

November 1988

# FINANCIAL AUDIT

## Veterans Administration's Financial Statements for Fiscal Years 1987 and 1986



Comptroller General  
of the United States

B-226801

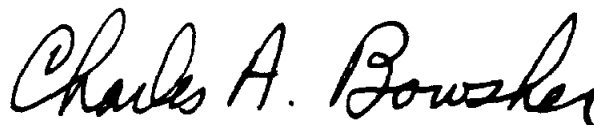
November 30, 1988

To the President of the Senate and the  
Speaker of the House of Representatives

This report presents the results of our examination of the Veterans Administration's (VA) consolidated financial statements for fiscal years 1987 and 1986. Our report describes restrictions on the scope of our examination for fiscal year 1986, which limited our opinion on that year's financial statements to VA's consolidated statement of financial position. The opinion for both fiscal years is qualified for the unknown effect of any adjustments that might have been necessary had we been able to satisfy ourselves that VA's real property and equipment accounts were presented fairly. Our opinion for both fiscal years is also qualified because the consolidated statement of financial position reflects a \$3-billion overstatement in the life insurance reserves due to the use of statutory actuarial assumptions rather than more realistic assumptions permitted by generally accepted accounting principles.

The report contains separate reports on VA's system of internal accounting controls and on its compliance with laws and regulations. VA's real property accounts and automated data processing functions have internal accounting control weaknesses that need to be improved. Our compliance with laws and regulations report discloses that VA violated the debt collection provisions of the Veterans' Rehabilitation and Education Act Amendments of 1980 (38 U.S.C. 3115) and that it did not fully comply with the Prompt Payment Act (31 U.S.C. 3901-3906).

We are sending copies of this report to the Chairman, Senate Committee on Veterans' Affairs; the Chairman, House Committee on Veterans' Affairs; the Director, Office of Management and Budget; the Secretary of the Treasury; and the Administrator of Veterans Affairs.



Charles A. Bowsher  
Comptroller General  
of the United States

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auditing procedures as to the net aggregate book value of these older assets. Furthermore, although equipment records are maintained in an automated system, accounting records of land and buildings are kept manually, are not always subject to centralized or uniform accounting controls, and, at the VA sites visited during our examination, contain a high degree of error in recorded values. Accordingly, as in our 1986 audit, we determined that it was not practical to perform, nor did we perform, sufficient alternative auditing procedures to remove our qualification relating to the presentation of these assets.

The accompanying financial statements reflect statutorily calculated insurance reserves totaling \$11.6 and \$11.4 billion for fiscal years 1987 and 1986, respectively (see note 6). These reserves, which cover policy benefits relating to five VA life insurance programs, were established under federal statutes which prescribed conservative investment yields and mortality assumptions. Under generally accepted accounting principles for federal agencies, more realistic interest earnings projections and actual mortality experiences are used for calculating such reserves. Insurance policy reserves, calculated using interest rates ranging from 7 to 8.5 percent and mortality assumptions which are based on actual program experience, would amount to approximately \$8.6 and \$8.3 billion for fiscal years 1987 and 1986, respectively. Thus, using the statutory assumptions has resulted in an excess accumulation of about \$3 billion more than needed to ultimately cover present policy benefits. Any excess fund accumulations inure, based on statutory requirements, to policyholders and will ultimately be distributed to them as dividends and other benefit enhancements. Nevertheless, the use of statutory assumptions does not materially affect operating expenses for fiscal year 1987. VA did not compute the difference in operating expenses that would have resulted from using statutory assumptions for fiscal year 1986.

As discussed in note 5, the financial condition of certain sectors of the economy, particularly the energy and agricultural sectors, adversely affected the home mortgage industry's performance during 1987. The rate of housing foreclosures for VA has increased substantially since 1986. For example, the average foreclosure rate on VA guaranteed home loans increased from 16.8 percent in fiscal year 1986 to 19.6 percent in fiscal year 1987. While VA expects this trend to reverse itself in 1988, other mortgage industry experts expect the trend to continue. At the same time, the number of VA guaranteed loans has also increased. This greatly increases VA's exposure to losses in its loan guaranty revolving fund because the revolving fund's fees are not intended to fully cover

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assurance that (1) obligations and costs are in compliance with applicable laws, (2) funds, property, and other assets are safeguarded against waste, loss, and unauthorized use or misappropriation, and (3) assets, liabilities, revenues, and expenditures applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over assets. Because of inherent limitations in any system of internal accounting controls, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

VA evaluated its system of internal accounting and administrative controls in accordance with the Federal Managers' Financial Integrity Act of 1982. In its Financial Integrity Act report for fiscal year 1987, dated December 31, 1987, VA reported that its systems of internal accounting and administrative controls, taken as a whole, provided reasonable assurance that the required control requirements were being complied with. We reviewed VA's report and considered its statements in conducting our study and evaluation in determining the nature, timing, and extent of audit tests.

Our study and evaluation, made for the limited purpose described in the second paragraph, would not necessarily disclose all material weaknesses in the system of internal accounting controls. Accordingly, we do not express an opinion on VA's system of internal accounting controls taken as a whole or on any of the categories of controls identified in the second paragraph. However, our study and evaluation disclosed two conditions which we believe pose a high degree of risk that material errors or irregularities could occur and not be promptly detected. The first condition involves VA's buildings and related depreciation accounts. The second condition involves controls over data processing activities. Although our audit procedures did not disclose any significant errors resulting from deficient automated data processing controls, we believe the condition poses a sufficiently high degree of risk to warrant management's immediate attention.

In our report on our fiscal year 1986 study and evaluation of internal accounting controls, made as a part of our examination of VA's consolidated financial statements (GAO/AFMD-87-38, dated July 29, 1987), we disclosed a condition which we believed would adversely affect VA's ability to record, process, and report financial data. We determined the need for

involves both early and late capitalization of costs from construction work-in-process. We noted cases where amounts were transferred from work-in-process when the applicable construction was less than 50 percent complete. In other cases, buildings were already in use prior to September 30, 1987, but remained in VA's work-in-process account.

- Failure to calculate depreciation in accordance with VA's policy. This occurred at 13 of the 28 medical centers we visited during our fiscal year 1987 examination. Problems included (1) failing to include all buildings and structures in depreciation calculations, (2) depreciating beyond the cost of the property, and (3) various mathematical errors.

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## ADP Controls Need Strengthening

Federal Information Resource Management Regulations and Office of Management and Budget (OMB) policies charge agencies with maintaining adequate controls to ensure that data is safeguarded and that systems are reliable. Our review of VA's automated data processing (ADP) internal controls disclosed weaknesses in VA's software maintenance and data integrity controls at all three data processing centers (Austin, Texas; Hines, Illinois; and Philadelphia, Pennsylvania). We also found processing problems in the compensation and pension system and errors in specific payroll and loan guaranty programs. Furthermore, certain manual compensating controls that are separate from the ADP function, such as reconciliations between systems or between control and subsidiary accounts, were not adequate in several areas.

These weaknesses individually are not material in relation to VA's consolidated financial statements; taken collectively, however, they pose a high degree of risk that data errors or incorrect processing could occur which could affect both account balances and financial reports and not be detected. In addition, many of VA's financial systems are outdated, inadequately documented, and difficult to maintain. Several are scheduled to be modernized. Although VA's ADP weaknesses pose a high degree of risk, our testing of accounting records and other auditing procedures did not disclose any errors material to the financial statements taken as a whole for fiscal years 1987 and 1986.

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## Software Maintenance

The software maintenance process is critical to ensuring that ADP systems continue to work as intended and are responsive to changing user requirements. There are two types of computer software: (1) system software, which performs generalized functions for more than one application (such as programs that control user access) and (2) application software, which is specific to an individual process (such as payroll). We

- have unrestricted access to all the system's production data, and the restrictions on access to application software can be easily bypassed.
- Even though they may not be assigned responsibility for a particular system or component, system software programmers at the Austin DPC have complete access to production data, which includes payroll, personnel, financial, and loan information. For example, at our request, a system programmer accessed the payroll production file which contains pay information for all VA employees.

OMB circular A-123 states that access to resources and records should be limited to authorized individuals, and federal computer security guidelines indicate that authorization should be limited to individuals who require such data for their jobs. Because changes made by a system programmer have less chance of being discovered than changes made by other data processing personnel, they can do more damage. As a result, it is particularly critical that controls over system software programs exist.

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### Processing Problems and Program Errors

Computer applications should be able to substantiate transaction processing, including the capability to reconstruct control totals. At the Hines and Austin DPCs, we found processing problems in the compensation and pension system and errors in specific payroll and loan guaranty software programs. Some examples follow.

- We noted two processing problems in the compensation and pension system. First, VA's computer-generated control reports, designed to control data through the master record updating process, are not reconciled. For example, in a 2-month period, one such control report, which compares the change in compensation and pension master records to the net effect of the processing cycle, showed an unexplained difference of 30 percent. VA views this as a control problem rather than a processing problem. Second, transaction counts are not tracked throughout the data processing cycle to ensure complete and accurate processing.
- As a result of a programming error detected in determining VA's fiscal year 1987 unfunded annual leave liability, the agency's fiscal year 1986 financial statements were restated to decrease the previously reported leave liability by \$63 million.

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### Inadequate Compensating Controls

Generally accepted accounting control mechanisms in the accounting process could partially mitigate the ADP control weaknesses. Such controls, which are intended to aid in substantiating and maintaining the



statements, but, more importantly, to also provide accurate data for use by agency decisionmakers to better manage VA programs.

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## Recommendations

We recommend that the Administrator of Veterans Affairs:

- Direct the Controller and the Director of Facilities to develop an automated property management accounting system which includes improved internal controls over transactions affecting property and related accounts. The improvements should include:
  - (1) issuing additional guidance to medical centers on identifying the operational fund expenditures that should be capitalized,
  - (2) revising capitalization procedures to identify responsibilities of individuals involved in making capitalization decisions and to ensure that costs are capitalized when buildings or capital improvements are placed in use, and
  - (3) implementing internal controls to ensure that medical centers accurately calculate depreciation on buildings and other structures.
- Direct the Office of Information Systems and Telecommunications and the Department of Veterans Benefits to improve the automated data processing controls in their respective areas at each of VA's three data processing centers. These corrective actions should include (1) implementing effective manual or automated documented reviews of software program code changes for sensitive applications and (2) incorporating software maintenance and data integrity controls, such as establishing independent audit test files at the Austin Data Processing Center.
- Reiterate to department directors the need to follow all internal accounting control procedures and to adhere to VA policies, with particular emphasis on performing and finalizing reconciliations of account balances.

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## Other Opportunities for Improvement

During the course of our examination, we identified a number of other weaknesses in ADP and internal accounting controls and procedures which, although not as significant as those discussed in this report, nonetheless merit corrective action to strengthen the controls. Accordingly, we are reporting them separately to the Administrator of Veterans Affairs.

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# Report on Compliance With Laws and Regulations

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We have examined the consolidated financial statements of the Veterans Administration (VA) for the fiscal year ended September 30, 1987, and have issued our opinion thereon. Our examination was made in accordance with generally accepted government auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures, including tests of compliance with laws and regulations, as we considered necessary in the circumstances.

This report pertains only to our review of compliance with laws and regulations for the fiscal year ended September 30, 1987. Our report on compliance with laws and regulations for the fiscal year ended September 30, 1986, is presented in GAO/AFMD-87-38, dated July 29, 1987. The conditions noted therein were considered in determining the nature and scope of the procedures performed for our 1987 review.

Our review of compliance with laws and regulations, made for the limited purpose described in the preceding paragraphs, does not necessarily cover all laws and regulations that VA is required to comply with. Accordingly, we are expressing an opinion only with respect to those transactions tested. In our opinion, VA complied with the terms and provisions of laws and regulations for the transactions tested that could have materially affected its consolidated financial statements; however, we found instances of noncompliance for which we recommend VA take corrective action.

Our report on compliance with laws and regulations in fiscal year 1986 disclosed two cases of noncompliance with certain laws and identified two actions by VA which presented compliance issues requiring further analysis. These were

- (1) violations of the Veterans' Rehabilitation and Education Amendments of 1980;
- (2) violations of the Prompt Payment Act;
- (3) applicability of section 11 of the Debt Collection Act of 1982 to VA; and
- (4) VA's treatment of October 1, 1986, veterans' benefits entitlement payments.

## Violations of the Veterans' Rehabilitation and Education Act Amendments of 1980

The Veterans' Rehabilitation and Education Amendments of 1980 (Public Law 94-466, now codified as 38 U.S.C. 3115) specify interest and administrative costs to be charged to VA's delinquent debtors. The law requires that interest on delinquent debt be accrued based on the Department of the Treasury's rate, which, as of September 30, 1987 and 1986, was 7 and 8 percent, respectively. However, during both fiscal year 1987 and fiscal year 1986, VA did not fully comply with this provision because it did not assess interest and administrative costs on certain debts generated by its compensation and pension programs. These debts principally relate to overpayment of compensation and pension benefits for which VA is seeking reimbursement. Also, VA continued to charge interest at 4 percent annually on its loan guaranty accounts receivable rather than the current interest rate required by the 1980 amendments to the act.

In his comments to the Chairman, Senate Committee on Governmental Affairs, on our fiscal year 1986 compliance report, the Administrator of Veterans Affairs expressed concern as to the potential effects of charging interest and administrative costs to low-income compensation and pension recipients and the need to "review practical alternatives in collecting the overpayments." VA maintains it is seeking legislation to exempt compensation and pension receivables from interest charges. However, there has not been any legislative action. If VA does not receive legal authority to exempt compensation and pension receivables from interest charges, extensive computer programming will be needed to implement necessary automated system changes for applying the charges.

The Administrator's reference to the need for reviewing practical alternatives in collecting these particular compensation and pension benefits overpayments relates to the problems VA is experiencing in recovering the overpayments. According to VA, most of these particular debtors are pension recipients whose changes in income or dependency status have terminated their entitlements to payments. The Administrator recognizes that it is reasonable to request payment of interest and administrative costs on erroneous payments. However, he realizes the problems involved in recovering funds from individuals at or near the poverty income level and is concerned with the potential effects of adding interest and administrative costs to the receivables. But, he has not exercised his authority under 38 U.S.C. 3102 to waive interest and administrative costs in cases where recovery would be against equity and good conscience.

In its fiscal year 1987 Prompt Payment Act report, VA reported that it paid approximately \$454,000 in interest penalties on payments made after the grace period. VA also reported that it did not pay an estimated \$431,000 in interest penalties that were due. The interest penalties that were not paid primarily related to certain invoices that are still processed manually as opposed to ones processed through VA's computer invoice payment system. Our testing of 202 payments VA made during fiscal year 1987 disclosed approximately the same late payment percentage as VA reported.

## Conclusions

VA did not comply with applicable laws and regulations in two areas: assessment of penalties and interest and vendor invoice payment timing. These problems were also identified in our 1986 examination.

During fiscal year 1987, VA continued its practice of not charging interest and administrative costs on certain debts generated by its compensation and pension programs. However, the Veterans' Rehabilitation and Education Act Amendments of 1980 require VA to charge current interest rates, which were 7 and 8 percent as of September 30, 1987 and 1986, respectively. VA maintains that it is seeking legislation to relieve it of responsibility for assessing penalties and interest on accounts receivable associated with its compensation and pension programs. VA believes that assessing interest on these types of debts should not be required because the majority of the debtors are living near the poverty level. It is experiencing problems in collecting the basic overpayments that comprise these receivables and is concerned with the potential effects of adding the interest and administrative costs to these cases. Under section 3102 of title 38 of the United States Code, VA is also allowed to waive interest and administrative costs if recovery is deemed to be against equity and good conscience.

