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

	2003	2002
ASSETS		
Intragovernmental		
Fund Balance with Treasury (Note 2)	$ 90,392	$ 73,092
Accounts Receivable	28,328	13,952
Other Assets	6,642	4,416
Total Intragovernmental	125,362	91,460
Accounts Receivable	41	284
Property, Plant and Equipment, Net (Note 3)	24,389	28,511
Other Assets	97	2
Total Assets	**$ 149,889**	**$ 120,257**
LIABILITIES		
Intragovernmental Liabilities		
Accounts Payable	$ 243	$ 357
Other Liabilities (Note 5)	9,722	1,383
Total Intragovernmental	9,965	1,740
Accounts Payable	7,495	2,563
Other Liabilities (Notes 4 & 5)	24,533	28,461
Total Liabilities	**41,993**	**32,764**
NET POSITION	**$ 107,896**	**$ 87,493**
TOTAL LIABILITIES AND NET POSITION	**$ 149,889**	**$ 120,257**

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

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

	2003	2002
PROGRAM COSTS		
Gross Costs Intragovernmental	$ 36,634	$ 22,751
Less: Intragovernmental Earned Revenue	(202,475)	(136,856)
Intragovernmental Net Costs	(165,841)	(114,105)
Gross Costs Public	147,757	92,018
NET COST OF OPERATIONS	**$ (18,084)**	**$ (22,087)**

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

	2003	2002
NET POSITION		
Beginning Balance	**$ 87,493**	**$ 61,591**
OTHER FINANCING SOURCES:		
Transfers-In	1,199	759
Imputed Financing	3,783	3,426
Total Financing Sources	**4,982**	**4,185**
NET COST OF OPERATIONS	18,084	22,087
Cumulative Effect of Change in Accounting Principle (Note 6)	(2,663)	(370)
TOTAL NET POSITION	**$ 107,896**	**$ 87,493**

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

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

	2003	2002
BUDGETARY RESOURCES		
Unobligated Balance at the Beginning of the Period	$ 52,682	$ 38,016
Spending Authority from Offsetting Collections	214,353	144,987
Total Budgetary Resources	**267,035**	**183,003**
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred	194,179	130,321
Unobligated Balance Available (Note 2)	54,414	50,887
Unobligated Balance Not Available (Note 2)	18,442	1,795
Total Status of Budgetary Resources	**267,035**	**183,003**
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Obligated Balance, Net - Beginning of the Period	20,410	14,039
Less: Obligated Balance, Net - End of the Period		
Accounts Receivable	(28,328)	(13,911)
Undelivered Orders (Note 2)	4,865	2,628
Accounts Payable	40,999	31,693
Outlays:		
Disbursements	182,637	128,175
Collections	(199,937)	(149,212)
Net Outlays	**$ (17,300)**	**$ (21,037)**

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

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

	2003	2002
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated		
Obligations Incurred	$ 194,179	$ 130,321
Less: Spending Authority from Offsetting Collections and Adjustments	(214,353)	(144,987)
Net Obligations	**(20,174)**	**(14,666)**
Other Resources		
Transfers-In	1,199	759
Financing Imputed for Cost Subsidies	3,783	3,426
Net Other Resources Used to Finance Activities	**4,982**	**4,185**
Total Resources Used to Finance Activities	**(15,192)**	**(10,481)**
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	(4,674)	(4,953)
Resources that Finance the Acquisition of Assets Property, Plant and Equipment	(5,780)	(16,575)
Resources that Fund Expenses Recognized in Prior Periods	244	(227)
Total Resources Used to Finance Items Not Part of Net Cost of Operations	**(10,210)**	**(21,755)**
Total Resources Used to Finance the Net Cost of Operations	**(25,402)**	**(32,236)**
COMPONENTS NOT REQUIRING OR GENERATING RESOURCES		
Depreciation and Amortization	10,152	9,700
Gain/Loss on Disposition of Assets	(251)	191
Other	(2,583)	258
	7,318	**10,149**
NET COST OF OPERATIONS	**$ (18,084)**	**$ (22,087)**

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002
(DOLLARS IN THOUSANDS)

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

Created by Congress in 1996, as one of six Franchise Fund pilots operating within the Executive Branch of Government, the Department of Veterans Affairs' (VA) Franchise 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 activity centers (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. The consolidated financial statements include the six individual activity centers of the Fund. All material intrafund transactions have been eliminated.

B. Basis of Presentation

The VA Franchise Fund consolidated financial statements report all activities of Franchise Fund components. The consolidated financial statements differ from the financial reports used to monitor and control budgetary resources, but are prepared from the same books and records. The statements should be read with the understanding that the VA Franchise Fund is a component unit of the U.S. Government. The Franchise Fund's fiscal year (FY) 2003 and 2002 financial statements are presented in conformity with the Office of Management and Budget's (OMB) Bulletin 01-09, "Form and Content of Agency Financial Statements," as amended.

C. 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 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 in the United States of America for Federal governmental entities.

