands administered by the Bureau of Indian Affairs and held in trust.

The majority of public lands that are under the management of DOI were acquired by the government during the first century of the Nation's existence between 1781 and 1867.

Stewardship land is used and managed in accordance with the statutes authorizing acquisition or directing use and management. Additional detailed information concerning stewardship land, such as agency stewardship policies, physical units by major categories, and the condition of stewardship land, can be obtained from the financial statements of DOI, DOD, DOE, HHS, TVA, and USDA.

Heritage assets are government-owned assets that have one or more of the following characteristics:

- Historical or natural significance;
- Cultural, educational, or artistic importance; and/or
- Significant architectural characteristics

The cost of heritage assets often is not determinable or relevant to their significance. Like stewardship land, the government does not expect to use these assets to meet its obligations. The most relevant information about heritage assets is non-financial. The public entrusts the government with these assets and holds it accountable for their preservation. Examples of heritage assets include the Mount Rushmore National Memorial and Yosemite National Park. Other examples of heritage assets include the Declaration of Independence, the U.S. Constitution, and the Bill of Rights preserved by the National Archives. Also included are national monuments/structures such as the Vietnam Veterans Memorial, the Jefferson Memorial, and the Washington Monument, as well as the Library of Congress. Many other sites such as battlefields, historic structures, and national historic landmarks are placed in this category, as well.

Many laws and regulations govern the preservation and management of heritage assets. Established policies by individual federal agencies for heritage assets ensure the proper care and handling of the assets under their control and preserve these assets for the benefit of the American public.

Some heritage assets are used both to remind us of our heritage and for day-to-day operations. These assets are referred to as multi-use heritage assets. One typical example is the White House. The cost of acquisition, betterment, or reconstruction of all multi-use heritage assets is capitalized as general Property, Plant, and Equipment (PP&E) and is depreciated.

The government classifies heritage assets into two broad categories: collection type and non-collection type. Collection type heritage assets include objects gathered and maintained for museum and library collections. Non-collection type heritage assets include national wilderness areas, wild and scenic rivers, natural landmarks, forests, grasslands, historic places and structures, memorials and monuments, buildings, national cemeteries, and archeological sites.

This discussion of the government's heritage assets is not exhaustive. Rather, it highlights significant heritage assets reported by federal agencies. Please refer to the individual financial statements of the DOC, VA, DOT, State, DOD, as well as websites for the Library of Congress (http://loc.gov), the Smithsonian Institution (http://si.edu), and the Architect of the Capitol (http://aoc.gov) for additional information on multi-use heritage assets, agency stewardship policies, and physical units by major categories.

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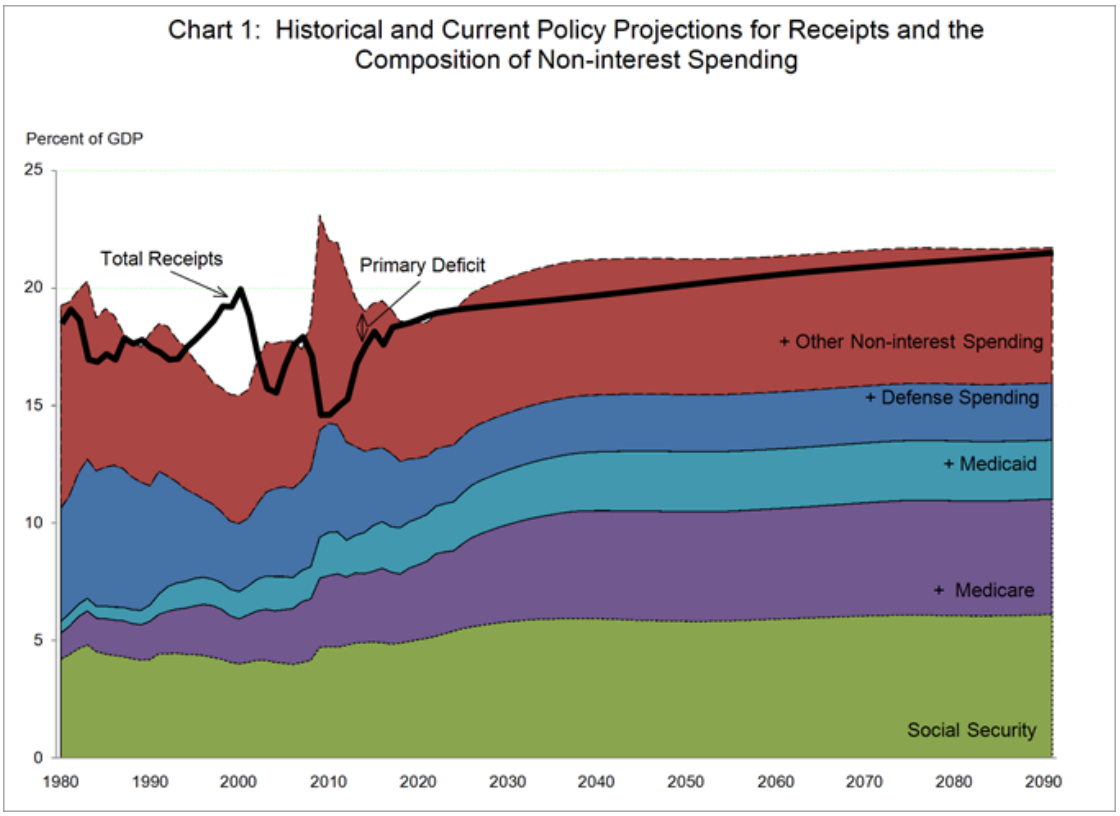
United States Government Required Supplementary Information (Unaudited) For the Years Ended September 30, 2016, and 2015

The Sustainability of Fiscal Policy

One of the important purposes of the *Financial Report* is to help citizens and policymakers assess whether current fiscal policy is sustainable and, if it is not, the urgency and magnitude of policy reforms necessary to make fiscal policy sustainable. A sustainable policy is one where the ratio of debt held by the public to GDP (the debt-to-GDP ratio) is ultimately stable or declining.

As discussed below, the projections in this report indicate that current policy is not sustainable. If current policy is left unchanged, the projections show the debt-to-GDP ratio will fall about 6 percentage points between 2016 and 2024 before commencing a steady rise, exceeding its 2016 level by 2030, exceeding 100 percent by 2039, and reaching 252 percent in 2091. For comparison, under the 2015 projections, the debt-to-GDP ratio fell about 6 percentage points between 2015 and 2025 before commencing a steady rise, exceeding the 2015 level (74 percent) by 2031, exceeding 100 percent by 2043, and reaching 223 percent in 2090.

These conclusions are rooted in the projected trends in receipts, spending, and surpluses/deficits in the context of current law and policy, although, as described in the following pages, there is considerable uncertainty surrounding these projections. The projections are on the basis of policies currently in place and are neither forecasts nor predictions.



Current Policy Projections for Primary Deficits

A key determinant of growth in the debt-to-GDP ratio and hence fiscal sustainability is the primary deficit-to-GDP ratio. The primary deficit is the difference between non-interest spending and receipts, and the primary deficit-to-GDP ratio is the primary deficit expressed as a percent of GDP. As shown in Chart 1, the primary deficit-to-GDP ratio grew rapidly in 2009 due to the financial crisis and the recession and the policies pursued to combat both. The ratio remained high from 2010 to 2012 despite shrinking in each successive year, and fell significantly in 2013 and 2014. The primary deficit is projected to shrink in the next few years as the discretionary spending limits called for in the *Budget Control Act of 2011* (BCA) remain in effect and the economy continues to recover. Starting in 2020, receipts are projected to exceed non-interest spending, and this primary surplus is projected to peak at 0.3 percent of GDP in 2021. After 2022, however, increased spending for Social Security and health programs due in part to the continued retirement of the baby boom generation is expected to cause the primary surplus to steadily deteriorate and become a primary deficit in 2025 that reaches 1.0 percent of GDP in 2029. The primary deficit peaks at 1.6 percent of GDP in 2038, gradually decreases beyond that point as the aging of the population continues at a slower pace, and reaches 0.2 percent in 2091.

The receipt share of GDP fell substantially in 2009 and 2010 and remained low in 2011 and 2012 because of the recession and tax reductions enacted as part of the *2009 American Recovery and Reinvestment Act* (ARRA) and the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010*. The share was 17.6 percent in 2016, exceeding its 30-year average of 17.3 percent due to continued economic growth and the higher tax rates enacted under the *American Tax Relief Act* (ATRA) *of 2012*. Receipts are projected to grow slightly more rapidly than GDP as increases in real (i.e., inflation-adjusted) incomes cause more taxpayers and a larger share of income to fall into the higher individual income tax brackets. Other possible paths for the receipts-to-GDP ratio and the implications for projected debt are analyzed in the "Alternative Scenarios" section.

On the spending side, the non-interest spending share of GDP is projected to stay at or below its current level of about 19 percent until 2026, and to then rise gradually to 21.2 percent of GDP by 2041 and 21.7 percent of GDP by 2091. The reductions in the non-interest spending share of GDP over the next few years are mostly due to the expected reductions in spending for overseas contingency operations (OCO), caps on discretionary spending and the automatic spending cuts mandated by the BCA, and the subsequent increases are principally due to faster growth in Medicare, Medicaid, and Social Security spending (see Chart 1). The aging of the baby boom generation over the next 25 years, among other factors, is projected to increase the Social Security, Medicare, and Medicaid spending shares of GDP by about 1.1 percentage points, 1.6 percentage points, and 0.6 percentage points, respectively. After 2041, the Social Security spending share of GDP remains relatively stable, while the combined Medicare and Medicaid spending share of GDP continues to increase, albeit at a slower rate, due to projected increases in health care costs.

The *Patient Protection and Affordable Care Act*, as amended by the *Health Care and Education Reconciliation Act of 2010* (ACA), significantly affects projected spending for both Medicare and Medicaid. That legislation expands health insurance coverage, including Medicaid, includes many measures designed to reduce health care cost growth, and significantly reduces Medicare payment rates. On net, the ACA is projected to substantially reduce the annual increases in Medicare payment rates over the next 75 years. The Medicare spending projections in the long-term fiscal projections are based on the projections in the 2016 Medicare trustees' report, and those projections show a substantial slowdown in Medicare cost growth. The projections assume that Medicaid enrollment increases in line with demographic trends and that Medicaid cost per beneficiary grows at the same reduced rate as Medicare cost growth per beneficiary. As discussed in Note 22 to the U.S. Government's Financial Statements, these projections are subject to much uncertainty about the ultimate effects of the ACA's provisions to reduce health care cost growth. Even if those provisions work as intended and as assumed in this projection, Chart 1 shows that there is still a long-term gap between projected receipts and projected total non-interest spending.

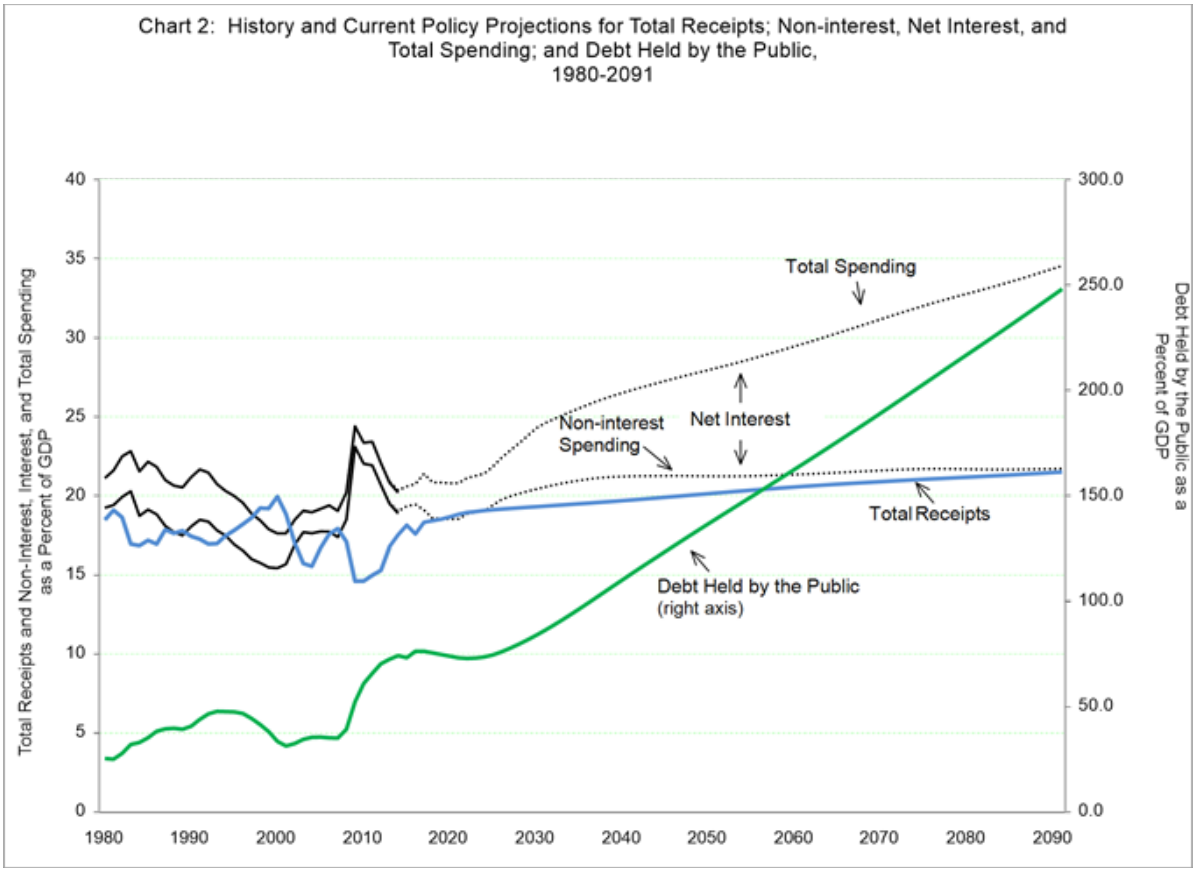
Current Policy Projections for Debt and Interest Payments

The primary deficit projections in Chart 1, along with projections for interest rates and GDP, determine the projections for the debt-to-GDP ratio that are shown in Chart 2 (right axis). That ratio was 77 percent at the end of fiscal year 2016. Under current policy the ratio is projected to be 71 percent in 2026, 122 percent in 2046, and 252 percent in 2091. The continuous rise of the debt-to-GDP ratio after 2026 indicates that current policy is unsustainable.

The change in debt held by the public from one year to the next is approximately equal to the unified budget deficit, the difference between total spending and total receipts.[1] Total spending is non-interest spending plus interest spending. Chart 2 (left axis) shows that the rapid rise in total spending and the unified deficit is almost entirely due to projected interest

[1] The change in debt each year is also affected by certain transactions not included in the unified budget deficit, such as changes in Treasury's cash balances and the non-budgetary activity of Federal credit financing accounts. These transactions are assumed to hold constant at about 0.4 percent of GDP each year, with the same effect on debt as if the primary deficit was higher by that amount.

payments on the growing debt. As a percent of GDP, interest spending was 1.3 percent in 2016, and under current policy is projected to reach 4.7 percent in 2036 and 12.8 percent in 2091.



Another way of viewing the change in the financial outlook in this year's report relative to previous years' reports is in terms of the projected debt-to-GDP ratio in 2089, the last year of the projection period in the FY 2014 report. This ratio is projected to reach 246 percent in the fiscal year 2016 projections, which compares with 220 percent projected in the fiscal year 2015 projections and 321 percent projected in the fiscal year 2014 projections.[2]

The Cost of Delay in Closing the 75-Year Fiscal Gap

The longer policy action to close the fiscal gap is delayed, the larger the post reform primary surpluses must be to achieve the target debt-to-GDP ratio at the end of the 75-year period. This can be illustrated by varying the years in which reforms closing the fiscal gap are initiated while holding the ratio of debt to GDP in 2091 equal to its level in 2016. Three reforms are considered, each one beginning in a different year, and each one increasing the primary surplus relative to current policy by a fixed percent of GDP starting in the reform year. The analysis shows that the longer policy action is delayed, the larger the post-reform primary surplus must be to bring the debt-to-GDP ratio to the target level in 2091. Future generations are harmed by delays in policy changes because delay necessitates higher primary surpluses during their lifetimes, and those higher primary surpluses must be achieved through some combination of lower spending and higher taxes and other receipts.

As previously shown in Chart 1, under current policy, primary deficits occur in much of the projection period. Table 1 shows primary surplus changes necessary to make the debt-to-GDP ratio in 2091 equal to its level in 2016 under each of the three policies. If reform begins in 2017, then it is sufficient to raise the primary surplus share of GDP by 1.6 percentage points in every year between 2017 and 2091 in order for the debt-to-GDP ratio in 2091 to equal its level in 2016. This policy raises the average 2017-2091 primary surplus-to-GDP ratio from -0.8 percent to +0.8 percent.

[2] For further information on changes from the 2014 projections, see Note 24 in the 2015 *Financial Report*.

Table 1
Costs of Delaying Fiscal Reform

Timing of Reforms	Required Change in Average Primary Surplus
Reform in 2017 (No Delay)	1.6 percent of GDP between 2017 and 2091
Reform in 2027 (Ten-Year Delay)	1.9 percent of GDP between 2027 and 2091
Reform in 2037 (Twenty-Year Delay) ...	2.4 percent of GDP between 2037 and 2091

Note: Reforms taking place in 2016, 2026, and 2036 from the 2015 Financial Report were 1.2, 1.5, and 1.9 percent of GDP, respectively.

In contrast to a reform that begins immediately, if reform begins in 2027 or 2037, then the primary surpluses must be raised by 1.9 percent and 2.4 percent of GDP, respectively, in order for the debt-to-GDP ratio in 2091 to equal its level in 2016. The difference between the primary surplus increase necessary if reform begins in 2027 and 2037 (1.9 and 2.4 percent of GDP, respectively) and the increase necessary if reform begins in 2017 (1.6 percent of GDP) is a measure of the additional burden policy delay would impose on future generations. The costs of delay are due to the additional debt that accumulates between 2016 and the year reform is initiated, in comparison to the scenario in which reform begins immediately.

These projections likely understate the cost of lengthy policy delays because they assume interest rates will not rise as the debt-to-GDP ratio grows. Under the current projections, the debt-to-GDP ratio is stable through 2025 and then grows rapidly. If a higher debt-to-GDP ratio causes the interest rate on government borrowing to rise, thus making it more costly for the government to service its debt and simultaneously slowing private investment, then the primary surplus required to return the debt-to-GDP ratio to its 2016 level would also increase. This dynamic may accelerate with higher ratios of debt to GDP, potentially resulting in there being no feasible level of taxes and spending that would reduce the debt-to-GDP ratio to its 2016 level. The potential impact on the projections of interest rates rising as the debt-to-GDP ratio rises is explored in the "Alternative Scenarios" section.

Alternative Scenarios

The long-run outlook for the budget is extremely uncertain. This section illustrates this inherent uncertainty by presenting alternative scenarios for the growth rate of health care costs, interest rates, discretionary spending, and receipts. (Not considered here are the effects of alternative assumptions for long-run trends in birth rates, mortality, and immigration.)

The population is aging rapidly and will continue to do so over the next several decades, which puts pressure on programs such as Social Security, Medicare, and Medicaid. A shift in projected fertility, mortality, or immigration rates could have important effects on the long-run projections. Higher-than-projected immigration, fertility, or mortality rates would improve the long-term fiscal outlook. Conversely, lower-than-projected immigration, fertility, or mortality rates would result in deterioration in the long-term fiscal outlook.

Effect of Changes in Health Care Cost Growth

One of the most important assumptions underlying the projections is the projected growth of health care costs. Enactment of the ACA in 2010 reduced the projected long-run growth rates of health care costs, but these growth rates are still highly uncertain. As an illustration of the dramatic effect of variations in health care cost growth rates, Table 2 shows the effect on the size of reforms necessary to close the fiscal gap of per capita health care cost growth rates that are one percentage point higher or two percentage points higher than the growth rates in the base projection, as well as the effect of delaying closure of the fiscal gap.[3] As indicated earlier, if reform is initiated in 2017, eliminating the fiscal gap requires that the 2017-2091 primary surplus increase by an average of 1.6 percent of GDP in the base case. However, that figure increases to 4.6 percent of GDP if per capita health cost growth is assumed to be 1 percentage point higher, and 9.6 percent of GDP if per capita health cost growth is 2 percentage points higher. The cost of delaying reform is also increased if health care cost growth is higher, due to the fact that debt accumulates more rapidly during the period of inaction. For example, the lower part

[3] The base case health cost growth rates are derived from the projections in the 2016 Medicare trustees' report. These projections are summarized and discussed in Note 22 (see Table 1B in particular) and the "Medicare Projections" section of the RSI for the SOSI.

of Table 2 shows that delaying reform initiation from 2017 to 2027 requires that 2027-2091 primary surpluses be higher by an average of 0.3 percent of GDP in the base case, 0.9 percent of GDP if per capita health cost growth is 1 percentage point higher, and 1.8 percent of GDP if per capita health cost growth is 2 percentage points higher. The dramatic deterioration of the long-run fiscal outlook caused by higher health care cost growth shows the critical importance of managing health care cost growth, including through effective implementation of the ACA.

Table 2
Impact of Alternative Health Cost Scenarios on Cost of Delaying Fiscal Reform

	Primary Surplus Increase (% of GDP) Starting in:		
Scenario	**2017**	**2027**	**2037**
Base Case	1.6	1.9	2.4
1% pt. higher per person health cost growth	4.6	5.5	6.9
2% pt. higher per person health cost growth	9.6	11.4	14.1

	Change in Primary Surplus Increase if Reform is Delayed From 2016 to:	
	2027	**2037**
Base Case	0.3	0.8
1% pt. higher per person health cost growth	0.9	2.2
2% pt. higher per person health cost growth	1.8	4.6

NOTE: Increments may not equal the subtracted difference of the components due to rounding.

Effects of Changes in Interest Rates

A higher debt-to-GDP ratio is likely to increase the interest rate on Government debt, making it more costly for the Government to service its debt. Table 3 displays the effect of several alternative scenarios using different nominal (and real) interest rates than assumed in the base case on the size of reforms to close the fiscal gap as well as the effect of delaying closure of the fiscal gap. If reform is initiated in 2017, eliminating the fiscal gap requires that the 2017-2091 primary surplus increase by an average of 1.6 percent of GDP in the base case, 1.9 percent of GDP if the interest rate is 0.5 percentage point higher in every year, and 1.3 percent of GDP if the interest rate is 0.5 percentage point lower in every year. The cost of delaying reform is also increased if interest rates are higher, due to the fact that interest paid on debt accumulates more rapidly during the period of inaction. For example, the lower part of Table 3 shows that delaying reform initiation from 2017 to 2027 requires that 2027-2091 primary surpluses be higher by an average of 0.3 percent of GDP in the base case, 0.4 percent of GDP if the interest rate is 0.5 percentage point higher in every year, and 0.2 percent of GDP if the interest rate is 0.5 percentage point lower in every year.

Table 3
Impact of Alternative Interest Rate Scenarios on Cost of Delaying Fiscal Reform

	Primary Surplus Increase (% of GDP) Starting in:		
Scenario	**2017**	**2027**	**2037**
Base Case: Average of 5.4 percent over 75 years	1.6	1.9	2.4
0.5 percent higher interest rate in each year	1.9	2.3	3.0
0.5 percent lower interest rate in each year	1.3	1.5	1.8

	Change in Primary Surplus Increase if Reform is Delayed From 2016 to:	
	2027	**2037**
Base Case: Average of 5.4 percent over 75 years	0.3	0.8
0.5 percent higher interest rate in each year	0.4	1.1
0.5 percent lower interest rate in each year	0.2	0.5

NOTE: Increments may not equal the subtracted difference of the components due to rounding.

Effects of Changes in Discretionary Spending Growth

The growth of discretionary spending has a large impact on long-term fiscal sustainability. The current base projection for discretionary spending assumes that after 2021, discretionary spending keeps pace with the economy and grows with GDP. The implications of two alternative scenarios are shown in Table 4. The first alternative scenario allows discretionary spending to grow with inflation and population after 2021 so as to hold discretionary spending constant on a real per capita basis. (This growth rate assumption is still larger than the standard 10-year budget baseline assumption, which assumes that discretionary spending grows with inflation but not with population.) The second alternative scenario sets discretionary spending in 2022 to levels consistent with the path established prior to the sequestration required by the failure of the Joint Select Committee on Deficit Reduction, and then grows discretionary spending with GDP from that point forward. As shown in Table 4, the fiscal gap is eliminated if discretionary spending grows with inflation and population. Conversely, if discretionary spending rises to the levels prior to Joint Committee sequestration in 2022 and then grows with GDP, the fiscal gap increases from 1.6 percent of GDP to 1.9 percent of GDP. The cost of delaying reform is greater when discretionary spending levels are higher. Initiating reforms in 2027 requires that the primary surplus increase by an average of 0.3 percent of GDP per year in the base case, and also increase by 0.4 percent of GDP if discretionary levels return to pre-Joint Committee sequestration levels. If delayed until 2037, the primary surplus must increase by an average of 0.8 percent of GDP in the base case, and increase by 0.9 percent of GDP at pre-sequestration levels.

Table 4
Impact of Alternative Discretionary Spending Growth Scenarios on Cost of Delaying Fiscal Reform

Scenario	Primary Surplus Increase (% of GDP) Starting in: 2017	2027	2037
Base Case: Discretionary spending growth with GDP after 2021	1.6	1.9	2.4
Growth with inflation and population after 2021	-	(0.1)	(0.1)
Reversion in 2022 to pre-Joint Committee sequester levels and growth with GDP	1.9	2.3	2.8

	Change in Primary Surplus Increase if Reform is Delayed From 2017 to: 2027	2037
Base Case: Discretionary spending growth with GDP after 2021	0.3	0.8
Growth with inflation and population after 2021	(0.1)	(0.1)
Reversion in 2022 to pre-Joint Committee sequester levels and growth with GDP	0.4	0.9

NOTE: Increments may not equal the subtracted difference of the components due to rounding.

Effects of Changes in Individual Income Receipt Growth

The growth rate of receipts, specifically individual income taxes, is another key determinant of long-term sustainability. The base projections assume growth in individual income taxes over time to account primarily for the slow shift of individuals into higher tax brackets due to real wage growth ("real bracket creep"). This assumption approximates the long-term historical growth in individual income taxes relative to wages and salaries and is consistent with current tax code policy without change, as future legislation would be required to prevent real bracket creep. As an illustration of the effect of variations in individual income tax growth, Table 5 shows the effect on the size of reforms necessary to close the fiscal gap and the effect of delaying closure of the fiscal gap if long-term receipt growth as a share of wages and salaries is 0.1 percentage point higher, than the base case, as well as 0.1 percentage point lower than the base case. If reform is initiated in 2017, eliminating the fiscal gap requires that the 2017-2091 primary surplus increase by an average of 1.6 percent of GDP in the base case, only 0.5 percent of GDP if receipt growth is 0.1% higher, but 2.7 percent of GDP if receipt growth is 0.1% lower. The cost of delaying reform is also affected if receipt growth assumptions change, much as was the case in the previous alternative scenarios.

Table 5
Impact of Alternative Revenue Growth Scenarios on Cost of Delaying Fiscal Reform

Scenario	Primary Surplus Increase (% of GDP) Starting in: 2017	2027	2037
Base Case: Individual income tax bracket creep of 0.1% of wages and salaries per year	1.6	1.9	2.4
0.2% of wages and salaries per year after 2025	0.5	0.6	0.7
0.0% of wages and salaries per year after 2025 (no bracket creep)	2.7	3.2	4.0

	Change in Primary Surplus Increase if Reform is Delayed From 2017 to: 2027	2037
Base Case: Individual income tax bracket creep of 0.1% of wages and salaries per year	0.3	0.8
0.2% of wages and salaries per year after 2025	0.1	0.2
0.0% of wages and salaries per year after 2025 (no bracket creep)	0.5	1.3

NOTE: Increments may not equal the subtracted difference of the components due to rounding.

Fiscal Projections in Context

In this report, a sustainable policy has been defined as one where the Federal debt-to-GDP ratio is stable or declining. However, this definition does not indicate what a sustainable debt-to-GDP ratio might be. Any particular debt ratio is not the ultimate goal of fiscal policy. Rather, the goals of fiscal policy are many, including: financing public goods, such as infrastructure and government services; a strong and growing economy; and managing the national debt so that it is not a burden to future generations. These goals are interrelated, and readers should consider how policies intended to affect one might depend on or affect another.

This report shows that current policy is not sustainable. In evaluating policies that could make policy sustainable, note that national debt may play roles in both facilitating and hindering a healthy economy. For example, Government deficit spending may support demand and allow economies to emerge from recessions more quickly. Debt may also be a cost-effective means of financing capital investment, promoting economic growth, which may in turn make debt levels more manageable in the future. However, economic theory also suggests that high levels of national debt may contribute to higher interest rates, leading to lower investment and a smaller capital stock which the economy can use to grow. Unfortunately, it is unclear what debt-to-GDP ratio would be sufficiently high to produce these negative outcomes, or whether the key concern is the level of debt per se, or a trend that shows debt increasing over time.

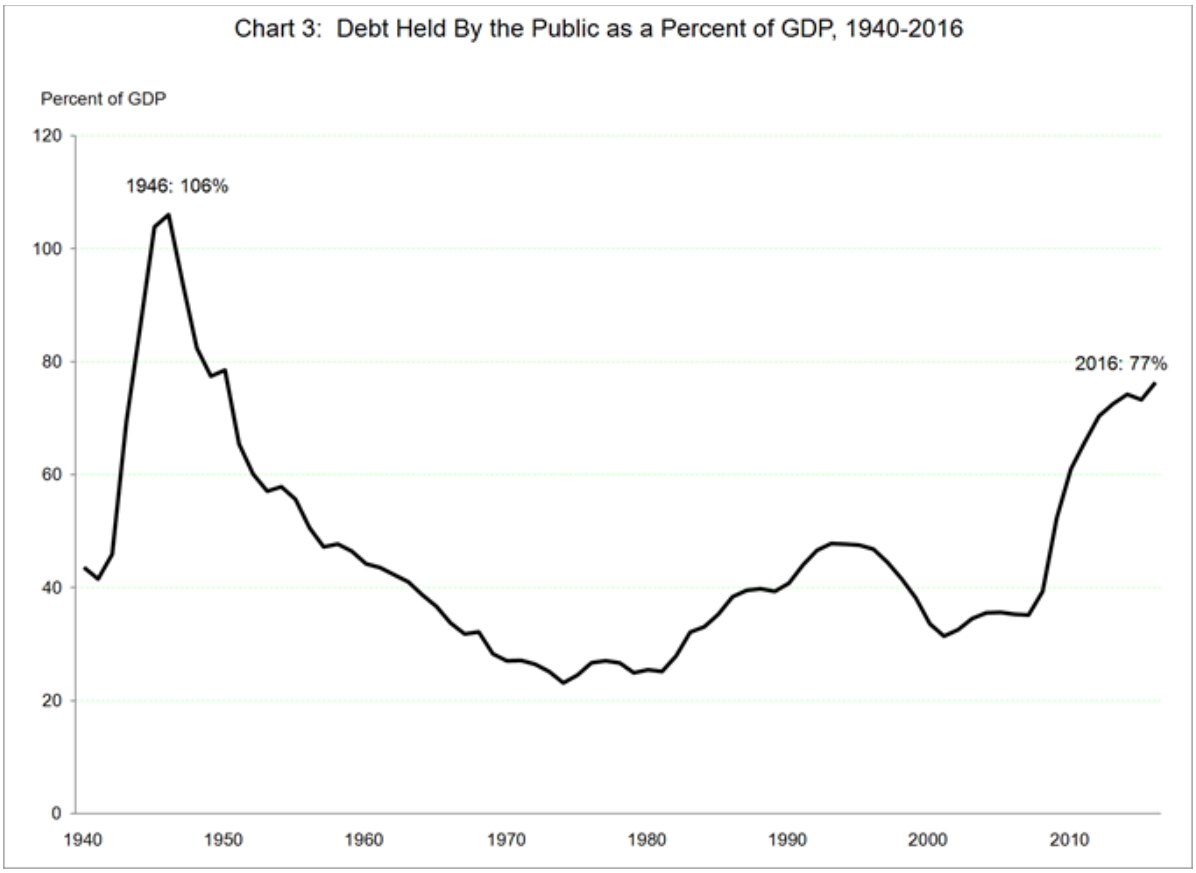
It is difficult to discern a definite relationship between national debt and economic growth from the past experience of countries. The historical experience, while valuable, is filled with confounding events and circumstances. Some countries with high debt-to-GDP ratios have been observed to experience lower-than-average growth, while other countries with similarly high debt ratios continue to enjoy robust growth. Analogously, low debt-to-GDP ratios are no guarantee of strong economic growth. Moreover, the direction of causality is unclear. High debt may undermine growth; low growth may contribute to high debt.

