

Consolidated Financial Statements

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
 CONSOLIDATED BALANCE SHEETS
 AS OF SEPTEMBER 30,
 (Dollars in Thousands)

	<u>2002</u>	<u>2001</u> Restated
ASSETS		
Intragovernmental		
Fund Balance with Treasury (Note 2)	\$ 73,092	\$ 52,055
Accounts Receivable	13,952	14,422
Other Assets	4,416	867
Total Intragovernmental	<u>91,460</u>	<u>67,344</u>
Accounts Receivable	284	57
Property, Plant and Equipment, Net (Note 3)	28,511	25,207
Other Assets	2	1
	<u>2</u>	<u>1</u>
Total Assets	<u>\$ 120,257</u>	<u>\$ 92,609</u>
LIABILITIES		
Intragovernmental Liabilities		
Accounts Payable	\$ 357	\$ 212
Other Liabilities (Note 5)	1,383	1,670
Total Intragovernmental	<u>1,740</u>	<u>1,882</u>
Accounts Payable	2,563	3,861
Other Liabilities (Note 4 & 5)	28,461	25,275
	<u>28,461</u>	<u>25,275</u>
Total Liabilities	<u>32,764</u>	<u>31,018</u>
NET POSITION	<u>\$ 87,493</u>	<u>\$ 61,591</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 120,257</u>	<u>\$ 92,609</u>

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENTS OF NET COST
FOR THE FISCAL YEARS ENDED SEPTEMBER 30,
(Dollars in Thousands)

	<u>2002</u>	<u>2001</u>
PROGRAM COSTS		
Gross Costs Intragovernmental	\$ 22,751	\$ 24,673
Less: Intragovernmental Earned Revenue	<u>(136,856)</u>	<u>(140,985)</u>
Intragovernmental Net Costs	(114,105)	(116,312)
Gross Costs Public	<u>92,018</u>	<u>106,280</u>
NET COST OF OPERATIONS	<u><u>\$ (22,087)</u></u>	<u><u>\$ (10,032)</u></u>

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION
FOR THE FISCAL YEARS ENDED SEPTEMBER 30,
(Dollars in Thousands)

	<u>2002</u>	<u>2001</u>
NET POSITION		
Beginning Balance	<u>\$ 61,591</u>	<u>\$ 47,156</u>
OTHER FINANCING SOURCES		
Transfers-In	759	512
Imputed Financing	3,426	3,903
Other	<u>0</u>	<u>(11)</u>
Total Financing Sources	<u>4,185</u>	<u>4,404</u>
NET COST OF OPERATIONS	22,087	10,032
Cumulative Effect of Change in Accounting Principle (Note 6)	<u>(370)</u>	<u>(1)</u>
TOTAL NET POSITION	<u><u>\$ 87,493</u></u>	<u><u>\$ 61,591</u></u>

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Consolidated Financial Statements

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
 COMBINED STATEMENTS OF BUDGETARY RESOURCES
 FOR THE FISCAL YEARS ENDED SEPTEMBER 30,
 (Dollars in Thousands)

	<u>2002</u>	<u>2001</u>
BUDGETARY RESOURCES		
Unobligated Balance at the Beginning of the Period	\$ 38,016	\$ 5,926
Spending Authority from Offsetting Collections	144,987	144,754
Total Budgetary Resources	<u>183,003</u>	<u>150,680</u>
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred	130,321	112,664
Unobligated Balance Available (Note 2)	50,887	36,221
Unobligated Balance Not Available (Note 2)	1,795	1,795
Total Status of Budgetary Resources	<u>183,003</u>	<u>150,680</u>
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Obligated Balance, Net - Beginning of the Period	14,039	39,069
Less: Obligated Balance, Net - End of the Period		
Accounts Receivable	(13,911)	(14,346)
Unfilled Customer Orders from Federal Sources	0	(3,790)
Undelivered Orders	2,628	4,338
Accounts Payable	31,693	27,837
Outlays:		
Disbursements	128,175	133,866
Collections	(149,212)	(140,926)
Net Outlays	<u>\$ (21,037)</u>	<u>\$ (7,060)</u>

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENTS OF FINANCING
FOR THE FISCAL YEARS ENDED SEPTEMBER 30,
(Dollars in Thousands)