Although VA does charge interest on its loan guaranty accounts receivable, the interest rate charged is lower than the rate required by the 1980 amendments to the act. VA agrees that it should be charging the higher interest rate. However, VA maintains that because of the extensive computer software programming required to implement this project and because of competing computer software needs, it will be unable to do so until 1991.

VA also needs to improve its cash vendor invoice payment procedures for certain purchases to comply with the Prompt Payment Act and its implementing regulations. During fiscal year 1987, VA paid about

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Prompt Payment Act area to convert more of its manually processed invoice payments to its computer assisted invoice payment system.

**Financial Statements**

**Consolidated Statement of Operations**

FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 1987 AND 1986

(Dollars in Thousands)

	1987	(Restated) (Unaudited) 1986
<b>OPERATING EXPENSES AND DIVIDENDS:</b>		
Expenses by Category:		
Personnel Compensation and Fringe Benefits	\$ 6,982,792	\$ 6,641,146
Veterans Benefits	15,630,956	15,673,194
Claims and Indemnities	3,272,296	2,206,460
Depreciation	363,477	337,997
Supplies and Materials	1,622,952	1,537,771
Contractual Services	1,320,649	1,180,408
Rent, Communications, and Utilities	516,267	503,446
Other	262,591	335,455
<b>Total Operating Expenses</b>	<b>29,971,980</b>	<b>28,415,877</b>
Provisions for Dividends to Policyholders	928,845	907,170
Provisions for Servicemen's Group Life Insurance Reserve	9,027	9,533
	<b>\$30,909,852</b>	<b>\$29,332,580</b>
<b>OPERATING REVENUE AND FINANCING SOURCES:</b>		
Operating Revenues:		
Premium Income	\$ 877,756	\$ 848,402
Interest Income	1,383,742	1,350,391
Loan Origination fees	340,972	258,111
Reimbursements and Other	395,015	277,456
<b>Total Operating Revenue</b>	<b>2,997,485</b>	<b>2,734,360</b>
Financing by Source:		
Appropriations and Financing Sources Realized	26,560,145	25,633,985
Funds to be Provided by Future Appropriations	1,119,116	640,360
Transfers, Reimbursements, and Other	233,106	323,875
<b>Total Financing Sources</b>	<b>27,912,367</b>	<b>26,958,220</b>
	<b>\$30,909,852</b>	<b>\$29,332,580</b>

The accompanying notes are an integral part of this statement.  
Note 11 includes financial information by major program area.

## Financial Statements

### Notes to the Financial Statements

#### NOTE 1: SIGNIFICANT ACCOUNTING POLICIES

##### Entity and Basis of Consolidation

In fulfilling its mission to provide veterans with care, support, and recognition, the Veterans Administration maintains 15 general funds, 10 revolving funds, 5 trust funds, and 10 other funds. The financial activities of these funds have been classified into the following functional areas: Medical and Construction; Veterans Benefits (compensation, pension, education, and other benefits); Housing Credit Assistance; Life Insurance; and Administration. Some of the trust and revolving fund activities for the insurance and housing credit assistance programs are augmented by budget appropriations.

The consolidated financial statements account for all funds for which the VA is responsible and are presented on the accrual basis of accounting as required by the GAO policy and procedures manual for guidance of Federal agencies (Title 2). All significant intra-agency balances and transactions have been eliminated in consolidation.

##### Recognition of Financing Sources

The current congressional budgetary process under which VA operates does not distinguish between capital and operating expenditures. For budgetary purposes, both are recognized as a use of budgetary resources (outlays) as paid. For financial reporting purposes under accrual accounting, however, operating expenses are recognized currently while expenditures for capital and other long-term assets are capitalized and are not recognized as expenses until they are consumed in the VA's operations. Financing sources for these expenses, which derive both from current and prior year appropriations and operations, are recognized on this same basis. The consolidated statement of changes in financial position and reconciliation to budget presents a reconciliation of operating expenses on an accrual basis with budgetary expenditures.

For certain accrued expenses (e.g., annual leave earned but not taken, insurance premiums for disabled veterans funded by appropriations, and losses on guaranteed loans), current or prior year appropriations are not available to fund the expenses. However, such expenses are customarily financed (funds appropriated, or for a portion of the loan losses, revenues received) in the year payment is required. An amount due from future financing sources is therefore recognized in operations each year for the year's accrued amount of such expenses. The cumulative amount of these accruals is reflected on the consolidated statement of financial position as an asset, future financing sources. The total amount of the future financing sources account is also reflected in the liability section of this statement as part of various liability accounts.

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## Financial Statements

Estimated losses on anticipated defaults of guaranteed loans are recorded as expenses, and a reserve is established at the time loans are guaranteed. This reserve represents the estimated cost of defaults for those guaranteed loans which will, based on prior default experience, default in the future. A portion of this reserve is subsequently reclassified as a reduction to direct home loans receivable when such loans are issued (see NOTE 8) and as a reduction of foreclosed property held for sale when property is acquired, in order to record such property at its net realizable value.

### Annual, Sick, and Other Types of Leave

Annual leave is accrued as it is earned, and the accrual is reduced as leave is taken. At least once per 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.

### Insurance Program Liabilities

Insurance program liabilities are recorded for unpaid claims in process, for an experience based estimate of claims incurred but not reported, and for incurred death and permanent disability installment claims. These liabilities are included in accounts payable.

### Dividends Payable

Dividends from the VA's insurance programs are recorded as a liability when declared by the Administrator of Veterans Affairs. Dividends are normally declared when fund balances are in excess of statutorily required insurance claim reserves.

### Trust Fund Balances

Trust fund balances are comprised of the Post-Vietnam Educational Assistance Trust Fund, Insurance Trust funds, and the General Post Fund. These funds are accounted for separately and can be used only for specified purposes. They are not available to fund general purpose governmental activities and thus are excluded from VA's equity accounts.

### Deferred Appropriations

Deferred appropriations include VA's investment in plant, property and equipment, and certain accounts receivable for which outlay authority is not available until collection.

### Workers Compensation

Legal actions brought by employees of the VA for on-the-job injuries fall under the Federal Employees Compensation Act (FECA), administered by the Department of Labor (DOL). DOL bills each agency annually as its claims are paid; however, payment on these bills is deferred two years so they may be funded through the budget process. Using estimates provided by the Department of Labor, VA has recorded FECA liabilities for balances billed to VA by DOL and for an estimate of the present value of the long-term payments related to cases on hand at the end of the fiscal year. An actuarial evaluation of the



**Financial Statements**

offers a savings plan to which VA will automatically contribute 1 percent of pay and then match employee contributions up to an additional 4 percent of basic pay.

Employees participating in FERS are also covered under the Federal Insurance Contributions Act (FICA) for which VA contributes an employer's matching amount to the Social Security Administration.

VA's total contributions for CSRS and FERS participants, including contributions to Social Security, during fiscal year 1987 and fiscal year 1986 were as follows:

	1987	1986
CSRS	\$306,844,931	\$353,345,340
FERS	132,990,446	
FICA	<u>104,309,122</u>	<u>93,015,593</u>
Total VA Contributions	<u>\$544,144,499</u>	<u>\$450,360,933</u>

While VA has no liability for future payments to employees under these programs, the Federal Government is liable for future payments to employees through the various agencies administering the programs.

- o Certain legal matters to which VA may be a named party are administered and, in some instances, litigated and paid by other Federal agencies. These primarily relate to allegations of medical malpractice but also include other tort claims and contract disputes. Generally, amounts (over \$2,500 for Federal Tort Claims Act cases) to be paid under any decision, settlement, or award pertaining to these litigations are funded from a special appropriation called the Judgment Fund that is maintained on deposit with the Department of Treasury. Since VA, except for contract dispute payments, is not required to reimburse the Judgment Fund for payments made on its behalf, the amount of payments from the Fund for VA are not reflected in VA's statements. Amounts paid from the Judgment Fund on behalf of VA were \$30 million and \$33 million in fiscal years 1987 and 1986, respectively. Amounts reimbursed the Judgment Fund by VA for contract dispute payments were not material.

**NOTE 3: RESTATEMENT OF FISCAL YEAR 1986 STATEMENTS**

The fiscal year 1986 consolidated statement of financial position and consolidated statement of operations and changes in financial position and reconciliation to budget have been restated to recognize VA's liability for workers' compensation benefits, to reflect corrections of errors in insurance reserves and accrued annual leave, to reduce accounts receivable from the Department of Defense, and to reclassify items described below. In total these changes have increased assets by \$755 million, liabilities by \$706 million, and equity by \$49 million.

**Financial Statements**

**NOTE 4: FUTURE LIABILITY FOR COMPENSATION AND PENSIONS**

Veterans or their dependents receive compensation benefits if the veteran was disabled or died from military service-connected causes. War veterans or their dependents receive pension benefits if the veteran was disabled or died from non service-connected causes or is age 65 or older. Certain pension benefits are subject to specific income limitations. The compensation and pension benefits for fiscal years 1987 and 1986 were:

<u>Fiscal Year</u>	<u>Compensation</u>	<u>Pension</u>
1987	\$10,513,080,000	\$3,792,945,000
1986	\$10,427,024,000	\$3,850,179,000

The VA has a future liability for benefits expected to be paid in future fiscal years to veterans and, if applicable, their survivors who have met or are expected to meet defined eligibility criteria. The future liability of the compensation and pension programs is not currently funded, nor is there any intent to do so. Rather, payments for benefits that become due in a particular fiscal year are financed from that year's appropriation; in effect, on a pay-as-you-go basis. Payments of the future liability as it becomes due rely on congressional authorization of future tax revenues or other methods, such as public borrowing, for their financing.

The future liability for compensation and pension benefits represents the present value, using a 8.7 percent discount rate, of projected annual benefit payments. Projected benefit payments were based on assumed cost of living increases ranging from 3.1 percent to 5.1 percent for 1988 - 1992 and 2.6 percent to 5.6 percent thereafter. In addition, the mortality and accession rates used were based on trends in the current veteran population.

This calculation was not based on an independent actuarial study, and thus there is a risk that the assumptions and methods underlying it may not be reflective of actual economic and demographic trends affecting veterans.

The present value of the estimated future liability for compensation and pension benefits payable for the next five fiscal years and thereafter is as follows (dollars in thousands):

1988	\$ 13,512,659
1989	12,371,058
1990	11,292,115
1991	10,303,321
1992	9,387,798
Thereafter	<u>79,587,692</u>
TOTAL	<u>\$136,454,643</u>

No liability for compensation and pension benefits has been included in the accompanying consolidated statement of financial position.

## Financial Statements

The reserve balances as of September 30, 1987, and September 30, 1986, are recorded as follows (dollars in thousands):

	<u>1987</u>	<u>1986</u>
Offsets against loans receivable (Note 8)	\$ 133,088	\$ 107,056
Offsets against foreclosed property held for sale	101,616	83,451
Reserve for losses on guaranteed loans	<u>2,718,898</u>	<u>1,735,252</u>
Total reserve balance	<u>\$2,953,602</u>	<u>\$1,925,759</u>
Discount rate	8.7%	9.2%

The discount rate is based on the average interest rate of U.S. interest-bearing debt. The decrease in the interest rate increased the present value of the cost of defaults. However, the increase in the cost of defaults attributable to the change in interest rates is not material.

### Impact of reserve on future appropriations

The projected cost of guaranteed loan defaults will not necessarily reflect the VA's future appropriation requests over the next nine years, since those requests will also include anticipated inflows and outflows of resources for non operating uses such as for transfers, purchases and sales of property, and issuances and repayments of loans, sale of loans, and the receipt of the 1 percent funding fee.

To the extent revolving fund revenues are not sufficient to fund future costs, then financing will have to be obtained from future appropriations or other congressionally approved sources.

### Loan Sales

During fiscal year 1987, VA sold certain of its vendee loans to the public under agreements with recourse provisions for \$890,462,000. Under these agreements, loans sold that subsequently default are repurchased by the VA. Any losses from defaults of repurchased loans are borne by the VA. Estimated losses from defaults of loans sold with recourse are a component of the reserve for losses on guaranteed loans, discussed above.

The VA was to sell certain of its vendee loans to the public without recourse, starting in fiscal year 1987. However, VA has made only one such offering in April 1987, which was not successful because the reduced proceeds the VA would have received were not considered acceptable. In October 1987, legislation was enacted (Public Law 100-136) to sell loans with recourse or at face value or higher if sold without recourse. Subsequent to enactment of this legislation, VA has made three loan sales with recourse. However, all future loan sales are currently planned to be without recourse.

## Financial Statements

Additionally, since the foreclosure rate has greatly increased in these states, VA, other government agencies, and private lenders have accumulated increasing inventories of foreclosed properties. The market to sell these properties is extremely competitive, resulting in overall depressed property values.

### SUBSEQUENT EVENTS

#### Lapse in authority to collect fees

During fiscal year 1988, the enabling legislation authorizing the collection of the loan origination fee lapsed for six weeks. As a result of this lapse in legislation, VA lost an estimated \$30 million in revenues to the loan guaranty revolving fund.

#### Emergency supplemental appropriation request

Presently, the high level of foreclosures resulting in increased cash outlays in property acquisition and claim costs, implementation of policies requiring loan sales without recourse, and the temporary loss of authority to collect loan origination fees have severely strained the revolving fund resources. As reported above, VA will also need to make the final payment of the PCs in August 1988, adding to the financial difficulties of the revolving fund.

Therefore, in January 1988, VA requested an emergency supplemental appropriation for an increase of \$526.6 million for the loan guaranty revolving fund as part of a \$1,049.7 million total request. To forestall curtailed loan guaranty operations, VA also transferred \$200 million to the loan guaranty revolving fund from its Readjustment Benefits (education) appropriation. On April 29, 1988, Congress appropriated \$526.6 million for the loan guaranty revolving fund and an additional \$182.5 million to reimburse the Readjustment Benefits appropriation. Therefore, the loan guaranty revolving fund has required a total of \$726.6 million in additional funds in fiscal year 1988. Although loan guaranty operations for the remainder of fiscal year 1988 will be continued since the emergency supplemental appropriation was approved, a continuing high rate of foreclosures on VA guaranteed mortgages may require additional supplemental appropriations in future years.

### NOTE 6: INSURANCE PROGRAMS

The Veterans Administration administers the following life insurance programs which provide permanent (whole life) and term coverage: National Service Life Insurance (NSLI); United States Government Life Insurance (USGLI); Veterans Special Life Insurance (VSLI); Veterans Reopened Insurance (VRI); and Service-Disabled Veterans Insurance (SDVI). Data on insurance in force for each of these programs is as follows:

**Financial Statements**

The statutory insurance reserve balance as of September 30, 1986, consists of reserves for:

<u>Program</u>	<u>Death Benefits</u>	<u>Death Benefit Annuities</u>	<u>Disability Income and Waiver of Premium</u>	<u>Other</u>	<u>1986 Statutory Reserve Total</u>
(dollars in thousands)					
NSLI	\$7,832,314	\$498,663	\$ 929,186	\$135,512	\$ 9,395,775
USGLI	181,837	35,728	2,798	1,371	221,734
VSLI	792,724	3,420	121,572	10,600	928,316
SDVI	248,075	2,341	148,600		399,016
VRI	407,153	1,219	29,383		437,755
<b>TOTAL</b>	<b>\$2,462,103</b>	<b>\$541,371</b>	<b>\$1,231,519</b>	<b>\$147,583</b>	<b>\$11,532,578</b>

These statutorily computed reserves for guaranteed benefits differ from those computed under generally accepted accounting principles (GAAP) for Federal agencies (title 2). Under GAAP, future policy reserves are based on recent mortality experience and on interest assumptions that are expected to hold true for at least the next 10 years. As a result, GAAP policy reserves are lower than those computed using statutory assumptions. The remainder is called Participating Policyholders' Interest in Accumulated Participating Earnings (Participating Policyholders' Interest). It represents future benefits that inure to program participants based on statutory requirements and practices. Currently, however, this remaining balance cannot be fully disbursed without seriously affecting the solvency of the programs.