Nevertheless, to put the current and projected debt-to-GDP ratios in context, it is instructive to examine how the United States experience compares with that of other countries. The United States Government's debt as a percentage of GDP is relatively large compared with central government debt of other countries, but far from the largest among developed

countries. Based on historical data as reported by the International Monetary Fund (IMF) for 27 select countries, the debt-to-GDP ratio in 2014 ranged from 14 percent of GDP to 199 percent of GDP.[4] The United States is not included in this set of statistics, which underscores the difficulty in calculating debt ratios under consistent definitions, but the IMF does report a similar debt statistic for the United States as 83 percent of GDP.[5] Despite using consistent definitions where available, these debt measures are not strictly comparable due to differences in the share of government debt that is debt of the central government, how government responsibilities are shared between central and local governments, how current policies compare with the past policies that determine the current level of debt, and how robustly each economy grows.

The historical experience of the U.S. may also provide some perspective. As Chart 3 shows, the debt-to-GDP ratio was highest in the 1940s, following the debt buildup during World War II. In the projections in this report, the U.S. would reach the previous peak debt ratio in 2041. However, the origins of current and future Federal debt are quite different from the wartime debt of the 1940s, which limits the pertinence of past experience.

As the cross-country and historical comparisons suggest, there is a very imperfect relationship between the current level of central government debt and the sustainability of overall government policy. Past accrual of debt is certainly important, but current policies and their implications for future debt accumulation are as well. The U.S. has made progress towards sustainability in recent years. The projections in this *Financial Report* show the relative stability in the U.S. Federal debt-to-GDP ratio for the next decade under current policies, followed by a rising trend that implies current policies are unsustainable in the long run.



[4] Government Finance Statistics Yearbook, Main Aggregates and Balances, available at http://data.imf.org. Data is for D1 debt liabilities for the central government, excluding social security funds.

[5] Data is for D1 debt liabilities for the central government, including social security funds. For the few countries where both central government debt ratios (excluding and including social security funds) are reported, the values are similar.

Conclusion

The United States took a potentially significant step towards fiscal sustainability in 2010 by reforming its system of health insurance through enactment of the ACA. The legislated changes for Medicare, Medicaid, and other health coverage hold the prospect of lowering the long-term growth trend for health care costs and significantly reducing the long-term fiscal gap. Furthermore, enactment of the BCA in August 2011 placed limits on future discretionary spending, while enactment of ATRA in January 2013 increased receipts under current policy. With these laws in place, the debt-to-GDP ratio is projected to remain relatively stable for the next decade. However, the projections beyond the next decade in this *Financial Report* indicate that if policy remains unchanged the debt-to-GDP ratio will continually increase over the next 75 years and beyond, which implies current policies are not sustainable and must ultimately change. Subject to the important caveat that policy changes are not so abrupt that they slow continued economic growth, the sooner policies are put in place to avert these trends, the smaller are the receipt increases and/or spending decreases necessary to return the Nation to a sustainable fiscal path, and the lower the burden of the national debt will be to future generations.

Social Insurance

The social insurance programs consisting of Social Security, Medicare, Railroad Retirement, and Black Lung were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the Government. Because taxpayers rely on these programs in their long-term planning, social insurance program information should indicate whether the current statutory provisions of the programs can be sustained, and more generally what effect these provisions likely have on the Government's financial condition. The resources needed to run these programs are raised through taxes and fees. Eligibility for benefits depends in part on earnings and time worked by the individuals. Social Security benefits are generally redistributed intentionally toward lower-wage workers (i.e., benefits are progressive). In addition, each social insurance program has a uniform set of eligibility events and schedules that apply to all participants.

Social Security and Medicare

Social Security

The Federal Old Age and Survivors Insurance (OASI) Trust Fund was established on January 1, 1940, as a separate account in the Treasury. The Federal Disability Insurance (DI) Trust Fund, another separate account in the Treasury, was established on August 1, 1956. The OASI fund pays cash retirement benefits to eligible retirees and their eligible dependents and survivors, and the much smaller DI fund pays cash benefits to eligible individuals who are unable to work because of medical conditions and certain family members of such eligible individuals. Though the events that trigger benefit payments are quite different, both trust funds have the same dedicated financing structure: primarily payroll taxes and income taxes on benefits. All financial operations of the OASI and DI Programs are handled through these respective funds. The two funds are often referred to as the combined OASDI Trust Funds. At the end of calendar year 2015, OASDI benefits were paid to approximately 60 million beneficiaries.

The primary financing source for these two funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Since 1990, with the exception of calendar years 2011 and 2012, employers and employees have each paid 6.2 percent of taxable earnings, and the self-employed have paid 12.4 percent of taxable earnings. In 2011 and 2012, payroll tax rates paid by employees and the self-employed were each reduced by 2 percentage points and the General Fund reimbursed the OASDI Trust Fund for the resulting reduction in payroll tax revenues. Payroll taxes are levied on wages and net earnings from self-employment up to a specified maximum annual amount, referred to as maximum taxable earnings ($118,500 in 2016), that increases each year with economy-wide average wages.

Legislation passed in 1984 subjected up to half of OASDI benefits to income tax and allocated the revenue to the OASDI Trust Funds. In 1993 legislation increased the potentially taxed portion of benefits to 85 percent and allocated the additional revenue to the Medicare's Hospital Insurance Trust Fund.

Medicare

The Medicare Program, created in 1965, has two separate trust funds: the Hospital Insurance (HI) Trust Fund (otherwise known as Medicare Part A) and the Supplementary Medical Insurance (SMI) Trust Funds (which consists of the Medicare Part B and Part D[6] accounts). HI pays for acute inpatient hospital services, hospice, and major alternatives to hospitals (skilled nursing services, for example). SMI pays for hospital outpatient services, physician services, and assorted other services and products through the Part B account and for prescription drugs through the Part D account.

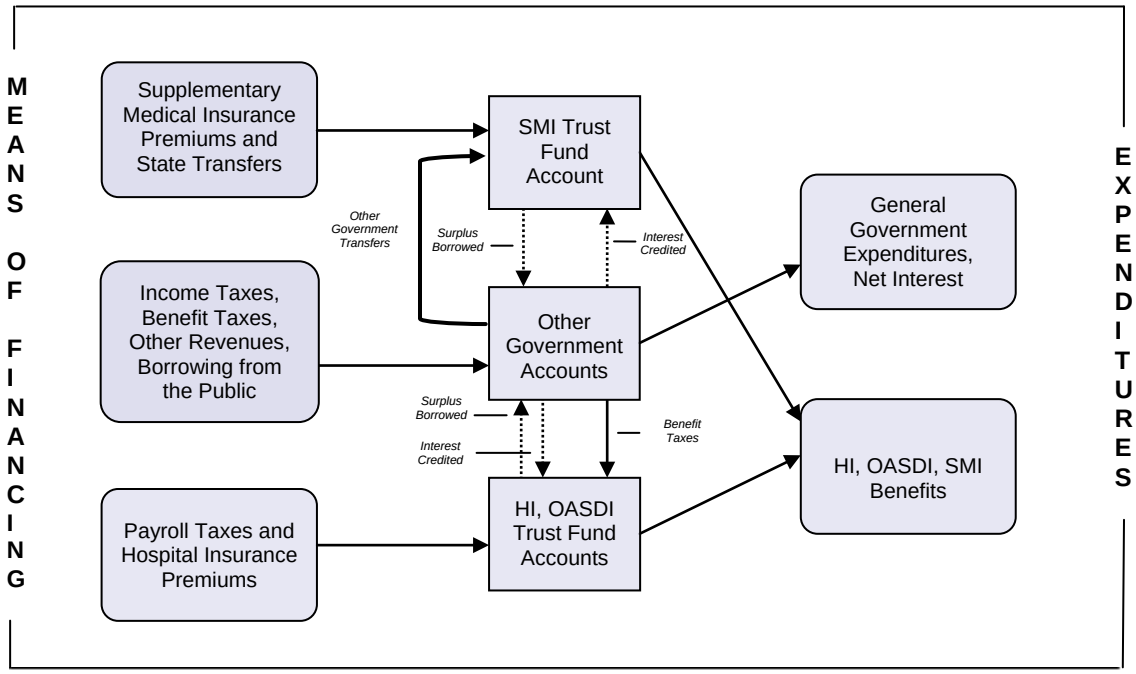
Though the events that trigger benefit payments are similar, HI and SMI have different dedicated financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Currently, employers and employees each pay 1.45 percent of earnings, while self-employed workers pay 2.9 percent of their net earnings. Beginning in 2013, employees and self-employed individuals with earnings above certain thresholds pay an additional HI tax of 0.9 percent on earnings above those thresholds. Other income to the HI Trust Fund includes a small amount of premium income from voluntary enrollees, a portion of the federal income taxes that beneficiaries pay on Social Security benefits (as explained above), and interest

[6] Medicare legislation in 2003 created the new Part D account in the SMI Trust Fund to track the finances of a new prescription drug benefit that began in 2006. As in the case of Medicare Part B, approximately three-quarters of revenues to the Part D account will come from future transfers from the General Fund. Consequently, the nature of the relationship between the SMI Trust Fund and the Federal Budget described below is largely unaffected by the presence of the Part D account though the magnitude will be greater.

credited on Treasury securities held in the HI Trust Fund. As is explained in the next section, these Treasury securities and related interest have no effect on the consolidated statement of governmentwide finances.

For SMI, direct transfers from the General Fund financed 76 percent and 78 percent of 2016 program costs for Parts B and D, respectively. Premiums paid by beneficiaries and, for Part D state transfers, generally financed the remainder of expenditures. For beneficiaries dually eligible for Medicare and Medicaid, states must pay the Part D account a portion of their estimated foregone drug costs for this population (referred to as state transfers). As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund. These Treasury securities and related interest have no effect on the consolidated statement of governmentwide finances. See Note 22—Social Insurance, for additional information on Medicare program financing.

Figure 1
Social Security, Medicare, and Governmentwide Finances



Social Security, Medicare, and Governmentwide Finances

The current and future financial status of the separate OASDI, HI, and SMI Trust Funds is the focus of the Social Security and Medicare Trustees' Reports, a focus that may appropriately be referred to as the "trust fund perspective." In contrast, the Government primarily uses the *unified budget* concept as the framework for budgetary analysis and presentation. It represents a comprehensive display of all federal activities, regardless of fund type or on- and off-budget status, and has a broader focus than the trust fund perspective that may appropriately be referred to as the "budget perspective" or the "governmentwide perspective." Social Security and Medicare are among the largest expenditure categories of the U.S. federal budget. Together, they now account for more than a third of all federal spending and the percentage is projected to rise dramatically for the reasons discussed below. This section describes in detail the important relationship between the trust fund perspective and the governmentwide perspective.

Figure 1 is a simplified depiction of the interaction of the Social Security and Medicare Trust Funds with the rest of the federal budget.[7] The boxes on the left show sources of funding, those in the middle represent the trust funds and other Government accounts, which include the General Fund into which that funding flows, and the boxes on the right show simplified expenditure categories. The figure is intended to illustrate how the various sources of program revenue flow through the budget to beneficiaries. The general approach is to group revenues and expenditures that are linked specifically to Social Security and/or Medicare separately from those for other government programs.

[7] The federal unified budget encompasses all Government financing and is synonymous with a governmentwide perspective.

Each of the trust funds has its own sources and types of revenue. With the exception of General Fund transfers to SMI, each of these revenue sources represents revenue from the public that is dedicated specifically for the respective trust fund and cannot be used for other purposes. In contrast, personal and corporate income taxes as well as other revenue go into the General Fund and are drawn down for any Government program for which Congress has approved spending.[8] The arrows from the boxes on the left represent the flow of the revenues into the trust funds and other Government accounts.

The heavy line between the top two boxes in the middle of Figure 1 represents intragovernmental transfers to the SMI Trust Fund from other Government accounts. The Medicare SMI Trust Fund is shown separately from the two Social Security Trust Funds (OASI and DI) and the Medicare HI Trust Fund to highlight the unique financing of SMI. Currently, SMI is the only one of the programs that is funded through transfers from the General Fund, which is part of the other Government accounts (the SMI Part D account also receives transfers from the states). The direct transfers finance roughly three-fourths of SMI Program expenses. The transfers are automatic; their size depends on how much the program requires, not on how much revenue comes into the Treasury. If General Fund revenues become insufficient to cover both the mandated transfer to SMI and expenditures on other general Government programs, Treasury has to borrow to make up the difference. In the longer run, if transfers to SMI increase beyond growth in general revenues—and as shown in the Medicare Trustees Report and Chart 5 later in this section, they are projected to increase significantly in coming years—then Congress must either raise taxes, cut other Government spending, reduce SMI benefits, or borrow even more.

The dotted lines between the middle boxes of Figure 1 also represent intragovernmental transfers but those transfers arise in the form of "borrowing/lending" between the Government accounts. Interest credited to the trust funds arises when the excess of program income over expenses is loaned to the General Fund. The vertical lines labeled *Surplus Borrowed* represent these flows from the trust funds to the other Government accounts. These loans reduce the amount the General Fund has to borrow from the public to finance a deficit (or likewise increase the amount of debt paid off if there is a surplus). However, the General Fund has to credit interest on the loans from the trust fund programs, just as if it borrowed the money from the public. The credits lead to future obligations for the General Fund (which is part of the other Government accounts). These transactions are indicated in Figure 1 by the vertical arrows labeled *Interest Credited*. The credits increase trust fund income exactly as much as they increase credits (future obligations) in the General Fund. From the governmentwide standpoint, at least in an accounting sense, these interest credits are a wash.

When the trust funds get the receipts that they loan to the General Fund, these receipts provide additional authority to spend on benefits and other program expenses. The General Fund, in turn, has taken on the obligation of paying interest on these loans every year and repaying the principal when trust fund income from other sources falls below expenditures.

How loans from the trust funds to the General Fund and later repayments of those loans affect tax income and expenditures of the General Fund is uncertain. Two extreme cases encompass the possibilities. At one extreme, each dollar the trust funds loan to the General Fund might reduce borrowing from the public by a dollar at the time the loan is extended, in which case the General Fund could repay all trust fund loans by borrowing from the public without raising the level of public debt above the level that would have occurred in the absence of the loans. At the other extreme, each dollar the trust funds loan to the General Fund might result in some combination of higher General Fund spending and lower General Fund revenues amounting to one dollar at the time the loans are extended, in which case General Fund loan repayments to the trust funds might initially be financed with borrowing from the public but must at some point be financed with a combination of higher General Fund taxes and lower General Fund spending than would have occurred in the absence of the loans. In this latter extreme, trust fund loans result in additional largess (i.e., higher spending and/or lower taxes) in General Fund programs at the time the loans are extended, but ultimately that additional largess is financed with additional austerity (i.e., lower spending and/or higher taxes) in General Fund programs at later dates. The actual impact of trust fund loans to the General Fund and their repayment on General Fund programs is at one of these two extremes or somewhere in between.

Actual dollar amounts roughly corresponding to the flows presented in Figure 1 are shown in Table 1 for fiscal year 2016. In Table 1, revenues from the public (left side of Figure 1) and expenditures to the public (right side of Figure 1) are shown separately from transfers between Government accounts (middle of Figure 1). Note that the transfers ($300.1 billion) and interest credits ($100.6 billion) received by the trust funds appear as negative entries under "All Other" and are thus offsetting when summed for the total budget column. These two intragovernmental transfers are the key to the differences between the trust fund and budget perspectives.

From the governmentwide perspective, only revenues received from the public (and states in the case of Medicare, Part D) and expenditures made to the public are important for the final balance. Trust fund revenue from the public consists of

[8] Other programs also have dedicated revenues in the form of taxes and fees (and other forms of receipt) and there are a large number of dedicated trust funds in the federal budget. Total trust fund receipts account for about 40 percent of total Government receipts with the Social Security and Medicare Trust Funds accounting for about two-thirds of trust fund receipts. For further discussion, see the report issued by the Government Accountability Office, *Federal Trust and Other Earmarked Funds*, GAO-01-199SP, January 2001. In the figure and the discussion that follows, all other programs, including these other dedicated trust fund programs, are grouped under "Other Government Accounts" to simplify the description and maintain the focus on Social Security and Medicare.

payroll taxes, benefit taxes, and premiums. For HI, the difference between total expenditures made to the public ($290.6 billion) and revenues ($278.7 billion) was $12.0 billion in 2016, indicating that HI had a relatively small negative effect on the overall budget outcome *in that year*. For the SMI account, revenues from the public (premiums) were relatively small, representing about 25 percent of total expenditures made to the public in 2016. The difference ($304.8 billion) resulted in a net draw on the overall budget balance in that year. For OASDI, the difference between total expenditures made to the public ($916.0 billion) and revenues from the public ($859.4 billion) was $56.6 billion in 2016, indicating that OASDI had a negative effect on the overall budget outcome in that year. Combined OASDI payroll and benefit tax revenues were increased by $42.4 billion in fiscal year 2016.

The trust fund perspective is captured in the bottom section of each of the three trust fund columns. For HI, total expenditures exceeded total revenues by $3.5 billion in 2016, as shown at the bottom of the first column. This cash deficit was made up by calling in past loans made to the General Fund (i.e., by redeeming trust fund assets). For SMI, total expenditures exceeded total revenues by $3.3 billion. The total revenue for SMI is $400.8 billion ($99.3 + $301.5), which includes $301.5 billion transferred from other Government accounts (General Fund). Transfers to the SMI Program from other Government accounts (the General Fund), amounting to about 74.1 percent of program costs, are obligated under current law and, therefore, appropriately viewed as revenue from the trust fund perspective. For OASDI, total revenues of $950.2 billion ($859.4 + $90.7) exceeded total expenditures of $916.0 billion by $34.1 billion. Total revenues for OASDI included $90.7 billion in transfers from the General Fund, made up of interest credits of $90.6 billion and transfers of $0.2 billion called for by Public Laws 111-147, 111-312, 112-78, and 112-96 to make up for the reduction in payroll tax revenues attributable to the temporary payroll tax rate reductions.

Table 1
Revenues and Expenditures for Medicare and Social Security Trust Funds and the Total Federal Budget for the Fiscal Year ended September 30, 2016

	Trust Funds					
(In billions of dollars)	HI	SMI	OASDI	Total	All Other	Total[1]
Payroll taxes and other public revenues:						
Payroll and benefit taxes	273.5	-	859.4	1,132.9	-	1,132.9
Premiums	5.2	86.7	-	91.9	-	91.9
Other taxes and fees	-	12.6	-	12.6	2,029.3	2,041.9
Total	278.7	99.3	859.4	1,237.4	2,029.3	3,266.7
Total expenditures to the public[2]	290.6	404.1	916.0	1,610.7	2,243.4	3,854.1
Net results for budget perspective[3]	(12.0)	(304.8)	(56.6)	(373.3)	(214.1)	(587.4)
Revenues from other Government accounts:						
Transfers	0.4	299.5	0.2	300.1	(300.1)	
Interest credits	8.0	2.0	90.6	100.6	(100.6)	
Total	8.4	301.5	90.7	400.7	(400.7)	
Net results for trust fund perspective[3]	(3.5)	(3.3)	34.1	27.4	N/A	N/A

[1] This column is the sum of the preceding two columns and shows data for the total federal budget. The figure $587.4 was the total federal deficit in fiscal year 2016.

[2] The OASDI figure includes $4.7 billion transferred to the Railroad Retirement Board for benefit payments and is therefore an expenditure to the public.

[3] Net results are computed as revenues less expenditures.

Notes: Totals may not equal the sum of components due to rounding.
"N/A" indicates not applicable.

Cash Flow Projections

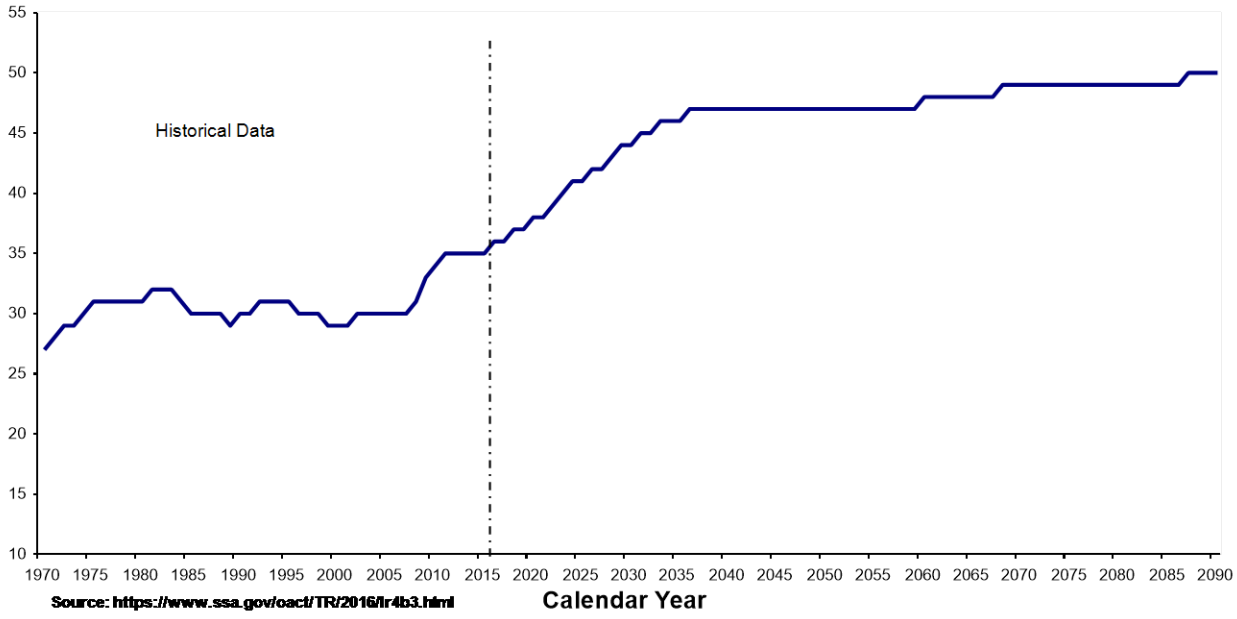
Background

Economic and Demographic Assumptions. The Boards of Trustees[9] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. The economic and demographic assumptions used for the most recent set of intermediate projections for Social Security and Medicare are shown in the “Social Security” and “Medicare” sections of Note 22—Social Insurance.

[9] There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor; the Commissioner of the Social Security Administration; and two public trustees who are appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees cannot both be members of the same political party.

Beneficiary-to-Worker Ratio. The expenditure projections for both the OASDI and Medicare Programs reflect the aging of the large baby-boom generation, born in the years 1946 to 1964, and its ultimate passing. Under the intermediate assumptions, cost rates are projected to rise rapidly between 2017 and 2035, primarily because the number of beneficiaries rises much more rapidly than the number of covered workers as the baby-boom generation retires. Chart 1 shows that the number of OASDI beneficiaries per 100 covered workers is projected to grow rapidly from 36 in 2016 to 46 in 2035 as the baby boom generation enters their retirement years and receives benefits. In rough terms, the beneficiary-to-worker ratio at any point in time reflects the birth rates experienced by the generations who are retired. The baby-boom generation had lower fertility rates than their parents, and it is expected that lower fertility rates will persist for all future generations; therefore, the ratio of beneficiaries to workers will rise rapidly and reach a permanently higher level after the baby-boom generation retires. Due to increasing longevity, the ratio of beneficiaries to workers will generally rise slowly thereafter, reaching 50 beneficiaries per 100 workers by 2090. A similar demographic pattern confronts the Medicare Program.

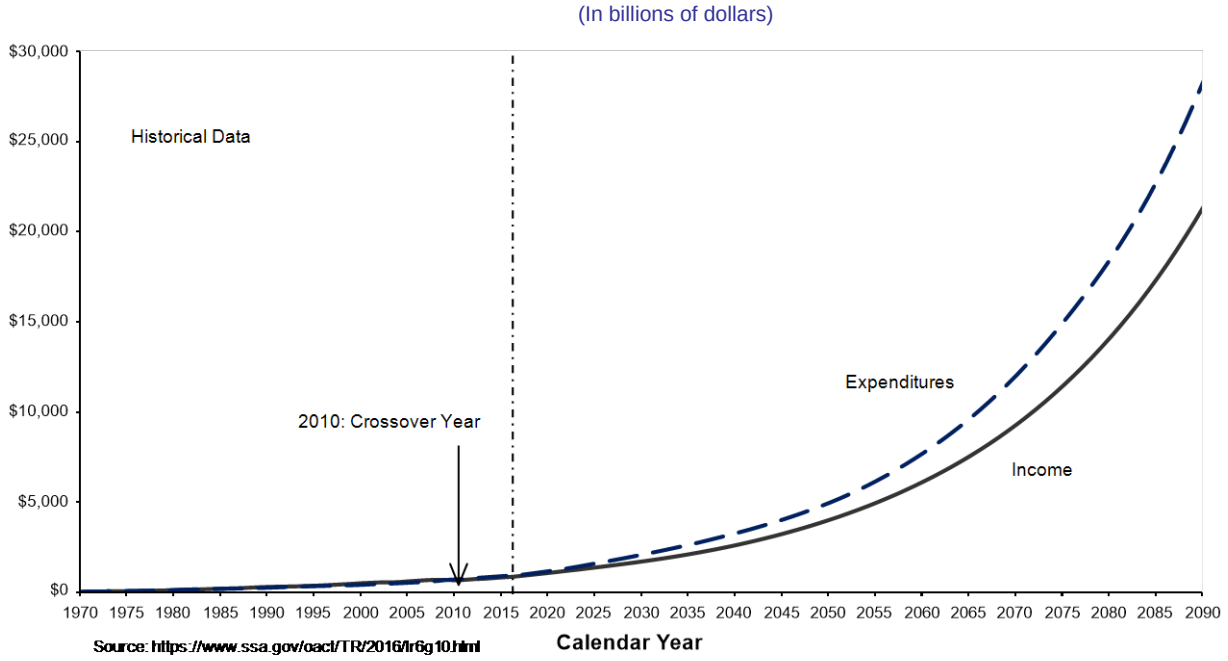
Chart 1—OASDI Beneficiaries per 100 Covered Workers 1970-2090



Social Security Projections

Income and Expenditures. Chart 2 shows historical values and actuarial estimates of combined OASDI annual noninterest income and expenditures for 1970-2090. The estimates are for the open-group population of all workers and beneficiaries projected to be alive in each year. The expenditure projections in Chart 2 and all subsequent charts assume all scheduled benefits are paid regardless of whether the income and assets are available to finance them.

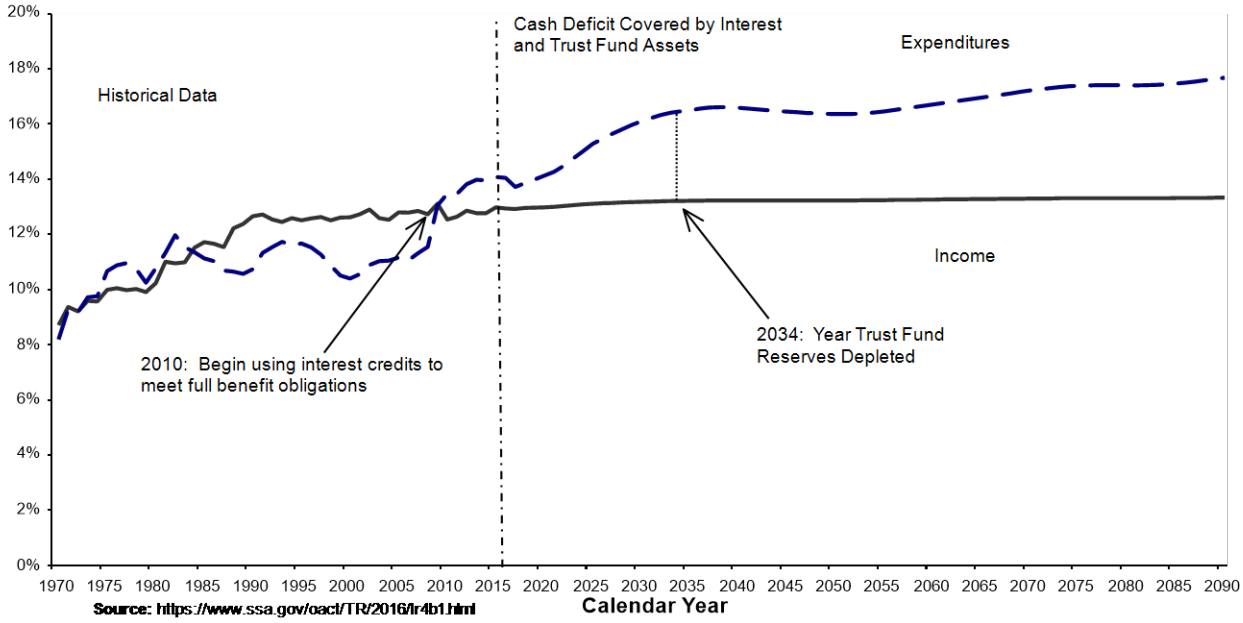
Chart 2—OASDI Income (Excluding Interest) and Expenditures 1970-2090



Social Security's surplus of noninterest income over expenditures was positive every year between 1984 and 2009, became negative in 2010, and is projected to remain negative in all years of the projection period. This pattern reflects the aging of the population documented in Chart 1, as well as growth of the economy and growth in the price level. As described above, surpluses that occurred prior to 2010 were "loaned" to the General Fund and accumulated, with interest, increasing reserve spending authority for the trust fund. The reserve spending authority represents an obligation for the General Fund. The government could finance this redemption by increasing its borrowing from the public, raising taxes (other than OASDI payroll taxes), and/or reducing expenditures (other than OASDI cost).

Income and Expenditures as a Percent of Taxable Payroll. Chart 3 shows annual noninterest income and expenditures expressed as percentages of taxable payroll, commonly referred to as the income rate and cost rate, respectively. Dividing noninterest income and expenditures by taxable payroll serves to isolate the effect of demographics on Social Security finances, and usefully gauges Social Security's financial imbalances against the size of the Social Security tax base. The time path of the cost rate in Chart 3 closely parallels that of the beneficiary-to-worker ratio in Chart 1. Under the intermediate assumptions, demographic factors would by themselves cause the projected cost rate to rise rapidly for the next two decades before leveling off in about 2035. However, the recent recession led to lower taxable earnings than expected and more beneficiaries than expected, which in turn sharply, but temporarily, increased the cost rate starting in 2009. Social Security began using interest credits to meet full benefit obligations in 2010, and is projected to begin drawing down trust fund asset reserves starting in 2020 and to deplete those reserves in 2034. After trust fund asset reserves are depleted, continuing noninterest income will be sufficient to finance 79 percent of scheduled benefits for the rest of 2034, declining to 74 percent of scheduled benefits for 2090.