	<u>2002</u>	<u>2001</u> Restated
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated		
Obligations Incurred	\$ 130,321	\$ 112,664
Less: Spending Authority from Offsetting Collections and Adjustments	<u>(144,987)</u>	<u>(144,754)</u>
Net Obligations	(14,666)	(32,090)
Other Resources		
Transfers-In	759	512
Financing Imputed for Cost Subsidies	<u>3,426</u>	<u>3,904</u>
Net Other Resources Used to Finance Activities	4,185	4,416
Total Resources Used to Finance Activities	(10,481)	(27,674)
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS		
Change in Budgetary Resources Obligated for Goods, Services and Benefits Ordered But Not Yet Provided	(4,953)	22,066
Resources that Finance the Acquisition of Assets		
Property, Plant and Equipment	(16,575)	(15,257)
Resources that Fund Expenses Recognized in Prior Periods	(227)	(54)
Other Resources that Do Not Affect Net Cost of Operations	<u>0</u>	<u>(2,775)</u>
Total Resources Used to Finance Items Not Part of Net Cost of Operations	(21,755)	3,980
Total Resources Used to Finance the Net Cost of Operations	(32,236)	(23,694)
COMPONENTS NOT REQUIRING OR GENERATING RESOURCES		
Depreciation and Amortization	9,700	9,898
Gain / Loss on Disposition of Assets	191	742
Other	<u>258</u>	<u>3,022</u>
	10,149	13,662
NET COST OF OPERATIONS	\$ (22,087)	\$ (10,032)

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

Notes to the Consolidated Financial Statements

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2002 and 2001
(Dollars in Thousands)

Note 1. Summary of Significant Accounting Policies

Reporting Entity

Created by Congress in 1996 as one of six Franchise Fund pilots operating within the Executive Branch of Government, VA's Franchise Fund (Fund) supports VA's mission by supplying common administrative services at competitive prices. By law, the business lines within the Fund can only sell to federal entities. This organization accounted for its funds in six lines of business (VA Enterprise Centers) and in one administrative organization: Austin Automation Center, Debt Management Center, Financial Services Center, Law Enforcement Training Center, Security and Investigations Center, VA Records Center and Vault and the Enterprise Fund Office.

Basis of Accounting

The accompanying consolidated financial statements have been prepared in accordance with Federal Accounting Standards Advisory Board (FASAB) standards and related concepts. The American Institute of Certified Public Accountants (AICPA) designated FASAB as the accounting standard-setting body for federal governmental entities. As a result, accounting principles promulgated by FASAB are considered accounting principles generally accepted (GAAP) in the United States of America for federal governmental entities.

Principles of Consolidation

The consolidated financial statements include the six individual activity centers of the Fund. All material intrafund transactions have been eliminated.

Accounts Receivable

Intragovernmental accounts receivable are from other federal entities and are considered fully collectible; therefore, no allowance for uncollectible accounts is necessary.

Public accounts receivable are incurred when the Fund makes payments on behalf of their employees. Examples of this would be advances for Permanent Change of Station (PCS) travel or advances for Federal Employees Health Benefits (FEHB) when employees are on leave without pay and their health benefits are paid to the health carriers. These receivables are considered fully collectible; therefore, no allowance for uncollectible accounts is necessary.

Other Liabilities

Other liabilities are classified as either intragovernmental or public. Intragovernmental liabilities arise from transactions between the Fund and federal entities, whereas public liabilities arise from transactions between the Fund and non-federal entities. Budgetary resources cover all other liabilities, both intragovernmental and public.

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2002 and 2001
(Dollars in Thousands)

Revenues and Financing Sources

The Fund receives an annual apportionment that allows it to incur obligations and to recognize revenue from its customers on a “fee-for-service” basis. Exchange revenues are recognized when earned. Expenses are recognized when incurred. All significant intra-entity balances and transactions have been eliminated in consolidation.

For financial reporting purposes under accrual accounting, operating expenses are recognized currently, while those for capital and other long-term assets are capitalized and not recognized as expenses until actually used. Financing sources for these expenses, which derive from both current and prior year appropriations and operations, are also recognized this way.

Annual, Sick and Other Types of Leave

Annual leave is accrued when earned and the accrual is reduced when leave is used. At least once a year, the balance in the accrued annual leave account is adjusted to reflect current pay rates of cumulative annual leave earned but not taken. Sick and other types of leave are expensed as taken.

Imputed Financing

The imputed financing of retirement benefit costs is borne by the Office of Personnel Management to support the retirement of our employees. This cost is not included within the billing rates charged to customers.

Note 2. Fund Balance with Treasury

The undisbursed account balance for the Fund is a revolving fund comprised of only entity assets. The funds available as of September 30,

	<u>2002</u>	<u>2001</u>
Fund Balance with Treasury	\$73,092	\$52,055

Notes to the Consolidated Financial Statements

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 FOR THE YEARS ENDED SEPTEMBER 30, 2002 and 2001
 (Dollars in Thousands)

The Fund does not receive an appropriation from Congress. The Fund receives an annual apportionment that allows it to incur obligations and to recognize revenue from its customers on a “fee-for-service” basis.

	<u>2002</u>	<u>2001</u>
Unobligated Apportionment		
Available	\$50,887	\$36,221
Unavailable	1,795	1,795
Undelivered Orders		
Unpaid	2,628	4,338
Total Unexpended Apportionment	<u>\$55,310</u>	<u>\$42,354</u>

Note 3. Property, Plant and Equipment

Property, plant and equipment, including transfers from other federal agencies, are recorded at cost. Expenditures for major additions, replacements, and alterations are capitalized. Routine maintenance is expensed when incurred. Items costing over \$5,000 with a useful life of 2 years or more are capitalized. All capitalized purchases are depreciated using the straight-line method over the estimated useful life, usually 3 to 5 years.