The GAAP Life Insurance Reserve Balances and Participating Policyholders' Interest as of September 30, 1987, are shown below:

<u>Program</u>	<u>Death Benefits</u>	<u>Death Benefit Annuities</u>	<u>Disability Income and Waiver of Premium</u>	<u>Other</u>	<u>1987 GAAP Reserve Total</u>	<u>Participating Policyholders Interest</u>
(dollars in thousands)						
NSLI	\$5,601,202	\$465,070	\$ 880,877	\$162,394	\$7,109,543	\$ 2,594,514
USGLI	100,086	32,149	2,496	1,220	135,951	67,785
VSLI	480,804	3,445	120,334	1,325	605,908	417,715
SDVI	257,854	2,299	148,462		408,615	
VRI	271,386	1,251	28,184		300,821	162,184
<b>TOTAL</b>	<b>\$6,711,332</b>	<b>\$504,214</b>	<b>\$1,180,353</b>	<b>\$164,219</b>	<b>\$8,560,818</b>	<b>\$3,242,198</b>

## Financial Statements

Under statutory principles, an asset is set up for uncollected premiums. Under GAAP, this asset is reduced. A comparison is provided below:

### Uncollected Premiums (dollars in thousands)

Program	9/30/87		9/30/86	
	Statutory	GAAP	Statutory	GAAP
NSLI	\$2,292	\$ 333	\$3,275	\$1,333
VSLI	447	202	549	243
SDVI	31	31	135	135
VRI	47	35	73	54
Total	<u>\$2,877</u>	<u>\$1,261</u>	<u>\$4,232</u>	<u>\$1,765</u>

### Policy Dividends

The VA Administrator annually determines the excess funds available for dividend payment. Dividends to be paid are based on an actuarial analysis of the individual programs as of the end of the preceding calendar year. Dividends are declared on a calendar year basis and are paid on policy anniversary dates. Policyholders may receive them in cash, use them to pay premiums in advance, repay loans, purchase paid-up insurance, or place them in an interest bearing account.

Dividends paid during fiscal years 1987 and 1986 were as follows:

	Dividends Paid	
	1987	1986
	(In Thousands)	
NSLI	\$804,378	\$764,086
USGLI	13,554	14,667
VSLI	76,033	69,018
VRI	33,035	35,164
TOTAL	<u>\$927,500</u>	<u>\$882,935</u>

Since July 1, 1972, NSLI policyholders with participating policies have been authorized to apply their dividends to purchase paid-up additional insurance. In April 1986, the Administrator approved an increase in the interest basis on paid-up additions reserves from 3.5 percent to 4.5 percent. As a result, effective January 1, 1987, approximately 810,000 NSLI policies were given an immediate one-time increase of approximately \$400 million of paid-up additional coverage. In addition, since the purchase rates under the new interest basis are lower than the prior rates, the same annual dividend will now purchase approximately 15 percent more paid-up additional coverage. A special notice of this action was included with the statements of paid-up additions released to policyholders on the 1987 anniversaries of the policies.

**Financial Statements**

VMLI Insurance in Force	<u>1-87</u>	<u>September 30 1986</u>
Number of Policies	5,534	5,658
Amount (in millions)	\$182.7	\$181.8

**Insurance Administrative Expenses**

Except for the SGLI and VRI programs, administrative costs are not charged to VA life insurance programs. Administrative costs charged the SGLI program were \$334,000 and \$319,000 in 1987 and 1986 respectively. Administrative costs charged the VRI program were \$1,316,000 in 1987 and \$1,235,000 in 1986. Administrative costs for the other insurance programs borne by VA appropriations were \$26,515,000 and \$26,072,000 in 1987 and 1986.

**NOTE 7: INVESTMENTS**

Insurance program investments, which comprise most of VA's investments, are in non-marketable U.S. Treasury special bonds and certificates and, to a lesser degree, in GNMA participation certificates. Interest rates for Treasury Special securities are based on average market yields for similar Treasury issues. The special bonds, which mature during various years through 2002, are generally held to maturity unless needed to finance insurance claims and dividends. The certificates are short-term in nature and are either redeemed or replaced at maturity depending upon the cash needs of the insurance program. At September 30, 1987, investment securities consist of:

<u>Security</u>	<u>Interest Range</u>	<u>Insurance Programs</u>	<u>Other Programs</u>	<u>Total</u>
(dollars in thousands)				
Special Bonds	5.875-13.75%	\$11,737,185		\$11,737,185
Certificates	8.375-10.375%	194,638		194,638
GNMA Certificates	6.2-6.45%	135,000		135,000
Bonds	7.875-8.5%		\$ 2,251	2,251
Notes	10-14.625%		18,743	18,743
Other	Various		154,746	154,746
		<u>\$12,066,823</u>	<u>\$175,740</u>	<u>\$12,242,563</u>

**Financial Statements**

The receivables as of September 30, 1987 consists of:

	<u>Current</u>	<u>Non-Current</u>	<u>Total</u>
<u>Accounts:</u>			
Individuals/Corporations	\$2,363,256	\$ 19	\$2,363,275
Federal Government	350,139	480	350,619
Less: Allowances for Loss	<u>1,982,060</u>		<u>1,982,060</u>
Accounts Receivable, net	<u>731,335</u>	<u>499</u>	<u>731,834</u>
<u>Advances:</u>			
Individuals/Corporations	44,933		44,933
Federal Government	<u>110,519</u>		<u>110,519</u>
Total Advances	<u>155,452</u>		<u>155,452</u>
<u>Loans</u>			
Individuals	202,118	1,857,405	2,459,523
Less: Allowances for Loss	<u>134,843</u>		<u>134,843</u>
Loans, Net	<u>67,275</u>	<u>1,857,405</u>	<u>1,924,680</u>
<b>Net Receivables</b>	<b><u>\$1,354,262</u></b>	<b><u>\$1,857,904</u></b>	<b><u>\$3,211,966</u></b>

The receivables as of September 30, 1986 consists of:

	<u>Current</u>	<u>Non-Current</u>	<u>Total</u>
<u>Accounts:</u>			
Individuals/Corporations	\$1,429,789	\$ 42,364	\$1,972,153
Federal Government	330,088	445	330,533
Less: Allowances for Loss	<u>1,545,919</u>		<u>1,545,919</u>
Accounts Receivable, net	<u>713,958</u>	<u>42,809</u>	<u>756,767</u>
<u>Advances:</u>			
Individuals/Corporations	56,550		56,550
Federal Government	<u>132,837</u>		<u>132,837</u>
Total Advances	<u>189,387</u>		<u>189,387</u>
<u>Loans</u>			
Individuals	536,287	1,968,101	2,504,388
Less: Allowances for Loss	<u>107,056</u>		<u>107,056</u>
Loans, Net	<u>429,231</u>	<u>1,968,101</u>	<u>2,397,332</u>
<b>Net Receivables</b>	<b><u>\$1,322,575</u></b>	<b><u>\$2,010,910</u></b>	<b><u>\$3,243,486</u></b>



## Financial Statements

Property and equipment consisted of the following as of September 30, 1986:

	Cost	Accumulated Depreciation	Net Book Value
	(dollars in thousands)		
Land	\$ 81,416	\$	\$ 81,416
Buildings	4,873,656	1,638,255	3,235,401
Equipment	2,543,943	1,433,636	1,110,307
Other	563,542	263,617	399,925
Construction in Progress	<u>1,483,000</u>		<u>1,483,000</u>
TOTAL	<u>\$9,545,557</u>	<u>\$3,335,508</u>	<u>\$6,210,049</u>

Prior to 1986, VA did not record depreciation for property and equipment, except for equipment in its Supply Fund. During 1986, in addition to recording 1986 depreciation, VA also recorded accumulated depreciation of \$2,982,024,000 relating to fiscal years prior to 1986. This amount has been treated as a prior period adjustment, and the deferred appropriations account has been adjusted accordingly. Current year depreciation amounted to \$361,477,000 in FY 1987 and \$337,997,000 in FY 1986.

VA leases facilities, primarily office space and medical facilities, from GSA. These leases are cancelable without penalty. In addition, VA has operating leases with the public for office, data processing, and other equipment. Fiscal year 1987 and fiscal year 1986 rent expense for these leases amount to approximately \$76,329,000 and \$76,125,000, respectively from GSA, and \$59,529,000 and \$57,900,000, respectively, from the public.

### NOTE 10: COMMITMENTS AND CONTINGENCIES

VA is committed under obligations it has incurred at the end of each year for goods and services which have been ordered but not yet received (undelivered orders). Aggregate undelivered orders amounted to \$1,805,952,000 and \$1,540,894,000 at September 30, 1987 and 1986, respectively. Of these amounts, \$960,440,000 in 1987 and \$755,962,000 in 1986 relate to construction projects of both-long and short-term duration. The remainder is principally comprised of obligations for medical supplies and equipment which were incurred by VA in the normal course of fulfilling its mission.

As previously stated in Note 2, VA is a party in various administrative proceedings, legal actions, and tort claims brought by or against it, primarily relating to allegations of medical malpractice. However, also as stated in Note 1, such legal settlements of tort claims awards in excess of \$2,500 and contract disputes are paid from a Governmentwide Judgment Fund appropriation maintained by the Department of the Treasury, with an agency having to reimburse the Fund for only contract dispute payments.

In the opinion of VA's management and general counsel, the ultimate resolution of legal actions still pending at September 30, 1987, will not materially affect VA's operations or financial position, especially when consideration is given to the availability of the Judgment Fund appropriation to pay court settled legal cases.

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF ASSETS, LIABILITIES, AND EQUITY BY MAJOR PROGRAM

SEPTEMBER 30, 1987  
(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>ASSETS:</b>						
Fund Balance with U.S. Treasury	\$ 3,624,002	\$ 1,849,305	\$ 119,902	\$ 19,808	\$ 384,010	\$ 5,997,027
Imprest Funds	9,616					9,616
Advances, Accounts, and Loans Receivable	243,527	322,909	1,172,506	1,408,271	64,753	3,211,966
Investments	20,994		154,746	12,066,823		12,242,563
Foreclosed Property Held for Sale			864,104			864,104
Land, Buildings, and Equipment Net of Accumulated Depreciation	6,836,854				2,409	6,839,263
Other Assets	31,043				120,572	151,615
Future Financing Sources	996,000	40,247	\$2,596,289	\$ 371,141	91,431	\$ 4,095,108
<b>TOTAL ASSETS</b>	<b>\$11,762,036</b>	<b>\$ 2,212,461</b>	<b>\$4,907,547</b>	<b>\$13,866,043</b>	<b>\$ 663,175</b>	<b>\$33,411,262</b>
<b>LIABILITIES, TRUST FUND BALANCES, AND EQUITY:</b>						
<b>LIABILITIES:</b>						
Accounts Payable, Principally to the Public	\$ 608,569	\$ 1	\$ 135,555	\$ 172,126	\$ 195,684	\$ 1,111,935
Accrued Compensation and Pension Benefits		1,280,054				1,280,054
Accrued Payroll and Payroll Related Liabilities	924,743				86,825	1,011,568
Dividends on Credit or Deposit				706,018		706,018
Insurance Dividends Payable				956,347		956,347
Other Liabilities	71,779		171,856	148,855	67,389	459,879
Reserve for Federal Employees Compensation Act	385,592				38,135	423,727
Reserve for Losses on Guaranteed Loans			2,718,898			2,718,898
Insurance Reserves				11,612,555		11,612,555
Borrowings from Treasury			1,730,078			1,730,078
<b>TOTAL LIABILITIES</b>	<b>1,990,683</b>	<b>1,280,055</b>	<b>4,756,387</b>	<b>13,595,901</b>	<b>388,033</b>	<b>22,011,059</b>
<b>TRUST FUND BALANCES</b>	<b>20,503</b>	<b>598,994</b>		<b>270,142</b>		<b>889,639</b>
<b>EQUITY OF THE U.S. GOVERNMENT:</b>						
<b>Unrealized Appropriations:</b>						
Deferred Appropriations	6,865,853	316,365			152,608	7,334,826
Unobligated Balances	1,205,316	0	151,157		13,313	1,369,786
Undelivered Orders	1,679,681	17,047	3		109,221	1,805,952
<b>TOTAL EQUITY OF THE U.S. GOVERNMENT</b>	<b>9,750,850</b>	<b>333,412</b>	<b>151,160</b>		<b>275,142</b>	<b>10,510,564</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$11,762,036</b>	<b>\$2,212,461</b>	<b>\$4,907,547</b>	<b>\$13,866,043</b>	<b>\$ 663,175</b>	<b>\$33,411,262</b>

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF EXPENSES, DIVIDENDS, REVENUE,  
AND FINANCING SOURCES BY MAJOR PROGRAM  
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1987  
(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>OPERATING EXPENSES AND DIVIDENDS:</b>						
Expenses By Category:						
Personnel Compensation and Fringe Benefits	\$ 6,420,086				\$562,706	\$ 6,982,792
Veterans' Benefits		\$ 15,630,956				15,630,956
Claims & Indemnities	176		\$2,131,936	\$1,140,184		3,272,296
Depreciation	362,617				860	363,477
Supplies & Materials	1,602,432				20,520	1,622,952
Contractual Services	1,256,107				64,542	1,320,649
Rent, Communications, and Utilities	389,585				126,682	516,267
Other	220,622				41,969	262,591
<b>Total Operating Expenses</b>	<b>10,251,625</b>	<b>15,630,956</b>	<b>2,131,936</b>	<b>1,140,184</b>	<b>817,279</b>	<b>29,971,980</b>
Provisions for Dividends to Policyholders				928,845		928,845
Provisions for SGLI Reserve				9,027		9,027
	<b>\$10,251,625</b>	<b>\$ 15,630,956</b>	<b>\$2,131,936</b>	<b>\$2,078,056</b>	<b>\$ 817,279</b>	<b>\$30,909,852</b>
<b>OPERATING REVENUE AND FINANCING SOURCES:</b>						
Operating Revenues:						
Premium Income				877,756		877,756
Interest Income			191,425	1,192,317		1,383,742
Loan Origination Fees			340,972			340,972
Reimbursements and Other	277,211	86,453	(45,021)	(8,404)	84,776	395,015
<b>Total Operating Revenue</b>	<b>277,211</b>	<b>86,453</b>	<b>487,376</b>	<b>2,061,669</b>	<b>84,776</b>	<b>2,997,485</b>
Financing by Source:						
Appropriations and						
Financing Sources Realized	9,881,636	15,271,150	674,593	5,848	726,918	26,560,145
Funds to be Provided by Future Financing Sources	92,778	40,247	969,967	10,539	5,585	1,119,116
Transfers, Reimbursements, and Other		233,106				233,106
<b>Total Budgetary Financing</b>	<b>9,974,414</b>	<b>15,544,503</b>	<b>1,644,560</b>	<b>16,387</b>	<b>732,503</b>	<b>27,912,367</b>
	<b>\$10,251,625</b>	<b>\$ 15,630,956</b>	<b>\$2,131,936</b>	<b>\$2,078,056</b>	<b>\$ 817,279</b>	<b>\$30,909,852</b>