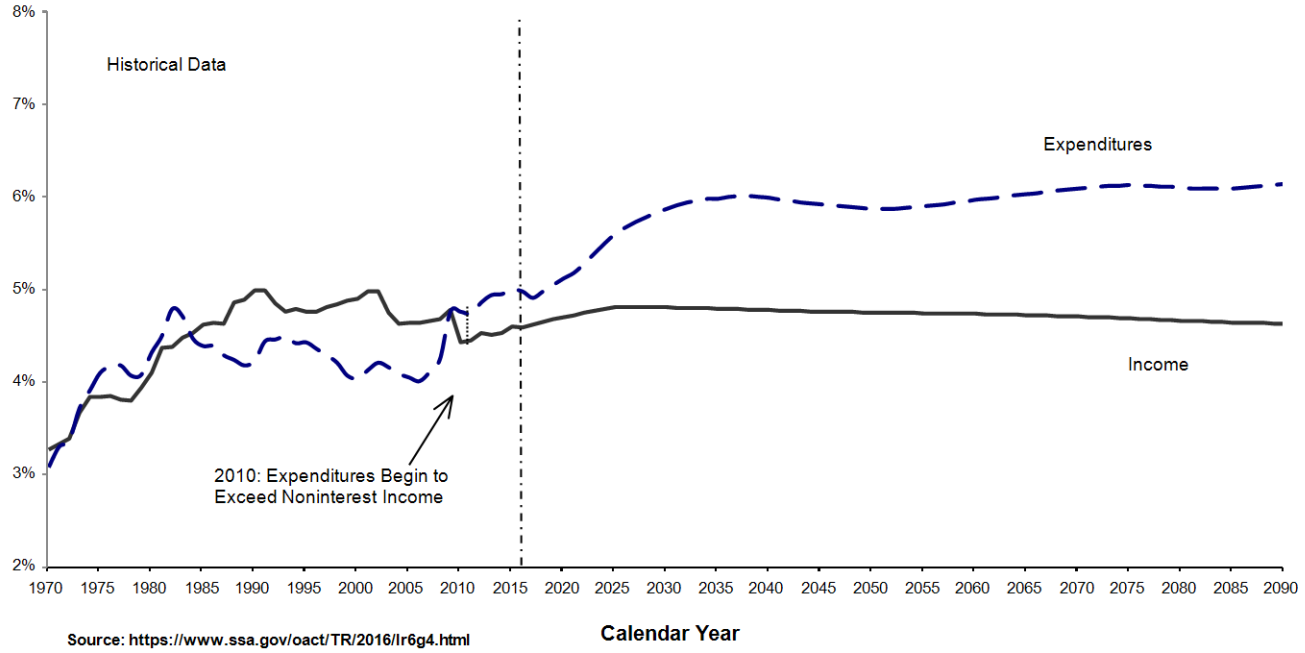
Chart 3—OASDI Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2090



Source: https://www.ssa.gov/oact/TR/2016/lr4b1.html

Income and Expenditures as a Percent of GDP. Chart 4 shows estimated annual noninterest income and expenditures, expressed as percentages of GDP, which is the total value of goods and services produced in the United States. This alternative perspective shows the size of the OASDI Program in relation to the capacity of the national economy to sustain it. In 2016, OASDI cost was about $929 billion, which was about 5.0 percent of GDP. The cost of the program (based on current law) will grow from 5.0 percent of GDP in 2016 to about 5.9 percent of GDP in 2030, hit a peak of 6.0 percent of GDP in 2037, then decline to 5.9 percent by 2050, and generally increase to 6.1 percent of GDP by 2090. The rapid increase from 2017 to 2030 is projected to occur as baby boomers become eligible for OASDI benefits, lower birth rates result in fewer workers per beneficiary, and beneficiaries continue to live longer. In 2090, expenditures are projected to exceed income by approximately 1.51 percent of GDP. As the economy recovers, Social Security's non-interest income, which reflects scheduled tax rates, increases from its current level of about 4.6 percent of GDP to about 4.8 percent of GDP for 2025. Thereafter, non-interest income as a percent of GDP declines gradually, to about 4.6 percent by 2090, because the share of employee compensation provided as non-covered fringe benefits is expected to increase gradually.

Chart 4—OASDI Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2090



Source: https://www.ssa.gov/oact/TR/2016/lr6g4.html

Sensitivity Analysis. Actual future income from OASDI payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors: the size and composition of the population that is receiving benefits, the level of monthly benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers' earnings. These factors will depend, in turn, upon future marriage and divorce rates, birth rates, death rates, migration rates, labor force participation and unemployment rates, disability incidence and termination rates, retirement age patterns, productivity gains, wage increases, cost-of-living increases, and many other economic as well as demographic factors.

This section presents estimates that illustrate the sensitivity of long-range expenditures and income for the OASDI Program to changes in *selected individual assumptions*. In this analysis, the intermediate assumption is used as the reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost (Alternative I) and high-cost (Alternative III) projections. For example, when analyzing sensitivity with respect to variation in real wages, income, and expenditure projections using the intermediate assumptions are compared to the outcome when projections are done by changing only the real wage assumption to either low-cost or high-cost alternatives.

The low-cost alternative is characterized by assumptions that improve the financial status of the program (relative to the intermediate assumption) such as slower improvement in mortality (beneficiaries die younger). In contrast, assumptions under the high-cost alternative worsen the financial outlook.

Table 2 shows the effects of changing individual assumptions on the present value of estimated OASDI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. For example, the intermediate assumption for the annual rate of *reduction in age-sex-adjusted death rates* is 0.78 percent. For the low-cost alternative, a slower reduction rate (0.42 percent) is assumed as it means that beneficiaries die at a younger age relative to the intermediate assumption, resulting in lower expenditures. Under the low-cost assumption, the shortfall drops from $14,169 billion to $11,915 billion, a 16 percent smaller shortfall. The high-cost death rate assumption (1.16 percent) results in an increase in the shortfall, from $14,169 billion to $16,601 billion, a 17 percent increase in the shortfall. Clearly, alternative death rate assumptions have a substantial impact on estimated future cash flows in the OASDI Program.

A higher fertility rate means more workers relative to beneficiaries over the projection period, thereby lowering the shortfall relative to the intermediate assumption. An increase in the rate from 2.0 to 2.2 percent results in a 10 percent smaller shortfall (i.e., expenditures less income), from $14,169 billion to $12,754 billion. If the ultimate total fertility rate were changed from 2.0 to 1.8 percent, the shortfall for the period of estimated OASDI income relative to cost would increase from $14,169 billion to $15,466 billion, a 9 percent increase in the shortfall.

The annual real-wage differential is the difference between the percentage increases in: (1) the average annual wage in OASDI covered employment; and (2) the average annual Consumer Price Index (CPI). Higher real wage growth results in faster income growth relative to expenditure growth. Table 2 demonstrates that if the ultimate real-wage differential were changed from 1.20 percentage points, the intermediate assumption, to 0.59 percentage points, the shortfall for the period of estimated OASDI income relative to cost would increase to $16,357 billion from $14,169 billion; if the ultimate real-wage differential were changed from 1.20 to 1.83 percentage points, the shortfall would decrease from $14,169 billion to $10,846 billion.

Table 2 demonstrates that if the ultimate annual increase in the CPI were changed from 2.6 percent, the intermediate assumption, to 2.0 percent, the shortfall for the period of estimated OASDI income relative to cost would increase to $14,620 billion from $14,169 billion; if the ultimate annual increase in the CPI were changed to 3.2 percent, the shortfall would decrease from $14,169 billion to $13,676 billion. The seemingly counter-intuitive result that higher CPI increases result in decreased shortfalls (and vice versa) is explained by the time lag between the effects of the CPI changes on taxable payroll and on benefit payments. The effect on taxable payroll due to a greater increase in average wages is experienced immediately, while the effect on benefits is experienced with a lag of about one year. For this reason, larger increases in the CPI cause earnings and income to increase sooner and, therefore, by more each year, than benefits and cost.

Very little difference is discernible in the first few years among the estimates of present values of net annual cash flow based on the three sets of assumptions about annual immigration. However, as the effect of these three levels of net annual immigration accumulate, variations in present values become more apparent. Because immigration generally occurs at relatively young adult ages, the effects initially are similar to those of total fertility rates. There is no significant effect on beneficiaries (and, therefore, on benefits) in the early years but the effect on the numbers of workers (and, therefore, on payroll tax income) is immediate. Therefore, even in the early years, the present values, year by year, are generally higher (less negative in later years) for higher net annual immigration. However, the increased payroll taxes for a given year are eventually offset by benefits paid in that year to earlier immigrant cohorts. Therefore, the present values based on the three assumptions about net annual immigration become more similar at the end of the projection period. Table 2 shows that if the intermediate immigration assumptions were changed so that the average level for the 75-year period decreased from 1,291,000 persons to 961,000 persons,

the present value of the shortfall for the period of estimated OASDI income relative to cost would increase to $14,946 billion from $14,169 billion. If, instead, the immigration assumptions were changed so that net annual immigration would be expected to average 1,629,000 persons, the present value of the shortfall would decrease from $14,169 billion to $13,461 billion.

Finally, Table 2 shows the sensitivity of the shortfall to variations in the real interest rate or, in present value terminology, the sensitivity to alternative discount rates assuming a higher discount rate results in a lower present value. The shortfall is 15 percent lower, decreasing from $14,169 billion to $12,064 billion, when the real interest rate is 3.2 percent rather than 2.7 percent. The shortfall is 19 percent higher, increasing to $16,814 billion, when the real interest rate is 2.2 percent rather than 2.7 percent.

Table 2
Present Values of Estimated OASDI Expenditures in Excess of Income Under Various Assumptions, 2016-2090

(Dollar values in billions; values of assumptions shown in parentheses)

	Financing Shortfall Range		
Assumption	**Low**	**Intermediate**	**High**
Average annual reduction in death rates	11,915 (0.42)	14,169 (0.78)	16,601 (1.16)
Total fertility rate	12,754 (2.2)	14,169 (2.0)	15,466 (1.8)
Real wage differential	10,846 (1.83)	14,169 (1.20)	16,357 (0.59)
CPI change	13,676 (3.2)	14,169 (2.6)	14,620 (2.0)
Net immigration	13,461 (1,629,000)[1]	14,169 (1,291,000)[1]	14,946 (961,000)[1]
Real interest rate	12,064 (3.2)	14,169 (2.7)	16,814 (2.2)

[1] Amounts represent the average annual net immigration over the 75-year projection period.

Source: 2016 OASDI Trustees Report and SSA.

Medicare Projections

Medicare Legislation. The *Affordable Care Act as amended by the Health Care and Education Reconciliation Act of 2010* (the "Affordable Care Act" or ACA) significantly improves projected Medicare finances. The most important cost saving provision in the ACA is a revision in payment rate updates for Parts A and B services other than for physicians' services. Prior to the ACA, Medicare payment rates for most non-physician provider categories were updated annually by the increase in providers' input prices for the market basket of employee wages and benefits, facility costs, medical supplies, energy and utility costs, professional liability insurance, and other inputs needed to produce the health care goods and

services[10]. To the extent that health care providers can improve their productivity each year, their net costs of production (other things being equal) will increase more slowly than their input prices—but the Medicare payment rate updates prior to the ACA were not adjusted for potential productivity gains. Accordingly Medicare costs per beneficiary would have increased somewhat faster than for the health sector overall. In particular, it is assumed that the full market basket increase would be approximately 3.4 percent annually. The ACA requires that many of these Medicare payment updates be reduced by the 10-year moving average increase in economy-wide productivity, which the Trustees assume will be 1.1 percent per year over the long range. The ACA also achieves substantial cost savings by benchmarking payment rates for private health plans providing Parts A and B services (Part C or Medicare Advantage) to more closely match per beneficiary costs. Partly offsetting these changes was an increase in prescription drug coverage. In addition, the ACA increases Part A revenues by: (a) taxing high-cost employer-provided health care plans and thereby giving employers incentives to increase the share of compensation paid as taxable earnings, and (b) imposing a new 0.9 percent surtax on earnings in excess of $200,000 (individual tax return filers) or $250,000 (joint tax return filers) starting in 2013.

The ACA substantially reduces the Medicare cost projections. Growth in Medicare cost per beneficiary in excess of growth in per capita GDP is referred to as "excess cost growth." In the 2009 *Financial Report*, the last report released prior to the passage of the ACA, excess cost growth was assumed to average one percentage point over the last 50 years of the 75-year projection period—that is, Medicare expenditures per beneficiary were assumed to grow, on average, about one percentage point faster than per capita GDP over the long range. That assumption for excess cost growth in Medicare was optimistic in the sense that it is smaller than in recent history; excess cost growth averaged 1.4 percentage points between 1985 and 2014, and such growth was slower in recent years, averaging about 0.2 percent from 2008 to 2014.[11] Nevertheless, the slowdown has been substantial and has continued for several years. In this year's *Financial Report*, long-term excess cost growth is projected to be between 0.9 percent and 1.0 percent, which is slower than the historical average. Although not a factor in the recent slowdown, one reason why that growth will probably remain below historical rates beyond the next 10 years is that the program now includes a number of institutions, incentives, and mechanisms, such as the Center for Medicare & Medicaid Innovation and the Independent Payment Advisory Board, that could reduce spending growth in the program over time.

The 2016 Medicare Trustees' Report warns that the financial projections for the Medicare program reflect substantial, but very uncertain, cost savings deriving from provisions of the ACA and MACRA, such as the productivity adjustments discussed above, that lower increases in Medicare payment rates to most categories of health care providers. Without fundamental change in the current delivery system, these adjustments would probably not be viable indefinitely. In view of these issues with provider payment rates, actual future costs for Medicare could exceed those shown by the current-law projections that underlie both the Trustees' Report and this *Financial Report*.

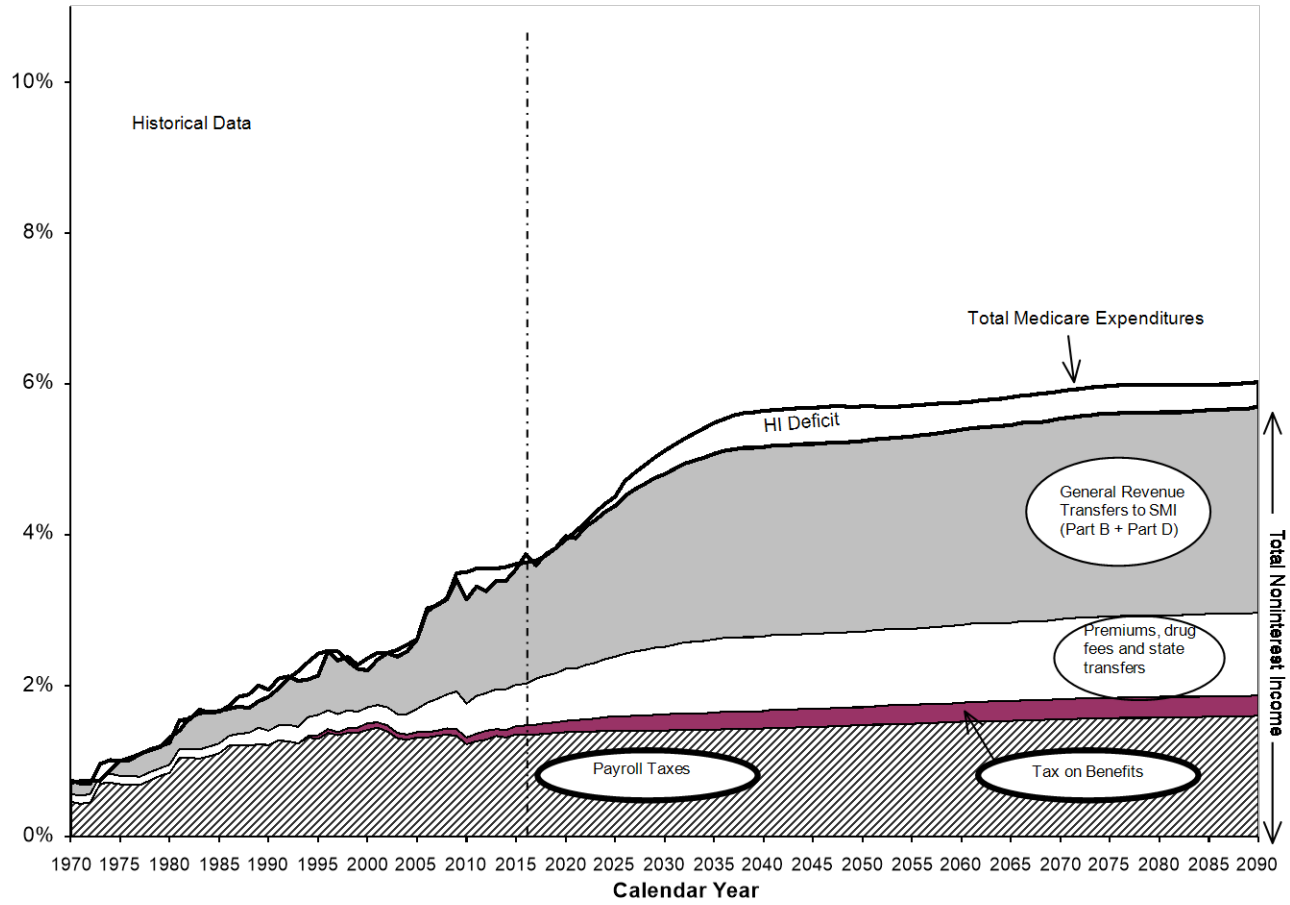
Changes in Projection Methods. The projections in this year's report, with one exception related to Part A, are based on current law; that is, it is assumed that laws on the books will be implemented and adhered to with respect to scheduled taxes, premium revenues, and payments to providers and health plans. The one exception is that the projections disregard payment reductions that would result from the projected depletion of the Medicare Hospital Insurance (HI) Trust Fund. Under current law, payments would be reduced to levels that could be covered by incoming tax and premium revenues when the HI Trust Fund was depleted.

[10] Historically, lawmakers frequently reduced the payment updates below the increase in providers' input prices in an effort to slow Medicare cost growth or to offset unwarranted changes in claims coding practices. The law did not specify any such adjustments after 2009.

[11] Congressional Budget Office, the Long-Term Budget Outlook, June 2016.

Total Medicare. Chart 5 shows expenditures and current-law noninterest revenue sources for HI and SMI combined as a percentage of GDP. For 2016, total Medicare expenditures are expected to continue to exceed noninterest revenue, but by only a very small margin due to the revenue increasing more rapidly than expenditures. A deficit is expected for 2017, and then modest surpluses are projected for 2018 through 2020. Deficits are expected to return in 2021 and to remain for the balance of the projection, as expenditures grow faster than revenue. Under the ACA, beginning in 2013 the HI Trust Fund receives an additional 0.9 percent tax on earnings in excess of $250,000 for joint tax return filers and $200,000 for individual tax return filers. As a result of this provision, it is projected that payroll taxes will grow slightly faster than GDP. HI revenue from income taxes on Social Security benefits will gradually increase as a share of GDP as the share of benefits subject to such taxes increases. Beginning in 2009, as HI payroll tax receipts declined due to the recession and general revenue transfers increased, the latter income source became the largest single source of income to the Medicare program as a whole. General revenue transfers to the Part B account have increased significantly in 2016, as required by the *Bipartisan Budget Act* (BBA) of 2015 to compensate for premium revenue that has not been received in 2016 under the BBA requirements to calculate the monthly Part B premium as if the hold harmless provision did not apply. After decreasing from 2016 to 2017, general revenues will gradually increase as a share of Medicare financing from 2017 through 2029 and grow to about 48 percent by 2030, stabilizing thereafter. SMI premiums will also grow in proportion to general revenue transfers, placing a growing burden on beneficiaries. For high-income enrollees, SMI premiums began to increase more rapidly in 2011 and will continue to do so as a result of ACA provisions that increase Part D premiums and freeze the income thresholds used to determine Part B and Part D income-related premiums for 2011-2019. MACRA contains further provisions that affect the income-related premium thresholds and that will result in more premium income to Part B and Part D. SMI general revenues currently equal 1.5 percent of GDP and will increase to an estimated 2.7 percent in 2090 under current law.

Chart 5—Total Medicare (HI and SMI) Expenditures and Noninterest Income as a Percent of GDP 1970-2090

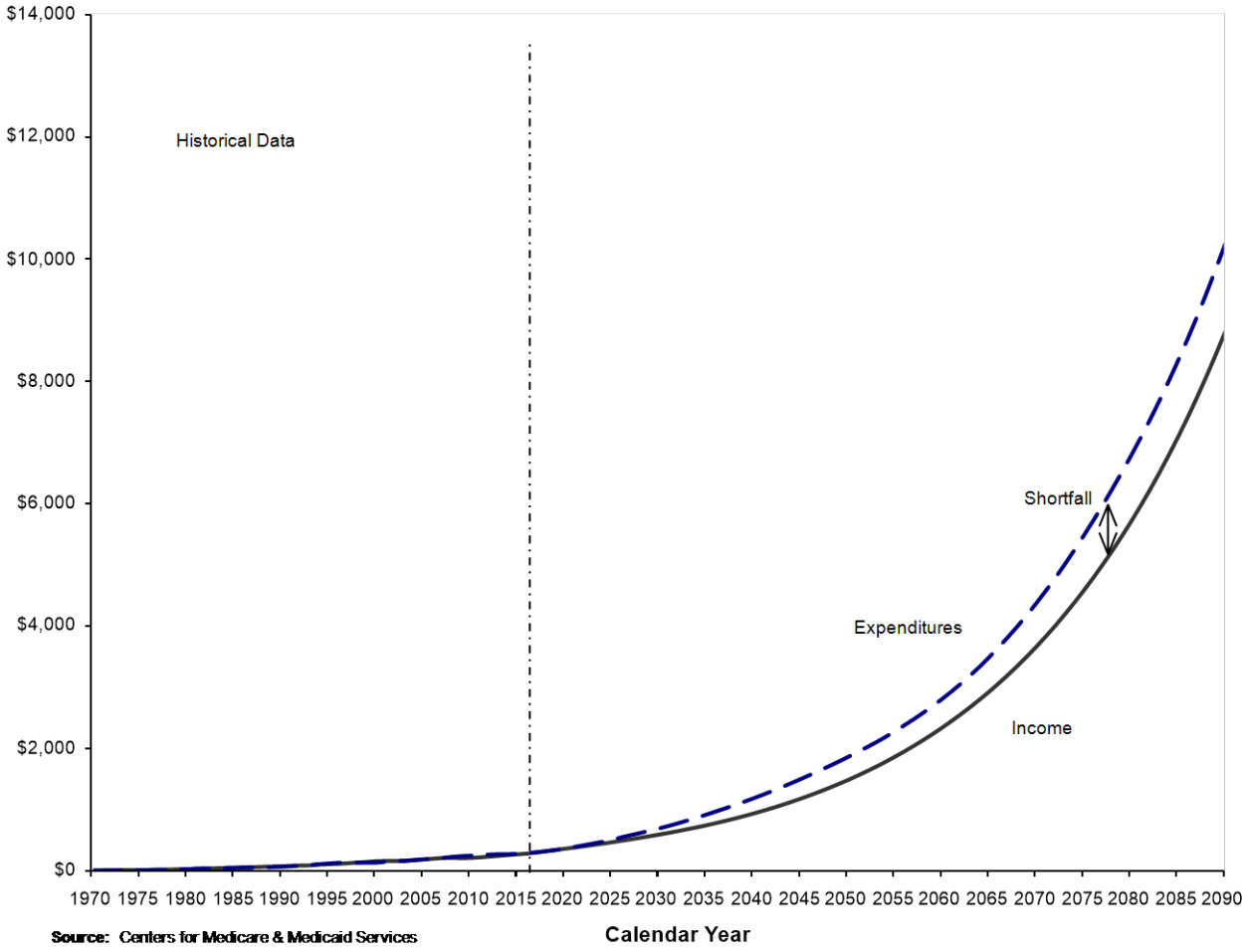


Source: https://www.ssa.gov/OACT/TRSUM/images/LD_ChartC.html

Medicare, Part A (Hospital Insurance)— Income and Expenditures. Chart 6 shows historical and actuarial estimates of HI annual income (excluding interest) and expenditures for 1970-2089 in nominal dollars. The estimates are for the open-group population.

Chart 6—Medicare Part A Income (Excluding Interest) and Expenditures 1970-2090

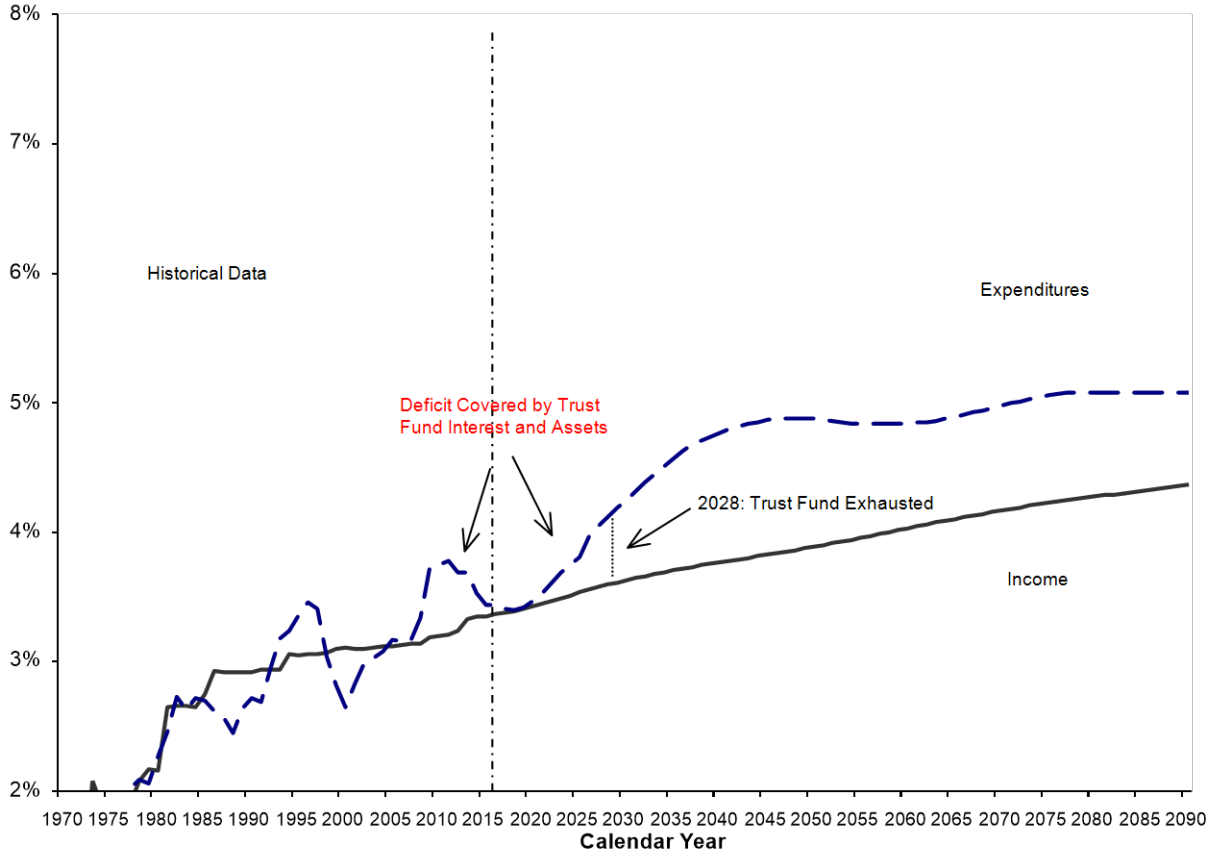
(In billions of dollars)



Source: Centers for Medicare & Medicaid Services

Medicare, Part A Income and Expenditures as a Percent of Taxable Payroll. Chart 7 illustrates income (excluding interest) and expenditures as a percentage of taxable payroll over the next 75 years. The chart shows that beginning in 2016, the expenditure rate exceeds the income rate, and cash deficits continue thereafter. The cost rate declined for 2014 and 2015 and is projected to continue to decline through 2018, largely due to expenditure growth that was constrained in part by the sequester and low payment updates, as well as a rebound of taxable payroll growth from 2007-2009 recession levels. Subsequent to 2018, the cost rate is projected to rise primarily due to retirements of those in the baby boom generation and partly due to a projected return to modest health services cost growth. This cost rate increase is moderated by the accumulating effect of the productivity adjustments to provider price updates, which are estimated to reduce annual HI per capita cost growth by an average of 0.9 percent per year through 2025 and 1.1 percent per year thereafter. Trust fund interest earnings and assets provide enough resources to pay full benefit payments until 2028 with general revenues used to finance interest and loan repayments to make up the difference between cash income and expenditures during that period. Pressures on the federal budget will thus emerge well before 2028. Present tax rates would be sufficient to pay 87 percent of scheduled benefits after trust fund exhaustion in 2028 and 86 percent of scheduled benefits in 2090.

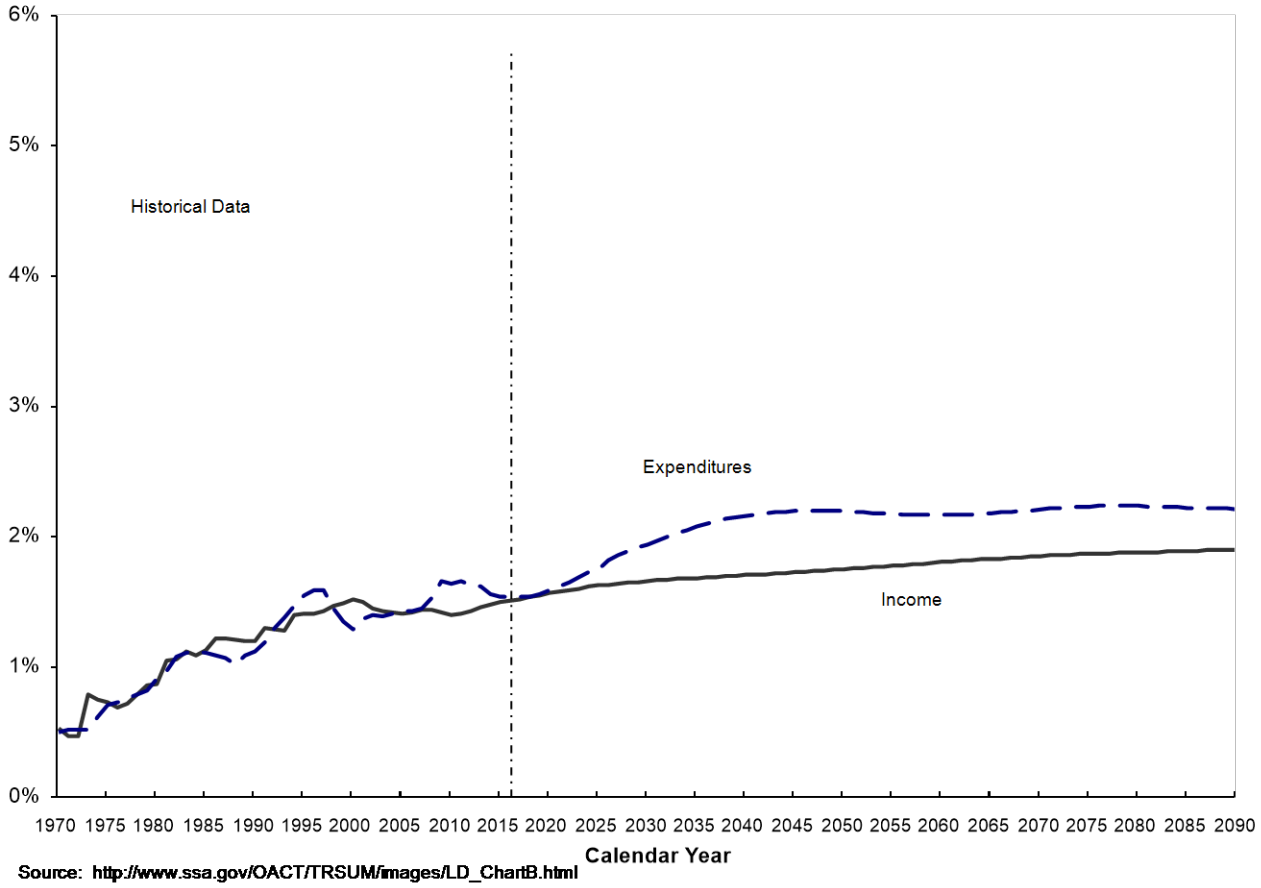
Chart 7—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2090



Source: https://www.ssa.gov/OACT/TRSUM/images/LD_ChartB.html

Medicare, Part A Income and Expenditures as a Percent of GDP. Chart 8 shows estimated annual noninterest income and expenditures, expressed as percentages of GDP, the total value of goods and services produced in the United States. This alternative perspective shows the size of the HI Program in relation to the capacity of the national economy to sustain it. Under the intermediate assumptions, the HI balance is negative for each year of the projection period. Annual deficits decrease from 2016 to 2018, increase through 2045, and then generally decline thereafter. The gap between expenditure and income shares of GDP widens to 0.47 percent in 2042, remains fairly stable through 2046, and then commences a slight decline, reaching 0.31 percent of GDP in 2090.