D. Fund Balance with Treasury

The Department of the Treasury (Treasury) performs cash management activities for all Federal Government agencies. The Fund Balance with Treasury represents the right of the VA Franchise Fund to draw on the Treasury for allowable expenditures.

E. 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 travel or advances for Federal Employees Health Benefits 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.

F. Property, Plant and Equipment

The majority of the general Property, Plant and Equipment (PP&E) is used to provide common administrative services to the VA and other federal entities and is valued at cost, including transfers from other federal agencies. Major additions, replacements, and alterations are capitalized, whereas routine maintenance is expensed when incurred. Individual items are capitalized if the useful life is 2 years or more and the unit price is $100,000 or greater. Equipment is depreciated on a straight-line basis over its useful life, usually 3 to 5 years. There are no restrictions on the use or convertibility of general PP&E.

G. 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.

H. 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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002
(DOLLARS IN THOUSANDS)

for these expenses, which derive from both current and prior year appropriations and operations, are also recognized this way.

I. 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.

J. 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.

K. Litigation

VA is a party in various administrative proceedings, legal actions, and claims brought against it. In the opinion of VA Franchise Fund management and legal counsel, the ultimate resolutions of these proceedings, actions, and claims will not materially affect the financial position or results of VA Franchise Fund operations.

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002
(DOLLARS IN THOUSANDS)

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,

	2003	2002
Fund Balance with Treasury	**$ 90,392**	**$ 73,092**

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.

	2003	2002
Unobligated Apportionment		
Available	$ 54,414	$ 50,887
Unavailable	18,442	1,795
Undelivered Orders		
Unpaid	4,865	2,628
Total Unexpended Apportionment	**$ 77,721**	**$ 55,310**

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002
(DOLLARS IN THOUSANDS)

Note 3. Property, Plant and Equipment

PP&E, 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 $100,000 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 Departmental threshold of $100,000.

PP&E As of September 30, 2003:

	Acquisition Cost	Accumulated Depreciation	Net Book Value
Furniture & Equipment	$ 1,503	$ (725)	$ 778
Capital Leases	7,921	(7,921)	–
ADP Equipment	20,296	(8,830)	11,466
Software	8,196	(6,088)	2,108
Leasehold Improvements	17,540	(7,503)	10,037
Total PP&E	**$ 55,456**	**$ (31,067)**	**$ 24,389**

PP&E As of September 30, 2002:

	Acquisition Cost	Accumulated Depreciation	Net Book Value
Furniture & Equipment	$ 2,557	$ (1,053)	$ 1,504
Capital Leases	7,921	(7,758)	163
ADP Equipment	22,096	(8,750)	13,346
Software	9,660	(6,014)	3,646
Leasehold Improvements	15,912	(6,060)	9,852
Total PP&E	**$ 58,146**	**$ (29,635)**	**$ 28,511**

(DOLLARS IN THOUSANDS)

Note 4. Leases

The Franchise Fund has both capital and operating leases. The capital lease liability is $0 and $163,000 as of September 30, 2003 and 2002, respectively. Due to the number of operating leases, the future commitment for operating leases is not known. The Franchise Fund's FY 2003 operating lease costs were $713,934 for real property rentals and $40,967 for equipment rentals. The FY 2002 operating lease costs consisted of $612,000 for real property rentals and $21,000 for equipment rentals. The following chart represents the Franchise Fund's estimate for operating lease costs for the next 5 years, assuming a range of 2.5 to 2.9 percent annual increase in cost.

OPERATING LEASES			
Fiscal Year	Percentage Increase	Real Property	Equipment
2004	2.5	$ 732	$ 42
2005	2.6	751	43
2006	2.7	771	44
2007	2.8	793	45
2008	2.9	816	47

Note 5. Other Liabilities

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

	2003	2002
Intragovernmental		
Accrued Payables - Federal	$ 8,972	$ 515
Advances – Federal	750	868
Total Intragovernmental Liabilities	**$ 9,722**	**$ 1,383**
Public		
Accrued Payables	$ 19,783	$ 23,952
Accrued Salaries & Wages	1,400	1,171
Accrued Funded Annual Leave	3,350	3,175
Capital Lease Liability (see Note 4)	–	163
Total Public Liabilities	**$ 24,533**	**$ 28,461**

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED SEPTEMBER 30, 2003 AND 2002
(DOLLARS IN THOUSANDS)

Note 6. Changes in Accounting Principles

The capitalization threshold for Departmental fixed assets was raised from $25,000 to $100,000 effective June 1, 2002. During FY 2002, the capitalization threshold for the Fund's fixed assets remained at $5,000, except for leasehold improvements, which were capitalized at the Departmental level. The capitalization threshold for the Fund's fixed assets was raised from $5,000 to $100,000 effective October 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 PP&E book value for the Fund's leasehold improvements for FY 2002 and the $2,663,000 reduction in PP&E book value for the Fund's fixed assets for FY 2003.