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF SOURCES AND USES OF  
RESOURCES AND RECONCILIATION TO BUDGET BY MAJOR PROGRAM  
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1967  
(Dollars in Thousands)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>NET USE OF RESOURCES:</b>						
Operations:						
Operating Expenses	\$10,251,625	\$ 15,630,956	\$ 2,131,936	\$ 1,140,184	\$ 817,279	\$ 29,971,980
Items Requiring (Providing) Funds:						
(Increase) in Reserves	(52,488)		(983,646)	(229,979)	(5,191)	(1,271,304)
Depreciation	(362,617)				(860)	(363,477)
Increase (Decrease) in Accounts Receivable	(37,217)	10,675	(384,818)	(4,842)	(4,289)	(420,471)
Decrease (Increase) in Accounts Payable and Accruals	(64,610)	(41,608)	(38,274)	(93,155)	(37,068)	(274,715)
Revenues Accounted for as Offsetting Collections	(277,221)	(319,559)	(487,376)	(1,094,351)	(84,776)	(2,263,283)
Funds Used (Provided) by Operations	9,457,472	15,280,464	237,822	(282,143)	685,115	25,378,730
Non-Operating Uses:						
Dividends				927,500		927,500
Acquisitions of Land, Buildings, and Equipment	954,782				15,211	969,993
Purchase of Foreclosed Property Held for Sale			1,380,338			1,380,338
Insurance and Repurchase of Loans and Liens		(2,002)	1,224,720	104,657		1,327,375
Other, Net	(807)				(2,255)	(3,062)
Financing Activities:						
Sale of Foreclosed Property Held for Sale			(1,482,928)			(1,482,928)
Sale of Loans, with Recourse			(849,196)			(849,196)
Loan/Lien Repayments/Out Income Settlements			(161,761)	(211,139)		(372,900)
Disposal of Equipment and Other	(95,260)			(6)		(95,266)
Revenues Collected for Treasury	(33,004)	(195,542)				(228,546)
<b>NET USE OF BUDGETARY RESOURCES (OUTLAYS)</b>	<b>10,283,183</b>	<b>15,082,920</b>	<b>348,222</b>	<b>538,869</b>	<b>698,071</b>	<b>26,952,035</b>
<b>SOURCES OF BUDGETARY RESOURCES PROVIDED</b>						
Intra-agency Transfers						
Current Year Appropriation	10,514,378	15,215,750	100,000	4,770	770,500	26,605,398
Interest on Government Securities				964,383		964,383
Net Transfers, Reimbursements, and Other	21,931	(200,706)		(3,488)	16,290	(165,973)
Funds Returned to Treasury	(160,069)	(661)			(9,496)	(170,226)
<b>TOTAL RESOURCES PROVIDED</b>	<b>10,376,240</b>	<b>15,014,383</b>	<b>100,000</b>	<b>965,665</b>	<b>777,294</b>	<b>27,233,582</b>
<b>INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>						
Funds Exchanged for U.S. Government Securities	93,057	(68,537)	(248,995)	426,796	79,223	281,544
<b>NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>	<b>91,768</b>	<b>(68,537)</b>	<b>(248,995)</b>	<b>(5,009)</b>	<b>79,223</b>	<b>(151,550)</b>
<b>U.S. TREASURY AND IMPREST FUNDS:</b>						
Balance of Year	3,541,850	1,317,842	368,897	24,817	304,787	6,158,193
End of Year	\$ 3,633,618	\$ 1,249,305	\$ 119,902	\$ 19,808	\$ 384,010	\$ 5,006,643

**Financial Statements**

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

**BUDGETED AND ACTUAL OUTLAYS BY FUNCTION AND PROGRAM  
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1987  
(Dollars in Thousands)**

	Budgeted Outlays		
	President's Budget	Enacted Bill	Actual Outlays
<b>HOSPITAL AND MEDICAL CARE:</b>			
Medical Care	\$ 8,960,952	\$ 9,500,505	\$ 9,499,750
Medical and Prosthetic Research	187,332	212,729	195,123
Medical Administration	43,952	43,417	40,265
Construction	687,328	607,851	537,156
Proposed Legislation	(185,173)		
All Other	40,934	(19,347)	10,889
<b>Total Hospital and Medical Care</b>	<b>9,735,025</b>	<b>10,345,155</b>	<b>10,283,183</b>
<b>BENEFITS:</b>			
Income Security for Veterans:			
Compensation	10,415,000	10,418,900	10,502,353
Pensions	3,825,000	3,830,500	3,793,200
Burial and Other Benefits	134,392	135,908	130,730
Proposed Legislation	243,800		
Reinstated Entitlement for Survivors		5,398	(2,845)
<b>Subtotal Income Security</b>	<b>14,618,192</b>	<b>14,390,706</b>	<b>14,423,438</b>
Education, Training, and Rehabilitation:			
Readjustment Benefits (G.I. Bill)	754,897	756,297	776,401
Post-Vietnam Era Education	(75,700)	(7,750)	50,501
Veterans Job Training	5,384	41,737	38,005
All Other	(192,448)	(212,238)	(205,425)
Proposed Legislation	25,573		
<b>Subtotal Education, Training, and Rehabilitation</b>	<b>517,706</b>	<b>578,046</b>	<b>659,482</b>
<b>Total Benefits</b>	<b>15,135,898</b>	<b>14,968,752</b>	<b>15,082,920</b>
<b>HOUSING CREDIT ASSISTANCE:</b>			
Loan Guaranty	148,900	277,800	382,059
Proposed Legislation	(131,800)		
Direct Loans	(43,453)	(36,900)	(33,064)
<b>Total Housing Credit Assistance</b>	<b>(26,353)</b>	<b>240,900</b>	<b>348,995</b>
<b>INSURANCE PROGRAMS</b>	<b>747,832</b>	<b>612,744</b>	<b>538,869</b>
<b>ADMINISTRATION</b>			
Other Benefits and Services	759,317	757,684	698,071
Proposed Legislation	952		
<b>Total Administration</b>	<b>760,269</b>	<b>757,684</b>	<b>698,071</b>
<b>TOTAL VETERAN ADMINISTRATION</b>	<b>\$26,352,671</b>	<b>\$26,925,235</b>	<b>\$26,952,038</b>

Where actual outlays exceeded outlays budgeted in the enacted bill, funds were obtained from available unobligated balances. This does not constitute a violation of the Anti-Deficiency Act (31 U.S.C. 1341).

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF ASSETS AND LIABILITIES  
 BY LIFE INSURANCE FUND ON SEPTEMBER 30, 1987  
 (Dollars in Thousands)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SDVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>ASSETS:</b>							
Fund Balance (Cash)	\$ 430	\$ 8,549	\$ 231	\$ 10,125	\$ 286	\$ 187	\$ 19,808
Investments (U.S. Treasury Securities)	221,986	10,125,109	1,092,590		482,184	144,954	12,066,823
Policy Loans	21,560	925,992	73,538	38,565	27,167		1,086,822
Policy Liens		562	73	741	57		1,433
Accrued Interest (Treasury Securities)	4,112	242,486	26,224		12,117	3,125	288,064
Accrued Interest (Policy Loans)	467	23,925	2,366	1,394	923		29,075
Other		2,292	447	91	47		2,877
Future Financing Sources		4,755		366,386			371,141
<b>Total Assets</b>	<b>\$248,555</b>	<b>\$11,333,670</b>	<b>\$1,195,469</b>	<b>\$417,302</b>	<b>\$522,791</b>	<b>\$148,266</b>	<b>\$13,866,043</b>
<b>LIABILITIES AND TRUST FUND BALANCES:</b>							
<b>LIABILITIES:</b>							
Insurance Claims	\$ 12,330	\$ 140,392	\$ 7,391	\$ 7,043	\$ 4,970		\$ 172,126
Dividends Payable	12,316	826,400	84,265		33,366		956,347
Dividends on Credit or Deposit	19,180	600,220	68,080		18,538		706,018
Deferred Credits	23	105,487	23,341	1,447	3,487		133,785
Other	970	13,131	520	197	252		15,070
Insurance Statutory Reserves	198,276	9,590,610	973,680	408,615	441,374		11,612,555
<b>Total Liabilities</b>	<b>243,095</b>	<b>11,276,240</b>	<b>1,157,277</b>	<b>417,302</b>	<b>501,987</b>		<b>13,595,901</b>
<b>TRUST FUND BALANCES</b>	<b>5,460</b>	<b>57,430</b>	<b>38,192</b>		<b>20,794</b>	<b>148,266</b>	<b>270,142</b>
<b>Total Liabilities and Trust Fund Balances</b>	<b>\$248,555</b>	<b>\$11,333,670</b>	<b>\$1,195,469</b>	<b>\$417,302</b>	<b>\$522,791</b>	<b>\$148,266</b>	<b>\$13,866,043</b>

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF EXPENSES, DIVIDENDS, REVENUE  
 AND FINANCING SOURCES BY LIFE INSURANCE FUND  
 FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1987  
 (Dollars in Thousands)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SOVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>OPERATING EXPENSES AND EARNINGS DISTRIBUTION PROVISIONS:</b>							
Insurance Claims & Indemnities	\$ 8,198	\$ 951,398	\$ 91,954	\$47,333	\$38,600	\$ 2,701	\$1,140,184
Total Operating Expenses	\$ 8,198	\$ 951,398	\$ 91,954	\$47,333	\$38,600	\$ 2,701	\$1,140,184
Provisions for Dividends to Policyholders	13,522	801,047	84,434		29,842		928,845
Provisions for SGLI Reserve						9,027	9,027
	\$21,720	\$1,752,445	\$176,388	\$47,333	\$68,442	\$11,728	\$2,078,056
<b>OPERATING REVENUE AND FINANCING SOURCES:</b>							
Operating Revenues:							
Premium Income	\$ 123	\$ 749,729	\$ 78,789	\$30,234	\$18,881		\$ 877,756
Interest Income	18,251	1,004,611	104,990	2,712	50,025	11,728	1,192,317
Reimbursements and Other	3,333	(3,882)	(7,391)		(464)		(8,404)
Total Operating Revenue	\$21,707	\$1,750,458	\$176,388	\$32,946	\$68,442	\$11,728	\$2,061,669
<b>Financing by Source:</b>							
Appropriations and Financing Sources Realized	13	1,914		3,921			5,848
Funds to be Provided by Future Financing Sources		73		10,466			10,539
Total Budgetary Financing	\$21,720	\$1,752,445	\$176,388	\$47,333	\$68,442	\$11,728	\$2,078,056

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF SOURCES AND USES OF  
 RESOURCES AND RECONCILIATION TO BUDGET  
 BY LIFE INSURANCE FUND FOR THE FISCAL  
 YEAR ENDED SEPTEMBER 30, 1997  
 (Dollars in Thousands)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SDVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>NET USE OF RESOURCES:</b>							
Operations							
Operating Expenses	\$ 8,198	\$951,398	\$ 91,954	\$47,333	\$38,600	\$ 2,701	\$1,140,184
Items Requiring (Providing) Funds:							
Decrease (Increase) in Reserves	23,458	(194,835)	(45,364)	(9,599)	(3,639)		(229,979)
Increase (Decrease) in Accounts Receivable	(367)	(3,178)	2,214	7	161	(3,679)	(4,842)
Decrease (Increase) in Accounts Payable and Accruals	144	(75,109)	(14,017)	322	(4,322)	(173)	(93,155)
Revenues Accounted for as Offsetting Collections	(619)	(793,615)	(183,936)	(39,784)	(68,669)	(11,728)	(1,094,351)
Funds Used (Provided) by Operations	\$30,814	(\$115,339)	(\$149,149)	\$ 2,279	(\$37,869)	(\$12,879)	(\$ 282,143)
Non-Operating Uses:							
Dividends	13,554	804,878	76,033		33,035		927,500
Issuance and Repurchase of Loans and Liens	1,430	81,816	10,052	6,585	4,774		104,657
Financing Activities:							
Loan and Lien Repayments and Optional Income Settlement	(5,408)	(176,182)	(15,149)	(6,880)	(7,520)		(211,139)
Other		(6)					(6)
Net Use of Resources (Budgetary Outlays)	\$40,390	\$595,167	(\$ 78,213)	\$ 1,984	(\$ 7,580)	(\$12,879)	\$ 538,869
<b>RESOURCES PROVIDED:</b>							
Current Year Appropriation		4,770					4,770
Interest on Government Securities	17,617	946,766					964,383
Other		843				(4,331)	(3,488)
Total Budgetary Resources Provided	\$17,617	\$952,379				\$ 4,331	\$ 965,665
<b>INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>							
Funds Exchanged for U.S. Government Securities	( 22,893)	356,846	78,469		7,627	11,756	431,805
NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS	120	366	(256)	(1,984)	(47)	(3,208)	(5,009)
<b>U.S. TREASURY FUNDS</b>							
Beginning of Year	310	8,183	487	12,109	333	3,395	24,817
End of year	\$ 430	\$ 8,549	\$ 231	\$ 10,125	\$ 286	\$ 187	\$ 19,808



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Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF SOURCES AND USES OF  
 RESOURCES AND RECONCILIATION TO BUDGET  
 BY LIFE INSURANCE FUND FOR THE FISCAL  
 YEAR ENDED SEPTEMBER 30, 1986  
 (Dollars in Thousands)  
 (Restated and Unaudited)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SDVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>NET USE OF RESOURCES:</b>							
Operations							
Operating Expenses	\$ 7,793	\$916,092	\$ 96,279	\$48,123	\$40,957	\$ 2,966	\$1,112,210
Items Requiring (Providing) Funds:							
Decrease (Increase) in Reserves	24,043	(188,144)	(53,909)	(9,948)	46,737		(181,221)
Increase (Decrease) in Accounts Receivable	(80)	(788)	2,535	69	(1,144)	3,680	4,272
Decrease (Increase) in Accounts Payable and Accruals	3,153	(50,977)	(12,560)	(134)	(649)	127	(61,040)
Revenues Accounted for as Offsetting Collections	(1,282)	(769,895)	(171,314)	(40,486)	(72,232)	(12,499)	(1,067,708)
Funds Used (Provided) by							
Operations							
Non-Operating Uses:	\$33,627	(\$ 93,712)	(\$118,969)	(\$ 2,376)	\$13,669	(\$ 5,726)	(\$ 193,487)
Dividends	14,667	764,086	69,018		35,164		882,935
Issuance and Repurchase of Loans and Liens	1,487	91,872	11,095	6,031	5,006		115,491
Other Net							
Financing Activities:							
Loan and Lien Repayments and Optional Income Settlement	(5,181)	(157,418)	(13,282)	(6,075)	(13,733)		(195,689)
Other		(46)	(18)	(113)	17		(160)
Net Use of Resources (Budgetary Outlays)	\$44,600	\$604,782	(\$ 72,156)	(\$ 2,533)	\$40,123	(\$ 5,726)	\$ 609,090
<b>RESOURCES PROVIDED:</b>							
Current Year Appropriation		9,750					9,750
Less: Reductions Pursuant to P.L. 99-177 (Gramm-Rudman-Hollings)		(5)					(5)
Current Year Appropriations Net		9,745					9,745
Interest on Government Securities	19,504	924,452					943,956
Other		(845)				4,330	3,485
Total Resources Provided	\$19,504	\$933,352				\$ 4,330	\$ 957,186
<b>INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>							
Funds Exchanged for U.S. Government Securities	(\$25,096)	\$328,570	\$ 72,156	\$ 2,533	(\$40,123)	\$10,056	\$ 348,096
NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS	24,075	(337,239)	(72,247)		39,895	(12,701)	(358,217)
NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS	(1,021)	(8,669)	(91)	2,533	(228)	(2,645)	(10,121)
<b>U.S. TREASURY FUNDS</b>							
Beginning of Year	1,331	16,852	578	9,576	561	6,040	34,938
End of Year	\$ 310	\$ 8,183	\$ 487	\$ 12,109	\$ 333	\$ 3,395	\$ 24,817