Chart 8—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2090

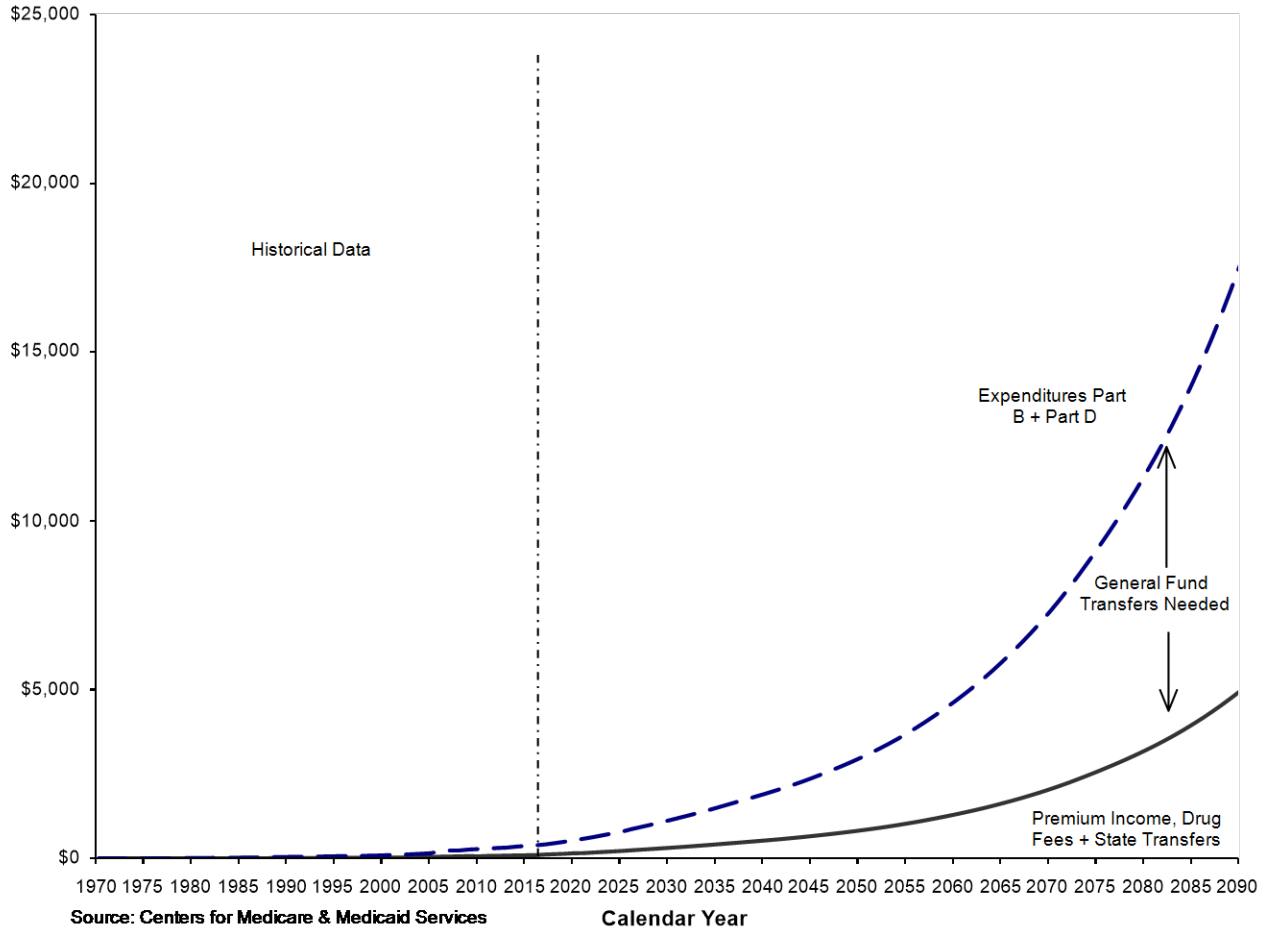


Source: http://www.ssa.gov/OACT/TRSUM/images/LD_ChartB.html

Medicare, Parts B and D (Supplementary Medical Insurance). Chart 9 shows historical and actuarial estimates of Medicare Part B and Part D premiums (and Part D state transfers) as well as expenditures for each of the next 75 years, in dollars. Beneficiary premiums and general revenue contributions for both Part B and Part D are established annually to cover the expected costs for the upcoming year. Should actual costs exceed those anticipated when the financing is determined, future financing rates can include adjustments to recover the shortfall. Likewise, should actual costs be less than those anticipated, the savings would result in lower future financing rates. The gap between program expenditures and revenues from premiums, drug fees, and state transfers grows throughout the projection period. This gap will need to be filled with general revenue transfers.

Chart 9—Medicare Part B and Part D Premium and State Transfer Income and Expenditures 1970-2090

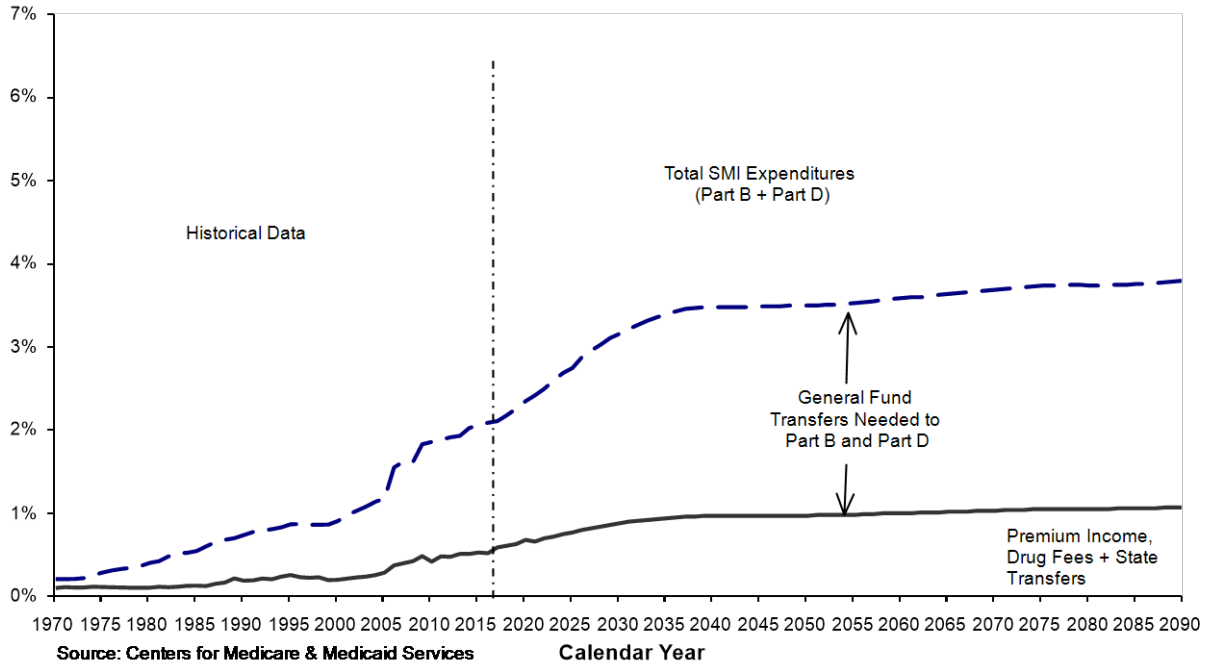
(In billions of dollars)



Source: Centers for Medicare & Medicaid Services

Medicare Part B and Part D Premium as well as State Transfer Income and Expenditures as a Percent of GDP. Chart 10 shows expenditures for the Supplementary Medical Insurance Program over the next 75 years expressed as a percentage of GDP, providing a perspective on the size of the SMI Program in relation to the capacity of the national economy to sustain it. SMI costs are projected to continue to outpace growth in GDP but at a slower rate compared to the last 10 years. Annual SMI expenditures grew from about 1.2 percent of GDP in 2005 to 1.6 percent of GDP in 2006 with the commencement of prescription drug coverage, and in 2015 they amounted to 2.1 percent of GDP. Under current law, SMI expenditures would grow to about 3.5 percent of GDP within 25 years and to 3.8 percent by the end of the projection period. The relatively high growth during the period 2016-2025 is due to the continuing retirement of the baby boom generation, further economic recovery, and modest increases in cost trends. Growth rates are projected to decline during the 2026-2040 period primarily as a result of a deceleration in beneficiary population growth. For the last 50 years of the projection period, cost growth moderates further due to the continued deceleration in beneficiary population growth and lower ultimate growth rate assumptions. As a share of GDP, premium and state transfer income grows from about 0.53 percent in 2016 to 1.10 percent of GDP in 2090. The portion of SMI expenditures financed by General Fund transfers to SMI is projected to be about 74 percent throughout the projection period.

Chart 10—Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP 1970-2090



Medicare Sensitivity Analysis. This section illustrates the sensitivity of long-range cost and income estimates for the Medicare Program to changes in *selected individual assumptions*. As with the OASDI analysis, the intermediate assumption is used as a reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost and high-cost projections (see description of sensitivity analysis for OASDI).

Table 3 shows the effects of changing various assumptions on the present value of estimated HI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. Several factors, such as the utilization of services by beneficiaries or the relative complexity of services provided, can affect costs without affecting tax income. Clearly, the financial status of the HI Trust Fund is extremely sensitive to alternative assumptions about the growth in health care cost. For the low-cost alternative, the slower growth in health costs causes the shortfall to drop from $3,822 billion to a surplus of $3,198 billion, a 184 percent change. The high-cost assumption results in nearly quadrupling the shortfall, from $3,822 billion to $15,054 billion.

Relative to the intermediate case, the low and high real wage growth rate scenarios result in about a -54 and +34 percent change in the shortfall, respectively. Wages are a key cost factor in the provision of health care. A higher real-wage differential immediately increases both HI expenditures for health care and wages for all workers. Higher wages results in greater payroll tax income. CPI inflation, fertility, and net immigration changes have very little effect on net HI expenditures. (When CPI inflation is varied, the real interest rate is held constant, which implies that the nominal interest changes one for one with the assumed rate of CPI inflation.) Higher immigration decreases the net shortfall modestly as the 75-year projection period captures a higher share of additional immigrants' tax payments than it does of their benefits.

Table 3 also shows that the present value of net HI expenditures is 15 percent lower if the real interest rate is 3.2 percent rather than 2.7 percent and 18 percent higher if the real interest rate is 2.2 percent rather than 2.7 percent.

Table 3
Present Values of Estimated Medicare Part A Expenditures in Excess of Income Under Various Assumptions, 2016-2090

(Dollar values in billions; values of assumptions shown in parentheses)

	Financing Shortfall Range		
Assumption [1]	**Low**	**Intermediate**	**High**
Average annual growth in health costs [2]	(3,198) (2.8)	3,822 (3.8)	15,054 (4.8)
Total fertility rate [3]	3,318 (2.2)	3,822 (2.0)	4,280 (1.8)
Real wage differential	1,748 (1.8)	3,822 (1.2)	5,116 (0.6)
CPI change	2,902 (3.2)	3,822 (2.6)	5,133 (2.0)
Net immigration [4]	3,558 (1,629,000)	3,822 (1,291,000)	4,153 (961,000)
Real interest rate	3,266 (3.2)	3,822 (2.7)	4,505 (2.2)

[1] The sensitivity of the projected HI net cash flow to variations in future mortality rates also is of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Part A, mortality sensitivity.

[2] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low-cost and high-cost alternatives assume that costs increase 1 percent slower or faster, respectively, than the intermediate assumption, relative to growth in taxable payroll.

[3] The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year and if she were to survive the entire childbearing period.

[4] Amount represents the average annual net immigration over the 75-year projection period.

Source: Center for Medicare & Medicaid Services

Table 4 shows the effects of various assumptions about the growth in health care costs on the present value of estimated SMI (Medicare Parts B and D) expenditures in excess of income. As with HI, net SMI expenditures are very sensitive to

changes in the health care cost growth assumption. For the low-cost alternative, the slower assumed growth in health costs reduces the governmentwide resources needed for Part B from $19,964 billion to $14,468 billion and in Part D from $8,657 billion to $6,108 billion, about a 28 percent and 29 percent difference for Part B and Part D, respectively. The high-cost assumption increases governmentwide resources needed to $28,538 billion for Part B and to $12,715 billion for Part D, about a 43 percent and a 47 percent difference for Part B and Part D, respectively.

Table 4
Present Values of Estimated Medicare Parts B and D Future Expenditures Less Premium Income and State Transfers Under Three Health Care Cost Growth Assumptions, 2016-2090

(In billions of dollars)

	Governmentwide Resources Needed		
Medicare Program	Low (3.3)	Intermediate (4.3)	High (5.3)
Part B	14,468	19,964	28,538
Part D	6,108	8,657	12,715

[1] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low and high scenarios assume that costs increase one percent slower or faster, respectively, than the intermediate assumption.

Source: Centers for Medicare & Medicaid Services

Sustainability of Social Security and Medicare

75-Year Horizon

According to the 2016 Medicare Trustees Report, the HI Trust Fund is projected to remain solvent until 2028 and, according to the 2016 Social Security Trustees Report, the OASI and DI Trust Funds are projected to have sufficient asset reserves to pay full benefits on time until 2035 and 2023, respectively. The *Bipartisan Budget Act of 2015*, passed by Congress and signed into law by the President, reallocated a portion of the payroll tax rate from the OASI Trust Fund to the DI Trust Fund. Under the intermediate assumptions, this reallocation is expected to ensure full payment of disability benefits into 2023. Without reallocation, the DI Trust Fund asset reserves were projected to have been depleted by the fourth quarter of 2016. In each case, some general revenues must be used to satisfy the authorization of full benefit payments until the year of trust fund depletion. This occurs when the trust fund interest income and balances accumulated during prior years are needed to pay benefits, which leads to a transfer from general revenues to the trust funds. Moreover, under current law, General Fund transfers to the SMI Trust Fund will occur into the indefinite future and will continue to grow with the growth in health care expenditures.

The potential magnitude of future financial obligations under these three social insurance programs is, therefore, important from a unified budget perspective as well as for understanding generally the growing resource demands of the programs on the economy. A common way to present future cash flows is in terms of their *present value*. This approach recognizes that a dollar paid or collected next year is worth less than a dollar today because a dollar today could be saved and earn a year's worth of interest.

Table 5 shows the magnitudes of the primary expenditures and sources of financing for the three trust funds computed on an open-group basis for the next 75 years and expressed in present values. The data are consistent with the Statements of Social Insurance included in the principal financial statements. For HI, revenues from the public are projected to fall short of total expenditures by $3,822 billion in present value terms which is the additional amount needed in order to pay scheduled benefits over the next 75 years.[12] From the trust fund perspective, the amount needed is $3,628 billion in present value after subtracting the value of the existing trust fund balances (an asset to the trust fund account but an intragovernmental transfer

[12] Interest income is not a factor in this table as dollar amounts are in present value terms.

to the overall budget). For SMI, revenues from the public for Part B and D combined are estimated to be $28,621 billion less than total expenditures for the two accounts, an amount that, from a budget perspective, will be needed to keep the SMI program solvent for the next 75 years. From the trust fund perspective, however, the present values of total revenues and total expenditures for the SMI Program are roughly equal due to the annual adjustment of revenue from other Government accounts to meet program costs.[13] For OASDI, projected revenues from the public fall short of total expenditures by $14,169 billion in present value dollars, and by $11,357 billion from the trust fund perspective.

From the governmentwide perspective, the present value of the total resources needed for the Social Security and Medicare Programs over and above current-law funding sources (payroll taxes, benefit taxes, and premium payments from the public) is $46,612 billion. From the trust fund perspective, which counts the trust funds ($3,076 billion in present value) and the general revenue transfers to the SMI Program ($28,621 billion in present value) as dedicated funding sources, additional resources needed to fund the programs are $14,916 billion in present value.

Table 5
Present Values of Costs Less Revenues of 75-Year Open Group Obligations
HI, SMI, and OASDI

(In billions of dollars, as of January 1, 2016)

		SMI			
	HI	Part B	Part D	OASDI	Total
Revenues from the public:					
Taxes	20,701	-	-	60,232	80,933
Premiums, State transfers	-	7,520	3,556	-	11,076
Total	20,701	7,520	3,556	60,232	92,009
Total costs to the public	24,523	27,484	12,213	74,401	138,621
Net results - budget perspective*	3,822	19,964	8,657	14,169	46,612
Revenues from other Government accounts	-	19,964	8,657	-	28,621
Trust fund balances as of 1/1/2016	194	68	1	2,813	3,076
Net results - trust fund perspective*	3,628	(68)	(1)	11,357	14,916

*Net results are computed as costs less revenues and trust fund balances. Negative values are indicative of surpluses.

Note: Totals may not equal the sum of components due to rounding.

Source: 2016 OASDI and Medicare Trustees' Reports

Infinite Horizon

The 75-year horizon represented in Table 5 is consistent with the primary focus of the Social Security and Medicare Trustees' Reports. For the OASDI Program, for example, an additional $14.2 trillion in present value will be needed above currently scheduled taxes to pay for scheduled benefits ($11.4 trillion from the trust fund perspective). Experts have noted that limiting the projections to 75 years understates the magnitude of the long-range unfunded obligations because summary measures (such as the actuarial balance and open-group unfunded obligations) reflect the full amount of taxes paid by the next two or three generations of workers, but not the full amount of their benefits. One approach to addressing the limitations of 75-year summary measures is to extend the projection horizon indefinitely, so that the overall results reflect the projected costs and revenues after the first 75 years. Such extended projections can also help indicate whether the financial imbalance would be improving or continuing to worsen beyond the normal 75-year period. The open-group infinite horizon net obligation is the present value of all expected future program outlays less the present value of all expected future program tax and premium revenues. Such a measure is provided in Table 6 for the three trust funds represented in Table 5.

[13] The SMI Trust Fund has $69 billion of existing assets.

From the budget or governmentwide perspective, the values in line 1 plus the values in line 4 of Table 6 represent the value of resources needed to finance each of the programs into the infinite future. The sums are shown in the last line of the table (also equivalent to adding the values in the second and fifth lines). The total resources needed for all the programs sums to $90.5 trillion in present value terms. This need can be satisfied only through increased borrowing, higher taxes, reduced program spending, or some combination.

The second line shows the value of the trust fund at the beginning of 2016. For the HI and OASDI Programs this represents, from the trust fund perspective, the extent to which the programs are funded. From that perspective, when the trust fund is subtracted, an additional $32.1 trillion is needed to sustain the OASDI program into the infinite future, while the HI program reflects a projected surplus of $2.8 trillion over the infinite horizon. However, looking just at present values ignores timing differences in the underlying projected cash flows; the HI Trust Fund is projected to remain solvent only until 2028. As described above, from the trust fund perspective, the SMI Program is fully funded; from a governmentwide basis, the substantial gap that exists between premiums, state transfer revenue, and program expenditures in the SMI Program ($36.8 trillion and $21.5 trillion for Parts B and D, respectively) represents future general revenue obligations of the federal budget.

In comparison to the analogous 75-year number in Table 5, extending the calculations beyond 2090, captures the full lifetime benefits, plus taxes and premiums of all current and future participants. The shorter horizon understates the total financial needs by capturing relatively more of the revenues from current and future workers and not capturing all of the benefits that are scheduled to be paid to them.

Table 6
Present Values of Costs Less Tax, Premium and State Transfer Revenue through the Infinite Horizon, HI, SMI, OASDI

(in trillions of dollars as of January 1, 2016)

		SMI			
	HI	Part B	Part D	OASDI	Total
Present value of future costs less future taxes, premiums, and state transfers for current participants	10.3	16.7	6.1	31.9	65.0
Less current trust fund balance	0.2	0.1	-	2.8	3.1
Equals net obligations for past and current participants	10.1	16.6	6.1	29.1	61.9
Plus net obligations for future participants	(13.0)	20.1	15.4	3.0	25.5
Equals net obligations through the infinite future for all participants	(2.8)	36.7	21.5	32.1	87.5
Present values of future costs less the present values of future income over the infinite horizon	(2.7)	36.8	21.5	34.9	90.5

Note: Totals may not equal the sum of components due to rounding.

Source: 2016 OASDI and Medicare Trustees' Reports

Railroad Retirement, Black Lung, and Unemployment Insurance

Railroad Retirement

The Railroad Retirement Board (RRB) was created in the 1930s to establish a retirement benefit program for the Nation's railroad workers. As the Social Security Program legislated in 1935 would not give railroad workers credit for service performed prior to 1937, legislation was enacted in 1934, 1935, and 1937 (collectively the Railroad Retirement Acts of the 1930s) to establish a railroad retirement program separate from the Social Security Program.

Railroad retirement pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

Payroll taxes paid by railroad employers and their employees provide a primary source of income for the Railroad Retirement and Survivors' Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay Tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: the RRB-SSA-CMS Financial Interchanges with the Social Security and Medicare Trust Funds, earnings on investments, federal income taxes on railroad retirement benefits, and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits). See Note 22—Social Insurance, for additional information on railroad retirement program financing.

Amounts in the Railroad Retirement Account and the SSEB Account that are not needed to pay current benefits and administrative expenses may be transferred to the NRRIT or used to offset transfers from the NRRIT to the Railroad Retirement Account. The NRRIT's sole purpose is to manage and invest railroad retirement assets. NRRIT's Board of Trustees is empowered to invest trust assets in nongovernmental assets, such as equities and debt, as well as in Government securities.

Since its inception, NRRIT has received $21.3 billion from RRB (including $19.2 billion in fiscal year 2003, pursuant to RRSIA) and returned $19.2 billion. During fiscal year 2016, the NRRIT made net transfers of $1.4 billion to the RRB to pay retirement benefits. Administrative expenses of the trust are paid out of trust assets. The balance as of September 30, 2016, and 2015, of non-federal securities and investments of the NRRIT are disclosed in Note 7—Debt and Equity Securities.

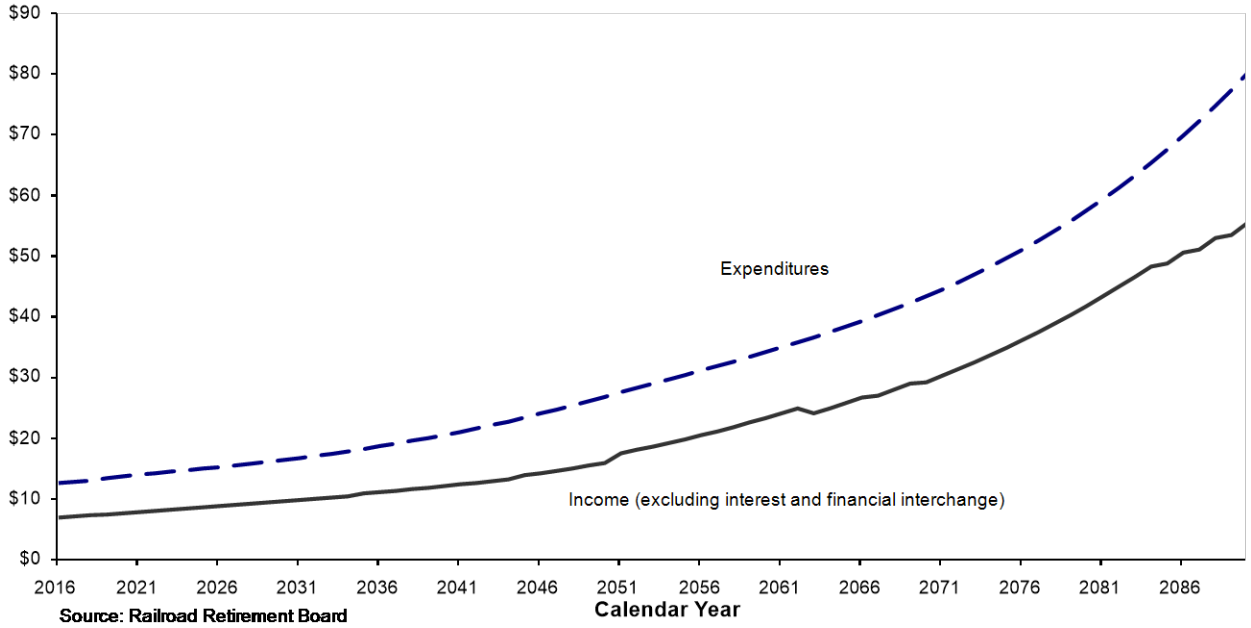
Cash Flow Projections

Economic and Demographic Assumptions. The economic and demographic assumptions used for the most recent set of projections are shown in the "Railroad Retirement" section of Note 22—Social Insurance.

Income and Expenditures. Chart 11 shows, in dollars, estimated railroad retirement income (excluding interest and financial interchange income) and expenditures for the period 2016-2090 based on the intermediate set of assumptions used in the RRB's actuarial valuation of the program. The estimates are for the open-group population, which includes all persons projected to participate in the Railroad Retirement Program as railroad workers or beneficiaries during the period. Thus, the estimates include payments from, and on behalf of, those who are projected to be employed by the railroads during the period as well as those already employed at the beginning of the period. They also include expenditures made to, and on behalf of, such workers during that period.

Chart 11—Estimated Railroad Retirement Income (Excluding Interest and Financial Interchange Income) and Expenditures 2016-2090

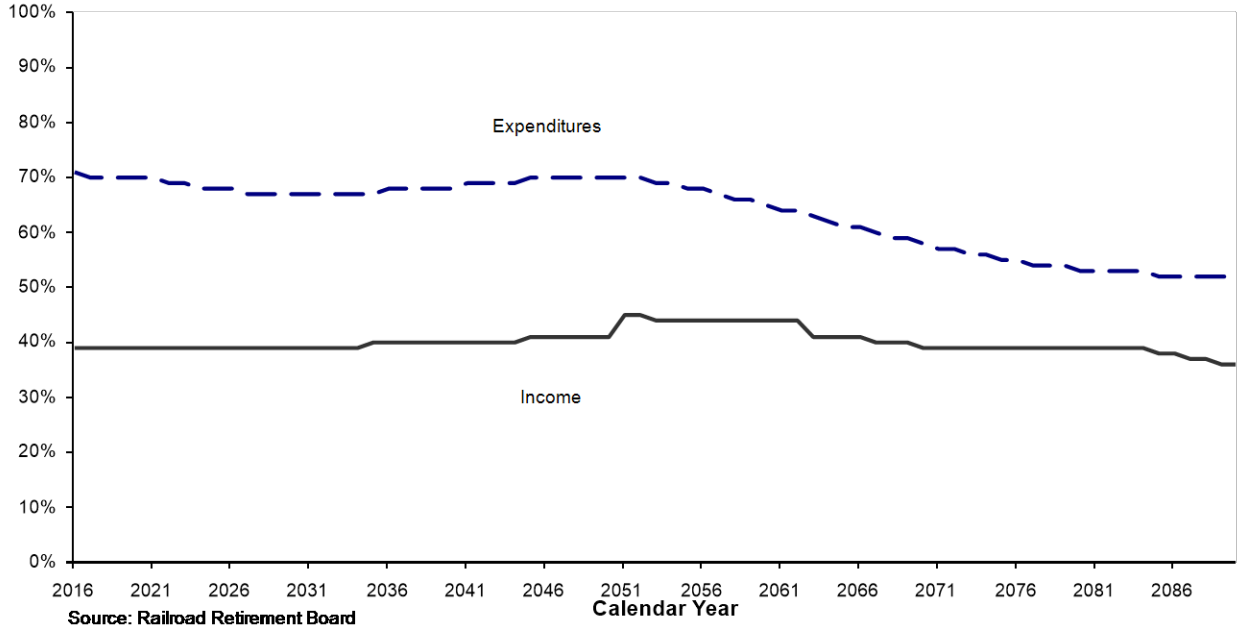
(In billions of dollars)



As Chart 11 shows, expenditures are expected to exceed tax income for the entire projection period. The imbalance generally grows at a moderate amount until about 2083 when it begins to grow a little more rapidly.

Income and Expenditures as a Percent of Taxable Payroll. Chart 12 shows estimated expenditures and income as a percent of Tier II taxable payroll. Expenditures as a percentage of payroll range between 67 percent and 71 percent through 2057, after which the percentage decreases until reaching 52 percent in 2085 through 2090. This is largely due to the anticipated decline in the number of annuitants per full-time employee.

Chart 12—Estimated Railroad Retirement Income (Excluding Interest and Financial Interchange Income) and Expenditures as a Percent of Tier II Taxable Payroll 2016-2090



Source: Railroad Retirement Board

Sensitivity Analysis. Actual future income from railroad payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors as mentioned above. Two crucial assumptions are employment growth and the interest rate. The interest rate assumption reflects the expected rate of return on NRRIT investments. Table 7 shows the sensitivity of the shortfall in the Railroad Retirement Program to variations in these two assumptions. Note that beginning in fiscal year 2016, the present values are on a fiscal year basis, as of October 1. In the past, present values were on a calendar year basis, as of January 1. The low-cost employment scenario has a 7.1 percent smaller shortfall of income to expenditures, and the high-cost scenario has a 7.6 percent higher shortfall. A higher discount rate reduces future values relative to a lower rate. As seen in the table, the shortfall is 27.0 percent lower if the interest rate is 10.0 percent rather than 7.0 percent and 69.9 percent higher when the interest rate is 4.0 percent rather than 7.0 percent.

Table 7
Present Values of Railroad Retirement Expenditures in Excess of Income Under Various Employment and Interest Rate Assumptions, 2016-2090

(Dollar values in billions; values of assumptions shown in parentheses)

Assumption	Low	Middle	High
Employment[1]	98.6 (-0.5%)	106.1 (-2.0%)	114.2 (-3.5%)
Interest rate	77.5 (10.0%)	106.1 (7.0%)	180.3 (4.0%)

[1] The low and middle employment scenarios have passenger service employment remaining at 46,000 workers per year and the remaining employment base declining at 0.5 percent and 2.0 percent, respectively, for 25 years, at a reducing rate over the next 25 years, and remaining level thereafter. The high-cost scenario has passenger service employment declining by 500 workers per year until a level of 35,000 is reached with the remaining employment base declining by 3.5 percent per year for 25 years, at a reducing rate over the next 25 years, and remaining level thereafter.

Source: Railroad Retirement Board

Sustainability of Railroad Retirement

Table 8 shows the magnitudes of the primary expenditures and sources of financing for the Railroad Retirement Program computed on an open-group basis for the next 75 years and expressed in present values as of October 1, 2015. The data are consistent with the Statements of Social Insurance.

From a governmentwide perspective, revenues are expected to fall short of expenditures by approximately $106.1 billion, which represents the present value of resources needed to sustain the Railroad Retirement Program. From a trust fund perspective, when the trust fund balance and the financial interchange and transfers are included, the combined balance of the NRRIT, the Railroad Retirement Account, and the SSEB Account show a slight surplus.

Table 8
Present Values of 75-Year Projections of Revenues and Expenditures for the Railroad Retirement Program[1,2]

(In billions of present-value dollars as of October 1, 2015)

Estimated future income (excluding interest) received from or on behalf of: [3]	
Current participants who have attained retirement age	8.4
Current participants not yet having attained retirement age	73.1
Those expected to become participants	72.8
All participants	154.3
Estimated future expenditures: [4]	
Current participants who have attained retirement age	131.2
Current participants not yet having attained retirement age	99.0
Those expected to become participants	30.2
All participants	260.4
Net obligations from budget perspective (expenditures less income)	106.1
Railroad retirement program assets (mostly investments stated at market) [5]	26.3
Financial interchange from Social Security Trust	81.5
Net obligations from trust fund perspective	(1.7)

[1] Represents combined values for the Railroad Retirement Account, SSEB Account, and NRRIT, based on middle employment assumption.
[2] The data used reflect the provisions of RRSIA of 2001.
[3] Future income (excluding interest) includes Tier I taxes, Tier II taxes, and income taxes on benefits.
[4] Future expenditures include benefits and administrative expenditures.
[5] The value of the fund reflects the 7.0 percent interest rate assumption. The RRB uses the relatively high rate due to investments in private securities.

Note: Totals may not equal the sum of components due to rounding. Employee and beneficiary status are determined as of 1/1/2015, whereas present values are as of 10/1/2015.

Source: Railroad Retirement Board

Black Lung

The *Federal Coal Mine Health and Safety Act of 1969* created the Black Lung Disability Benefit Program to provide compensation, medical, and survivor benefits for eligible coal miners who are totally disabled due to pneumoconiosis (black lung disease) arising out of their coal mine employment and to eligible survivors of coal miners who died due to pneumoconiosis. DOL operates the Black Lung Disability Benefit Program. Prior to fiscal year 2016, the beneficiary population was assumed to be a nearly closed universe in which attrition by death exceeds new entrants by a ratio of more than ten to one. During fiscal year 2016, the number of participants who joined the rolls increased due to, among other things, adjudicated liability as a result of responsible mine operator (RMO) bankruptcy.

Excise taxes on coal mine operators, based on the domestic sale of coal, are the primary source of financing black lung disability payments and related administrative costs. The *Black Lung Benefits Revenue Act* provided for repayable advances to the BLDTF from the General Fund, in the event that BLDTF resources were not adequate to meet program obligations. Prior to legislation enacted in 2008 that allowed for the restructuring of BLDTF debt, the trust fund had accumulated large liabilities from significant and growing shortfalls of excise taxes relative to benefit payments and interest expenses.

The *Energy Improvement and Extension Act of 2008* (Public Law 110-343), enacted on October 3, 2008, contained several provisions that significantly improved the BLDTF's financial position, including:

- Continuation of a previously-enacted increase in coal excise tax rates for an additional 5 years, through December 2018;
- Provision for the restructuring of BLDTF debt by refinancing the outstanding repayable advances with proceeds from issuing new debt instruments with lower interest rates; and
- Establishment of a one-time appropriation that significantly reduced the outstanding debt of the BLDTF.