Leasehold Improvements and related depreciation are accounted for as Departmental assets. The Franchise Fund utilizes these assets in the production of revenue. Since the leasehold improvements are VA assets, they are recorded at the VA Departmental threshold of \$100,000.

The Property, Plant and Equipment for the Franchise Fund as of September 30,

	Cost	Accumulated Depreciation	2002 Net Book Value	2001 Net Book Value
Furniture & Equipment	\$ 2,557	\$ (1,053)	\$ 1,504	\$ 1,495
Capital Leases	7,921	(7,758)	163	3,010
ADP Equipment	22,096	(8,750)	13,346	7,270
Software	9,660	(6,014)	3,646	4,073
Leasehold Improvements	15,912	(6,060)	9,852	9,359
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Property, Plant and Equipment	<u>\$ 58,146</u>	<u>\$ (29,635)</u>	<u>\$ 28,511</u>	<u>\$ 25,207</u>

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 FOR THE YEARS ENDED SEPTEMBER 30, 2002 and 2001
 (Dollars in Thousands)

Note 4. Leases

The Franchise Fund has both capital and operating leases. The capital lease liability is \$163,000 and \$3,010,000 as of September 30, 2002 and 2001, respectively. Due to the number of operating leases, the future commitment for operating leases is not known. The Franchise Fund's FY 2002 operating lease costs were \$612,000 for real property rentals and \$21,000 for equipment rentals. The FY 2001 operating lease costs consisted of \$117,000 for real property rentals and \$34,000 for equipment rentals. The following chart represents the Franchise Fund's estimate for operating lease costs in thousands for the next 5 years, assuming a range of 3.4 to 3.6 percent yearly increase in cost.

OPERATING LEASES

Year	Percentage Increase	Real Property	Equipment
2003	3.5	\$634	\$22
2004	3.4	655	22
2005	3.5	678	23
2006	3.6	703	24
2007	3.6	728	25

Note 5. Other Liabilities

Budgetary resources fund all other liabilities, both intragovernmental and public.

	<u>2002</u>	<u>2001</u>
Intragovernmental		
Accrued Payables - Federal	\$ 515	\$ 1,480
Advances – Federal	868	190
Total Intragovernmental Liabilities	<u><u>\$ 1,383</u></u>	<u><u>\$ 1,670</u></u>
Public		
Accrued Payables	\$23,952	\$17,621
Accrued Salaries & Wages	1,171	1,708
Accrued Funded Annual Leave	3,175	2,936
Capital Lease Liability	163	3,010
Total Public Liabilities	<u><u>\$ 28,461</u></u>	<u><u>\$ 25,275</u></u>

Notes to the Consolidated Financial Statements

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2002 and 2001
(Dollars in Thousands)

Note 6. Changes in Accounting Principles

The capitalization threshold for VA Departmental fixed assets was raised from \$25,000 to \$100,000 effective June 1, 2002. The capitalization threshold for the Fund's assets remained at \$5,000, except for leasehold improvements, which are capitalized at the Departmental level. The capitalization threshold for the Fund's leasehold improvements was also increased to \$100,000 effective June 1, 2002.

A line item titled "Cumulative Effect of Change in Accounting Principle" has been included on the Statement of Changes in Net Position to report the \$370,000 reduction in property, plant and equipment book value for FY 2002 and a \$1,000 reduction in property, plant and equipment book value for FY 2001.

Note 7. Subsequent Events

The capitalization threshold for the Fund fixed assets was raised from \$5,000 to \$100,000 effective October 1, 2002.

Note 8. Restatement of Fiscal Year 2001

The accompanying 2001 consolidated financial statements have been restated to reflect the recording and classification of capital leases that were incorrectly recorded as operating leases. The effect of the restatement was to increase both property, plant, and equipment and public liabilities by \$3,010.

	2001	2001 Restated	Variance
Consolidated Balance Sheets			
Property, Plant & Equipment	22,197	25,207	3,010
Total Assets	89,599	92,609	3,010
Other Liabilities	22,265	25,275	3,010
Total Liabilities	28,008	31,018	3,010
Total Net Position	61,591	61,591	0
Total Liabilities & Net Position	89,599	92,609	3,010
Consolidated Statements of Net Cost			
No Change			
Consolidated Statements of Changes in Net Position			
No Change			
Combined Statements of Budgetary Resources			
No Change			
Consolidated Statements of Financing			
Resources Used to Finance Items Not Part of the Net Cost of Operations			
Property, Plant & Equipment	(7,336)	(15,257)	(7,921)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	11,901	3,980	(7,921)
Total Resources Used to Finance the Net Cost of Operations	15,773	23,694	7,921
Components Not Requiring or Generating Resources			
Depreciation & Amortization	4,987	9,898	4,911
Other	12	3,022	3,010
Total Components Not Requiring or Generating Resources	5,741	13,662	7,921