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF EXPENSES, DIVIDENDS, REVENUE  
 AND FINANCING SOURCES BY LIFE INSURANCE FUND  
 FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1966  
 (Dollars in Thousands)  
 (Restated and Unaudited)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SDVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>OPERATING EXPENSES AND EARNINGS DISTRIBUTION PROVISIONS:</b>							
Insurance Claims & Indemnities	\$ 7,793	\$ 916,092	\$ 96,279	\$48,123	\$40,957	\$ 2,966	\$1,112,210
Total Operating Expenses	\$ 7,793	\$ 916,092	\$ 96,279	\$48,123	\$40,957	\$ 2,966	\$1,112,210
Provisions for Dividends to Policyholders	12,910	788,014	74,984		31,262		907,170
Provisions for SGLI Reserve						9,533	9,533
	\$20,703	\$1,704,106	\$171,263	\$48,123	\$72,219	\$12,499	\$2,028,913
<b>OPERATING REVENUE AND FINANCING SOURCES:</b>							
Operating Revenues:							
Premium Income	90	721,157	76,774	30,116	20,265		848,402
Interest Income	20,153	984,142	94,945	2,543	51,676	12,499	1,165,958
Reimbursement and Other	460	(3,156)	(456)		278		(2,874)
Total Operating Revenue	\$20,703	\$1,702,143	\$171,263	\$32,659	\$72,219	\$12,499	\$2,011,517
<b>Financing by Source:</b>							
Appropriations and Financing Sources Realized		1,595		7,796			9,391
Funds to be Provided by Future Financing Sources		368		7,668			8,036
Total Budgetary Financing	\$20,703	\$1,704,106	\$171,263	\$48,123	\$72,219	\$12,499	\$2,028,913

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION  
 SCHEDULE OF ASSETS AND LIABILITIES  
 BY LIFE INSURANCE FUND ON SEPTEMBER 30, 1986  
 (Dollars in Thousands)

	U.S. GOVERNMENT LIFE INSURANCE USGLI	NATIONAL SERVICE LIFE INSURANCE NSLI	VETERANS SPECIAL LIFE INSURANCE VSLI	SERVICE- DISABLED VETERANS INSURANCE SDVI	VETERANS REOPENED INSURANCE VRI	SERVICEMEN'S GROUP LIFE INSURANCE SGLI	TOTAL LIFE INSURANCE
<b>ASSETS:</b>							
Fund Balance (Cash)	\$ 310	\$ 8,183	\$ 487	\$ 12,109	\$ 333	\$ 3,395	\$ 24,817
INVESTMENTS	244,879	9,768,263	1,014,121		474,557	133,198	11,635,018
(U.S. Treasury Securities)							
Policy Loans	25,297	1,010,077	78,001	38,280	29,541		1,181,196
Policy Liens	15	635	80	699	61		1,490
Accrued Interest (Treasury Securities)	4,483	234,402	23,795		11,917	2,795	277,392
Accrued Interest (Policy Loans)	550	26,059	2,471	1,338	982		31,400
Other		3,275	549	135	73		4,032
Future Financing Sources		4,682		355,920			360,602
<b>Total Assets</b>	<b>\$275,534</b>	<b>\$11,055,576</b>	<b>\$1,119,504</b>	<b>\$408,481</b>	<b>\$517,464</b>	<b>\$139,388</b>	<b>\$13,515,947</b>
<b>LIABILITIES AND TRUST FUND BALANCES:</b>							
<b>LIABILITIES:</b>							
Insurance Claims	\$ 14,198	\$ 138,703	\$ 7,053	\$ 7,803	\$ 4,986		\$ 172,743
Dividends Payable	13,680	807,065	76,331		32,638		929,714
Dividends on Credit or Deposit	19,639	540,271	55,770		14,701		630,381
Deferred Credits	42	100,615	21,704	1,440	3,120		126,921
Other	749	11,886	539	222	297		13,693
Insurance Statutory Reserves	221,734	9,395,775	928,316	399,016	437,735		11,382,576
<b>Total Liabilities</b>	<b>270,042</b>	<b>10,994,315</b>	<b>1,089,713</b>	<b>408,481</b>	<b>493,477</b>		<b>13,256,028</b>
<b>TRUST FUND BALANCES</b>	<b>5,492</b>	<b>61,261</b>	<b>29,791</b>		<b>23,987</b>	<b>139,388</b>	<b>259,919</b>
<b>Total Liabilities and Trust Fund Balances</b>	<b>\$275,534</b>	<b>\$11,055,576</b>	<b>\$1,119,504</b>	<b>\$408,481</b>	<b>\$517,464</b>	<b>\$139,388</b>	<b>\$13,515,947</b>

Financial Statements

NOTE 11: (CONTINUED) VETERANS ADMINISTRATION

BUDGETED AND ACTUAL OUTLAYS BY FUNCTION AND PROGRAM  
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986  
(Dollars in Thousands)

	Budgeted Outlays		Actual Outlays
	President's Budget	Enacted * Bill	
<b>HOSPITAL AND MEDICAL CARE:</b>			
Medical Care	\$ 9,051,700	\$ 9,067,560	\$ 9,095,306
Medical and Prosthetic Research	187,080	181,491	181,246
Medical Administration	57,379	55,631	54,780
Construction	737,800	555,081	522,386
All Other	(27,192)	19,450	31,254
<b>Total Hospital and Medical Care</b>	<b>10,006,767</b>	<b>9,879,213</b>	<b>9,884,972</b>
<b>BENEFITS:</b>			
Income Security for Veterans:			
Compensation	10,194,000	10,453,000	10,416,201
Pensions	3,833,000	3,835,000	3,874,368
Burial and Other Benefits	136,800	128,007	121,909
Proposed Legislation	285,700		
Reinstated Entitlement for Survivors		14,970	9,856
<b>Subtotal Income Security</b>	<b>14,449,500</b>	<b>14,430,977</b>	<b>14,422,334</b>
Education, Training, and Rehabilitation:			
Readjustment Benefits (G.I. Bill)	1,034,500	910,422	918,056
Post-Vietnam Era Education	40,000	(210,600)	(98,624)
Veterans Job Training	35,000	49,200	34,192
All Other	(7,570)	(158,215)	(119,102)
<b>Subtotal Education, Training, and Rehabilitation</b>	<b>1,101,930</b>	<b>590,807</b>	<b>734,522</b>
<b>Total Benefits</b>	<b>15,551,430</b>	<b>15,021,784</b>	<b>15,156,856</b>
<b>HOUSING CREDIT ASSISTANCE:</b>			
Loan Guaranty	383,500	285,450	162,769
Proposed Legislation	(604,600)		
Direct Loans	(45,600)	(44,740)	(28,669)
<b>Total Housing Credit Assistance</b>	<b>(266,700)</b>	<b>240,710</b>	<b>134,100</b>
<b>INSURANCE PROGRAMS</b>	<b>685,961</b>	<b>678,633</b>	<b>609,090</b>
<b>ADMINISTRATION</b>	<b>751,456</b>	<b>718,025</b>	<b>750,692</b>
<b>TOTAL</b>	<b>\$26,728,914</b>	<b>\$26,538,365</b>	<b>\$26,535,710</b>

\* After reduction pursuant to P.L. 99-177 (Gramm-Rudman-Hollings). Where actual outlays exceeded outlays budgeted in the enacted bill, funds were obtained from available unobligated balances. This does not constitute a violation of the Anti-Deficiency Act (31 U.S.C. 1341).

Financial Statements

NOTE 11: (CONTINUED)

**VETERANS ADMINISTRATION**  
**SCHEDULE OF SOURCES AND USES OF**  
**RESOURCES AND RECONCILIATION TO BUDGET BY MAJOR PROGRAM**  
**FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986**  
 (Dollars in Thousands)  
 (Restated and Unaudited)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>NET USE OF RESOURCES:</b>						
Operations:						
Operating Expenses	\$ 9,760,855	\$ 15,673,194	\$ 1,094,250	\$ 1,112,210	\$ 775,368	\$ 28,415,877
Items Requiring (Providing) Funds:						
(Increase) in Reserves	(45,945)		(513,875)	(181,221)	(4,544)	(745,585)
Depreciation	(337,997)					(337,997)
Increase (Decrease) in Accounts Receivable	75,482	(15,799)	(5,433)	4,272	22,546	61,068
Decrease (Increase) in Accounts Payable and Accruals	(118,674)	24,217	(8,055)	(61,040)	3,827	(159,725)
Revenues Accounted for as Offsetting Collections	(259,716)	(298,682)	(441,846)	(1,067,708)	(46,505)	(2,114,457)
Funds Used (Provided) by Operations	9,074,005	15,362,910	125,041	(193,487)	750,692	25,119,181
Non-Operating Uses:						
Dividends				882,935		882,935
Acquisitions of Land, Buildings, and Equipment	952,690					952,690
Purchase of Foreclosed Property Held for Sale			1,147,210			1,147,210
Issuance and Repurchase of Loans and Liens			969,590	115,491		1,085,081
Other, Net	4,065	3,531	26,487			34,083
Financing Activities:						
Sale of Foreclosed Property Held for Sale			(1,214,867)			(1,214,867)
Sale of Loans, with Recourse			(818,368)			(818,368)
Loan/Lien Repayments/Out Income Settlements			(100,993)	(195,689)		(296,682)
Disposals of Equipment and Other	(145,328)	(96,812)		(160)		(242,300)
Revenues Collected for Treasury	(460)	(112,793)				(113,253)
<b>NET USE OF BUDGETARY RESOURCES (OUTLAYS)</b>	<b>9,884,972</b>	<b>15,156,856</b>	<b>124,100</b>	<b>602,020</b>	<b>750,692</b>	<b>26,535,710</b>
<b>RESOURCES PROVIDED:</b>						
Intra-agency Transfers	(43,984)	35,000			8,984	0
Current Year Appropriation	10,165,045	15,349,800	200,000	9,750	739,831	26,464,426
Less: Reductions Pursuant to P.L. 99-177 (Grass-Roots-Hollings)	(156,659)	(45,232)		(5)	(32,157)	(234,053)
Current Year Appropriations, Net	9,964,402	15,339,568	200,000	9,745	716,659	26,230,373
Interest on Government Securities				943,956		943,956
Net Transfers, Reimbursements, and Other	4,507	(107,628)	(2,120)	3,485	6,571	(95,185)
Funds Returned to Treasury	(53,151)	(785)			(4,787)	(58,723)
<b>TOTAL RESOURCES PROVIDED</b>	<b>9,915,758</b>	<b>15,231,155</b>	<b>197,880</b>	<b>957,186</b>	<b>718,442</b>	<b>27,020,421</b>
<b>INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>						
Funds Exchanged for U.S. Government Securities	30,786	74,299	63,780	348,096	(32,250)	484,711
Funds Exchanged for U.S. Government Securities	(2,394)			(358,217)		(360,611)
<b>NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>	<b>28,392</b>	<b>74,299</b>	<b>63,780</b>	<b>(10,121)</b>	<b>(32,250)</b>	<b>124,100</b>
<b>U.S. TREASURY AND IMPREST FUNDS:</b>						
Beginning of Year	3,513,458	1,843,541	305,117	34,938	337,037	6,034,091
End of Year	\$ 3,541,850	\$ 1,917,842	\$ 368,897	\$ 24,817	\$ 304,787	\$ 6,158,193

Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF EXPENSES, DIVIDENDS, REVENUE,  
AND FINANCING SOURCES BY MAJOR PROGRAM  
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 1986  
(Dollars in Thousands)  
(Restated and Unaudited)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>OPERATING EXPENSES</b>						
<b>AND DIVIDENDS:</b>						
Expenses By Category:						
Personnel Compensation and Fringe Benefits	\$ 6,092,588				\$ 548,558	\$ 6,641,146
Veterans' Benefits		\$ 15,673,194				15,673,194
Claims & Indemnities			\$ 1,094,250	\$ 1,112,210		2,206,460
Depreciation	337,997					337,997
Supplies & Materials	1,525,631				12,140	1,537,771
Contractual Services	1,133,073				47,335	1,180,408
Rent, Communications, and Utilities	374,624				128,822	503,446
Other	296,942				38,513	335,455
Total Operating Expenses	9,760,855	15,673,194	1,094,250	1,112,210	775,368	28,415,877
Provision for Dividends to Policyholders				907,170		907,170
Provision for SGLI Reserve				9,533		9,533
	\$ 9,760,855	\$ 15,673,194	\$ 1,094,250	\$ 2,028,913	\$ 775,368	\$ 29,332,580
<b>OPERATING REVENUE AND FINANCING SOURCES:</b>						
Operating Revenues:						
Premium Income				848,402		848,402
Interest Income			184,433	1,165,958		1,350,391
Loan Origination Fees			258,111			258,111
Reimbursements and Other	259,716	(25,193)	(698)	(2,874)	46,505	277,456
Total Operating Revenue	259,716	(25,193)	441,846	2,011,486	46,505	2,734,360
Financing by Source:						
Appropriations and Financing Sources Realized	9,386,027	15,374,512	138,529	9,391	725,526	25,633,985
Funds to be Provided by Future Financing Sources	115,112		513,875	8,036	3,337	640,360
Transfers, Reimbursements, and Other		323,875				323,875
Total Budgetary Financing	9,501,139	15,698,387	652,404	17,427	728,863	26,598,220
	\$ 9,760,855	\$ 15,673,194	\$ 1,094,250	\$ 2,028,913	\$ 775,368	\$ 29,332,580



Financial Statements

NOTE 11: (CONTINUED)

VETERANS ADMINISTRATION

SCHEDULE OF ASSETS, LIABILITIES, AND EQUITY BY MAJOR PROGRAM

SEPTEMBER 30, 1986  
(Dollars in Thousands)  
(Restated)