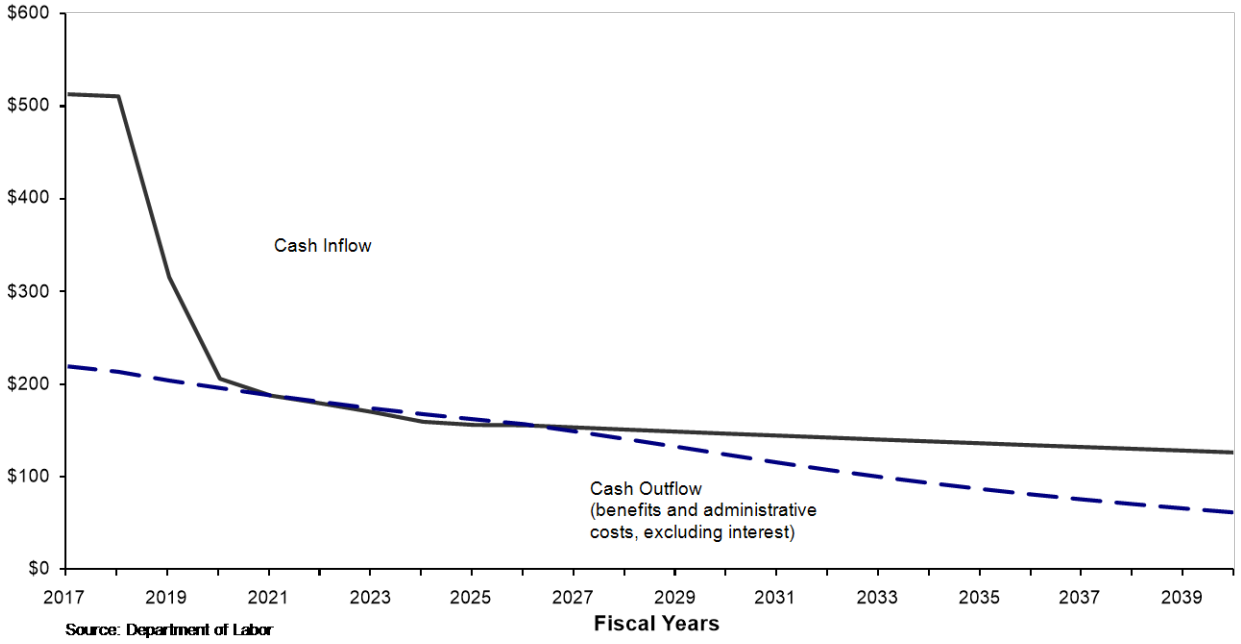
This Act also allowed that any debt issued by the BLDTF subsequent to the refinancing may be used to make benefit payments, other authorized expenditures, or to repay debt and interest from the initial refinancing. All debt issued by the BLDTF was effected as borrowing from the Treasury's Bureau of the Fiscal Service.

On September 30, 2016, total liabilities of the BLDTF exceeded assets by $5.6 billion. This net position represents the accumulated shortfall of excise taxes necessary to meet benefit payments, administrative costs, and interest expense incurred prior to and subsequent to the debt refinancing pursuant to P.L. 110-343. Prior to the enactment of Public Law 110-343, this shortfall was funded by repayable advances to the BLDTF, which were repayable with interest. Pursuant to Public Law 110-343, these repayable advances were restructured as zero coupon bonds and any future shortfall is financed with one-year borrowing from Treasury. Outstanding debt at September 30, 2016 was $5.7 billion, bearing interest rates ranging from 0.589% to 4.556%. Excise tax revenues of $439.6 million, benefit payment expense of $122.8 million, and interest expense of $213.7 million were recognized for the year ended September 30, 2016. The interest expense is accrued and capitalized to the principal of the debt until the debt reaches its face value at the time of maturity. On September 30, 2016, the BLDTF issued debt in the amount of $910.0 million, bearing interest at 0.589% and maturing on September 30, 2017. At September 30, 2016, there were 25 debt instruments with staggered maturities of September 30 for years 2017 through 2040, with a total carrying value of nearly $5.7 billion and a total face value at maturity of nearly $8.9 billion. Of these 25 debt instruments, 24 are from the October 2008 refinancing and one debt instrument was issued on September 30, 2016.

From the budget or consolidated financial perspective, Chart 13 shows projected black lung expenditures (excluding interest) and excise tax collections for the period 2017-2040 in constant dollars. The significant assumptions used in the most recent set of projections, in constant dollars, are coal excise tax revenue estimates, the tax rate structure, the number of beneficiaries, life expectancy, federal civilian pay raises, medical cost inflation, the interest rate on new debt issued by the BLDTF, and the CPI-U for goods and services. The projected coal excise tax revenue estimates reflect, among other things, regulation pursuant to the Clean Power Plan, and future cash inflows from excise taxes have decreased significantly from those reported in prior years. The projections, in constant dollars for the open group, made over the 24-year period ending September 30, 2040, indicate that cash inflows from excise taxes will exceed cash outflows for benefit payments and administrative expenses for most of the years in the projection period. Cumulative net cash inflows are projected to reach $827.0 million by fiscal year 2040. However, when payments from the BLDTF's maturing debt are applied against this surplus cash inflow, the BLDTF's cash flow turns negative in all periods included in the projections. Net cash outflows after payments on maturing debt are projected to reach $8.1 billion by the end of fiscal year 2040, resulting in a projected deficit of nearly $10.95 billion at September 30, 2040.

Chart 13—Estimated Black Lung Disability Trust Fund Income and Expenditures (Excluding Interest) in Constant (or Inflation-Adjusted) Dollars 2017-2040

(In millions of dollars)



Source: Department of Labor

Table 9
Present Values of 24-Year Projections of Expenditures and Revenues for the Black Lung Disability Trust Fund

(in billions of present value dollars as of September 30, 2016)

Projected future expenditures	3.5
Projected future tax income	4.8
Net obligations from budget perspective (expenditures less income)	(1.3)
Accumulated balance due General Fund	5.6
Net obligations from trust fund perspective	4.3

Note: Totals may not equal the sum of components due to rounding.

Source: Department of Labor

Table 9 shows present values of 24-year projections of expenditures and revenues for the Black Lung Disability Trust Fund computed as of September 30, 2016. Cash flows were discounted using a rate of 1.63 percent. From a governmentwide (budget) perspective, the present value of expenditures is expected to be less than the present value of income by $1.3 billion (a surplus). From a trust fund perspective, a large balance ($5.6 billion) is owed to the General Fund. From that perspective, when that accumulated balance is combined with the cash flow surplus, the program has a shortfall of $4.3 billion in present value dollars.

Unemployment Insurance

The Unemployment Insurance Program was created in 1935 to provide temporary partial wage replacement to workers who lost their jobs. The program is administered through a unique system of federal and state partnerships established in federal law but administered through conforming state laws by state agencies. The program includes the 50 states and Puerto Rico, U.S. Virgin Islands, and the District of Columbia. DOL interprets and enforces federal law requirements and provides broad policy guidance and program direction, while program details such as benefit eligibility, duration, and amount of benefits are established through individual state unemployment insurance statutes and administered through state unemployment insurance agencies.

The program is financed through the collection of federal and state unemployment taxes that are credited to the UTF and reported as federal tax revenue. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for federal and state administration of the Unemployment Insurance Program, veterans' employment services, state employment services, and the federal share of extended unemployment insurance benefits. Federal unemployment taxes also are used to maintain a loan account within the UTF, from which insolvent state accounts may borrow funds to pay unemployment insurance benefits.

Chart 14 shows the projected cash contributions and expenditures over the next 10 years under expected economic conditions (described below) in constant dollars. The significant assumptions used in the projections include total unemployment rates, civilian labor force levels, percent of unemployed receiving benefits, total wages, distribution of benefit payments by state, state tax rate structures, state taxable wage bases, interest rates on UTF investments, and the Consumer Price Index for goods and services. These projections, excluding interest earnings, indicate a positive net cash flow in fiscal year 2017 through fiscal year 2026.

The *Federal/State Extended Unemployment Compensation Act of 1970* provides for the extension of the duration of unemployment insurance benefits during periods of high unemployment to individuals who have exhausted their regular unemployment benefits. When the insured unemployment level within a state, or in some cases total unemployment, reaches certain specified levels, the state must extend benefit duration by 50 percent, up to a combined maximum of 39 weeks; certain states voluntarily extended the benefit duration up to a combined maximum of 46 weeks. These extended benefits are financed one-half by state unemployment taxes and one-half by federal unemployment taxes. However, the *American Recovery and Reinvestment Act of 2009* (ARRA) began temporary 100 percent federal funding of extended benefits.

Subsequent legislation, most recently P.L. 112-240, the *American Taxpayer Relief Act of 2012*, authorized continuing 100 percent federal funding of extended unemployment benefits to December 31, 2013.

During prolonged periods of high unemployment, Congress may authorize the payment of emergency unemployment benefits to supplement extended Unemployment Insurance (UI) benefit payments. Emergency benefits began in July 2008, authorized under the *Supplemental Appropriations Act, 2008*. This emergency program was temporarily extended and additionally funded by the ARRA of 2009 and has been subsequently modified several times, most recently by P.L. 112-240, the *American Taxpayer Relief Act of 2012*, which extended the emergency unemployment insurance program to January 1, 2014. Although the programs for emergency unemployment benefits and 100 percent federal funding of extended unemployment benefits expired in fiscal year 2014, the UI program continues to process residual transactions for benefit costs incurred prior to the programs' expiration. Total cash inflows exceed total cash outflows in fiscal year 2017 and throughout the projection period. The net inflow (excluding interest) decreases from $12.6 billion in fiscal year 2017 to $11.2 billion in fiscal year 2018 and decreases from about $7.0 billion to less than $900 million between fiscal years 2019 and 2026. The net inflow is sustained primarily by the excess of federal tax collections over federal expenditures in fiscal years 2017 through 2023, and then primarily by interest on federal securities in fiscal years 2024 through 2026.

Chart 14—Estimated Unemployment Trust Fund Cash Flow Using Expected Economic Conditions in Constant (or Inflation-Adjusted) Dollars 2017-2026

(In billions of dollars)

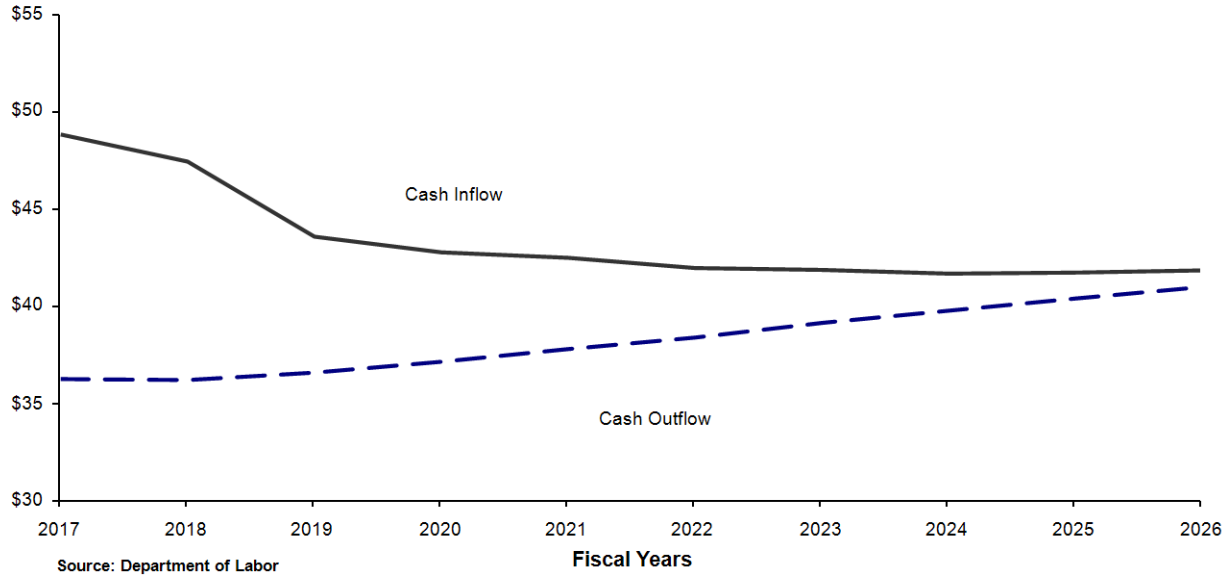


Table 10 shows 10-year projections of revenues and expenditures for the Unemployment Insurance Program in constant dollars. Three sets of numbers are presented in order to show the effects of varying economic conditions as reflected in different assumptions about the unemployment rate. For expected economic conditions, the estimates are based on an unemployment rate of 4.68 percent during fiscal year 2017, and remaining between 4.60 percent and 4.80 percent thereafter. Under Sensitivity Analysis I which utilizes a higher unemployment rate of 5.83 percent beginning in fiscal year 2017, net cash inflows are negative in fiscal years 2017 through 2020, but become positive in fiscal year 2021, and continue to be positive through 2026. Under Sensitivity Analysis II, which utilizes a higher unemployment rate of 6.11 percent in fiscal year 2017, net cash outflows including interest earnings and expenses, are projected in fiscal years 2017 through 2022 by amounts between about $400 million and $35.0 billion, but outflows exceed inflows in fiscal years 2023 through 2026 by amounts between $2.8 billion and $12.0 billion. Net cash inflows are reestablished in fiscal year 2023 and peak in fiscal year 2025 with a drop in the unemployment rate to 8.30 percent in fiscal year 2020 and then steadily downward for fiscal years 2021 through 2026.

Each analysis uses an open group that includes current and future participants of the Unemployment Insurance Program. Table 10 shows the impact on the UTF projections of varying projected unemployment rates. For example, in Sensitivity Analysis II, while tax income is projected to increase as higher layoffs result in higher employer taxes, benefit outlays increase even more. From the Governmentwide (budget) perspective, under expected conditions, future cash income exceeds future expenditures by $51.5 billion. From the same perspective, under Sensitivity Analysis II, future cash expenditures exceed future income by $66.4 billion. From a trust fund perspective, which takes into account the $45.2 billion trust fund balance, the program has a surplus of $41.9 billion under the economic conditions for Sensitivity Analysis I.

Table 10
10-Year Projections of Expenditures and Revenues for Unemployment Insurance in Constant (or Inflation-Adjusted) Dollars Under Three Alternative Analyses for Economic Conditions

(in billions as of September 30, 2016)

	Economic Conditions		
	Expected	**Sensitivity Analysis I**	**Sensitivity Analysis II**
Projected future expenditures	382.8	540.4	684.5
Projected future cash income	434.3	537.1	618.1
Net obligations from budget perspective (expenditures less income)	(51.5)	3.3	66.4
Trust fund assets	45.2	45.2	45.2
Net obligations from trust fund perspective [1]	(96.7)	(41.9)	21.2

[1]Net obligations from the trust fund perspective equals net obligations from the budget perspective minus trust fund assets. The negative values in this line are indicative of surpluses.

Note: Totals may not equal the sum of components due to rounding.

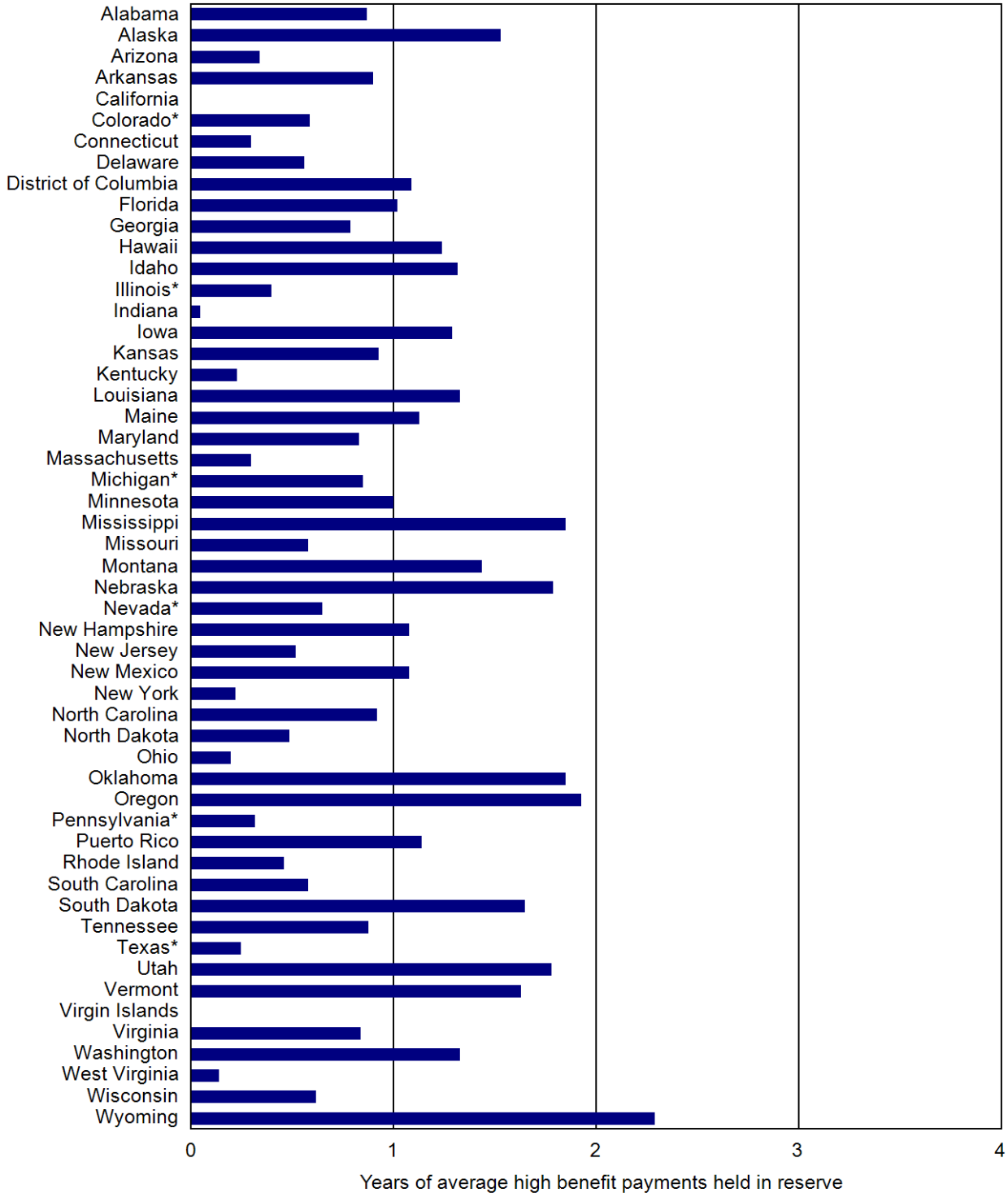
Source: Department of Labor

Unemployment Trust Fund Solvency

Each state's accumulated UTF net assets or reserve balance should provide a defined level of benefit payments over a defined period. To be minimally solvent, a state's reserve balance should provide for one year's projected benefit payment needs based on the highest levels of benefit payments experienced by the state over the last 20 years. A ratio of 1.0 or greater indicates a state is minimally solvent. States below this level are vulnerable to exhausting their funds in a recession. States exhausting their reserve balance borrow funds from the Federal Unemployment Account (FUA) to make benefit payments. In fiscal year 2016, there were no FUA borrowings, and in fiscal year 2015, the FUA repaid all its outstanding borrowings.

Chart 15 presents the state by state results of this analysis as of September 30, 2016. As the chart illustrates, 30 state funds plus the fund of the Virgin Islands were below the minimal solvency ratio of 1.0 at September 30, 2016.

Chart 15—Unemployment Trust Fund Solvency as of September 30, 2016



*State has outstanding Unemployment Insurance bond debt to private bondholders which is not included in its current trust fund balance solvency level.

Deferred Maintenance and Repairs

Deferred maintenance and repairs result from maintenance not being performed on a timely basis and is the estimated cost to bring Government-owned property, plant, and equipment to an acceptable condition. Deferred maintenance and repairs exclude the cost of expanding the capacity of assets or upgrading them to serve needs different from those originally intended. The consequences of not performing regular maintenance and repairs could include increased safety hazards, poor service to the public, higher costs in the future, and inefficient operations. Estimated deferred maintenance and repairs costs are not accrued in the Statements of Net Cost or recognized as a liability on the Balance Sheets.

The amounts disclosed for deferred maintenance and repairs are allowed to be measured using one of the following three methods:

- Condition assessment surveys which are periodic inspections of Government-owned property to determine the current condition and estimated cost to bring the property to an acceptable condition.
- Life-cycle cost forecast that is an acquisition or procurement technique that considers operation, maintenance, and other costs in addition to the acquisition cost of assets.
- Any other method of choice that is similar to the condition assessment survey or life-cycle costing methods.

The table below of deferred maintenance and repairs is presented as a single estimate in accordance with SFFAS No. 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32.* These amounts were all measured using the condition assessment survey method. Please refer to the individual financial statements of DOI, DOD, USDA, DOE, HHS, NASA, and VA for detailed significant information on deferred maintenance and repairs.

Deferred Maintenance and Repairs as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Asset category:		
General property, plant, and equipment	165.3	167.5
Heritage assets	19.5	15.6
Stewardship land	0.4	0.4
Total deferred maintenance and repairs	185.2	183.5

Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest) that may be paid for claims pending judicial review by the federal courts or, internally, by appeals. The total estimated payout (including principal and interest) for claims pending judicial review by the federal courts is $4.8 billion and $2.1 billion for fiscal years 2016 and 2015, respectively. For those under appeal, the estimated payout is $2.3 billion and $2.7 billion for fiscal years 2016 and 2015, respectively. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, for reporting the amounts in the balance sheets or for disclosure in the notes to the financial statements. However, they meet the criteria in SFFAS No. 7, *Accounting for Revenue and Other Financing Sources*, for inclusion as required supplementary information. To the extent judgments against the Government for these claims prompt other similarly situated taxpayers to file similar refund claims, these amounts could become significantly greater.

Tax Assessments

The Government is authorized and required to make inquiries, determinations, and assessments of all taxes that have not been duly paid. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as enforcement programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. Under federal accounting standard, unpaid assessments are categorized as taxes receivable if taxpayers agree or a court has determined the assessments are owed. If neither of these conditions are met, the unpaid assessments are categorized as compliance assessments. Assessments with little or no future collection potential are called write-offs. Although compliance assessments and write-offs are not considered receivables under federal accounting standards, they represent legally enforceable claims of the Government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

Compliance assessments and pre-assessment work in process are $77.3 billion and $82.1 billion for fiscal years 2016 and 2015, respectively. The amount of allowance for uncollectible amounts pertaining to compliance assessments cannot be reasonably estimated, and thus the net realizable value of the value of the pre-assessment work-in-process cannot be determined. The amount of assessments that agencies have statutory authority to collect at the end of the period but that have been written off and excluded from accounts receivable are $139.0 billion and $138.0 billion for fiscal years 2016 and 2015, respectively.

Risk Assumed

Risk assumed information is important for all federal insurance and guarantee programs (i.e., USDA-Federal Crop Insurance Corporation programs, DHS-National Flood Insurance Program, NCUA-Credit Unions), except social insurance, life insurance, and loan guarantee programs. Risk assumed is generally measured by the present value of unpaid losses net of associated premiums, based on the risk inherent in the insurance or guarantee coverage in force. In addition to the liability for unpaid insurance claims included in Note 15─Insurance and Guarantee Program Liabilities, for events that have already occurred, the Government also is required to report as supplementary information risk assumed amounts and the periodic changes in those amounts.

The assessments of losses using the risk assumed are made by actuarial or financial methods that include information and assumptions applicable to the economic, legal, and policy environment in force at the time the assessments are made. Management has estimated the loss amounts based on the risk assumed as well as the periodic changes.

Please refer to the individual financial statements of the USDA, and NCUA for further detailed information, including information as to the indicators of the range of uncertainty around expected estimates and the indicators of the sensitivity of the estimates to changes in major assumptions. The table does not include all federal insurance and guarantee programs.

Risk Assumed Information as of September 30, 2016, and 2015

(In billions of dollars)	2016	2015
Present value of unpaid losses, net of associated premiums:		
Department of Agriculture - Federal Crop Insurance Corporation programs	8.3	7.6
National Credit Union Administration - Credit Unions	0.2	0.2
Total	8.5	7.8
Period changes in risk assumed amounts:		
Department of Agriculture	0.7	-
Department of Homeland Security	-	(0.4)
Total	0.7	(0.4)

Federal Oil and Gas Resources

DOI plays an integral part in the implementation of the President's *Blueprint for a Clean and Secure Energy Future*, designed to build a safe, secure energy future by using cleaner, alternative fuels to power our homes and economy, producing more oil and gas domestically, and improving energy efficiency. The DOI is responsible for managing the nation's oil and natural gas resources and the mineral revenues on federal lands, both onshore and on the Outer Continental Shelf. This management process can be broken down into six essential analysis components: pre-leasing, post-leasing and pre-production, production and post-production, revenue collection, fund disbursement, and compliance.

Federal Oil and Gas Resources as of September 30, 2016, and 2015

(In billions of dollars)	Offshore		Onshore		Total	
	2016	2015	2016	2015	2016	2015
Oil and lease condensate	23.7	31.6	12.8	14.8	36.5	46.4
Natural gas, wet after lease separation	2.6	2.8	12.3	14.1	14.9	16.9
Total	26.3	34.4	25.1	28.9	51.4	63.3

The above table presents the estimated present value of future federal royalty receipts on estimated proved reserves[14] as of September 30, 2016 and 2015. The federal government's estimated petroleum royalties have as their basis the DOE's Energy Information Administration (EIA) estimates of proved reserves. The EIA provides such estimates directly for federal offshore areas and they are adjusted to extract the federal subset of onshore proved reserves. The federal proved reserves were then further adjusted to correspond with the effective date of the actual production for calendar year 2014, the most recently published EIA proved reserves report and then are projected, separately for oil and natural gas, over time to simulate a schedule of when the reserves would be produced. Future royalties are then calculated from these production streams by applying future price estimates by the OMB, and effective royalty rates, adjusted for transportation allowances and other allowable deductions. The valuation method used for gas captures royalties from three products–dry gas, wet gas, and natural gas liquids–which collectively are reported as natural gas, wet after lease separation. The present value of these royalties are then determined by discounting the revenue stream back to the effective date at a public discount rate assumed to be equal to the OMB's estimates of future 30-year Treasury bill rates. The 30-year rate was chosen because this maturity life most closely approximates the productive lives of the proved reserves estimates.

[14] Per the EIA, lease condensate is a mixture consisting primarily of pentanes and heavier hydrocarbons which is recovered as a liquid from natural gas in lease separation facilities. This category excludes natural gas plant liquids, such as butane and propane, which are recovered at downstream natural gas processing plants or facilities. Also per the EIA, natural gas, wet after lease separation, is the volume of natural gas remaining after removal of lease condensate in lease and/or field separation facilities, if any, and after exclusion of nonhydrocarbon gases where they occur in sufficient quantity to render the gas unmarketable. Natural gas liquids may be recovered from volume of natural gas, wet after lease separation, and at natural gas processing plants (http://www.eia.gov/naturalgas/data.cfm).

Estimated Federal Oil and Gas Petroleum Royalties (Proved Reserves)
As of September 30, 2016, and 2015

Petroleum Category	Quantity (in millions)		Average Purchase Price ($)		Average Royalty Rate (%)	
	2016	2015	2016	2015	2016	2015
Oil and lease condensate (Bbl):						
Offshore	4,362.2	4,623.6	37.77	56.45	13.08	13.42
Onshore	2,655.0	2,377.1	35.79	49.95	12.14	12.26
Total	7,017.2	7,000.7				
Natural gas, wet after lease separation (Mcf):						
Offshore	7,327.7	6,858.8	2.43	3.25	11.77	12.84
Onshore	44,836.7	46,310.8	2.31	3.14	9.68	10.11
Total	52,164.4	53,169.6				

Bbl = barrels
Mcf = 1,000 cubic feet

The table above provides the estimated quantity, a weighted average purchase price, and a weighted average royalty rate by category of estimated federal petroleum royalties at the end of fiscal year 2016 and 2015.[15] The estimated quantities, average purchase prices and royalty rates vary by region; the above table reflects an overall weighted average purchase price and royalty rate, and is not presented on a regional basis, but is instead calculated based on regional averages. The prices and royalty rates are based upon historical (or estimated) averages, excluding prior-period adjustments, if any, and are affected by such factors as accounting adjustments and transportation allowances, resulting in effective average prices and royalty rates. Prices are valued at the lease rather than at the market center, and differ from those used to compute the asset estimated present values, which are forecasted and discounted based upon OMB economic assumptions. For further details on federal oil and gas resources, refer to the financial statements of DOI. In addition to the oil and gas resources discussed above, the federal government also owns oil and gas resources that are not currently under lease.

[15] Gulf of Mexico proved reserves are royalty bearing volumes. In the Gulf of Mexico, an additional 884.3 million Bbl for fiscal year 2016 and 879.0 million Bbl for fiscal year 2015 of proved oil reserves, and 1,104.2 million Mcf for fiscal year 2016 and 1,097.0 million Mcf for fiscal year 2015 of proved gas reserves are not reflected in these totals as they are estimated to be producible royalty free under various royalty relief provisions. The net present value of the royalty value of the royalty free proved reserves volumes in the Gulf of Mexico is estimated to be $5.0 billion for fiscal year 2016 and $6.5 billion for fiscal year 2015.

Federal Natural Resources Other than Oil and Gas

Federal Natural Resources Other than Oil and Gas as of September 30, 2016, and 2015

(in billions of dollars)

Natural Resource Category	2016	2015
Coal royalties	8.8	10.5
Total	8.8	10.5

DOI plays an integral part in the implementation of the President's *Blueprint for a Clean and Secure Energy Future* which is designed to build a safe, secure energy future by using cleaner, alternative fuels to power our homes and economy, producing more oil and gas domestically and improving energy efficiency. DOI is responsible for managing the Nation's coal resources and revenues on federal lands.

The Office of Natural Resources Revenue (ONRR) within DOI is responsible for the management and collection of revenues associated with federal coal leases which are managed by the Bureau of Land Management (BLM) within DOI. The ONRR achieves optimal value by ensuring that all natural resource revenues are efficiently and accurately collected as well as disbursed to recipients in a timely manner by performing audit and revenue compliance activities.

The Mineral Leasing Act of 1920, as amended, and the *Mineral Leasing Act for Acquired Lands of 1947*, as amended, gives DOI the responsibility for coal leasing on approximately 700 million acres of federal mineral estate which includes 570 million of acres where coal development is allowed. The surface estate of these lands may be under the control of BLM, the U.S. Forest Service (within USDA), private or state land owners, or other federal agencies.

Public lands are available for coal leasing after the lands have been evaluated through a multiple-use planning process. *The Mineral Leasing Act,* as amended by the *Federal Coal Leasing Amendments Act of 1976*, generally requires that coal be leased competitively and that the federal government must receive a fair market value for land leased for coal development. Once a lease is issued, federal coal leasing laws and lease terms determine the federal government's share of production from coal leasing operations.

DOI receives coal leasing revenues from a bonus paid at the time of the lease, an annual rent payment of $3.00 per acre, and royalties paid on the value of the coal after it has been mined. A portion of the total federal coal royalties will be distributed to other non-federal entities. The royalty rate for surface-mining methods is 12.5 percent and is 8 percent for underground mining, and the BLM can approve reduced royalty rates based on maximum economic recovery. Regulations that govern BLM's coal leasing program are contained in Title 43, Groups 3000 and 3400 of the Code of Federal Regulations.

The above table presents the estimated present value of federal coal royalties under lease contract or other long-term arrangements as of September 30, 2016 and 2015. The federal government's estimated coal royalties have as their basis the DOI's BLM estimates of recoverable reserves. The federal recoverable reserves are then further adjusted to correspond with the effective date of the analysis and then are projected over time to simulate a schedule of when the reserves would be produced. Futures royalties are then calculated by applying future price estimates and effective royalty rates, adjusted for transportation allowances and other allowable deductions. The present value of these royalties are then determined by discounting the revenue stream back to the effective date at a public discount rate assumed to be equal to the OMB's estimates of future 30-year Treasury bill rates. The 30-year rate was chosen because this maturity life most closely approximates the productive lives of the recoverable reserves estimates.

In addition to the coal resources discussed above, the federal government has other natural resources under lease contract whereby the lessee is required to pay royalties on the sale of the natural resource. These natural resources include soda ash, potash muriates of potash and langbeinite phosphate, lead concentrate, copper concentrate, and zinc concentrate. Soda ash and potash have the largest estimated present value of future royalties. The federal government also owns coal resources and certain other natural resources that are not currently under lease. For further details on federal natural resources-other than oil and gas, refer to the financial statements of DOI.

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United States Government Other Information (Unaudited) for the Years Ended September 30, 2016, and 2015

Unexpended Balances of Budget Authority

For the past two fiscal years, the President's budget has been available before the publication date of the *Financial Report*. However, the President's Fiscal Year 2018 Budget will not be released before publication of the *Financial Report* for fiscal year 2016. The President's budget with actual unexpended balances of budget authority for fiscal year 2016 is expected to be released in February 2017. Therefore, unexpended balances of budget authority reported below reflect the amounts previously published in the 2015 *Financial Report*.

The President's budget and the federal budget process largely use a distinct administrative process of accounting, through which federal agencies control, monitor, and report on the status of funds at their disposal. Government agencies can be granted authority to enter into obligations that result in immediate or future outlays by law; this authority is known as budget authority. Unexpended balances of budget authority consist of the unobligated and obligated, but unliquidated balances.

Unobligated balances, including amounts for trust funds, are the cumulative amount of budgeted balances that are not contractually committed or bound legally by the government and that remain available for obligation. At the end of each fiscal year, unobligated balances that are still available for new obligations are carried forward to the start of the next fiscal year. Unobligated balances that are expiring (i.e., are not available for new obligation) are canceled and not carried forward to the start of the next fiscal year. The total unobligated balances as of September 30, 2015, and 2014, are $896.0 billion and $871.6 billion, respectively.

Obligated balances refer to the balances where there have been legally binding action but for which payment has not yet been made; however, payment will be required in the future. By law, obligated balances are either no-year, or available to pay unpaid expenses (normally for five expired years, after which the obligated balances are canceled). In no-year accounts, the unobligated balance is carried forward until specifically rescinded by law, or the head of the agency concerned or the President determines that the purposes for which it was provided have been accomplished and disbursements have not been made against the appropriation for two consecutive years. Therefore, the obligated balances that are still available are carried forward to the start of the next fiscal year. The total obligated balances as of September 30, 2015, and 2014, are $1,413.5 billion and $1,399.5 billion, respectively.

The President's Fiscal Year 2017 Budget (issued on February 9, 2016) is located at www.whitehouse.gov/omb and includes the actual unexpended balances of budget authority for fiscal year 2015 in the supplemental materials section under "Balances of Budget Authority."

Tax Burden

The Internal Revenue Code provides for progressive tax rates, whereby higher earned income is generally subject to higher tax rates. The following tables present the latest available information on income tax and related income, deductions, and credit: for individuals by income level, and for corporations by size of assets.

Individual Income Tax Liability for Tax Year 2014

Adjusted Gross Income (AGI)	Number of Taxable Returns (In thousands)	AGI (in millions of dollars)	Total Income Tax (in millions of dollars)	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	36,377	72,237	1,968	1,986	54	2.7%
$15,000 under $30,000	30,212	665,587	18,657	22,031	618	2.8%
$30,000 under $50,000	26,072	1,021,446	56,423	39,178	2,164	5.5%
$50,000 under $100,000	32,221	2,303,583	201,406	71,493	6,251	8.7%
$100,000 under $200,000	17,501	2,361,756	297,112	134,950	16,977	12.6%
$200,000 under $500,000	4,979	1,419,777	276,487	285,153	55,531	19.5%
$500,000 or more	1,245	1,926,649	525,744	1,547,509	422,284	27.3%
Total	148,607	9,771,035	1,377,797			

Corporation Income Tax Liability for Tax Year 2013

Total Assets (In thousands of dollars)	Income Subject to Tax (in millions of dollars)	Total Income Tax After Credits (in millions of dollars)	Percentage of Income Tax After Credits to Taxable Income
Zero Assets	43,388	11,044	25.5%
$1 under $500	6,981	1,364	19.5%
$500 under $1,000	4,100	1,035	25.2%
$1,000 under $5,000	11,476	3,376	29.4%
$5,000 under $10,000	7,737	2,502	32.3%
$10,000 under $25,000	12,949	4,236	32.7%
$25,000 under $50,000	12,133	3,918	32.3%
$50,000 under $100,000	14,511	4,666	32.2%
$100,000 under $250,000	25,250	8,047	31.9%
$250,000 under $500,000	29,332	9,040	30.8%
$500,000 under $2,500,000	133,541	39,321	29.4%
$2,500,000 or more	957,085	204,808	21.4%
Total	1,258,483	293,357	

Tax Gap

The tax gap is the difference between what taxpayers should pay and what they actually pay on time. The tax gap, about $458.0 billion annually based on updated estimates, represents the amount of noncompliance with the tax laws. It is estimated that $52.0 billion of the gross tax gap will eventually be collected resulting in a net tax gap of $406.0 billion. 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 (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 three types of noncompliance: not filing required tax returns on time or at all (the nonfiling 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). Underreporting of income tax, employment taxes, and other taxes represents 84 percent of the gross tax gap. 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. 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 assessed 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 IRS 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 IRS' 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 non-compliance).

Unmatched Transactions and Balances

(in millions of dollars)	Fiscal Year 2016	Fiscal Year 2015
Change in intragovernmental unmatched balances:		
Debt/investment	3.8	(32.0)
Interest payable/receivable*	(2.7)	1.8
Interest payable/receivable-loans and not otherwise classified*	6.5	-
Accounts payable/receivable capital transfers	(13.4)	2.8
Loans payable/receivable	(1.1)	(1.6)
Benefit program contributions payable/receivable	12.4	33.7
Accounts payable/receivable	167.6	314.4
Advances from/to others & deferred credits/prepayments	(301.7)	(295.6)
Transfers payable/receivable	14.5	24.0
Other assets/liabilities	1,976.1	(4,360.1)
Fund balance with Treasury	1,074.7	(11,961.6)
Asset for custodial and non-entity asset/liability	13,727.7	(12,065.1)
	16,664.4	(28,339.3)
Unmatched intragovernmental transactions:		
Federal securities interest revenue/expense-investment exchange	(12.5)	4.0
Borrowings interest revenue/expense-exchange	2.9	(36.4)
Borrowings gains/losses	(9.0)	903.7
Nonexpenditure transfers-in/out	2,218.1	(99.8)
Expenditure transfers-in/out	426.9	643.2
Nonexpenditure transfers-in/out capital transfers	-	5.9
Transfers-in/out without reimbursement	208.3	157.0
Imputed financing source/cost	(0.1)	(55.7)
Benefit program revenue/cost	(906.2)	(938.6)
Nonreciprocating**	(19,150.9)	58,767.6
Other non-budgetary financing sources for debt accruals/amortization**	-	-
Appropriations expended**	(361.3)	-
Appropriations used	300.3	(28,928.3)
Appropriations received/warrants issued	3,296.0	5,835.6
Appropriations of unavailable special or trust fund receipts transferred out/in	(3.0)	(0.2)
Custodial and non-entity collections transferred out/in	(11,445.5)	(2,886.5)
Other taxes and receipts/trust fund warrants	(2,787.6)	(2,984.6)
Accrual amounts collected/transferred in	5.0	(6,382.3)
Other	(113.7)	(772.5)
	(28,332.3)	23,232.1
Unmatched transactions and balances, net	(11,667.9)	(5,107.2)

( ) Parentheses indicate a decrease to Net Position.

* The fiscal year 2015 amounts for interest payable/receivable-loans and not otherwise classified are included under "Interest payable/receivable."

** The fiscal year 2015 amounts for other non-budgetary financing sources for debt accruals/amortization and appropriations expended are included under "Nonreciprocating."

The Statement of Operations and Changes in Net Position includes an amount for unmatched transactions and balances that result from the consolidation of federal reporting entities. Transactions between federal entities must be eliminated in consolidation to calculate the financial position of the government. Many of the amounts included in the table represent intragovernmental activity and balances that differed between federal agency trading partners and often totaled significantly more in the absolute than the net amounts shown. The table also reflects other consolidating adjustments and other adjustments that contributed to the unmatched transactions and balances amount.

Unmatched transactions and balances between federal entities impact not only in the period in which differences originate but also in the periods where differences are reconciled. As a result, it would not be proper to conclude that increases or decreases in the unmatched amounts shown in the "Unmatched Transactions and Balances" table reflect improvements or deteriorations in the Government's ability to reconcile intragovernmental transactions. The federal community considers the identification and accurate reporting of intragovernmental activity a priority.

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United States Government Required Supplementary Stewardship Information (Unaudited) for the Years Ended September 30, 2016, and 2015

Stewardship Investments

Stewardship investments focus on government programs aimed at providing long-term benefits by improving the Nation's productivity and enhancing economic growth. These investments can be provided through direct federal spending or grants to state and local governments for certain education and training programs, research and development, and federally financed but not federally owned property, such as bridges and roads. When incurred, these investments are included as expenses in determining the net cost of operations. Stewardship investments for the current year and for the immediately preceding four years are shown in the table below.

Stewardship Investments for the Years Ended September 30, 2012, through 2016

(In billions of dollars)	Fiscal Year 2016	Fiscal Year 2015	Fiscal Year 2014	Fiscal Year 2013	Fiscal Year 2012
Investments in non-federal physical property	65.1	64.8	65.6	66.1	68.1
Investments in human capital	131.1	97.8	108.5	58.7	87.1
Research and development:					
Investments in basic research	35.5	29.4	34.0	35.2	34.2
Investments in applied research	32.5	28.8	28.1	28.0	29.1
Investments in development	64.9	63.3	61.8	64.1	67.0
Total investments	329.1	284.1	298.0	252.1	285.5

Non-Federal Physical Property

The Government makes grants and provides funds for the purchase, construction, and/or major renovation of state and local government physical properties. Costs for non-federal physical property programs are included as expenses in the Statements of Net Cost and are reported as investments in the table. They are measured on the same accrual basis of accounting used in the *Financial Report* statements. DOT, HUD, and EPA had $55.8 billion (86 percent), $3.7 billion (6 percent), and $3.3 billion (5 percent), respectively, of the total non-federal physical property investments in fiscal year 2016 as shown in the table. Within DOT, the Federal Highway Administration invested $40.9 billion during fiscal year 2016, primarily via reimbursement from the Highway Trust Fund, for States' construction costs on projects related to the federal highway system. The main programs in which the States participate are the National Highway System, Interstate Systems, Surface Transportation, and Congestion Mitigation/Air Quality Improvement programs. The States' contribution is 10 percent for the Interstate System and 20 percent for most other programs.

Human Capital

The Government runs several programs that invest in human capital. Those investments go toward increasing and maintaining a healthy economy by educating and training the general public. Costs do not include training expenses for federal workers.

Education, VA, and DOL had $102.4 billion (78 percent), $15.6 billion (12 percent), and $6.2 billion (5 percent), respectively, of the total human capital investments in fiscal year 2016 shown in the table. Increases and decreases in Education's annual human capital investments are primarily attributable to fluctuations in the loan program subsidy estimate and loan modification costs. VA's annual human capital investments increased in fiscal years 2012 through 2014 due to implementation of the Post 9/11 GI Bill and subsequently decreased in fiscal year 2015 due to fewer participants in vocational rehabilitation and education assistance programs.

Education administers a wide variety of programs related to general public education and training programs that are intended to increase or maintain national economic productive capacity. The Office of Federal Student Aid administers need-based financial assistance programs for students pursuing postsecondary education and makes available federal grants, direct loans, and work-study funding to eligible undergraduate and graduate students.

The significant human capital programs administered by DOL relate to grants for job training and employment programs. The significant human capital programs administered by VA include veterans rehabilitation and employment programs which are provided to service disabled veterans; they are designated to improve employability and promote independence for the disabled. They also include education and training programs intended to provide higher education to dependents that might not be able to participate otherwise.

Research and Development

Federal investments in research and development (R&D) comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other future benefits.

- Investments in basic research are for systematic studies to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind.
- Investments in applied research are for systematic studies to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met.
- Investments in development are the systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems, or methods, including the design and development of prototypes and processes.

With regard to basic and applied research, HHS had $17.2 billion (48 percent) and $11.9 billion (37 percent), of the total basic and applied research investments, respectively, in fiscal year 2016 as shown in the table. HHS also had similar R&D investment amounts (and percentage contributions) in each of the preceding four years.

Within HHS, the National Institutes of Health (NIH) conducts almost all (97 percent) of the Department's basic and applied research. The NIH research program includes all aspects of the medical research continuum, including basic and disease-oriented research, observational and population-based research, behavioral research, and clinical research, including

research to understand both health and disease states, to move laboratory findings into medical applications, to assess new treatments or compare different treatment approaches; and health services research.

The NIH regards the expeditious transfer of the results of its medical research for further development and commercialization of products of immediate benefit to improved health as an important mandate.

With regard to development, the DOD and NASA had $54.8 billion (84 percent) and $6.8 billion (10 percent), respectively, of total development investments in fiscal year 2016, shown in the table. Major outputs of DOD development are scientific studies, investigations, research papers, hardware components, software codes, or limited construction of a weapon system component, to include non-system-specific development efforts. Development takes what has been discovered or learned from basic research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of five stages: 1) advanced technology development, 2) advanced component development and prototypes, 3) system development and demonstration, 4) research, development, test and evaluation management support, and 5) operational systems development.

NASA development includes activities to extend the knowledge of Earth, its space environment, and the universe, and to invest in new aeronautics and advanced space transportation technologies that support the development and application of technologies critical to the economic, scientific, and technical competitiveness of the United States.

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Appendix A: Reporting Entity

This appendix lists the organizations and agencies (entities) included in the U.S. Government's consolidated reporting entity for the *Financial Report*, as well as some entities not included in the reporting entity. Federal Accounting Standards Advisory Board's (FASAB) Statement of Federal Financial Accounting Concept (SFFAC) No. 2, *Entity and Display*, provides criteria for determining which entities are included in the reporting entity.

Under the first, conclusive criterion, any entity appearing in the "Federal Programs by Agency and Account" section of the federal budget is included in the consolidated reporting entity. Also, based on a consideration of the indicative criteria in the aggregate, certain entities not meeting the conclusive criteria are also included in the consolidated reporting entity, as the general purpose financial statements might be misleading or incomplete if the organization were not included therein. Indicative criteria are that an entity (1) exercises government sovereign power to carry out federal functions, (2) is owned by the federal government, particularly if the ownership is of the organization and not just the property, (3) is subject to the direct or continuing administrative control of the reporting entity, (4) carries out federal missions and objectives, (5) determines the outcome or disposition of matters affecting recipients of services that the federal government provides, and (6) has a fiduciary relationship with a reporting entity.

1. Entities included in the Reporting Entity for the Financial Report:

There are a total of 154 entities that met either the conclusive or indicative criteria, and as such are included in the *Financial Report*. The lists below describe three groups of entity types that comprise the reporting entity for the *Financial Report* and include entities from all three branches of government.

Twenty-Four Chief Financial Officer Act Agencies

Department of Agriculture
www.usda.gov
Department of Commerce
www.doc.gov
Department of Defense
www.defense.gov
Department of Education
www.ed.gov
Department of Energy
www.energy.gov
Department of Health and Human Services
www.hhs.gov
Department of Homeland Security
www.dhs.gov
Department of Housing and Urban Development
www.hud.gov
Department of the Interior
www.doi.gov
Department of Justice
www.usdoj.gov
Department of Labor
www.dol.gov
Department of State
www.state.gov
Department of Transportation
www.dot.gov
Department of the Treasury
www.treasury.gov
Department of Veterans Affairs
www.va.gov
Environmental Protection Agency
www.epa.gov
General Services Administration
www.gsa.gov
National Aeronautics and Space Administration
www.nasa.gov
National Science Foundation
www.nsf.gov
Office of Personnel Management
www.opm.gov
Small Business Administration
www.sba.gov
Social Security Administration
www.ssa.gov
U.S. Agency for International Development
www.usaid.gov
U.S. Nuclear Regulatory Commission
www.nrc.gov

Fifteen Additional Significant Entities

Defense Security Cooperation Agency
www.dsca.mil
Export-Import Bank of the United States
www.exim.gov
Farm Credit System Insurance Corporation
www.fcsic.gov
Federal Communications Commission
www.fcc.gov
Federal Deposit Insurance Corporation
www.fdic.gov
General Fund of the U.S. Government
www.fiscal.treasury.gov
Millennium Challenge Corporation
www.mcc.gov
National Credit Union Administration
www.ncua.gov
Overseas Private Investment Corporation
www.opic.gov
Pension Benefit Guaranty Corporation
www.pbgc.gov
Railroad Retirement Board
www.rrb.gov
Securities and Exchange Commission
www.sec.gov
Smithsonian Institution
www.si.edu
Tennessee Valley Authority
www.tva.gov
U.S. Postal Service
www.usps.com

One Hundred Fifteen Additional Entities/Funds

Administrative Conference of the United States
Advisory Council on Historic Preservation
African Development Foundation
American Battle Monuments Commission
Appalachian Regional Commission
Architect of the Capitol
Architectural and Transportation Barriers Compliance Board
Armed Forces Retirement Home
Barry Goldwater Scholarship and Excellence in Education Foundation
Broadcasting Board of Governors
Bureau of Consumer Financial Protection
Central Intelligence Agency
Chemical Safety Hazard Investigation Board
Christopher Columbus Fellowship Foundation
Commission for the Preservation of America's Heritage Abroad
Commission of Civil Rights
Commission of Fine Arts
Commission on International Religious Freedom
Commission on Security and Cooperation in Europe
Commission to Eliminate Child Abuse and Neglect Fatalities*
Committee for Purchase from People Who Are Blind or Severely Disabled
Commodity Futures Trading Commission
Congressional Budget Office
Congressional-Executive Commission on the People's Republic of China
Consumer Product Safety Commission
Corporation for National and Community Service
Council of the Inspector General on Integrity and Efficiency
Court of Appeals for Veterans Claims
Court Services and Offender Supervision Agency for DC
DC Courts
DC Courts–Defender Services
Defense Nuclear Facilities Safety Board
Delta Regional Authority
Denali Commission
Dwight D. Eisenhower Memorial Commission
Election Assistance Commission
Environmental Dispute Resolution Fund
Equal Employment Opportunity Commission
Executive Office of the President
Farm Credit Administration
Federal Election Commission
Federal Financial Institutions Examination Council Appraisal Subcommittee
Federal Housing Finance Agency
Federal Labor Relations Authority
Federal Maritime Commission
Federal Mediation and Conciliation Service
Federal Mine Safety and Health Review Commission
Federal Retirement Thrift Investment Board
Federal Trade Commission
Financial Crisis Inquiry Commission*
Government Accountability Office
Government Publishing Office
Gulf Coast Ecosystem Restoration Council
Harry S. Truman Scholarship Trust Fund

Indian Law and Order Commission*
Institute of Museum and Library Services
Intelligence Community Management Account
Interagency Council on the Homeless
Inter-American Foundation
International Trade Commission
James Madison Memorial Fellowship Foundation
Japan-United States Friendship Commission
John C. Stennis Center
John F. Kennedy Center for the Performing Arts
Library of Congress
Marine Mammal Commission
Medicaid and Children's Health Insurance Program Payment and Access Commission
Medicare Payment Advisory Commission
Merit Systems Protection Board
Military Compensation and Retirement Modernization Commission*
Morris K. Udall Scholarship Foundation
National Archives and Records Administration
National Capital Planning Commission
National Council on Disability
National Endowment for the Arts
National Endowment for the Humanities
National Gallery of Art
National Labor Relations Board
National Mediation Board
National Railroad Passenger Corporation, Office of the Inspector General
National Railroad Retirement Investment Trust
National Transportation Safety Board
Neighborhood Reinvestment Corporation
Northern Border Regional Commission
Nuclear Waste Technical Review Board
Occupational Safety and Health Review Commission
Office of Compliance
Office of Government Ethics
Office of Navajo and Hopi Indian Relocation
Office of Nuclear Waste Negotiator*
Office of Special Counsel
Office of the Federal Coordination for Alaska Natural Gas Transportation Projects*
Open World Leadership Center
Patient Centered Outcomes Research Trust Fund
Peace Corps
Presidio Trust
Privacy and Civil Liberties Oversight Board
Public Defender Service
Recovery Act Accountability and Transparency Board*
Ronald Reagan Centennial Commission*
Selective Service System
Senate Preservation Fund
St. Lawrence Seaway Development Corporation
State Justice Institute
Surface Transportation Board
U.S. Capitol Police
U.S. Capitol Preservation Commission
U.S. China Security Review Commission
U.S. Holocaust Memorial Museum
U.S. Institute of Peace
U.S. Tax Court
U.S. Trade and Development Agency
Vietnam Education Foundation
Woodrow Wilson International Center for Scholars
WWI Centennial Commission

*These entities are no longer active and have either returned all remaining fund balances to Treasury during fiscal year 2016 or have remaining fund balances pending final return to Treasury as of September 30, 2016.

Legislative and Judicial Branches

There are no legal or other requirements for the legislative or judicial branches to prepare consolidated audited financial statements or to provide accrual-based accounting data for inclusion in the governmentwide financial statements. However, a portion of legislative and judicial branch entities voluntarily prepare accrual-based financial statements (e.g., Government Accountability Office, Government Printing Office, and Library of Congress) and are included in the 154 entities listed above. The other entities of the legislative and judicial branch voluntarily provide accrual-based accounting data for inclusion in the governmentwide financial statements, except for the U.S. Senate which is included on a cash basis.

2. Entities not Included in the Reporting Entity of the Financial Report

The entities discussed below either do not meet the conclusive criteria or indicative criteria or were specifically excluded from the consolidated reporting entity in accordance with SFFAC No. 2. Information about the federal government's relationship with and investments in or liabilities to certain of these entities are disclosed in the notes to the financial statements.

Entities that Did not Meet the Conclusive or Indicative Criteria

The following entities are examples of entities with which the federal government has business relationships but did not meet the above mentioned conclusive or indicative criteria:

Federal Home Loan Banks
National Railroad Passenger Corporation (does business as Amtrak)
Resolution Funding Corporation
Student Loan Marketing Association
The Financing Corporation
Thrift Savings Plan

Entities Specifically Excluded From the Consolidated Reporting Entity

SFFAC 2 specifically excludes the Federal Reserve System—the Board of Governors of the Federal Reserve System and the Federal Reserve Banks. The Federal Reserve System could be considered as functioning consistent with the indicative criteria presented above since it establishes and monitors monetary policy. However, in the United States, the organization and functions pertaining to monetary policy are traditionally separated from and independent of the other central government organizations and functions in order to achieve more effective monetary and fiscal policies and economic results. Therefore, the Federal Reserve System is not considered part of the governmentwide reporting entity.

SFFAC 2 also excludes bailout entities. The Federal government may guarantee or pay debt for a privately owned entity whose failure could have an adverse impact on the nation's economy, commerce, national security, etc. As a condition of the bailout, the Federal government may obtain rights similar to the authorities associated with the indicative criteria presented above. However, the existence of these rights does not make the bailed out entity part of the governmentwide reporting entity.

Examples of bailout entities are:

Federal Home Loan Mortgage Corporation (Freddie Mac)
Federal National Mortgage Association (Fannie Mae)

Appendix B: Acronyms

This appendix lists the acronyms used in the Financial Statements and Notes to the Financial Statements section of this *Financial Report*.

ACA	Affordable Care Act
ACH	Automated Clearing House
AFR	Agency Financial Reports
AIG	American International Group, Inc.
AMT	Alternative Minimum Tax
ARRA	American Recovery and Reinvestment Act of 2009
ASC	Accounting Standards Codification
ATDA	Accountability of Tax Dollars Act of 2002
ATRA	American Taxpayer Relief Act of 2012
BBEDCA	Balanced Budget and Emergency Deficit Control Act
Bbl	Barrel
BCA	Budget Control Act
BLDTF	Black Lung Disability Trust Fund
BLM	Bureau of Land Management
Board	Federal Reserve Board of Governors
CCC	Commodity Credit Corporation
CDCI	Community Development Capital Initiative
CDFI	Community Development Financial Institutions
CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act
CFO	Chief Financial Officers
CFO Act	Chief Financial Officers Act of 1990
CFPB	Bureau of Consumer Financial Protection
CMS	Centers for Medicare and Medicaid Services
COLA	Cost of Living Adjustments
CPI	Consumer Price Index
CPI-U	Consumer Price Index for All Urban Consumers
CPIM	Consumer Price Index–Medical
CPI-W	Consumer Price Index for Urban Wage Earners and Clerical Workers
CPP	Capital Purchase Program
CSRDF	Civil Service Retirement and Disability Fund
CSRS	Civil Service Retirement System
DACA	Deferred Action for Childhood Arrivals
DFAS	Defense Finance and Accounting Service
DHS	Department of Homeland Security
DI	Disability Insurance
DIF	Deposit Insurance Fund
DIP	Debtor in Possession

DOC	Department of Commerce
DOD	Department of Defense
DOE	Department of Energy
DOI	Department of the Interior
DOJ	Department of Justice
DOL	Department of Labor
DOT	Department of Transportation
DM&R	Deferred Maintenance and Repairs
Education	Department of Education
EESA	Emergency Economic Stabilization Act of 2008
EPA	Environmental Protection Agency
EOP	Executive Office of the President
ESF	Exchange Stabilization Fund
FAA	Federal Aviation Administration
Fannie Mae	Federal National Mortgage Association
FASAB	Federal Accounting Standards Advisory Board
FASB	Financial Accounting Standards Board
FCC	Federal Communications Commission
FCRA	Federal Credit Reform Act of 1991
FCSIC	Farm Credit System Insurance Corporation
FDIC	Federal Deposit Insurance Corporation
FECA	Federal Employees' Compensation Act
FEGLI	Federal Employees' Group Life Insurance
FEHB	Federal Employees Health Benefits Program
FERS	Federal Employees Retirement System
FERSA	Federal Employees' Retirement System Act of 1986
FFAS	Farm and Foreign Agricultural Services
FFEL	Federal Family Education Loan
FFMIA	Federal Financial Management Improvement Act of 1996
FHA	Federal Housing Administration
FHFA	Federal Housing Financing Agency
FHWA	Federal Highway Administration
FICA	Federal Insurance Contribution Act
FMFIA	Federal Managers' Financial Integrity Act
FOMC	Federal Open Market Committee
FR	Financial Report
FR System	Federal Reserve System
FRBNY	Federal Reserve Bank of New York
FRBs	Federal Reserve Banks
Freddie Mac	Federal Home Loan Mortgage Corporation
FRTIB	Federal Retirement Thrift Investment Board
FSA	Farm Service Agency

FUA	Federal Unemployment Account
FUTA	Federal Unemployment Tax Act
GAAP	U.S. Generally Accepted Accounting Principles
GAO	U.S. Government Accountability Office
GDP	Gross Domestic Product
General Fund	General Fund of the U.S. Government
Ginnie Mae	Government National Mortgage Association
GMRA	Government Management Reform Act of 1994
G-PP&E	General Property, Plant, and Equipment
GSA	General Services Administration
GSE	Government-Sponsored Enterprises
HBP	Health Benefits Program
HEA	Higher Education Act of 1965
HERA	Housing and Economic Recovery Act of 2008
HFA	Housing Financing Agencies
HHS	Department of Health and Human Services
HI	Hospital Insurance
HMO	Health Maintenance Organization
HUD	Department of Housing and Urban Development
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
IRS	Internal Revenue Service
LAC	Latest Acquisition Cost
LOC	Library of Congress
MAC	Moving Average Cost
MBS	Mortgage-Backed Securities
MCC	Millennium Challenge Corporation
Mcf	The volume of 1,000 cubic feet of natural gas
MDBs	Multilateral Development Banks
MERHCF	Medicare Eligible Retiree Health Care Fund
MMA	Medicare Prescription Drug, Improvement, and Modernization Act
MRF	Military Retirement Fund
NAB	New Arrangement to Borrow
NASA	National Aeronautics and Space Administration
NCUA	National Credit Union Administration
NIH	National Institutes of Health
NRC	U.S. Nuclear Regulatory Commission
NRRIT	National Railroad Retirement Investment Trust
NSF	National Science Foundation
NSLI	National Service Life Insurance
NTIA	National Telecommunications and Information Administration
NYSE	New York Stock Exchange

OASDI	Old-Age, Survivors, and Disability Insurance
OASI	Old-Age and Survivors Insurance
OCO	Overseas Contingency Operations
OECD	Organization for Economic Co-operation and Development
OFS	Office of Financial Stability
OMB	Office of Management and Budget
ONRR	Office of Natural Resources Revenue
OPEB	Other Postemployment Benefits
OPIC	Overseas Private Investment Corporation
OPM	Office of Personnel Management
ORB	Other Retirement Benefits
PAR	Performance and Accountability Reports
PBGC	Pension Benefit Guaranty Corporation
PCF	Periodic Commitment Fee
PEFCO	Private Export Funding Corporation
PMAs	Power Marketing Authorities
PP&E	Property, Plant, and Equipment
PPACA	Patient Protection and Affordable Care Act
PPIF	Public Private Investment Funds
PPIP	Public Private Investment Program
PPO	Preferred Provider Organization
PSRHB	Postal Service Retiree Health Benefits
QFI	Qualified Financial Institution
R&D	Research and Development
RCRA	Resource Conservation and Recovery Act
RD	Rural Development
REDUX	Military Retirement Reform Act of 1986
RRB	Railroad Retirement Board
RRSIA	Railroad Retirement and Survivors Improvement Act
RSI	Required Supplementary Information
RSSI	Required Supplementary Stewardship Information
SAFETEA-LU	Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users
SBA	Small Business Administration
SCSIA	Statement of Changes in Social Insurance Amounts
SDRs	Special Drawing Rights
SDRCs	SDR Certificates
SEC	Securities and Exchange Commission
SECA	Self-Employment Contributions Act
SFFAC	Statement of Federal Financial Accounting Concept
SFFAS	Statement of Federal Financial Accounting Standards
SFP	Supplementary Financing Program
SGR	Sustainable Growth Rate

SI	Smithsonian Institution
SLMA	Student Loan Marketing Association
SMI	Supplementary Medical Insurance
SOCNP	Statements of Operations and Changes in Net Position
SOMA	System Open Market Account
SOSI	Statement of Social Insurance
SPSPA	Senior Preferred Stock Purchase Agreements
SSA	Social Security Administration
SSEB	Social Security Equivalent Benefit
TFL	TRICARE for Life
TIP	Targeted Investment Program
TIPS	Treasury Inflation-Protected Securities
TPTCCA	Temporary Payroll Tax Cut Continuation Act of 2011
Treasury	Department of the Treasury
TRIA	Terrorism Risk Insurance Act
TSP	Thrift Savings Plan
TVA	Tennessee Valley Authority
TVARS	Tennessee Valley Authority Retirement System
U.S.C.	United States Code
USAID	U.S. Agency for International Development
USDA	United States Department of Agriculture
U.S. GAAP	U.S. Generally Accepted Accounting Principles
USPS	United States Postal Service
UTF	Unemployment Trust Fund
VA	Department of Veterans Affairs
VRI	Veterans Reopened Insurance
VSLI	Veterans Special Life Insurance

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U.S. GOVERNMENT ACCOUNTABILITY OFFICE

441 G St. N.W.
Washington, DC 20548

Independent Auditor's Report

The President
The President of the Senate
The Speaker of the House of Representatives

In our audits of the U.S. government's consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, we found the following:

- Certain material weaknesses[1] in internal control over financial reporting and other limitations on the scope of our work resulted in conditions that continued to prevent us from expressing an opinion on the accompanying accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[2]

- Significant uncertainties (discussed in Note 22 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth, prevented us from expressing an opinion on the sustainability financial statements,[3] which consist of the 2016 and 2015 Statements of Long-Term Fiscal Projections; the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance; and the 2016 and 2015 Statements of Changes in Social Insurance Amounts.[4] A material weakness in internal control also prevented us from expressing an opinion on the 2016 and 2015 Statements of Long-Term Fiscal Projections.

[1]A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

[2]The accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Unified Budget Deficit, (4) Statements of Changes in Cash Balance from Unified Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis. We previously reported that certain material weaknesses and, for some years, other limitations on the scope of our work prevented us from expressing an opinion on the accrual-based consolidated financial statements of the U.S. government for fiscal years 1997 through 2015.

[3]The Statements of Long-Term Fiscal Projections for fiscal years 2016 and 2015 present, for all the activities of the federal government, the present value of projected receipts and noninterest spending under current policy without change, the relationship of these amounts to projected gross domestic product (GDP), and changes in the present value of projected receipts and noninterest spending from the prior year.

[4]Statements of Social Insurance are presented for the current year and each of the 4 preceding years in accordance with U.S. generally accepted accounting principles. Also, the sustainability financial statements do not interrelate with the accrual-based consolidated financial statements. In addition, with respect to the Statement of Social Insurance, the valuation date is January 1 for the Social Security and Medicare programs, October 1 for the Railroad Retirement program, and September 30 for the Black Lung program. The valuation date for the Statement of Long-Term Fiscal Projections is September 30.

- Material weaknesses resulted in ineffective internal control over financial reporting for fiscal year 2016.

- Material weaknesses and other scope limitations discussed in this audit report limited our tests of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements for fiscal year 2016.

The following sections of this audit report discuss in more detail (1) our report on the accompanying consolidated financial statements, which includes (a) two emphasis of matters—equity investments, related to the federal government's actions to stabilize financial markets and to promote economic recovery, and long-term fiscal challenges, (b) required supplementary information (RSI),[5] required supplementary stewardship information (RSSI),[6] and other information[7] included with the consolidated financial statements in the *Fiscal Year 2016 Financial Report of the United States Government* (*2016 Financial Report*), and (c) information on Chief Financial Officers Act of 1990 (CFO Act) agency financial management systems; (2) our report on internal control over financial reporting; (3) our report on compliance with laws, regulations, contracts, and grant agreements; and (4) the Department of the Treasury's (Treasury) and the Office of Management and Budget's (OMB) comments on a draft of this audit report. Appendix I discusses our audit objectives, scope, and methodology.