	Medical and Construction	Veterans Benefits	Housing Credit Assistance	Life Insurance	Administration and Other	Consolidated
<b>ASSETS:</b>						
Fund Balance with U.S. Treasury	\$ 3,532,060	\$ 1,917,842	\$ 368,897	\$ 24,817	\$ 304,787	\$ 6,148,403
Imprest Funds	9,790					9,790
Advances, Accounts, and Loans Receivable	215,204	354,076	1,208,749	1,495,510	69,947	3,343,486
Investments	19,671		134,800	11,635,018		11,789,489
Foreclosed Property Held for Sale			807,531			807,531
Land, Buildings, and Equipment Net of Accumulated Depreciation	6,307,381				2,668	6,310,049
Other Assets	34,544				120,041	154,585
Future Financing Sources	903,221		1,626,322	360,602	85,846	2,975,991
<b>TOTAL ASSETS</b>	<b>\$11,021,871</b>	<b>\$ 2,271,918</b>	<b>\$4,146,299</b>	<b>\$13,515,947</b>	<b>\$ 583,289</b>	<b>\$31,539,324</b>
<b>LIABILITIES, TRUST FUND BALANCES, AND EQUITY:</b>						
Accounts Payable, Principally to the Public	\$ 612,829	\$ 5	\$ 109,373	\$ 172,743	\$ 141,445	\$ 1,036,395
Accrued Compensation and Pension Benefits		1,237,046				1,237,046
Accrued Payroll and Payroll Related Liabilities	854,053				81,888	935,941
Dividends on Credit or Deposit				630,381		630,381
Insurance Dividends Payable				929,714		929,714
Other Liabilities	8,309	6,552	159,767	140,614	71,879	387,121
Reserve for Federal Employees Compensation Act	333,104				32,944	366,048
Reserve for Losses on Guaranteed Loans			1,735,252			1,735,252
Insurance Reserves				11,382,576		11,382,576
Borrowings from Treasury			1,730,078			1,730,078
<b>TOTAL LIABILITIES</b>	<b>1,808,295</b>	<b>1,243,603</b>	<b>3,734,470</b>	<b>13,256,028</b>	<b>328,156</b>	<b>20,370,552</b>
<b>TRUST FUND BALANCES</b>	<b>21,011</b>	<b>648,491</b>		<b>259,919</b>		<b>929,421</b>
<b>EQUITY OF THE U.S. GOVERNMENT:</b>						
Unrealized Appropriations:						
Deferred Appropriations	6,337,930	340,894			167,783	6,846,607
Unobligated Balances	1,419,041	13,144	411,826		7,839	1,851,850
Undelivered Orders	1,435,594	25,786	3		79,511	1,540,894
Insurance Fund Balances						
<b>TOTAL EQUITY OF THE U.S. GOVERNMENT</b>	<b>9,192,565</b>	<b>379,824</b>	<b>411,829</b>		<b>255,133</b>	<b>10,239,351</b>
<b>TOTAL LIABILITIES, TRUST FUND BALANCES, AND EQUITY</b>	<b>\$11,021,871</b>	<b>\$2,271,918</b>	<b>\$4,146,299</b>	<b>\$13,515,947</b>	<b>\$ 583,289</b>	<b>\$31,539,324</b>

## Financial Statements

### NOTE 11: SUPPLEMENTAL INFORMATION

The following schedules provide further detail, by major program area, of assets, liabilities and U.S. Government equity, of revenue, financing sources and expenses, of sources and uses of funds by major program area and of budgeted and actual outlays.

- o The medical program area includes financial data for the medical care program, including the VA's 172 medical facilities, medical research and administration, and construction. The construction program was included since most of its activities relate to medical facilities.
- o The veterans' benefits area includes the compensation, pension, and education programs, as well as the burial and miscellaneous assistance and veterans' job training programs.
- o Housing credit assistance includes both VA's loan guaranty and direct loan programs.
- o The administration area includes costs of managing the Agency as a whole and the National Cemetery System. Also included are costs of managing the Supply Fund and automated data processing systems.

Personnel compensation and fringe benefits for employees involved in veterans benefits, housing credit assistance, and life insurance have not been allocated to these major program areas and are included in the administration area.

**Financial Statements**

**NOTE 8: RECEIVABLES (Continued)**

**"Kicker" Contributions**

Receivables representing funding for certain veterans education benefits are not included in accounts receivable. These benefits, called "Kicker" Contributions, represent amounts to be provided by the Department of Defense (DOD) at the discretion of the Secretary of Defense to the Post-Vietnam Era Veterans Education Assistance Program (VEAP) account of any participant over and above the regular DOD contributions (\$2 for every \$1 contributed by the participant) in order to encourage persons to enter or remain in the Armed Forces. The Department of Justice recently ruled that the failure of Congress to specify how these contributions are to be made (whether the total expected amount should be deposited at the time a participant enrolls in an educational program or whether the branch of service may contribute to the fund on a "pay-as-you-go" basis) enables the Department of the Army to deposit "Kicker" contributions on an annual or semiannual basis. Thus, since DOD does not recognize the liability, it is improper for VA to record the receivable. The balances attributable to these funds were \$180 million and \$60 million in 1987 and 1986, respectively.

**NOTE 9: PROPERTY AND EQUIPMENT**

The majority of the reported property represents facilities and equipment used to provide medical care to veterans. Property and equipment, including transfers from other Federal agencies, are valued at cost. Expenditures for major additions, replacements, and alterations are capitalized. Routine maintenance is recognized as an expense when incurred. Costs of construction are capitalized as Construction in Progress until completed and then transferred to the appropriate property account.

Buildings are depreciated using the straight line method over estimated useful lives ranging from 25 to 40 years, based upon the American Hospital Association's estimate of useful lives of hospital assets. Equipment is depreciated using the straight line method over useful lives, which, for most equipment, range from 5 to 20 years.

Property and equipment consisted of the following as of September 30, 1987:

	<u>Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
	(dollars in thousands)		
Land	\$ 85,123	\$	\$ 85,123
Buildings	5,215,825	1,746,422	3,469,403
Equipment	2,786,842	1,649,730	1,137,112
Other	732,127	291,568	440,559
Construction in progress	<u>1,707,066</u>		<u>1,707,066</u>
TOTAL	<u>\$10,526,983</u>	<u>\$3,687,720</u>	<u>\$6,839,263</u>

**Financial Statements**

At September 30, 1985, investment securities consist of:

	<u>Interest Range</u>	<u>Insurance Programs</u>	<u>Other Programs</u>	<u>Total</u>
(\$dollars in thousands)				
Special Bonds	5.875-10.75%	\$11,285,674		\$11,285,674
Certificates	7.125-11%	214,344		214,344
GNMA Certificates	5.2-6.45%	135,000		135,000
Bonds	7.875-8.5%		\$ 2,251	2,251
Notes	7-14.625%		17,420	17,420
Other	Various		134,800	134,800
		<u>\$11,735,018</u>	<u>\$151,471</u>	<u>\$11,792,489</u>

All investments are in securities issued by the U.S. Department of Treasury except for GNMA, which were issued by the Government National Mortgage Association, a subdivision of the U.S. Department of Housing and Urban Development. Other VA programs with investments are Housing Credit and Medical.

**NOTE 8: RECEIVABLES**

Non-Federal accounts receivable principally represent amounts due from individuals for Education Loan defaults, Home Loan Guaranty and Direct Loan defaults, and Compensation & Pension overpayments. Federal accounts receivable are mostly accrued interest payments due from the U.S. Treasury Department on VA investments. Non-Federal advance payments are principally advances to VA construction contractors, grant recipients, beneficiaries, and VA employees engaged in official travel. Federal advance payments are mostly to the General Services Administration for the procurement of supplies and equipment. Current loans receivable are wholly amounts due under VA's Housing Credit Assistance Program. Non-Current loans receivable represent amounts due from loans and liens against VA-issued life insurance policies and also amounts owed VA's Housing Credit Assistance Program beyond the next 12 months.

## Financial Statements

During fiscal year 1986, in addition to regular annual dividends, VRI policyholders or their beneficiaries received a termination dividend of approximately \$100,000. This termination dividend was a return of excess funds in insurance reserves to policyholders.

### Insurance Cash Surrender Value

All whole life policies build cash surrender values equal to policy reserves plus any dividends held on account. Policyholders may borrow up to 94 percent of the cash surrender value or use it to purchase reduced paid-up insurance.

### VA Supervised Insurance Programs

VA also supervises the administration of the Servicemen's Group Life Insurance Program (SGLI) and the Veterans Mortgage Life Insurance (VMLI). SGLI is supervised by VA, but directly administered by the Prudential Life Insurance Company of America which provides group life insurance coverage and pays all claims and expenses associated with the program. This coverage is provided to active members of the Military Services, to cadets attending service academies, and to active members of the Armed Forces Reserves, National Guard, and ROTC.

VA's responsibilities are to establish premium rates and to act as the transfer agent for premiums paid by payroll deductions and for extra hazard costs paid by the service organizations involved. VA also determines the adequacy of SGLI's insurance reserves, and, if excess reserves exist, VA can both lower premium rates and withdraw excess funds. To date, VA has withdrawn approximately \$94 million from these reserves. These funds, together with investment interest earned thereon, are held in a trust which, as of September 30, 1987, had a balance of \$144.9 million. On September 30, 1986, this balance was \$133.2 million. This balance is used as a premium stabilization fund to augment premium payments remitted by the insured.

#### SGLI Insurance In Force

	<u>1987</u>	<u>1986</u>
Number of Policies	3,540,376	3,484,241
Amount (in millions)	\$176,065.3	\$173,156.9

In addition to SGLI, VA supervises a similar program, Veterans Group Life Insurance, which provides life insurance to discharged Veterans.

The VMLI program, similar to SGLI, is supervised by the Veterans Administration and directly administered by Bankers Life Insurance Company of Nebraska. Under this program disabled veterans can obtain coverage of up to \$40,000 of the outstanding balance of their home mortgages. Coverage ceases at age 70. Premiums based on standard mortality tables, are deducted from the veterans' monthly compensation payment. Administrative expenses and the additional cost of insuring these medically impaired lives are borne by the government through appropriations.

**Financial Statements**

The GAAP Life Insurance Reserve Balances and Participating Policyholders' Interest as of September 30, 1986, are shown below:

Program	Death	Death	Disability	Other	1986	Participating
	Benefits	Benefit	Income and		GAAP	
		Annuities	Waiver of		Reserve	Interest
			Premium		Total	
(dollars in thousands)						
NSLI	\$5,330,897	\$498,663	\$ 929,186	\$135,612	\$6,894,358	\$2,614,294
USGLI	111,825	35,728	2,798	1,371	151,722	75,504
VSLI	434,710	3,420	121,572	10,500	570,302	398,365
SDVI	248,075	2,341	148,500		199,016	
VRI	261,094	1,219	29,363		291,676	170,756
<b>TOTAL</b>	<b>\$6,386,001</b>	<b>\$541,371</b>	<b>\$1,231,519</b>	<b>\$147,583</b>	<b>\$8,307,074</b>	<b>\$3,258,619</b>

Statutory reserves are based on interest rates ranging from 2.3 percent to 4.5 percent. GAAP reserves are based on interest rate assumptions ranging from 7 percent to 8.5 percent. Actual average investment yield for insurance program securities was 9.58 percent as of September 30, 1987 and 9.57 percent as of September 30, 1986.

Statutory mortality assumptions include the American Experience Table, the 1941 CSO Table and the 1958 CSO Basic Table. GAAP mortality assumptions are based on actual mortality experience of the insurance programs, with a provision for adverse deviation.

One of the differences between total GAAP with Participating Policyholders' Interest and total Statutory is the Trust Fund balance for individual life insurance policies. Certain premium items are also accounted for differently under Statutory and GAAP principles. Statutorily, a liability is set up for unearned premiums and advance premiums. Under GAAP, the liability for these items is reduced. A comparison is provided below:

Unearned Premium Reserve and Advance Premium  
(dollars in thousands)

Program	9/30/87		9/30/86	
	Statutory	GAAP	Statutory	GAAP
NSLI	\$105,487	\$48,111	\$100,615	\$47,057
USGLI	23	23	42	42
VSLI	23,341	11,347	21,704	10,566
SDVI	1,447	1,447	1,440	1,440
VRI	3,487	2,538	3,120	2,391
<b>Total</b>	<b>\$133,785</b>	<b>\$63,566</b>	<b>\$125,921</b>	<b>\$61,496</b>

**Financial Statements**

Insurance in Force  
As of September 30, 1987 and 1986

Program	Number of Policies (Thousands)		Amount of Insurance (Millions)		Principal Veterans Group Covered
	1987	1986	1987	1986	
NSLI	2,913	3,011	\$21,547	\$21,595	WW II
USGLI	53	58	194	223	WW I
VSLI	341	357	3,075	3,162	Korea
VRI	130	133	491	908	WW II/Korea
SDVI	130	184	1,552	1,568	WWII/Korea/Vietnam
<b>Total</b>	<u>3,567</u>	<u>3,743</u>	<u>\$27,869</u>	<u>\$27,556</u>	

**Insurance Reserves**

Statutory insurance reserves consist of the actuarial computation of the present value of amounts that will be necessary to pay benefits in the future as policyholders or their beneficiaries make benefit claims. The two most important factors used to compute these reserves are assumed investment yields and mortality rates. The assumed investment yields and mortality rates used by the VA are prescribed by Federal statutes. The statutory reserve standard is necessary to insure the solvency and equity of the insurance program. This standard is on a basis similar to that used by many mutual life insurance companies in the United States.

The statutory insurance reserve balance as of September 30, 1987, consists of reserves for:

Program	Death Benefits	Death Benefit Annuities	Disability Income and Waiver of Premium	Other	1987 Statutory Reserve Total
(dollars in thousands)					
NSLI	\$8,082,269	\$465,070	\$ 880,877	\$162,394	\$ 9,590,610
USGLI	162,411	32,149	2,496	1,220	198,276
VSLI	848,576	3,445	120,334	1,325	973,680
SDVI	257,854	2,299	148,452		408,605
VRI	411,939	1,251	28,184		441,374
<b>TOTAL</b>	<u>\$9,763,049</u>	<u>\$504,214</u>	<u>\$1,180,353</u>	<u>\$164,239</u>	<u>\$11,612,555</u>

Participation Certificates

In fiscal year 1988, the final series of Federal Asset Financing Trust (FAFT) Participation Certificates (PCs) will mature. VA's current share of these PCs is \$577.7 million. The PCs are secured by a portion of VA's loans receivable. VA has transferred \$431.6 million in principal payments to a sinking fund established at the Government National Mortgage Association (GNMA). GNMA determined in September 1984 that principal payments received to date were sufficient to meet future principal payments, and suspended transfer of principal collections. VA has also transferred \$455 million in interest payments to GNMA for coverage of the periodic interest payments on the PCs. In September 1985, GNMA determined that the interest payments received to date were also sufficient to meet the interest due to PC holders, and suspended transfers of interest collections.

GNMA has invested funds not needed to meet current interest payments on the PCs. The balances associated with this investment at September 30, 1987, and September 30, 1986, were \$154.7 million and \$134.8 million, respectively (Note 7). VA has recognized income from the GNMA investment monthly, although the funds were retained in GNMA's sinking account. Furthermore, VA has, for budget purposes, considered this income to be an increase in its unobligated balance available for current operations rather than reserving the funds for payment of the debt. Therefore, to fund its final payment due at the maturity of the PCs on August 12, 1988, VA has included the necessary funding for the balance due at maturity as part of the emergency supplemental appropriation submitted in January 1988.

PRINCIPAL DUE ON PCs	\$577,684,000
VA PRINCIPAL PAYMENTS	<u>431,637,845</u>
BALANCE DUE AT MATURITY	<u>\$146,046,155</u>

Factors Impacting The Loan Guaranty Revolving Fund

The financial condition of certain sectors of the economy, particularly the energy and agricultural sectors, has adversely affected the housing mortgage industry's performance over the last year. The rate of housing foreclosures has increased substantially. The average foreclosure rate on VA guaranteed home loans increased from 16.8 percent in fiscal year 1986 to 19.6 percent in fiscal year 1987. The foreclosure rate for VA guaranteed mobile homes increased from 47.8 percent in fiscal year 1986 to 65.7 percent in fiscal year 1987. The record number of defaults by veterans in oil-producing states, such as Texas, Oklahoma, and Colorado, accounted for more than one-third of the total number nationwide in 1987.