Report on the Consolidated Financial Statements

The Secretary of the Treasury, in coordination with the Director of OMB, is required to annually submit audited financial statements for the U.S. government to the President and Congress. GAO is required to audit these statements.[8] As noted above, the consolidated financial statements consist of the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, and the sustainability financial statements, consisting of the 2016 and 2015 Statements of Long-Term Fiscal Projections; the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance; the 2016 and 2015 Statements of Changes in Social Insurance Amounts; and the related notes to the financial statements.

We performed sufficient audit work to provide this report on the consolidated financial statements. We considered the limitations on the scope of our work regarding the accrual-based consolidated financial statements and the sustainability financial statements in forming our conclusions. Our work was performed in accordance with U.S. generally accepted government auditing standards.

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[5]RSI consists of Management's Discussion and Analysis and information in the Required Supplementary Information section of the *Fiscal Year 2016 Financial Report of the United States Government*.

[6]RSSI consists of information on stewardship investments in the Required Supplementary Stewardship Information section of the *Fiscal Year 2016 Financial Report of the United States Government*.

[7]Other information consists of information in the *Fiscal Year 2016 Financial Report of the United States Government* other than the consolidated financial statements, RSI, RSSI, the auditor's report, and the Statement of the Comptroller General of the United States.

[8]The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. § 331(e). Treasury and OMB have elected to include certain financial information on the legislative and judicial branches in the consolidated financial statements as well.

Management's Responsibility

Management of the federal government is responsible for (1) the preparation and fair presentation of annual consolidated financial statements of the U.S. government in accordance with U.S. generally accepted accounting principles; (2) preparing, measuring, and presenting RSI and RSSI in accordance with U.S. generally accepted accounting principles; and (3) preparing and presenting other information included in documents containing the consolidated financial statements and auditor's report, and ensuring the consistency of that information with the consolidated financial statements, RSI, and RSSI. This includes maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these consolidated financial statements based on conducting the audit in accordance with U.S. generally accepted government auditing standards. We are also responsible for applying certain limited procedures to the RSI, RSSI, and other information included with the consolidated financial statements. Because of the matters discussed below, we were unable to obtain sufficient appropriate evidence to provide a basis for audit opinions on the consolidated financial statements.

Basis for Disclaimers of Opinion on the Consolidated Financial Statements

Accrual-Based Consolidated Financial Statements

The federal government is not able to demonstrate the reliability of significant portions of the accompanying accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, principally resulting from limitations related to certain material weaknesses in internal control over financial reporting and other limitations affecting the reliability of these financial statements and the scope of our work as discussed below.[9] As a result of these limitations, readers are cautioned that amounts reported in the accrual-based consolidated financial statements and related notes may not be reliable.

The federal government did not maintain adequate systems or have sufficient appropriate evidence to support certain material information reported in the accompanying accrual-based consolidated financial statements. The underlying material weaknesses in internal control, which have existed for years, contributed to our disclaimer of opinion on the accrual-based consolidated financial statements. Specifically, these weaknesses concerned the federal government's inability to

- satisfactorily determine that property, plant, and equipment and inventories and related property, primarily held by the Department of Defense (DOD), were properly reported in the accrual-based consolidated financial statements;

[9]In addition to the limitations discussed in this audit report, as of the date of this audit report, the audited financial statements for fiscal year 2016 were not issued for (1) the Department of Defense (DOD), (2) the Department of Housing and Urban Development (HUD), (3) the National Science Foundation (NSF), and (4) the Smithsonian Institution. Also, the Department of Agriculture obtained an unmodified opinion on its consolidated balance sheet as of September 30, 2016, but its consolidated statement of net cost, consolidated statement of changes in net position, combined statement of budgetary resources, and the related notes for the fiscal year ended September 30, 2016, were not audited.

- reasonably estimate or adequately support amounts reported for certain liabilities, such as environmental and disposal liabilities, or determine whether commitments and contingencies were complete and properly reported;

- support significant portions of the reported total net cost of operations, most notably related to DOD, and adequately reconcile disbursement activity at certain federal entities;

- adequately account for and reconcile intragovernmental activity and balances between federal entities;

- reasonably assure that the consolidated financial statements are (1) consistent with the underlying audited entities' financial statements, (2) properly balanced, and (3) in accordance with U.S. generally accepted accounting principles; and

- reasonably assure that the information in the (1) Reconciliations of Net Operating Cost and Unified Budget Deficit and (2) Statements of Changes in Cash Balance from Unified Budget and Other Activities is complete and consistent with the underlying information in the audited entities' financial statements and other financial data.

These material weaknesses continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost, as well as the financial and nonfinancial performance, of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder the federal government from having reliable financial information to operate in an efficient and effective manner. Due to these material weaknesses and to other limitations on the scope of our work discussed below, additional issues may exist that were not identified and could affect the accrual-based consolidated financial statements. Appendix II describes these material weaknesses in more detail and highlights the primary effects of these material weaknesses on the accompanying accrual-based consolidated financial statements and on the management of federal government operations.

Sustainability Financial Statements

Significant uncertainties (discussed in Note 22 to the consolidated financial statements), which primarily relate to the achievement of projected reductions in Medicare cost growth, affect the sustainability financial statements. In addition, the material weakness related to the Reconciliations of Net Operating Cost and Unified Budget Deficit and the Statements of Changes in Cash Balance from Unified Budget and Other Activities, discussed above, hampers the federal government's ability to demonstrate the reliability of historical budget information used for certain key inputs to the 2016 and 2015 Statements of Long-Term Fiscal Projections. As a result of these significant uncertainties and this material weakness, readers are cautioned that amounts reported in the 2016 and 2015 Statements of Long-Term Fiscal Projections; the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance; the 2016 and 2015 Statements of Changes in Social Insurance Amounts; and the related notes to such financial statements may not fairly present, in all material respects, the sustainability information for those years in accordance with U.S. generally accepted accounting principles.

For 2016 and 2015, these significant uncertainties primarily relate to the following.

- Medicare projections in the 2016 and 2015 Statements of Long-Term Fiscal Projections and the 2016 and 2015 Statements of Social Insurance were based on benefit formulas under current law and included a significant reduction in Medicare payment rate updates for productivity improvements for most categories of Medicare providers,[10] based on full implementation of the provisions of the Patient Protection and Affordable Care Act, as amended (ACA),[11] and physician payment updates specified by the Medicare Access and CHIP Reauthorization Act of 2015 (MACRA).[12]

- Management has noted that actual future costs for Medicare are likely to exceed those shown by the current law projections presented in the 2016 and 2015 Statements of Social Insurance due, for example, to the likelihood of modifications to the scheduled reductions in Medicare payment rate updates for productivity adjustments relating to most categories of Medicare providers and to the specified physician payment updates. The extent to which actual future costs exceed the current law amounts due to changes to the scheduled reductions in Medicare payment rate updates for productivity adjustments and to specified physician payment updates depends on both the specific changes that might be legislated and whether such legislation would include further provisions to help offset such costs. Consequently, there are significant uncertainties concerning the achievement of these projected reductions in Medicare payment rate updates.

- Management has developed an illustrative alternative projection intended to provide additional context regarding the long-term sustainability of the Medicare program and to illustrate the uncertainties in the Statement of Social Insurance projections. The present value of future estimated expenditures in excess of future estimated revenue for Medicare, included in the illustrative alternative projection in Note 22, exceeds the $32.5 trillion estimate in the 2016 Statement of Social Insurance by $11.0 trillion.

- Management noted that these significant uncertainties about projected reductions in health care cost growth also affect the projected Medicare and Medicaid costs reported in the 2016 and 2015 Statements of Long-Term Fiscal Projections.

The 2014, 2013, and 2012 Statements of Social Insurance were affected by significant uncertainties, primarily related to the achievement of projected reductions in Medicare payment rate updates for productivity improvements. The 2013 and 2012 Statements of Social Insurance were also affected by uncertainties related to projected reductions in Medicare payment rates for physician services. Specifically, the Medicare projections in the 2013 and 2012 Statements of Social Insurance were based on benefit formulas in current law and included significant reductions in Medicare payment rates for productivity improvements and physician services.

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[10]These categories include, but are not limited to, inpatient/outpatient hospital services, skilled nursing facilities, home health care, ambulance, ambulatory surgical centers, durable medical equipment, and prosthetics.

[11]ACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010). In this report, references to the ACA include any amendments made by the Health Care and Education Reconciliation Act of 2010.

[12]MACRA, Pub. L. No. 114-10, title I, § 101, 129 Stat. 87, 89 (Apr. 16, 2015). MACRA included many provisions that affect Medicare, including the repeal of the sustainable growth rate (SGR) formula for calculating annual updates to Medicare reimbursement payment rates to physicians and certain nonphysician medical providers and established an alternative set of annual updates.

The 2014 Statement of Social Insurance reflected a change from the assumption regarding scheduled reductions in Medicare payment rates for physician services that was used in the 2013 and 2012 Statements of Social Insurance. Specifically, the 2014 Statement of Social Insurance reflected a projected baseline that assumed that the physician payment rate reductions would not occur and that physician payment rates would annually increase at a rate equal to the average sustainable growth rate (SGR) override that occurred over the 10-year period ending on March 31, 2015. For 2014, 2013, and 2012, management noted that actual future costs for Medicare were likely to exceed those shown by the current-law projections presented in the 2014, 2013, and 2012 Statements of Social Insurance due, for example, to the likelihood of modifications to the scheduled reductions in Medicare payment rates for productivity adjustments.

Projections of Medicare costs are sensitive to assumptions about future decisions by policymakers and about the behavioral responses of consumers, employers, and health care providers as policy, incentives, and the health care sector change over time. Such secondary impacts are not fully reflected in the sustainability financial statements but could be expected to influence the excess cost growth rate used in the projections.[13] Key drivers of uncertainty about the excess cost growth rate include the future development and deployment of medical technology, the evolution of personal income, and the cost and availability of insurance, as well as federal policy changes, such as the implementation of the ACA. The Required Supplementary Information section of the *2016 Financial Report* includes unaudited information concerning how changes in various assumptions would change the present value of future estimated expenditures in excess of future estimated revenue. As discussed in that section, the projections are very sensitive to changes in the health care cost growth assumption.

As discussed in Notes 22 and 23 to the financial statements, the sustainability financial statements are based on management's assumptions. These sustainability financial statements present the present value of the U.S. government's estimated future receipts and future spending using a projection period sufficient to illustrate long-term sustainability.[14] The sustainability financial statements are intended to aid users in assessing whether future resources will likely be sufficient to sustain public services and to meet obligations as they come due. The Statements of Social Insurance and Changes in Social Insurance Amounts are based on income and benefit formulas in current law (except for the 2014 Medicare projections, which use the projected baseline) and assume that scheduled benefits will continue after any related trust funds are exhausted. The Statements of Long-Term Fiscal Projections are based on the continuation of current policy and also assume that scheduled benefits will continue after any related trust funds are exhausted. The sustainability financial statements are not forecasts or predictions.

In preparing the sustainability financial statements, management considers and selects assumptions and data that it believes provide a reasonable basis to illustrate whether current policy or law is sustainable. Assumptions underlying such sustainability information do not consider changes in policy or all potential future events that could affect future receipts, future spending, and sustainability, such as, for example, implementation of policy changes to avoid trust fund exhaustion or unsustainable debt levels.

[13]The excess cost growth rate is the increase in health care spending per person relative to the growth of GDP per person after removing the effects of demographic changes on health care spending.

[14]The projection period used for the Social Security, Medicare, and Railroad Retirement social insurance programs is 75 years. For the Black Lung program, the projections are through September 30, 2040.

As discussed in the unaudited Required Supplementary Information section of the *2016 Financial Report*, the Social Security and Medicare Hospital Insurance (Part A) trust funds are, based on achievement of the cost reductions discussed above, projected to be exhausted in 2034 and 2028, respectively, at which time they would be unable to pay the full amount of scheduled future benefits.[15] For Social Security, future revenues were projected to be sufficient to pay 79 percent of scheduled benefits in 2034, the year of projected trust funds (combined) exhaustion, and decreasing to 74 percent of scheduled benefits in 2090. For Medicare Hospital Insurance (Part A), future revenues were projected to be sufficient to pay 87 percent of scheduled benefits in 2028, the year of projected trust fund exhaustion, and then decreasing to 86 percent of scheduled benefits in 2090.

Because of the large number of factors that affect the sustainability financial statements and the fact that future events and circumstances cannot be estimated with certainty, even if current policy is continued, there will be differences between the estimates in the sustainability financial statements and the actual results, and those differences may be material.

Other Limitations on the Scope of Our Work

For fiscal years 2016 and 2015, there were other limitations on the scope of our work, in addition to the material weaknesses and significant uncertainties noted above, that contributed to our disclaimers of opinion on the consolidated financial statements. Such limitations primarily relate to our ability to obtain adequate representations from management. Treasury and OMB depend on representations from certain federal entities to provide their representations to us regarding the U.S. government's consolidated financial statements. Treasury and OMB were unable to provide us with adequate representations regarding the U.S. government's accrual-based consolidated financial statements for fiscal years 2016 and 2015, primarily because of insufficient or no representations provided to them by certain federal entities, including DOD.

Disclaimers of Opinion on the Consolidated Financial Statements

Accrual-Based Consolidated Financial Statements

Because of the significance of the related matters described in the Basis for Disclaimer of Opinion paragraphs above, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the accrual-based consolidated financial statements. Accordingly, we do not express an opinion on the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015.

Sustainability Financial Statements

Because of the significance of the related matters described in the Basis for Disclaimer of Opinion paragraphs above, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the Statements of Long-Term Fiscal Projections for 2016 and 2015; the Statements of Social Insurance for 2016, 2015, 2014, 2013, and 2012; and the Statements of Changes in Social Insurance Amounts for 2016 and 2015. Accordingly, we do not express an opinion on these sustainability financial statements.

[15]The combined Social Security trust funds consist of the Federal Old-Age and Survivors Insurance trust fund and the Federal Disability Insurance trust fund, whose assets are projected to be exhausted in 2035 and 2023, respectively.

Emphasis of Matters

The following key items deserve emphasis in order to put the information contained in the consolidated financial statements and the Management's Discussion and Analysis section of the *2016 Financial Report* into context. However, our disclaimers of opinion noted above are not modified with respect to these matters.

Equity Investments Related to the Federal Government's Actions to Stabilize Financial Markets and to Promote Economic Recovery

In 2008, during the financial crisis, the federal government placed the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) under conservatorship and entered into preferred stock purchase agreements with these government-sponsored enterprises (GSE) to ensure their financial stability. The agreements with the GSEs could affect the federal government's financial position. As of September 30, 2016, the federal government continued to report about $109 billion of investments in the GSEs, which is net of about $86 billion in valuation losses.

In valuing these equity investments, management considered and selected assumptions and data that it believed provided a reasonable basis for the estimated values reported in the accrual-based consolidated financial statements. However, as discussed in Note 1 to the consolidated financial statements, there are many factors affecting these assumptions and estimates that are inherently subject to substantial uncertainty arising from the uniqueness of the transactions and the likelihood of future changes in general economic, regulatory, and market conditions. As such, there will be differences between the estimated values as of September 30, 2016, and the actual results, and such differences may be material. Also, as discussed in Note 1 to the consolidated financial statements, the financial statements do not include the assets, liabilities, or results of operations of entities in which Treasury holds either a direct, indirect, or beneficial equity interest. Treasury and OMB have determined that none of the entities meet the criteria for a federal entity.[16]

Long-Term Fiscal Challenges

The comprehensive long-term fiscal projections presented in the Statement of Long-Term Fiscal Projections, and related information in Note 23 and in the unaudited Required Supplementary Information section of the *2016 Financial Report* show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path. In fiscal year 2016, the 75-year debt-to-GDP projections were higher than the fiscal year 2015 projections, but still lower than fiscal year 2014. The projections in the *2016 Financial Report* show a slight improvement in the near term with the unified budget deficit decreasing over the next 5 years before increasing in 2022. In fiscal year 2016, the unified budget deficit increased following 6 years of declining deficits.[17] Over the long term, the imbalance between spending and revenue that is built into current law and policy is projected to lead to continued growth of the deficit and debt

[16]For additional information on the criteria used to determine which federal entities are included in the reporting entity for the consolidated financial statements, as well as the reasons for not including certain entities, such as Fannie Mae and Freddie Mac, see appendix A of the *2016 Financial Report*.

[17]As we reported in last year's audit report for fiscal year 2015, the enactment of the Bipartisan Budget Act of 2015 and the Consolidated Appropriations Act, 2016, which both included spending provisions intended to achieve certain national priorities and goals, contributed to the higher deficit in fiscal year 2016.

held by the public as a share of gross domestic product (GDP). This situation—in which debt grows faster than GDP—means the current federal fiscal path is unsustainable.

Under these projections, spending for the major health and retirement programs will increase more rapidly than GDP in coming decades as more members of the baby boom generation become eligible for benefits. These projections, with regard to Social Security and Medicare, are based on the same assumptions underlying the information presented in the Statement of Social Insurance and assume that the provisions enacted in the ACA designed to slow the growth of Medicare costs are sustained and remain effective throughout the projection period.[18] They also reflect the effects of MACRA, which, among other things, revised the methodology for determining physician payment rates. If, however, the Medicare cost containment measures and physician payment rate methodology are not sustained over the long term—concerns expressed by the Trustees of the Medicare trust funds, the Centers for Medicare & Medicaid Services' (CMS) Chief Actuary, the Congressional Budget Office, and others—spending on federal health care programs will grow more rapidly than assumed in the projections.

GAO also prepares long-term federal fiscal simulations, using different sets of assumptions, which continue to show debt held by the public rising as a share of GDP.[19] Under GAO's Alternative simulation,[20] using the CMS Office of the Actuary's alternative health care cost projections, future spending in excess of receipts would be greater and debt held by the public as a share of GDP would grow more quickly than the projections in the *2016 Financial Report*. Under the Alternative simulation, debt held by the public as a share of GDP will surpass its historical high (106 percent in 1946) by 2032.

Both the projections in the *2016 Financial Report* and our long-term simulations follow the spending limits enacted in the Balanced Budget and Emergency Deficit Control Act of 1985 (BBEDCA), as amended.[21] Under these limits, discretionary spending will continue to decline as a share of the economy and within the next 5 years will be lower as a share of GDP than any

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[18]ACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010).

[19]GAO, *Fiscal Outlook: Federal Fiscal Outlook*, accessed January 4, 2017, http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview.

[20]Our 2017 Alternative simulation, the most recent one available as of the date of our audit report, incorporates the CMS Office of the Actuary's 2016 alternative projections for health care cost growth, which assume certain cost controls are not maintained over the long term. Our Alternative simulation also assumes that tax provisions that are scheduled to expire, such as the credit for construction of energy-efficient new homes, are extended. In the Alternative simulation, discretionary spending follows the limits established in the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, but not the lower limits triggered by the automatic enforcement procedures.

[21]The Budget Control Act of 2011 (BCA) amended BBEDCA, imposing discretionary spending limits for fiscal years 2012 through 2021 to reduce projected spending by about $1 trillion. Pub. L. No. 112-25, 125 Stat. 240 (Aug. 2, 2011). BCA also established the Joint Select Committee on Deficit Reduction (Joint Committee), which was tasked with proposing legislation to reduce the deficit by at least an additional $1.2 trillion through fiscal year 2021. The Joint Committee did not report a proposal, and Congress and the President did not enact legislation. This triggered the sequestration process in section 251A of BBEDCA. Section 251A, as amended by BCA, required (1) a sequestration for fiscal year 2013 and (2) annual downward adjustments to discretionary spending limits and sequestration of direct spending from fiscal years 2014 through 2021. BBEDCA has been amended several times since August 2011, most recently by the Bipartisan Budget Act (BBA) of 2015, which increased discretionary spending limits for fiscal years 2016 and 2017. The BBA of 2015 also extended the sequestration of direct spending through fiscal year 2025 and made other changes to direct spending and revenue. Pub. L. No. 114-74, §§ 101, 102, 129 Stat. 584, 585-87 (Nov. 2, 2015).

level seen in the last 50 years. At the same time, the projections in the *2016 Financial Report* show revenues rising in the near term. Our long-term simulations also show revenues overall rising in the near term.

Debt held by the public as a share of GDP, however, remains well above the post-World War II historical average of 44 percent since 1946. At the end of fiscal year 2016, debt held by the public reached about 77 percent of GDP—the highest it has been as a share of GDP since 1950. Debt held by the public at these high levels could limit the federal government's flexibility to address emerging issues and unforeseen challenges, such as another economic downturn or large-scale disaster. Further, our past work has also identified a variety of fiscal exposures—responsibilities, programs, and activities that explicitly or implicitly expose the federal government to future spending.[22] Fiscal exposures vary widely as to source, extent of the government's legal commitment, and magnitude. Over the past decade, some fiscal exposures have grown because of events and trends and the government's response to them. Increased attention to these fiscal exposures will be important for understanding risks to the federal fiscal outlook and enhancing oversight of federal resources.

Other Matters

Required Supplementary Information and Required Supplementary Stewardship Information

U.S. generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) require that RSI and RSSI be presented in the *2016 Financial Report* to supplement the financial statements. Although RSI and RSSI are not a part of the financial statements, FASAB considers this information to be an essential part of financial reporting for placing the financial statements in appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the RSI and RSSI in accordance with U.S. generally accepted government auditing standards because of the material weaknesses and other scope limitations discussed in this audit report. We did not audit and do not express an opinion or provide any assurance on the RSI or RSSI.

Other Information

Other information included in the *2016 Financial Report* contains a wide range of information, some of which is not directly related to the consolidated financial statements. This information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements, RSI, or RSSI. We read the other information included with the consolidated financial statements in order to identify material inconsistencies, if any, with the consolidated financial statements. We did not audit and do not express an opinion or provide any assurance on the other information in the *2016 Financial Report*.

Readers are cautioned that the material weaknesses, significant uncertainties, and other scope limitations discussed in this audit report may affect the reliability of certain information contained in the RSI, RSSI, and other information that is taken from the same data sources as the accrual-based consolidated financial statements and the sustainability financial statements.

[22]GAO, *Fiscal Outlook: Federal Fiscal Outlook*, accessed January 4, 2017, http://www.gao.gov/fiscal_outlook/federal_fiscal_outlook/overview#t=3, and *Fiscal Exposures: Improving Cost Recognition in the Federal Budget*, GAO-14-28 (Washington, D.C.: Oct. 29, 2013).

CFO Act Agency Financial Management Systems

The federal government's ability to efficiently and effectively manage and oversee its day-to-day operations and programs relies heavily on the ability of entity financial management systems to produce complete, reliable, timely, and consistent financial information for use by executive branch agencies and Congress.[23] The Federal Financial Management Improvement Act of 1996 (FFMIA) was designed to lead to system improvements that would result in CFO Act agency managers routinely having access to reliable, useful, and timely financial-related information with which to measure performance and increase accountability throughout the year.

The 24 CFO Act agencies are responsible for implementing and maintaining financial management systems that substantially comply with the requirements of FFMIA. FFMIA requires auditors, as part of the 24 CFO Act agencies' financial statement audits, to report whether those agencies' financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the federal government's *U.S. Standard General Ledger* at the transaction level.

For fiscal year 2016, auditors at 9 of 21 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements.[24] For fiscal year 2015, auditors at 12 of the 24 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. Agency management at the 24 CFO Act agencies also annually report on FFMIA compliance. For fiscal year 2016, agency management at 7 of 21 CFO Act agencies reported that their agencies' financial management systems were not in substantial compliance with one or more of the three FFMIA requirements. For fiscal year 2015, agency management at 10 of the 24 CFO Act agencies reported that their agencies' financial management systems were not in substantial compliance with one or more of the three FFMIA requirements. Based on agency financial reports, the differences in the assessments of substantial compliance between the auditors and agency management reflected differences in management's and auditors' views on the impact of reported deficiencies on agencies' financial management systems.

Long-standing financial management systems weaknesses at several large CFO Act agencies, along with the size and complexity of the federal government, continue to present a formidable management challenge in providing accountability to the nation's taxpayers and have contributed significantly to certain of the material weaknesses and other limitations discussed in this audit report.

[23]The Federal Financial Management Improvement Act of 1996, which is reprinted in 31 U.S.C. § 3512 note, defines "financial management systems" to include the financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions.

[24]As of the issue date of this audit report, the audited financial statements were not issued for three of the CFO Act agencies—DOD, HUD, and NSF.

Report on Internal Control over Financial Reporting

Management's Responsibility

Management of the federal government is responsible for (1) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, and (2) evaluating the effectiveness of internal control over financial reporting, based on criteria established under the Federal Managers' Financial Integrity Act (FMFIA).[25]

Auditor's Responsibility

The purpose of an audit of financial statements is to express an opinion on the financial statements. An audit of financial statements includes considering internal control over financial reporting to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of internal control over financial reporting. We did not consider all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations.

Our responsibility is to report any material weaknesses or significant deficiencies in internal control over financial reporting for fiscal year 2016 that come to our attention as a result of our audit. Based on the scope of our work and the effects of the other limitations on the scope of our audit noted throughout this audit report, our internal control work was not designed to, and would not necessarily, identify all deficiencies in internal control, including those that might be material weaknesses or significant deficiencies.[26] Therefore, additional material weaknesses or significant deficiencies may exist that were not identified. Our work was performed in accordance with U.S. generally accepted government auditing standards.

Definitions and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and (2) transactions are executed in accordance with provisions of applicable laws, including those governing the use of budget authority; regulations; contracts; and grant agreements, noncompliance with which could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error.

[25]31 U.S.C. § 3512 (c), (d) (commonly referred to as FMFIA). This act requires executive agency heads to evaluate and report annually to the President and Congress on the adequacy of their internal control and accounting systems and on actions to correct significant problems.

[26]A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Material Weaknesses Resulted in Ineffective Internal Control over Financial Reporting

The material weaknesses discussed in this audit report resulted in ineffective internal control over financial reporting. Consequently, the federal government's internal control did not provide reasonable assurance that a material misstatement of the consolidated financial statements would be prevented, or detected and corrected, on a timely basis.

In addition to the material weaknesses that contributed to our disclaimers of opinion on the accrual-based consolidated financial statements and the sustainability financial statements, which were discussed previously, we found the following three other material weaknesses in internal control. These other material weaknesses were the federal government's inability to

- determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them,
- identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and
- effectively manage its tax collection activities.

These material weaknesses are discussed in more detail in appendix III, including the primary effects of the material weaknesses on the accompanying accrual-based consolidated financial statements and on the management of federal government operations.

We also found two significant deficiencies in the federal government's internal control related to implementing effective internal controls at certain federal entities for the following areas:

- loans receivable and loan guarantee liabilities and
- federal grants management.

These significant deficiencies are discussed in more detail in appendix IV.

Further, individual federal entity financial statement audit reports identified additional control deficiencies that were reported by the entities' auditors as either material weaknesses or significant deficiencies at the individual entity level. We do not consider these additional deficiencies to represent material weaknesses or significant deficiencies with respect to the U.S. government's consolidated financial statements.

Intended Purpose of Report on Internal Control over Financial Reporting

The purpose of this report on internal control over financial reporting is solely to describe the scope of our consideration of internal control over financial reporting, and the results of our procedures, and not to provide an opinion on the effectiveness of internal control over financial reporting. This report on internal control over financial reporting is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering internal control. Accordingly, this report on internal control over financial reporting is not suitable for any other purpose.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

Management's Responsibility

Management of the federal government is responsible for the federal government's compliance with laws, regulations, contracts, and grant agreements.

Auditor's Responsibility

An audit of federal financial statements includes testing compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements that have a direct effect on the determination of material amounts and disclosures in the consolidated financial statements, and performing certain other limited procedures. Accordingly, we did not test the federal government's compliance with all laws, regulations, contracts, and grant agreements. Due to the limitations discussed below and the scope of our procedures, noncompliance may occur and not be detected by these tests.

Our objective was not to provide an opinion on the federal government's compliance with laws, regulations, contracts, and grant agreements. Accordingly, we do not express such an opinion. Our work was performed in accordance with U.S. generally accepted government auditing standards.

Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

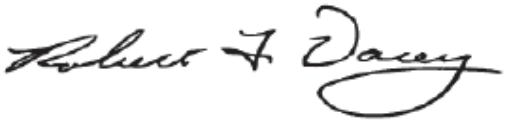
Our work to test compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements was limited by certain of the material weaknesses and other scope limitations discussed in this audit report. U.S. generally accepted government auditing standards and OMB guidance require auditors to report on entities' compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements. Certain component entity audit reports contain instances of noncompliance. None of these instances were deemed to be reportable noncompliance with regard to the accompanying U.S. government's consolidated financial statements.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report on compliance with laws, regulations, contracts, and grant agreements is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the results of that testing, and not to provide an opinion on compliance. This report on compliance with laws, regulations, contracts, and grant agreements is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

Agency Comments

We provided a draft of this audit report to Treasury and OMB officials, who provided technical comments that we have incorporated as appropriate. Treasury and OMB officials expressed their continuing commitment to addressing the problems this report outlines.



Robert F. Dacey
Chief Accountant
U.S. Government Accountability Office

January 4, 2017

Appendix I

Objectives, Scope, and Methodology

Our objectives were to audit the consolidated financial statements consisting of the (1) accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2016, and 2015, and (2) sustainability financial statements, which consist of the 2016 and 2015 Statements of Long-Term Fiscal Projections; the 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance; and the 2016 and 2015 Statements of Changes in Social Insurance Amounts. Our objectives also included reporting on internal control over financial reporting and on compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements.

The Chief Financial Officers Act of 1990 (CFO Act), as expanded by the Government Management Reform Act of 1994 (GMRA), requires the inspectors general of the 24 CFO Act agencies to be responsible for annual audits of agency-wide financial statements prepared by these agencies.[27] GMRA requires GAO to be responsible for the audit of the U.S. government's consolidated financial statements,[28] and the Accountability of Tax Dollars Act of 2002 (ATDA) requires most other executive branch entities to annually prepare financial statements and have them audited.[29] The Office of Management and Budget (OMB) and the Department of the Treasury (Treasury) have identified 39 federal entities that are significant to the U.S. government's fiscal year 2016 consolidated financial statements, including the 24 CFO Act agencies.[30] We consider these 39 entities to be significant component entities for purposes of our audit of the consolidated financial statements. Our work was performed in coordination and cooperation with the inspectors general and independent public accountants for these significant component entities to achieve our respective audit objectives.[31] Our audit approach regarding the accrual-based consolidated financial statements primarily focused on determining the current status of the material weaknesses that contributed to our disclaimer of opinion on the accrual-based consolidated financial statements and the other material weaknesses affecting internal control that we reported in our report on the consolidated financial statements for fiscal year 2015.[32] We also separately audited the financial statements of certain component entities, and parts of a significant component entity, including the following.

- We audited and expressed an unmodified opinion on the Internal Revenue Service's (IRS) financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[33] In

[27]31 U.S.C. § 3521(e). GMRA authorized the Office of Management and Budget to designate agency components that also would receive financial statement audits. See 31 U.S.C. § 3515(c).

[28]GMRA, Pub. L. No. 103-356, § 405(c), 108 Stat. 3410, 3416-17 (Oct. 13, 1994), *codified at* 31 U.S.C. § 331(e)(2).

[29]ATDA, Pub. L. No. 107-289, 116 Stat. 2049 (Nov. 7, 2002), *codified at* 31 U.S.C. § 3515.

[30]See *Treasury Financial Manual*, vol. I, pt. 2, ch. 4700, for a listing of the 39 entities.

[31]For fiscal years 2016 and 2015, the Defense Security Cooperation Agency and the General Fund of the U.S. Government were not audited.

[32]GAO, *Financial Audit: U.S. Government's Fiscal Years 2015 and 2014 Consolidated Financial Statements*, GAO-16-357R (Washington, D.C.: Feb. 25, 2016).

[33]GAO, *Financial Audit: IRS's Fiscal Years 2016 and 2015 Financial Statements*, GAO-17-140 (Washington, D.C.: Nov. 10, 2016).

fiscal years 2016 and 2015, IRS collected about $3.3 trillion in tax payments each year and paid about $426 billion and $403 billion, respectively, in refunds to taxpayers. For fiscal year 2016, we continued to report a material weakness in internal control over unpaid assessments that resulted in ineffective internal control over financial reporting. In addition, we continued to report a significant deficiency in IRS's internal control over financial reporting systems. We also reported that we found no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Schedules of Federal Debt managed by Treasury's Bureau of the Fiscal Service (Fiscal Service) for the fiscal years ended September 30, 2016, and 2015.[34] For these 2 fiscal years, the schedules reported (1) approximately $14.2 trillion (2016) and $13.1 trillion (2015) of federal debt held by the public;[35] (2) about $5.4 trillion (2016) and $5.0 trillion (2015) of intragovernmental debt holdings;[36] and (3) about $273 billion (2016) and $251 billion (2015) of interest on federal debt held by the public. We also reported that Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2016. In addition, we reported that we found no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested related to the Schedule of Federal Debt.

- We audited and expressed unmodified opinions on the U.S. Securities and Exchange Commission's (SEC) and its Investor Protection Fund's (IPF) financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[37] We also reported that SEC maintained, in all material respects, effective internal control over financial reporting for both the entity as a whole and the IPF as of September 30, 2016. In addition, we reported that we found no reportable noncompliance for either SEC or IPF for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Federal Housing Finance Agency's (FHFA) financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[38] We also reported that FHFA maintained, in all material respects, effective internal control over financial reporting as of September 30, 2016. In addition, we reported that we found no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

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[34]GAO, *Financial Audit: Bureau of the Fiscal Service's Fiscal Years 2016 and 2015 Schedules of Federal Debt*, GAO-17-104 (Washington, D.C.: Nov. 10, 2016).

[35]Debt held by the public on the Schedules of Federal Debt represents federal debt issued by Treasury and held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments.

[36]Intragovernmental debt holdings represent federal debt owed by Treasury to federal government accounts, primarily federal trust funds, such as Social Security and Medicare.

[37]GAO, *Financial Audit: Securities and Exchange Commission's Fiscal Years 2016 and 2015 Financial Statements*, GAO-17-158R (Washington, D.C.: Nov. 15, 2016).

[38]GAO, *Financial Audit: Federal Housing Finance Agency's Fiscal Years 2016 and 2015 Financial Statements*, GAO-17-139R (Washington, D.C.: Nov. 15, 2016).

- We audited and expressed an unmodified opinion on the Office of Financial Stability's (OFS) financial statements for the Troubled Asset Relief Program (TARP) as of and for the fiscal years ended September 30, 2016, and 2015.[39] We also reported that OFS maintained, in all material respects, effective internal control over financial reporting for TARP as of September 30, 2016. In addition, we reported that we found no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Bureau of Consumer Financial Protection's (CFPB) financial statements as of and for the fiscal years ended September 30, 2016, and 2015.[40] We also reported that although certain internal controls could be improved, CFPB maintained, in all material respects, effective internal control over financial reporting as of September 30, 2016. In addition, we reported that we found no reportable noncompliance for fiscal year 2016 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

In addition, we considered the CFO Act agencies' and certain other federal entities' fiscal years 2016 and 2015 financial statements and the related auditors' reports prepared by the inspectors general or contracted independent public accountants. Financial statements and audit reports for these entities provide information about the entities' operations. Each entity audit report also contains details regarding any identified material weaknesses or significant deficiencies and related recommendations for the respective entity. We did not audit, and we do not express an opinion on, any of these individual federal entity financial statements.

We considered OMB's and Treasury's representation regarding the Department of Defense's (DOD) noncompliant financial management systems and lack of reasonable assurance that internal controls over financial reporting were effective. In addition, OMB and Treasury represented that the previously reported DOD material weaknesses continue to exist in several areas, including (1) property, plant, and equipment; (2) inventory and operating material and supplies; (3) environmental liabilities; (4) intragovernmental eliminations; and (5) material amounts of unsupported accounting entries needed to prepare DOD's annual consolidated financial statements.

Our audit approach for the 2016 and 2015 Statements of Long-Term Fiscal Projections focused primarily on assuring that the information relating to the Statements of Social Insurance is properly reflected therein and testing the methodology used as well as evaluating key assumptions. We also evaluated whether the internal control deficiencies concerning the accrual-based consolidated financial statements affected certain key inputs used in generating the projections.

Because of the significance of the amounts presented in the Statements of Social Insurance and Statements of Changes in Social Insurance Amounts related to the Social Security Administration (SSA) and the Department of Health and Human Services (HHS), our audit approach regarding these statements focused primarily on these two agencies. For each federal entity preparing a Statement of Social Insurance and Statement of Changes in Social Insurance

[39]GAO, *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Years 2016 and 2015 Financial Statements*, GAO-17-125R (Washington, D.C.: Nov. 10, 2016).

[40]GAO, *Financial Audit: Bureau of Consumer Financial Protection's Fiscal Years 2016 and 2015 Financial Statements*, GAO-17-138R (Washington, D.C.: Nov. 15, 2016).

Amounts,[41] we considered the entity's 2016, 2015, 2014, 2013, and 2012 Statements of Social Insurance and the 2016 and 2015 Statements of Changes in Social Insurance Amounts, as well as the related auditor's reports prepared by the inspectors general or contracted independent public accountants.

We performed sufficient audit work to provide our reports on (1) the consolidated financial statements; (2) internal control over financial reporting; and (3) compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements. We considered the limitations on the scope of our work regarding the accrual-based consolidated financial statements and the sustainability financial statements in forming our conclusions. Our work was performed in accordance with U.S. generally accepted government auditing standards.

[41]These entities are SSA, HHS, the Railroad Retirement Board, and the Department of Labor.

Appendix II

Material Weaknesses Contributing to Our Disclaimer of Opinion on the Accrual-Based Consolidated Financial Statements

The continuing material weaknesses discussed below contributed to our disclaimer of opinion on the federal government's accrual-based consolidated financial statements.[42] The federal government did not maintain adequate systems or have sufficient appropriate evidence to support information reported in the accompanying accrual-based consolidated financial statements, as described below.

Property, Plant, and Equipment and Inventories and Related Property

The federal government could not satisfactorily determine that property, plant, and equipment (PP&E) and inventories and related property were properly reported in the accrual-based consolidated financial statements. Most of the PP&E and inventories and related property are the responsibility of the Department of Defense (DOD). As in past years, DOD did not maintain adequate systems or have sufficient records to provide reliable information on these assets. Certain other entities' auditors also reported continued deficiencies in internal control procedures and processes related to PP&E.

Deficiencies in internal control over such assets could affect the federal government's ability to fully know the assets it owns, including their location and condition, and its ability to effectively (1) safeguard assets from physical deterioration, theft, or loss; (2) account for acquisitions and disposals of such assets and reliably report asset balances; (3) ensure that the assets are available for use when needed; (4) prevent unnecessary storage and maintenance costs or purchase of assets already on hand; and (5) determine the full costs of programs that use these assets.

Liabilities and Commitments and Contingencies

The federal government could not reasonably estimate or adequately support amounts reported for certain liabilities. For example, DOD was not able to estimate with assurance key components of its environmental and disposal liabilities. In addition, DOD could not support a significant amount of its estimated military postretirement health benefits liabilities included in federal employee and veteran benefits payable. These unsupported amounts related to the cost of direct health care provided by DOD-managed military treatment facilities. Further, the federal government could not determine whether commitments and contingencies, including any related to treaties and other international agreements entered into to further the federal government's interests, were complete and properly reported.

Problems in accounting for liabilities affect the determination of the full cost of the federal government's current operations and the extent of its liabilities. Also, deficiencies in internal control supporting the process for estimating environmental and disposal liabilities could result in improperly stated liabilities, as well as adversely affect the federal government's ability to determine priorities for cleanup and disposal activities and to appropriately consider future budgetary resources needed to carry out these activities. In addition, to the extent disclosures of

[42]The material weakness related to the Reconciliations of Budget Deficit to Net Operating Cost and Changes in Cash Balance also contributed to our disclaimer on the 2016 and 2015 Statements of Long-Term Fiscal Projections.

commitments and contingencies are incomplete or incorrect, reliable information is not available about the extent of the federal government's obligations.

Cost of Government Operations and Disbursement Activity

Reported net costs were affected by the previously discussed material weaknesses in reporting assets and liabilities; material weaknesses in financial statement preparation, as discussed below; and the lack of adequate disbursement reconciliations at certain federal entities. As a result, the federal government was unable to support significant portions of the reported total net cost of operations, most notably those related to DOD.

With respect to disbursements, auditors of certain federal entities reported continued control deficiencies in reconciling disbursement activity. For fiscal years 2016 and 2015, inadequate reconciliations of disbursement activity included (1) unreconciled differences between federal entities' and the Department of the Treasury's (Treasury) records of disbursements and (2) unsupported federal entity adjustments, which could also affect the balance sheet.

Unreliable cost information affects the federal government's ability to control and reduce costs, assess performance, evaluate programs, and set fees to recover costs where required or authorized. If disbursements are improperly recorded, this could result in misstatements in the financial statements and in certain data provided by federal entities for inclusion in *The Budget of the United States Government* (President's Budget) concerning obligations and outlays.

Accounting for and Reconciliation of Intragovernmental Activity and Balances

Significant progress has been made over the past few years; however, the federal government continues to be unable to adequately account for and reconcile intragovernmental activity and balances between federal entities. Federal entities are responsible for properly accounting for and reporting their intragovernmental activity and balances in their entity financial statements. When preparing the consolidated financial statements, intragovernmental activity and balances between federal entities should be in agreement and must be subtracted out, or eliminated, from the financial statements. If the two federal entities engaged in an intragovernmental transaction do not both record the same intragovernmental transaction in the same year and for the same amount, the intragovernmental transactions will not be in agreement, resulting in errors in the consolidated financial statements. The Office of Management and Budget (OMB) and Treasury require the chief financial officers (CFO) of the significant component entities to reconcile, on a quarterly basis, selected intragovernmental activity and balances with their trading partners. In addition, these entities are required to report to Treasury, their respective inspectors general, and GAO on the extent and results of intragovernmental activity and balance-reconciliation efforts as of the end of the fiscal year.

Treasury has continued to actively work with significant federal component entities to resolve intragovernmental differences through its quarterly scorecard process.[43] This process highlights differences requiring the entities' attention, identifies differences that need to be resolved

[43]For each quarter, Treasury produces a scorecard for each significant entity that reports various aspects of the entity's intragovernmental differences with its trading partners, including the composition of the differences by trading partner and category. Entities are expected to resolve, with their respective trading partners, the differences identified in their scorecards.

through a formal dispute resolution process,[44] and reinforces the entities' responsibilities to resolve intragovernmental differences. In fiscal year 2016, Treasury made all the scorecards available to the financial communities of all the significant component entities in order to raise the scorecards' visibility and generate additional scrutiny of intragovernmental differences at the government-wide level. Previously, each scorecard was available to only the significant component entity to which it related. In addition to improvements to the scorecard process, Treasury continued to implement a new initiative for identifying and monitoring systemic root causes of intragovernmental differences. As a result of these and other actions, a significant number of intragovernmental differences were identified and resolved. While progress was made, we continued to note that amounts reported by federal entity trading partners to Treasury were not in agreement by material amounts. Reasons for the differences cited by several CFOs included differing accounting methodologies, accounting errors, and timing differences.

Further, a significant portion of intragovernmental differences are related to unreconciled transactions between the General Fund of the U.S. Government (General Fund)[45] and federal entity trading partners related to appropriations and other intragovernmental transactions, which amount to hundreds of billions of dollars. Treasury continued to develop and refine its policies and procedures over accounting for and reporting all significant General Fund activity and balances and reconciling the activity and balances between the General Fund and its trading partners. However, the ability to effectively reconcile General Fund transactions will be hampered until General Fund-related activity and balances are properly accounted for, reported, and audited. Furthermore, General Fund internal policies and procedures still need to be adopted and further changes are needed to enhance guidance regarding General Fund-related activity and balances in the *Treasury Financial Manual*. Treasury plans to obtain an audit of the General Fund activity and balances.

As a result of the above-noted circumstances, the federal government's ability to determine the impact of these differences on the amounts reported in the accrual-based consolidated financial statements is significantly impaired. Resolving the intragovernmental transactions problem remains a difficult challenge and will require a strong and sustained commitment by federal entities to timely resolve differences with their trading partners, as well as continued strong leadership by Treasury and OMB.

Preparation of Consolidated Financial Statements

Treasury, in coordination with OMB, has implemented several corrective actions during the past few years related to the preparation of the consolidated financial statements. Corrective actions included implementing new systems to collect certain additional data from component entities and to compile the consolidated financial statements, and new or enhanced procedures to

[44]When an entity and its respective trading partner cannot resolve an intragovernmental difference, the entity must request Treasury to resolve the dispute. Treasury will review the dispute and issue a decision on how to resolve the difference, which the entities must follow.

[45]The General Fund is a component of Treasury's central accounting function. It is a stand-alone reporting entity that comprises the activities fundamental to funding the federal government (e.g., issued budget authority, cash activity, and debt financing activities).

address certain internal control deficiencies detailed in our previously issued report.[46] However, the federal government's systems, controls, and procedures were not adequate to reasonably assure that the consolidated financial statements are consistent with the underlying audited entity financial statements, properly balanced, and in accordance with U.S. generally accepted accounting principles (U.S. GAAP). During our fiscal year 2016 audit, we found the following.

- For fiscal year 2016, auditors reported internal control deficiencies at several component entities regarding entities' financial reporting processes that could affect information in those entities' closing packages.[47] As in past years, Treasury had to record significant adjustments to correct errors found in federal entities' audited closing package information. These errors primarily related to intragovernmental activity and balances and totaled tens of billions of dollars. To reasonably assure consistency of underlying entity information and financial data with the U.S. government's consolidated financial statements, entity auditors are required to separately audit and report on the financial information that the significant component entities send to Treasury through closing packages.[48]

- Treasury is unable to properly balance the accrual-based consolidated financial statements. To make the fiscal years 2016 and 2015 consolidated financial statements balance, Treasury recorded net decreases of $11.7 billion and $5.1 billion, respectively, to net operating cost on the Statements of Operations and Changes in Net Position, which were identified as "Unmatched transactions and balances."[49] Treasury recorded an additional net $0.5 billion and $1.9 billion of unmatched transactions in the Statement of Net Cost for fiscal years 2016 and 2015, respectively. The material weakness in the federal government's ability to account for and reconcile intragovernmental activity and balances, discussed above, significantly contributes to the unmatched transactions and balances and consequently impairs Treasury's ability to fully eliminate such intragovernmental activity and balances.

- Over the past several years, Treasury has taken significant actions to assist in ensuring that financial information is reported or disclosed in the consolidated financial statements in accordance with U.S. GAAP. For example, Treasury has developed and implemented U.S. GAAP compliance operating procedures and checklists. However, Treasury's reporting of certain financial information required by U.S. GAAP continues to be impaired. Due to certain control deficiencies noted in this audit report—for example, commitments and contingencies related to treaties and other international agreements—Treasury is precluded from determining if additional disclosure is required by U.S. GAAP in the consolidated financial

[46]Most of the issues we identified in fiscal year 2016 existed in fiscal year 2015, and many have existed for a number of years. Most recently, in July 2016, we reported the issues we identified to Treasury and OMB and provided recommendations for corrective action. See GAO, *Management Report: Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*, GAO-16-621 (Washington, D.C.: July 13, 2016).

[47]The closing package methodology links federal component entities' audited consolidated department-level financial statements to certain line items, note disclosures, and other information of the U.S. government's consolidated financial statements.

[48]There are 39 significant component entities, including the General Fund; however, the General Fund did not submit a closing package in fiscal year 2016.

[49]Although Treasury was unable to determine how much of the unmatched transactions and balances relates to net operating cost, it reported this amount as a component of net operating cost in the accompanying consolidated financial statements.

statements, and we are precluded from determining whether the omitted information is material. Further, Treasury's ability to report information in accordance with U.S. GAAP will also remain impaired until federal entities, such as DOD, can provide Treasury with complete and reliable information required to be reported in the consolidated financial statements.

- In fiscal year 2016, Treasury continued to make progress with corrective actions intended to resolve internal control deficiencies in the processes used to prepare the consolidated financial statements. For example, Treasury enhanced its procedures for obtaining audited closing packages from component entities identified as significant to the consolidated financial statements. However, other internal control deficiencies existed in the processes used to prepare the consolidated financial statements, such as inadequate processes for monitoring and assessing internal controls over the preparation of the consolidated financial statements. As a result, we identified errors, such as unclear or incomplete disclosures, in draft consolidated financial statements that were subsequently corrected.

- In fiscal year 2016, Treasury continued to improve its systems and processes for preparing the consolidated financial statements. For example, Treasury continued to enhance the automated tool used in the compilation process. However, challenges remain regarding systems and processes for certain central accounting functions related to accurately reporting, as well as obtaining audit assurance over, General Fund transactions and components of the budget deficit. It is important that Treasury (1) continues to improve its systems and (2) remains committed to maintaining the progress that has been made in this area and building on that progress to make needed improvements to fully address the magnitude of the financial reporting challenges it faces.

Until these internal control deficiencies have been fully addressed, the federal government's ability to reasonably assure that the consolidated financial statements are consistent with the underlying audited federal component entities' financial statements, properly balanced, and in accordance with U.S. GAAP will be impaired. Resolving these internal control deficiencies remains a difficult challenge and will require a strong and sustained commitment from Treasury and OMB as they continue to execute and implement corrective actions.

Reconciliations of Budget Deficit to Net Operating Cost and Changes in Cash Balance

Over the past 3 years, Treasury has improved its process for preparing the (1) Reconciliation of Net Operating Cost and Unified Budget Deficit and (2) Statement of Changes in Cash Balance from Unified Budget and Other Activities (Reconciliation Statements). For example, during fiscal year 2016, Treasury continued to refine its process to ensure the consistency of reconciling items reported on the Reconciliation Statements to entity financial information that is processed through Treasury's records. However, the federal government has not established and implemented effective processes and procedures for (1) identifying and reporting all items needed to prepare the Reconciliation Statements and (2) reasonably assuring that the information in these statements was fully consistent with the underlying information in the significant component entities' audited financial statements and other financial data. Until Treasury develops and fully implements an effective process for reasonably assuring completeness and consistency of the information in the statements and is able to fully reconcile this information, the effect on the U.S. government's consolidated financial statements will continue to be unknown.

The Reconciliation Statements report unified budget deficits for fiscal years 2016 and 2015 of about $587 billion and $439 billion, respectively.[50] The budget deficit is calculated by subtracting actual budget outlays (outlays) from actual budget receipts (receipts). Also, such outlays and receipts are key inputs to the Statements of Long-Term Fiscal Projections. Treasury and OMB continue to lack an effective process for reasonably assuring the consistency of the information among (1) information that Treasury uses to compute the budget deficit reported in the consolidated financial statements, (2) Treasury's records of cash transactions processed through its central accounting function, and (3) information reported in federal entity financial statements and underlying entity financial information and records. Over the past few years, Treasury has made progress by developing and implementing procedures to reconcile outlays and receipts between Treasury's records used to compute the budget deficit reported in the consolidated financial statements and underlying federal entity financial information and records.

In fiscal year 2016, we again noted that several entities' auditors reported internal control deficiencies related to monitoring, accounting, and reporting of budgetary transactions. These control deficiencies could affect the reporting and calculation of the net outlay amounts in the entities' Statements of Budgetary Resources. In addition, such deficiencies may also affect the entities' ability to report reliable budgetary information to Treasury and OMB and may affect the unified budget deficit reported in the accrual-based consolidated financial statements. Treasury also reports the unified budget deficit in its *Combined Statement of Receipts, Outlays, and Balances*,[51] and in other federal government publications.

[50]The budget deficit, receipts, and outlays amounts are reported in Treasury's *Monthly Treasury Statement* and the President's Budget.

[51]Treasury's *Combined Statement of Receipts, Outlays, and Balances* presents budget results and cash-related assets and liabilities of the federal government with supporting details. According to Treasury, this report is the recognized official publication of receipts and outlays of the federal government based on entity reporting.

Appendix III

Other Material Weaknesses

Material weaknesses in internal control discussed in this audit report resulted in ineffective controls over financial reporting. In addition to the material weaknesses discussed in appendix II that contributed primarily to our disclaimer of opinion on the accrual-based consolidated financial statements, we found the following three other material weaknesses in internal control.

Improper Payments

The federal government is unable to determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them. Reducing improper payments is critical to safeguarding federal funds.[52] The Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA),[53] requires federal executive branch entities to (1) review all programs and activities, (2) identify those that may be susceptible to significant improper payments, (3) estimate the annual amount of improper payments for those programs and activities identified as risk susceptible, (4) implement actions to reduce improper payments and set reduction targets with respect to the risk-susceptible programs and activities, and (5) report on the results of addressing the foregoing requirements.

The Office of Management and Budget (OMB) reported that the government-wide improper payment error rate, among programs and activities that reported estimates, increased to 4.7 percent of program outlays in fiscal year 2016 from 4.4 percent in fiscal year 2015 when including the Department of Defense's (DOD) Defense Finance and Accounting Service (DFAS) Commercial Pay program.[54] When excluding the DFAS Commercial Pay program, the reported government-wide error rate was 5.1 percent of program outlays in fiscal year 2016 compared to 4.8 percent in fiscal year 2015. In May 2013, we reported on major deficiencies in DOD's process for estimating fiscal year 2012 improper payments in the DFAS Commercial Pay program, including deficiencies in identifying a complete and accurate population of payments.[55] The foundation of reliable statistical sampling estimates is a complete, accurate, and valid population from which to sample. As of October 2016, DOD's efforts to establish and implement key quality assurance procedures to ensure the completeness and accuracy of sampled

[52]Under the Improper Payments Information Act of 2002, as amended, an improper payment is statutorily defined as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes any payment to an ineligible recipient, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts. Office of Management and Budget guidance also instructs agencies to report as improper payments any payments for which insufficient or no documentation was found.

[53]IPIA, Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002), as amended by IPERA, Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010), and IPERIA, Pub. L. No. 112-248, 126 Stat. 2390 (Jan. 10, 2013), and reprinted in 31 U.S.C. § 3321 note.

[54]Reported error rates reflect the estimated improper payments as a percentage of total program outlays.

[55]GAO, *DOD Financial Management: Significant Improvements Needed in Efforts to Address Improper Payment Requirements*, GAO-13-227 (Washington, D.C.: May 13, 2013).

populations were still under development. Therefore, DOD's fiscal year 2016 improper payment estimates, including its estimate for the DFAS Commercial Pay program, may not be reliable.

Without the DFAS Commercial Pay program, federal entity improper payment estimates totaled $144.3 billion in fiscal year 2016, a significant increase from the prior-year estimate of $136.7 billion. The increase in estimated improper payments was mostly attributable to increased program outlays in the Department of Health and Human Services' (HHS) Medicaid program. It is important to note that pursuant to OMB implementing guidance, reported improper payment estimates include overpayments, underpayments, and payments for which adequate documentation was not found, and may also include amounts of payment for years prior to the current fiscal year.

While the specific programs included in the government-wide improper payment estimate may change from year to year, a net of 10 fewer programs were included in fiscal year 2016 when compared to fiscal year 2015.[56] In addition, eight federal entities did not report fiscal year 2016 estimated improper payment amounts for 18 risk-susceptible programs, including the Department of Agriculture's (USDA) Supplemental Nutrition Assistance Program and HHS's Temporary Assistance for Needy Families.[57] Further, various inspectors general reported deficiencies related to compliance with the criteria listed in IPERA for fiscal year 2015 at their respective federal entities,[58] including risk-susceptible programs that did not report improper payment estimates, estimation methodologies that may not produce reliable estimates, and risk assessments that may not accurately assess the risk of improper payment.

For fiscal year 2016, federal entities reported improper payment error rates that exceeded 10 percent for 11 risk-susceptible programs, accounting for more than 70 percent of the

[56]Additionally, two entities reported estimates for four new programs, but these estimates were excluded from the government-wide estimate by OMB because they did not have approved methodologies. These four programs were (1) the Corporation for National and Community Service's (CNCS) Foster Grandparents, (2) CNCS's Retired and Senior Volunteer, (3) CNCS's Senior Companion, and (4) DOD's Navy Commercial Bill Pay Office – Naples.

[57]The remaining 16 programs were (1) CNCS's AmeriCorps; (2) USDA's Child and Adult Care Food Program; (3) DOD's Navy Commercial Bill Pay Office – Singapore; (4) HHS's Advance Premium Tax Credit; (5) HHS's Cost-Sharing Reduction; (6) the Department of Housing and Urban Development's (HUD) Single Family Insurance Claims; (7) HUD's Community Planning and Development Entitlement Grants; (8) HUD's HOME Investments Program; (9) the Department of the Treasury's (Treasury) Advance Child Tax Credit; (10) Treasury's Additional Opportunity Tax Credit; (11) Treasury's Premium Tax Credit; (12) the Department of Veterans Affairs' (VA) Communications, Utilities, and Other Rent; (13) VA's Medical Care Contracts and Agreements; (14) VA's Prosthetics; (15) VA's VA Community Care Choice payments made from the Veterans Choice Fund; and (16) the Environmental Protection Agency's Grants.

[58]IPERA established a requirement for entity inspectors general to report annually on entities' compliance with criteria listed in section 3 of IPERA. The six criteria are that the entity has (1) published an annual financial statement and accompanying materials in the form and content required by OMB for the most recent fiscal year and posted that report on the entity website; (2) conducted a risk assessment for each specific program or activity that conforms with IPIA, as amended; (3) published estimates of improper payments for all programs and activities identified as susceptible to significant improper payments under the entity's risk assessment; (4) published corrective action plans for programs and activities assessed to be at risk for significant improper payments; (5) published and met annual reduction targets for all programs and activities assessed to be at risk for significant improper payments; and (6) reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published. The most recent inspectors general reports on compliance with the criteria listed in IPERA were issued in 2016 for fiscal year 2015. Pursuant to the OMB implementing guidance in OMB Memorandum M-15-02, appendix C to OMB Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* (Oct. 20, 2014), inspectors general reports are due within 180 days of publication of the performance and accountability reports or agency financial reports. Therefore, inspectors general reports on fiscal year 2016 compliance with the criteria listed in IPERA are generally expected to be issued by May 2017.

government-wide improper payment estimate.[59] Under IPERA, an entity that is determined by its inspector general to not be in compliance with the criteria listed in IPERA, such as reporting an improper payment rate of 10 percent or greater for any risk-susceptible program or activity, must submit a plan to Congress describing the actions that the entity will take to come into compliance.

Further, entity auditors continued to report internal control deficiencies over financial reporting in their fiscal year 2016 financial statement audit reports, such as financial system limitations and information system control weaknesses. Such deficiencies could significantly increase the risk that improper payments may occur and not be detected promptly.

The President's fiscal year 2016 and fiscal year 2017 budgets included program integrity proposals at multiple agencies aimed at reducing improper payments. Also, efforts continue to implement requirements established by IPERIA, which was enacted in January 2013 to intensify efforts to identify, prevent, and recover payment error, waste, fraud, and abuse within federal spending. Among other things, IPERIA enacted into law elements of the President's Do Not Pay initiative by requiring entities to review prepayment and pre-award procedures and ensure a thorough review of available databases to determine program or award eligibility before the release of any federal funds. IPERIA also directs OMB to annually identify a list of high-priority federal programs for greater levels of oversight and review and requires each entity responsible for administering one of these high-priority programs to annually submit a program report to its inspector general and make a report copy available to the public.

Until the federal government has implemented effective processes to determine the full extent to which improper payments occur and has taken appropriate actions across entities and programs to effectively reduce improper payments, it will not have reasonable assurance that the use of federal funds is adequately safeguarded.

Information Security

GAO has reported information security as a high-risk area across government since February 1997. During our fiscal year 2016 audit, we found that serious and widespread information security control deficiencies continued to place federal assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption.[60] Specifically, control deficiencies were identified related to (1) security management; (2) access to computer resources (data, equipment, and facilities); (3) changes to and configuration of information system resources; (4) segregation of incompatible duties; and (5) contingency planning.

Such information security control deficiencies unnecessarily increase the risk that data recorded in or transmitted by federal financial management systems are not reliable and available. A

[59]The 11 programs that reported improper payment estimates that exceeded 10 percent in fiscal year 2016 were (1) VA's VA Community Care, (2) VA's Purchased Long-Term Services and Supports, (3) Treasury's Earned Income Tax Credit, (4) USDA's School Breakfast, (5) USDA's Supplemental Revenue Assistance Payments, (6) USDA's National School Lunch, (7) USDA's Livestock Indemnity, (8) the Small Business Administration's Disbursement for Goods and Services, (9) HHS's Medicaid, (10) HHS's Medicare Fee-for-Service, and (11) the Department of Labor's Unemployment Insurance programs.

[60]Nineteen of the 24 agencies covered by the Chief Financial Officers Act of 1990 reported information security as a significant deficiency or material weakness for fiscal year 2016.

primary reason for these deficiencies is that federal entities generally have not yet fully institutionalized comprehensive security management programs, which are critical to identifying information security control deficiencies, resolving information security problems, and managing information security risks on an ongoing basis.

Although significant challenges remain, the federal government has continued to take actions toward improving information security. For example, in July 2016, OMB released its updated Circular No. A-130 on managing federal information resources to address the protection and management of federal information and systems as well as personally identifiable information.[61] The administration has also continued to monitor agencies' efforts to implement cybersecurity capabilities such as strong authentication,[62] continuous monitoring, anti-phishing and malware defense.[63] In its fourth quarter fiscal year 2016 Cybersecurity Update, the administration reported that an increasing number of the 23 civilian Chief Financial Officers Act of 1990 (CFO Act) agencies were meeting targets for the metrics that correspond to these capabilities.[64] However, until entities identify and resolve information security control deficiencies and effectively manage information security risks on an ongoing basis, federal data and systems, including financial information, will remain at risk.

Tax Collection Activities

During fiscal year 2016, a material weakness continued to affect the federal government's ability to effectively manage its tax collection activities. While the Department of the Treasury's Internal Revenue Service (IRS) made necessary and appropriate adjustments to its financial statements, IRS's underlying records did not always reflect the correct amount of taxes owed by the public to the federal government due to financial system limitations and errors in taxpayers' accounts. Such errors may cause undue burden and frustration to taxpayers who either have already paid taxes owed or owe significantly lower amounts.

Collectively, these deficiencies indicate that internal controls were not effective in (1) ensuring that reported amounts of taxes receivable and other tax assessments were accurate on an ongoing basis and could be relied upon by management as a tool to aid in making and supporting resource allocation decisions and (2) supporting timely and reliable financial statements, accompanying notes, and required supplementary information and other information without extensive supplemental procedures and adjustments.

[61]Office of Management and Budget, *Managing Federal Information as a Strategic Resource*, OMB Circular No. A-130 (Washington, D.C.: July 28, 2016).

[62]Authentication is the process a computer system uses to establish the validity of a user's claimed identity by requesting some kind of information, such as a password, that is known only by the user.

[63]According to OMB, anti-phishing and malware defense involves the implementation of technologies, processes, and training to reduce the risk of malware introduced through email and malicious or compromised websites.

[64]According to the administration, its fourth quarter fiscal year 2016 Cybersecurity Update only reflects data from the 23 civilian CFO Act agencies and does not include information from DOD and non-CFO Act agencies.

Appendix IV

Significant Deficiencies

In addition to the material weaknesses discussed in appendixes II and III, we found two significant deficiencies in the federal government's internal control related to implementing effective internal controls at certain federal entities, as described below.

Loans Receivable and Loan Guarantee Liabilities

Internal control deficiencies were identified at certain significant component entities accounting for the majority of the reported balances for loans receivable and loan guarantee liabilities.[65] The deficiencies primarily involved credit subsidy estimation and internal control over such estimation. The issues and complexities associated with estimating the costs of lending and other loan-related financing activities significantly increase the risk that misstatements in agency and government-wide financial statements could occur and go undetected. Further, these control deficiencies can adversely affect the federal government's ability to support annual budget requests for these programs, make future budgetary decisions, manage program costs, and measure the performance of lending activities.

Federal Grants Management

In fiscal year 2016, several federal entities' auditors continued to identify internal control deficiencies related to grants management.[66] Reported deficiencies primarily related to monitoring of grant activities, estimating grant accruals, and accounting for formula grants.[67] These internal control deficiencies could adversely affect the federal government's ability to provide reliable financial statements as well as reasonable assurance that grants are awarded properly, recipients are eligible, and federal grant funds are used as intended.

[65]Key significant component entities contributing to the significant deficiency for Loans Receivable and Loan Guarantee Liabilities include the Departments of Education, Transportation, Housing and Urban Development, and Veterans Affairs.

[66]Key significant component entities contributing to the significant deficiency for Federal Grants Management include the Departments of Homeland Security, Housing and Urban Development, and Health and Human Services.

[67]Formula grants are awarded to all eligible grantees based on a statutory allocation formula, which may be based on a number of variables, including population, poverty rate in a given area, or tax effort. The grants are typically awarded to states, which often pass funds through to eligible local government agencies and nonprofit organizations.