NOTE 5: HOUSING CREDIT ASSISTANCE PROGRAM - COST OF GUARANTEED  
LOAN DEFAULTS

Most of the VA's housing credit assistance program involves the partial guaranty of loans, primarily home mortgages, issued to eligible veterans by private lenders. Although VA continues its direct loan program, the majority of VA's housing credit activities, such as the issuance of loan guaranties and the sale of foreclosed property on credit terms (vendee loans), are funded through the loan guaranty revolving fund.

The total amount of such loans at September 30, 1987, was \$182 billion, of which VA had guaranteed \$77 billion, and the total amount of such loans at September 30, 1986, was \$143 billion, of which VA had guaranteed \$63 billion. This increase in the level of VA guaranteed loans has increased VA's exposure to losses to its loan guaranty revolving fund. The Loan Guaranty funding fee, 1 percent of the loan principal, is not intended to fully fund the losses and other costs associated with foreclosures of VA guaranteed mortgages.

VA's guaranty in effect transfers some or all risk of default from the lender to the VA. It also provides other benefits to the veteran by inducing lenders to provide interest rates which are usually lower than conventional mortgage rates and by not requiring a down payment. Thus a subsidy is provided to veterans since they are receiving terms that are more favorable than would exist without Federal Government involvement.

Reserve for losses on guaranteed loans

One element of this subsidy is the present value of the cost the VA will bear as loans already guaranteed default in the future. A reserve for estimating losses from such defaults was included in fiscal year 1986 statements and has been included in the consolidated statement of financial position for fiscal year 1987. The present value of the costs of defaults is based on historical default data developed by the VA and assumes that the remaining outstanding guaranteed loans will default over a nine-year period, as follows (dollars in thousands):

1988	\$ 674,862
1989	741,507
1990	525,589
1991	340,407
1992	315,513
1993 - 1996	<u>355,724</u>
	<u>\$2,351,602</u>

## Financial Statements

In accordance with title 2's requirements, a liability has been established recognizing VA's portion of the long-term liability for employee injuries administered under the Federal Employees Compensation Act by the Department of Labor (DOL). As discussed in Note 1, "Workers Compensation", the liability consists of actual billings received by VA and included in its annual budget submissions as well as an estimate of the long-term compensation payments for cases on-hand as of the end of the fiscal year. In FY 1987, DOL estimated its long-term liability for future payout, net of current billings to the agencies, as part of its annual financial statements. GAO has opined that under title 2 each agency must recognize its portion of the long-term liability. Because this information was previously unavailable for recognition on the agency level, VA has restated its 1986 financial statements to reflect both the billed and estimated long-term liabilities for workers' compensation claims.

Life Insurance programs reserves have been restated and increased by \$153 million principally to recognize a reserve in the SDVI program for waiver of premium. Previously these reserves were erroneously omitted from VA's financial reporting although VA's statutory accounting principles require their inclusion. "Future financing sources" has been increased by \$361 million because these premiums are paid from VA's annual appropriation; Trust Fund Balances were increased by \$208 million.

Accrued annual leave as of September 30, 1986, has been restated to correct an overstatement of the liability of \$63 million which resulted from a software programming error. Amounts to be provided from future financing sources have been correspondingly decreased.

Veterans benefits accounts receivable and equity have been reduced by \$60.6 million based on a fiscal year 1987 ruling by the Department of Justice allowing the Department of Defense to fund certain education benefits on an as-needed basis as described in Note 8, "Receivables". Previously these receivables were recognized and reported when veterans were enrolled in a program of studies.

Certain other financial information has been reclassified to conform to the current year's presentation. Significant among these reclassifications was the establishment of a Provision for Amounts to be Provided by Future Financing Sources of \$640 million. Previously these amounts were included in Appropriations Realized. Trust fund balances have been reclassified and are reported as separate liabilities reflecting the restricted nature of these funds and segregating them from appropriated and other equity accounts related to general purpose activities of the Administration. Consistent with OMB policy, which precludes VA's recognizing certain veterans benefits accounts receivable as available budget authority until these accounts are collected, unobligated balances of \$294 million have been reclassified as deferred appropriations.

## Financial Statements

long-term liability for FECA is currently underway, and adjustment to the balances recognized for these financial statements may be necessary when actuarially-based liabilities are made available to agencies.

### NOTE 2: INTRAGOVERNMENTAL FINANCIAL ACTIVITIES

The VA's financial activities interact with and are dependent upon those of the Federal Government as a whole. Thus, VA's financial statements do not reflect the results of all financial decisions and activities applicable to it, as if it were a stand-alone entity.

- o The VA's consolidated financial statements are not intended to report the Agency's proportionate share of the Federal deficit or of public borrowing, including interest thereon. Financing for budget appropriations reported on the VA's statement of operations could derive from tax revenues or public borrowing or both; the ultimate source of this financing, whether it be tax revenues or public borrowing, has not been specifically allocated to the VA.
- o Financing for major and minor construction projects was obtained through budget appropriations. To the extent this financing was derived from public borrowing, no interest has been capitalized since such borrowings are recorded in total by the Department of the Treasury and are not allocated to individual departments and agencies.
- o Since the U.S. Treasury Department does not charge agencies interest on borrowings from the Treasury, VA does not recognize interest costs related to foreclosed property in its financial records. In fiscal year 1987, VA held foreclosed properties an average of 8 months. Based on this estimate and the average interest rate for the public debt (8.7 percent), the holding costs associated with the foreclosed property held for sale were approximately \$68 million in fiscal year 1987.
- o VA's Housing Credit Assistance program has a liability to the U.S. Treasury of \$1.7 billion. These funds were originally provided to support the direct loan fund, but were subsequently transferred to the loan guaranty fund and have since been fully used. The liability bears no interest and VA's ability to pay it is contingent upon receiving other financing.
- o During fiscal year 1986, the majority of the VA's employees participated in the contributory Civil Service Retirement System (CSRS), to which VA makes matching contributions. The VA does not, however, report CSRS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to its employees since this data is only reported in total by the Office of Personnel Management.

On January 1, 1987, the new Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. Employees hired after December 31, 1983, are automatically covered by FERS while employees hired prior thereto may elect to either join FERS or remain in CSRS. One of the primary differences between FERS and CSRS is that FERS

## Financial Statements

### Operating Revenue And Other Financing Sources Recognition

Interest income, which is earned primarily from the investments of the insurance program, is recognized on the accrual basis. Insurance premiums are recognized as revenue when due. Loan origination fees, which are charged to veterans at a rate of 1 percent of the loan principal, are recognized as revenues at the time of the guaranty.

### Funds With U.S. Treasury

VA does not maintain cash in commercial bank accounts. Cash receipts and disbursements are processed by the U.S. Treasury. The balance in the U.S. Treasury represents appropriated and trust funds that are available to pay current liabilities and finance authorized purchase commitments. As of September 30, 1987, and 1986, \$1,325,952,000 and \$1,540,894,000, respectively represent funds earmarked to pay outstanding purchase commitments.

### Property and Equipment

The majority of the reported property represents facilities and equipment used to provide medical care to veterans. Property and equipment, including transfers from other Federal agencies, are valued at cost. Expenditures for major additions, replacements, and alterations are capitalized. Routine maintenance is recognized as an expense when incurred. Costs of construction are capitalized as Construction in Progress until completed and then transferred to the appropriate property account.

Buildings are depreciated using the straight line method over estimated useful lives ranging from 25 to 40 years, based upon the American Hospital Association's estimate of useful lives of hospital assets. Equipment is depreciated using the straight line method over useful lives, which, for most equipment, range from 5 to 20 years.

### Accrued Compensation and Pension Benefits

Compensation and pension benefits are accrued when veterans have satisfied the VA's eligibility criteria. This accrual only pertains to benefits due and payable in a particular fiscal year. See note 4 for a description of the VA's future liability under its compensation and pension program.

### Losses on Guaranteed Loans

Upon foreclosure of a guaranteed loan, the VA may be required to pay the maximum claim, acquire the property, or acquire the property and pay less than the maximum claim pursuant to criteria established in Section 1816 of Title 38, United States Code. Thus, when the VA acquires the property, the cost is comprised of the claimed amount paid the lender less net proceeds from the sale of the property. The VA incurs an additional cost for direct home (vendee) loans, issued upon the sale of foreclosed properties, that subsequently default.

**Financial Statements**

**Consolidated Statement of Changes in Financial Position and Reconciliation to Budget**

FOR THE FISCAL YEARS ENDED SEPTEMBER 30, 1987 AND 1986  
(Dollars in Thousands)

	1987	(Restated) (Unaudited) 1986
<b>NET USE OF RESOURCES:</b>		
Operating Expenses	\$ 29,971,980	\$ 28,415,877
Items Requiring (Providing) Funds:		
(Increase) in Reserves	(1,271,304)	(745,585)
Depreciation	(363,477)	(337,997)
(Decrease) Increase in Accounts Receivable	(420,471)	61,068
Increase in Accounts Payable and Accruals	(274,715)	(159,725)
Revenues Accounted for as		
Offsetting Collections	(2,263,283)	(2,114,457)
Funds Used By Operations	25,378,730	25,119,181
Non-Operating Uses:		
Dividends (note 6)	927,500	882,935
Acquisitions of Land, Buildings, and Equipment	969,993	952,690
Purchase of Foreclosed Property Held for Sale	1,380,338	1,147,210
Issuance and Repurchase of Loans and Liens	1,327,375	1,085,081
Other, Net	(3,062)	34,083
Financing Activities:		
Sale of Foreclosed Property Held for Sale	(1,482,928)	(1,214,867)
Sale of Loans, with Recourse	(849,196)	(818,368)
Loan/Lien Repayments/Optional Income Settlements	(372,900)	(296,682)
Disposals of Equipment and Other	(95,266)	(242,300)
Revenues Collected for Treasury	(228,546)	(113,253)
<b>NET USE OF RESOURCES (BUDGETARY OUTLAYS)</b>	<b>26,952,038</b>	<b>26,535,710</b>
<b>SOURCES OF BUDGETARY RESOURCES PROVIDED</b>		
Current Year Appropriation	26,605,398	26,464,426
Less: Reductions Pursuant to P.L. 99-177 (Gramm-Rudman-Hollings)		(234,053)
Current Year Appropriations, Net	26,605,398	26,230,373
Interest on Government Securities	964,383	943,956
Net Transfers, Reimbursements, and Other	(165,973)	(95,185)
Funds Returned to Treasury	(170,226)	(58,723)
<b>TOTAL RESOURCES PROVIDED</b>	<b>27,233,582</b>	<b>27,020,421</b>
<b>INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>		
IMPREST FUNDS	281,544	484,711
Funds Exchanged for U.S. Government Securities	(433,094)	(360,611)
<b>NET INCREASE (DECREASE) IN U.S. TREASURY AND IMPREST FUNDS</b>	<b>(151,550)</b>	<b>124,100</b>
<b>U.S. TREASURY AND IMPREST FUNDS:</b>		
Beginning of Year	6,158,193	6,034,093
End of Year	\$ 6,006,643	\$ 6,158,193

The accompanying notes are an integral part of this statement.  
Note 11 includes financial information by major program area.

# Financial Statements

## Consolidated Statement of Financial Position

SEPTEMBER 30, 1987 AND 1986

(Dollars in Thousands)

	1987	(Restated) 1986
<b>ASSETS:</b>		
Fund Balance with U.S. Treasury	\$ 5,997,027	\$ 6,148,403
Imprest Funds	9,616	9,790
Advances, Accounts, and Loans Receivable, net (note 8)	3,211,966	3,343,486
Investments (note 7)	12,242,563	11,789,489
Foreclosed Property Held for Sale	864,104	807,531
Land, Buildings, and Equipment Net of Accumulated Depreciation (note 9)	6,839,263	6,310,049
Other Assets	151,615	154,585
Future Financing Sources	\$ 4,095,108	\$ 2,975,991
<b>TOTAL ASSETS</b>	<b>\$ 33,411,262</b>	<b>\$ 31,539,324</b>
<b>LIABILITIES, TRUST FUND BALANCES, AND EQUITY:</b>		
Accounts Payable, Principally to the Public	\$ 1,111,935	1,036,395
Accrued Compensation and Pension Benefits	1,280,054	1,237,046
Accrued Payroll and Payroll Related Liabilities	1,011,568	935,941
Dividends on Credit or Deposit (note 6)	706,018	630,381
Insurance Dividends Payable (note 6)	956,347	929,714
Other Liabilities	459,879	387,121
Reserve for Federal Employees Compensation Act	423,727	366,048
Reserve for Losses on Guaranteed Loans (note 5)	2,718,898	1,735,252
Insurance Statutory Reserves (note 6)	11,612,555	11,382,576
Borrowings from Treasury	1,730,078	1,730,078
<b>TOTAL LIABILITIES</b>	<b>22,011,059</b>	<b>20,370,552</b>
<b>TRUST FUND BALANCES</b>	<b>889,639</b>	<b>929,421</b>
<b>EQUITY OF THE U.S. GOVERNMENT:</b>		
Unrealized Appropriations:		
Deferred Appropriations	7,334,826	6,846,607
Unobligated Balances	1,369,786	1,851,850
Undelivered Orders	1,805,952	1,540,894
<b>TOTAL EQUITY OF THE U. S. GOVERNMENT</b>	<b>10,510,564</b>	<b>10,239,351</b>
<b>TOTAL LIABILITIES, TRUST FUND BALANCES, AND EQUITY</b>	<b>\$ 33,411,262</b>	<b>\$ 31,539,324</b>

The accompanying notes are an integral part of these statements.  
Note 11 includes financial information by major program area.

\$454,000 in interest associated with late payments, but it should have paid an additional amount estimated at \$431,000. The interest charges that were due, but not paid, resulted primarily from the manual processing of several types of invoice payments.

In connection with our examination, nothing came to our attention that caused us to believe that VA was not in compliance with the terms and provisions of laws and regulations for those transactions not tested; however, we believe the instances of noncompliance discussed above merit VA taking corrective action.

The matters discussed above were considered in determining the nature, timing, and extent of the audit tests to be applied in our examination, and they do not affect our opinion on VA's consolidated financial statements dated May 16, 1988.

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## Recommendations

We recommend that the Administrator of Veterans Affairs:

- Require the Director of the Department of Veterans Benefits to:
  - (1) Determine an effective and appropriate method of resolving the issue of charging interest on accounts receivable relating to the compensation and pension benefit overpayments as required by the 1980 Amendments to the Veterans' Rehabilitation and Education Act. At least two potential alternatives include: (a) issuing waivers as authorized by 38 U.S.C. 3102 for cases where charging interest and administrative costs is deemed to be against equity and good conscience or (b) obtaining the legislative approval to exempt compensation and pension receivables from interest and administrative costs charges.
  - (2) Reevaluate the priority given the computer software reprogramming workload to determine whether the 1980 legal requirement for charging current interest rates on loan guaranty receivables can be implemented earlier than 1991.
- Direct the Controller to complete the conversion to the automated invoice payment system of invoices handled manually.

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## Agency Comments

Although we did not obtain formal comments on this report, we did provide appropriate VA officials with a draft of the report and have incorporated their comments where appropriate. VA has initiated action in the

In his comments to the Committee on Governmental Affairs, the Administrator also agreed to change the interest rate charged on loan guaranty debts. However, he did not establish a specific implementation date, citing the need for "extensive programming" to implement necessary automated system changes. As of May 16, 1988, VA continued to charge 4 percent interest on loan guaranty accounts receivable. VA has determined that because of the extensive system programming changes which will be required, it will not be able to complete its reprogramming efforts and thereby provide a means for increasing the interest rate charges on loan guaranty receivables until 1991.

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## The Prompt Payment Act and Applicable Regulations Are Not Fully Complied With

As VA reported to the Office of Management and Budget (OMB) under the requirements of the Prompt Payment Act (31 U.S.C. 3905) and as confirmed by our audit test, VA paid a majority (86 percent for fiscal year 1987) of the vendor payments that it considers subject to the act within the prescribed payment due-date criteria. For the remaining 14 percent of the payments, about 6 percent were paid during the grace period permitted by the act, with only 8 percent being paid after the grace period. The payments in this latter category are subject to interest penalties and it is with this category that VA continues to experience difficulty in fully complying with the act's requirements. While VA properly paid out over \$454,000 in interest penalties during fiscal year 1987, it did not pay additional interest penalties totaling nearly the same amount that were also due.

The Prompt Payment Act provides governmentwide payment standards for determining when federal agencies should pay commercial vendors. Basically, the act:

- specifies that unless the contract states otherwise or the purchase involves meat or other perishable agricultural commodities, the payment due-date is 30-days after receipt of a proper invoice or acceptance of goods or services, whichever is later, and
- requires payment of interest penalties for payments made to commercial vendors after a grace period, 15 days after the specified payment due date.

OMB circular A-125 implements the act's requirements and requires federal agencies to, among other things, annually report various Prompt Payment Act information to OMB.



The first two items are instances of noncompliance disclosed in our compliance report for fiscal year 1986 which we again report for fiscal year 1987. These are discussed in detail in latter segments of this report.

Regarding item three, we reported in our report on fiscal year 1986 that VA was not accruing penalties on its delinquent debt under section 11 of the Debt Collection Act of 1982 (31 U.S.C. 3717). VA believed that its program debts are subject to the interest and administrative cost provisions of the Veterans' Rehabilitation and Education Amendments of 1980 (38 U.S.C. 3115), and not the interest and penalty provisions of the Debt Collection Act. To address this issue, VA requested a Comptroller General decision which was pending when we issued our report on fiscal year 1986. We subsequently issued B-222973 on June 8, 1987, in which we agreed with VA that its program debts are not subject to the interest and penalty provisions of the Debt Collection Act of 1982. Therefore, this issue is resolved.

Regarding item four, we questioned whether VA properly terminated processing benefit entitlements under its compensation and pension benefit programs late in fiscal year 1986, treated these entitlements as fiscal year 1987 obligations, and subsequently used its fiscal year 1987 appropriation to pay these benefits. Because these questions arose late in our audit, we stated that we would address them separately. We subsequently issued a Comptroller General decision (B-226801) on March 2, 1988, which concluded that VA violated 31 U.S.C. 1501(a) by failing to record compensation and pension benefits claims established as entitlements in September 1986 as fiscal year 1986 obligations. We further concluded that since none of VA's fiscal year 1987 appropriation was available for fiscal 1986 year obligations, the Anti-Deficiency Act (12 U.S.C. 1341(a)(1)) precluded the use of the appropriation to liquidate fiscal year 1986 obligations.

As in fiscal year 1986, VA did not properly record as fiscal year 1987 obligations all compensation and pension benefit claims established as entitlements in September 1987. In addition, VA did not record certain education benefit claims that were also established as entitlements in September 1987. However, unlike the prior year, this did not affect the funding source available to pay benefits because the Continuing Resolution for fiscal year 1988 (Public Law No. 100-202) authorized VA to use its fiscal year 1988 appropriation to pay prior year accrued obligations required to be recorded in the last quarter of fiscal year 1987. VA is correcting its obligation recording practices and we therefore consider it resolved.

Except for the problems relating to buildings and equipment, which caused us to qualify our opinion on VA's consolidated financial statements, the weaknesses in the system of internal accounting controls do not affect our opinion.

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## Agency Comments

We did not request formal comments on this report. However, we did provide appropriate VA officials with a draft of the report and have incorporated their comments where appropriate. VA has initiated corrective action on many of our recommendations. For example, in June 1988, VA initiated a major effort in the property accounting area to capitalize approximately \$750 million of the construction-in-process balance. VA is also taking action in the insurance system software area at the Philadelphia DPC. VA is converting the DPC's obsolete system applications to another computer language so that the applications can run on computer systems which have better access controls.

accuracy of account postings and balances, include (1) data reconciliations between systems and (2) reconciliations between control accounts and subsidiary ledgers. However, we found problems at VA in this area as well. Some examples follow.

- At 6 of the 37 VA regional offices and medical centers we visited, differences between the payroll system subsidiary ledger and the trial balance system control account for VA's stations were not reconciled.
- Reconciliations between the housing credit general ledger system and its subsidiary system for accounts receivable were not performed at 4 of the 10 regional offices covered in our examination. For example, in one VA regional office, the claims receivable account for the housing credit assistance program has not been reconciled since late 1970. The difference as of December 1987 was over \$1 million.
- Of the 28 medical centers we visited, 18 did not complete their reconciliation of accounting control accounts with supply records (the subsidiary or detailed records) for non-expendable property. Adequate reconciliation procedures, at a minimum, should include not only the identification of differences but also, where warranted, actual adjustments to either the control accounts or subsidiary records to reconcile the two.

Reconciliations can also provide a means to assess whether controls need to be improved. For example, in reconciling the supply records, the reasons for the differences may identify that better controls are needed or that existing controls are not properly implemented. We were unable to determine why the various VA units did not perform the required reconciliations.

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## Conclusions

As a result of the weaknesses in VA's property accounting and ADP controls, there is a high degree of risk that material errors or irregularities could occur and not be promptly detected. Implementing an automated accounting and property system for buildings and structures would greatly aid in correcting the principal problems relating to property accounting. Such a system would not only provide a more efficient means for an audit of the account balances, but it would also provide an efficient mechanism for applying management capitalization policies and centralized reviews of adherence to these policies.

Appropriately implemented ADP controls in the accounting area would improve the integrity of computer-generated data and accounting transactions. This assurance is needed not only to prepare accurate financial

found inadequate software maintenance procedures for both software types at all three data processing centers (DPCs), as the following examples illustrate.

- At each DPC, neither VA's system auditors nor its programming divisions routinely or consistently review system and application software program codes (the actual computer instructions). As per the National Bureau of Standards' Federal Information Processing Standard Publication 73, Guidelines for Security of Computer Applications, this type of review (known as a "code review") is the most effective technique for preventing fraudulent or improper modifications to software.
- At the Austin DPC, the integrity of application modification testing is compromised because programmers, rather than certain system auditors, control major aspects of the test. The system auditors responsible for financial and administrative systems typically certify batch application software modifications. However, their review is based on output provided and tested by programmers, using test files that can be changed by programmers.
- Application programmers at the Philadelphia DPC have access to newly certified software for life insurance before installation, thereby increasing the risk that unauthorized changes could be made to the software or that an incorrect software version could be installed.

It is imperative that strong controls exist in the software maintenance process because when changes to program codes are being made, errors could occur in a program that could destroy data or modify it so that it is not usable or codes can be inserted that could perpetuate fraudulent activity.

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## Data Integrity

Data integrity controls are those which safeguard the propriety of transactions from unauthorized modification or processing. The following are examples of data integrity control weaknesses we found at VA's DPCs:

- System users at each DPC can bypass normal system controls and make unauthorized modifications to programs or data. This weakness is the result of inadequate controls over certain utility programs.
- Because of obsolete system software, maintenance of the insurance system software at the Philadelphia DPC is not readily obtainable (that is, the vendor no longer provides maintenance support to the primary system software). Also, all insurance system users at the Philadelphia DPC

stronger internal accounting controls to ensure that all veterans receiving medical services for which VA should be reimbursed were identified and billed. The results of our examination of fiscal year 1987 transactions indicate that, although certain basic controls required by VA are not being complied with by many medical centers, VA has improved its eligibility determinations and billing effectiveness in this area. We believe this improvement is primarily attributable to two factors: (1) increased use of VA's new computerized admission and discharge system at medical centers and (2) more detailed reviews of patient eligibility factors. Accordingly, we no longer consider this a material control weakness from a financial statement standpoint for 1987.

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## Property Accounting Needs Improvement

As reported in our opinion on VA's fiscal year 1987 and 1986 financial statements, it was impracticable for us to extend our audit procedures sufficiently for us to express an opinion on the fair presentation of VA's land, buildings, and equipment and related depreciation accounts. We were unable to do so for two reasons. First, documents supporting the cost of most of the items, which were acquired over a period of years dating back to the agency's establishment in 1930, were unavailable. Secondly, and more importantly, the lack of consistent adherence to management policies relating to the capitalization and depreciation of buildings has resulted in inaccurate account balances. This latter problem is due in part to VA's manual, real property accounting system. This manual system does not provide (1) efficient and consistent capitalization of improvements to buildings and other structures or (2) efficient, centralized review of recorded amounts. VA is currently considering various approaches and property accounting systems to meet its needs.

VA increases its building accounts primarily through two capital acquisition programs: operating funds are used for many major additions, replacements, and alterations that also meet VA's real property capitalization policy, while major projects are funded through construction funds (that is, VA's capital construction projects). Examples of the types of inaccuracies, inconsistencies, and lack of adherence to policies that we noted relative to capital items follow.

- Expensing items purchased with operating funds that meet VA's capitalization policy. Our limited test in fiscal year 1987 showed that the incorrect accounting practices we disclosed in 1986 were still occurring.
- Improper transferring of project costs from work-in-process to completed facilities. We found this problem in 23 of the 62 capital construction projects that we tested during our 1987 examination. The problem

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# Report on Internal Accounting Controls

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We have examined the consolidated financial statements of the Veterans Administration (VA) for the fiscal years ended September 30, 1987 and 1986, and have issued our opinion thereon. As part of our examination, we made a study and evaluation of the system of internal accounting controls to the extent we considered necessary to evaluate the system as required by generally accepted government auditing standards. The purpose of our study and evaluation was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on VA's consolidated financial statements. This report pertains only to our study and evaluation of the system of internal accounting controls for the fiscal year ended September 30, 1987. Our report on our study and evaluation of the system of internal accounting controls for the fiscal year ended September 30, 1986, is presented in GAO/AFMD-87-38, dated July 29, 1987.

For purposes of this report, we have classified the significant internal accounting controls in the following categories:

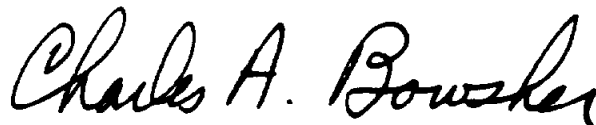
- medical care and construction;
- life insurance;
- compensation, pension, and education benefits;
- housing credit assistance;
- administration and other, including all payroll; and
- financial reporting.

Our study included all of the control categories listed above, but we did not evaluate the internal accounting controls over all functions within the categories. Also, we did not evaluate accounting controls in the various miscellaneous funds VA administers, such as the General Post Fund. For the areas where controls were not evaluated, it was more efficient to expand the scope of our substantive audit tests. Our study and evaluation was more limited than would be necessary to express an opinion on the system of internal accounting controls taken as a whole or on any of the categories of controls previously identified.

The management of VA is responsible for establishing and maintaining a system of internal accounting controls in accordance with the Accounting and Auditing Act of 1950 and the Federal Managers' Financial Integrity Act of 1982. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system of internal accounting controls are to provide management with reasonable

the losses and other costs associated with foreclosures of VA guaranteed mortgages. The continuing high level of foreclosures which result in increased cash outlays for property acquisitions has severely strained the revolving fund's resources. In response, VA obtained, primarily through a fiscal year 1988 supplemental appropriation, \$726.6 million in additional funds for the loan guaranty revolving fund. Although loan guaranty operations for the remainder of fiscal year 1988 will be continued because the emergency supplemental appropriation has been obtained, a continuing high rate of foreclosures on VA guaranteed mortgages may require additional supplemental appropriations in future years.

In our opinion, except for the effect of adjustments, if any, that might have been necessary had we been able to perform necessary auditing procedures to substantiate the asset and related expense accounts, as discussed in paragraph three above, and, except for the \$3-billion overstatement in insurance reserves due to the use of statutory assumptions rather than more realistic assumptions under generally accepted accounting principles, as discussed in paragraph four above, the consolidated financial statements referred to above present fairly the financial position of the Veterans Administration at September 30, 1987 and 1986, and the results of operations, the changes in financial position, and the reconciliation to budget for the fiscal year ended September 30, 1987, in conformity with generally accepted accounting principles for federal agencies applied on a consistent basis during the period.



Charles A. Bowsher  
Comptroller General  
of the United States

May 16, 1988



United States  
General Accounting Office  
Washington, D.C. 20548

Comptroller General  
of the United States

B-226801

To the Administrator of Veterans Affairs  
Veterans Administration

We have examined the consolidated statement of financial position of the Veterans Administration (VA) as of September 30, 1987 and 1986, and the related consolidated statements of operations and changes in financial position and reconciliation to budget for the fiscal years then ended. Our examinations were made in accordance with generally accepted government auditing standards and, accordingly, included such tests of accounting records and such other auditing procedures as we considered necessary in the circumstances, except as described in the following two paragraphs. In addition to this report on our examination of VA's 1987 and 1986 consolidated financial statements, we are reporting on our evaluation of internal accounting controls and compliance with laws and regulations. During our examination, we identified matters which do not affect the fair presentation of the financial statements, but nonetheless warrant management's attention. We are reporting them separately to VA.

Fiscal year 1986 was the first year that VA prepared its financial statements and maintained its accounting records in accordance with generally accepted accounting principles for federal agencies. In addition, our examination of VA's consolidated statement of financial position for fiscal year 1986 (GAO/AFMD-87-38, dated July 29, 1987) was the first year this statement had been audited in accordance with generally accepted government auditing standards. Because of these conditions, it was not practical for us to perform various auditing procedures with respect to determining whether, as of October 1, 1985, the beginning of the 1986 fiscal year, the amounts of advances, accounts and loans receivable, accounts payable, and the related amounts of revenues and expenses were recorded in the proper accounting period. These amounts were material to determining operating expenses and revenues and the adjustments affecting the report on reconciliation to budget. Accordingly, we do not express an opinion on the accompanying consolidated statements of operations and changes in financial position and reconciliation to budget for the fiscal year ended September 30, 1986. Our opinion on the fiscal year 1986 consolidated statement of financial position was qualified because documents supporting the original cost of land, buildings, and equipment, many of which were acquired by VA over periods dating back to its establishment in 1930, were not readily obtainable, and we were unable to satisfy ourselves by means of alternative



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# Contents

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Letter		1
Opinion Letter		4
Report on Internal Accounting Controls		8
	Property Accounting Needs Improvement	10
	ADP Controls Need Strengthening	11
	Conclusions	14
	Recommendations	15
	Other Opportunities for Improvement	15
	Agency Comments	16
Report on Compliance With Laws and Regulations		17
	Violations of the Veterans' Rehabilitation and Education Act Amendments of 1980	19
	The Prompt Payment Act and Applicable Regulations Are Not Fully Complied With	20
	Conclusions	21
	Recommendations	22
	Agency Comments	22
Financial Statements		24
	Consolidated Statement of Financial Position	24
	Consolidated Statement of Operations	25
	Consolidated Statement of Changes in Financial Position and Reconciliation to Budget	26
	Notes to the Financial Statements	27

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## Abbreviations

ADP	automated data processing
DPC	data processing center
GAO	General Accounting Office
OMB	Office of Management and Budget
VA	Veterans Administration

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